

Asia Distribution and Retail
Teresa Lam, Christy Li, Renne Chan

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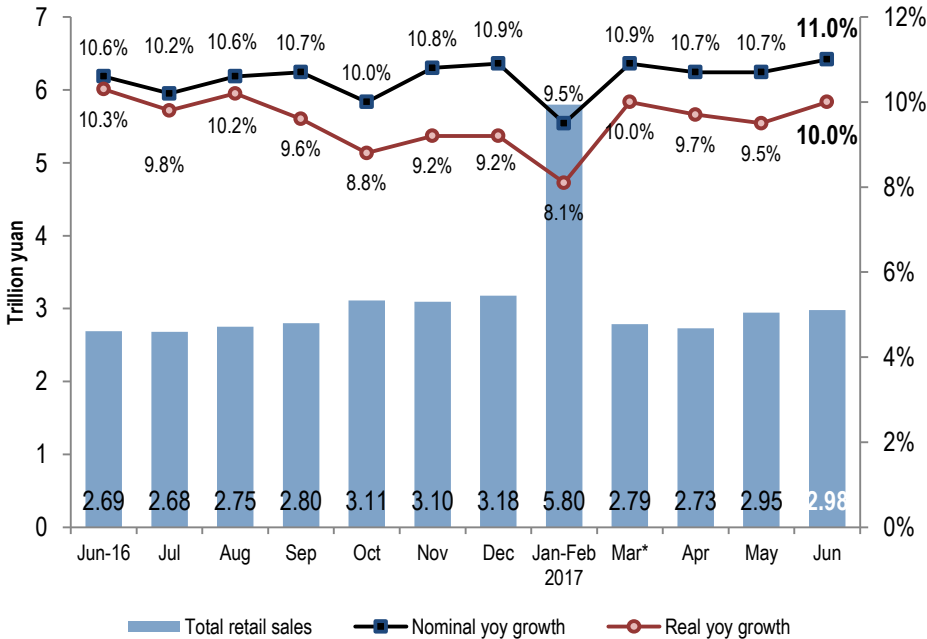
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I. Market overview

1. Retail sales up by 10.4% yoy in 1H17

Total retail sales of consumer goods increased nominally by 10.4% year-on year (yoy) to reach 17.24 trillion yuan in 1H17. By month, the nominal growth in April and May were both 10.7% yoy. Total retail sales of consumer goods reached 2.98 trillion yuan in June 2017, up nominally by 11.0% yoy.

Exhibit 1: Total retail sales of consumer goods, June 2016 – June 2017

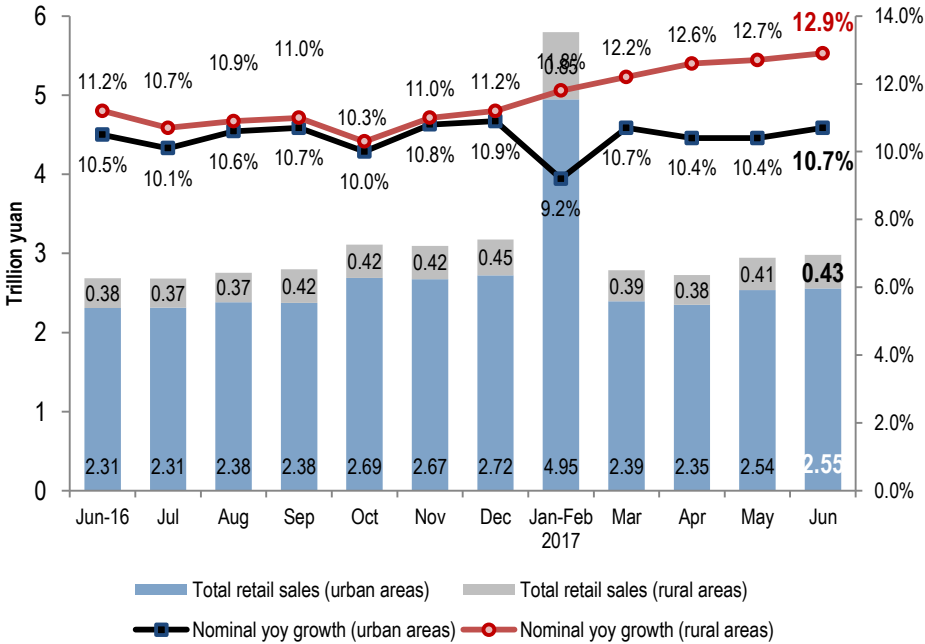


Source: National Bureau of Statistics of the PRC; compiled by Fung Business Intelligence

2. Rural retail sales continue to grow faster than urban retail sales in 1H17

Rural retail sales have been growing at a faster pace than urban retail sales. Rural retail sales increased nominally by 12.3% yoy to 2.46 trillion yuan in 1H17, while urban retail sales rose 10.1% yoy to 14.78 trillion yuan. By month, rural retail sales amounted to 0.43 trillion yuan in June 2017, up by 12.9%, while urban retail sales amounted to 2.55 trillion yuan, up by 10.7% yoy.

Exhibit 2: Total retail sales of consumer goods, urban vs. rural areas, June 2016 – June 2017



Source: National Bureau of Statistics of the PRC ; compiled by Fung Business Intelligence

The increase in rural household income contributed to the fast growth of rural retail sales. Per capita disposable income of urban and rural households reached 18,322 yuan and 6,562 yuan in 1H17, up by 8.1% and 8.5% yoy in nominal terms respectively. Rural household income grew faster than that of urban households, but the per capita disposable income of urban households was almost triple than that of their rural counterparts.

Exhibit 3: Per capita disposable income of urban and rural households, 1H16 – 1H17

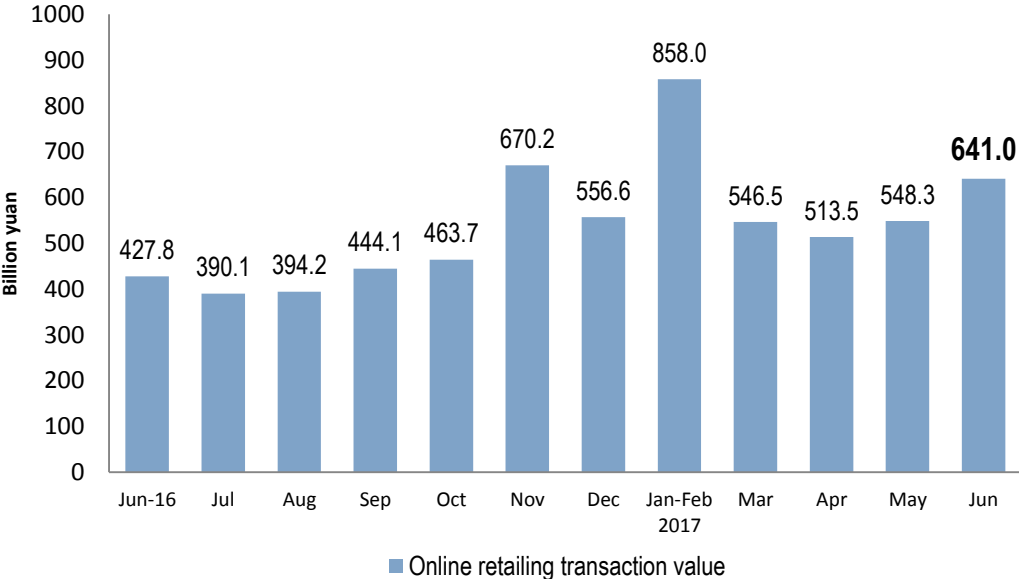
	Urban households		Rural households	
	Absolute value (yuan)	yoy growth	Absolute value (yuan)	yoy growth
Quarterly data				
1Q16	9,255	8.0%	3,578	9.1%
1Q17	9,986	7.9%	3,880	8.4%
Half-yearly data				
1H16	16,957	8.0%	6,050	8.9%
1H17	18,322	8.1%	6,562	8.5%
1-3Q data				
1-3Q16	25,337	7.8%	8,998	8.4%
Yearly data				
FY16	33,616	7.8%	12,363	8.2%

