

A Business Model Analysis of Sneaker Trading Industry – Whether the Sneaker has become an Alternative Investment?

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ABSTRACT

This paper seeks to investigate the sneaker trading industry through the analysis of the business model. Through a variety of ways of data collection, including both primary and secondary data, the mechanism of sneaker speculation was able to be found. The analysis of the profit model also helps to explain the reasons for the high-sky prices of sneakers. The buyers of sneakers are composed of two categories: enthusiasts and speculators, where speculators only take up a small proportion. The high prices of sneakers were achieved due to the Hunger Promotion by the suppliers, and the act of sneaker speculation has a lot of similarities to the stock market.

Introduction and Background

Sneakers have captured more and more people's attention not only for its fashion but also for higher and higher price in the secondary market. The price of sneaker AJ1 has raised 900% in four days and is traded for RMB 12,000 from the issuance price 1299. A lot more examples can be seen on the market (See Chart 1). Seeing the rich profitability, a lot of investors has considered the sneakers as an alternative to enrich and diversify their investment portfolio. Not only on the consumer side, for the business side, start-ups are taking part and building up the platform to facilitate the sneaker trading and earn the commission fee. For example, Poison, a trading platform in China, does not limit their service to facilitate the trade, but also provide services like authentication and shipping (Zheng, 2019). Their target customers are young generations who owns free concept of consumption and has their own ideas for fashions. For other platforms like Nice, Stock X are also popular online shopping platforms and earn huge profit for their niche market in sneaker trading. What's more, sneaker trading market is more and more like the stock market through using leverage, margin and installment plan (Alan, A., 2019). So, in this paper, the author is trying to answer three questions:

1. What is the value-chain look like for the sneaker trading market?
2. Why is the sneaker selling with such a high premium?
3. What are the customer persona and the motivation like for the sneaker traders?

Table 1. Sneaker issue and market price

Sneaker Series	Issue Price (RMB)	Market Price (RMB)	Celebrities' endowment	Premium(multiples)
Adidas Yeezy boost 350 v2	1899	4500-9600	N/A	5.1
Trophy room x AJ5 Black&Red	1599	49000-52000	He Chen	32.5
AJ1 Retro OG High NRG Igloo	1299	38000-50000	N/A	38.5
off-white x AJ1 European limited-edition	1299	26000-50000	Jay Chau	38.5
Strange love x nike SB dunk	969	6100-17000	Celebrities' style	17.5
Nike Air yeezy 2 October	1999	90000-100000	Kayne	50.0
Nike Air yeezy 2 Nrg	1999	56000-90000	Kayne	45.0
Adidas yeezy 750 OG Grey	2799	19000-30000	N/A	10.7

Source: Desktop research

Theoretical Framework and Methodology

Demand and Supply Analysis Method

1. Demand

Demand is referred as the willingness and ability of consumers in a market. The graph of demand has an x-axis of quantity demanded, and a y-axis of price. Graph of demand has a downward slope, which can be explained by the law of demand: as the price increases, demand decreases, and when the price decreases, demand increases. The demand of consumers are determined by the prices of the products, and consumers tend to have higher demand towards products with lower prices as purchasing the product would not take up a large proportion of consumers' wealth.

2. Supply

Supply is referred as the willingness and ability of producers to produce in a market, while the graph of supply is upward sloping. The graph of supply has a x-axis of quantity supplied and a y-axis of price. The law of demand claims

at higher prices, producers are able to supply a larger amount of goods, whereas at lower prices, producers supply less. Producers need to ensure the amount of profit they earn, thus when the prices for their product is low, they won't be willing to produce a lot. This paper has adopted the supply and demand analysis framework to explain the pricing strategies and logics of the sneakers trading on the secondary market.

Interview Method

Interview method refers to a researcher asks questions to the interviewee according to the predetermined interview outline around a specific topic, using tools to record the conversation and learn the relative social situation. Before sending out large amount questionnaires on general respondents who might not be a sneaker trader, the author interviewed an sneaker trader to adjust the question designs and get access to more of the sneaker traders through him for valuable information, which helped the author to gain insights like the enthusiasts' motivations for spending premiums on sneakers.

