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Dec 15, 2021 04:03 PM
BUSINESS

In Depth: Ride-Hailing Industry Contends With Tightening Regulations Amid Didi Fallout

By Qian Tong

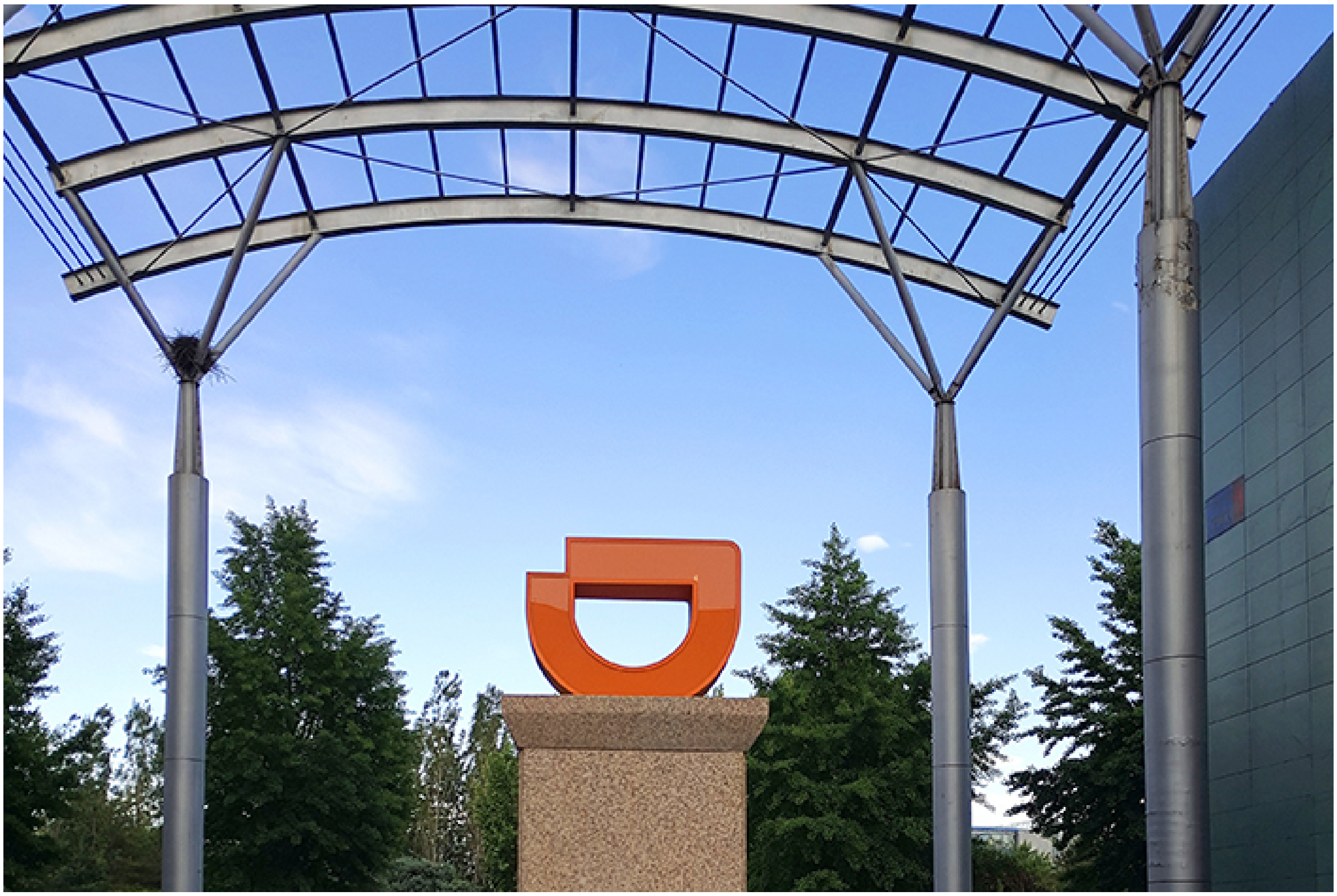

Photo: VCG

As hard as it will be for ride-hailing giant Didi Global to **move its stock** to Hong Kong from New York, the real 800-pound gorilla in the room is the government's cybersecurity review and other regulatory issues.

They amount to a black cloud hovering over the business. Didi's ride-hailing orders have fallen by 30% compared with the same time last year, Caixin has learned. Dozens of Didi's mobile apps have been barred from new downloads over the past few months on the order of the Cyberspace Administration of China

After Didi's main app was removed from app stores on the evening of July 9, the CAC **removed 25 mobile other applications** operated by Didi. As of now, applications related to Didi have not yet appeared in Chinese app stores.

