

# Issue 1 | General Retail

## Executive Summary

### **China's retail sector sees modest growth in 2017; yet China-U.S. trade war is set to dampen consumer sentiment and drive down retail sales growth.**

China has been the world's second-largest retail and consumer market after the U.S. since 2014. Total retail sales of consumer goods reached 36.6 trillion yuan in 2017, up nominally by 10.2% yoy. In 1H18, total retail sales of consumer goods increased nominally by 9.4% yoy to reach 18.0 trillion yuan. However, the escalating China-U.S. trade war is set to hinder economic growth, which in turn will affect consumer sentiment and consumer spending. China's retail sector as a whole will be adversely affected and is expected to see single-digit sales growth in the coming year.

**Millennials and generation Z reshape the retail landscape.** Middle class consumers in China, particularly the millennials and post-millennials (or generation Z), are becoming increasingly influential in the retail sector. China will have the world's largest middle class population by 2027, a segment whose strong spending power will reshape consumption domestically and internationally over the next decade. Local and international retailers are ramping up efforts to engage more effectively with these influential consumers. To lure young shoppers, brands are increasingly turning to young celebrities and influencers to market their products, and are launching new product lines with younger tastes.

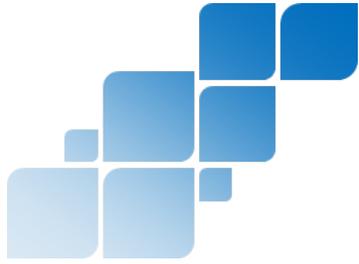
### **Retailers strive to diversify their product and service offerings and deliver enriched lifestyle shopping experiences.**

To entice shoppers, many retailers have expanded into new sectors and collaborated with other market players to expand service offerings and generate new revenue streams. Meanwhile, to meet the higher expectations of today's consumers, more and more retailers -- especially department stores and shopping mall operators -- have upgraded by introducing new and innovative concept stores and more lifestyle services.

**O2O continues to dominate the retail scene.** Pursuit of online-to-offline (O2O) strategies has become a preoccupation for most brands and retailers. Many traditional retailers in China have actively pursued digital expansion and deployed O2O strategies to ensure seamless integration of all channels -- physical, online, mobile and social. At the same time, some leading e-commerce companies and "pure-clicks" enterprises have tiptoed into bricks-and-mortar in the hope of providing a better shopping experience.

**Use of smart technologies gains steam.** China's retail sector is being redefined by a new wave of technologies to facilitate O2O integration while significantly enhancing customer experience. A multitude of technology-driven business models and business formats has emerged recently. Digitized experiential stores and AI-driven pop-up stores, unmanned stores are examples.

**Pop-up retailing comes on the scene.** Pop-up retailing has gained popularity in recent years, with brands and retailers opening pop-up stores backed by innovative marketing content to promote products and raise awareness. Some also use the pop-up format to test new technologies, concepts and collections, and to gain market insights. One of the major advantages of pop-up retailing is that the set-up costs are far lower than for permanent stores with long-term leases.



# Issue 2 | E-commerce

## Executive Summary

**China's online retail market continues to drive economic growth.** China's online retail market, the world's largest, has shown resilient growth despite a slowing economy. The transaction value of China's online retail market increased 32.2% yoy to reach 7.18 trillion yuan in 2017. This rapid growth is attributable mainly to China's large population of Internet users and the early adoption of mobile shopping by Chinese consumers. Mobile commerce accounted for 81.3% of total online shopping transactions in 2017.

**E-commerce giants strive to increase offline presence and expand their ecosystems.** With the rise of omnichannel retailing, e-commerce giants are actively penetrating offline retailing with the idea of perfecting their physical retail networks and further expanding their business ecosystems. Alibaba and JD.com, in particular, have accelerated the pace of their offline expansion by merging with or acquiring physical retailers. They hope to build an all-encompassing business ecosystem that fully blends online and offline channels so as to become ubiquitous and indispensable in the daily life of all Chinese consumers.

**Social commerce becomes increasingly popular; short video platforms facilitate digital marketing.** Eying the high level of consumer penetration by social media platforms such as WeChat, Weibo, Pinduoduo, and live-streaming and short video platforms, such as Douyin, brands and retailers are increasingly trying to sell and market their products via these channels.