Questionnaire Method

Questionnaire method refers to a researcher asks respondents to do questions in the form of survey, and hence gather information. The author adopts a questionnaire method to collect primary data to understand the demand-sides—sneaker buyers' characteristics. The draft questionnaire is critiqued and tested by one interviewer who is a 3-year experienced sneaker buyers. The interviewer also helps to spread the questionnaire to ensure people who answered these questions are those with secondary market sneaker buying experience.

Secondary data analysis

Secondary data refers to the data that is collected by others but not the researcher on their own, compared with primary data, secondary data is less time consuming and would require less effort. The author adopts reports from XKB Data Research Center, iiMedia Research and other sources in the third section--demand analysis part to gain more insights on the market size, people distribution of the sneaker market speculation.

Analysis

The Source of Sneaker Speculation—Brands

Brands are those who issue the new sneakers. Because of their demand for higher revenue per deal, the sneaker brands may launch limited amount products to boost the price of the sneakers. The reasons for sneaker speculation are because the demand is far more than the current supply. As the sneaker producers, they have full control of the supply-side, who determines how many sneakers supply of a certain series to the market. If the brand issue sneakers that are far below the market demand, then the price of the shoes will be very high for market demand is far above the supply.

This is the business logic behind the limited edition and is presented through the graph below.

