Stewart Investors
Sustainable Funds Group

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Sharing Economy
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Sharing resources has gone on for as long as humans have been living in tribes. But without the enabling role of the internet or mobile devices it is hard work in a large complex society with a myriad of goods and services. The internet is now helping to solve this problem. It co-ordinates and connects individuals to enable transactions. GPS-equipped mobile devices and the internet allow precise, real-time measurement of spare capacity as well as the ability to locate where it's needed. These platforms act as networks to intermediate supply and demand, drastically lowering the barriers to entry for individual suppliers and the transaction costs for rental transactions among strangers. They also provide a trust framework for both suppliers and consumers to build a digital brand reputation via the opportunity for participants to give free feedback on transactions. Ultimately, the internet widens the circle of potential sharing partners from immediate friends to everyone connected to the network and it is trust that keeps the sharing economy going.

Some tangible examples
Botsman and Rogers divide the sharing economy into three examples: product service systems, redistributed markets and collaborative lifestyles.

Redistributed markets is the practice of and platforms for the exchange of pre-owned goods. The most obvious example of this is eBay. This is not really sharing or renting of goods but old fashioned exchange and ownership.

Product service systems, which is the core of the concept, refers to using data to sell goods as if they are services, a pay as you go (PAYG) system with access trumping ownership. To provide a more meaningful distinction this category can be split into two.

The one we are probably most familiar with is physical product service systems, often referred to as collaborative consumption. Cloud computing is an example of this; we do not need to own much computing power as businesses or as consumers because it is cheaper and easier to rent virtual computers from Google or Microsoft's datacentres. Mobility is another segment that has been subject to the conversion of goods into services through the use of car sharing services such as Zipcar and co-operative car ownership clubs. In these examples, participants can subscribe and get access to cars parked within a given proximity that they can rent and use more cheaply and easily than they would owning a car.

Virtual product service systems are slightly different given the nature of the goods. Unlike physical products as services, they are 'non-rivalrous'; use by one person does not diminish the ability of others to use them. The subject here is data in the form of media. From the advent of Napster and P2P file sharing, this has evolved into a subscription based model dominated by the likes of Spotify and Netflix. The ability to stream through fast broadband and 4G networks has diminished the need to own media. Access wins and a subscription model can certainly be cheaper given these service providers can offer very affordable access once they reach scale given the marginal cost of adding a user is almost nothing.

The category that Botsman and Rogers call collaborative lifestyles covers a range of platforms which they describe as those which "connect people to share less tangible assets like time, space, skills and money". This perhaps stretches the boundaries of a reasonable definition given money is not really a spare resource people have and can share. The most prominent platform in this category is Airbnb, which facilitates the renting out of anything from a couch to a house for short periods. The idea is to make money from underutilised space, including when travelling. This sounds like a physical product service system, but it is the location and space that is being let out, rather than floorboards, walls or a ceiling.

The other main form of collaborative lifestyles is individuals renting out their time and skills. Websites like Taskrabit and Fiverr allow people to commission from online micro-entrepreneurs, either via a direct contract or through a crowdsourcing approach, anything from creating an animation to picking up laundry. The internet allows these micro-businesses to go direct to consumers and the platform allows for public moderation of quality and reputation.

A good thing for all involved?

The benefits of such models are fairly obvious. For providers, the draw is the ability to receive income from assets, physical or not, that would otherwise be idle. For consumers, the attractions are two-fold. It's the triumph of access over ownership: "I don't need a drill, I need a hole in my wall". The same functional outcomes can be achieved without the hassle of ownership, which is especially pertinent in the case of goods like cars. And in almost every case, the user will get use of an asset cheaper than was previously possible through owning an item themselves and/or going through a traditional provider. Why would I buy a car when Citycarclub lets me rent by the hour, takes care of the road tax, insurance, petrol and maintenance, and costs me so much less than owning a car that would stand unused most of the time? There are also significant social benefits. Privately owned cars remain parked 96% of the time. Increasing the utilisation of fixed assets implies a far more efficient use of society's resources.