**E-commerce players and Internet giants launch their own private labels.** Some e-commerce companies have taken bold initiatives to launch their own private labels to offer consumers quality, premium and personalized products and services. NetEase, Alibaba, JD.com, Tencent, Xiaomi and Mia.com are cases in point. Some e-commerce companies have even set up physical stores to sell their own private labels.

**Rural e-commerce continues to thrive.** The rural online retail market has become a new growth engine for e-commerce in China with the near saturation of the urban online market. The government has been very supportive of this development. Recognizing the ample growth potential of the rural e-commerce market, leading retailers and e-commerce companies have adopted "going rural" strategies.

**China's first E-commerce Law launches.** The E-commerce Law, which is to take effect on 1 January 2019, is designed to safeguard the legitimate rights and interests of all parties involved in e-commerce; to regulate e-commerce practices; maintain the sound order of the market, and foster the further development of e-commerce in a manner that is sustainable and healthy.



# Issue 3 | Department Stores

## Executive Summary

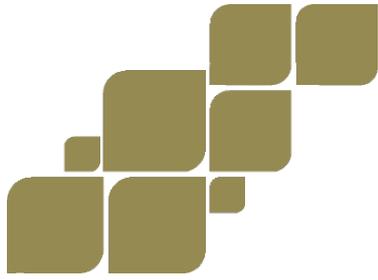
**Department store sector maintains stable sales growth; new store openings continue.** China's department store sector witnessed positive and stable growth in the past year. According to the NBS, retail sales of department stores above a designated size (enterprises with annual sales of 5 million yuan or above and with employee strength of 60 or more) increased by 4.6% yoy in 1H18. MOFCOM statistics also show that the yoy growth of 5,000 key retailers reached 4.6% in 1H18, with department stores accounting for 4.5% yoy. In terms of new store openings, over the past two years, the number of newly opened department stores was still slightly more than that of department stores which were closed or revamped, resulting in a net rise.

**Transformation efforts have started to pay off.** Recently, the department store sector has made every effort to transform and adjust to keep pace with changing consumer needs, whether through the upgrade of hardware and stores, the refinement of merchandise and services, supply chain integration, or the restructuring of business models and operating systems. The sector as a whole has started to reap the benefits. According to a survey by the China Commerce Association for General Merchandise, nearly 65% of 85 department stores surveyed enjoyed positive yoy sales growth in 2017.

**Leveraging technologies to pursue O2O integration; forming partnerships with Internet companies and e-commerce players is common practice.** Many department store operators have adopted advanced technologies such as mobile Internet, big data, the IoT (Internet of Things) and even AI to achieve O2O integration -- namely, a seamless integration across physical stores, online platforms and mobile terminals --along with digital transformation. Meanwhile, increasing numbers of department store operators have formed strategic alliances with Internet or large-scale e-commerce companies to roll out O2O initiatives that leverage the latter's huge traffic resources, big data as well as logistics capabilities.

**Diversifying retail formats and tapping into other business sectors.** To adapt to the changing needs of consumers, more and more department stores have sought to expand their scope of business and engage in multi-format, multi-sector operations. For example, in recent years Golden Eagle Retail Group has launched boutique supermarkets, bookstores, pet stores and beauty stores, to meet the discerning needs of middle class consumers. Recognizing the fast growth potential of convenience stores, players such as Wangfujing Group, Rainbow Department Store and New World Department Store have tapped into the convenience store segment, launching their own convenience store brands.

**Offering additional sales channels to enhance product uniqueness and gross profit margins.** To enhance product and service uniqueness and provide customers with a differentiated shopping experience, many department store operators have expedited the expansion of direct sales business. Some operators such as the Bailian Group, Wangfujing Group, Wanda Department Store and New World Department Store have taken even bolder steps by developing their own private labels and set up buyer (multi-brand) shops to sell exclusive brands and private labels.