Source: National Bureau of Statistics of the PRC; compiled by Fung Business Intelligence

3. Online retail market scales up in 1H17 amid slower growth

Total transaction value of online retail sales of goods and services increased by 33.4% yoy to reach 3.11 trillion yuan in 1H17. Of which, online sales of goods amounted to 2.37 trillion yuan, up by 28.6% yoy and accounted for 13.8% of the total retail sales of consumers goods. By month, total online retail sales of goods and services in April and May were 513.5 billion yuan and 548.3 billion yuan, respectively. Total online retail sales in June amounted to 641.0 billion yuan.

Exhibit 4: Transaction value of online retail sales of goods and services, June 2016 – June 2017

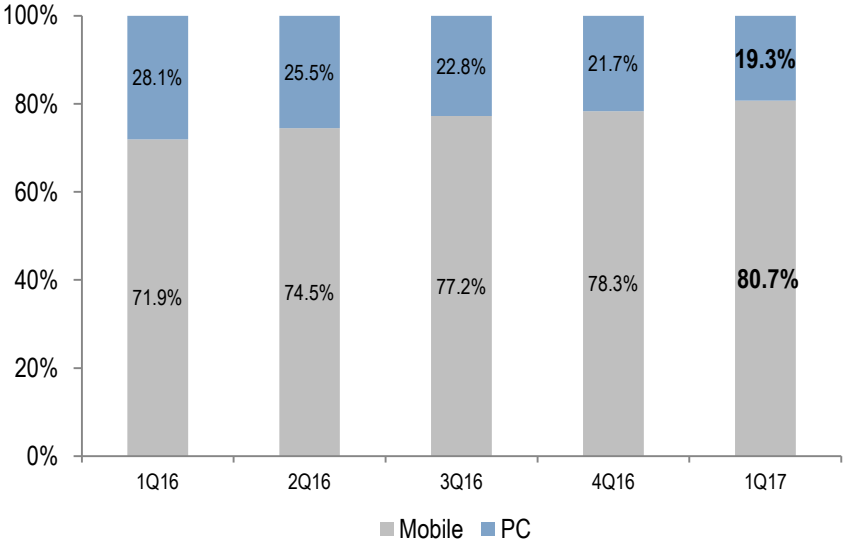


Source: National Bureau of Statistics of the PRC; compiled by Fung Business Intelligence

4. Mobile-based online shopping continues its growth momentum in 1Q17

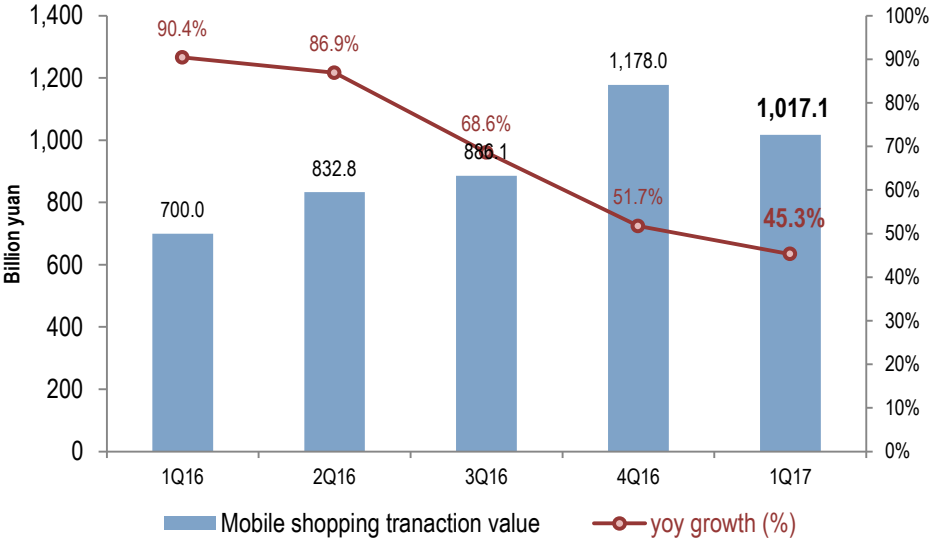
80.7% of the online shopping transactions were made on mobile devices in 1Q17 and total transaction value of mobile shopping reached 1,017.1 billion yuan, up 45.3% yoy.

