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China Retail & E-commerce Quarterly: COVID-19 Special (II)

FUNG BUSINESS INTELLIGENCE

China retail is gradually moving into a recovery period, but headwinds remain

On 8 April, China ended its lockdown in Wuhan – the city where COVID-19 first reported. Since then, the country has steadily released the restrictions imposed to tackle the COVID-19 pandemic and gradually moved into a recovery period. Retail sales growth gradually picked up in April and May after the steep drop in 1Q20, while online retail sales continued to grow at a much faster pace than that of total retail sales as the shift from offline to online remained significant.

However, the recovery path is not without headwinds. In early June, Beijing reintroduced lockdowns and travel restrictions following a new outbreak of domestically transmitted COVID-19 cases in Beijing. It is too early to judge the impact of the resurgence of new cases on China's retail sector. But with the government's determined efforts to curb the spread of the virus inside and outside the city, we believe the sector's recovery will be well on track.

We expect retail sales growth to return to positive in 3Q20. Given the uncertainly of how the new COVID-19 cases will affect retail recovery, we devised two scenarios for retail sales growth. In the baseline scenario, the country's retail sales are expected to return to positive growth as soon as June with the assumption that the fresh COVID-19 outbreak has little impact on overall retail sales. If the new outbreak continues to escalate and more stringent measures are put in place by the government, retail sales may flatten out before returning to positive growth (see page 3).

China's path to recovery, to a certain extent, can provide a roadmap for what might happen in the rest of the world in coming months. In particular, the new outbreak comes as China was returning to normal after largely containing the virus, and it holds a lesson for the rest of the world that a resurgence in COVID-19 cases is highly possible after lockdowns are lifted.

In retail, COVID-19 has caused a shift in consumer behavior and buying preference, brands and retailers have to recalibrate their strategies to keep their businesses afloat. Going ahead, retailers need to continue to look for ways to navigate the uncertainty and disruption caused by COVID-19 in order to emerge strong in the post-pandemic era (see page 12).

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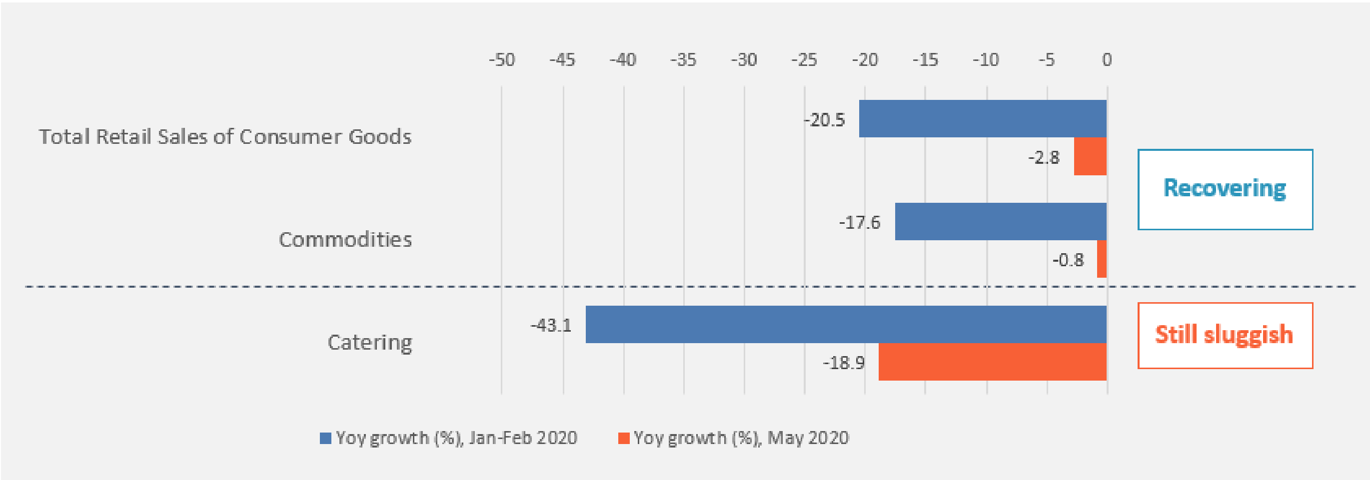
Part I: Market insights

Retail sector begins to recover, yet headwinds remain

Retail sales growth gradually picked up in 2Q20 – April and May figures showed further improvements after the steep drop of 20.5% yoy in total retail sales growth for the January and February period and a drop of 15.8% in March. Total retail sales of consumer goods in April and May were down nominally by 7.5% yoy and 2.8% yoy respectively (Exhibit 1). Most retail businesses and services reopened, and consumer footfall increased significantly but still not yet back to the pre-COVID-19 levels. Sales of commodities in May recovered to a level similar to that of a year ago. Catering sales, however, were still sluggish and down by 18.9% yoy as restaurants take longer time to recover with social distancing regulations still in place.

Exhibit 1: Total retail sales of consumer goods, January-February vs May 2020



Source: National Bureau of Statistics, Fung Business Intelligence

During the extended Labor Day Holiday spanning from 1 to 5 May, which is the first long holiday after the resumption of business, sales of major retail enterprises across the country up 32.1% compared with the 3-day Ching Ming Festival holiday in April[1]. This shows that the consumer market started to regain momentum.

However, in the second week of June, Beijing reported new COVID-19 cases. During 11-18 June, the capital reported over 180 domestically transmitted cases – all linked to the Xinfadi wholesale food market. The capital quickly reintroduced partial lockdowns and strict precautionary measures, such as quarantine requirements and travel restrictions, and rolled out massive testing as the cases have reportedly spread to four nearby provinces, namely Hebei, Zhejiang, Sichuan and Liaoning[2]. It is too early to judge the impact of the resurgence of new COVID-19 cases on China's retail sector. But with the government's determined efforts to curb the spread of the virus inside and outside the city, we believe the sector's recovery will be well on track.

Fung Business Intelligence expects retail sales growth to return to positive in 3Q20. Given the uncertainty of how the new COVID-19 cases will affect retail recovery, we devised two scenarios for retail sales growth (Exhibit 2). In Case 1 (baseline scenario), the country's retail sales are expected to return to positive growth as soon as June with the assumption that the fresh COVID-19 outbreak in Beijing has little impact on overall retail sales. If the new outbreak continues to escalate and more stringent measures are put in place by the government, retail sales may flatten out before returning to positive growth (Case 2).

Exhibit 2: Forecast of nominal growth of total retail sales of consumer goods, December 2019 – December 2020

Case 1 (Baseline scenario)