# Issue 4 | Shopping malls

## Executive Summary

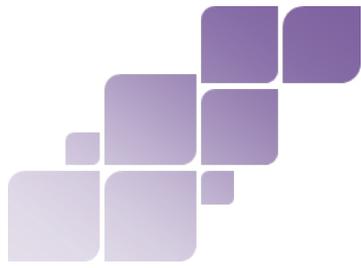
**Shopping malls sector maintains robust development.** In 2017, most large-scale shopping malls in China delivered a positive sales performance. According to iziRetail, the total sales of 190 such centers across 51 cities in China reached 441.3 billion yuan in 2017, up 11.3% yoy. A study by Linkshop also shows that the top 20 shopping malls in China all achieved positive yoy sales growth in 2017.

**Shopping mall operators shift to more consumer-centric business models.** In recent years, increasing numbers of mall operators have changed their mindset and transformed their operations and business models by adopting a more consumer-centric approach. Many shopping malls have endeavored to strengthen their physical assets in all aspects including upgrading hardware and facilities, reconfiguring unit layouts, refining tenant mixes, as well as enhancing in-mall service facilities. They are also responding swiftly to consumers' needs by providing more interactive features in the mall, including entertainment, leisure activities, a variety of food options and unique concepts that differentiate their offerings.

**Exploring new development concepts.** Shopping mall operators in China have actively been exploring new development concepts. A trend is emerging of "shopping mall + shopping precinct" (or "streetscaped") malls with Sanlitun Taikoo Li as a successful forerunner, followed by Chengdu Taikoo Li, and the recently opened MIXc World and UpperHills in Shenzhen. The new concept features a combination of indoor and outdoor elements, with a shopping center plus a pedestrian area that has shops and restaurants – all within a landscaped environment. It can create a unique ambiance for shopping and bring consumers a special experience.

**Leveraging technologies and multichannel strategies to transform the mall experience.** Many shopping mall operators realize that the best way to deal with rapid technological change is to embrace it. They are utilizing digital capabilities to take the shopping experience to the next level. Beyond providing basic services such as free WiFi; accepting mobile payments, and running different promotions to encourage social media engagement, mall operators are adopting in-mall technologies such as AI-powered services to improve the omnichannel experience and strengthen relationships with consumers.

**E-commerce giants make forays into shopping mall sector.** Recently, the shopping mall sector in China has seen the emergence of a new competitive landscape with the entrance of e-commerce giants. The opening in April 2018 of the Alibaba Group's first bricks-and-mortar shopping mall, in Hangzhou, is a major step by the Group towards achieving its goal of blending digital prowess with a footprint in the physical world.



## Issue 5 |

# Hypermarkets/ Supermarkets Executive Summary

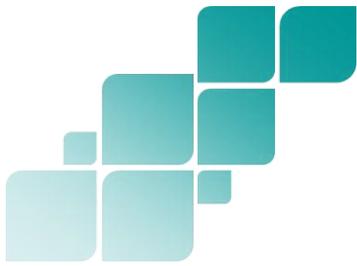
**Hypermarket and supermarket operators see improvement in sales growth.** In recent years, the hypermarket and supermarket sector has faced fierce competition from the e-commerce sector as well as from smaller-scale retail formats such as convenience stores, community stores and specialty stores. That being said, many hypermarket and supermarket operators have stepped up efforts to revamp their operations to cater the changing needs of Chinese consumers. Their efforts have paid off with solid improvements in sales performance. The sales growth of supermarkets above a designated size (enterprises with annual sales of 5 million yuan or above and with employee strength of 60 or more) was 7.4% yoy in 1H18, up from 6.3% yoy in 1H17. Most of the top hypermarket and supermarket chain operators in China achieved a better performance in 2017 than in 2016, thanks both to new store openings and format expansion.

**Players are adapting to “New Consumption” era.** Over the past year, many traditional hypermarket and supermarket operators have proactively adapted themselves to the “New Consumption” era. Many have used data analytics to increase store traffic and offer more targeted promotions to shoppers. Some have integrated their inventory and supply chain management systems with e-commerce or solutions platforms to improve warehouse management, inventory planning and last-mile delivery. Others have invested in technologies and launched “smart stores” to create a better in-store experience and higher level of interaction with shoppers. Meanwhile, many hypermarket and supermarket chain operators have partnered with third-party O2O local lifestyle service platforms, such as JD Daojia and Dmall, to provide O2O shopping and speedy delivery services.

