



FUNG BUSINESS INTELLIGENCE
 Asia Distribution and Retail
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Background

Small format shops, especially convenience and community stores, have gained popularity in recent years in response to consumer demand for more readily accessed, more personalized shopping experiences. As a small-scale retailer, convenience store has the advantage of being more accessible to customers, while offering quicker services and better experiences. In China, the convenience store sector is considered to be the pioneer of retail transformation and reinvention, as well as an active participant in online-to-offline (O2O) integration. It has undergone rapid transformation and reinvention amid the rapidly evolving retail environment.

This article summarizes four key trends in China's convenience store sector.

<p>Digitalization plays a key role in connecting convenience stores and consumers</p> <div style="display: flex; justify-content: space-around;"> <div style="text-align: center;">  <p>Partnering with O2O service platforms</p> </div> <div style="text-align: center;">  <p>Providing self-checkout services</p> </div> </div>	<p>Convenience store operators make greater efforts to launch private labels</p> <div style="text-align: center;">  <p>of surveyed operators said that sales of private label products accounted for over 10% of their total sales in 2018</p> </div>
<p>E-commerce players help traditional mom-and-pop stores and convenience stores embark on digital transformation</p> <div style="display: flex; justify-content: space-around;"> <div style="text-align: center;">  <p>Alibaba LST</p> </div> <div style="text-align: center;">  <p>JD Xintonglu</p> </div> </div>	<p>Convenience stores increase product variety and provide more services for local communities</p> <div style="display: flex; justify-content: space-around;"> <div style="text-align: center;">  <p>Fresh vegetables and fruits</p> </div> <div style="text-align: center;">  <p>Medicine</p> </div> <div style="text-align: center;">  <p>Laundry service</p> </div> </div>

This article is an update of an article published earlier in the Blue Book of China's Commercial Sector (2019-2020) ("Blue Book"). Published in October 2019, the Blue Book tracks developments in China's commercial sector to provide a comprehensive and authoritative account of latest trends and issues. Sectors covered include retail and e-commerce, internet finance, logistics and catering. Also included is detailed analysis of China's consumer market and of the changing preferences and behavior of Chinese consumers. It is an essential resource for businesses, analysts, scholars and governments to gain further insight into this fast-evolving sector.

Please visit <https://www.fbicgroup.com/?q=book/blue-book-china%E2%80%99s-commercial-sector-2019-20> for more information about the Blue Book.

1. Digitalization plays a key role in connecting convenience stores and consumers

In recent years, many convenience store operators have made relentless efforts to transform and upgrade their businesses, often through digitalization. Some convenience store operators have introduced proprietary apps and WeChat Mini Programs. They have also started digitalizing their supply chains. Wuhan-based Today Convenience Store is a case in point. In September 2018, the retailer set up a cloud platform to digitalize warehousing, logistics, merchandising, etc. It also launched an app and WeChat Mini Program to connect with consumers online and offline. At the same time, many first movers in the market have rolled out various initiatives to integrate their online and offline businesses with an aim to provide customers with a better shopping experience.

Partnering with O2O service platforms

Local lifestyle service O2O market in China has developed rapidly over recent years, driven by consumers' increasing pursuit of better quality of life as well as growing demand for convenience. Many convenience store operators have partnered with O2O delivery platforms such as JD Daojia, Ele.me, Meituan Waimai to offer O2O services. Convenience store players can leverage the apps of these platforms to reach out to more customers, while providing other O2O services such as delivery. According to JD Daojia, as of July 2018, it has cooperated with over 10,000 convenience store branches – including leading convenience store operators such as FamilyMart, Lawson and 7-Eleven, as well as regional convenience store chains such as OurHours, Buddies, Today, Wudongfeng, Meiyijia and Youke – to offer O2O services. JD Daojia has also deepened relationship with many convenience store operators by helping them to proceed with digital transformation.

Providing self-checkout services

Some convenience stores have adopted WeChat's "scan-and-go" payment method to optimize checkout process. Shoppers can simply scan product QR code with their mobile devices to check product details and do self-checkout with WeChat Pay. As an example, Beijing FamilyMart launched a specific "scan and go" Mini Program on WeChat in summer 2019 which can be used in all Beijing branches. Meanwhile, it also launched self-checkout machines in Shanghai FamilyMart in August 2019 to reduce waiting time at checkout.

