

China's Department Stores Report 2018-2019

March 2019





Introduction

China's department store sector has gone through some ups and downs in the last decade. The lackluster performance since 2010 was due in part to the rise of e-commerce as well as the government's strengthened anti-corruption efforts to eliminate lavish gifts for government officials since late 2012.

In recent years, many department store operators have become more customer-centric. They have made relentless efforts to transform and upgrade their businesses by incorporating more experiential elements to enhance shopping ambience, enriching product offerings, engaging in direct sales business, among others. Many department store operators have seen some signs of rebound in both total sales and profits.

China's Department Stores Report 2018-2019 analyses the macroeconomic data and collects financial data from 90 domestic department store operators to gauge the sector's performance in 2018. The report also discusses the key innovation and transformation initiatives of leading department store operators, major issues and challenges faced by the sector, and development trends for 2019.

In producing this report, Fung Business Intelligence is delighted to join force once again with China Commerce Association for General Merchandise (CCAGM). We would like to express our utmost gratitude to all department store operators and industry experts who have supported us and participated in the preparation of this report.

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Executive summary

To cope with China's ever-changing retail environment, increasing numbers of department store operators have reinvented and upgraded their businesses by pursuing innovation and transformation initiatives. In 2018, China's department store sector showed some signs of bottoming out with plenty of department store operators saw their sales and profits rebound.

Key innovation and transformation initiatives adopted by department store operators include:

- **Actively pursuing omni-channel and digital transformation**

- As O2O integration and digital transformation have become mainstream, department store operators increasingly leverage big data and other breakthrough technologies to bring online and offline experiences seamlessly together and improve operational efficiencies.
- Many operators use big data analytics and other algorithms to better predict and understand customers' needs, review and fine-tune product portfolio and provide personalized products and services. This enables department store operators to accelerate digitalization and carry out targeted marketing strategies. Meanwhile, some operators leverage technologies to revamp consumption scenes, enhance customers' in-store experience and better engage with customers.
- It is worth noting that some operators have chosen to partner with leading Internet companies or large-scale e-commerce players to implement digital transformation – by leveraging their business partners' huge traffic flows, big data as well as logistics capabilities.

- **Strengthening direct sales business to enhance brand equity and increase profits**

- Recognizing the drawbacks of the concessionary model, many department store operators have expanded their direct sales business through increasing the scale of direct product procurement, launching self-operated buyer/multi-brand stores and actively developing private labels. They hope to enhance product and services uniqueness and provide better shopping experience for customers.

- **Introducing innovative business models and diversifying retail formats**

- To stay relevant in the increasingly competitive marketplace, many operators have branched out into different retailing businesses and engaged in multi-format operation. This not only enables them to better meet the diversified needs of consumers, but also increase revenue streams. Our survey shows that supermarket/hypermarket format and shopping mall format are the two most popular retail formats that the department store operators have tapped into.
- Department store operators have been eager to explore new business models and introduce new retail concepts, such as tapping into catering business and rolling out on-demand delivery services.
- However, due in part to the economic uncertainty, two-thirds of surveyed department store operators showed reservations in expanding further into other businesses in the next 12 months.

- **Focusing more on experiential consumption**

- To adapt to consumers' growing desire for experiential shopping, many department store operators are endeavoring to provide more experiential elements such as family and child-related services and shops, art and culture exhibitions, IP contents and entertainment to lure customers.

Despite facing increasing challenges from e-commerce players, department store is still one of the major and most influential distribution channels in China and an indispensable part of consumers' lives. Department store operators' relentless efforts to transform and upgrade their businesses by pursuing digitalization, engaging in direct sales business to enrich product offerings and incorporating experiential elements to enhance shopping ambience will help drive the consumption upgrading trend in the country. Going forward, China's department store sector is set to maintain an overall stable growth with the continuation of the consumption upgrading trend as well as the government's determined efforts to boost consumption.

I. Market overview



1. Overview of China's department store sector

In 2018, China's retail sector experienced slower growth with total retail sales of consumer goods increased nominally by 9% year-on-year (yoy) to 38 trillion yuan; after eliminating the effects of price changes, the real growth was 6.9% yoy, a relatively low growth rate in recent years. Nevertheless, the department store sector showed some signs of bottoming out after undergoing years of profound transformation. For example, SKP Beijing's sales hit a record high of 13.5 billion yuan in 2018, up from 12.5 billion yuan in 2017; Intime Department Store's same store sales increased remarkably by 37% yoy; Wangfujing Group's net profit set a 5-year high in 2018; Far Eastern Department Stores' business in China turned profitable for the first time in 10 years; and Parkson Retail Group also continued to see steady growth in 2018 after turning to profit in 2017.

Major characteristics of the department store sector are as follows:

(1) Department store operators start seeing meaningful results with their O2O/omni-channel strategies

Online and offline (O2O) integration has become a major trend in the retail market. Realizing the importance of adopting O2O strategies, retail players have been adjusting their business strategies to adapt to evolving market trends, from PC-based e-commerce and O2O integration to mobile commerce and social commerce. Many department store operators in China have adopted a more diversified and pragmatic O2O strategy, which can be connected and applied to different retailing and marketing processes. For instance, Intime Department Store has launched an app, allowing customers to search for products, place orders and track delivery. Another example is New World Department Store China. The retailer has launched "Xinshangou", an online shopping platform dedicated to flash sales, offering best-selling items and discounted products, and allowing customers to order online and pick up their orders offline. Hanguang Department Store and Eurasia Group have also leveraged on WeChat to grow their businesses. The former has drawn on WeChat to send out personalized promotion information to customers, while the latter has opened its WeChat Mini Program store to boost sales.

Selected examples of omni-channel initiatives adopted by 10 major department store operators are shown in Exhibit 1.

Exhibit 1. Selected examples of omni-channel initiatives adopted by 10 major department store operators

Department store operator	Omni-channel initiatives	Format	Details
Bailian Group	iBailian (www.bl.com/)	<ul style="list-style-type: none"> • PC-based e-commerce • App • Official account 	E-commerce platform
	Bailian Daojia	<ul style="list-style-type: none"> • WeChat Mini Program 	Delivery service
Chongqing General Trading Group	SJGO365.com (www.sjgo365.com/)	<ul style="list-style-type: none"> • PC-based e-commerce 	E-commerce platform
Changchun Eurasia Group	Ouya Weidian (www.oysd.cn)	<ul style="list-style-type: none"> • Official account 	E-commerce platform
	Ouya Daojia	<ul style="list-style-type: none"> • App 	Official online shopping website
	Ouya Membership program	<ul style="list-style-type: none"> • WeChat Mini Program 	Membership services
Wuhan Department Store Group	Wushang.com (http://www.wushang.com/)	<ul style="list-style-type: none"> • PC-based e-commerce • App • Official account 	E-commerce platform, with a Official account providing customer services
	Wushang Supermarket Scan to Buy	<ul style="list-style-type: none"> • WeChat Mini Program 	-
Wangfujing Group	Wangfujing Department Store	<ul style="list-style-type: none"> • Official account • WeChat Mini Program • Flagship store on Tmall 	-
Dashang Company Limited	Tiangou.com	<ul style="list-style-type: none"> • App • Official account 	-
Beiguo-Renbai Group	Ruyig.com (http://www.ruyig.com/)	<ul style="list-style-type: none"> • PC-based e-commerce 	-
	Ruyigou.cc	<ul style="list-style-type: none"> • App • Official account 	-
Rainbow Department Store	Red Scarf	<ul style="list-style-type: none"> • PC-based e-commerce • App 	
	Rainbow Department Store	<ul style="list-style-type: none"> • Official account • WeChat Mini Program 	Enabling self-service and providing home delivery and parking services on its WeChat Mini Program
Zhenhua Group	Zhenhua Department Store	<ul style="list-style-type: none"> • Official account 	E-commerce platform
Intime Retail Group	Yintai.com (www.yintai.com)	<ul style="list-style-type: none"> • App • Official account • WeChat Mini Program • Flagship store on Tmall • Available on Miao Street • Available on Fuwu.alipay.com 	Mainly providing information on its Official account and WeChat Mini Program (services varied by region); Miao Street is the only official app of the retailer

Source: Internet sources; compiled by CCAGM

(2) M&A activities continue to rise

Merger and acquisition (M&A) activities in the department store sector have remained robust in recent years. More than half of the nearly 20 retail M&A activities happened during January 2018 to February 2019 involved department store businesses (Exhibit 2). Examples of department store operators engaged in M&A deals include Intime Department Store's full acquisition of Kaiyuan Retail; the merger between Guangbai Group and Guangzhou Friendship Group; Suning's takeover of 37 Wanda department stores; and the consolidation between Beijing Tourism Group and Beijing Wangfujing Dongan Group Company Limited. The M&A activities took place for two common reasons: collaborations between major competitors to further drive business growth or small companies taken over by larger players.

Meanwhile, M&A activities have sped up market concentration in the department store sector and enabled market players to expand upstream. By absorbing the capabilities and resources of their target companies, acquirers can increase competitiveness, sales and share in the market, further facilitating consolidation in the sector. Upstream M&A activities have seen rapid growth in recent years. A typical example is Dashang Group, which has invested in Australia's food company Beston Global Food Company.