"The company is looking forward to the results of the cybersecurity review," a Didi employee told Caixin. "Only when the results come out will there be hope for the business to restart."

The market is also anxiously awaiting the outcome of the investigation, which may have a profound impact not only on Didi but also on a broader range of Chinese companies listed abroad.

In the ride-hailing business, market share and order volume are the most important indicators of a company's market value. Didi once had a market share of more than 80% and a daily volume of 30 million orders. In 2020, Didi's revenue reached 141.7 billion yuan ($22.2 billion). In the first quarter of 2021, revenue was 42.2 billion yuan. Providing bike-sharing, taxi, financial and other services, Didi was valued at $67 billion at the time of its $4.4 billion U.S. share sale June 30. Ride-hailing is still its main source of revenue.

Since the cybersecurity investigation was launched two days after Didi's New York share sale, the company has suffered a series of regulatory setbacks including the suspension of new-user registrations. More than half of its debut-day market value was wiped out.

Now Didi is **moving to delist** from the New York Stock Exchange and prepare for a listing in Hong Kong. A source close to Didi said the company's decision to **move its stock** from New York to Hong Kong came in response to a request by authorities as part of the investigation. The person predicted that the change of listing venue will help Didi to resolve the cybersecurity review.

Didi, which has raised more than $30 billion over eight years to fund aggressive expansion, is under mounting pressure to solve its problems. Established in 2012, Didi combined rivals Kuaidi and Uber China to become the country's largest ride-hailing platform. Before going public, Didi went through 20 rounds of private placements with nearly 100 private equity investors, the largest number among Chinese internet companies.

An early investor in Didi said the regulatory risks facing the company are still difficult to assess, and the Hong Kong listing path is full of uncertainties. The

Several institutional investors including Hillhouse Capital Group have dumped their holdings of Didi as its stock has plunged.

Compliance pressures

China's closer regulatory scrutiny and stricter compliance requirements for the industry are limiting platforms' growth prospects. In 2017, the Ministry of Transport issued industrywide rules requiring all drivers and vehicles in service to be licensed.

In September this year, five ministries summoned 11 ride-hailing platforms including Didi and pressed them to meet the requirements by year-end. Didi's compliance rate was 43%, lower than that of most competitors, Caixin has learned.

"The most difficult thing to comply with is in big cities like Beijing and Shanghai where authorities demanded that ride-hailing drivers have local household registrations," excluding a huge number of immigrant drivers, a ride-hailing industry veteran said.

"There might be less than 5% of drivers meeting compliance requirements in Beijing," a Didi employee said. "If Beijing and Shanghai strictly enforce the requirements, many platforms will have to quit the business in the two cities." A withdrawal from Beijing and Shanghai would lead to a 10% decline in Didi's orders, the person said.

Regulators' recent order to cap commission fees charged by ride-hailing platforms could put more pressure on Didi. On Nov. 30, the Ministry of Transport and eight other ministries urged ride-hailing platforms to set a reasonable upper limit on their of commission rates. Although the regulators are still working on details of the new commission rules, a ceiling would have a deep impact on the core profit model, the person close to the company said.

Zeng Weimin, a global partner of Bain & Co., said a lot of variable costs can be amortized and optimized through dynamic pricing strategies. However, the upper limit for commissions would mean that platforms' room to amortize costs will be limited.

"This policy has a great impact on all platforms, not only Didi," said a ride-hailing industry veteran.

The cybersecurity review of Didi that so far has lasted nearly six months created opportunities for other competitors. Didi's main rivals include new ride-hailing businesses initiated by auto manufacturers and other internet platforms that are increasingly tapping into transportation services.

Ride-hailing platforms backed by vehicle manufacturers or the taxi industry are multiplying. Cao Cao Mobility, T3 Chuxing, Xiangdao Chuxing and other rivals accelerated their expansion across China. After Geely-backed Cao Cao Mobility raised 3.8 billion yuan in September 2021, T3 Chuxing, which is backed by some of China's largest automakers, announced in October the completion of a 7.7 billion yuan series A funding round. At the end of 2020, Xiangdao, the mobility service brand of SAIC Motor Corp. Ltd., received more than 300 million yuan in series A funding from Alibaba Group Holding Ltd. and battery-maker Contemporary Amperex Technology Co. Ltd., known as CATL.

Vehicle manufacturers have advantages in car supply, but they are usually regional businesses. Due to difficulties in controlling vehicle operations in other regions, "it is difficult for them to expand and replicate the business in other regions, so they will not directly impact Didi's market status," a Didi source said.