Exhibit 6: Market structure of online retailing: mobile vs. PC, 1Q16 – 1Q17



Source: iResearch Consulting Group; compiled by Fung Business Intelligence

Exhibit 7: Transaction value of mobile shopping, 1Q16 – 1Q17

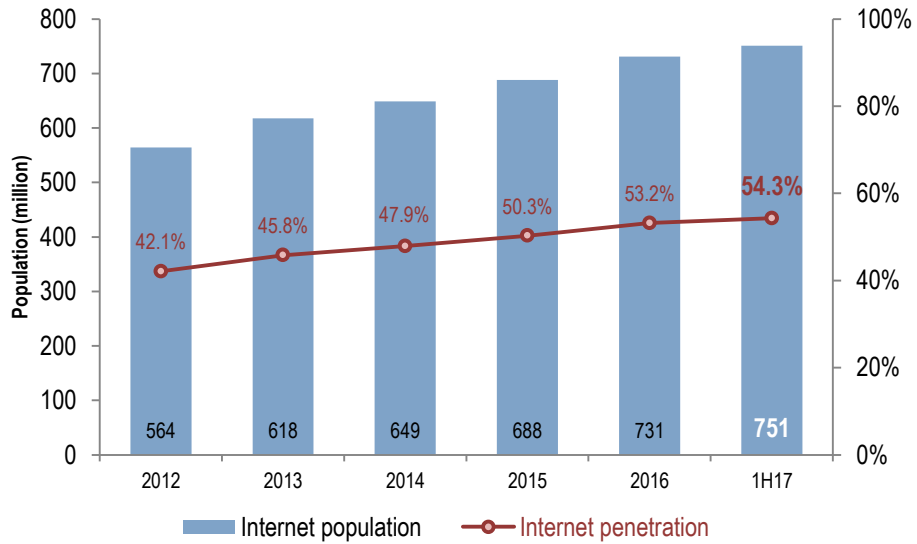


Source: iResearch Consulting Group; compiled by Fung Business Intelligence

5. China has 751 million Internet users and 514 million online shoppers in 1H17

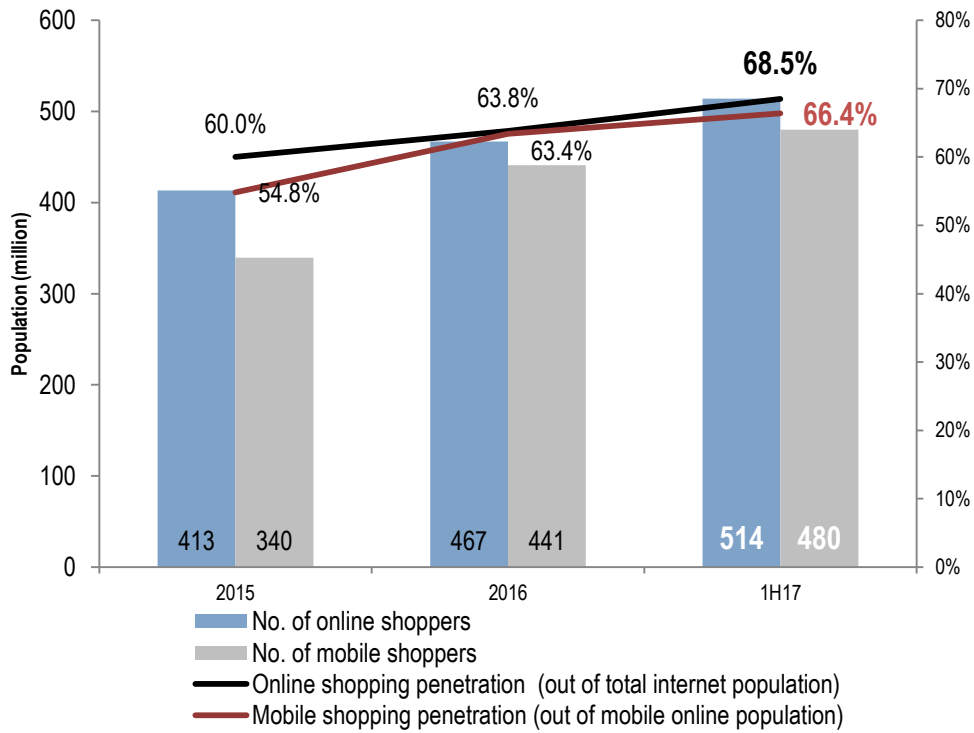
As of 1H17, there were 751 million Internet users in China, and the Internet penetration rate was 54.3%. Of which, 514 million were online shoppers. A total of 480 million people used mobile devices to access the Internet.

Exhibit 8: Internet population and penetration, 1H17



Source: China National Commercial Information Center; compiled by Fung Business Intelligence

Exhibit 9: Online shoppers population and penetration, 1H17

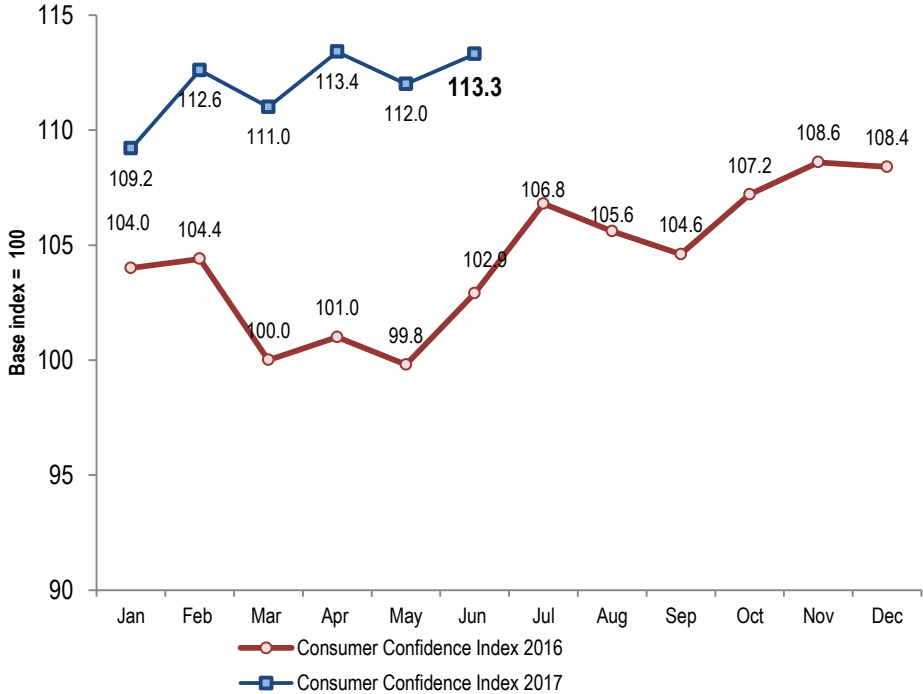


Source: China National Commercial Information Center; compiled by Fung Business Intelligence

6. Chinese consumers more upbeat, consumer confidence surges in 1H17

Consumer confidence index gradually picked up since the end of 2016, and continued to rise in 1H17, suggesting that the consumption atmosphere in China remained positive. Consumer confidence index in April, May and June exceeded 112.

Exhibit 10: Consumer Confidence Index, January 2016 – June 2017



Source: National Bureau of Statistics of the PRC; compiled by Fung Business Intelligence

7. Performance of large-scale retailers picks up in 1H17

Retail sales growth of 100 key retailers increased by 3.1% yoy in 1H17, up from 2.7% yoy in 1Q17. By month, retail sales growth increased by 5.7% yoy and 5.3% yoy in April and May, then decreased by 0.2% yoy in June.

Exhibit 11: Yoy growth of retail sales of 100 key retailers in China, June 2016 – June 2017



Source: China National Commercial Information Center; compiled by Fung Business Intelligence

II. Latest developments

General retail

1. Chinese companies make into the global retail scene

In July, Fortune Magazine announced the 2017 Fortune 500 list. 44 retail companies from around the world made it into the list, 21 of which are based in the U.S., five in France and three in China. The three Chinese companies are JD.com, Alibaba and Suning.com. Together, they had a total revenue of US\$85.039 billion and net profit of US\$6.023 billion, which accounted for 2.8% and 4.6% of the 44 retailers' revenue and profit respectively¹.

2. Total number of Chinese outbound tourists increases steadily with higher spending

According to the statistics released by the China National Tourism Administration, the number of Chinese outbound tourists reached 62.03 million in 1H17, up 5% yoy from 59.03 million in the same period last year. Thailand was the most popular destination for Chinese tourists, followed by Japan and Singapore. Meanwhile, a total of 69.5 million inbound tourists visited China in 1H17, exceeding the number of outbound tourists by 7.47 million².