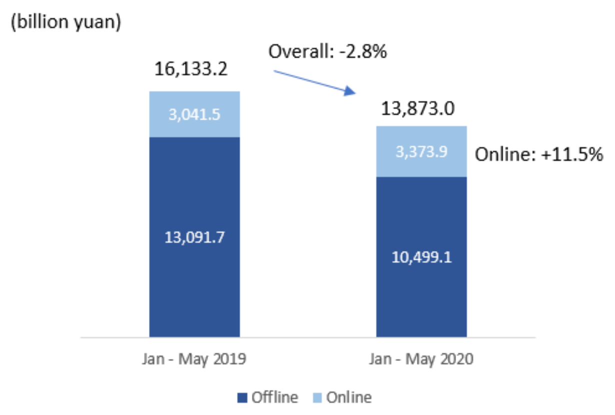
Case 2

Source: Fung Business Intelligence

Online consumption increases notably, especially for food and daily use products

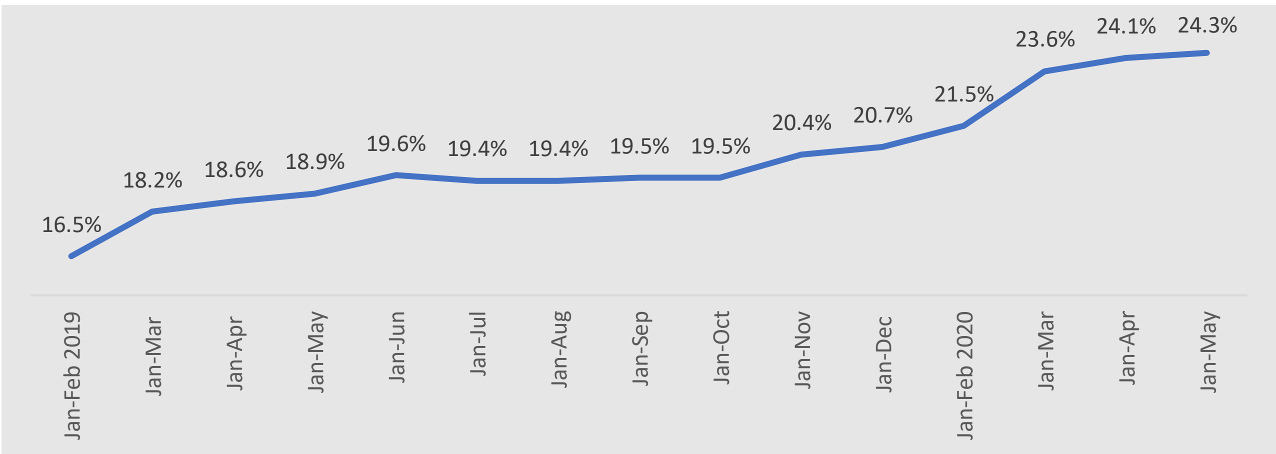
In May 2020, online sales continued to grow fast compared with offline sales. In January-May 2020, online retail sales increased by 4.5% yoy to 4,017.6 billion yuan; the growth is much higher than that of total retail sales growth. Among which, online retail sales of physical goods increased by 11.5% yoy to 3,373.9 billion yuan, accounting for 24.3% of total retail sales, up from 20.7% in FY19 (Exhibit 3, 4). Notably, online retail sales of food and daily use products increased by 37.0% and 14.9% yoy respectively, showing that consumers increased their online spending on these categories amid the social distancing and lockdown requirements.

Exhibit 3: Online and offline retail sales of physical goods, January-May 2019 vs January-May 2020



Source: National Bureau of Statistics, Fung Business Intelligence

Exhibit 4: Share of online retail sales for physical goods to total retail sales of consumer goods, January-February 2019 – January-May 2020

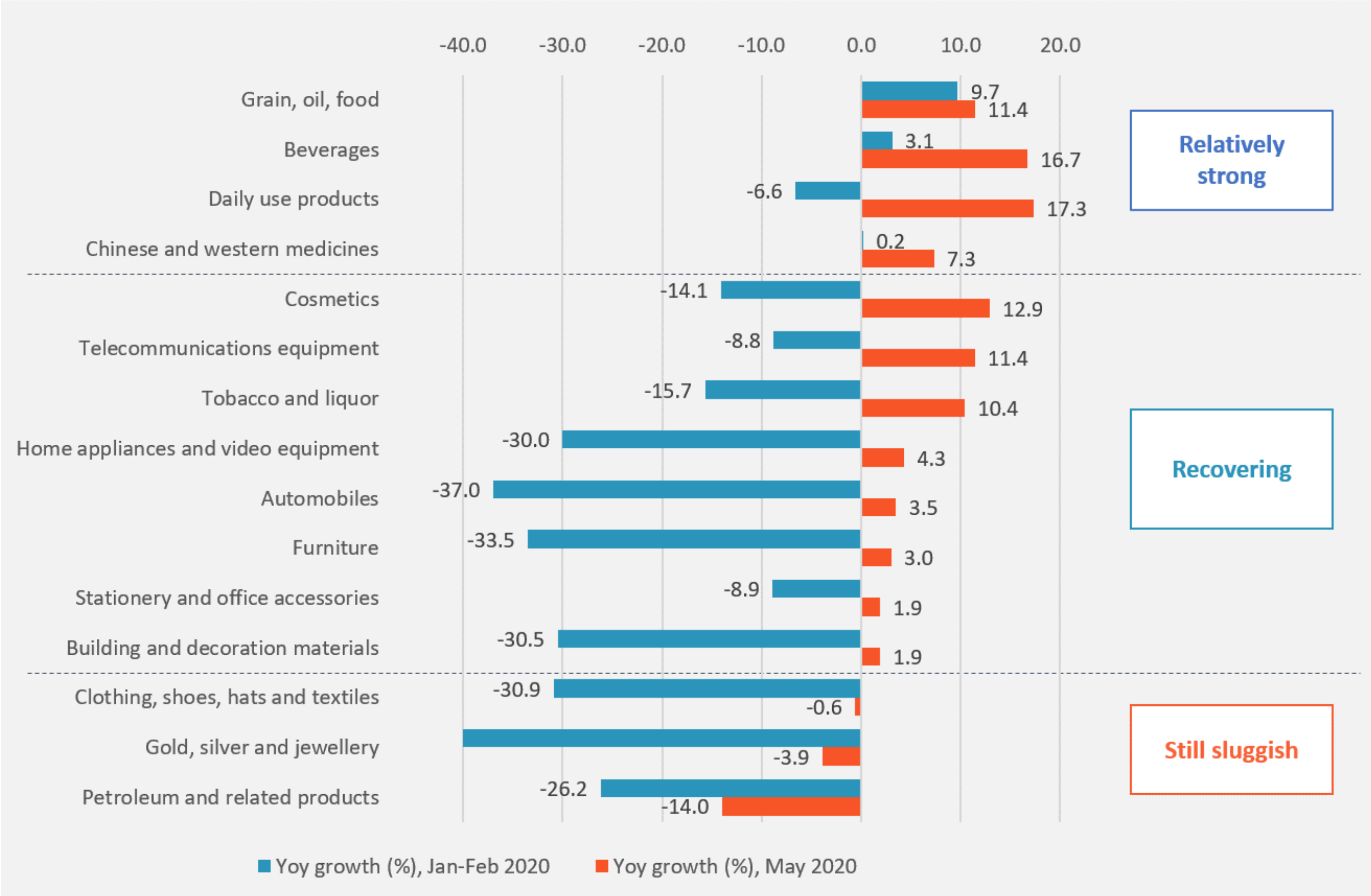


Source: National Bureau of Statistics, Fung Business Intelligence

Various product categories show signs of recovery

In this quarter, there were some signs of recovery across different product categories. While retail sales growth of grain, oil, food, beverages, and daily necessities remained resilient in May, some categories outside of the basics such as cosmetics, telecommunications equipment, and tobacco and liquor also recorded double-digit retail sales growth (Exhibit 5). The reopening of department stores and professional stores further sped up the recovery of sales of cosmetics and consumer electronics. Sales of other discretionary products will soon pick up as normality continues to resume, though the speed of recovery will differ by region.

Exhibit 5: Comparison of retail sales by category, January-February 2020 vs May 2020