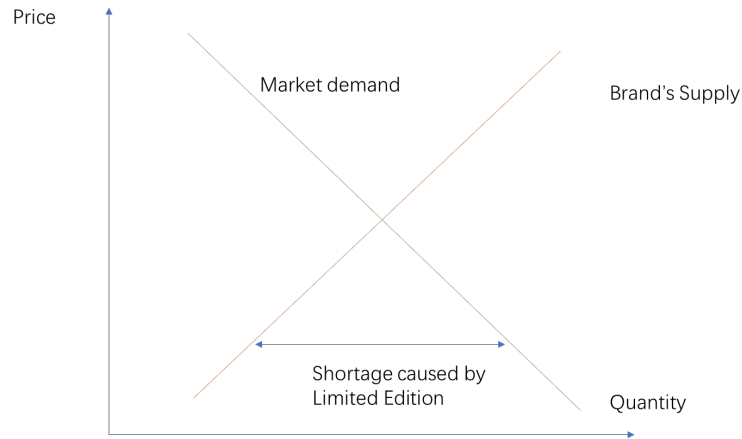


Figure 1. Demand and Supply Analysis of Limited Edition caused by shortage

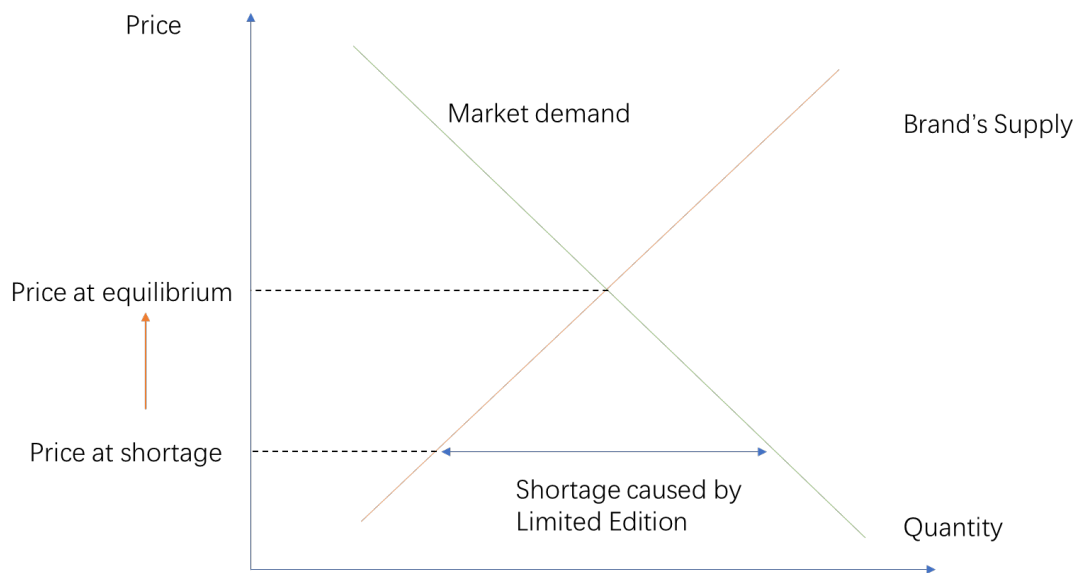


Figure 2. Demand and Supply Analysis for price enhancement of Limited-edition shortage

The intermediaries of Sneaker Speculation—Platforms

The intermediaries include the online platform, which engaged sneaker resellers for sneaker trading. Their business models are in two formats: one is the commission fee; the other is the service fee. Commission fee is earned because the platform has helped the products expose to more buyers, which increases the possibilities for product sales. As a result, the platform will take 5-10% as commission fee for providing a trading platform and the exposure. The service fee is earned because the platform can also provide services like identification, shipping and cleaning. The famous

platform includes stockX, Goat, Nice and Youhuo. The graph presents the trading platform provided by StockX, where the users can trade the sneakers as stock by checking the bid price and ask price to buy low and sell high. The mechanism is the seller will ask the market for a price for the limited-edition shoes. It is the lowest price that the sale will take. The buyer will bid for the product by providing the highest amount that he/she is willing to pay. When the buyer's price is higher than the asks' price, there is a deal.

Overview of the key plays among intermediaries

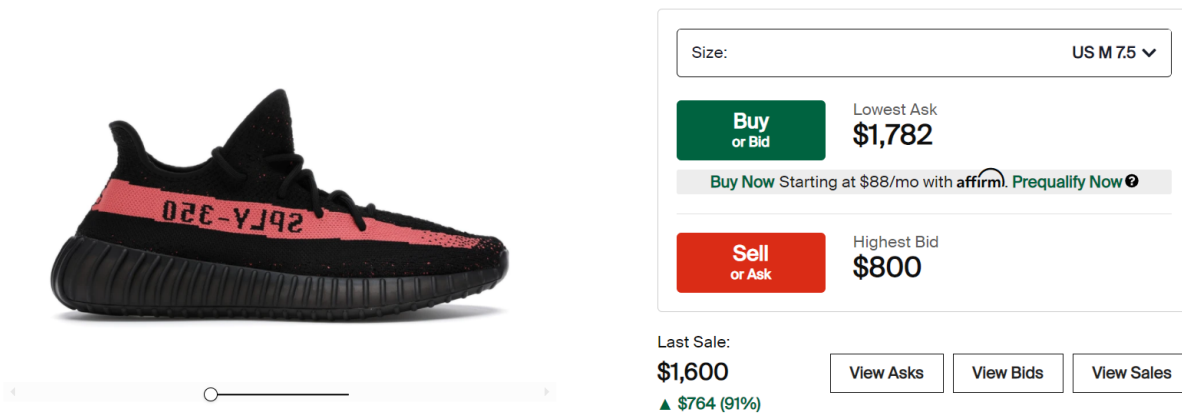


Figure 3. Picture of selling and buying page from intermediary

There are several key intermediaries in China including StockX, Goat, Nice and Poison.

The core competitiveness for Stock X is that first, it highlights the characteristics of fidelity, and both sellers and buyers can check the real-time trading price through the platform. Second, it provides convenience for the merchants, they do not need to register a store, and the sneakers can be listed through the Stock X pre-set templates.

Poison is recognized by a lot of traders for it provides comprehensive quality inspection services, including photos of product details, authenticity identification through optical analysis and component analysis, and tie exclusive anti-counterfeiting buckles after the identification to win the trust for consumers. Because of the trustworthiness, it will charge the seller a corresponding commission in different proportions according to the commodity category as part of their revenue. Goat and Nice are a lot like Poison. But poison wins more trust buy the good services.

