

What the **Experts Say**

Ten Highlights of China's Commercial Sector 2020

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Contents

Foreword

01

About the Organizations

03

Expert Panel Members

04

Executive Summary

05

Implications and Key Tips for Foreign
Investors

09

Ten Highlights for 2020

13

Ten Highlights of China's Commercial Sector 2020



07 Renovation of pedestrian streets facilitates consumption upgrading; trend for coordinated development between commerce, tourism and cultural businesses



01 Domestic consumption sees steady growth; further improving China's consumption structure and business environment



04 Transformation of consumer market and circulation sector accelerates; creates a stronger domestic market



08 Community retailing shifts towards services; "last-100-meter" retail gains attention



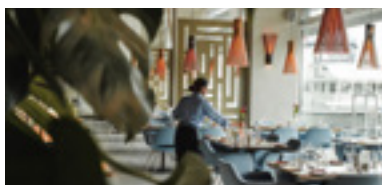
02 Night-time shopping and consuming proliferates, bringing new growth opportunities



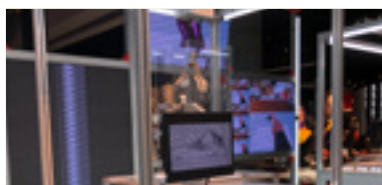
05 Innovative retail formats and new business models become evident, capturing diverse and fast-changing consumer demands



09 Joint efforts to promote rural e-commerce, food traceability and poverty relief lead to mutual gains



03 Services consumption continues to boom; catering industry thrives and enters a smart new era



06 Digitalization becomes the "new normal"; a revolution in the circulation industry facilitates reconstruction of production processes



10 Agricultural distribution channels accelerate transformation; rural issues and consumption upgrading are better addressed

Foreword

2019 has proven to be a volatile year. Domestic and external economic challenges have exerted downward pressure over the year on China's economy. At the same time, rapidly evolving consumer demand and the rise of both new technologies and innovative business models have continued to reshape – if not disrupt – the commercial landscape. That said, Chinese consumers have demonstrated resilience on the back of rising incomes. Lower-tier cities, in particular, have opened new opportunities for local and foreign enterprises. Moreover, the government has launched a series of measures to boost domestic consumption such as facilitating the development of the services sector, the so-called night-time economy, community retailing, rural e-commerce and tackled other issues, further strengthening the role of consumption in driving China's overall economic growth.

In 2020, we expect the government's policy support will start to see some positive outcomes; ongoing consumption upgrading and the services consumption boom will create new demand and opportunities. Moreover, the anticipated first-phase China-U.S. trade agreement is set to reduce business uncertainty and help regenerate economic and consumption growth. To thrive and survive in the market, commercial enterprises need to strategically position themselves to better adapt to new customer needs and be more innovative and forward-thinking. They have to continue to adopt breakthrough technologies and transform.

For the 17th consecutive year, Fung Business Intelligence and the Expert Committee of the China General Chamber of Commerce jointly present their annual publication – *Ten Highlights of China's Commercial Sector*. The report presents the key trends identified by over 160 top-tier experts in China's commercial sector together with additional Fung Business Intelligence analyses, aiming to draw essential insights into China's commercial developments over the coming year. Over successive years, the report has offered the single most authoritative account of those trends and issues impacting China's commercial landscape, serving as an important reference point for global brands and retailers, commercial enterprises, and individuals aiming to better understand the latest commercial trends and issues in China.

We would like to thank all panel members on the Expert Committee of the China General Chamber of Commerce for sharing their insights. We also thank our colleagues at Fung Business Intelligence for their contributions and assistance.

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About the Organizations

The Expert Committee of the China General Chamber of Commerce

The Expert Committee of the China General Chamber of Commerce (ECCGCC), a sub-division of the CGCC, comprises over 160 prominent experts from various government departments, research institutes and universities, leading corporations, professional associations, consultancy firms and newspaper offices, which include the Ministry of Commerce, the Chinese Academy of Social Sciences, China Chain Store and Franchise Association, the Development Research Centre of the State Council, the Renmin University, the Capital University of Economics and Business, and the Beijing Technology and Business University, etc.

The ECCGCC serves as a platform for the experts to exchange ideas on the development of commercial enterprises and the distribution sector.

The China General Chamber of Commerce

Founded in 1994, the China General Chamber of Commerce (CGCC) is a quasi-government association endorsed by the State Council. The CGCC has around 70,000 members, encompassing enterprises from retail, distribution, services and tourism sectors, local commercial chambers, national professional associations, intermediary organizations and individuals.

Commissioned by the Chinese Government, the CGCC consists of 14 committees, working on areas such as retailing, wholesaling, public relations and industry analyses, etc.; it also supervises 40 national associations, and over 30 newspapers and magazines published both inside and outside China.

Fung Business Intelligence

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

Headquartered in Hong Kong, it leverages unique relationships and information networks to monitor, research and report on these global issues with a particular focus on business trends and developments in China. Fung Business Intelligence makes its data, impartial analysis and specialist knowledge available to businesses, scholars and governments 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 consulting 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 is a privately-held business entity headquartered in Hong Kong with a rich history in trading and supply chain management dating back to 1906. It is the major shareholder of the Fung Group of companies whose diverse 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.