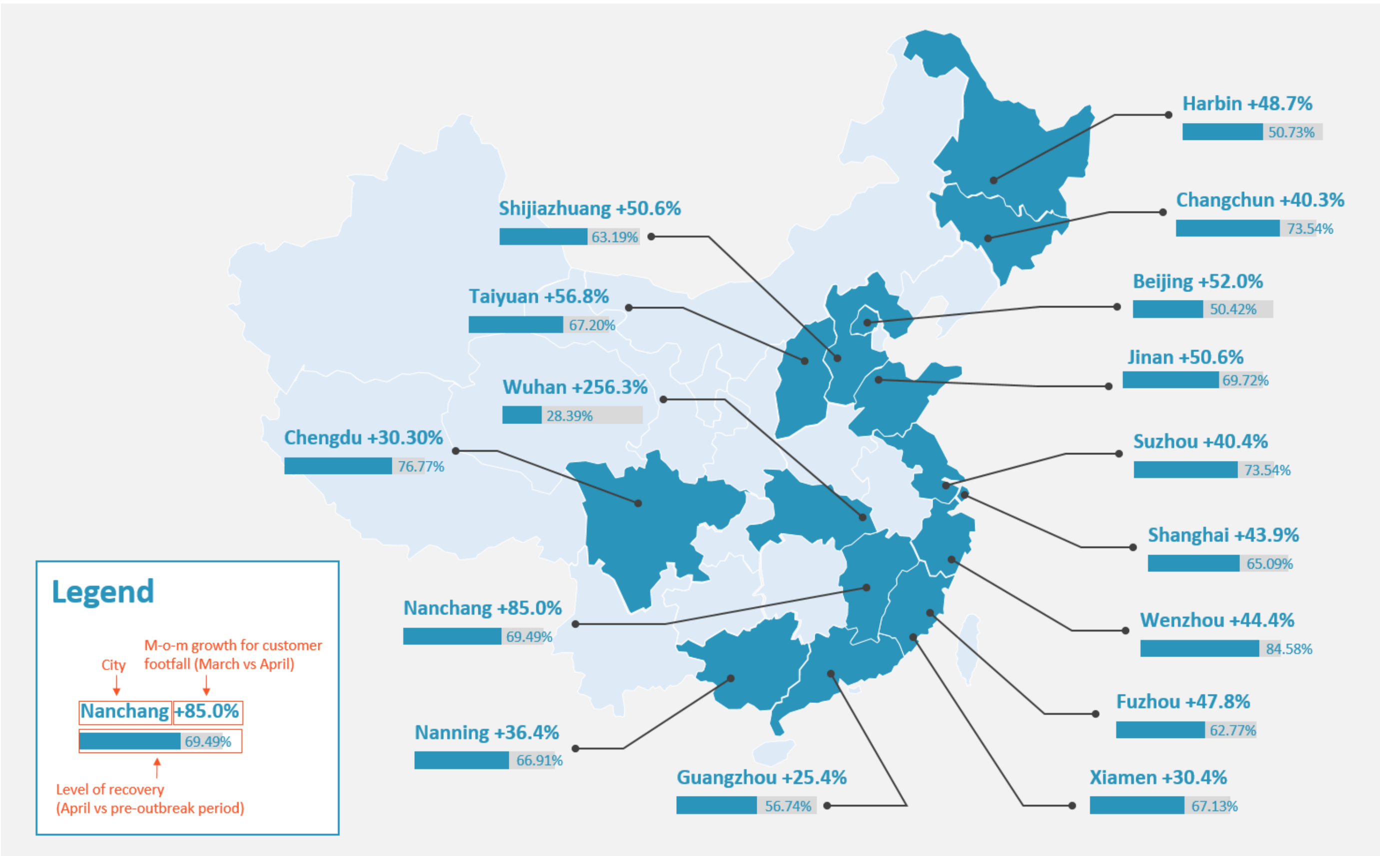
Source: National Bureau of Statistics, Fung Business Intelligence

It is noteworthy that automobile sales picked up significantly from -37.0% yoy in January-February 2020 to 3.5% yoy in May 2020 as the government ramped up efforts to stimulate automobile consumption. For instance, the State Council announced in March that the central government will extend new energy vehicles subsidies for an additional two years and use fiscal money to compensate the replacement of diesel vehicles in key areas such as Beijing, Hebei and Tianjin; the government will also extend the exemption of used car VAT tax from 1 May to the end of 2023[3].

Traditional retail channels reactivate business activities; offline customer flow starts to recover

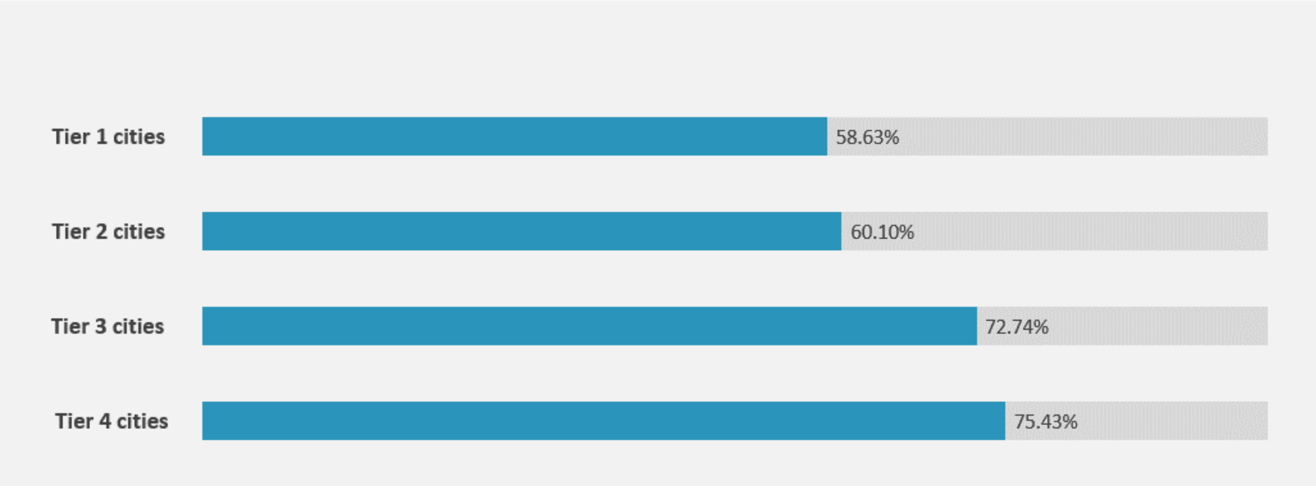
In 2Q20, most but not all previously closed retail stores, department stores and shopping malls across China resumed normal operation and reactivated business activities. A survey conducted by China Commerce Association for General Merchandise (CCAGM) showed that the operation rate of department stores and shopping malls improved from 60% in late February to 80% in mid-April. Customer footfall at shopping malls in tier 1 and 2 cities increased noticeably in April compared to March, with Wuhan showing the biggest increase as the city ended its nearly three-month lockdown on 8 April (Exhibit 6, 7). Nevertheless, customer footfall at shopping malls in Wuhan recovered to just over 28% of the pre-outbreak levels, whereas footfall in other tier 1 and 2 cities recovered to 50-85% of the pre-outbreak levels[4]. We expect customer footfall to further increase in 3Q20 – retail stores in some cities may even see customer traffic returning to the pre-outbreak levels toward the end of 3Q20.

Exhibit 6: Customer footfall at shopping malls in tier 1 and 2 cities, March vs April 2020



Source: Win Data, Fung Business Intelligence

Exhibit 7: Level of recovery of customer footfall by city tier, April 2020 vs pre-outbreak period



**Note: Pre-outbreak period = November – December 2019*
Source: Win Data, Fung Business Intelligence

Domestic tourism shows encouraging signs of recovery in May

China's domestic tourism industry saw promising signs of revival over the extended Labor Day Holiday as the country's domestic travel restrictions have been gradually loosened. The country recorded 115 million travelers during the 5-day holiday from 1-5 May, generating a total of 47.56 billion yuan in domestic tourism revenue, according to the Ministry of Culture and Tourism[5]. Daily average domestic tourism revenue amounted to 9.51 billion yuan during the Labor Day Holiday, which is far higher than the 2.75 billion yuan daily average during the Ching Ming Festival in April. However, it is still a far cry from the daily average of 29.42 billion yuan during last year's Labor Day holiday.

On the other hand, as global travel bans remain strict worldwide, airport retail, duty-free sales and other inbound tourist-oriented trade are still struggling due to the abrupt halt in visitor arrivals resulting from travel restrictions. For the tourism sector and travel retail, all eyes are on Hainan island – a popular holiday destination for the locals – with the further easing of its duty-free policy as outlined in a master plan for the Hainan free trade port jointly issued by the Central Committee of the Communist Party of China (CPC) and the State Council on 1 June. The policy measures proposed to increase the annual offshore duty-free quotas for shoppers vising Hainan island from 30,000 yuan to 100,000 yuan and expand the existing list of duty-free product categories. The free trade port policies are expected to be established by 2025 and will "become more mature" by 2035. We believe the measures will help boost the duty-free business and encourage local people to purchase larger amounts of luxury goods in Hainan.

Government initiatives to boost domestic consumption take effect

Domestic consumption plays an important role in driving economic recovery as China's economy is now more consumption- and service-driven. The government is counting on consumer spending to help pull the country out of economic downturn.

Consumption vouchers have been effective so far to boost short-term spending

Since the outbreak of COVID-19, over 19 billion-yuan worth of consumption vouchers have been handed out by 170-plus local governments across 28 provinces and cities nationwide[6]. Hangzhou has so far given out the highest value of consumption vouchers, followed by Zhejiang and Beijing (Exhibit 8). Distributing consumption vouchers can incentivize people to spend money, thereby boosting retail sales. For instance, the 445 million-yuan worth of consumption vouchers distributed by the local government in Hangzhou during 27 March to 5 May reportedly generated sales of 5.135 billion yuan[7].