Physical retailers with distinctive e-commerce capabilities such as Suning.com and Intime Department Store are expected to play a key role in upcoming M&A activities and gain more dominance in the market amid continued consolidation.

Exhibit 2. Examples of major retail M&A deals in January 2018 to February 2019

Time	Acquirer	Target	Details of the M&A deals
February 2019	Suning.com	Wanda Department Store	Suning.com announced to acquire 37 Wanda department stores
February 2019	China Holding Construction & Investment Group	Xiongfeng Group	China Holding Construction & Investment Group acquired 100% stake in Xiongfeng Group
January 2019	Better Life Group	Hunan Joindoor Hypermarket Company Limited	Better Life Group agreed to acquire 22 outlets of Hunan Joindoor Hypermarket and its store assets
January 2019	Zhongnan Commercial Group	Easy Home	Zhongnan Commercial Group announced plans to issue additional stock to finance its acquisition of 100% stake in Easy Home
December 2018	Shirble Department Store	TFG International	Shirble Department Store acquired 19% stake in TFG International
December 2018	Guangbai Group	Guangzhou Friendship Group	Guangbai Group acquired 100% stake in Guangzhou Friendship Group with cash consideration
November 2018	Jiajiayue Group	Zhangjiakou Fuyuexiang Supermarket Chain	Jiajiayue Group acquired 67% stake in Zhangjiakou Fuyuexiang Supermarket Chain for 156 million yuan
July 2018	Macro-Link International Investment Company Limited	Junefield Department Store	Macro-Link International Investment Company Limited completed its acquisition of 66.75% stake in Junefield Department Store
July 2018	Wumart Holdings	Xinhua Department Store	Wumart Holdings agreed to acquire less than 6% of the total issued shares of Xinhua Department Store
May 2018	Wangfujing Group	C.banner International Holdings Limited	Wangfujing Group announced plans to acquire new share issued by C.banner International Holdings Limited for no more than 100 million yuan
May 2018	Liqun Commercial Group	Lotte Mart	Liqun Commercial Group acquired 100% stake in 72 Lotte Mart stores in Eastern China for 1.665 billion yuan
April 2018	Wumart Holdings	Lotte Mart	Wumart Holdings acquired 87% stake in 21 Lotte Mart stores in Beijing for 1.42 billion yuan
March 2018	Intime Department Store	Kaiyuan Retail	Intime Department Store acquired 100% stake in Kaiyuan Retail for 3.5 billion yuan
February 2018	Tencent, JD.com	Better Life Group	Tencent and JD.com jointly acquired 11% stake in Better Life Group for 1.626 billion yuan
January 2018	Beijing Tourism Group	Beijing Wangfujing Dongan Group Company Limited	Stated-owned Assets Supervision and Administration Commission of Beijing announced to transfer 100% state-owned stake in Beijing Wangfujing Dongan Group Company Limited to Beijing Tourism Group without consideration
January 2018	Yonghui Superstores	Chengdu Hongqi Chain Company Limited	Yonghui Superstores acquired 21% stake in Chengdu Hongqi Chain Company Limited for 1.659 billion yuan, making Yonghui Superstores the second largest shareholder in the target company

Source: Internet sources; compiled by CCAGM

(3) Department store operators move further into direct sales business

Since many department stores in China are operated under the concessionary model – with less than 5% of them adopting direct sales business, many department store operators have limited product procurement and operational capabilities. Moreover, the concessionary model also makes it harder for department store operators to maintain control over brands and catch up with changing market trends and demands.

The drawbacks brought by the concessionary model have prompted more department store operators to engage in direct sales business. However, operators may face some obstacles during the process. For example, enterprises have to ponder whether they have ample capital to withstand the margin pressure and cover additional costs for expanding and nurturing their buying teams; they also need to consider if their partners – brands and distributors are satisfied with the new profit-sharing schemes as well as changes in prices due to the new distribution systems.

Despite the difficulties, some department store operators have been actively exploring ways to strengthen their direct sales businesses. Xinyulou Department Store and Anhui Andeli Department Store are two typical examples of traditional department store chains adopting the self-operated model. Other department store operators that have jumped on the self-operation bandwagon include Parkson Retail Group, which has increased the proportion of its direct sales business to around 20%; Wangfujing Group, which has launched its in-house brand named “Wangfujing Dream Factory”; New World Department Store China, which has launched its private labels under the N+ series; and Hanguang Department Store, which owns most of the cosmetic products sold in the store.

(4) Multi-brand stores diversify product lines

Setting up multi-brand stores has been a key initiative of some traditional department store operators. Developed based on the concept of specialty stores, multi-brand stores feature one product category or a group of related categories of products. For retailers, one of the major advantages of multi-brand stores is their ability to drive foot traffic and attract customers. Gathering an extensive range of products from various brands under one roof, multi-brand stores create curated selections and provide great shopping experience for shoppers. Besides, by making good use of its retail space and improving visual merchandising, multi-brand stores motivate customers to make repeat purchases, thereby maximizing the chance of sales.

Selected examples of multi-brand stores operated by department stores include House Selection by Intime Department Store; G·Beauty by Golden Eagle Department Store; and Parkson Beauty by Parkson Retail Group. Apart from accelerating their expansion into fashion and cosmetic categories, some operators have also made foray into new categories, such as catering, recreation and entertainment, or even jewelry. A typical example is Matro Mall. The department store operator expanded into the jewelry category by opening a multi-brand jewelry store MATRO GBJ in Suzhou in December 2017, and two more stores in Shanghai and Beijing in August 2018.

(5) IP, culture and experience – key to driving consumer engagement

Low foot traffic is one of the challenges facing retailers today. To increase foot traffic and drive customer engagement, some department store operators have added more experiential and service elements, created own IP contents and embraced culture marketing. As a case in point, Wangfujing Group rolled out its in-house creative cultural product brand “Wangfujing Dream Factory” in 2017 after kick-starting its incubation program in 2014. Another department store operator Shanghai No.1 Department Store, which reopened in 2018 after undergoing a facelift for more than a year, has strengthened its cultural elements by introducing four new themes featuring the old city of Shanghai – Great Theatre of China, Wutong (a type of Chinese parasol trees typically located in many Shanghai streets), Longtang (old alleys in Shanghai) and Shanghai Nights (nightlife in Old Shanghai) allowing customers to experience Shanghai in old days. Intime Department Store has worked with China International Cartoon & Animation Festival Exhibition Office to integrate cartoon and animation elements into its outlets. Targeting young consumers, Shanghai New World Daimaru Department Store launched an animation IP exhibition named “EVA EXPO 3.0” in July to August 2018, featuring Japanese anime television series Neon Genesis Evangelion. Other retailers including K11 and SKP have also created unique shopping experience for shoppers by integrating contemporary art and culture exhibitions into their outlets, successfully luring more shoppers to visit their stores.

(6) Technology enables department store operators to upgrade their customer loyalty programs

As the market has gradually become saturated, it is critical for department store operators to gain more new customers and retain existing customers, especially the most loyal customers. Realizing the importance of having an outstanding customer loyalty program, which helps enterprises better engage with their customers and collect customer data to carry out targeted marketing, many department store operators have stepped up efforts in upgrading their membership system by adopting digital technologies.

In 2018, Intime Department Store rolled out a paid membership program, which is the first of its kind in China's department store sector. Backed by digital technologies, the membership program enables the retailer to collect customer data both online and offline. The number of its digital subscribers are expected to reach 5 million soon. Shanghai New World Daimaru Department Store's membership program had over 330,000 subscribers in 2018, contributing up to 56.6% of its total sales. Suning's acquisition of 37 Wanda department stores has also taken its member number to more than 4 million. Better Life Group has announced that in 2019, the company will focus on loyalty marketing, cloud network integration and digitalization of supply chain, aiming for 10 million digital subscribers.

With the adoption of advanced technologies, many department store operators have significantly improved their membership management capabilities. Such digital upgrading enables retailers to optimize their loyalty programs, collect customer data and carry out precise marketing, helping them better understand and serve their customers.

2. Sales performance of key department store operators

The China Commerce Association for General Merchandise (CCAGM) conducted a survey with 90 key department store operators from November 2018 to January 2019 to obtain information on their financial and operating results in 2018. The survey provides a panoramic and representative view of the industry's performance as the majority of surveyed department store operators are leading enterprises in China's department store sector.

According to the survey, total sales revenue of the 90 surveyed department store operators increased 4.2% yoy in 2018 and core operating profits up 5.7% yoy. Total expenses showed a decline of 3.7% yoy. Net profits and year-end net asset value of the sampled department store operators increased by 6.4% yoy and 7.5% yoy respectively. Total operating area of the 90 surveyed department store operators rose slightly by 2.1% yoy, while the average number of employees of the sampled department store operators dropped by 3.1% yoy (Exhibit 3).

