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China cracks down on algorithms as it attempts to rein in Big Tech

Article

The news: China rolled out a new regulation this week that would require apps using algorithmic recommendations to **let users opt out of personalized content and product suggestions**, per the South China Morning Post.

- The law is part of a wider crackdown **on Big Tech**, which has seen former superstars of the Chinese economy, such as ride-sharing app **Didi Chuxing,** fall afoul of the government.

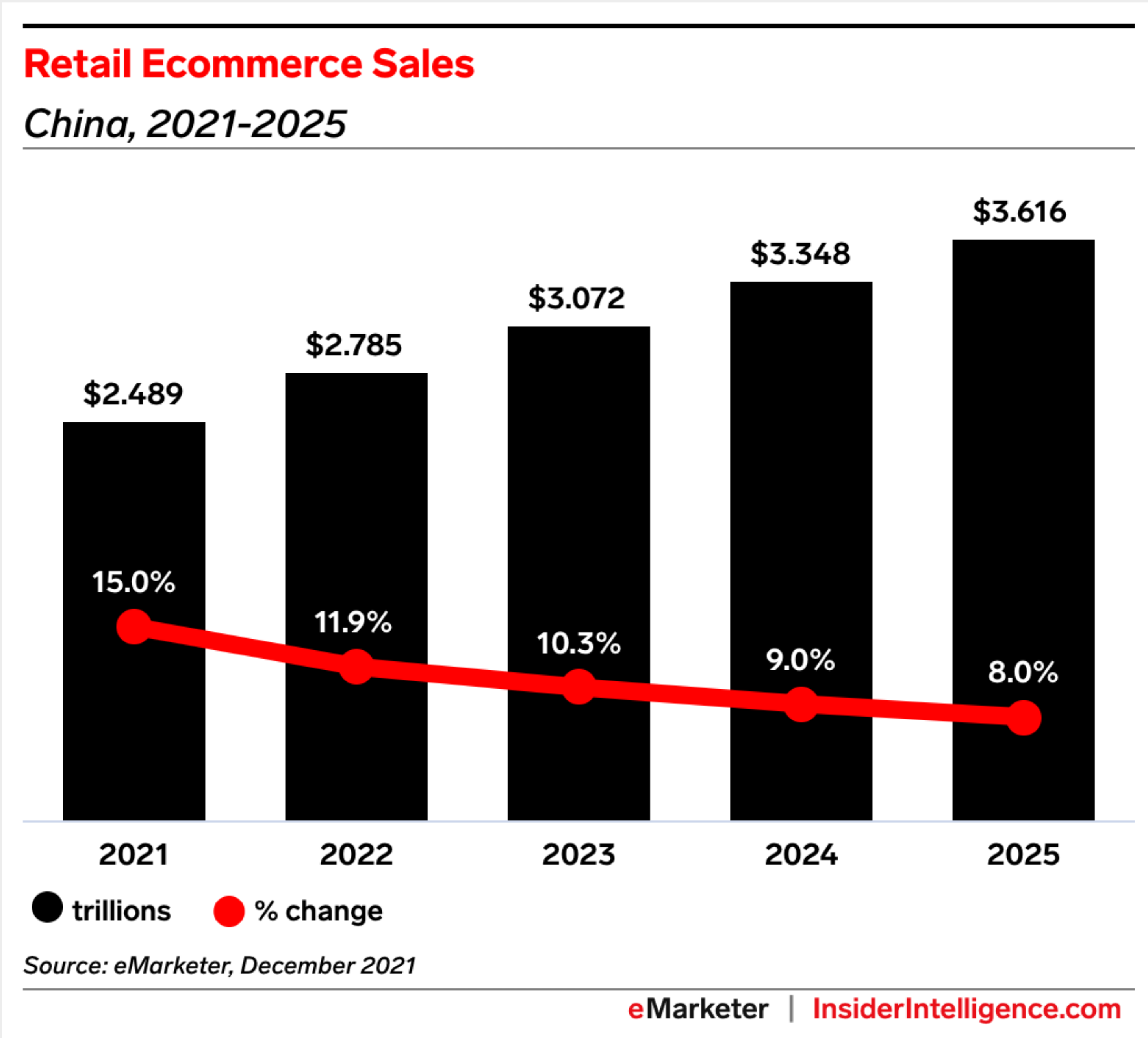
- The law's remit is broad, however, and how Beijing will implement and enforce it remains unclear.

