

GLOBAL EMERGING MARKETS

OUTCOMES
BEYOND
PERFORMANCE

OUTCOME #33

Evidencing of human rights abuses in its supply chain to an Asian internet operator garnered an immediate response and action, opening up further channels for disclosure and communication.



Problem

Alibaba is a US-listed online marketplace originating in China. In 2013, the company sought an IPO in the US after the Hong Kong Stock Exchange rejected its proposed partnership structure which gives a small founder-led team the right to nominate up to a simple majority of the board for election by all shareholders. With \$25 billion raised, the IPO has been the largest one to date globally.

The company uses variable interest entity structures (VIEs) to hold internet content provider licences, and other licences and approvals for businesses in which foreign ownership is restricted or prohibited under local regulations in China. These VIEs have exclusive contractual relationships with subsidiaries of the listed company registered in the Cayman Islands. The legal and shareholding structure has been a controversial topic among investors. Other contentious issues it faces are the way it deals with the authenticity and quality of goods available on its various platforms, plus allegations of human violations by its suppliers.

For a number of years consumers (and the market) have been concerned about Alibaba's quality control and stewardship of its customers' purchasing rights, as some Chinese buyers have been wrong-footed by merchants of counterfeit products operating on Alibaba's platforms.



Action

We initiated our engagement programme soon after the group's September 2014 IPO, with the aim of helping the company to protect not only consumers but also its brand and future cash flows. Through our dialogue, we gained insights into the changes in board dynamics and governance strategy that have occurred since it was a private company. We pushed for a breakdown of its different businesses. We met with stakeholders and representatives such as the board director of its entrepreneurship fund to obtain more information about the company's mission and values. We visited its headquarters in Hangzhou to improve our understanding of its big data systems and analysis and find out how the company manages counterfeits, cyber security and data privacy issues.



Result

In June 2016, Alibaba held its first investor day and for the first time provided guidance on its annual revenues. It also provided historical financial data that was not previously available and explained to us the characteristics of its approach to human capital management and how cultural assessment is embedded within the decision-making process on mergers and acquisitions.

Alibaba has created a number of initiatives to fight counterfeits including the IP Joint Force System. To ensure sufficient buyer protection is in place, it has established a seven-day unconditional refund policy to reimburse affected customers. It uses its global payment network system to follow the flow of funds and help trace illegal business activities and on numerous occasions has helped local authorities in China and overseas clamp down on illegal operations.

The company continues to improve its ability to identify hackers in its customer base and also to help improve disclosure, transparency and user discipline by making increasing use of public disclosure through a number of websites to educate online buyers and sellers. Additionally, the executive chair was appointed as special adviser to the UN on youth entrepreneurship and small businesses, opening up further channels for disclosure and communication.



To read the full case study, visit <https://www.hermes-investment.com/ukw/blog/eos-case-studies/alibaba-cyber-security-disclosure/>

This document is for Professional Investors only. In Australia this document is directed at 'Wholesale Clients' only. Investing with Hermes may be restricted in other countries and as such, any person who receives this document is required to make themselves aware of their respective jurisdictions and observe any restrictions. This document does not constitute a solicitation or offer to any person to buy or sell any related securities or financial instruments. It pays no regard to the investment objectives or financial needs of any recipient. No action should be taken or omitted to be taken based on this document. Tax treatment depends on personal circumstances and may change. This document is not advice on legal, taxation or investment matters so investors must rely on their own examination of such matters or seek advice. Before making any investment (new or continuous), please consult a professional and/or investment adviser as to its suitability.

Any opinions expressed may change. The value of investments and income from them may go down as well as up, and you may not get back the original amount invested. All figures, unless otherwise indicated, are sourced from Hermes. Issued and approved by Hermes Investment Management Limited ("HIML") which is authorised and regulated by the Financial Conduct Authority. Registered address: Lloyds Chambers, 1 Portsoken Street, London E1 8HZ. HIML is a registered investment adviser with the United States Securities and Exchange Commission ("SEC").

For professional investors only

www.hermes-investment.com



HERMES
INVESTMENT MANAGEMENT