Exhibit 3. Operating results of 90 sampled department store operators, 2018

	2018 vs. 2017 YoY changes
Total sales revenue	4.2%
Core operating profits	5.7%
Total expenses	-3.7%
Net profits	6.4%
Year-end net asset value	7.5%
Average number of employees	-3.1%
Operating area	2.1%

Source: CCAGM; compiled by Fung Business Intelligence

As shown in Exhibit 4, 57.8% of the sampled department stores enjoyed positive yoy sales growth in 2018, while 42.2% witnessed a drop in total sales revenue. Among those who registered positive sales growth, 10.0% of surveyed department stores enjoyed exceptional sales growth of more than 20% yoy in 2018.

Exhibit 4. YoY changes in total sales revenue of 90 sampled department store operators, 2018

Positive growth		57.8%
YoY changes in sales revenue	Percentage of total sample	Cumulative percentage
>5%	5.6%	5.6%
>10%	16.7%	22.2%
>20%	10.0%	32.2%
Negative growth		42.2%
YoY changes in sales revenue	Percentage of total sample	Cumulative percentage
<-10%	35.6%	35.6%
>-10%	6.7%	42.3%

Source: CCAGM; compiled by Fung Business Intelligence

In terms of business scale, 88.9% of surveyed enterprises had annual sales revenue of 100 million yuan or above in 2018; among them, 38.9% had annual sales revenue over 1 billion yuan and 10.0% had annual sales revenue in excess of 10 billion yuan (see Exhibit 5).

Exhibit 5. Annual sales revenue of 90 surveyed department store operators, 2018

Annual sales revenue in 2018 (million yuan)	Number of surveyed enterprises	Percentage of total sample	Cumulative percentage
Total	90	100.0%	—
10,001 or above	9	10.0%	10.0%
5,001-10,000	3	3.3%	13.3%
2,001-5,000	10	11.1%	24.4%
1,001-2,000	13	14.4%	38.9%
501-1,000	14	15.6%	54.4%
101-500	31	34.4%	88.9%
100 or below	10	11.1%	100.0%

Source: CCAGM; compiled by Fung Business Intelligence

II. Key innovation and transformation initiatives



1. Omni-channel development deepens; technology as a catalyst for change

(1) O2O integration and digital transformation become mainstream

Nowadays in China's department store sector, O2O integration and digital transformation have become a high priority for many companies. Increasing numbers of department store operators relentlessly leverage leading-edge technologies to pursue O2O integration. This helps department store operators to reinvent their businesses and drive innovations in business model, brand mix, store atmosphere, etc.

According to a recent survey¹ conducted by the CCAGM and Fung Business Intelligence, 84.4% of department store operators cited "pursuing O2O integration" as the most important developmental goal in the next 12 months (Exhibit 6), followed by "strengthening the relationship between consumers, products and consumption scenes" (76.7%), "adding more technology elements" (65.6%) and "implementing digitalization in their businesses" (60.0%), reflecting the operators' eagerness to upgrade their businesses through adopting O2O strategies.

Exhibit 6. Developmental goals of surveyed department store operators in the next 12 months



Source: "Department stores survey 2018-2019". CCAGM and Fung Business Intelligence.

Indeed, some traditional department store operators such as Wangfujing Department Store, Maoye Department Store, Chongqing Department Store and Intime Department Store started e-commerce business some time ago. They either launched their own e-commerce platforms or partnered with e-commerce giants to roll out O2O strategies and digital transformation. In our survey, 59.6% of department store operators have already started their e-commerce business (Exhibit 7). Among them, 72.5% have established self-operated transactional websites, while 9.8% sold solely on third-party e-commerce platforms; 17.7% sold and marketed their products on both third-party e-commerce platforms and their own websites (Exhibit 8).

Exhibit 7. Penetration of e-commerce business among surveyed department store operators



Source: "Department stores survey 2018-2019". CCAGM and Fung Business Intelligence.

¹ A quantitative survey was conducted by the China Commerce Association for Merchandise (CCAGM) and Fung Business Intelligence among 90 key department store operators in China from November 2018 to January 2019.

Exhibit 8. Forms of e-commerce business among surveyed department store operators



Source: "Department stores survey 2018-2019". CCAGM and Fung Business Intelligence.

New World Department Store's self-operated e-commerce platform "Xinshangou" provides a good illustration. The platform was first launched in March 2018 with the hope to bring new experiences and better meet the ever-changing consumer needs. Consumers in Beijing could place orders on the e-commerce platform; the goods would be delivered by SF Express through direct mail. After a half-year exploration and testing, an upgraded version of Xinshangou was re-launched on WeChat in September 2018. The upgraded platform only allows customers to order online and pick up the products at various branches of New World Department Store, aiming to bring online shoppers to the department stores and drive sales, and vice versa. At present, the number of new members grows at 20% per month, and total sales increase by 50% monthly.

At the same time, some department store operators also deploy digital technologies across the whole supply chain from product procurement and production to inventory management and sales to membership management. Their aim is to enable seamless flow of data across the supply chain. Liqun Group is one of the pioneers to carry out digital transformation across the whole supply chain. Ever since its establishment in 1998, Liqun has set up its own computer center and self-developed business intelligence and information system to handle operational data, including SKU management, auditing, POS system and parcel delivery system. At the same time, Liqun has developed an invoicing management system to better control and manage product pricing, inventory, cost and sales; a smart analytic tool to analyze product sales and inventory data, and aid the decision-making process; and a digitalized membership system to send customized promotions and messages to its members. In 2018, Liqun created an integrated, smart supply chain information management platform which fully connects the POS, wholesale, logistics, as well as financial sharing center and OA office system.

(2) Partnering with leading Internet companies and e-commerce players to implement digital transformation

Increasing numbers of department store operators have realized that forming strategic collaboration with Internet companies or large-scale e-commerce players is a fast track to achieving O2O integration, through leveraging their huge traffic flows, big data as well as logistics capabilities.

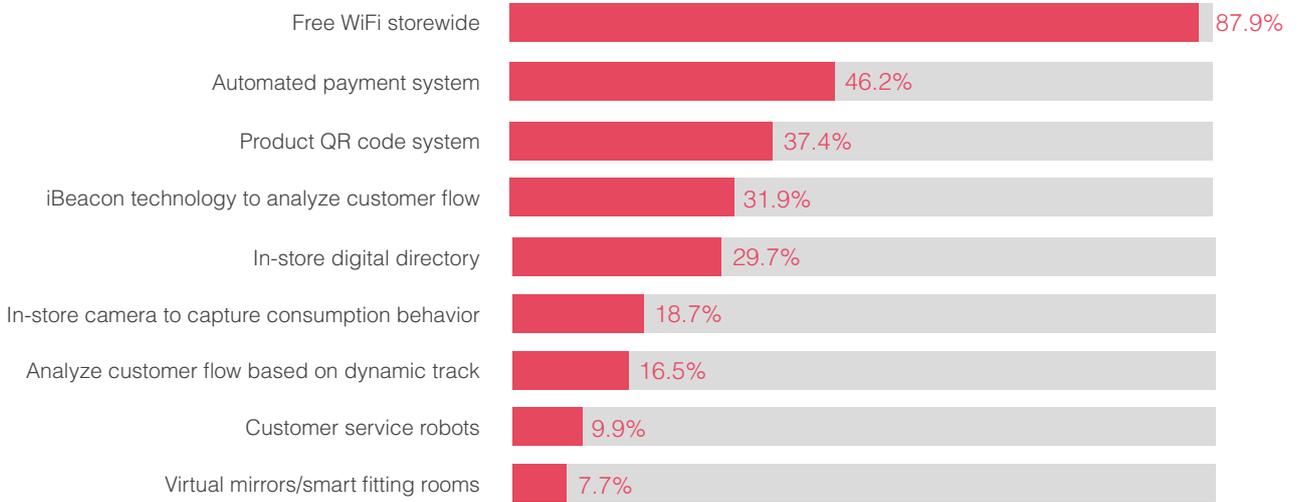
The strategic partnership between Intime Department Store and Alibaba is a case in point. Starting from 2013, the two companies have worked together on a number of O2O initiatives, including the introduction of Tao-brands to Intime's physical stores, the launch of Intime's first online supermarket on Tmall Supermarket (chaoshi.tmall.com), and the adoption of Alibaba's one-stop shopping and location-based mobile app "Miao Street" in all Intime physical stores. Later in 2017, Alibaba Group officially privatized Intime Retail Group. Upon completion of the deal, Alibaba became the controlling shareholder of Intime and took over Intime's physical networks across the country, including 29 department stores and 17 shopping malls. The successful privatization of Intime signifies Intime's determination to implement O2O strategies, and ride on Alibaba's resources and support to fully integrate its online and offline businesses.

Rainbow Department Store's determined efforts to push forward O2O integration has also drawn huge attention nationwide. As early as 2013, Rainbow has put huge emphasis on the seamless integration of its online and offline channels, and data sharing across marketing, inventory planning, payment and logistics systems. To further its digitalization push, Rainbow teamed up with Tencent to explore smart technology applications such as order-placing via WeChat Mini Program and smart car parking function on WeChat Mini Program. As of June 2018, Rainbow had more than 6 million WeChat members, 370,000 members on WeChat Mini Program and more than 7.5 million Red Scarf members; over 80 million members reportedly had exchanged information or made a purchase through Red Scarf, and the proportion of transaction done through tablets in the department store's counters has reached 91.9%.

