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Conference Paper

A Study of Startups in Hong Kong

22nd Biennial Conference of the International Telecommunications Society (ITS): "Beyond the Boundaries: Challenges for Business, Policy and Society", Seoul, Korea, 24th-27th June, 2018

Provided in Cooperation with:

International Telecommunications Society (ITS)

Suggested Citation: Lee, Paul S. N. (2018) : A Study of Startups in Hong Kong, 22nd Biennial Conference of the International Telecommunications Society (ITS): "Beyond the Boundaries: Challenges for Business, Policy and Society", Seoul, Korea, 24th-27th June, 2018, International Telecommunications Society (ITS), Calgary

This Version is available at:

<https://hdl.handle.net/10419/190409>

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A Study of Startups in Hong Kong

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**Paper presented at the Conference of ITS Seoul 2018 held in June 24-27, 2018 at
Korea University, Seoul, Korea**

A Study of Startups in Hong Kong

Abstract

This study examines the factors contributing to the success of startups in attaining a unicorn status by comparing three successful companies, namely, WeLab, SenseTime, and GoGoVan. We investigate the development of these startups and the various stages of their growth, with a focus on the success factors for getting continuing funding from various sources.

We found that a competitive business model of a startup is a first factor to nurture a unicorn. The second factor is the executive power of the founder(s). Almost without exception, there are ups and downs of running a startup, which highlights the importance of leadership. The founders do not need only vision and passion, but soft skills in managing the business and attracting financial support as well. We also found that all three startups have a “China” element. The attractiveness to Chinese market and capital seems to be a must for Hong Kong unicorn to come into shape.

Interestingly, profit is not that important a factor for a startup to become a unicorn. Very often, investors buy on the potential of the startup rather than immediate profit. The four factors, namely, competitiveness, executive power of founder(s), attractiveness to Chinese market and capital, and future potential have proved to be important for a startup to succeed in Hong Kong.

At the end of the paper, we discuss three different models of running a successful startup. It ranges from facilitating financial loans, using innovative AI technology to solve specific problems, to providing a one-stop e-commerce platform. We anticipate that more startups will succeed in Hong Kong since the unicorns have thrown light on the path which latecomers can follow.

A Study of Startups in Hong Kong

Introduction

In 2015, Startup Genome pointed out in its report the weaknesses of the startup ecosystem in Hong Kong. The weaknesses included a gap in global knowhow, a seed-funding gap, a talent gap, a lack of sub-sector strategies such as FinTech and IoT, and a lack of entrepreneurial mindset [1]. The Hong Kong SAR Government, however, later advertised through BBC StoryWorks, claiming that Hong Kong has become the fifth fastest growing and 25th largest overall start-up ecosystem in the world according to a survey done by Compass in 2015 [2].

Among the five successful startups in the report, WeLab was particularly important as it had valued at more than US\$1 billion, becoming the territory's first "unicorn" - a startup company valued at over US\$1 billion. WeLab operates WeLend which is Hong Kong's leading online lending platform, and Wolaidai, one of China's largest mobile lending platforms. In 2016, WeLab was named in a KPMG-Sponsored report as one of the top 100 fintech companies in the world – No. 6 in China and No. 33 globally [3]. Despite its "unicorn status", Hong Kong people know little about it – reflecting a low community awareness of startups and their activities in Hong Kong.

It was not until August 2017 when another startup GoGoVan became a "unicorn" then Hong Kong people started to know they had the "first" unicorn in town, thanks to the media blitz. In fact, before GoGoVan, Hong Kong had another unicorn after WeLab. It is SenseTime which develops its own AI deep learning algorithm for image recognition. It has more than 400 customers and strategic partners, including China Mobile, Meitu, Sina Weibo, China UnionPay and Huawei Technologies. It reached its unicorn status one month earlier than GoGoVan [4]. The reason why GoGoVan was conceived by people as the "first" unicorn in Hong Kong is probably due to its popular van-hiring service which has been used by many in Hong Kong. WeLend targets some specific sectors while SenseTime deals mainly with B2B services. Most people have no experience in using the service of WeLend or SenseTime. But GoGoVan is ready for everyone to use with a simple tap on a mobile app.