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Executive Summary

01

Domestic consumption sees steady growth; further improving China's consumption structure and business environment

Against the backdrop of a more complicated internal and external economic environment, the Chinese government has continued to strengthen the role of domestic consumption in maintaining economic growth. In particular, the rapid growth of services consumption has fuelled advances in services subsectors that include catering, travel, sports, entertainment, healthcare and elderly-care services. In 2020, the government will step up efforts to boost consumption and optimize the business environment. It is expected that China and the U.S. will reach beyond their anticipated phase-one trade deal, and that global trade will improve gradually in 2020. An easing of trade tensions between the two countries will reduce business uncertainty and help regenerate economic and consumption growth. Meanwhile, China's Belt and Road Initiative will open up more export and investment opportunities for Chinese enterprises while also encouraging more imported goods from the many countries along the Belt and Road, thereby further stimulating domestic consumption.



02

Night-time shopping and consuming proliferates, bringing new growth opportunities

Recent research studies indicate that there are vast opportunities for China to develop its "night-time economy". According to a survey of consumption habits, conducted by the Ministry of Commerce, 60% of Chinese consumption now occurs during the night hours. The night-time economy saw rapid growth in 2019 with the government's determined efforts to boost consumption. Initiatives include extending the operating hours of museums, shopping centers and restaurants, and turning more public places and vacant factories into entertainment, sport, food, tourism and shopping venues to support the development of business formats for night-time consumption. The night-time economy is set to become a priority in the coming year as the government strives to stimulate domestic demand and promote consumption. The focus will increasingly be on night-time cultural content as well as experiential and social elements.



03

Services consumption continues to boom; catering industry thrives and enters a smart new era

In recent years, China's services consumption has maintained strong growth momentum and become a new force driving the country's economic growth. Rising residential incomes and extensive government support for the services sector have underpinned the robust growth of domestic services consumption, which is playing an increasingly important role in driving the ongoing upgrading of Chinese consumption. In addition, the advent of the 5G communication era and introduction of new digital technologies have combined with ongoing consumption upgrading to drive digital transformation in services businesses. This is particularly the case in the catering industry which has actively undergone business format innovation by adopting smart technologies ranging from concierge and service robots to smart cooking machines and facial recognition technology, while expanding product and services offerings.



04

Transformation of consumer market and circulation sector accelerates; creates a stronger domestic market

China's consumer market has maintained solid growth momentum in recent years, signalling its key role in facilitating the country's high-quality economic growth and pushing forward supply-side structural reform. Creating a stronger domestic market is a priority for China's economy; as a result, the government has unveiled practical measures to boost domestic consumption and increase investment. Meanwhile, with ongoing consumption upgrading in China, commercial enterprises are making vigorous efforts to transform and innovate. Some companies are actively tapping lower-tier cities and rural markets – which are set to be the major drivers of growth in China over the next decade; other companies are introducing new business models and retail formats, and developing private labels, with the aim of providing higher-quality, more diverse products and services to meet ever higher consumer preferences.



05

Innovative retail formats and new business models become evident, capturing diverse and fast-changing consumer demand

Generation Z consumers, who are highly familiar with mobile technologies and are socially fluid, demand more convenient ways of shopping than older generations. Their demands have prompted retailers and e-commerce players to evolve and launch innovative retail formats and business models to engage with them. In particular, social commerce – the use of social networks to drive e-commerce sales – is transforming direct-to-consumer transactions and the e-commerce experience. Mini Programs have increasingly become an effective selling channel online while live-streamed shopping, particularly through short video platforms, has also become vital for e-commerce sales. Pop-up stores and IP-themed stores or events are also gaining in popularity and have become effective marketing strategies for many brands and retailers in the offline scene. Additionally, to capture the needs of these new consumers, retailers and brands have identified new business opportunities such as tapping the singles economy, penetrating local community preferences, and leveraging the so-called “first-store” economy to rejuvenate local retail markets.



Executive Summary

06

Digitalization becomes the “new normal”; revolution in the circulation industry facilitates reconstruction of production processes

In 2019, digitalization became the dominant factor for business success, especially for retail. Having experienced the initial advantages brought by the digital economy and big data analysis, enterprises are more determined to embrace digitalization and technology innovation. For the future, retailers and e-commerce platforms will continue to leverage big data analytics and other digital tools to perform target marketing, optimize inventory management and develop private labels.

On the retail side, digitalization is set to drive digital and technological upgrades, speeding up processes along the supply chain, from factory to consumer. At the same time, retailers are being empowered by customer demands to drive the adoption of smart manufacturing. Digitalization is set to spark yet another transformative cycle in wholesale trades and logistics, eventually deepening reform and upgrading the circulation industry.



07

Renovation of pedestrian streets facilitates consumption upgrading; trend for coordinated development between commerce, tourism and cultural businesses

The government has stepped up support for the development of pedestrian streets in recent years. In December 2018, the Ministry of Commerce (MOFCOM) published a notice on developing a number of world-class pedestrianized streets. It published a more detailed proposal in August 2019 that states clearly its goal to develop up to 50 enhanced pedestrianized streets in municipalities and capital cities across the country and achieve a 30% increase in visitor traffic and sales within three years. With state-led measures in place, another wave of pedestrianized street renovations and upgrading is expected in 2020. At the same time, the trend for coordinated development between commerce, tourism and cultural businesses will be accentuated.



08

Community retailing shifts towards services; “last-100-meter” retail gains attention

Community retailing has been developing rapidly. Formerly focused primarily on product sales, this form of retail has, since 2019, started to transform and upgrade services that are more life related, particularly those aimed at promoting welfare and convenience in local communities. New developments such as government-sponsored one-stop community centers, and neighborhood commercial districts, have come on the scene to provide goods and services that can satisfy the everyday needs of residents. Meanwhile, with increasing consumer demand for faster services and more convenient shopping experiences, “last-100-meter” retail has gained popularity over recent years. Convenience stores, small-format stores and store-front warehouses (spaces designated inside stores to act as warehouses) are key retail channels to provide “last-100-meter” services and, having grown quickly in 2019, are expected to maintain their growth impetus in 2020.