(3) Adopting leading-edge technologies to enhance customer experience

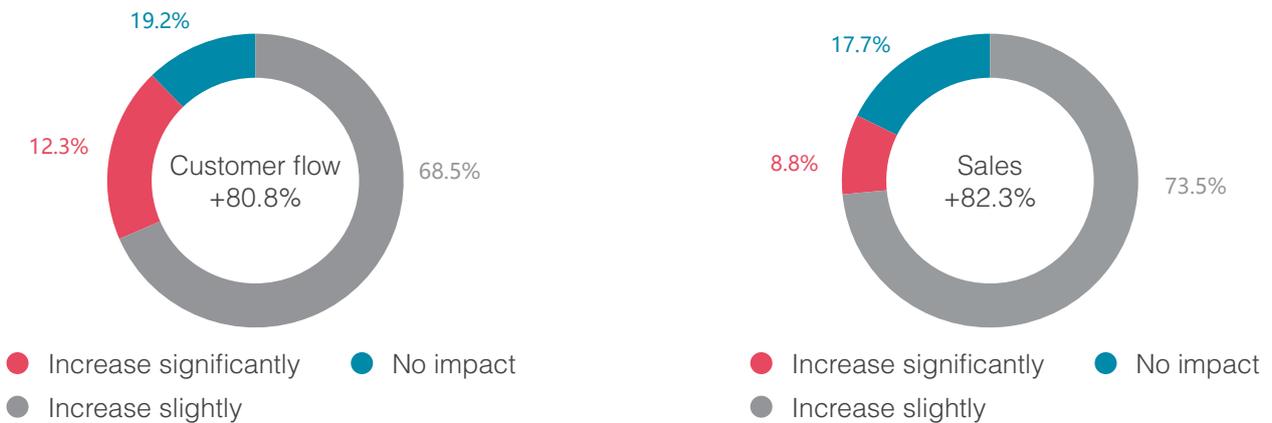
Currently, the adoption of breakthrough technologies such as artificial intelligence (AI), the Internet of Things (IoT), Global Positioning System, 5G technology, augmented reality (AR)/ virtual reality (VR) and blockchain technology in retailers' transformation journey has gathered pace. Many department store operators utilize these advanced technologies in-store to enhance shopping experience and better engage with customers. Among the department store operators in our survey who have applied technologies in their physical stores, 87.9% have set up free WiFi storewide, 46.2% have launched automated payment system, 37.4% have set up QR code system, and 31.9% have leveraged iBeacon to analyze customer flow (Exhibit 9). When asked about the benefits of adopting technologies in their stores, 12.3% and 68.5% of surveyed operators claimed to see either significant increase or slight increase in customer traffic respectively after adding technological elements in-store; over 82% of surveyed operators claimed to see an increase in sales after introducing technological elements in-store (Exhibit 10). Meanwhile, over 78% of surveyed department store operators said that they plan to add more technology elements in-store in the coming 12 months (Exhibit 11).

Exhibit 9. Adoption of technologies in physical stores of surveyed department store operators



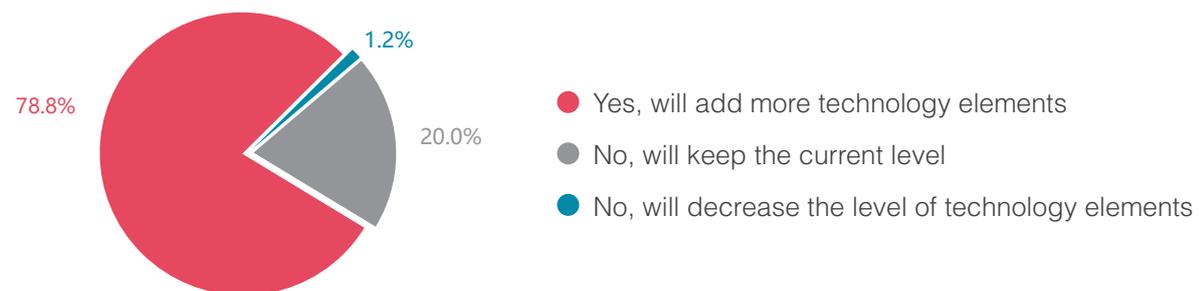
Source: "Department store survey 2018-2019". CCAGM and Fung Business Intelligence.

Exhibit 10. Impact of adding technology elements in-store among surveyed department store operators



Source: "Department store survey 2018-2019". CCAGM and Fung Business Intelligence.

Exhibit 11. Likelihood of adding technology elements in-store among surveyed department store operators



Source: "Department store survey 2018-2019". CCAGM and Fung Business Intelligence.

New World Department Store is one of the pioneers in the sector to adopt technologies in their stores. One of the company's major initiatives is to re-position its New World Department Store Shanghai Huaihai branch as a Smart Mall by embracing innovations to attract young customers. It has partnered with Koubei, Alibaba's local services platform, to set up an automated cash register system with facial recognition function in-store; more than 15% of the transaction were reportedly completed through the system after its launch in October 2018.

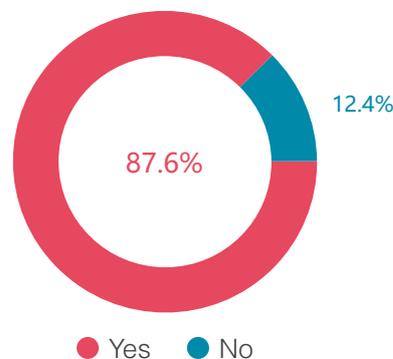
Another department store Hi Department Store has collaborated with Smart Code, a provider of smart store solutions, to launch Hi-Smart Unmanned Department Store – the first unmanned department store – in April 2018. Located inside Hi Department Store in Grandview Mall in Guangzhou, Hi-Smart positions itself as an offline version of Tmall; it allows customers to scan product QR code to place orders and pay, learn more about product information and contact online customer service representative for enquiries.

(4) More customer-focused – accelerating digitalization and implement targeted marketing strategies

These days, department store operators not only use technologies to revamp consumption scenes and enrich shopping experience, but also deploy digitalization to carry out targeted marketing strategies. Many operators use big data analytics and other algorithms to better predict and understand customers' needs, review and fine-tune product portfolio and provide personalized products and services.

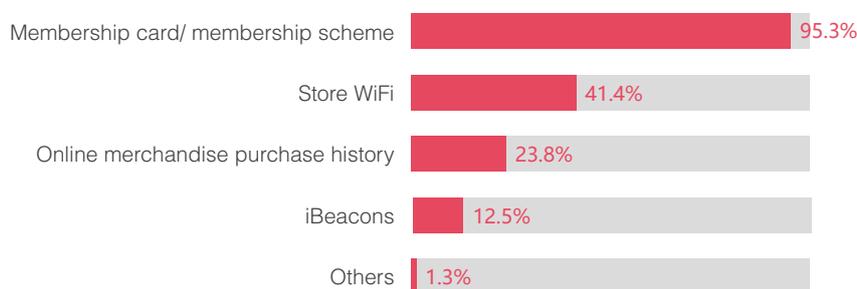
Our survey shows that over 87% of surveyed department store operators have collected consumer data and carried out big data analysis (Exhibit 12). Among them, 95.3% of surveyed department store enterprises have gathered consumer data through membership card/ membership scheme, 41.4% through store WiFi, 23.8% through online merchandise purchase history, 12.5% through iBeacons (Exhibit 13). The collected consumer data were mainly used to carry out precision marketing (89.0%), understand consumer preferences (85.3%), provide customers with more personalized products/services (76.5%), optimize in-store merchandise mix (66.5%) and new product development (11.3%) (Exhibit 14).

Exhibit 12. Proportion of surveyed department store operators that have collected consumer data and carried out big data analysis



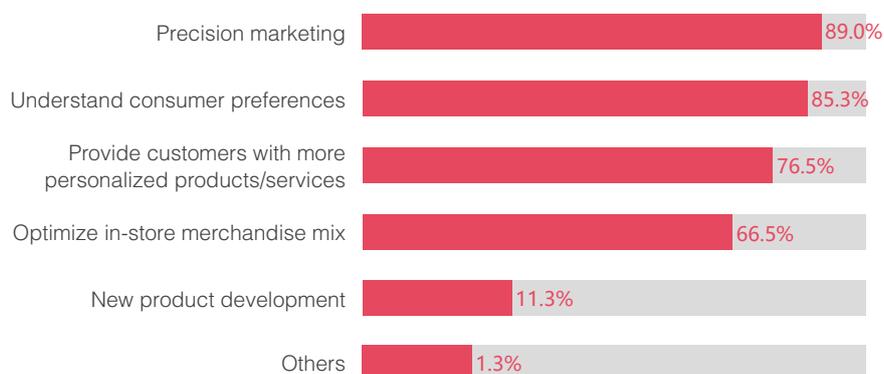
Source: "Department store survey 2018-2019". CCAGM and Fung Business Intelligence.

Exhibit 13. Means of collecting customer data by surveyed department store operators



Source: "Department stores survey 2018-2019". CCAGM and Fung Business Intelligence.

Exhibit 14. Major purposes of collecting consumer data of surveyed department store operators



Source: "Department stores survey 2018-2019". CCAGM and Fung Business Intelligence.