Data from the World Tourism Organization indicated that Chinese outbound spending still ranks the highest in the world. However, a new survey by consultancy Oliver Wyman showed that Chinese tourist spending on shopping dropped 17% last year. One reason for the change is the easier access to foreign goods in mainland China due to the booming cross-border e-commerce (CBEC) market³.

Internet & E-commerce

3. Investment in AI heats up; Internet companies accelerate AI innovation

Chinese Internet giants are increasingly investing in artificial intelligence (AI). In August, Alibaba launched a smart speaker "Tmall Genie X1", which is similar to Amazon Echo and Google Home. Powered by AliGenie, the voice assistant service developed by Alibaba's homegrown team, Tmall Genie X1 allows users to control with verbal commands. This technology ensures more accurate and secure commands, allowing users not only to purchase from Alibaba's shopping sites but also to make payments through the device. It also supports connection with other smart home appliances on Alibaba's smart home platform such as Tmall Box, air conditioners, and air purifiers⁴. Earlier in March, Alibaba launched "Dian Xiaomi", an AI-aided customer service robot for e-tailers, which can help online stores at Tmall platform to control labor cost. With its vast computer resources and access to online data from hundreds of millions of consumers, Alibaba aims to deliver personalized shopping experiences and marketing solutions through AI technology.

Also in July, Baidu held its inaugural AI developer conference, “Baidu Create” and announced the official launch of its autonomous driving platforms, Apollo and DuerOS open platform. Before that, Robin Li, the company founder made an internal announcement in May, saying that the company is changing the company vision for the first time after 17 years, that is, to transform Baidu from being the country’s leading search engine to the leader in the emerging field of AI. To further its push into AI, the company is constantly acquiring AI startups. Most recently in July, Baidu acquired Seattle-based chatbot startup Kitt.ai. With this acquisition, Baidu hopes to integrate Kitt.ai’s voice ability and natural language processing ability into Baidu platform and fully open the backend to Baidu’s cooperating partners⁵. A month earlier, it acquired xPerception, a U.S. technology company that provides visual perception software and hardware solutions for robotics, virtual reality, and devices for people who are visually impaired. Earlier in February, Baidu also acquired Beijing-based Raven Tech, a Chinese smart home control and smart hardware start-up utilizing AI and big data. Baidu’s aggressive acquisition spree is viewed as a decisive step for the Internet giant to catch up with its peers – Alibaba and Tencent, which have both achieved great success during the mobile Internet boom, while Baidu has apparently lagged behind.

Other leading tech giants are also actively building various AI applications. In April, JD.com introduced AI shopping assistant to offer customer support via voice recognition for logistics enquiries, product recommendation, and after-sale services. In the future, AI shopping assistant will cover other lifestyle services such as air ticket and hotel booking, top-up service and payment service⁶. In May, Tencent opened an AI research lab in Seattle⁷; and in July, it started an AI accelerator program to provide relevant technology and business knowledge to 25 selected startups over a six-month period⁸.

4. Third-party payment companies continue to accelerate overseas expansion

Third-party payment companies continue to accelerate overseas expansion. In July, Alipay and WeChat Pay have both formed partnership with U.S. third-party payment platform Stripe, allowing online merchants to accept Alipay and WeChat Pay payment via Stripe. Tencent, on the other hand, signed partnership agreement with German payment technology company Wirecard, who will support the launch of WeChat Pay in Europe by providing solutions to merchants regarding the use of WeChat Pay starting from November in 2017⁹.

At the same time, some third-party payment companies are ramping up their overseas marketing promotion efforts. Alipay is a case in point. To encourage consumers to use Alipay overseas, Alipay and Japanese convenience store chain Lawson jointly launched a cross-border marketing promotion campaign in all Lawson stores in Japan and China. Starting from 11 July, consumers checking out with Alipay in any Lawson store in Japan or China will get cash reward in their Alipay account or electronic coupons in accordance to the campaign arrangements. Earlier this year, Lawson has introduced Alipay as one of the payment solutions in all its branches in Japan¹⁰.

5. PBOC set up nationwide online clearing house to monitor third-party online payments

Recently, the China National Clearing Centre, the People’s Bank of China (PBOC)’s settlements and clearing arm, announced the **Notice of Connecting Third-party Online Payment Systems to the New Platform for Processing**. According to the Notice, banks and all third-party online payment systems including Alibaba’s AliPay and Tencent’s Tenpay must connect to the new platform by 15 October, 2017, and be ready to route transactions through it from

30 June, 2018. The new platform is the online version of UnionPay's clearing service for transactions involving third-party online payment firms and banks. It offers standardized service for all third-party online payment firms¹¹. The new platform allows the Chinese central bank to directly monitor third-party online payments and transactions.

6. E-commerce players seek to better serve overseas consumers

Recently, Chinese e-commerce players are actively launching overseas platforms as part of their globalization strategy. For example, Alibaba announced the official launch of Tmall World. The new platform aims to connect the over 100 million overseas Chinese shoppers worldwide with more than 1.2 billion products offered on its flagship e-commerce portals, including Taobao and Tmall via PC or mobile app. The new program will initially focus on countries which have sizable Chinese populations, including Hong Kong, Taiwan, Singapore and Malaysia. Tmall World will offer these countries or regions logistics, payment and localization support catering to the needs of each of the local market. Indeed, during the "618 shopping festival" (1-18 June) this year, Alibaba tried to tap the Hong Kong market by launching new services on Tmall Supermarket for Hong Kong consumers. Tmall Supermarket partnered with Cainiao Alliance to set up around 40 self-pickup points in Hong Kong, while also providing home delivery service¹².

Meanwhile, JD.com also launched JD Global to compete with Tmall World in June. In the initial phase, JD Global offers a few hundred thousand SKUs directly sourced by JD.com and a few million SKUs from third-party sellers on the platform. Customers from over 200 countries and regions around the world can have access to these products via JD Global. Overseas customers buying from JD Global enjoy the same price and discount as local buyers. JD.com accepts payment through debit cards issued by Chinese banks, international credit cards, as well as WeChat Pay. JD.com has also developed a global logistics system to support international shipment consolidation and splitting¹³.

7. Foreign companies remain upbeat in China's CBEC market

In recent months, there are quite a number of foreign brands and retailers entered the China market via the CBEC channel. For instance, German discount supermarket chain Lidl launched its China web store on Tmall Global in May. The web store offers several Lidl's private labels, such as Combino, Bellarom and Sondey. The retailer said the current focus of the store is on grain and dry food and it will expand its product range in the future. Orders will be shipped directly from Germany and imported to China through a subsidiary in Hong Kong¹⁴.

Earlier in May, Sam's Club launched its flagship store on JD Worldwide. It sells around 200 SKUs, primarily personal care products, maternity and baby products and nutritional supplements that are not available in China. Sam's Club said it will expand the product offerings to around 700 SKUs before the end of the year¹⁵.

South Korean Shinsegae Department Store also opened its overseas flagship store on Tmall Global in June. The store currently sells over 400 SKUs, including apparel, cosmetics, bag, home electronics, home products, mother-and-infant product, female shoes, as well as snacks. The store uses Cainiao Network as its logistics service provider so as to shorten the time needed for custom clearance when importing to China¹⁶.