09

Joint efforts to promote rural e-commerce, food traceability and poverty relief lead to mutual gains

Thanks to the coordinated efforts of central government authorities, local communities and countless enterprises, rural e-commerce and food traceability systems in China have been making rapid strides. These efforts involve breaking down operational barriers as well as promoting harmonization and integration of systems across entire supply chains. Backed by advanced digital traceability technologies such as blockchain, the Internet of Things (IoT) and big data-based tracking systems, the government has launched food traceability pilot projects throughout the countryside. Such projects have supported the growth of rural cooperatives, whole chain traceability systems, brand awareness of rural farm products and new distribution channels. These developments have also improved the supply and demand cycle for agricultural products, and enhanced food safety and quality while playing an important role in poverty reduction and agricultural modernization in rural areas.



10

Agricultural distribution channels accelerate transformation; rural issues and consumption upgrading are better addressed

Large numbers of traditional agricultural wholesale markets have taken ambitious steps to transform and upgrade over recent years. Examples include an integrated agricultural supply chain to support online-to-offline integration and enhance efficiency; improved standardization and brand integrity of farm produce; and the accelerated building of distribution centers at points of origin. Upgraded agricultural wholesale markets play an increasingly significant role in connecting farmers with consumers in urban areas and addressing mismatches in supply and demand for farm products. Additionally, wholesale market transformation can also promote the distribution of higher value rural products, contributing to significant income growth in the countryside.



Implications and Key Tips for Foreign Investors

The past year has seen significant challenges for the commercial sector. Notably, the China-U.S. trade tensions have taken a massive toll on the global economy, possibly to be ameliorated to an extent going forward with the signing of a phase one agreement between the two countries in December. Meanwhile, China's economic growth has cooled further over 2019 and retail sales growth has continued to weaken. However, as reflected in this year's *Ten Highlights* report, the government has taken ambitious steps to boost consumption. For instance, it has launched substantial policy measures – at central and local levels – to support the development of the services sector, the so-called night-time economy and community retailing, among others. At the same time, the government has taken major steps to promote rural e-commerce and facilitate the transformation and upgrading in agricultural distribution. This helps to unleash the vast potential of the country's rural areas and smaller cities.

To survive and prosper in the new era of such challenges and opportunities, commercial enterprises need to be aware of all the evolving trends impacting the commercial sector and adapt swiftly to change. They should pay particular attention to the following issues:



Power of youth: Generation Z and small town youth drive consumption growth

Today, young consumers, especially millennials born in the early 1990s (better known as the “post-90s” generation) and even younger Generation Z consumers born between 1995 and 2009, are collectively becoming a new engine of China's consumption growth. They have huge consumption potential, and seek a lifestyle where shopping is an individualized, immediate and convenient experience. They are also digital “natives” who were born and raised in a digital and media-saturated world, and have formed unique shopping habits online, and via social media networks. Apart from young consumers in key cities, those residing in lower-tier cities and small towns, the so-called “small town youth”, have emerged and became a major consumer group. Since living costs are less in lower-tier cities, small town youth have strong spending power; additionally, they enjoy a more relaxed lifestyle and have more free time to spend as compared to their counterparts in tier-1 and tier-2 cities. Young consumers in key and smaller cities present excellent opportunities for brands and retailers.

Our take: Winning the loyalty of young consumers – particularly the post-90s generation and the Generation Z consumers – is key to business success in the consumer-driven market. Successful enterprises are those able to appreciate and meet the needs of these empowered young customers and to engage closely with them via multiple offline and digital touchpoints to create better experiences for them.

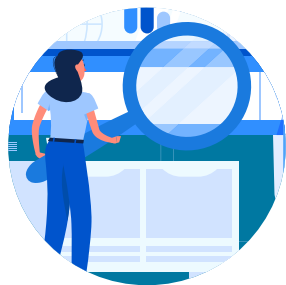


Social commerce becomes the next wave of retail; embracing social-media centric O2O strategies is at the heart of business innovation

Today, mobile shopping, peer-to-peer selling and Internet key opinion leaders (KOLs) marketing are continually on the rise, while social commerce is becoming the next wave of retail. More enterprises – from apparel and cosmetics brands to offline supermarket chains and retailers in different industries – are leveraging social media platforms to sell their products, as well as retain current and gain new customers. Besides, the types of social commerce platforms are becoming more diverse. These platforms – such as for content-sharing, membership, group buying and live-streaming – allow relationship building and help retailers penetrate lower-tier cities.

At the same time, omnichannel retailing, or online-to-offline (O2O) integration which has been a trend for many years, will continue to dominate the retail scene. To stay ahead in the innovation race, many enterprises are proactively refining their O2O strategies – by fusing various online and offline channels, adopting new technologies for payment, logistics and supply chain operations, while providing personalized and convenient shopping experiences to consumers via all touchpoints.

Our take: Social commerce is inevitable, driven by changing shopping habits and preferences of young consumers. To better facilitate this growing trend, enterprises need to adopt the right mobile- and social media-centric O2O strategies to provide seamless consumer shopping experiences. It is imperative that they choose the appropriate platforms, channels and marketing approaches to reach and attract customers. Hiring KOLs or other types of social influencers to create relevant content and market products is essential in connecting with consumers, especially those within the increasingly influential Generation Z group.