By leveraging Alibaba’s advanced technologies and digital strengths, Intime Department Store has carried out digital transformation on its membership system, product assortment and consumption scenes over recent years. Through integrating its membership system with Alibaba’s membership system, Intime leverages Alibaba’s consumer analytics collected from Taobao and Tmall to select the best-selling products. It also makes use of its location-based Miao Street app to draw shoppers to nearby Intime store. Similarly, it collaborates with Cainiao and Ele.me to entice users living within 1km from the Intime store to visit the store. As of September 2018, Intime has over 5 million digitalized members, product digitization rate reached 58%; its same-store sales growth was 18% yoy, which is the highest growth over the past ten years.

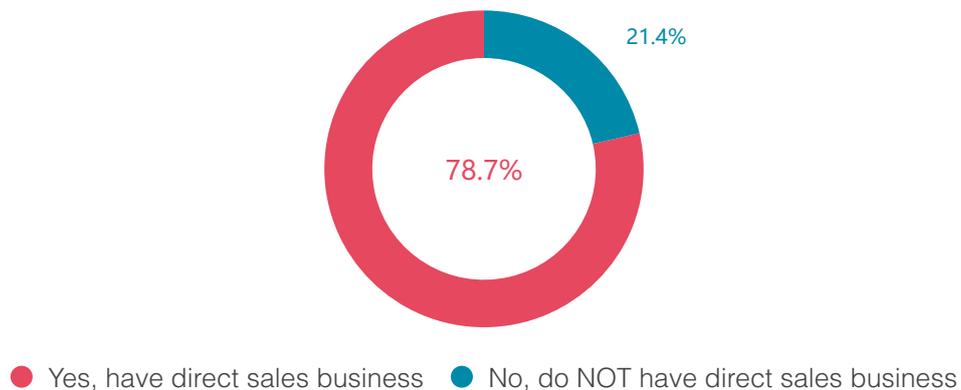
Changchun Eurasia Group is another case in point. Eurasia Group rolled out its first digitalization project as early as 2015, hoping to have better understanding of its customers through the application of big data analytics. Thereafter, the Group has launched a new smart information platform to help the company make better business decisions. The new system integrates all the sales, inventory, product categories and membership data and carries out real-time data enquiries and ad-hoc analysis based on the data available. Data set will be updated every ten minutes so that Eurasia Group can obtain the most up-to-date information, including sales data, customers’ purchase records, inventory data and other financial information. This greatly assists the management to make accurate business decisions and enhance operational efficiencies – Eurasia Group reportedly recorded profit growth for two consecutive years through leveraging the data in the system for product portfolio adjustment.

2. Strengthening direct sales business to enhance brand equity and increase profits

Recognizing the drawbacks of the concessionary model, many department store operators have expanded their direct sales businesses through increasing the scale of direct product procurement, launching self-operated buyer/multi-brand stores and actively developing private labels. They hope to establish unique positioning and brand image, while offering differentiated products and better shopping experience for customers.

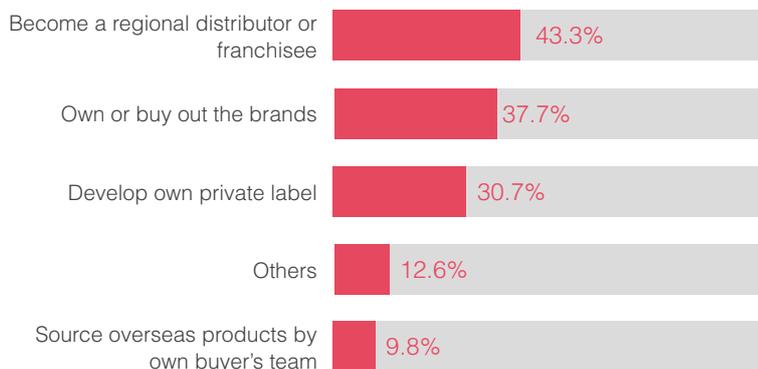
According to our survey, over 78% of department store operators have engaged in direct sales business (Exhibit 15). Among which, 43.3% are the master distributors or regional distributors, 37.7% own the brands through buying-out the brands, 30.7% launch their own private labels and 9.8% source the products overseas through their buyer's team (Exhibit 16). That said, the scale of their direct sales businesses remained small; over half of the surveyed department store operators stated that the proportion of direct sales in their business was less than 10% (Exhibit 17). When asked about their intention to expand their direct sales businesses, over 46% of surveyed department store operators cited that they plan to increase the proportion of direct sales business in the next 12 months (Exhibit 18).

Exhibit 15. Penetration of direct sales business among surveyed department store operators



Source: "Department stores survey 2018-19". CCAGM and Fung Business Intelligence.

Exhibit 16. Types of direct sales model adopted by surveyed department store operators



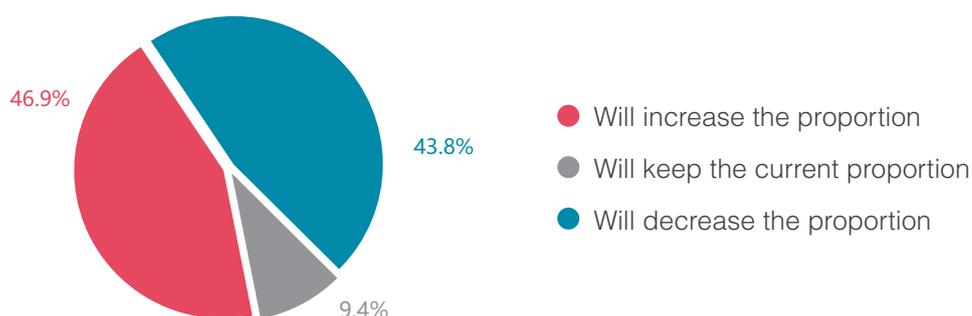
Source: "Department stores survey 2018-19". CCAGM and Fung Business Intelligence.

Exhibit 17. Proportion of direct sales business of surveyed department store operators

Proportion of direct sales business	Among operators with direct sales business...
≤ 5.0%	41.7%
5.1% - 10.0%	15.0%
10.1% - 15.0%	8.3%
15.1% - 20.0%	11.7%
≥ 20.1%	23.3%

Source: "Department stores survey 2018-2019". CCAGM and Fung Business Intelligence.

Exhibit 18. Percentage of surveyed department store operators that have plans to increase the proportion of direct sales business in the next 12 months



Source: "Department stores survey 2018-2019". CCAGM and Fung Business Intelligence.

(1) Setting up multi-brand stores to offer differentiated goods and services

In recent years, some department store operators have created their own multi-brand stores in the hope of enhancing uniqueness and providing better shopping experience for customers. As an example, in December 2018, Wangfujing Group opened a new multi-brand lifestyle store "ShangFu" in Wangfujing Department Store in Beijing. With an operating area of around 60 sqm, ShangFu offers household products, daily necessities, apparel, and fashion accessories. It features a large variety of unique and stylish international brands, exclusive product lines and imported European niche brands. ShangFu also houses Wangfujing's newly developed private label "Jingpin", which currently covers home products and basic apparel items. The store is designed in a way to provide a cozy ambience and enable customers to shop in a comfortable atmosphere. Wangfujing expects to open more ShangFu stores in its department stores in other cities in 2019. Going forward, Wangfujing will continue to expand its direct sales and private label businesses through obtaining distributorship rights of more overseas brands, exploring global sourcing opportunities, developing more private labels and setting up more multi-brand stores.



Wangfujing Group's new multi-brand lifestyle store "ShangFu" at its Beijing outlet
Photo source: Fung Business Intelligence

Earlier in May 2018, Parkson Retail Group launched its first standalone specialty concept store "Parkson Beauty" in Changsha IFS. With an area of over 5,000 sqm, the store houses top international cosmetics and skin care products, body care products and fragrances; it also offers customized makeup and skincare consultation services for customers. Meanwhile, Parkson's newly launched multi-brand store "Play Up" also opened at Parkson Beauty. Targeting mainly the younger millennials and Generation Z (post-95s and post-00s generations), Play Up offers a large array of popular online products launched by fashion and trendy KOLs, with more than 70 brands and 1,300 types of popular products.



Parkson Beauty at Changsha IFS
Photo source: Jiemian

Another example is MATRO Mall, which opened MATRO GBJ (Global Boutique Jewelry), a jewelry multi-brand store in Suzhou at the end of 2017. The store is also China's first jewelry multi-brand store that brings together over 15 boutique jewelry and well-known designer brands from countries including the U.S., Italy, Britain, Germany, France and Australia. After opening its first store in Suzhou, MATRO Mall opened two more stores in Shanghai and Beijing in 2018. MATRO GBJ plans to open a total of 30 stores in high-end shopping malls in major cities across the country in 2019, and introduce MATRO GBJ exhibition halls for fine jewelry and MATRO GBJ exhibition halls for affordable jewelry in different regions, depending on market sentiments and consumer demand.

(2) Actively developing private labels

In today's new consumption era, consumers increasingly demand better quality and yet value-for-money products and services. Some department store operators have stepped up efforts to launch their own private labels to better meet the new needs of consumers, while increasing margins and profits.