In this study, we will examine the factors contributing to the success of a startup in attaining a unicorn status by comparing the three successful companies, namely,

WeLend, SenseTime and GoGoVan. We hope to throw light on the successful path for other startups to follow. The method of case study is used. We examine the development of these startups and the various stages of their growth, with a focus on the success factors for getting continuing funding from various sources.

Profile of Three Unicorns in Hong Kong

WeLab was founded in January 2013 by Stanford graduate Simon Loong. In July the same year, WeLend was launched as Hong Kong's first fintech online lending platform. A year later, WeLab expanded into China by launching Wolaidai, another mobile lending platform. The fintech drew an initial Series A funding of US\$20 million in January 2015 from a group of investors including Sequoia Capital and Hong Kong tycoon Li Ka-Shing's TOM Group. It has grown impressively and succeeded in getting US\$160 million in Series B financing at a valuation estimated at nearly US\$1 billion in early 2016. The investors for this round included Malaysia's Khazanah Nasional Berhad, ING Bank and China's Guangdong Technology Financial Group. In November 2017, it raised US\$220 million further from World Bank's International Finance Corporation and Alibaba Entrepreneurs Fund. The firm's Wolaidai and WeLend services have 25 million users and processed US\$28 billion of loans [5].

SenseTime entered the unicorn league when it raised US\$410 million in a Series B round in July 2017, with a valuation of US\$1.5 billion. SenseTime was founded in 2014 by a group of academics, researchers and students, led by Professor Xiaoou Tang of the Chinese University of Hong Kong (CUHK) and CEO Li Xu, who received his PhD from CUHK in 2010. The group focused on computer vision and deep learning technologies with application in facial, image and text recognition. Its system can differentiate several ten thousand people in a second, with information about their age, gender and even emotions. Its application include crowd control, detection of criminals and network security.

SenseTime's first major funding round was in December 2016 when it raised US\$120 million from investors that included Beijing-based CDH Investments, Dalian Wand Group, IDG Capital Partners and Star VC. It now has more than 400 customers and strategic partners, including China Mobile, Meitu, China UnionPay, Sina Weibo,

China Merchants Bank, Huawei Technologies and Xiaomi. SenseTime also works with the Ministry of Public Security's Third Research Institute to develop China's citizen network identity infrastructure. The team has established subsidiaries in Kyoto and Tokyo. They picked Japan because it has more advanced automobile and manufacturing industries [6].

GoGoVan was started by Steven Lam when he was 26 years old and had recently graduated from UC Berkeley's Haas School of Business. Lam launched the company in 2013 as a mobile app to help people in Hong Kong hire cargo vans to move furniture, goods and package delivery. By the end of its first year, GoGoVan had signed up 4,000 cargo vehicles and their drivers. In 2014, it raised US\$6.5 million which helped the startup to expand its services to Singapore, Taipei, Melbourne and Sydney. In 2015 it obtained US\$10 million for its series B financing.

In May 2016, the team got "a decent amount" for future business expansion in its series C funding. The amount was not disclosed. New Horizon Capital, Singapore Press Holdings and Alibaba were among the investors. In August 2017, GoGoVan completed a merger with 58 Suyun, the freight business of mainland Chinese online classifieds giant 58 Home to become another unicorn in Hong Kong. The merger will leverage 58 Suyun's existing premium brand, larger user base and online traffic for a quick expansion into 300 cities in China. GoGoVan now has 180,000 registered drivers with their vehicles on its network [7].

Success Factors in Becoming Unicorns

A unicorn is a startup company with a total valuation of more than US\$1 billion. The use of the term for defining this kind of company is attributed to Aileen Lee [8].

According to Techcrunch.com in 2017, the number of unicorn companies was 267 with a total valuation of US\$920.8 billion and a total amount raised of US\$176 billion [9]. Only a very small percentage of startups could become unicorns.

There have been many studies on the success factors for startups. The European Commission issued a report entitled *How to Catch a Unicorn* in 2016. The report concludes that unicorns in general are:

1. IT-based and grounded in network effects;

2. Rather young global companies that match unsatisfied demand;
3. Capable of scaling up its supply through production;
4. Very affordable with their innovative services and products;
5. Relying on a strong favourable business environment;
6. Building on fast expanding markets;
7. Depending on Venture Capital;
8. Potentially disruptive for other sectors and firms [10].