In July, U.S. FMCG brand Reckitt Benckiser opened an official flagship store on JD Worldwide. The first batch of products made available in the store include Schiff, a leading supplements and healthcare product brand in the U.S., as well as a host of its sub-brands, including Move Free, Airborne, Megared, etc¹⁷.

Apart from brands and retailers, State of Michigan, an American state known for its traditional manufacturing and agricultural industries, also set up a “State Pavilion” on Tmall Global in June. It is the first State Pavilion on Tmall Global to be set up by an administrative state in a foreign country. Representative of the State of Michigan said that the state government will explore opportunities to collaborate with Alibaba in terms of logistics. It will also look at how to work with Alibaba’s travel service Fliggy.com to develop its tourism industry. Jack Ma of Alibaba said that he looks forward to allowing SMEs and farm owners in the U.S. to sell to China and Asia through the Internet as well as Alibaba’s platform¹⁸. Currently, Tmall Global houses 17 country/region pavilions, including the U.S., the U.K., France, Denmark, Japan, Holland, Canada, Russia, Spain, Italy, South Korea, Australia, Germany, Thailand, New Zealand, Hong Kong and Taiwan.

E-commerce logistics

8. E-commerce logistics sector sees waves of collaborations

Strategic partnerships and collaborations in the e-commerce logistics arena remain on trend. The partnership between JD.com and Japanese logistics company Yamato in areas such as cold chain logistics is a notable case. JD.com announced in July that it has entered into a strategic partnership with Yamato Transport Co., Ltd., one of the largest logistics companies in Japan. The agreement involves collaboration in areas such as fresh produce cold chain logistics, cross-border logistics, global trade management, logistics technology R&D¹⁹.

In the same month, JD Daojia and Wal-mart China announced the extension of their partnership to more cities in China in an effort to further expand their O2O services. JD Daojia’s statistics showed that more than 50 Wal-mart China stores in 12 cities across China have newly joined the partnership with JD Daojia since March 2017. Currently, the partnership between Wal-mart China and JD Daojia covers 134 stores in 18 major cities across the country²⁰. In the meantime, JD Daojia also announced an upgrade of its service pledge of “7-day Unconditional Returns of Goods (including fresh produce category)” to “14-day Unconditional Returns”.

Supermarkets and hypermarkets

9. Fresh produce O2O retailers keen to pursue offline expansion

Recently, several major fresh produce O2O retailers are expanding rapidly offline. Leading player Hemaxiansheng is a case in point. Hemaxiansheng opened three new directly-operated stores in Beijing and Shanghai in June 2017. According to Hou Yi, Hemaxiansheng’s founder and CEO, the company will speed up its expansion nationwide as Hemaxiansheng’s first ever branch in Jinqiao of Shanghai turns profitable. It plans to open over 2,000 directly-operated or joint venture stores in China’s tier 1 cities, such as province-level municipalities and provincial capitals. Currently Hemaxiansheng has 13 stores in China, of which ten are in Shanghai, two in Beijing and one in Ningbo²¹.

Yonghui Superstore is also actively venturing into the fresh produce O2O market with the launch of two new brands – YH Life and Super Species. In June, YH Life opened its first 24-hour store in the Wanke Mall in the Taijiang district of Fuzhou. The interior design and merchandising of the 24-hour YH Life store is similar to that of the Shanghai and Beijing branches. YH Life's last-mile delivery is also handled by Yonghui Logistics. The store will not provide any cooked food in the initial phase of store opening; however, fresh produce such as fruits and vegetables, as well as frozen meat are available for sale. YH Life said that the 24-hour operation model is still in trial operation and the Fuzhou store will be used to test the feasibility of product delivery and night-time operation. The model will be quickly replicated to other stores upon a successful trial. Currently, YH Life has 57 stores in cities including Shanghai, Beijing, Fuzhou and Chongqing²². Super Species, which focuses on premium fresh produce O2O as well as catering services, is expanding fast too. The first store was opened in Xiamen in June and the second store in Shenzhen in July. As of end-July, it has six stores in China. Super Species aims to have 24-50 new stores by end of 2017²³.

In July, RT-Mart and Feiniu.com jointly opened a new O2O "New Retail" hypermarket "Feiniu Fresh" in Shanghai at RT-Mart's Yangpu branch. The new O2O store mainly sells fresh produce; it has pick and pack stations in the storage area of the store, allowing workers to pack the goods for delivery right after the order is placed. Feiniu Fresh offers 1-hour delivery service for customers who live within a 3-km distance from the store. Unlike Hemaxiansheng, Feiniu Fresh accepts various payment methods such as cash payment, WeChat Pay, Alipay, UnionPay, and Baidu Wallet. A special channel for this O2O store is going to be available on Feiniu.com and its mobile app. Customers can place orders physically in the store or on the Internet. RT-Mart said that tier 1 cities such as Beijing, Shanghai and Guangzhou will be its targeted markets for expansion in the initial phase²⁴.

Department stores and shopping malls

10. Cross-sector collaboration deepens

Recently, increasing numbers of department store operators are forming strategic partnerships with players in other sectors for expansion of business scope. In June, the Shanghai Media Group (SMG) and Bailian Group formed a strategic partnership to leverage the competitive advantage of both companies for joint development. The collaboration under this partnership includes the design and construction of a comprehensive experiential retail space that features performing arts and culture, as well as an indoor theme park targeting young consumers. The space will focus on content marketing and original content creation. Also, the two groups will work together in various areas such as television shopping channel, marketing and advertising, and new technology development, so as to promote joint development of the cultural and retail industry under the "New Retail" regime²⁵.

Also in June, Wangfujing Group formed a strategic partnership with Beijing Shouqi (Group) Co., Ltd., the car rental subsidiary of Beijing Tourism Group. According to the partnership agreement, both companies will collaborate to offer one-stop solution for the car rental and shopping needs of consumers – including areas such as resources sharing, channel development, core business development, membership development, as well as joint marketing. All car parks of Wangfujing Group's retail properties will be stationed with rental cars of Beijing Shouqi Group.

Parking facilities and signage for the sharing cars will also be built in the 55 department stores, shopping malls, outlets and supermarkets of Wangfujing Group across China²⁶.

11. Emergence of “New Retail” formats and business operations in the department store sector

To provide customers with unique products and better shopping experiences, department store operators are seeking new breakthroughs in their operations. For instance, Rainbow Department Store opened its first unmanned convenience store “Well GO” at the first floor of Rainbow’s headquarters building in Shenzhen Bay on 8 August. With an operating area of 12 sqm, the store offers around 300 SKU, covering snacks, beverages and daily necessities, etc. The store is currently open to Rainbow’s members only. With RFID technology, smart security systems, cloud-based customer services, and online payment tools, Well GO can offer instant, convenient and smart shopping experience to consumers. It connects with Rainbow’s app “Rainbow Scarf” and allows customers to use the app to shop²⁷.