In our survey, over 30% of surveyed department store operators have launched their own private labels (Exhibit 19). Among which, over 57% of department store operators said they have increased the proportion of private labels in the past year (Exhibit 20). As shown in Exhibit 21, most of the surveyed department store operators launched private label brands in food & beverages (26.5%), apparel (23.8%) and home products (15.4%).

Exhibit 19. Proportion of surveyed department store operators that have launched their own private labels

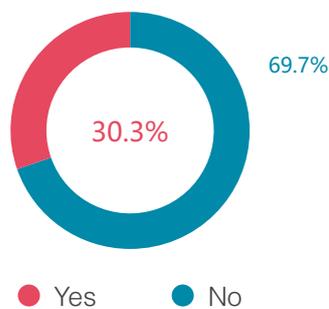
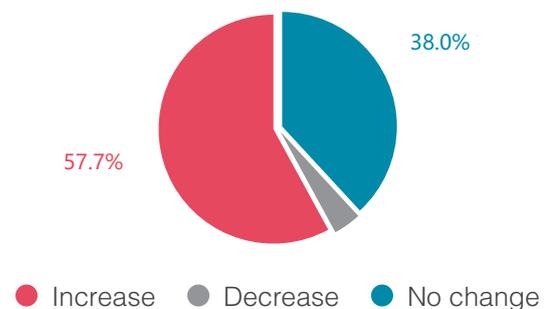
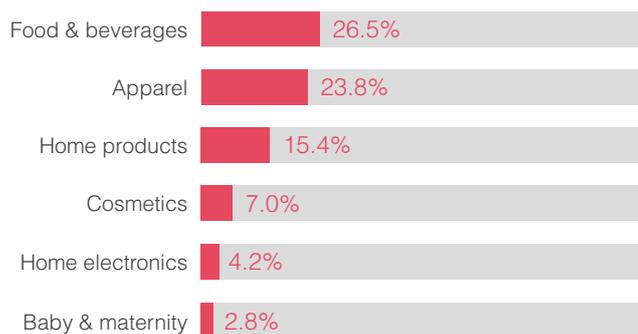


Exhibit 20. Percentage of surveyed department store operators that have increased the proportion of private labels in the past year



Source: "Department stores survey 2018-2019". CCAGM and Fung Business Intelligence.

Exhibit 21. Major private label product categories of surveyed department store operators



Source: "Department stores survey 2018-2019". CCAGM and Fung Business Intelligence.

Leading regional department store operator Xinyulou Department Store is one of the earliest players to adopt the direct sales model. To address consumers' growing demand for quality products, Xinyulou has stepped up efforts to launch its own private labels and started to engage in global sourcing. Currently, Xinyulou has 17 private label brands in various product categories including food products, general merchandise, jewelry, menswear and womenswear; it also sells a few hundreds types of customized products that are sourced directly from manufacturers as well as nearly 100 imported brands in food and personal care product categories.

Other traditional department store operators have also put stronger efforts in developing private labels. An example is Golden Eagle Retail Group. To meet middle class consumers' demand for high quality lifestyle, Golden Eagle has continued to expand its G.LIFE series – in 2018, it added a total of 11 G.LIFE stores including four G.MART premium supermarkets, three G.TAKAYA lifestyle bookstore, three G.BEAUTY beauty and skin care stores and one pet care center G.PET. At the same time, Golden Eagle also partnered with key fabric providers in China to develop a series of “premium quality single item merchandise” under five own brands, namely Aquila Doro, IVREA, RESTYLE, Wonderful Life and LISALEN, in an effort to provide value-for-money merchandise to its customers.

New World Department Store has also proactively expanded its private label business in recent years. It has expanded its multi-category private label series N+ and LOL (Love • Original • Life) Concept Shop (“LOL”) to diversify the composition in direct sales business. To date, there are four private labels in the N+ series, including high-end bakery brand “N+ Natural Taste Plus” (launched in 2016), mother-and-baby themed supermarket “N+ Baby” (launched in 2017), convenience store “N+ Convenience Store” and the newly created “N+ Quality Goods” (launched in 2018) which offers a variety of household goods, cosmetics and beauty products, gifts, snacks, cell phone accessories, etc. At the same time, New World has categorized its LOL Concept Shop into three different store types according to the needs of different consumer groups and further enriched its categories by introducing trendy products that fit the different positioning of the stores. As of 30 June 2018, there were 20 LOL stores across the country.

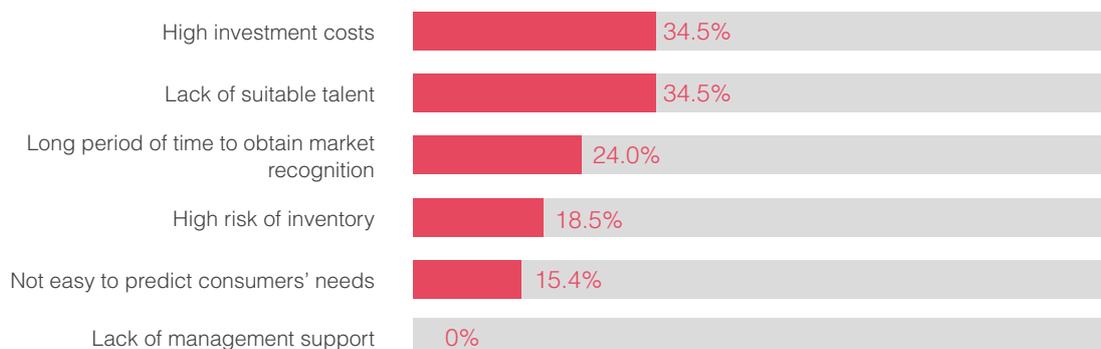


N+ Quality Goods Shop at Beijing New World Department Store

Photo source: Fung Business Intelligence

Nonetheless, many operators are still not yet ready to develop their own private brands. As shown in Exhibit 22, 34.5% of surveyed department store operators cited high investment costs and lack of suitable talent as the major challenges of launching private labels, followed by fairly long period of time to obtain market recognition.

Exhibit 22. Major challenges encountered by surveyed department stores when developing private labels



Source: “Department stores survey 2018-2019”. CCAGM and Fung Business Intelligence.

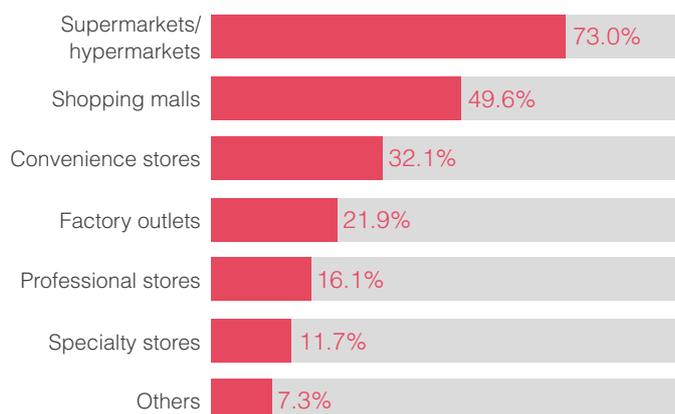
3. Introducing innovative business models and diversifying retail formats

(1) Actively expanding business scope and engaging in multi-format operation

In recent years, the consumption upgrading trend, rising operational costs and the threat of e-commerce have imposed considerable pressure on department store operators. To stay competitive, many operators have branched out into different retailing businesses and engaged in multi-format operation. This not only enables them to better meet the diversified needs of consumers, but also increase revenue streams.

As reflected in our survey, over 75% of surveyed department store operators have tapped into other retail formats; the majority of operators (73.0%) have ventured into the supermarket/hypermarket format (73.0%) and shopping mall format (49.6%) (Exhibit 23).

Exhibit 23. Other retail formats surveyed department store operators have ventured into



Source: "Department stores survey 2018-2019".
CCAGM and Fung Business Intelligence.

To stay competitive in the market, some traditional department store operators have expanded their business scope and tapped into other business sectors. Parkson Group is a case in point. The Group has been proactively diversifying its businesses over recent years. It set up its first shopping mall, Lion Mall, in Qingdao back in 2016 and joined hands with Korea's E.Land Group to open Parkson Newcore Citymall in Shanghai and Nanchang. In the same year, Parkson also launched a boutique supermarket, Parkson Supermarket and a flagship bakery store, Hogan Bakery in Shanghai. In May 2018, Parkson launched a beauty concept store, Parkson Beauty in Changsha to expand its business scope. In November 2018, it's renovated and upgraded mall, Parkson Young Mall, was opened in Chongqing to provide an all-in-one experience to young consumers.

Another example is Ito Yokado, which launched its first lifestyle grocery store in Chengdu in November 2018. The store offers good quality grocery products, targeting middle-class families who live within 1 km from the store. The store also houses a kitchen and an area for cooking demonstration.



Ito Yokado's lifestyle grocery store at Chengdu
Photo source: Linkshop

Traditional department store operator Bailian Group has also been eager to engage in different retail formats. In January 2018, Bailian Group's Oriental Department Store (Wujiaochang branch) was transformed into an urban outlet under the new name of UMAX. It is Bailian's first urban outlet project. UMAX has added some new restaurants as well as culture and entertainment activities; it has also enhanced payment and checkout experience by enabling merchants to settle payment via iPad in their store, and there is only one cash register on each floor to handle cash transactions.