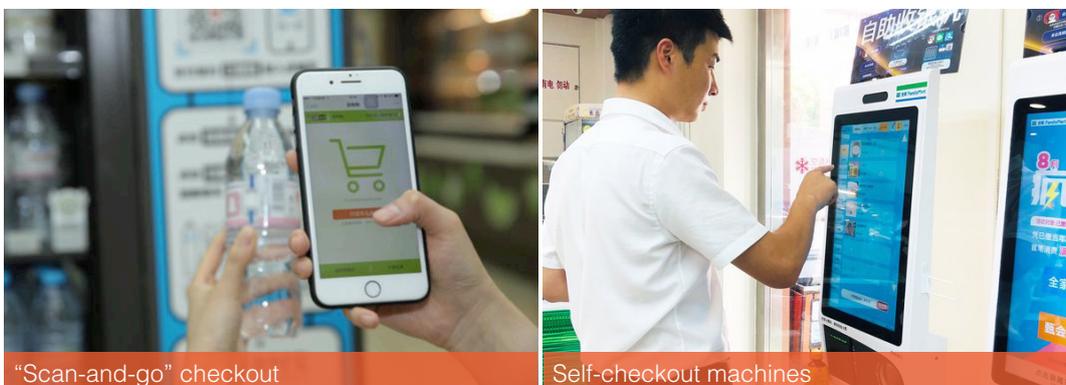


Photo source: Sina, Kknews

2. E-commerce players help traditional mom-and-pop stores and convenience stores embark on digital transformation

Recently, some e-commerce giants such as Alibaba and JD.com are striving to help traditional mom-and-pop stores and convenience stores digitalize their operations.

Alibaba – LST

Alibaba launched its LST (Lingshou Tong) system in 2016 to help mom-and-pop stores embark on digital transformation. LST platform helps small retailers or mom-and-pop stores to transform to "Tmall Xiaodian"; analyze sales and operations data and turn this into insights. Its algorithm advises on the selection of necessary, basic and optional products based on the stores' geographic location, surrounding community and other specialties. With less inventory pressure, smaller retailers can focus on building their own core competences and uniqueness.

In March 2019, Alibaba announced that 1.3 million mom-and-pop stores or unchained convenience store in China – over one-sixth of the total market – have connected with the LST system to provide “one-stop solution for digital transformation” and offer better services to their local neighborhoods. Alibaba has also formed business collaborations with 50 local and overseas brands.



Photo source: Sohu, Linkshop

JD.com – JD Xintonglu

For JD.com, it launched the Xintonglu department (JD Xintonglu), the FMCG B2B arm of JD.com, in 2015. JD Xintonglu helps convenience store owners, especially those in lower-tier cities and rural areas, to revamp and transform their stores. It provides training, branding services and product sourcing to store owners. Store owners need to pay a deposit to connect to JD Xintonglu, adopt JD.com’s ERP system and transform their stores to “JD Convenience Store”; they still retain full ownership of the stores. Store owners can source different types of products including FMCG, digital products, home appliances, apparel and home furnishings through JD.com’s ZGB product ordering system. They can also adopt smart store management systems powered by JD.com. Stores will be linked with JD.com’s other services such as JD Daojia service (online grocery and delivery platform), and Jingxi (group-buying social-commerce platform) to provide one-stop shopping experiences to customers. By connecting the segmented mom-and-pop stores, JD.com hopes to gain local insights in a digitalized way which can in turn benefit JD.com’s whole ecosystem.