While the EU report attempts to provide a comprehensive picture for the success of startups, some studies focus on the macro-social and economic factors, or the micro- or meso-level managerial and entrepreneurial factors. For example, in a study on startups in emerging markets, Prashantham and Yip [11] point out four key factors for multinationals to consider when they want to forge partnership with startups. These factors are:

1. The maturity of the entrepreneurial ecosystem;
2. Appetite for entrepreneurship;
3. Outsider status of venture capitals;
4. Access to novel innovations.

In other words, startups which do not handle these four factors well are less likely to get the capital they need for expansion and upscaling.

Nicole Gravagna, coauthor of *Venture Capital for Dummies*, advises venture capitalists to look for three things of a startup to decide if they want to invest in it:

1. A founder that has the appetite to take the company all the way;
2. The company's challenges are aligned with the unique advantages of the team;
3. The team is willing to work with the venture capitalist on clarity of vision [12].

The quality of the entrepreneur and his/her team has been emphasized by keen observers of startup businesses. Startup leaders not only need a vision and a business model, but the ability to execute the vision with a strong team and see through various stages of growth, fundraising, upscaling, and taking hold of market share. Throughout the process, the leaders need to produce compelling new products, overcome

customers' fear that the venture will fail, demonstrate growth and profit potential, and shift strategy and technology if needed [13].

In the following, we will examine the experience of the three unicorns in Hong Kong, and see if they share similar factors for success.

An Innovative Business Model

From the development of the three unicorns in Hong Kong, one can see that a crucial factor for a startup to succeed is to first have an innovative business model. That model matches the unsatisfied demand. GoGoVan is a good example for the innovative business model. At the beginning, Steven Lam and his friends started an advertising business. It helped clients to place advertising stickers on take-away boxes which were provided free to restaurants and food shops. They however found it very difficult to hire cargo vans during peak hours to deliver the boxes to restaurants. Hiring a cargo van was a pain for consumers and businesses. Truck drivers also suffered by slow and inefficient services provided by various middlemen. The team was alerted to this business opportunity. They found a problem and tried to solve it by matching the unmet demand for quick and efficient logistic services for moving furniture, goods, package delivery, etc. Then GoGoVan was launched. They signed up as many cargo vans and their drivers as they can. By the end of its first year, GoGoVan saw its transaction volume doubled every two weeks.

WeLab also started with an innovative business model in lending. Its founder, Simon Loong, operated Hong Kong's first online lending platform. It disrupted the conventional lending market which demanded at least one personal interview between the financier and borrower. Using risk-testing technology to conduct credit assessment online, WeLab however enables clients to borrow money with a few taps of their smartphones without the need of seeing a loan broker. WeLab boasts of approving a loan in as fast as 1.7 seconds. It claims to have a delinquency rate of 1% on loans that are 30 days past due, lower than most credit cards issued to new users. In the early years, WeLab adopted a policy of "loan less, repay less", providing a loan with a maximum amount around US\$4,000 and charging an interest below market rate [14]. WeLab succeeded in serving a relatively unserved market of young and low-income people.

A Strong Team with Leadership

Apart from a sound business model, a strong team with leadership is also crucial to the success of startups. The founders are particularly important. They are not only initiators with a vision and passion, they are also captains steering the course of a voyage. They need to be sensitive to market trends, competitors, and technological changes. They also need soft skills to manage staff, customers, financiers, suppliers, and media. GoGoVan's development provides an example to demonstrate the crucial role of leadership in startups.

No sooner after GoGoVan made its presence felt in the market, Uber made a surprise move into GoGoVan's territory by launching its UberCargo in Hong Kong in 2015. In that year, GoGoVan already signed up 70,000 vans across six countries, including Hong Kong, Singapore, Australia, South Korea, Taiwan and China [15]. With this portfolio, it succeeded in getting series B funding of US\$10 million. If GoGoVan had limited its service to Hong Kong, and could not get the series B funding, Uber would probably continue to stay in the market rather than withdrew its cargo service after one and a half year.