Keeping a close eye on new business models and innovative retail formats

Many brands and retailers are seeking new breakthroughs to meet ever-evolving consumer demand, resulting in the emergence of new business models and innovative retail formats – both online and offline. These channels need to deliver the unique shopping experience and excitement that consumers require. Pop-up, IP themed and community stores are some of the recently emerging offline channels that are most popular. Innovative marketing content, retail technologies and experiential elements in these stores can help brands promote their products and enhance brand awareness. Some fast-evolving online platforms aided by social-commerce tools such as Mini Programs and live-streamed shopping are revolutionizing the ways consumers receive product information and shop for goods. They provide brands and retailers with unique opportunities to deliver the much desired “immersive shopping experience”, while building customer loyalty.

Our take: To keep pace with the rapidly evolving commercial landscape, enterprises need to introduce new business models and retail practices, as well as carry out format innovations. These new retail formats or practices – whether online or offline – should be capable of creating immersive experiences for customers with quality content, state-of-the-art technologies, entertainment and other experiential elements. Enterprises are advised to regularly assess the efficiency of these new channels and retail formats for converting traffic into actual sales as well as creating synergies with core businesses.



Leveraging data analytics and information technology to build an integrated supply chain

Digitalization in retail is transitioning from launching new retail formats and consumption scenes to rigorously adopting predictive analytics and advanced information systems. With digitalization, retailers can optimize inventory forecasts and targeted marketing, while taking a more active role in the supply chain, and driving upstream digital and technological upgrades. The supply chains will therefore be shortened and become more efficient. Retailers can then direct more resources to developing private labels, and expanding offline or exploring different formats. Factories, on the other hand, will need to develop digitalized capabilities to cope with changes in retail demand.

Our take: Enterprises will continue to embrace big data analytics and employ digital tools and software that allow information flows while executing instructions to be shared and exchanged with supply chain partners. When enterprises digitalize certain applications, they must ensure that this will contribute to the construction of a fully integrated, cohesive ecosystem. Enterprises have to be prepared to work with technology firms in China to achieve local adaptation.



Tapping the services boom

With consumption upgrading in full swing across China, consumers are using more services such as catering, travel, sports, entertainment, healthcare, elderly services, education and training. Services consumption is now a dominant force driving China's economic development, accounting for nearly 50% of the country's total consumer spending. In adherence to this trend, the government is committed to unleashing the consumption potential in the services sector and increasing the supply of quality services in the market. For example, it has deepened reform of the income distribution system in a bid to increase the incomes of lower-paid groups and at the same time to expand the size of middle-income earners; it has also relaxed restrictions on market access for some service businesses, such as removing the investment threshold in culture, sports and other related fields. Additionally, the government is endeavored to improve social and legal conditions and to enhance the business environment. All these measures will help to create favorable conditions for foreign investors.

Our take: While China's services sector is opening further to the rest of the world, it is continuously enriched by technological innovations. This will provide ample development opportunities for investors. Enterprises should consider tapping the services sector for new business development options. The government is determined to support services sector development while enterprises need to update themselves on government policies and capitalize on opportunities these provide.



Lower-tier cities and rural e-commerce: The next wave of growth

While the markets in China's tier-1 and tier-2 cities are becoming increasingly saturated, there are distinct opportunities elsewhere in lower-tier cities, small towns and rural areas. With increasing incomes and lower living costs, consumption power is expanding fast in less-developed, lower-tier cities and small towns. Residents in these smaller cities offer huge, untapped potential for e-commerce. According to QuestMobile, there are 128 million Internet users in tier-3 or lower-tier cities who have not yet bought anything online compared to the 74 million users in tier-1 and tier-2 cities. Moreover, improving e-commerce infrastructure in rural areas – particularly in distribution channels, delivery and payment – also helps drive the growth of rural e-commerce.

Our take: When tapping these new markets, enterprises are advised to choose channels and business models that are in line with the needs and preferences of customers in these markets. For instance, social commerce – especially the group-buying model and shopping via short video apps – is popular among shoppers in lower-tier cities. Enterprises must fully leverage social media as part of their omni-channel retailing strategies when reaching out to consumers in the lower-tier cities and rural markets.



Keeping abreast of government policies and measures

In 2019, the Chinese government stepped up efforts to launch policy measures to stimulate domestic demand and push for consumption upgrading. For instance, the State Council issued a policy package entitled *Opinions on Accelerating the Development of the Circulation Industry to Boost Consumption*, highlighting initiatives to develop the night-time economy, innovate pedestrian streets, increase the number of convenience stores, refurbish public places and vacant factories to become consumption scenes, as well as enhance those scenes with experiential and social elements.

Local governments will provide infrastructure, transportation, information exchange mechanisms and security measures for such developments. Government's role also includes facilitating cross-sector cooperation to achieve coordinated development between commerce, tourism and cultural businesses.

Our take: Enterprises should be aware of these state-led measures and policy guidelines and prepare to tap new business opportunities and government incentives. They should reserve resources for potential expansion into new commercial areas or lower-tier cities and be flexible in extending their operational hours to accommodate increased traffic.

01

Domestic consumption sees steady growth; further improving China's consumption structure and business environment



In 2019, China's economy faced further downward pressure against the backdrop of a more complicated internal and external economic environment. In particular, the deceleration in investment growth, as well as the slowdown in export growth due to the trade tensions between China and the U.S. have taken a toll on business and consumer confidence; this might change for the better in 2020 given the new phase one trade agreement in December between the two countries. Yet, against the prevailing backdrop, the Chinese government continued to strengthen the role of domestic consumption in maintaining economic growth. It issued a number of measures in 2019 to boost consumption, for example as manifested by accelerating the development of the circulation industry* and supporting the growth of services consumption. These government-led initiatives have provided a solid foundation for the steady development of the consumer market, particularly in increasing the supply of quality products, introducing new retail formats and expanding the scope of services.