YOHO! Buy provides consumers with a platform with Chinese fashion online collection store so that consumers can buy many different trendy brands on the same platform it provides consumers with flavored packaging to improve customers' experience after purchase: simple but not monotonous, and exquisite packaging

The Profit Model of Intermediaries

First, the market maker may add certain amount to the ask price, and when there is a deal, the market maker will get the additional amount it added to the original ask price.

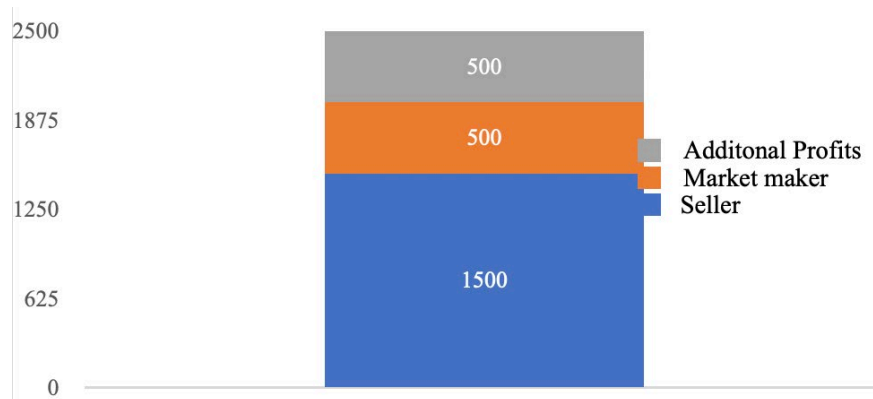


Figure 4. Profit Distribution of a pair of 2,500 shoes

For example, if the asking price of a pair of shoes is 1,500 RMB, the market maker will add 500 RMB and sell for 2000. However, if the shoes can be sold for 2,500 RMB, the market maker will lose 500 additional profits for the conservative pricing. In this business model, the market makers should have strong pricing capability. If they price the product too high, the product can hardly be sold and there is no profit. If they price the product less high, they will lose potential higher profit.

Intermediaries and buyers Dynamics

Additionally, these market makers also provide additional services to expand their revenue. For example, the shoes identification and shipping fees are also provided as a package. Almost all the buyers need this service, and they will buy together with the shoes as a bundle, which generates additional sources of revenue for the market maker companies. Compared with financial market makers, they are in similar roles.

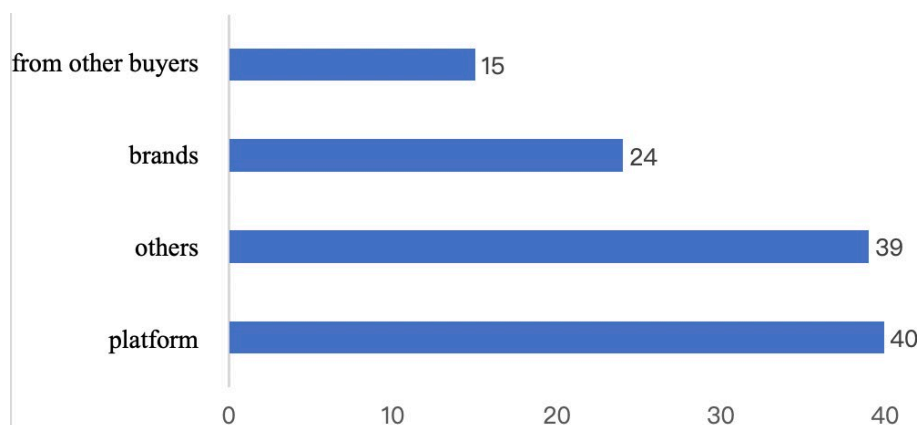
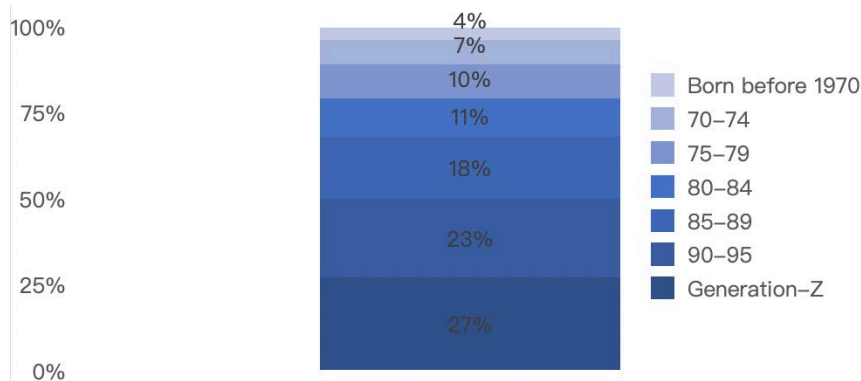