Earlier on 4 August, Rainbow debuted a new retail format named “Global In Select” at its Houhai Branch in Shenzhen. Phase 1 of Global In Select houses six sections and sells various products, including beauty and cosmetic, maternity and baby, products from Australia and New Zealand, food products, specialty products from Europe and the U.S., and wine. By leveraging RFID technology, Global In Select supports self-checkout in-store. The system can recognize the product categories, volume, total price, discounts, etc. all by itself without human touch. Customers can use Rainbow’s app to scan the QR code displayed on the screen to complete the payment²⁸.

Another example is Bailian Group. In June, Bailian Group opened a new hypermarket brand “RISO” in Shanghai. RISO is a new form of hypermarket combining food delicacies and shopping. Located in the Hualian Commercial Building in Pudong New District, RISO occupies two floors and has a total floor space of 4,500 sqm, which is almost half of the total floor space of the Hualian Commercial Building. The first floor mainly sells bakery, fruits, seafood, fresh food and drinks. There is also an area for customers to enjoy cooked food. On the second floor, there is a kitchen for food processing, as well as product areas selling red wine, wine set, and other general merchandise²⁹.

Convenience stores

12. Unmanned/cashier-less convenience stores come on the scene

Unmanned/cashier-less convenience store is recently trending, mirroring the hybrid of vending machines and convenience stores. Increasing numbers of players are testing the new model, including Internet giant Alibaba and several large-scale retailers such as Sun Art, Easyhome, Rainbow Department Store, etc. In July, Alibaba showcased its new “take and go” coffee shop Tao Café in the Taobao Maker Festival. The 200 sqm-store offers beverages, fast food and snacks and can accommodate around 50 customers at a time. To enter the store, first-time customers are required to use Taobao’s app to scan the QR code, as well as to consent to the terms on collection and use of personal data, Alipay services agreement, etc. Once consumers have entered the shop, they can shop without using their mobile phone. The system will automatically calculate the amount due and deduct it from the user’s Alipay account with a notification when the shopper leaves the shop³⁰.

Another example is Bingo Box, a fully-automated and unmanned 24-hour convenience store under Sun Art's Auchan Hypermarket. Auchan opened two such stores in Shanghai in June. Shoppers can complete the whole shopping process from purchase to payment on their own. Having a floor space of around 15 sqm, Bingo Box sells more than 500 SKU of products, including food and other general merchandise. For more details, please refer to our publication ["New Retail" in action: Bingo Box – The revolutionary unmanned convenience store](#).

Japanese convenience store chain Lawson announced that it would trial run self-checkout service in its China branches. Customers will be able to complete the checkout process with the Mars Rabbit mobile app, a Chinese app developed to facilitate the payment process in physical retail stores. In July, Lawson trialed the application in two of its Shanghai branches in Hong Kong Plaza and Mixc shopping mall³¹.

Earlier in June, Moby Mart, an autonomous self-contained store built on wheels, designed by Swedish startup Wheelys together with Heifei University of Technology, was beta-tested on the streets of Shanghai. Operated 24 hours a day, Moby Mart offered snacks, beverages, lunch, etc. It could accommodate 3-4 customers at one time. Currently, Moby Mart can only be moved around by humans but the creators said future versions will use computer vision to navigate the streets and come to customers^{32, 33}.

Apparel market

13. Apparel and footwear brands tie up with peers to drive synergies

Forming partnership with peers allows apparel and footwear companies to expand product offerings, enhance competitiveness as well as extend market reach. For instance, Huimei Group, the parent company of Taobao brand Inman, formed a strategic partnership with BALLOP, a South Korean specialty sports brand known for its ultra-light sports shoes in June. BALLOP will enter the China market by leveraging the online distribution capability of Huimei, while Huimei will expand into the sports fashion category to cater to the diversified needs of its online store customers. The partnership also allows Huimei to leverage on the product innovation and manufacturing capabilities of BALLOP³⁴.

In June, Chinese footwear company C.banner International Holdings Ltd. announced that it will form a joint venture with Hong Kong-based Madden International Ltd. to operate the sales and distribution business of American footwear and fashion brand Steve Madden in China. According to C.banner, the joint venture will open 150 retail stores in China by the end of 2020. Also, the JV will sell Steve Madden's products through online platforms³⁵.

14. Apparel retailers seek IPO for further expansion

Going public is one of the major ways for apparel retailers to secure more funding for further expansion. Shenzhen Annil Kidswear Co. Ltd was successfully listed on the Shenzhen Stock Exchange on 1 June. Annil raised a total of 379 million yuan and the capital raised will be used in opening new stores, R&D investment, as well as construction of information technology infrastructure. Founded in the mid-90s, Annil is now the third-largest kidswear brand in China in terms of market share³⁶.

Some other apparel companies are seeking a listing on the stock exchange. For instance, Shanghai La Chapelle Fashion published its listing prospectus and sought listing on the Shanghai Stock Exchange in May. The company planned to raise around 1.64 billion yuan through the issuance of no more than 54.77 million shares. According to the prospectus, La Chapelle Fashion plans to spend 1.556 billion yuan on expanding its retail network, and 84 million yuan on IT infrastructure to support its “New Retail” operation. In the coming three years, La Chapelle Fashion will open 3,000 new retail stores, which will increase its total store number to over 10,000³⁷.

Maternity wear and products brand O.C.T. Mami is also seeking a listing on the Shanghai Stock Exchange, subject to the approval by the authority. According to its IPO prospectus, the company plans to raise 219 million yuan through the issuance of no more than 15 million shares. The company said that it will use the money raised in four major areas, namely building up sales network, constructing design and testing centre, investing on IT system infrastructure, as well as supporting daily operation. O.C.T. Mami is an omni-channel retailer of maternity products. Its major product categories include maternity wear, maternity cosmetics as well as babies’ product and services. Notably, O.C.T. Mami published its first IPO prospectus in June 2016³⁸.

Luxury market

15. E-commerce giants foray into the luxury segment

E-commerce giants, led by Tmall and JD.com, have been aggressively courting international luxury brands to their sites. Two recent cases are Swiss luxury watch and jewellery brand Chopard and Italian affordable luxury brand Furla. On 17 August, Chopard launched an online flagship store on JD.com. This is the first attempt of Chopard to enter China’s e-commerce market. The online store sells Chopard’s signature products, including the exclusive Happy Hearts Bangle and watches from the Happy Ocean collection. Earlier on 14 August, Furla opened a flagship store on Tmall. The online flagship store currently sells Furla’s latest collections of bags and accessories. The company will reportedly launch two Tmall-exclusive items on 21 September.

On 2 August, Tmall launched the “Luxury Pavilion”, which is an invite-only online platform for premium and luxury brands. The platform is exclusive to a selected number of ultra-rich consumers. The new platform currently features a wide range of luxury products, including apparel, watches, beauty and cosmetics, and luxury auto. Luxury brands such as Burberry, Hugo Boss, Maserati, Guerlain and Zenith have joined the platform³⁹. Following the launch of the Luxury Pavilion, on 9 August, Tmall announced the launch of “Tmall Space”, an online pop-up luxury retail platform. Loewe under LVMH is among the first batch of brands launching in Tmall Space. Loewe will release a limited-edition Barcelona bag tailored for the Chinese Valentine Day exclusively on Tmall Space. This is the first time Loewe sells online while the offline stores will only display the product. Tmall Space will continue to cooperate with other luxury brands⁴⁰. It is believed that these initiatives are part of Alibaba’s strategy to push forward its New Retail initiative in the luxury segment to reach out to the country’s super wealthy online shoppers, while pledging to fight counterfeiting.