* The circulation sector covers all the processes between production and consumption, including the flow of goods, services, information and capital. It includes the wholesale and distribution, retail, catering and logistics industries.



In 2020, the Chinese government will make greater moves to boost domestic consumption and optimize business environment. These will provide a solid foundation for the steady development of the consumer market, particularly in increasing the supply of quality products, introducing new retail formats and expanding the scope of services.

Cha Jinxiang, Director, Department of Market System Development, Ministry of Commerce of the PRC

Domestic trade review: major developments in 2019

GDP growth was stable at 6.2% yoy in 1-3Q19; consumption becomes the main growth engine of domestic economy

In 1-3Q19, China's GDP amounted to 69.8 trillion yuan; real GDP growth was 6.2% year-on-year (yoy), slightly lower than 6.7% yoy in 1-3Q18. The services sector has continued to grow at a faster pace than the secondary sector, with services sector value-added contributing 54.0% of China's GDP in 1-3Q19, 0.6 percentage point (ppt) higher than over the same period in 2018. By contrast, secondary sector value-added contributed 39.8% of China's GDP in 1-3Q19, 0.7 ppt lower than over the same period in 2018. The role of consumption in driving economic growth continued to strengthen in 1-3Q19; consumption contributed 60.5% of GDP growth. Our experts expect GDP growth in FY19 to be about 6.1% yoy.

CPI growth moderated towards the end of the year, except pork prices

The yoy growth rate for China's consumer price index (CPI) rose 2.5% yoy in 1-3Q19, up 0.4 ppt from the same period in 2018. CPI growth of the food component jumped by 6.5% yoy, up 5.1 ppts from 1-3Q18 while CPI growth of the non-food component increased by 1.5% yoy, down 0.7 ppt from the 1-3Q18. Noticeably, pork prices surged by 21.3% yoy, up 31.6 ppts from 1-3Q18; pork prices rose 101.3% yoy in October, pushing CPI to a nearly eight year high. Surging pork prices, due to the year-long outbreak of African swine fever, was the main driver of CPI growth in 2019. To curb a further hike in pork prices, the government launched various policies to increase pork supply such as by increasing pork imports, and granting subsidies for pig farmers. These policies have started to see positive outcomes with wholesale prices of pork starting to decrease in November. Our experts believe pork supply will become more stable in the coming months with prices returning to former levels.

Services consumption maintained strong growth momentum

Services consumption continued its fast growth momentum in 2019. In 1-3Q19, the household per capita consumption expenditure was 15,464 yuan, up 8.3% nominally over the same period in 2018. Of which, the per capita consumption expenditure of services increased by 10.2% yoy, much faster than the consumption expenditure on goods. Currently, consumption expenditure of services account for 50.6% of total expenditure, exceeding goods to become the major contributor of consumption growth.

Retail sales growth moderated; sales of daily consumables and upgraded products grew rapidly

China's nominal retail sales of consumer goods rose by 8.2% yoy to 29,667.4 billion yuan in 1-3Q19, 1.1 ppts down from the same period in 2018. By month, total retail sales growth of consumer goods remained stable at between 7.2% and 9.8%. The decrease in retail sales in 1-3Q19 is partly explained by the decelerating growth of automobile-related and petroleum-related sales. Sales of automobile-related products by enterprises above the designated size in 1-3Q19 went down by 0.7% yoy, while petroleum-related sales grew 1.7 yoy. Excluding the automobile sector, retail sales of consumer goods grew 9.1% yoy nominally in 1-3Q19, compared with 9.3% yoy nominal growth for total retail sales of consumer goods in over the same period in 2018.

By product category, daily consumables' sales growth of enterprises above the designated size was on an upward trend. In 1-3Q19, grain, oil and food sales growth rose 10.6% yoy, beverages up 9.8% yoy, daily use products up 13.6% yoy, and cosmetics up 12.8% yoy – all faster than for growth in the same period of 2018. Meanwhile, demand for upgraded products such as wearable smart devices, smart home appliances and audiovisual equipment, and new energy vehicles also increased rapidly, showing the growing trend for consumption upgrading.

Our experts expect total retail sales growth to have rebounded in 4Q19, driven in part by the spending boom during the National Day holidays and 11.11 Global Shopping Festival, as well as stable sales growth for daily consumables. Total retail sales for FY19 is estimated at around 8.0%.

Share of online retail sales to total sales continued to increase

Total online retail sales of goods and services reached 7,323.7 billion yuan in 1-3Q19, up 16.8% yoy. Online sales of goods accounted for 5,777.7 billion yuan, up 20.5% yoy, much lower than the growth of 27.7% yoy in the same period in 2018. The share of online retail sales further increased and accounted for 19.5% of total consumer retail sales, up from 17.5% over the same period in 2018. Moreover, online retail sales growth was

faster than that for physical store sales. In 1-3Q19, the contribution of online sales of goods as a constituent in the growth of total retail sales was 43.7%, the same as its contribution over the same period in 2018. With further integration of online and offline offerings, innovation of online retail channels, as well as improved online shopping experiences, online retail sales growth still outpaced that for offline retail sales.

Rural consumption became the focus

Rural retail sales have been growing faster than the urban figure over recent years. Rural retail sales rose 9.0% yoy to 4,315.0 billion yuan in 1-3Q19, 1.5 ppts lower than over the same period in 2018, while urban retail sales expanded 8.0% yoy to 25,352.4 billion yuan, 1.0 ppt down from the same 2018 period.