**Format revamp is gaining traction.** Many hypermarket and supermarket chain operators have revamped their stores or launched new store formats (e.g. smaller-sized format and fresh-food supermarkets) to better suit the changing needs of customers. They have also created more spaces for occasion- or experience-based activities (e.g., in-store dining) to improve customer stickiness.

**Putting strong effort into developing private labels.** A number of hypermarket and supermarket chains have launched their own private labels in recent years. The profit margin for those who have done so is 15% higher. Developing private labels is thus winning strategy for hypermarkets and supermarkets that wish to differentiate themselves from their peers and earn higher profit margins

**Forming strategic alliances with Internet giants** is one commonly-used tactic for driving synergies between online and offline retailing. To achieve better O2O integration, some traditional grocery retailers have formed partnerships with Internet companies to gain access to payment tools, social media, big data analytics, etc. In turn, Internet companies can leverage the extensive physical store networks of hypermarkets and supermarkets to reach more customers.



# Issue 6 | Convenience Stores

## Executive Summary

**Convenience stores (CVS) have been the fastest-growing retail format in recent years.** Total sales revenue for the CVS sector (including forecourt stores) reached 190.5 trillion yuan in 2017, up 23% yoy, and the growth momentum is expected to continue as the small retail format continues to gain in popularity in China. According to the MOFCOM, the yoy growth of 5,000 key retailers reached 4.6% yoy in 1H18, with CVS recording the fastest growth among all retail formats: 7.6% yoy, compared with 4.5% yoy for supermarkets and 1.6% yoy for department stores. In 2017, the total number of CVS in China topped 100,000.

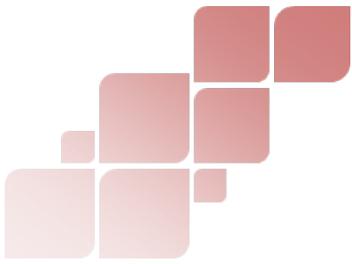
**O2O initiatives remain crucial.** To stay competitive, many CVS operators have drawn up seamless O2O strategies to attract and retain customers. Providing pick-up services and partnering with O2O local lifestyle service platforms are among common practices.

**CVS players make greater efforts to launch private labels.** Nowadays, Chinese consumers look for products that are personalized or even unique. To cater to this demand, CVS operators such as FamilyMart, 7-Eleven and Anda Convenience Store have stepped up efforts to launch their own private labels and to offer such products. That being said, private label development in China's CVS sector still lags far behind that of equivalent chains in developed countries such as Japan. Over 80% of sampled CVS operators in China said that sales of their private labels accounted for less than 10% of total sales.

**Emergence of technology-driven business models.** Technology advancement is a significant factor driving the growth of the CVS sector. Since the second half of 2017, there have been significant CVS initiatives involving the adoption of technologies that can transform retail operations. This had led to the emergence of technology-driven business models including those featuring unmanned/cashierless CVS, smart shelves and smart vending machines.

**Launching fresh food community stores is a growing trend.** CVS is one of the most relevant formats for serving local communities. Recently, some CVS chains have upgraded and transformed their stores into fresh food community stores, catering to the growing appetite of Chinese consumers for fresh, healthy, quality products.

**Many mom-and-pop stores connect with Alibaba's LST and JD Convenience Store.** E-commerce giants Alibaba and JD.com have sought to extend their offline footprints by connecting with tens of thousands of mom-and-pop stores to help them digitalize their operations and increase their gross merchandise volume. Under its New Retail initiative, and to advance its O2O strategy, Alibaba has launched the LST "Ling Shou Tong" system to help mom-and-pop stores embark on digital transformation. JD.com has rolled out the JD Convenience Store initiative, partnering with owners of CVS across the country, particularly in rural areas, to help them revamp their stores.



# Issue 7 | Luxury Market

## Executive Summary

**China's personal luxury goods market enjoys robust growth in 2017.** Sales of personal luxury goods in China rose significantly to 20 billion euros in 2017, representing a 15% yoy growth at current exchange rates and a 18% yoy growth at constant exchange rates. This notable rebound suggests that the domestic personal luxury goods market has returned to robust growth.