But more internet platforms are also marching into the market, including Alibaba-backed navigation app Gaode Map. Using its popular map service platform, Gaode has become a main portal for connecting ride-hailing service providers with users, taking the second-largest market share after Didi. Other platforms, such as delivery giant Meituan, are also pushing into the market.

Regulatory risks

On July 16, the CAC and seven ministries jointly sent investigators to Didi to conduct a cybersecurity review.

"Didi deployed a lot of R&D and product personnel to cooperate with the investigation team," a source close to Didi told Caixin. "The review was detailed, and the team even checked the company's system logs."

As the cybersecurity review drags on, market speculation is rising that China's market regulator will resume an antitrust investigation into Didi's 2016 merger with Uber China. The investigation hasn't yet concluded, and Didi listed it as a major business risk in its U.S. prospectus, citing the possibility of fines and a business reshuffle.

Han Lijie, a partner of Chicago-based global law firm Katten Muchin Rosenman LLP, said Didi's potential market monopoly is not limited to the concentration of undertakings. From the perspective of consumer rights protection, the problems also include raising prices during rush hour, using big data to discriminate among customers, and conducting exclusive sales. But it is still unclear whether regulators will define such practices as violations under monopoly regulations.

The biggest concern is still the cybersecurity probe. A senior internet regulatory official told Caixin that regulators have almost formulated a plan for Didi. Since the case involves national security issues, it is incomparable with previous reviews and can be handled only as a special case.

Huaxi Securities Co. Ltd. wrote in a research report in November that the data handled by Didi includes navigation data, personal travel information and other advanced data. Any leakage of such information may pose risks to user privacy and national security.

On Nov. 14, China's cyberspace watchdog issued **new draft rules** on data collection and management for public comment. If enacted, the rules could create new headwinds for data-rich businesses like Didi that pivoted their capital-raising plans to Hong Kong after Beijing made clear that listings outside China were now subject to heightened scrutiny over the export of data that could affect national security.

"According to the data security regulations, it has been determined that the state has ultimate control over important data," said Xu Ke, a digital economy expert at the University of International Business and Economics in Beijing. "Although the right of control does not mean ownership, it determines that any action of the company on important data requires the approval and security assessments of the state."

Hao Shuai contributed to this story.

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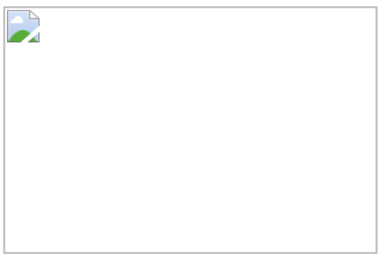
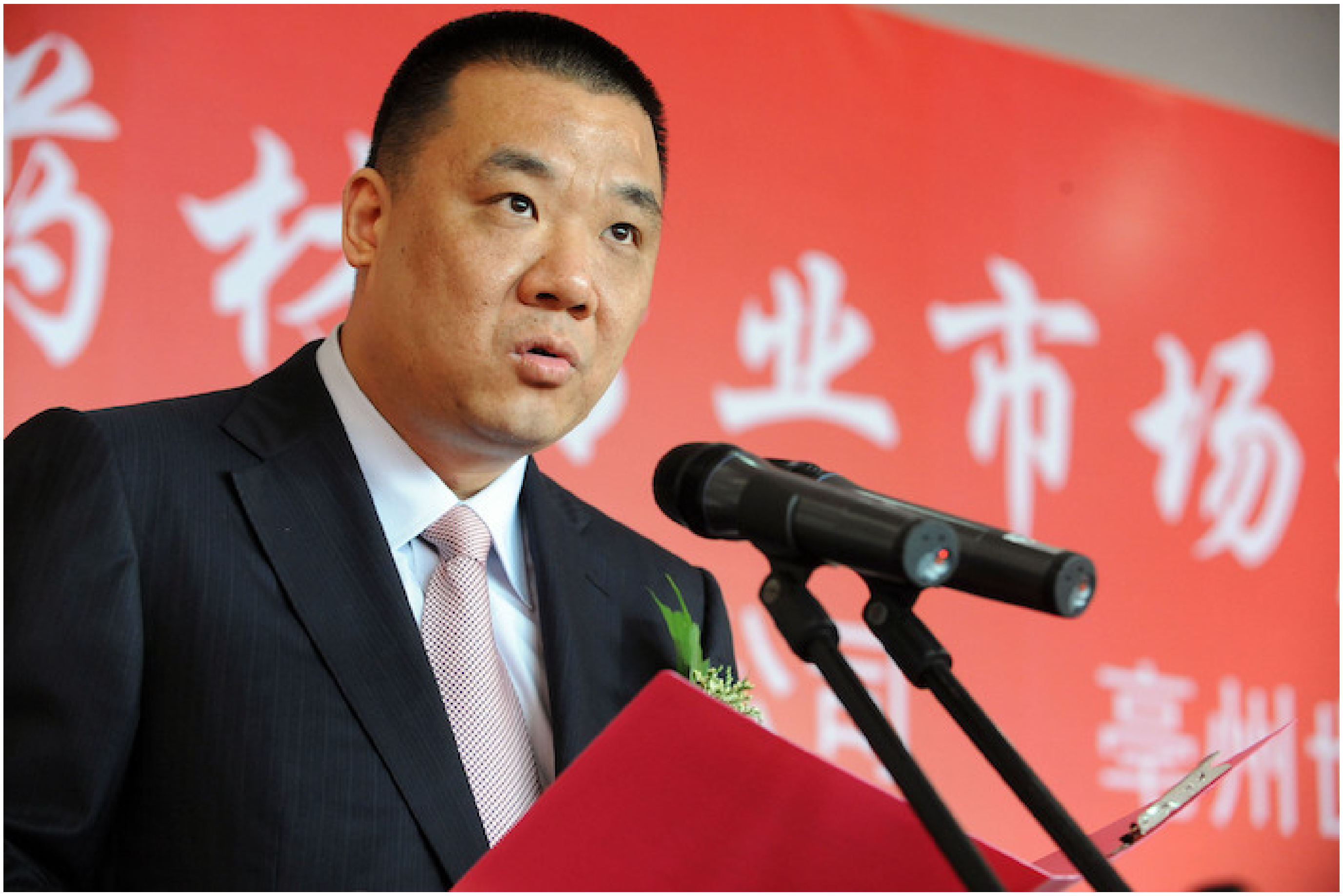