However, others consider the sharing economy to be a huge threat. "Renting and sharing could lead to lower home sales…as well as lower auto and retail sales… The ripple effects could also be catastrophic". Indeed, given consumption is the largest component of GDP, you would think the concept of a sharing economy is a significant headwind.

But a headwind to what? Hanging clothes on the line creates zero GDP, whereas using a washing machine, in the way we account for economic activity, does contribute despite the two situations combining the same starting position and outcome.

Threatened corporates

Firstly, distribution franchises which are threatened by disintermediation by the internet. An insight, from CLSA, is that "much of the value of traditional goods and services is the friction involved with connecting the asset with demand, at the time and place of need". A taxi franchise is not one built on outstanding quality or brand, but on proximity of supply to effective demand. The sharing economy disintermediates the distribution franchises making a small margin through dealing in the aforementioned friction. That profit either disperses to customers and suppliers, or is captured by the platforms likes Uber.

Secondly, those companies providing undifferentiated products or services that are vulnerable to new competitors. These entrants are usually the micro-entrepreneurs for whom the barriers of entry have been radically lowered by technology. An example of this is hotels, as Airbnb effectively now means they have a hundred thousand new potential competitors in the form of every single residential space in the city.

Thirdly, asset vendors themselves, both manufacturers and retailers. Ultimately, these are business models built on a linear model of consumption. Sharing should lead to reduced demand for purchases, especially for big ticket items and those that in other ways match the descriptions above of vulnerable goods and services. This impacts not only the manufacturers of cars and washing machines, but also the retailers of them. People effectively retail to each other via apps and websites. Even ancillary functions like advertising and marketing, maintenance and servicing (fewer cars means less mechanics), financing (it also means less car loans and less insurance) as well as the entire supply chain going back to extractive resource companies stand to lose from any shift away from consumption. They tend to share more and therefore buy and own less.

Hidden opportunities and adaptations

Ways in which companies can try to combat these threats are firstly participating in the sharing economy. Companies have plenty of underused assets, whether they are office space, capital equipment or staff. A potential new line of revenue is from renting out portions of warehouses which never get above 70% utilisation to small and medium-sized enterprises (SMEs) and allowing staff to sell their services to third parties in instances that they are underutilised. Kingfisher, the owner of B&Q, are quite advanced in thinking about the sharing economy given the potential headwinds they face from it, and have been looking at models of leasing power tools to consumers rather than selling them. However, an appreciation for the role 'friction' plays is required to successfully overcome these headwinds as they don't just have to be compelling on price; the offering has to be efficient in terms of time and facilitated by very easy to use online tools.

Another key means to adapt is to appreciate that sharing changes the economics of spending in a more complex way than just reducing it. Goods that were previously for personal use become assets to rent, and thus investments. A driver is more likely to pay up for a better car if he part-times as an Uber driver and knows he'll be able to more than recoup the extra investment through charging higher fares. Or you might opt for a flat with an extra bedroom than you need on the basis that renting it out can cover the additional rent to your landlord. As a result, quality, durability and resale value become more of a premium.

This extends to services too. If increasingly items are going to be sold online and peer-to-peer, there is more of a need to create an 'experience'. For retailers, for instance, there are clear examples like Apple and Hollister where the visit to the shop is more than a functional exercise. These are likely to have more resilience and more retailers are likely to try and replicate these sorts of differentiating elements as an alternative selling point. Reconfiguring products to suit their new mode of use is another way companies could adapt and the automotive industry is a good example of this. Manufacturers are now designing entry mechanism features to allow consumers to rent vehicles without having to exchange physical keys in a bid to support car sharing schemes.

Of course, not every industry can adapt like this. Some will face very significant headwinds, wherever the economics means P2P has cost advantages over B2C.

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