What the Experts say

Our experts project that, in 2020, the Chinese government will adhere to the general principle of “pursuing progress while ensuring stability” and continue to apply its new philosophy on ensuring development. Additionally, the government will strengthen supply-side structural reform and take further steps to ensure stability across employment, the financial sector, foreign trade, foreign and domestic investment, and overall expectations, aiming to stabilize economic growth and promote high-quality development.

Meanwhile, the government has articulated its efforts to boost domestic consumption and optimize the business environment. Since the beginning of 2019, it has released a number of policy documents underlining its determination to boost consumption. For example, in August 2019, the State Council released the *Opinions on Accelerating the Development of the Circulation Industry to Boost Consumption* which outlined 20 measures to promote consumption; these include liberalizing car-purchasing restrictions, encouraging sales of new energy vehicles,

expanding cross-border e-commerce imports to more cities, applying new technologies to promote product distribution, improving infrastructure of pedestrian streets, promoting the development of the night-time economy, and accelerating the development of chain convenience stores. Many of the areas are covered in detail in subsequent chapters. The government’s determined efforts – along with the ongoing consumption upgrading – are set to strengthen the fundamental role of consumption in driving economic growth.

At the same time, the government has been determined to make greater moves to build on a vibrant business environment in China. It has launched a series of measures to cut taxes and fees, and to further optimize the business environment. For example, in October 2019, the State Council announced the *Regulations on Optimizing the Business Environment* which will become effective on 1 January, 2020. The regulation states that the government will continue to optimize China’s business environment, further streamline administrative approval, improve supervision and decentralize decision making. The regulation also specifies the principles and directions for fostering a stable, fair, transparent

The faster growth in rural retail sales was partly attributed to higher rural household income growth. In 1-3Q19, the per capita disposable income of rural households increased nominally by 9.2% yoy (or 6.4% yoy in real terms) to reach 11,622 yuan, while the per capita disposable income of urban households rose 7.9% yoy in nominal terms (or 5.4% yoy in real terms) to reach 31,939 yuan. Moreover, in recent years, e-commerce players have turned their focus to lower-tier cities and rural areas to seek new growth opportunities, thus helping to boost rural retail sales growth. Meanwhile, the ongoing consumption upgrade has also led to higher demand for better quality and customized products from rural consumers.

Small enterprise retail sales and catering sales saw rapid growth

Small-format stores have gained in popularity and have become major drivers of consumption over recent years as consumers increasingly look for personalized goods and more convenient shopping experiences. In 1-3Q19, retail sales growth for retail enterprises below the designated size and individual retail enterprises rose 10.7% yoy, 6.8 ppts higher than the growth for retail enterprises above the designated size and accounted for 62.2% of total retail sales. Meanwhile, small catering enterprises continued to outperform larger ones. Growth for catering enterprises below the designated size and individual catering enterprises was up 10% yoy in 1-3Q19, 2.7 ppts higher than growth sales of those above the designated size, and accounted for 78.9% of total catering sales.

and predictable business environment. Such an enhanced business environment could better attract investment, thereby improve the employment rate, as well as boost consumer confidence and spending power.

Our experts also highlight their projections on domestic trade and commercial sector development in 2020:

Services consumption continues to flourish. Currently, there are more than 400 million middle class consumers in China, with the number growing fast. Enjoying higher incomes and rising demand for personalization in every aspect of life, this group of consumers is set to be the major driver of services consumption. The rapid growth of services consumption will fuel advances in services subsectors that include catering, travel, sports and entertainment, healthcare and elderly-care services. Given the rapid development of the services sector, our experts urge the government to consider including the proportion of services consumption in GDP as an indicator for city development. Moreover, our experts also suggest establishing a new calculation method for the nation's total retail sales. The current retail sales

figure includes only sales of physical goods, but not services consumption. Thus, the rapid growth of services consumption is not currently given sufficient weight in the broader economic picture for consumption.

Other positive factors support economic and consumption growth. Our experts believe that China and the U.S. will reach beyond an announced preliminary phase one trade deal, and that global trade will improve gradually in 2020. Easing trade tensions between the two countries will reduce business uncertainty and facilitate economic and consumption growth. Meanwhile, the impact of China's Belt and Road Initiative on trade is becoming more evident; this not only opens up more export and investment opportunities for Chinese enterprises, but also encourages more imported goods from many countries along the Belt and Road, thereby further stimulating domestic consumption.



02

Night-time shopping and consuming proliferates, bringing new growth opportunities



As urbanization continues, people who work by day find their consumption needs can only be fulfilled at night. China, like many other countries, is leveraging changing consumption habits to promote night-hours businesses. In 2019, the Chinese government issued a number of policy guidelines and applied significant resources to develop the so-called “night-time economy”. The overall direction is to extend the time for commercial activities and offer more interesting and entertaining consumption scenes so that people are more willing to spend money at night.

The night-time economy is set to become a priority in the coming year as the government strives to stimulate domestic demand, promote consumption and increase employment.



In recent years, the scope of night-time economy has extended far beyond night markets. It covers a diverse range of activities and content including shopping, eating, entertainment, arts and culture, and exhibitions.

Lai Yang, Director,

Institute of Commerce and Economics, Beijing College of Finance and Commerce Management

Night-time economy sees huge growth potential

Recently, some research and studies indicated that there are vast business opportunities for China to develop the night-time economy. According to a consumption habit survey conducted by the Ministry of Commerce, 60% of consumption occurs during the night hours. Also, shopping mall sales made between 6 p.m. and 10 p.m. accounted for half of total daily sales. The China Tourism Academy conducted a research on night-time tourism in 2019 and found that 92.4% of the surveyed tourists had participated in nightly tourist activities.