UMAX, urban outlet of Bailian Group
Photo source: iFeng.com

Currently, many operators have already tapped into other retail formats. But when asked about their intention to further expand into other businesses in the next 12 months, only about one-third of the surveyed department store operators have such intention. This is due in part to the economic uncertainty, making the operators more cautious when making investment decisions.

(2) Exploring new business models and innovative retail concepts

Transformation remains one of the most important themes in the retail sector. In response to the consumption upgrading trend, together with the new needs of consumers, increasing numbers of department store operators have reinvented their businesses by exploring new business models and introducing new retail concepts.

A typical example is Rainbow Department Store, which has actively carried out business innovation and transformation over recent years. Apart from engaging in digital transformation and multi-format operation, Rainbow has also introduced new retail concept to the market. In January 2019, Rainbow opened the company's first catering business "Hong Shi Hui" experiential restaurant in its supermarket at Rainbow Department Store's Guomao branch in Shenzhen. With a floor area of around 260 sqm, the restaurant focuses on providing new dining experience for customers; customers can buy fresh ingredients from Rainbow supermarket and have them cooked by the chefs of Hong Shi Hui. They can also try out the smart cooking facilities such as "robot chef" and join the cooking lessons offered by the restaurant. Furthermore, Rainbow also rolled out a new group-buying services in February 2019 which enables consumers to take part in the group-buying services via Rainbow's WeChat Mini Program. Consumers can choose the products they want to buy and either initiate a new group or join any existing group; they can then choose to pick up the products at any Rainbow stores once the group-buying deal is activated. Products available for group-buying include cosmetics products, fresh produce, wine, snacks, and more. Currently, each store offers 6-8 SKUs and the variety of goods differ from store to store. The group-buying services are now available in 16 Rainbow stores across the country.

Meanwhile, some department store operators such as Bailian Group, Changchun Eurasia Group and Ito Yokado have started to roll out on-demand delivery services to cater to consumers' growing needs for convenience and immediacy. Instead of setting up their own delivery fleets or additional warehousing facilities which involve high investment costs, some department store players choose to team up with third-party O2O local lifestyle service platforms such as JD Daojia, Ele.me and Meituan-Dianping.

4. Experiential consumption becomes a focal point of transformation

To adapt to the changing lifestyle habits of consumers, particularly the younger millennials and Generation Z (post-95s and post-00s), and greater demand for experiential shopping, many department store operators are endeavoring to provide more experiential elements such as family and child-related services and shops, art and culture exhibitions, dining, entertainment, IP/content-driven ACG (animation, comic, games) subculture and technology elements. Through introducing different types of experiential elements, department store players hope to create fresh and upgraded experience that can better appeal to customers.

Examples of experiential elements introduced by selected department stores are shown in Exhibit 24.

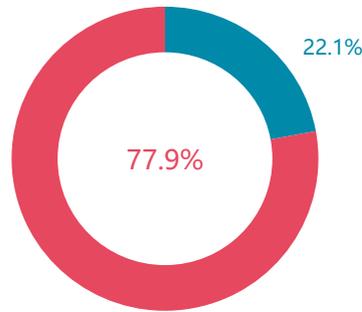
Exhibit 24. Examples of experiential elements introduced by selected department stores in 2018

Department store	Experiential elements/shopping experience enhancement
New World Department Store – Shanghai Huaihai branch	<ul style="list-style-type: none"> Introduced Internet KOL brands, art and technology elements to appeal to young consumers. Transformed and renovated the third level based on the concept of the Louvre Museum to enrich in-store ambience; created a stage-like retail space with virtual stores, display section and seating area as well as a 3D artistic wall for customers to take pictures. Launched a smart fitting room which enables customers to virtually try on the clothes, place order via the app and enjoy delivery services.
Shanghai New World Damairu Department Store	<ul style="list-style-type: none"> Hosted the “EVA EXPO 3.0”, China’s first exhibition featuring animation and comic artworks of Japanese anime series Neon Genesis Evangelion from 13 July to 19 August 2018. Joined force with Geely Automobile Holding Ltd. to launch a car-themed exhibition for kids on the seventh level, offering 16 fun, experiential and interactive activities for kids to play and learn about cars, auto mechanic, road safety, etc. The exhibition was held from 15 December 2018 to 3 March 2019.
New World Department Store – Beijing Wangjing branch	<ul style="list-style-type: none"> Created a thematic street zone “N+Kids” featuring IP/content-driven animation, comic and games. With an area of around 1,190 sqm, the zone has a “black technology” interactive area, a retail area selling family and child-related products, a game and reading area, etc. Set up a WeChat Mini Program specifically for N+Kids, providing a channel for customers to shop anytime, anywhere; customers can pick up the orders in-store or opt for delivery services.
Grandbuy Department Store	<ul style="list-style-type: none"> Set up a multi-brand store “G-baby” in its Beijing Road branch in Guangzhou in June 2018, offering imported maternity, baby & kids products and accessories, baby food, diapers, baby formula, etc. It also offers various fun, interactive activities and classes for moms and moms-to-be.

Source: Various Internet sources; compiled by Fung Business Intelligence

The relentless efforts of department store operators to enhance the shopping experience of customers have been manifested in our survey. Over 77% of surveyed department store operators have added experiential elements in their stores (Exhibit 25). Around 27% of the operators stated that the total area allocated for experiential shopping accounted for 11%-20% of the total store area; and nearly 40% said the total area allocated for experiential shopping accounted for less than 10% of the total area (Exhibit 26).

Exhibit 25. Proportion of surveyed department store operators that have added experiential elements in stores



● Yes, added experiential elements in-store ● No, did NOT add any experiential elements in-store

Source: "Department stores survey 2018-2019". CCAGM and Fung Business Intelligence.

Exhibit 25. Proportion of surveyed department store operators that have added experiential elements in stores

In-store experiential elements as a percentage of total store area	Among operators with merchandise direct sales...
<10%	39.66%
11%-20%	27.59%
21%-30%	18.97%
31%-40%	6.90%
41%+	0%

Source: "Department stores survey 2018-2019". CCAGM and Fung Business Intelligence.

III. Major issues and challenges



China's department store sector has witnessed a positive rebound with some signs of stable recovery over the past year. Nonetheless, being a relatively traditional retail format, it still faces some hurdles and challenges.

1. Bottlenecks to transformation

To stay competitive in the ever-changing retail environment, it is crucial for retailers to transform and reinvent their businesses. Indeed, many department store operators have already taken bold initiatives to expand their direct sales businesses and develop private labels to enhance product and services uniqueness. For those operators that have yet to start their transformation and upgrading journey, many have reflected that they face some bottlenecks when looking to transform their businesses. For instance, the limited scale of some department stores has made it uneconomic to add more experiential elements and facilities. Furthermore, the existing physical settings of the department stores have made it difficult and costly to carry out store revamp; in particular, it is hard to add more capacity for water, gas and electricity. To stay relevant in the market, these operators need to step up efforts to enrich merchandise and service portfolios, and improve product display and spatial planning.

2. Rising cost pressures weigh on department store operators

Apart from the rising rental and labor costs facing all retailers in China, department store operators need to face some additional costs such as the extra costs of renovating and upgrading existing stores, interior design fees, extra IP marketing costs and the costs of adopting new technologies in business operations, including the collection of consumer data, adoption of big data analytics and deployment of sales and marketing tools.

3. High product prices affect overall competitiveness

Currently, most of the products sold in department stores in China are obtained via the traditional distribution model, i.e. via several layers of distributors and agents, resulting in exceptionally high retail prices. This makes the products sold in department stores less competitive, particularly in terms of pricing; the problem has become more acute amid the growing threat of e-commerce players. Department store operators which could reap better profit margins are those eager to differentiate product and service offerings, place stronger efforts in expanding direct sales business and maintain the same prices for both online and offline consumers.

4. An urge to enhance core competencies, yet changes do not happen overnight

One of the imminent needs of department store operators is to build their capabilities in engaging in direct sales businesses. This involves substantial investments, be it capital investments, recruitment of in-house buyers or creation of employee incentive schemes. In addition, successful transformation initiatives also require the development of a mature and integrated supply chain as well as the creation of a trust mechanism in the society. However, these are not simple tasks and cannot be done overnight.

IV. Development trends and directions



1. China's department store sector to sustain steady growth

China's department store sector is set to maintain an overall stable growth in 2019 with the continuation of the consumption upgrading trend as well as the government's determined efforts to boost consumption. Over the years, the government has adopted a series of measures to cut import tariffs and boost imports; this enables department stores to increase the variety of products available while lowering the price of merchandise. In addition, the *E-Commerce Law of the PRC* establishes requirements for e-commerce platforms to be more accountable for merchants including "daigou" agents selling on their platforms; this could better regulate the "daigou" industry and minimize reseller activities, thereby bringing part of the overseas high-end consumption back to China.