It should be noted that apart from Uber, GoGoVan has a strong competitor in all these years. It is Lalamove which operates with the same model in logistics. It was launched in the same year as GoGoVan, originally named EasyVan. It now operates in more than 100 cities across China and Southeast Asia, with a pool of 2 million drivers. Facing this competitor with strong operation in China, GoGoVan moved to merge with 58 Suyun which is a leader of freight business in China market. According to Lam, "The combined company will leverage 58 Suyun's existing premium brand, large user base and online traffic for a quick expansion into 300 cities in mainland China" [16]. A visionary leader with a strong team to execute the vision is a crucial factor for the success of a startup.

China Connection

The third important factor for a startup in Hong Kong to succeed is to have China connection. WeLab has an operation Wolaidai in China about one year after its launch

of WeLend in Hong Kong. In 2016, three years after its operation, it had loaned money to 2.5 million customers, with a majority in mainland China [17]. The potential of China market was decisive for its success in getting US\$160 million in its Series B financing in 2016, and another US\$220 million in Series C financing in 2017.

Similarly, the Chinese customers, operation, and business partners of SenseTime have offered a strong backup for its success in raising funds. In an interview with *South China Morning Post*, Xu, the CEO of SenseTime, pointed out that the startup first explored mainland China because of the explosive demand in the market, where there is a huge population and big amounts of data being collected. Its first major funding round was in December 2016 when it raised US\$120 million from investors that included Beijing based CDH Investments, Dailian Wanda Group, IDG Capital Partners and Star VC [18]. SenseTime has emerged as the largest AI startup by revenues in China. Most of its revenues (87%) are generated from the China market [19].

The importance of China factor to startups in Hong Kong is probably due to the geographical and cultural proximity of Hong Kong to China. Since China is the second largest economy in the world with lots of capital seeking investment opportunities, Hong Kong startups become ideal targets as they understand Chinese cultural practices better than firms based in non-Chinese cultural settings. For the startups of Hong Kong, what they need is venture capital and promising revenue streams, both of which are accessible in the China market.

Potential of Generating Revenues

It is interesting to note that profit need not be a factor for startups to become a unicorn. Very often, investors buy on the potential of the startup rather than immediate profit. The “potential” is realized through genuine demands demonstrated by its operation in early stages.

In 2015 when GoGoVan started its operation for two years, it had a market share of over 60 percent, with around 20,000 drivers listed on its platform. Because of the vigorous competition, GoGoVan could not monetize its platform. It did not charge

drivers and customers for the service it provided. It had to expand its market share by soliciting as many drivers as it could until the company's scale was big enough for it to think about taking commissions or selling advertising space on its vans and app. However, it attracted a few rounds of venture capital, one of which was from the failing mainland social network Renren.com. The site invested HK\$80 million in GoGoVan for a 10 percent stake [20]. The startup then was valued at HK\$800 million based on the capital injection. This incident indicates that demonstrating growth potential in early stages is important for a startup to survive and upscale until it becomes a unicorn.

If a startup can garner profits in a short period, like SenseTime, its attraction to big funding will certainly be enhanced. SenseTime was launched in 2014, its sales figures kept climbing up with revenue growth by 400% each year. And it turned profits in 2017. The fast growth explains why in April 2018, it obtained a fresh Series C funding round of US\$600 million, just nine months after its then record-breaking (in the AI scene) Series B round of US\$410 million. The latest financing brought in new shareholders including Alibaba, Suning and Singapore's sovereign fund Temasek. The substantial funding enables the AI startup to not only develop new products, but to invest in companies which have products related to its AI technology [21].

Timing, teamwork, funding environment, community awareness, government support, and luck are certainly all important for a startup to succeed. Our study, however, shows that four factors, namely, a competitive business model, executive power of founder(s), attractiveness to China capital, and future potential are particularly important for a startup in Hong Kong to succeed.

The Models of Successful Startups

Benjamin Low, founder of D3SIGNS, considers that unicorns are created through business model innovation. The key success is being able to disrupt the existing market space, or create a new niche market that is totally unconventional. Amazon, eBay, and Alibaba are good examples of digital disruption in e-commerce [22]. Coincidentally, the three unicorns in Hong Kong represent three different models of running a successful startup. The models range from smoothening the process of

financial loans, using unique technical knowhow to solve specific problems, to providing a one-stop service platform. The three unicorns represent success in three areas: Fintech, AI high tech, and E-commerce.