UnionPay data showed that night-time spending accounted for 28.5% of total daily sales and 25.7% of orders made during the Chinese New Year in 2019. Tourists contributed to around a third of these sales. This suggests that the night hours tourism economy is becoming increasingly important as destinations gather significance.

Statistics from Meituan showed that, while catering spending on the platform during the day grew by a mere of 2% yoy in 2018, night-time catering spending increased by 47% yoy. It further disclosed that for the first six months of 2019, orders placed in Shanghai between 9 p.m. and 5 a.m. grew 127% yoy. The two hours from 9 p.m. to 11 p.m. accounted for nearly two-thirds of the orders. Other cities, such as Hangzhou and Shaoxing, saw more than 40% yoy growth in night hours orders during the first half of 2019.

A report on the night-time economy published by Alibaba indicated that sales made on Taobao during night hours accounted for 36% of total daily sales. It also stated that Alibaba's Freshippo supermarket (previously known as Hema supermarket), and food delivery platforms Koubei and Ele.me play an important role in driving night-time consumption. Moreover, Alibaba's 700 million users are a potential force for boosting the night-time economy.

Strong government support for the development of night-time economy

The night-time economy saw rapid growth in the past year with the government's determined efforts to boost consumption. On 27 August 2019, the General Office of the State Council issued a policy package entitled *Opinions on Accelerating the Development of the Circulation Industry to Boost Consumption* and rolled out 20 measures to accelerate national consumption. It highlights several initiatives to stimulate night hours consumption, including extending the operating hours of museums, shopping centers and restaurants, turning more public places and vacant factories into entertainment, sport, food, tourism and shopping venues from 6 p.m. to 6 a.m., and supporting the development of night-time business formats such as 24-hour convenience stores, midnight food stores and other featured food courts.

Following instructions by the central government, local governments have individually issued policies to develop the night-time economy:

- In July 2019, Beijing issued the *Measures to Further Develop Night-time Economy and Promote Consumption Growth in Beijing*, which outlines 13 measures to forge a world-renowned “Night Beijing” brand. This aims to establish a landmark night city and build several characteristic commercial and better living opportunities by the end of 2021.
- In April 2019, Shanghai issued the *Guiding Opinions on Promoting the Development of Night-time Economy in Shanghai*, which highlights the need to create a night hub that can compete with international counterparts, while featuring the unique features and characteristics of Shanghai. Its priority is to borrow from international experience and set up a coordination mechanism within different government departments.

To improve the supply of night hours businesses, Shanghai has launched iconic night markets since 2017 that serve a wide variety of food and Shanghainese cuisine to attract domestic and international tourists. These night markets are designated as pedestrian streets, food plazas and markets mixing commercial, touristic and cultural elements.

- In August 2019, Guangzhou issued the *Implementation Plan to Promote Night-time Economy in Guangzhou*, aiming to forge a world-renowned “Night Guangzhou” brand. The city hopes to build 13 nationally renowned commercial districts and cultural events, and 30 “nightlife districts” by 2020. In the same month, the Ministry of Commerce of Guangzhou Municipality also published the “Night-time Consumer’s Map of Guangzhou”. The Plan envisages fifteen key commercial and shopping districts, including Beijing Road pedestrian street, Tianhe commercial district and Zhujiang Party Pier to constitute the first batch of “Night Guangzhou” landmark districts.
- Local governments in Tianjin, Chongqing, Qingdao, Hangzhou, Shijiazhuang, Nanjing, Xi’an, Chengdu, Nanchang and Ningbo have also unveiled a series of measures to stimulate night-hours consumption in a bid to turn their cities into world-class “nightlife capitals.”





What the Experts say

Night-time economy covers a wide scope of activities and content

Currently, many people still perceive the “night-time economy” as traditional night markets that offer a variety of street food and cheap bargains. In fact, it has a much wider scope, including shopping, eating, entertainment, arts and culture, and exhibitions. For example, the Beijing Culture and Creation Market sells many high-quality cultural goods and is open until later hours; the Qinhai River, Nanjing night market offers a mix of catering services, light shows, night cruises and other entertainment activities; and Jinan’s “Ancient Alley” (also known as Jinan Laojie) stages Chinese opera shows and organizes workshops at night. These night markets have gained huge popularity and become attractive appearance spots for online celebrities.

Imbalance of north-south development

Our experts point out the night-time economy is better developed in the south than in the north. According to the previously-mentioned Alibaba report, of the 10 most active cities in terms of night consumption, nine were in the south. Beijing was the only northern city that made it to the top 10. It is believed the north-south imbalance is likely the result of differences in economic development, weather and consumption habits.

Development strategies for night-time economy

Our experts highlight the following strategies regarding the development of the night-time economy: improve urban management; increase the diversity of consumption scenes; add experiential and social elements; and enrich the content.

First, local authorities should prioritize better urban management and strike a balance between developing the night-time economy and maintaining safety and social order. It should

provide more night-time transportation, extend the operating hours of hospitals and clinics, and implement safety and environmental protection measures so that consumers will find it both convenient and safe to travel at night. Furthermore, sanitation may be a concern for night markets that offer street food in an open area. Local authorities could consider opening more indoor markets or organize clean and attractive “late-night canteens”.

Secondly, city planners and property developers should ride on the strengths and uniqueness of their cities and provide a wider range of consumption scenes and services that appeal to both international and domestic visitors, including conservative customers and “trend followers” as well as mass and niche markets. They are advised to take reference from the night-time economy models adopted by global, metropolitan cities such as London and New York.