Exhibit 8: Selected incentives given by local governments, as of April 2020

City / province	Total value of consumption voucher (million yuan)
Hangzhou	1,680
Zhejiang	1,000
Beijing	850
Wuhan	500
Zhengzhou	400
Qingdao	340
Nanjing	318
Shaoxing	180
Fuzhou	150
Ningbo	100
Foshan	100
Urumqi	42
Jinan	20
Jiangxi	20
Hebei	15
Hefei	10

Source: Sina, Jefferies, Fung Business Intelligence

Most of these government-issued consumption vouchers have designated purposes and could only be redeemed at participating catering, travel, cultural and recreational enterprises. Some local governments have also cooperated with various leading industry players, especially Internet players, to give out consumption vouchers that could be redeemed at specific online platforms. For example, Luyang District in Hefei cooperated with Alibaba to distribute the consumption vouchers, while Chengyang District in Qingdao cooperated with Tencent, and Qinhuai District in Nanjing cooperated with Meituan[8]. Some industry experts said that consumption vouchers not only could boost consumption expenditure, but also accelerate the digitalization of offline retail as local governments work closely with Internet players[9].

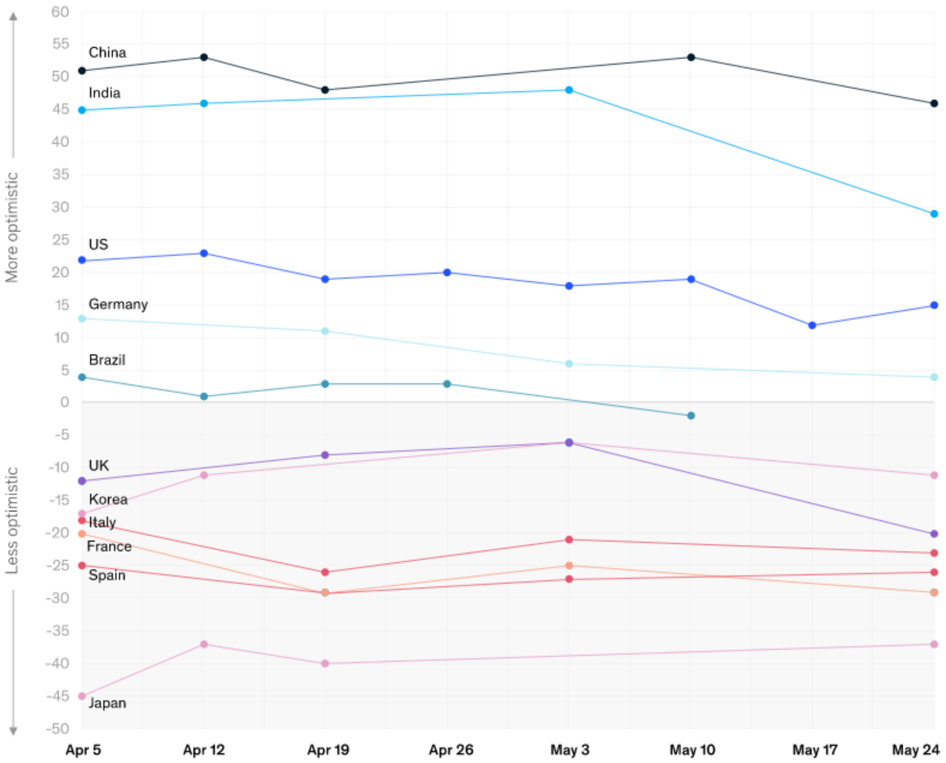
Massive consumption-boosting shopping festivals to drive retail recovery

In 2Q20, some local governments organized massive consumption-boosting campaigns to lure consumers to spend more. For example, the Shanghai municipal government organized the “5.5 Shopping Festival”, which offers hefty discounts and extended store opening hours in an attempt to boost consumption and make up for the losses caused by COVID-19. Instituted on 4 May, the event will run through the entirety of 2Q20, and straddle key holidays such as Labor Day Holidays, Children's Day and the Dragon Boat Festival. Many leading e-commerce platforms, enterprises, brands and retailers from Shanghai participated in the event. According to the MOFCOM Special Commissioner’s Office in Shanghai, the festival generated over 15.68 billion yuan in the first 24 hours[10]. In early June, the Shanghai municipal government launched the first “Night Life Festival”, which will be held from 6 to 30 June[11]. Over 180 featured activities will be organized with an aim to boost consumption upgrade and employment. Similarly, the Beijing municipal government also introduced the “Beijing Shopping Season”, a four-month sales promotion event starting on 6 June. Each district of Beijing will leverage its own resources and strength to launch featured activities in ten areas covering catering, shopping, culture, travel, leisure, etc.

Chinese consumers show higher confidence and spending intent than their global counterparts

Chinese consumers started to regain confidence in this quarter, supported by government measures and incentives to boost consumption (see page 20 for more details). According to a survey by McKinsey[12], Chinese consumers remained the most optimistic about an economic recovery (Exhibit 9). While their global counterparts spent largely on essentials such as food, household supplies, personal care items and home entertainment, Chinese consumers were more willing to spend on other categories such as food takeout and delivery, snacks, skin care, non-food baby products, fitness and wellness, and gasoline.

Exhibit 9: Optimism about country's economic recovery after COVID-19, % of respondents, 5 April – 24 May 2020



Source: McKinsey

Another survey conducted by domestic research agency Lexin Research in April[13] found that young Chinese consumers aged between 20 and 30 are becoming more optimistic about the future – 65% of the respondents said they are willing to increase spending, up 19 ppts from March. Meanwhile, 40.2% of the surveyed consumers said they will buy less but better-quality products, showing that Chinese consumers place more emphasis on product quality in the post-pandemic era.

What's next in 3Q20 and beyond?

Revitalizing domestic consumption a key theme for the Two Sessions; a strong boost to consumer market recovery
In late May, China's top leaders came together for the two-week annual meetings of National People's Congress (NPC) and the Chinese People's Political Consultative Conference (CPPCC) – commonly known as the "Two Sessions". Following over two months of delays due to the COVID-19 pandemic, the Two Sessions were held on 21-22 May. Revitalizing domestic consumption beyond the COVID-19 outbreak is one of the key themes for the Two Sessions. Premier of the State Council Li Keqiang, when delivering the work report of the government, announced that the government will implement multiple strategies to promote the recovery of consumption and expand domestic demand[14]. Key strategies include:

- Supporting the recovery and development of food and beverages, bricks-and-mortar businesses, culture, tourism, domestic services, and other consumer services
- Supporting all types of shopping malls and markets in fully resuming their business and consumer service industries in restoring normal operations
- Promoting online and offline integrated consumption and encouraging the development of new forms of business such as online shopping, green and healthy consumption
- Supporting the expansion of e-commerce and express delivery services in rural areas and addressing inadequacies in cold-chain logistics facilities for agricultural products
- Upgrading pedestrian streets
- Expediting the development of elderly care service systems, promoting in-depth integration between medical care and healthcare, and steadily advancing trials for long-term care insurance schemes

The government also announced to issue 3.75 trillion yuan of special local government bonds in 2020, an increase of 1.6 trillion yuan from 2019, to support new infrastructure, new urbanization initiatives and major projects. It will also strengthen the development of a new type of urbanization and renovate of 39,000 old urban residential communities; such move will encourage the development of community services such as elderly home care, on-demand delivery and cleaning[15]. We believe the government's determination to stimulate domestic consumption will give a further boost to consumer market recovery in 3Q20 and beyond.

The move towards digital to continue as normality resumes

COVID-19 pandemic has altered the way people shop. As consumers fall into the online shopping routine, they become more receptive to e-commerce; such a change in consumer shopping behavior is likely to retain beyond the pandemic. The accelerated adoption of smart technologies is poised to continue post-crisis. Retailers are set to continue to ramp up their digital efforts and maximize their investments in mainstream digital technologies such as digital payments, VR, AR, robotics, facial recognition, among others.

Moreover, at the height of the pandemic, many retailers in China adopted innovative digital marketing approaches such as leveraging livestreaming and private chat groups to keep customers engaged, and maximize sales with the use of social selling. Beyond COVID-19, we believe digital marketing tools and social selling will become mainstream and more widely used in retail.