The rationale: The Cyberspace Administration of China (CAC), one of the parties responsible for drafting the legislation, said the goal is to prevent "algorithmic discrimination," whereby apps charge people different prices for the same product or service depending on their spending habits. It also seeks to combat "content intoxication," which refers to the practice of keeping users engaged with an app through a constant flow of content tailored to their interests.

- The government is also worried about the ability of algorithms to shape public opinion and spread social movements via information recommendations, which partly explains why it is taking such a strict stance.

The implications: Several of China's most successful companies—including **Alibaba**, **Tencent**, **Meituan**, and **TikTok**'s parent company, **ByteDance**—rely heavily on algorithms to drive consumer engagement and sales. The new law will almost certainly hinder growth for these companies.

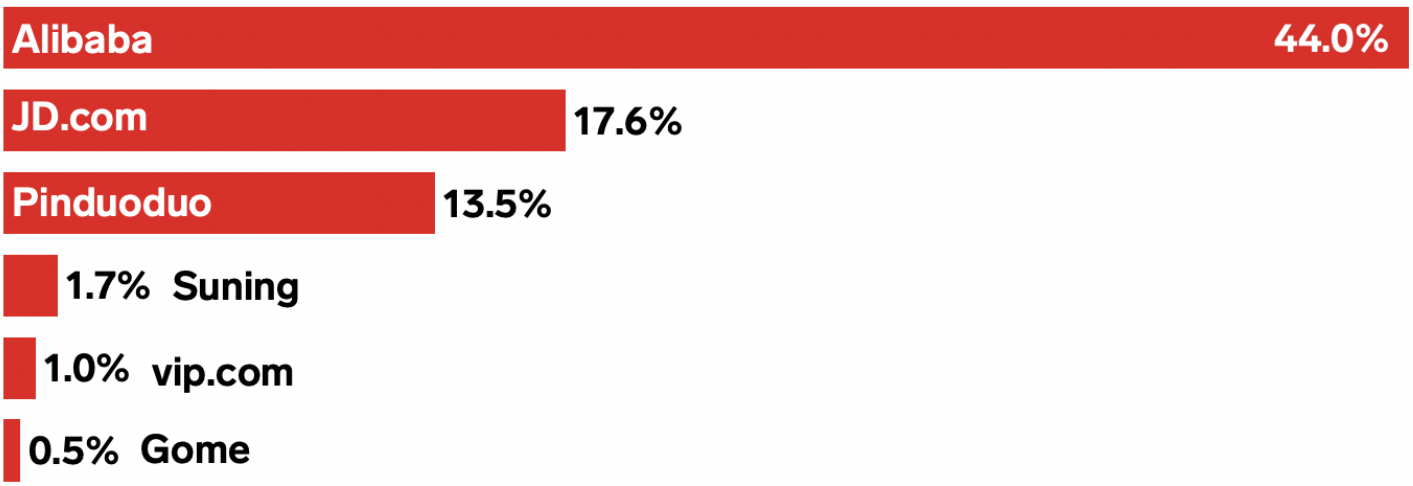
- In Q3 2021, Tencent reported its slowest revenue growth since it went public in 2004, while Alibaba's profitability **decreased by 38%** year over year, per The New York Times.
- We forecast that retail ecommerce sales growth in China will slow to **11.9%** this year, down more than 3 percentage points from 2021. It's getting more expensive to acquire new customers as it is, and with the new law potentially shrinking the lifetime value of each customer, the path to profit will become even more difficult.



Seen in the greater context of China's recent antimonopoly campaign, the reduction in algorithmic efficacy may help small businesses compete more effectively with dominant players. But given the tremendous market share that companies like Alibaba and **JD.com** already have, the odds of a new entrant being able to unseat established giants are low.

Top 6 Companies in China, Ranked by Retail Ecommerce Sales Share, 2022

% of total retail ecommerce sales



Note: includes products or services ordered using the internet via any device, regardless of the method of payment or fulfillment; excludes Hong Kong; excludes travel and event tickets, payments (such as bill pay, taxes, or money transfers), food services and drinking place sales, gambling, and other vice goods sales
Source: eMarketer, December 2021

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Will others follow? Anti-Big Tech movements have been gaining steam around the world, including in the US. While China's regulatory approach is more heavy-handed than most, other countries can study the effect of these regulations on homegrown innovation, economic growth, and consumer behavior, and apply those findings to their own legislative agendas.

- Expect to see some companies head off such legislation on their home turf. For example, **Instagram** head Adam Mosseri announced that the company would give users the option to revert to a chronological feed this year, following a congressional hearing into the harmful effects of algorithmically recommended content.