JD.com, on the other hand, also announced it was speeding up its push into the luxury sector with a partnership with Farfetch, a London-based luxury marketplace. In June, JD.com bought a stake in Farfetch for US\$397 million and became one of its largest shareholders. JD.com will help Farfetch to build a digitized sales and marketing

system in China with JD.com's technology and big data. For Farfetch, the partnership allows it to have direct access to the China market. Farfetch consumers can also use JD.com's recently launched premium delivery service, JD Luxury Express, as well as payment service JD Pay and microcredit service JD Baitiao. Moreover, Farfetch's partnering brands with physical stores in China will provide various omni-channel retailing services such as click & collect and buy online and return in-store⁴¹.

16. More international fashion brands set up self-operated online websites and WeChat stores to tap the market

Apart from selling on e-commerce platforms, increasing numbers of international luxury brands are jumping into China's e-commerce market by setting up self-operated transactional websites and WeChat stores. U.S. digital marketing consultancy firm L2 mentioned in its report "Digital IQ Index: Luxury China 2017" that setting up stores on Tmall and JD.com's platforms means that brands need to concede the full control of its online consumer search data.

A recent example of luxury brands setting up their own transactional website is Italian luxury fashion brand Gucci. The luxury fashion house has opened a self-managed online store in China (<https://www.gucci.cn/zh>). Consumers can order from the online store the full range of products from its current season's collection, including bags, shoes, apparel and jewellery. According to media report, Gucci.cn will be the only official online store for the brand in China⁴².

U.K. luxury brand Burberry, which is profitable in China, also said that through its marketing efforts on social media platforms, its online sales in China have doubled since 2016. Also, the China consumer reach of its WeChat marketing campaign has increased by two-folds in the past year⁴³.

III. Competitive landscape

Financial and operating performance of selected listed retailers, Internet and e-commerce companies:

1. Department stores and grocery players

Company	Parkson	Sun Art	Wangfujing	Bailian Group	Dashang
Financial period	1Q17*	1H17**	1Q17*	1Q17*	1Q17*
Total gross sales proceeds (million yuan)	4,406.9	54,080 (+2.1% yoy)	5,251.2	13,371.7 (-5.4% yoy)	7,724.1 (-9.6% yoy)
Net profit attributable to shareholders of the company (million yuan)	1.1	1,757 (+22.7% yoy)	190.1 (+1.5% yoy)	360.5 (-11.2% yoy)	329.2 (+11.8% yoy)
Total operating revenues (million yuan)	1,254.9 (+0.9% yoy)	2,925 (+33.0% yoy)	4,994.8 (+10.5% yoy)	NA	468.6 (+18.1% yoy)
SSS growth	-2.2%	-0.9%	NA	NA	NA
Merchandise gross margin	15.5% (-0.5ppt yoy)	23.3% (+0.5 ppt yoy)	17.91%	NA	NA
Current operating stores (Approx.)	58	446 hypermarkets	47 department stores and outlets Approx. 120 convenience stores	6,000	300

* For the quarter ended 31 March, 2017

** For the six months ended 30 June, 2017

Source: Company data; compiled by Fung Business Intelligence

2. Internet and e-commerce companies

Company	Alibaba	Tencent	JD.com
Financial period	1Q18*	2Q17**	2Q17**
Revenue (million yuan)	50,184 (+56% yoy)	56,606 (+59% yoy)	93,200 (+43.6% yoy)
GMV (million yuan)	NA	NA	234,800 (+46% yoy)
Annual active consumers	466 million (Jun 2017)	NA	258.3 million (Jun 2017)
MAU	Mobile MAU: 529 million (Mar 2017)	Combined MAU of Weixin and Wechat (Jun 2017): 963 million MAU of QQ (Jun 2017): 850 million	NA
Notes			<ul style="list-style-type: none"> • 7 fulfillment centers, 335 warehouses • JD.com reported a net loss of 287 million yuan, compared to a net profit of 127.6 million yuan for the same period last year, because of higher traffic acquisition costs, fulfilment expenses and marketing expenditure

* For the quarter ended 30 June, 2017

** For the quarter ended 30 June, 2017

Source: Company data, compiled by Fung Business Intelligence

IV. Regulation updates

Market supervision

1. Government beefs up efforts to guide and promote the development of the sharing economy

On 4 July 2017, eight departments including the National Development and Reform Commission issued the **Guiding Opinions on Promoting the Development of the Sharing Economy** <关于促进分享经济发展的指导性意见>, the first official regulatory document for sharing economy. The Opinions point out that the advent of the sharing economy can effectively improve the efficiency of resource utilization in the society, improve convenience for the general public, as well as promote supply-side reform. In particular, the Opinions set out efforts to overhaul administrative licensing items and registration items for commercial affairs which restrict the development of the sharing economy, remove or ease limitations on the market access for resource providers, and institute new policies on market access in a prudent manner.

Moreover, the Opinions call for strengthening the protection, creation and application of and services for intellectual property rights in relation to the development of the sharing economy, such as patents, copyrights and trademarks, and reinforcing legislation interpretations and amendments; making timely adjustments in accordance with relevant processes to those laws, regulations and policies that are not suitable for the development of the sharing economy and optimizing legal services constantly⁴⁴.

2. The State Council heightens protection of intellectual property rights and consumer rights

On 31 May 2017, the General Office of the State Council issued the **Major Tasks in the Nationwide Crack Down on Intellectual Property Infringement, Production and Sale of Counterfeits and Shoddy Goods (2017)** ("Major Tasks") <2017年全国打击侵犯知识产权和制售假冒伪劣商品工作要点的通知>, which states that related government departments such as the Customs, the Ministry of Public Security, State Administration for Industry and Commerce, General Administration of Quality Supervision, Inspection and Quarantine, and the State Intellectual Property Office will engage in special tasks to protect intellectual property rights and consumer rights and create a clean business environment.

Goods sold in the following markets, including e-commerce, rural and community markets, as well as cross-border exports to foreign countries, especially countries and regions participating in the Belt and Road Initiative, will be subject to more stringent supervision in 2017.

Meanwhile, regular inspection on products concerning people's life and health, property security and environmental protection will be strengthened. Regulation of goods postage and delivery will also be strengthened, while related market regulation will be enhanced. Actions will be taken to combat intellectual property infringement in product categories such as food, medicine, medical equipment, environment protection and high-technology products. Trademark protection will also be enhanced.

The Major Tasks also calls for the strengthening of supervision of online trade, especially in the areas of online intellectual property rights infringement and misleading advertisements. Actions will be taken to crack down on counterfeits and goods with quality issues sold online. The monitoring mechanism of goods sold online will be further refined, as the tracking of product origins conducted by related departments strengthen the accountability along the whole supply chain⁴⁵.