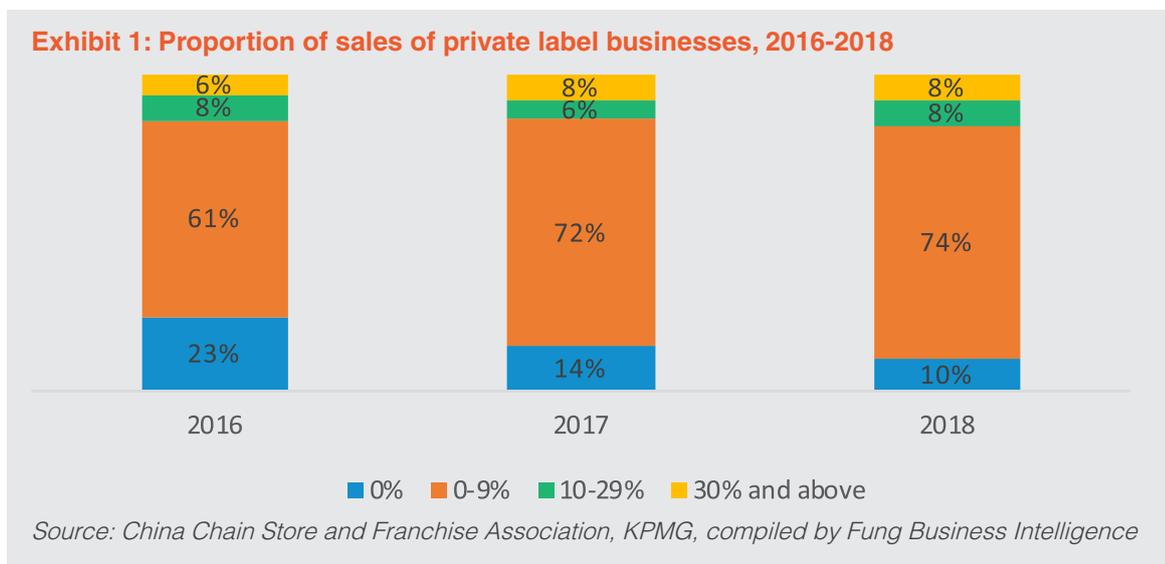
Photo source: Linkshop, Prnasia

Challenges facing JD Convenience Store	
Difficult to manage and control the quality of individual stores	Stores offer different product and shopping experiences even under the same banner of “JD Convenience Store”
Not much discount ordering from JD.com’s ZGB product ordering system	No return and exchange for unsold inventory to JD.com’s ZGB product ordering system
Have to participate in JD.com’s promotional events and provide discounts during shopping festivals	Inadequate training support by JD.com

3. Convenience store operators make greater efforts to launch private labels

Nowadays, Chinese consumers, especially the younger generation, are increasingly looking for unique products. To cater to this demand, many convenience store operators have launched their own private labels. For instance, FamilyMart has launched its own snack food brand “YUMMY” in China; 7-Eleven has introduced its own private label series “Seven Select”; and CP Fresh Mart has launched a number of private labels for fresh produce, wine, tea, etc.

It is noteworthy that private label development in China’s convenience store sector still lags far behind that of equivalent chains in developed countries such as Japan. According to a report by the China Chain Store and Franchise Association (CCFA) and KPMG, 90% of surveyed convenience store operators have launched private labels, and 16% of surveyed operators said that sales of private label products accounted for over 10% of their total sales in 2018 (Exhibit 1). By contrast, for many convenience stores in Japan, private label sales account for around 40-50% of total sales. Thus, there is still huge room for private label development in China’s convenience store sector.



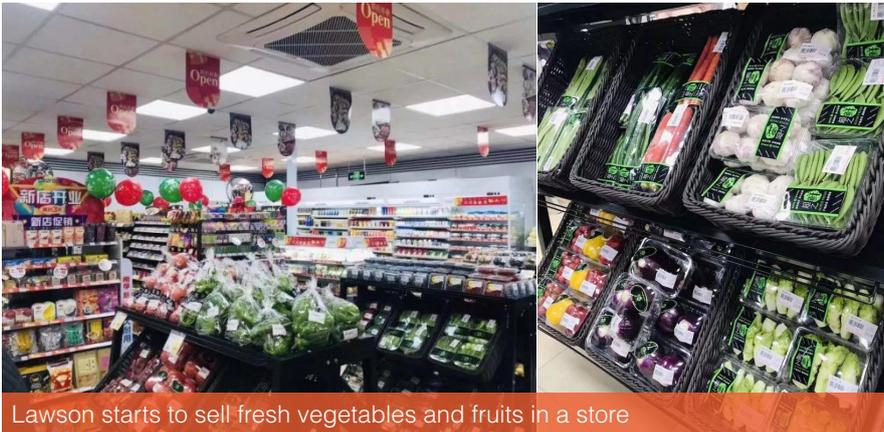
Besides developing and launching private labels themselves, some players are partnering with third-party to roll out private label business. An example is regional convenience store chain Anda Convenience Store. It sells a wide range of private label products sourced from NetEase Yanxuan, an e-commerce platform under NetEase, covering mainly daily necessities such as batteries, data cables, bandages, wet wipes, rags and cloths, bath sponges and slippers.