New consumer behaviors to remain post-pandemic

Besides the online shopping shift, a handful of some other new consumer behaviors, attitudes and purchasing habits that have emerged during the COVID-19 outbreak will likely remain post-pandemic. Retailers need to be aware of these trends and adapt quickly to changes. Examples include:

Greater focus on health and wellness

COVID-19 has significantly raised consumers' awareness of the importance of public health, product safety, and healthy lifestyles. Going forward, they will continue to expect higher standards of hygiene and cleanliness in retail stores, while demanding better quality products. According to McKinsey, 70% of surveyed consumers said that they will work to boost their physical immunity by exercising more and eating healthily in the post-COVID-19 era[16]. Similar survey done by Accenture also showed that personal health is the top priority for consumers going forward[17].

More rational in spending

In the post-COVID-19 era, consumers are more inclined to save than spend. Chinese investment bank China Renaissance conducted a survey of over 1,000 consumers in March. 54% of the surveyed consumers said COVID-19 has changed their spending mindset and they were more willing to save than spend. People aged between 18 and 35 thought about tightening their budget in the next 12 months, but people over the age of 45, as well as students, showed greater confidence in spending[18]. In particular, consumers are likely to spend less on discretionary categories in the near term[19]. According to a report by global communications consultancy group Ruder Finn, 82% of over 800 consumers surveyed in mid-March planned to cut back on spending in jewellery, handbag, and beauty products, but showed more willingness to spend on travel, fine dining, and high-end leather accessories[20].

Business model innovations to accelerate

COVID-19 has affected all our lives and cost businesses worldwide great loss and disruption. That said, the pandemic also serves as a testing ground for business model innovations and new offerings to address the changing needs of consumers. For instance, rising demand for on-demand delivery services during the lockdown has opened up new opportunities for on-demand delivery platforms such as JD Daojia, Yonghui Daojia and Dmall. We expect on-demand delivery service to continue to expand in scale and scope post-pandemic as consumers are getting used to using the service. At the same time, some COVID-19 fueled delivery services and options such as contactless delivery and pickup, autonomous delivery drones and robots, as well as "smart" lockers are expected to become the norm post-pandemic.

Conclusion and implications for retailers

As the first epicenter of the COVID-19 outbreak, China is some weeks ahead of the rest of the world in responding to the pandemic, and as expected, it is also the first major economy to see a recovery. China's path to recovery, to a certain extent, can provide a roadmap for what might happen in the rest of the world in coming months. In particular, the new outbreak in Beijing comes as China was returning to normal after largely containing the virus, and it holds a lesson for the rest of the world that a resurgence in COVID-19 cases is highly possible after lockdowns are lifted.

On top of this, what should retailers – both local and foreign – watch for as they look ahead? Evidently, COVID-19 has caused a shift in consumer behavior and buying preference, and at the same time pushed retailers to recalibrate their strategies to keep their businesses afloat. Going ahead, retailers need to continue to look for ways to navigate the uncertainty and disruption caused by COVID-19 in order to emerge strong in the post-pandemic era. Here are four points to keep in mind:

- **Online shopping will become a prominent buying channel.** There is an imminent need for retailers to ramp up their digital offerings, increase investments in e-commerce, particularly social commerce, and deploy social media-centric omnichannel/ O2O strategies.
- **The pandemic has accelerated the progress of digital transformation in retail.** The ability to leverage digital tools and state-of-the- art technologies to engage with consumers and optimize their operations has become a must for retailers – to survive and thrive in the uncertain times.
- **Innovative business models and services become more evident**. Some innovative business models and retail practices such as contactless delivery and pickup, autonomous delivery drones, livestreamed shopping and mobile payment have become the norm during the COVID-19 outbreak, and are likely to stay post-pandemic. Retailers should maximize the synergies between existing and new businesses, particularly in areas such as resource allocation and operations so that they can complement each other and enhance operational efficiencies.
- **Flexible and responsive supply chains keep business on the cutting edge of strategy**. Retailers have to put in place supply chains that are able to keep pace with evolving consumer demand – they are expected to respond swiftly to changing consumer preferences, be flexible, agile and responsive.

Part II: Sector review

Retail & E-commerce

1. CCFA unveils Top 100 retail chain operators in China

In June, the China Chain Store and Franchise Association (CCFA) released its annual list of the "Top 100 Retail Chain Operators in China" (the Top 100s). Total sales of the Top 100s in 2019 were 2.6 trillion yuan, up 5.2% yoy and accounted for 6.3% of total retail sales of consumer goods. Total number of stores of the Top 100s reached around 144,000, up 5.9% yoy. By retail format, the growth of retail sales of convenience stores was the highest at 16.5% yoy, followed by professional stores (10.4% yoy), supermarkets (4.0% yoy) and department stores (0.7% yoy).

Suning topped the list with retail sales of 378.7 billion yuan in 2019, followed by GOME Retail and Red Star Macalline Group with retail sales of 127.6 billion yuan and 125.6 billion yuan respectively. Exhibit 10 shows the top 10 chain retailers in 2019.

Exhibit 10: Top 10 chain retailers by retail sales, 2019

Rank in 2019	Rank in 2018	Enterprise	Sales, pre-tax (million yuan)	yoy growth (%)	Number of stores	yoy growth (%)
1	1	Suning.com Group Co., Ltd.	378,740	12.5%	8,216	-25.7%
2	2	Gome Retail Holdings Ltd.	127,646	-7.6%	2,602	22.6%
3	26	Red Star Macalline Group	125,633	12.6%	428	19.2%
4	4	Sun Art Retail Group Ltd.	101,868*	0.5%	486	0.4%
5	3	China Resources Vanguard Co., Ltd.#	95,100	-6.1%	3,234	1.3%
6	6	Yonghui Superstores Co., Ltd.	93,150	21.3%	1,440	12.9%
7	5	Walmart (China) Investment Co., Ltd.	82,280	3.8%	442	0.2%
8	7	Beijing Easyhome New Retail Development Co., Ltd.	81,110	14.2%	355	24.6%
9	9	Sinopec Group	70,000*	12.9%	27,600	1.5%
10	8	Chongqing General Trading (Group) Co., Ltd.	60,421	-10.7%	373	-9.7%

** Estimates*
Source: China Chain Store and Franchise Association, Fung Business Intelligence

The Top 100s also showed the following trends in 2019:

- **Significant growth for online retail sales** – Online sales growth of the Top 100s was 28.7% yoy, much higher than the growth of total retail sales of consumer goods of 9.2% yoy.
- **Provision of on-demand delivery services became the norm** – around one-third of the Top 100s already connected all of their branches with on-demand delivery service platforms; while half of the Top 100s connected some of their branches with on-demand delivery service platforms.
- **Enrichment of sales channels through embracing group buying and livestreaming commerce** - Around 60% of the Top 100s launched group-buying business; while 30% of the Top 100s adopted short-video marketing or livestreaming shopping[21].

2. "618" Shopping Festival kicks off; e-commerce players strive to win the sales race

The "618" Shopping Festival is the first large-scale shopping event since the outbreak of COVID-19. It is also one of the major battlefields for e-commerce operators. To win over customers and boost sales, some leading players offered consumption vouchers, big discounts and perks to customers. For instance, Alibaba's Tmall cooperated with local governments and brands to release over 14 billion of cash consumption coupons and allowance to boost the sales during the festival. The GMV made on Tmall in the first ten hours increased by 50% yoy. In less than half a day, the GMV made has already exceeded that of the first day of the festival last year. The number of merchants participating the event doubled compared with last year, offering over 10 million SKUs at discount prices. During 1-18 June, Alibaba achieved record GMV of 698.2 trillion yuan.

Meanwhile, JD.com upgraded its service features to offer a frictionless 618 experience and promote service-led shopping. JD.com has formed alliances with more brands, retailers and manufacturers to drive sales during 618. Transaction volume of JD.com's "618" Shopping Festival transaction volume surged 74% yoy within the first 14 hours from midnight to 2 pm on 1 June[22]. During 1-18 June, JD.com saw a total GMV of 269.2 billion yuan, up 33.6% yoy.