2. Digitalization becomes a priority

For many department store operators, O2O integration has and will continue to be at the forefront of development. The pursuit of O2O strategies goes hand in hand with advanced technologies and digital tools deployment. More operators now leverage various breakthrough technologies to optimize their operations and ensure seamless connection between the three core business elements, namely customers, products and physical settings.

At the same time, many department store operators have actively pursued digital expansion by setting up their own app, WeChat Official account, WeChat Mini Program, etc., in addition to their own website. Going forward, it is expected that more department store operators will venture into social-commerce.

3. M&A activities remain rampant

China's retail sector is relatively fragmented compared to developed countries such as the U.S., Japan and other European countries; there is still ample of room for market consolidation. In 2018, the department store sector witnessed robust M&A activities; the trend is set to continue into 2019 and beyond. On the one hand, as China's department store sector has become increasingly saturated, M&A is an effective way to integrate resources of companies and enable acquiring companies to expand their scale and increase market share. On the other hand, M&A also provides a viable option for underperforming or financially struggling companies to overcome their financial problems.

4. Regionally-based department stores continue strong growth momentum

In recent years, some region focused department store operators have registered steady income growth, driven in part by their strong efforts in providing customized and comprehensive services for shoppers. Additionally, some of them have launched effective employee incentive programs to enhance individual and team performance and promote operational efficiencies. Moreover, the flexible operational style of some regional department stores has also enabled them to better adapt to changes and create a strong image among consumers.

One added advantage of regional department store operators is that they are more likely to secure the best store location, often right in the heart of key business districts. This is key to attracting customers and increasing store traffic.

5. Greater blurring of the lines between department stores and shopping malls

With department stores adding more experiential elements in-store and shopping malls striving to enhance brand management and adopt unified payment, the lines between large-scale department stores and urban shopping malls blur further. Moving forward, the growing needs to provide better products and services to consumers and enhance competitiveness will continue to contribute to the blurring boundaries, or deepened integration of department stores and shopping malls.

V. Implications and recommendations



1. Department store remains a major distribution channel

(1) Playing a big part in consumption upgrading

Despite facing increasing challenges from e-commerce players, department store is still one of the major and most influential distribution channels in China, as well as an indispensable part of consumers' lives. In recent years, many department stores have continued to upgrade themselves by enhancing product and service uniqueness and improving shopping experience. This helps drive the ongoing consumption upgrading trend in the country.

(2) Facilitating the service consumption boom

In China, most department stores are situated in relatively good and easily accessible locations, encouraging customers to visit and spend more at their stores. Moreover, an increasing number of department stores have undergone makeover to bring in more experiential elements – F&B, kids-related facilities, lifestyle services and entertainment, offering customers a convenient one-stop destination for shopping, dining, entertainment and networking. This contributes significantly to the fast development of service consumption in the country.

(3) Being major city landmarks

Department stores such as Beijing Wangfujing Department Store, Shanghai No.1 Department Store and Hangzhou Wulin Square have long been regarded as major landmarks in local cities. In recent years, every city in China has been keen to add more commercial facilities such as commercial centers and shopping malls in urban areas. Nevertheless, those department stores located in key urban districts are still irreplaceable given their great locations and renowned branding. Some department stores have even become famous tourist attractions and shopping destinations after completing store renovations.

(4) Serving as integrated platforms for community-based businesses

Community-based businesses play a significant part in urban commercial development. However, as community-based businesses are mainly small businesses with scattered distribution networks, many of them have difficulties in finding affordable retail space to grow their businesses. To support these community-based businesses, small and medium-sized department stores can serve as integrated platforms assigning retail spaces for community-based businesses and providing them relevant marketing and financing resources. As a case in point, Beijing Chang'an Mall has been closed recently for a major revamp, a move to reinvent itself around a more community-centered model by adding community-based services and turn itself into a hub for the local community where shoppers can share quality time with family and friends.

2. Implications for department store operators

(1) There is always room for improvement

Despite buffeted by continuing headwinds in recent years, the department store sector is more resilient to risks compared with other retail formats, thanks to its asset-light business model and relatively low inventory level. After going through a series of significant reforms and transformation initiatives, the department store sector finally showed some signs of bottoming out in 2018, with a number of department stores posting robust sales growth. Even with the strong rebound, the sector still has ample room for improvement in different areas, including product management, employee incentives, store layout and customer services, among others.

(2) Modernize management practices to keep pace with the evolving market

In China, department store is one of the most significant distribution channels with a long-standing history among other retail formats. Moreover, many department store operators are state-owned companies. To keep pace with the industry trends, department store operators should continue to reinvent themselves, not only in business operations but also in management practices. Since there is no “one-size-fits-all” approach and some of the traditional management practices may become obsolete, it is essential for department store operators to modernize their leadership and management approach to keep up with the market need. For example, some department store operators have offered various incentive programs to motivate their buying teams when strengthening their direct sales businesses.

(3) Transformation requires a multi-pronged approach

Transformation has been one of the hottest topics of discussion in the department store sector. Successful transformation requires a multi-pronged approach and cannot be achieved by simply upgrading store design and layout, visual merchandising, brand portfolio, service enhancement, etc., but also through refining organizational ideology and structure. This is especially true in the digital era which has driven radical changes in the way businesses operate.

(4) Digitalization reshaping every aspect of a business

Nowadays, digital technology has become an indispensable tool for retailers to seamlessly connect their customers, products and physical settings. In short, digitalization is reshaping every aspect of a business. It presents an opportunity for operators to enhance customers' in-store shopping experience during their purchasing journey, from selecting products, trying on and testing products, making payments to after-sales services, etc. It also facilitates product management, including inventory, settlement and pricing managements, among others. Going digital in physical settings enables operators to improve in-store display and visual merchandising, while encouraging more customer engagement. When it comes to omni-channel retailing, digitalization also plays an important part in connecting shoppers to both digital and in-store shopping, making O2O integration not as complicated as it sounds.

Conclusions

China's department store sector has gone through some ups and downs in the last decade. The lackluster performance since 2010 was due in part to the problems associated with the operation model and management level of the department store operators, as well as the slowing retail market and changing economic conditions. Over recent years, many operators have made relentless efforts to transform and upgrade their businesses by pursuing digitalization, engaging in direct sales business to enrich product offerings and incorporating experiential elements to enhance shopping ambience. Moving forward, against the backdrop of the ongoing process of urbanization and continuation of the consumption upgrading trend, the department store sector is set to see huge development prospects.

About the Organizations

CHINA COMMERCE ASSOCIATION FOR GENERAL MERCHANDISE

Founded in January 1990, China Commerce Association for General Merchandise (CCAGM) is a non-profit social organisation endorsed by the Ministry of Civil Affairs, under the guidance of the Stated-owned Supervision Administration Commission and the Ministry of Commerce. The CCAGM has nearly 800 members, encompassing large-and medium-sized domestic department stores, enterprises engaging in retail, wholesale, and manufacture of daily industrial products, and enterprises which provide related services to the department store industry. Its members come from 31 provinces, autonomous regions and municipalities in the country, covering all forms of ownerships. The CCAGM has 60 corporate members, including City Department Store Industry Association, Trade Association and Trans-regional Department Store Company Union Organisation, linking more than 15,000 indirect members.

After 20 years of growth and development, the CCAGM has completed the transformation of its work model from one that was influenced by the planned economy to one influenced by socialist marketing economy. In 2009, the CCAGM was appraised as a 4A social organisation by the Ministry of Civil Affairs.

FUNG BUSINESS INTELLIGENCE

Fung Business Intelligence collects, analyses and interprets market data on global sourcing, supply chains, distribution, retail and technology.

Headquartered in Hong Kong, it leverages unique relationships and information networks to track and report on these issues with a particular focus on business trends and developments in China and other Asian countries. Fung Business Intelligence makes its data, impartial analysis and specialist knowledge available to businesses, scholars and governments around the world through regular research reports and business publications.

As the knowledge bank and think tank for the Fung Group, a Hong Kong-based multinational corporation, Fung Business Intelligence also provides expertise, advice and consultancy services to the Group and its business partners on issues related to doing business in China, ranging from market entry and company structure, to tax, licensing and other regulatory matters.

Fung Business Intelligence was established in the year 2000.

THE FUNG GROUP

Fung Holdings (1937) Limited, a privately-held business entity headquartered in Hong Kong, is the major shareholder of the Fung Group of companies, whose core businesses operate across the entire global supply chain for consumer goods including trading, logistics, distribution and retail. The Fung Group comprises 42,000 people working in more than 40 economies worldwide. We have a rich history and heritage in export trading and global supply chain management that dates back to 1906 and traces the story of how Hong Kong and the Pearl River Delta emerged as one of the world's foremost manufacturing and trading regions. We are focused on both creating the Supply Chain of the Future to help brands and retailers navigate the digital economy as well as creating new opportunities, product categories and market expansion for brands on a global scale.

For more information, please visit www.funggroup.com.

Contacts

Fung Business Intelligence

Teresa Lam

Vice President

Renne Chan

Research Manager

Address

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

China Commerce Association for General Merchandise

Yang Qingsong

Deputy Secretary General

Address

21 Beifengwo Street,
Haidian District, Beijing, China;
Postcode: 100055
Phone: (101) 5191 9069
<http://www.ccagm.org.cn>



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