Internet and e-commerce

3. “Cyber Security Law”, “Provisions for the Administration of Internet News Information Services” and “Measures for the Examination of Online Products and Services (Trial Implementation)” effective 1 June 2017

From 1 June 2017, the first batch of laws and regulations governing the Internet, including the **Cyber Security Law** <《中华人民共和国网络安全法》>, the **Provisions for the Administration of Internet News Information Services** <《互联网新闻信息服务管理规定》> and the **Measures for the Examination of Online Products and Services (Trial Implementation)** <《网络产品和服务安全审查办法（试行）》> became effective.

The **Cyber Security Law** is the first comprehensive security regulation in the cyberspace. It specifically requires the protection of personal information privacy to be enhanced.

The **Provisions for the Administration of Internet News Information Services** states that a permit for the provision of news information on the Internet must be obtained for parties who provide to the public news information online through channels such as websites, mobile applications, forums, blogs, microblogs, public accounts, instant messengers and live stream broadcast. Provision of news information without a valid or suitable permit is strictly prohibited.

The **Measures for the Examination of Online Products and Services (Trial Implementation)** aims to control the cyber security risks of online products and services and to ensure national security. The Measures state that the procurement of network products and services that might pose security threats to the nation shall undergo cyber security reviews⁴⁶.

4. Supervision of online market heightens; SAIC and other departments issue Notice of Special Action Plan for the Supervision of Online Market (2017)

On 23 May 2017, the State Administration for Industry and Commerce (SAIC) and nine other authorities jointly issued the **Special Action Plan for the Supervision of Online Market (2017)** (the Plan) <《网络市场监管专项行动方案》>. The authorities will take joint action in carrying out the tasks specified in the Plan in the upcoming six months from May to November 2017. Major tasks outlined in the Plan include: the crackdown of right infringements and counterfeits, with a focus on product categories such as food and medicine, cosmetics, medical devices, fashion and accessories, kids and elderly products, home electronics, consumer electronics, auto parts, home décor and materials, agricultural products, and consumer goods or producer goods that have wide-spread usage in the society or may affect public safety and impact the health of the general public.

The authorities will also work together to strengthen law enforcement and closely monitor manufacturers and online e-commerce platforms. Also, the Plan states that joint efforts will be made to crack down false marketing and advertisements by strict enforcement of related regulations such as the **Anti-Unfair Competition Law** <反不正当竞争法>, the **Advertising Law** <广告法> and the **Interim Measures for the Administration of Internet Advertising** <互联网广告管理暂行办法>.

The Plan also vows to severely prosecute illegalities and violations such as malicious account registration, order brushing, fake credit record, false after-sale comments, divulging and selling users' personal information, as well as the posting and delivering of empty parcel for profit. Strict enforcement will be carried out against multi-layer marketing activity online. Also, the Plan states that authorities will jointly monitor the latest developments in new retail business models such as rural e-commerce, cross-border e-commerce, and WeChat business so as to detect and prosecute any illegalities in the market⁴⁷.

5. CAC issues measures governing cross-border transfer of data and cyber security examination

The Cyber Administration Office of China (CAC) released a draft of the **Measures of the Safety Review of Cross-border Transfer of Personal Information and Important Data** (the Review Measures) <个人资讯和重要资料出境安全评估办法（征求意见稿）> on 11 April, as well as the **Measures for the Examination of Online Products and Services (Trial Implementation)** (the Examination Measures) <网络产品和服务安全审查办法（试行）> on 2 May 2017. Among which the Examination Measures will be effective starting 1 June 2017.

The Examination Measures states that the CAC will establish a commission that will be responsible for conducting the security reviews. This commission will work with third-party institutions to carry out the assessments.

The Examination Measures states that cyber security reviews of network products and services procured by entities will be conducted in a range of key sectors on procurement that “may affect China’s national security.” Selected sectors mentioned in the Examination Measures include finance, telecommunication, energy, transportation, public communication, information services, water, public services and digital civil services.

The draft of the Review Measures highlights that safety assessments need to be conducted on actions concerning the cross-border transfer of personal information and important data.

According to the Review Measures, network operators shall store personal information and important data gathered and produced during operations within the territory of China. Where it is really necessary to provide such information and data to overseas parties, consent from the provider of personal information must be obtained. Also, self-assessment on the security of such transfer shall be conducted at least once a year by network operators in accordance with the requirements stated in the Review Measures⁴⁸.

Technologies

6. The State Council issues guidelines on artificial intelligence

On 8 July 2017, the State Council has recently issued the **Guideline on Developing Artificial Intelligence** <新一代人工智能发展规划>. According to the Guideline, AI will serve as a new major economic growth engine and help improve people's lives by 2020 and that China will achieve world-class level in the development of artificial intelligence (AI) technologies by then; the plan sets the target of China becoming a global innovation center in the field of AI by 2030, and that the total output of the AI industry would surpass 1 trillion yuan by then. Major tasks set out in the Guideline include:

- Further developing AI technologies with reference to the global trends as well as in accordance to the national development needs;
- Comprehensively improving the fundamental abilities in scientific innovation;
- Exploring the various applications of AI technologies; and
- Fully utilizing AI technologies in facilitating socio-economic development and national defense⁴⁹.

V. Outlook

1. China's retail industry to continue its upward development trend in 2017

The Ministry of Commerce (MOFCOM) published the “2016/17 Development Report of the Retail Industry in China” in July 2017. According to the report, China’s macro-economic environment has significantly improved over the past year. The regulatory regime for the retail industry has become more comprehensive, while information technologies such as the Internet, big data analytics and cloud computing have been widely adopted across the society. Changes in consumer preferences have prompted the industry to upgrade and transform under the “New Retail” era. The MOFCOM expects the growth of total retail sales of consumer goods to stay at around 10% yoy, while the growth of total transaction value of online retail sales of goods and services at around 25% yoy. Retail companies are expected to further embrace their omni-channel integration, provide diversified shopping scenarios for consumers through social media or concept stores, and promote digitalization of supply chain to increase operation efficiency⁵⁰.

2. Offline retail market rebounds in 1H17, but headwinds expected in 2H17

According to China National Commercial Information Center (CNCIC), China’s offline retail market rebounded in 1H17 with retail sales of 100 key large-scale retail enterprises increased by 3.1% yoy in 1H17; the growth rate was 6.3 pts higher than that in 2016. However, retail sales growth turned negative in June (-0.2% yoy), down from 4.% yoy, 5.7% yoy and 5.3% yoy in March, April and May respectively (see Exhibit 11). It is expected that the industry may face further pressure in 2H17⁵¹. In spite of this, the online retail sector is set to continue its growth momentum with leading online retailers contributing to the majority of the growth. In the coming months, we expect market players to put more efforts to control costs. The use of smart technologies, in particular AI technologies, is increasingly a popular means to achieve this. Big players are expected to perform better with more resources and more capital investments of technology innovation.

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