3. Shifting to domestic market: E-commerce giants support direct-from factory initiatives

Amid the depressed macro trade environment, many export-oriented factories and foreign trade firms are facing huge challenges as they lost overseas orders. Selling to the domestic market seems to be one of the possible ways to handle their excess inventory. Many e-commerce players offer help to these factories and foreign trade firms to sell domestically. For example, Jingxi, JD.com's group buying platform which focuses on lower-tier cities, announced its upgraded direct-from-factory campaign in April. By cooperating with factories in various industrial clusters, Jingxi on the one hand can push forward its C2M strategy and help factories sell in the domestic market, and on the other hand, it can help digitalize the operation of factories in different industrial clusters. By the end of 1Q20, Jingxi had reportedly set foot in 100 industrial clusters. Going forward, Jingxi aims to enable 100,000 factories to strengthen their C2M capabilities and better serve the consumption needs of lower-tier markets[23].

Alibaba has also ramped up its efforts to help factories sell in the domestic market. It launched a factory-incubation program, which offers online resources, account-management support and other tools to help manufacturers build their C2M capabilities. Meanwhile, in April, Alibaba also launched Taobao Deals – a dedicated app – to enable factories to sell OEM (factory direct) products directly to consumers at competitive prices. Within two months of the launch, the app has recruited over 500,000 factories to set up online stores and 1.2 million production-capable suppliers in China to join the platform[24].

4. Several leading e-commerce players head to secondary listing in Hong Kong

In this quarter, a number of Chinese Internet giants sought for secondary listing in Hong Kong. JD.com was listed on Hong Kong Stock Exchange (HKEX) on 18 June, raising approximately US$3 billion from the offering. Joining JD.com, NetEase reportedly has submitted its Hong Kong secondary listing application to the HKEX; the company plans to raise US$1 billion to US$2 billion and start trading on the HKEX by the end of June 2020. Following the moves by JD.com and NetEase, we expect more renowned Chinese Internet companies including Baidu and Ctrip will press ahead with plans for a secondary listing in Hong Kong[25].

5. E-commerce companies go on acquisition and investment spree

In this quarter, a number of e-commerce companies continued to go ahead with their acquisition plans amid the COVID-19 outbreak. Selected examples include:

Pinduoduo and JD.com invest in GOME Retail

In 2Q20, Pinduoduo and JD.com both bought convertible bonds in household appliance and electronics retailer GOME Retail Holdings Limited. On 19 April, Pinduoduo subscribed to US$200 million in convertible bonds issued by GOME for a tenure of three years. If these bonds are converted, Pinduoduo will be allotted approximately 1.28 billion GOME shares or about 5.6% of its existing issued share capital. Both parties also inked a strategic partnership such that Pinduoduo will help bring the entire GOME product range onto its e-commerce platform, while GOME will integrate its logistics, delivery and assembly services, namely Anxun Logistics and Gome Housekeeper, with the Pinduoduo platform and serve merchants on Pinduoduo[26].

Following Pinduoduo, JD.com bought US$100 million worth of convertible bonds in GOME on 28 May. The strategic cooperation between JD.com and GOME Retail is a further deepening of the cooperation between the two companies after GOME's official flagship store launched on JD.com in March 2020. If these bonds are converted, JD.com will be allotted approximately 2.80% of its existing issued share capital. The two companies will leverage their online and offline advantages over the years to achieve synergies and supply chain integration, as well as product purchases and sales such as joint procurement and joint marketing, as well as resource sharing in logistics services, financial services and other related services.

JD Retail and Kuaishou Technology form strategic partnership

On 27 May, JD Retail, the retail business unit of JD.com, announced a strategic partnership with Kuaishou Technology, China's leading video sharing and livestreaming platform. The two companies will deepen collaboration to help Kuaishou Xiaodian, the sales platform within the Kuaishou video app, enhance supply chain capabilities, brand marketing and data capabilities. JD Retail will provide selected self-owned products to Kuaishou Xiaodian; consumers will be able to make purchases directly from Kuaishou without being redirected back to JD.com, and enjoy the delivery and after-sales services provided by JD.com. Meanwhile, JD Retail will analyze data on product sales and Kuaishou will provide an analysis of the livestreaming metrics to improve sales performance together. The partnership kicked off during JD.com's "618" Shopping Festival and Kuaishou's "616" Shopping Festival – selected self-owned products from JD.com were made available to Kuaishou's livestreaming KOLs for selling[27].

Tencent further invests in Pinduoduo

Tencent invested an additional US$50 million in Pinduoduo on 3 April. As of now, Tencent holds approximately 29.2% of the total number of Class A ordinary shares in issue and is still the second largest shareholder. Tencent will continue to leverage Pinduoduo platform to develop mid-range and low-end, as well as C2C e-commerce business, to contend with Taobao and Taobao Deals[28].

Retail logistics

6. Cainiao and SF Express beef up capabilities through acquisitions

In this quarter, Cainiao completed the acquisition of on-demand logistics services provider Dianwoda while SF Express announced to buy competitor China Post. Cainiao became the controlling shareholder of Dianwoda in July 2018 to tap into its services network covering 350 cities in China. Dianwoda also provides outsourced services for other logistics providers to complete their last-mile deliveries to customers. Its corporate clients include Ele.me, YTO Express, ZTO Express and major supermarket and shopping mall operators[29].

The acquisition of China Post by SF Express will help the latter boost its market share to 65% in the locker system market and become the dominant player with full coverage across all tiers of cities. China Post, a state-owned enterprise, currently covers 79 cities, including all tier-1 cities, and maintains 94,000 locker units across China[30].

7. JD Logistics and SF Express expand services to find new growth points

In this quarter, JD Logistics and SF Express explored lower-tier markets and the food-delivery market respectively to find new growth opportunities. JD.com and JD Logistics joined hands with 11 courier services providers and e-commerce enterprises to propose the construction of smart logistics and supply chain facilities in lower-tier cities. JD.com aimed to offer last mile delivery services in villages and accelerate the implementation of 24-hour guaranteed delivery services in thousands of counties and towns. JD Logistics believed that through infrastructure improvement and penetration of logistics services, consumption potential of villages can be unleashed and agricultural commerce can be promoted and upgraded[31].

A subsidiary of SF Express launched a WeChat Mini Program called “Fengshi”, or “abundant food” in English, to provide food-delivery service targeting business clients buying in bulk. Fengshi has partnered with dozens of restaurant brands, including Pizza Hut, Dicos, Real Kungfu, Yoshinoya and Domino's Pizza. It is reported that SF Express subsidiaries will develop courier business in catering, supermarkets, medical, fresh produce and services in tier 1 and 2 cities, challenging the dominance of Meituan Dianping in the market[32].

8. Dada Nexus files for U.S. IPO; aims to raise US$303 million

In May, Dada Nexus, an on-demand retail and delivery platform, filed with the U.S. Securities and Exchange Commission for an initial public offering on the Nasdaq. The fund-raising target was revised up to US$303 million in June. Dada Nexus operates two delivery platforms, namely JD-Daojia and Dada Now. The company recorded rapid growth in the past three years, with net operating income reaching 1.22 billion yuan, 1.92 billion yuan and 3.1 billion yuan in 2017, 2018 and 2019 respectively[33]. It may become the first Chinese enterprise to be listed on U.S. stock exchanges since the Senate legislation of the “Holding Foreign Companies Accountable Act” on 20 May[34].

Department stores and shopping malls

9. Shopping malls continue to recover albeit at a slow rate

Lease termination of shopping malls reached alarming level amid the COVID-19 outbreak but showed signs of improvement in this quarter. Research center WinData found that the tenancy termination rate of ordinary shopping malls hit 21.1% amid the COVID-19 outbreak, up 5.4 ppts from 2H19 and exceeded the 20% warning threshold in the industry. It forecasted that new mall opening rate will drop to 40% or below in 2020 as mall owners' plans to launch new malls will be delayed by nine months on average[35].

Another research by WinData found that visitor traffic of shopping malls in tier 1 to 4 cities in April bounced back to 66% of the pre-COVID-19 levels (using the average daily visitors in November and December 2019 as base). The full business recovery of shopping malls has been hindered by the prolonged closure of cinemas and KTVs, which were the traffic boosters in normal times. In terms of commercial districts, shopping malls in regional commercial districts and emerging commercial circles outperformed those in municipal and matured business centers[36].