Didi’s Delisting, Relisting Plan Faces Bumpy Ride, Experts Say

Jan 10, 2022 02:39 PM
BUSINESS

Kangmei’s Former Chief Gets 12 Years in Final Verdict

By Wang Juanjuan and Denise Jia



Ma Xingtian, the former chairman of Kangmei Pharmaceutical Co. Ltd.

Ma Xingtian, the former chairman of **Kangmei Pharmaceutical Co. Ltd.**, was sentenced to 12 years in prison and fined 1.2 million yuan ($188,300) for manipulating the securities market, failure to disclose important information and bribery.

The Guangdong Higher People's Court rejected Ma's appeal and issued a final ruling in his case. The court upheld the trial court's November verdict, saying the evidence was sufficient, the conviction was accurate, and the sentence was appropriate.

Kangmei, one of China's biggest publicly traded drugmakers, was accused of financial reporting **fraud** involving 88.6 billion yuan of overstatements between 2016 and 2018. Regulators found that the company used fake bank deposit slips to inflate cash reserves, forged documents for nonexistent business activities and transferred company funds to related parties to trade in its own stock.

In November, the lower court found the drugmaker, its executives and its auditors responsible for financial fraud that caused 2.46 billion yuan ($385 million) of losses to 52,037 investors. Ma's wife, Xu Dongjin, who was Kangmei's who signed Kangmei's financial reports during the period of the fraud were among the defendants and were found partly liable for the compensation.

The finding of partial liability for the directors **triggered** a wave of resignations by outside board members from a dozen publicly traded Chinese companies.

From 2015 to 2018, Ma and other executives illegally raised a large amount of funds and manipulated Kangmei's stock price and trading volume by using multiple trading accounts under his control to buy and sell the stock, the court found.

Ma also organized, planned and directed company personnel to conduct financial fraud, disclose false business information to shareholders and the public, and fail to disclose more than 11.6 billion yuan of nonoperating funds that were embezzled by controlling shareholders and related parties. From 2005 to 2012, Ma paid bribes totaling $1.1 million to a number of government officials in exchange for benefits to the company, the court said.

At least five officials involved with Ma's bribery case were already removed from their positions and punished, including the **former Communist Party secretary of the southern city of Guangzhou** and the **former chief of the investor protection bureau at the China Securities Regulatory Commission**.

Kangmei's 2020 losses reached 27.7 billion yuan, up nearly fivefold from a loss of 4.7 billion yuan a year earlier. In April, a Kangmei creditor filed suit seeking a bankruptcy restructuring of the company, accusing Kangmei of failing to repay 49 million yuan.

Last month, state-owned Guangzhou Pharmaceutical Holdings Ltd. agreed to invest as much as **6.5 billion yuan** in a government-led rescue of Kangmei.

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