Hong Kong, as a global financial centre, a tax-free port, a world-class logistics hub, and an export base for China with well-established infrastructure, rule of law and freedom of communication, is a good place for fintech startups to launch their operation. However, to win out in keen competition, the business model must find an unmet demand to start with. WeLab is able to meet the demand for small loans among ordinary factory and office workers who could not provide collaterals. Yet, WeLab is able to have a reliable credit check by its own software using 800 data points related to potential borrowers to make decision on approval.

Quite a few fintech startups have set up their operation after WeLab's success. Some of them are successful in getting Angel funding or Series A funding. For example, founded in 2016, Qupital runs an online invoice discounting platform supporting SMEs to raise cash. It raised US\$2 million in a seed funding round in May 2017. TNG was founded in 2015 providing e-wallet services. In November 2017, it raised US\$115 million in Series A round. It now counts 13 countries, 852 banks and over 183,000 cash pick-up points [23]. Since financial transactions could involve high risks for both users and service providers, building up "mutual trust" is a very important factor for fintech startups to grow. Given Hong Kong's well-established infrastructure in banking, finance, judiciary, network security and taxation, fintech startups find it easier to launch its operation than in many other countries.

Apart from fintech, the second successful model for startups is to have technological innovations. SenseTime points to the favourable outcome of associating or collaborating with science researchers in Hong Kong. Prior to SenseTime, a successful entrepreneur, Tao Wang, who was a graduate of Hong Kong University of Science and Technology, launched its business in 2006, Da Jiang Innovation (DJI), in his dorm room. DJI is now the world's leader in the civilian drone and aerial imaging technology industry, accounting for 85% of the global consumer drone market [24]. This type of "technology-intensive" startups certainly bear high risks, but the return can also be very high, as demonstrated by the success of SenseTime.

The third type of successful model is providing a common platform for e-commerce. Basically, it undergoes a process of “disintermediation”, eliminating small middlemen in an industry. It seems the success of this business model depends on an early entry into an untapped market, in addition to the success factors discussed above.

Latecomers usually find it hard to compete with the incumbent who has taken a majority share of the market. GoGoVan started the cargo van delivery service early, which was a factor for its success in fending off Uber’s competition appeared two years later.

At present, Hong Kong witnesses some potential unicorns in the e-commerce area. They have something new to offer in a relatively untapped market. For example, DayDayCook was launched in 2012. It attracts millions of viewers to its recipes and video shared through a Facebook page, YouTube channel, website and app. It expanded into China in 2015 and succeeded in raising US\$10 million from two rounds of fundraising in 2017. Grana, another e-commerce startup, was launched in 2014 as an international platform that sells wardrobe essentials to customers across 67 countries from its warehouse in Hong Kong. It secured US\$6 million in a seed round, and US\$16 million in Series A round of funding [25].

Apart from fintech, AI high technology, and e-commerce, there are other areas for startups, such as social interaction, cybersecurity, big data, real estate, health care, hardware, etc. But so far, success has been seen only in the areas of fintech, AI high technology and e-commerce. Since the startup ecology of Hong Kong is given more attention by the government as well as the public now, thanks to the emergence of the three unicorns, it is anticipated that startup success will be seen in other areas later.

Conclusion

From a study of the three unicorns in Hong Kong, we found that a competitive business model of the startup is a prima facie factor to nurture a unicorn. The leadership and executive power of the founder(s) are crucial to the success of a startup. Without a determined team to carry out their vision, the startups could hardly survive and grow. The access to the market and capital of China seems to be a must for Hong Kong unicorn to come into shape. This is probably due to China’s proximity, in terms of culture and geographical location, to Hong Kong. Last but not

the least, the startup must demonstrate its potential to grow and generate revenue in future in order to get funding to continue its operation. This is particularly important in early stages.

So far, the three unicorns point to three areas which are favourable for startups in Hong Kong to attain success. They are fintech, AI high technology, and e-commerce. Fintech needs to build up a “mutual trust” between the service provider and customers. AI high technology must “innovate to lead” the market, not just to meet unsatisfied demand. It should show how innovative technology can change the current practice and ways of doing things. E-commerce basically carries out the process of “disintermediation”, eliminating middlemen and cutting the transaction costs for both suppliers and consumers. The unicorns have thrown light on the path which other startups can follow. As startups in Hong Kong just show their force through the three unicorns, it is anticipated that more successful startups will appear in Hong Kong.

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