The sign of recovery was particularly obvious during the Labor Day holiday. For example, from 1 to 5 May, 16 Wanda Plazas recorded 4.54 million visitors and 470 million yuan of sales, resuming to 90% and 101% of the number of visitors and sales level of the same period in 2019 respectively[37]. To accelerate recovery, shopping malls should seize the opportunity to refine tenant mix and introduce new formats according to market needs.

10. Continued refinement of retail formats and adoption of O2O strategies

In 2Q20, the pace of retail formation renovation and the adoption of O2O strategies further picked up in the department store sector. Shirble Department Store announced that it had completed the upgrading and renovation of ten department store spaces for traditional supermarket business into Freshippo stores. Shirble also cooperated with Hema Shanghai to build the "Hemali Shirble" brand, fully digitalized shopping malls whose offline and online operations can be managed centrally[38].

Wanda Group and Wumart Xinjiekou Department Store leveraged livestreaming commerce to boost sales. More than a dozen of Wanda shopping malls organized over 40 livestreaming shows individually during the Labor Day holiday[39]. Wumart Xinjiekou Department Store in Beijing joined hands with 100 brands, including Chow Tai Fook, L'Oréal, BeLLE, Kiss Cat, Uniqlo, Youngor, etc., as well as KOLs to organize online shopping activities. By the end of March, it had organized approximately 100 livestreaming events together with over 180 brands. It had seen its online sales increased by 300% and total online traffic reached 30,000 visits during that period[40].

In May, Rainbow Department Store Co., Ltd announced to change its company name to Rainbow Digital Commercial Co., Ltd to better reflect its businesses and development direction. Rainbow explained that in the past few years, it has aggressively transformed into a commercial enterprise with fully digitalized and experiential retail formats, including shopping centers, department stores, supermarkets and convenience stores. Its multiple retail channels have been integrated into a consumption services platform. Under this new model, its core assets include not only brick-and-mortar stores but also data from its digitalized physical stores. The name change will show its determination to embrace O2O strategies and capabilities[41].

Apparel

11. More apparel retailers set up accounts on Douyin during COVID-19

During the COVID-19 pandemic, more apparel players have set up accounts on Douyin, one of the most popular online video platforms in China, to keep their customers engaged and interested in their products. According to Donyin's "White Papers on Douyin Accounts Opened by Apparel Companies 2020" released in May, since late March 2019, the number of Douyin accounts set up by apparel firms has increased by 5.36 times, with the clickthrough rate up by 1.96 times, the number of videos posted on the platform up by 5.18 times, interactions between users (likes, comments and views) up by 1.84 times, and the number of followers up by 3.13 times. The report also indicated that most of the apparel companies launching on Douyin are from Guangdong, Jiangsu and Zhejiang[42].

12. Some apparel retailers announce new store openings amid COVID-19

With China heading towards recovery from COVID-19, some apparel retailers have regained their confidence and announced flagship/ debut store openings in the country. For example, Canadian sportswear brand Lululemon opened its largest China store in Hangzhou Hubin Yintai in77 shopping mall on 30 April. Jointly operated by Lululemon and Space fitness center, the flagship store comprises two floors, with a Lululemon retail store on the first floor and Space on the second floor. Lululemon has so far launched 34 stores in China, including those in Shanghai Xintiandi, Beijing Sanlitun, Shenzhen The MixC, Chengdu Sino-Ocean Taikoo Li and Guangzhou Taikoo Hui. The brand's e-commerce sales growth in China hit 70% yoy in 2019[43]. In late April, another foreign player Hummel, a century-old Danish sports brand, confirmed that it will debut in China by launching its first local flagship store in Shanghai Aegean Plaza. The debut store reportedly will cover around 600 sqm and be followed by more Hummel stores in core commercial districts in tier 1 and 2 cities across the country, covering Shanghai, Guangzhou, Jiangsu, Zhejiang, Chongqing, Jiangxi, Henan, Shandong, Jilin, Liaoning and others[44]. In May, domestic eco-outerwear clothing brand LangerChen also announced that it will open its first global flagship store in China in 2H20, hoping to promote the concept of environmentally friendly and sustainable lifestyle among more consumers through its retail stores. The brand will also roll out self-operated stores gradually across local fashion cities such as Shanghai, Chengdu, Beijing and more over the next five years[45].

Luxury market

13. Luxury retailers bolster e-commerce push in China by launching on Tmall and JD.com amid COVID-19

To nullify sales decline caused by the enforced store closures amid the COVID-19 outbreak, many luxury brands in China have bolstered their e-commerce push in China by launching on major e-commerce platforms such as Tmall and JD.com. For example, Kering Group-owned luxury brand Balenciaga officially entered Tmall on 15 May, while Richemont Group's luxury brand Chloé also unveiled its Tmall flagship store on 18 May, offering the brand's entire range of handbags, ready-to-wear, footwears, accessories and other fashion items. Balenciaga stated that its partnership with Tmall marks a major step for its business strategies in China, which aim to enhance digital experience for Chinese consumers and to further adapt the consumption scenes advocated by young shoppers[46]. LVMH Group-owned fine jewelry brand Bulgari, after sealing a strategic partnership with the e-commerce platform in April, officially launched its online store on Tmall in May, offering perfume and cosmetics on the platform. Previously, a number of luxury brands under LVMH Group including Rimowa, Guerlain, Benefit, Givenchy, Zenith, Moët Hennessy and others have set up their online stores on Tmall[47].

British designer brand Christopher Kane has also expanded its online presence in China by launching on JD.com. The brand opened its online flagship store on JD.com in May and announced that it will participate in JD.com's "618" Shopping Festival. It is reported that the products sold on the online flagship store are directly supplied by Christopher Kane, and are selected by JD.com's buyers according to Chinese consumers' preferences[48].

14. Major luxury groups see sales rebound in China, showing signs of recovery

Major luxury groups have witnessed sales rebound in China since March when the COVID-19 lockdown gradually lifted. For example, LVMH, the owner of Louis Vuitton, Dior, and Sephora, reported that the group's sales in China jumped 50% for the first half in April. Hermès also confirmed a double-digit sales growth in China. The company saw record sales at its Guangzhou branch, which, reopened in early April after an expansion project, generated sales of 2.46 million euros on its first day of operations. Kering, on 21 April, also revealed that the company experienced sales growth in numerous cities in China, especially in the southern and eastern parts of the country, with stores in some cities posting double sales growth compared to the same period last year. French beauty giant L'Oréal, which operates premium beauty brands Yves Saint Laurent, Giorgio Armani, Lancôme, and others, also recorded a 6.4% yoy sales growth in China between January and March 2020[49].

Regulation updates

Measures to boost consumption

1. NDRC and regional governments launch multiple measures to boost consumption

To cushion the economic hit caused by the COVID-19 outbreak, the National Development and Reform Commission (NDRC) affirmed on 24 May that it will take multiple measures to further promote consumption:

- Promoting consumption upgrade, strengthening the supervision of brands, product quality, industry standard and improving the consumption environment.
- Further expanding service consumption, accelerating the development of service consumption in culture, tourism, sports, elderly-care, childcare, housekeeping, and education.
- Accelerating the cultivation of new consumption models in areas for digital consumption, online consumption, information consumption, etc.; promoting the integration of online and offline consumption; promoting the transformation and upgrading of traditional offline retail formats.
- Promoting green consumption.
- Strengthening the construction of urban and rural logistics networks to facilitate consumption; promoting the construction of smart lockers[50].