Figure 5. The channels used for sneaker trading

Buyers in the sneaker market use a variety of different channels, the channel that is most preferred by the buyers are through platforms. Among the 46 respondents, 40 out of them buy sneaks from platforms. The next channel that is widely used by sneaker buyers is others. Some other channels includes eBay, GOAT, xianyu. Buying from Official brands is channel for over 50% of the respondents. The least preferred channel is through buying from the other buyers. In a nutshell, platforms are preferred by almost all the sneaker traders for their trustworthiness, transparency and convenience.

Demand side—enthusiasts and speculators

According to the research by i-Media, Generation-Z is the largest and youngest group in the primary sneaker market, which almost takes 30% of the sneaker demand side. People who were born at late 1980s together with Generation-Z, also two of the youngest generations, takes half of the total demand. As a result, with the strong demand and



enthusiasm of sneaker consumption and investment, these young generations will also be the major demand side of sneaker resales market.

Figure 6. 2018 Sneaker Demand-Side by Age Groups (Source: https://www.xkb.com.cn/article_555063)

Enthusiasts take the majority, and they contribute 88% of the total buyers, whereas speculators are the 12% of the buyers, however, they contribute almost half of the total sneaker online resales platform revenue. The result echoes insights from the primary research.

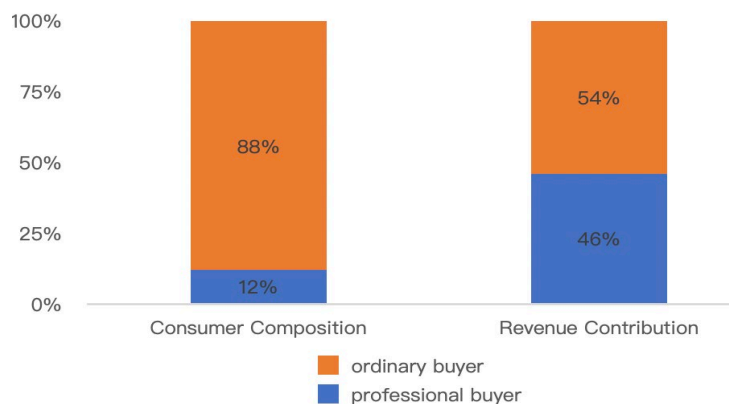


Figure 7. Consumer composition and revenue contribution of ordinary buyer and professional buyer
(Source: https://www.xkb.com.cn/article_555063)

The author also tests the authenticity of the secondary research through primary research.