**Chinese millennial consumers continue to drive global luxury growth.** The growth of Chinese luxury spending in 2017 was driven by several factors, the major one being millennials accelerating their spending on luxury. Millennials in China, especially those from the fast-growing middle class, have stronger spending power and are more willing to spend than counterparts in other countries. It is expected that by 2024, millennials will account for 50% of China's personal luxury market.

**Luxury retailers team up with young Chinese celebrities to market their products.** Increasing numbers of luxury retailers are ramping up efforts to better engage with millennials, the most powerful consumer group in China's luxury market today. To woo young shoppers, brands and retailers are turning to young celebrities and influencers to market their products. They are also launching new product lines catering to younger tastes.

**E-commerce players crack the luxury market; yet Chinese luxury shoppers still prefer offline.** Eying the increasing demand for luxury goods online, e-commerce players such as Alibaba and JD.com have set up luxury e-commerce platforms targeting this segment. Despite the enthusiasm of Chinese consumers for online shopping, many still prefer purchasing luxury products at bricks-and-mortar stores. These enable them to see, touch, feel and try out products, as well as to enjoy high-end customer experiences such as refreshments, invitations to private lounges where goods can be previewed, and other customized services.

**Luxury players scramble to strengthen social commerce presence; WeChat Mini Program is gaining popularity.** Considering that social media and word-of-mouth are major sources of information for Chinese consumers, increasing numbers of international luxury players are striving to boost their social commerce presence as a way to market their products in China. During the Qixi festival (China's equivalent to Valentine's Day), which in 2018 fell on 17 August, many luxury brands used the WeChat Mini Program to offer products exclusively for the festival.

**International brands lower prices in China in response to tariff cuts by the Chinese government.** To encourage domestic consumption while promoting imports, the State Council announced in May 2018 that the country would reduce import tariffs on a range of consumer goods with effect from 1 July 2018. In response, some international brands have marked down their product prices in China by an average 3% to 5%.



# Issue 8 | Cross-border E-commerce (Import) Executive Summary

**Cross-border e-commerce (CBEC) maintains stable development but at slower pace.** China's CBEC (import) market has maintained stable development in recent years, fueled mainly by individuals upgrading their level of consumption. According to iResearch, the transaction value of the CBEC import retail market increased by 49.6% yoy to 111.3 billion yuan in 2017 and is expected to balloon to over 350 billion yuan by 2021. Hectic though growth has been for China's CBEC (import) market, the pace has, in fact, slowed over the past three years. This is due in part to the launch in late March and early April 2016 of new CBEC tax policies and a positive list for permitted imported goods, which might pose uncertainties for the future development of cross-border trade.

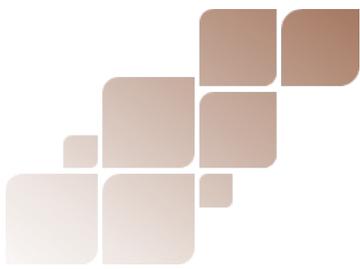
**NetEase Kaola, Tmall Global and JD Worldwide continue to top the list among CBEC (import) players.** NetEase's CBEC arm Kaola ranked first in the CBEC market by transaction value with 26.2% market share in 1H18, followed by Tmall Global with 22.4% market share and JD Worldwide with 13.4% market share.

**Food, beauty and personal care products, and apparel, footwear and bags are the best-selling categories for CBEC (import).** CBEC shoppers buy these products mostly from Japan, the U.S. and South Korea.

**The Chinese government establishes more pilot zones for CBEC.** As of August 2018, China has 35 CBEC Comprehensive Pilot Zones, 22 of which were approved by the State Council on 7 August, 2018. The State Council has also urged relevant government departments to support innovation and development in CBEC Comprehensive Pilot Zones, including streamlining logistics processes and custom clearance procedures, enhancing information sharing, promoting effective regulatory innovation, and pushing forward with international trade liberalization, facilitation and business innovation.

**Emergence of new CBEC operation models.** In recent years, some CBEC operators have trialed various ways to make shopping via CBEC (import) platforms more convenient and to provide customers with better shopping experiences. Two new operation models have emerged – the first is an **extension of the direct mail model, using overseas warehouses (the “direct mail + overseas warehouse” model)**; the second is the **modification of the bonded area import model, with the setting up of offline stores for transaction (the “bonded area import + offline store” model)**.