Meanwhile, several regional governments also launched various measures to boost consumption:

<u>Beijing</u>

The Beijing Municipal Bureau of Commerce published the "Action Plan to Boost Consumption and Improve the Quality of Life in Beijing" on 10 June. It proposed 22 measures to facilitate consumption upgrade and ensure the stable operation of the consumption market. These measures include:

- Nurturing new consumption models and promoting smart living. The government will facilitate the cooperation between e-commerce players and new media companies and promote the adoption of new business models such as social commerce, livestream commerce and online shopping. It will also guide the cooperation between e-commerce players and commercial districts and communities in the promotion of store-front warehouses and groceries shopping apps.
- Reconstructing governance to better serve the people. The government will improve community business planning, aiming to set up or improve 1,000 convenient services points by end of 2020. It will also establish community and business services centers.
- Creating international shopping centers by improving supplies. The government aims to attract first store and first launch business from quality brands by providing funds to their property landlords and e-commerce partners. To boost the consumption of imported goods, it will support the construction of cross-border e-commerce bonded warehouses and experiential stores. To boost automobile consumption, it will implement plans to phase out high emission and old vehicles. In addition, the government will launch "Beijing at Night" plan version 2.0 and design around 10 night-time travelling routes.
- Strengthening the supply of essential goods and developing infrastructure to facilitate distribution. The government will build a smarter, greener and more intensified logistics and supply chain system.
- Deepening "reforms to delegate power, streamline administration and optimize government services" and improving business environment of the consumption market. The government will provide more financial and other necessary support[51].

On the other hand, in March, Beijing also launched funding support for 11 areas in the commercial sector to bolster the development of the commercial sector in 11 areas: standardized development of chain store and franchise business; establishment of "Internet + circulation" innovative demonstration projects; promotion of modern trade and logistics business; setting up of public services platforms for headquarters; development of traceability projects for meat and vegetables; development of first store for brands; upgrading and transformation of traditional malls; installation of barrier free facilities; reduction of energy consumption; and development of wholesale market for agricultural products. Each area is entitled to a maximum of 5 million yuan of funding support[52].

Guangdong

Guangdong Bureau of Commerce published the "Political Measures to Accelerate Circulation and Boost the Development of Commercial Consumption in Guangdong Province" on 1 June. It proposed 20 measures to facilitate consumption in Guangdong, including formulating an implementation plan to develop international shopping cities in Guangdong; developing clusters of global brands; supporting qualified cities to set up duty-free shops; supporting enterprises to conduct "bonded display transactions" in areas under special customs supervision; allowing bonded display transactions of premier consumer goods such as automobiles in CBDs; facilitating the development of cross-border e-commerce integrated pilot zones; and expanding retail imports by cross-border e-commerce players[53].

Market supervision

2. China releases master plan for Hainan free trade port; to optimize custom duties and boost tourism and consumption

The CPC Central Committee and the State Council released a master plan for the Hainan free trade port on 1 June, aiming to make the southern island province a global free trade port. It proposed to boost tourism and consumption by optimizing tax schemes: talents enjoy a personal income tax of 15%; enterprises in the encouraged industries are entitled to a reduced corporate income tax rate of 15%; manufacturing equipment imported for self-usage are exempt from import tariffs, value-added and consumption taxes; import tariffs, value-added and consumption taxes of imported goods are waived for residents of Hainan; categories of offshore duty-free consumer goods are expanded and quota is raised to 100,000 yuan per person per year; enterprises in tourism, modern service and high-tech industries enjoy tax exemption for income from newly increased overseas direct investment before 2025; import tariffs and sales taxes are exempt for displayed offshore goods[54].

3. State Council supports export-oriented factories to sell domestically

On 22 June, the State Council issued the "Implementation Opinions on Supporting Export-oriented Factories to Sell to Domestic Market", aiming to help export-oriented factories survive in the post-COVID era. The Opinions put forward the following measures: simplifying product certification process and taxation procedures for export-oriented factories to sell domestically; supporting the launch of various retail channels/ platforms which target the domestic market, encouraging export-oriented factories to join force with e-commerce platforms and build their own private labels; and strengthening financial support to export-oriented factories to transform and sell domestically[55].

E-commerce

4. NDRC and local governments promote the development of new digital business models

To cultivate the development of a new economy, the NDRC and Cyberspace Administration of China (CAC) together issued the “Implementation Plan for Promoting the Development of New Economy with Smart Technologies” in April. It targeted to nurture digital enterprises, create digital supply chain solutions, and build digital ecosystems. The plan encouraged the development of sharing economy, digital trade and gig economy, while supporting the development of new retail business models, online shopping, contactless delivery services, online medical services, online education, new mobility services, co-employment, remote office solutions, stay-at-home economy and other new business models. Meanwhile, it also proposed to remove policy barriers for the development of such new business models[56].

Later in May, the NDRC, together with 145 units including Internet companies, leading industry players and industry associations, launched the “Action Plan for Digital Transformation Partnership (2020)” to help micro, small and medium-sized enterprises (MSMEs) lower their costs of digital transformation and shorten the transformation period. A first batch of 500 supportive measures will be provided to MSMEs, covering areas such as resources matching, software and hardware support, supply chain support, consulting services, professional training services, among others[57].

Local governments such as Shanghai also released action plan for promoting digital economic development. On 13 April, Shanghai Municipal Government issued the "Action Plan for Promoting Digital Economic Development in Shanghai, 2020-2022". It aimed to gather over 100 innovative enterprises, launch over 100 online application scenarios and create over 100 brands and services related to the new economy by 2022; and develop over 100 key technologies for the digital economy. It will also focus on 12 areas of development, namely, unmanned factories, industrial Internet, remote office solutions, online finance services, online entertainment, virtual exhibition services, fresh food e-commerce, contactless delivery services, new mobility services, online education, online research and design, and online medical services[58].

5. Regional governments promote livestreaming e-commerce

Some regional governments set out measures to promote the development of livestreaming e-commerce. For example, Guangzhou Municipal Commerce Bureau announced the “Guangzhou Livestreaming E-commerce Development Plan 2020-2022”, setting out 16 policies and measures to promote the development of livestreaming e-commerce (or live commerce) and innovative business models in the city. The Plan predicted that in 2022, Guangzhou will become the livestreaming e-commerce capital of China through setting up a batch of livestreaming e-commerce industry clusters, fostering the development of 10 livestreaming institutes that can serve as a role model and 100 influential MNC (multi-channel network) service providers, and incubating 1,000 KOL/online celebrity brands and 10,000 live commerce influencers[59].

On the other hand, Sichuan also released the first provincial-level development plan on livestreaming ecommerce. In April, Sichuan Provincial Department of Commerce released the "Action Plan for Development of Livestreaming E-commerce for Sichuan products, 2020-2022". The plan aimed that by 2022, total sales generated from livestreaming e-commerce will reach 10 billion yuan; it also expected that livestreaming will drive 100 billion yuan sales of other related industries. It targeted to set up 10 livestreaming e-commerce industry clusters, foster the development of 100 key service providers in livestreaming industry, and incubate 1,000 KOL/online celebrity brands and 10,000 live commerce influencers. This is the first provincial-level development plan on livestreaming e-commerce in China[60].

6. State Council approves the establishment of CBEC comprehensive pilot zones in 46 cities

In May, the State Council approved the establishment of cross-border e-commerce (CBEC) comprehensive pilot zones in 46 cities, including Xiongan New Area, Datong City, Manzhouli, Yingkou, Panjin, Jilin and Heihe. Together with the previously established 59 CBEC comprehensive pilot zones, there are totally 105 CBEC comprehensive pilot zones in China now, covering 30 provinces, autonomous regions and municipalities. The State Council will replicate the operating model of the existing CBEC comprehensive pilot zones, promote industrial transformation and upgrading, strengthen brand building, encourage innovation and development in CBEC business, and support high-quality development of international trade in these CBEC comprehensive pilot zones[61].

Logistics

7. NDRC and MOT announce measures to further reduce logistics costs

On 2 June, the NDRC and the Ministry of Transport (MOT) jointly issued the "Implementation Opinions on Further Reducing Logistics Costs", which aims at strengthening measures to reduce logistics costs. The plan proposed 24 measures in six aspects, including streamlining the process of customs clearance; broadening financing channels; implementing preferential tax for logistics industry; reducing railway freight and air freight charges; promoting the sharing of logistics information; accelerating the development of smart logistics; and facilitating the development of green logistics[62].

Convenience stores

8. MOFCOM further encourages development of chained convenience stores

On 30 April, the General Office of Ministry of Commerce (MOFCOM) issued the “Notice on Accelerating the Development of Chained Convenience Stores”, stating that all local governments should help convenience stores resume business under strict implementation of infection prevention control measures during the COVID-19 outbreak. It also encouraged the adoption of emerging business models such as online and offline integration, community group buying, and contactless delivery to enable residents to easily purchase daily necessities, thereby rejuvenating community consumption[63].

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