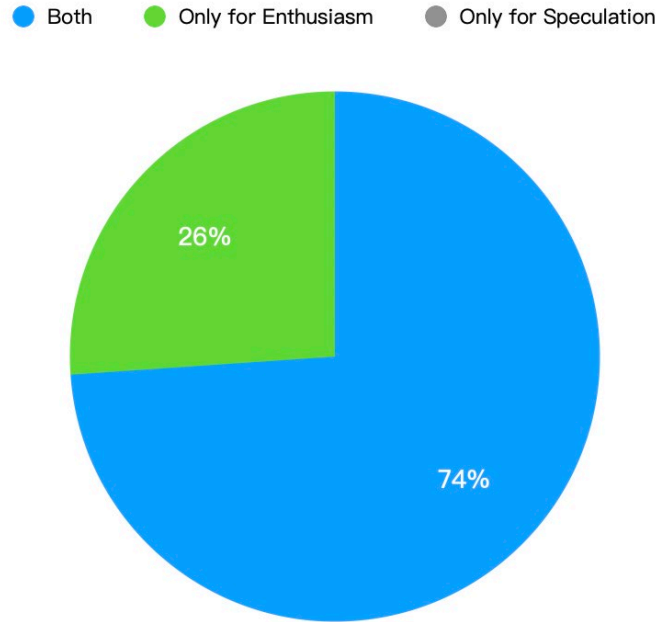


Figure 8. Proportion of enthusiast buyers and speculators

The demand side of sneaker resales market is composed by two parties: one is the enthusiasts; the other is the speculators. For the enthusiasts, they can hardly buy the shoes from the official channels. However, the prices are volatile, and the fake products are widely spread. As a result, their demand is to identify the products and buy at a relatively fair price. On the other side, the speculators are very sensitive to the prices so that they have to shifts around with several intermediaries and channels to make sure they get the sneakers with the fairest price to make a profit.

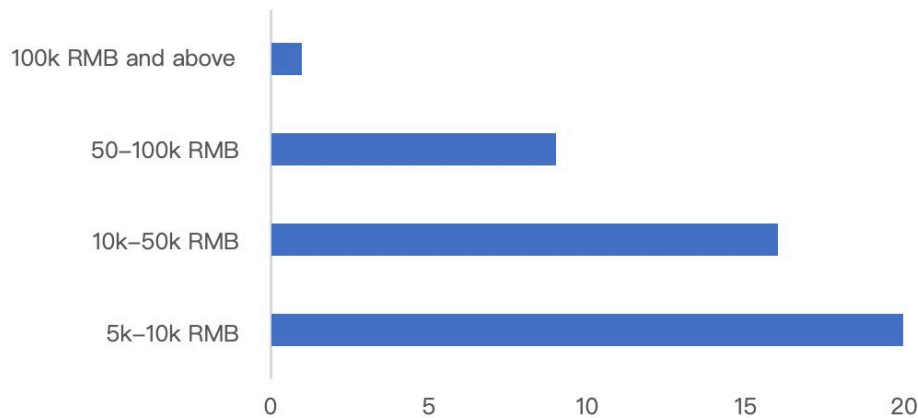


Figure 9. Price of Most Expensive Sneaker Bought

According to the survey, most of the buyers have their most expensive sneakers bought in the range from 5k to 10k RMB, and only a very small part has their most expensive shoes that cost 100k RMB and above. Though sneaker traders are generous on their sneaker collection and would like to spend more on the sneakers, the premium is on a reasonable range. Their willingness to pay is hardly higher than 50x multiples.

Conclusion and Implication

From the demand-side analysis, the primary research and secondary research both suggest that enthusiasts take most of the consumption in the shoes trading markets. The author believes that pure shoes traders only for-profit seeking is only a small party of the group. Most people are passionate about sneakers collecting. People choose to trade on the platforms because they are trustworthy, transparent and convenient.

Shoes trading platforms are a lot like the stock trading platform. The traders can choose when and how much to trade. The platforms are making profit through facilitating deals and providing services including sneaker authenticity identification. As a result, they are the most preferable platform for the traders. Among all the apps, Dewu app is the most widely used apps among all others.

The root of the premiums on the secondary market is limited supply. Brands, the source of the value chain, can issue limited edition to limit the supply and gain more attention through the Hunger Promotion. By limiting the supply, the price of limited edition is usually high, however, they are sold way much higher and added more premium in the secondary market.

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