**Players put more emphasis on product tracking system.** Blockchain technology is becoming increasingly popular among CBEC operators as a method for tracking products. With this technology, leading CBEC platforms can collect, integrate and display product information to consumers in a more transparent way, thus gaining customer trust and loyalty.



# Issue 9 | Retail and E-commerce Logistics Executive Summary

**Strong growth of online retail sales fuels demand for logistics services.** The fast growth of online retailing in China has given the logistics industry a boost in line with soaring demand for transport and delivery services. The total value of logistics activity reached a record 252.8 trillion yuan in 2017, up by 0.6% yoy in real terms.

**Express delivery market scales up; growing demand for intra-city courier services.** As a critical part of e-commerce logistics, the express delivery sector has grown rapidly. The total volume of completed deliveries amounted to 40.1 billion pieces in 2017, up 28.0% yoy, making China's express delivery market the largest in the world in terms of delivery volume. Total sales revenue for the sector amounted to 495.7 billion yuan in 2017, up 24.7% yoy. There has been a surge in demand for intra-city courier with the emergence of new retail practices such as O2O and the creation of large numbers of online channels selling fresh produce and healthcare products, coupled with increasing customer demand for fast delivery.

**“Smart logistics” dominates the agenda.** Adoption of advanced technologies such as Radio Frequency Identification (RFID), Global Positioning System (GPS), the Internet of Things (IoT), cloud computing, drones and robotics, in addition to automation of logistics processes to improve efficiency, has become imperative for the retail and e-commerce logistics sector. Recently, logistics and e-commerce operators have invested heavily in smart logistics, hoping to enhance fulfilment capability and efficiency, to streamline operations and reduce logistics costs.

**Innovations to strengthen last-mile delivery.** To cater to consumers' heightened expectations for fast delivery, retailers such as Uniqlo, Walmart (China), Yonghui, YH Super Species and Watsons have introduced “click & collect” services. Many retailers have partnered with O2O platforms or logistics companies to roll out such services. Meanwhile, some retailers and logistics operators have introduced innovative ways to speed up delivery and enhance consumer convenience through, for example, the use of drones and autonomous vehicle, and smart pick-up towers in key locations.

**E-commerce and logistics players put more emphasis on global logistics network expansion.** In recent years, companies engaged in e-commerce and logistics have stepped up global expansion of their logistics networks to better facilitate cross-border delivery between China and overseas countries. For example, Cainiao plans to build world-class logistics hubs in several locations around the world, and JD Logistics has upgraded its overseas warehousing services.

**Rural logistics is the next growth engine.** The promising outlook for rural e-commerce has prompted many leading e-commerce and Internet companies to push further ahead with “going rural” initiatives.

## Contacts

### Asia Distribution and Retail

Teresa Lam  
Vice President  
Email: [teresalam@fung1937.com](mailto:teresalam@fung1937.com)

Christy Li  
Senior Research Manager  
Email: [christyli@fung1937.com](mailto:christyli@fung1937.com)

Lucia Leung  
Research Manager  
Email: [lucialeung@fung1937.com](mailto:lucialeung@fung1937.com)

Renne Chan  
Research Manager  
Email: [rennechan@fung1937.com](mailto:rennechan@fung1937.com)

Tracy Chan  
Research Manager  
Email: [tracychansy@fung1937.com](mailto:tracychansy@fung1937.com)

### Fung Business Intelligence

10/F, LiFung Tower, 888 Cheung Sha Wan Road, Kowloon, Hong Kong  
Phone: (852) 2300 2470 | Fax: (852) 2635 1598  
Email: [fbicgroup@fung1937.com](mailto:fbicgroup@fung1937.com) | <https://www.fbicgroup.com>



© Copyright 2018 The Fung Business Intelligence. All rights reserved. The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Though the Fung Business Intelligence endeavours to ensure the information provided in this publication is accurate and updated, no legal liability can be attached as to the contents hereof. Reproduction or redistribution of this material without prior written consent of the Fung Business Intelligence is prohibited.