Inside the Anda Convenience Store
Photo source: Retailobservation

4. Convenience stores increase product variety and provide more services for local communities

Convenience store is the most relevant retail format serving local communities. As a small retail format, it can better understand and respond swiftly to the various needs of consumers in the communities. Providing more diverse services is now a key priority for many convenience stores. For instance, in December 2019, Lawson started to sell fresh vegetables and fruits in one of its franchise stores opened by Chaoshifa in Beijing. Back in 2017, Lawson and local supermarket chain Chaoshifa signed a cooperation agreement for five years, where Chaoshifa can open Lawson franchise stores in Beijing. Chaoshifa's strong supply chain capability enables the company to harness its advantages in terms of types of fresh food, pricing and quality amid the short turnaround times of products. The cooperation of the two companies can produce synergy and help Lawson to differentiate itself from its competitors.



Lawson starts to sell fresh vegetables and fruits in a store

Photo source: Linkshop

Another example is Wumart. In May 2019, Wumart began selling over-the-counter (OTC) medicine in 11 convenience store branches in Beijing. Currently, it offers around 200 kinds of Class B OTC drugs and around 50 kinds of medical devices. Each store has a staff with pharmacy knowledge to provide medication assistance.



Over-the-counter medicine available in some Wumart convenience stores

Photo source: CNPham, Linkshop

JD Convenience Store has also stepped up efforts to expand its service offerings. In May 2018, JD Convenience Store signed a cooperation agreement with Lemonxixi, a domestic O2O laundry service provider, to offer laundry service in selected JD Convenience Store branches. Besides, JD Convenience Store also provides various daily services including financing service, ticketing service, bill payment, delivery service, printing service, etc. Another example is Today Convenience Store, which has partnered with companies in other industries such as domestic fitness centers, Internet Cafés and orchards to launch co-branded convenience stores. These stores aim to provide tailored services and differentiated products for the specific communities.

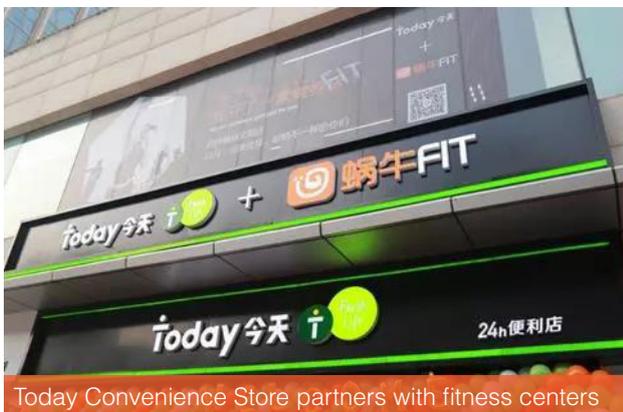


Photo source: Ovdream

Comments from Fung Business Intelligence

China's convenience store sector has undergone tremendous changes over recent years. Many players have revamped their businesses by embracing digital transformation, pursuing O2O initiatives, developing private labels, adopting new business models and expanding product and service offerings. The convenience store sector is set to continue to transform and grow in the coming year, given its eagerness to innovate and adapt to the changing needs of the market. The growth of the sector, however, is not without challenges. High labor costs, including turnover and training costs, as well as lack of funding, present significant hurdles, especially for homegrown convenience store operators. Moreover, some maintain that insufficient government support for the sector's development in some cities has made expansion difficult.

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