Thirdly, authorities and corporations should revitalize existing space by introducing new retail formats and adding more experiential and social elements. City dwellers, having spent a whole day at work, may well look for a variety of social and leisure activities. In this case, bars with live bands, beer-brewing restaurants, escape rooms, theaters, e-sports halls and immersive experiential shopping are among options that could suit their needs.

Finally, local authorities and developers are advised to continue enriching the content of the night-time economy, such as organizing drama shows, musicals, art exhibitions, fashion shows, opening late-night canteens and 24-hour bookstores. In one case, Hopson One, among Beijing’s most popular shopping malls, opened a late-night canteen in May 2019. It decorated its 20,000 square meters underground food and beverage area to replicate the narrow, stone-paved streets of an old town. The mall planned to turn this into a theatre by adding a variety of events, including street dance, music DJs and interactive activities for night-time entertainment.

03

Services consumption continues to boom; catering industry thrives and enters a smart new era



In recent years, domestic consumption has been a major contributor to China's economic growth, with services consumption now a hot spot for new growth. As increasing numbers of Chinese consumers turn inexorably to more services, sectors including catering, travel, housekeeping and others continue to expand and grow at a stellar pace. Driven by stronger domestic demand and ongoing consumption upgrading, China's services sector has made great strides in terms of the variety and range of services offered; these services are introducing a new consumption era in the country.



For the future, the services sector will continue to be a major powerhouse sustaining China's economic growth, while services consumption will become a new force driving the country's economic transformation. Rising residential incomes, ongoing consumption upgrading and strong government support for services consumption will continue to fuel the rapid growth of the services sector.

Guo Xinmei, Professor, Department of Economics, Beijing Technology and Business University

Services consumption maintains strong growth momentum

China's services consumption plays an increasingly important part in driving ongoing consumption upgrading, of particular significance in meeting its people's ever-growing needs for a better life, building a new economic growth engine and achieving higher-quality overall development.

In 1H19, domestic consumption of goods and services continued strong momentum, underpinning the robust growth of the consumer market. According to the National Bureau of Statistics of the PRC, domestic consumption contributed 60.1% to national economic growth, among which, catering, entertainment, travel, education, seniors' healthcare, housekeeping and other related-services consumption accounted for 49.4% of the country's total consumer spending, 0.6 ppt higher than in 1H18. In fact, services sector value-added contributed 52.2% of China's GDP, with services businesses covering information, education, senior care, healthcare, culture and others delivering rapid growth and forming bright spots in economic development.

The China Development Research Foundation revealed that before China achieved GDP per capital (at purchasing power parity) of US\$25,000, services consumption such as tourism, hospitality and catering, financial services, insurance, culture, sports and entertainment services – as well as other residential-oriented services – would take up an increasing proportion of consumer spending, while goods

consumption such as for food and clothing would decline. It follows that services consumption is set to be the major driver of overall consumption growth for the future.

The rapid growth of services consumption in China is driven primarily by the following factors:

- **Rising residential incomes and ongoing consumption upgrading.** With rising incomes and higher spending power, Chinese consumers increasingly demand better quality, personalized and diversified products and services, as well as new modes of consumption such as online shopping, customization, experiential consumption and smart retailing. These emerging consumption trends are also in line with the country's policies to drive a new era of development, structural changes in the consumption market and transformation towards stable and high-quality growth.
- **Strong government support for services consumption.** In recent years, the government has committed support for services sector development. The country's annual Central Economic Work Conference held 19-21 December 2018 introduced initiatives and policies to step up the development of services businesses in education, childcare, senior care, medical, culture and travel. And in October 2018, the General Office of the State Council issued the *Implementation Plan for Improving the Mechanism to Boost Consumption (2018-2020)*, highlighting further easing market access in the services sector to stimulate related consumption as one of the government's main

targets. The government has also announced further refinement of supporting policies for services businesses in housing and leases, housekeeping, senior care and childcare; accelerating the development of rural e-commerce and exploring the consumption potential of rural tourism; and removing investment thresholds in culture, sports and other related fields. The country's renewed progress in supply-side structural reform will also help promote more mature development of different consumer segments and increase the supply of quality services in the market.

Digital transformation accelerates in catering industry

The advent of the 5G communication era and introduction of new digital technologies have combined with ongoing consumption upgrading to drive digital transformation in services businesses. This is particularly the case in the catering industry which has actively undergone business format innovation, while expanding product and services offerings. Wider access to the Internet and smart technologies also enable catering market players to develop new services models that leverage resources from multiple channels, allowing customers to order online and then pick up or enjoy their meals in-store; manpower is replaced with state-of-the-art technologies while this trend encourages the launch of smart and unmanned restaurants.

As a case in point, in July 2018, Alibaba launched its first highly automated restaurant called Robot.he within one of its Freshippo supermarkets in Shanghai. The new robot-enhanced restaurant draws on advanced digital tools including the Hema app, QR codes and robots to create a futuristic dining experience – the Hema app

shows customers where to sit in the restaurant and is used to scan QR codes for browsing the menu, ordering food and making payments; customers can buy fresh produce from the Freshippo supermarket which is then delivered to the kitchen via ceiling-mounted conveyor belts; once the food is cooked, small box-like robots, acting like self-driving cars on roads, travel along tracks to deliver the food direct to customers' dining tables. Another robot collects the dishes and returns them to the kitchen for cleaning. Another example is JD.com's first fully robotically-run restaurant, XCAfe. The restaurant, launched in Tianjin in November 2018, adopts robotics and artificial intelligence-powered technologies in the entire restaurant operation, from ordering, preparing, cooking, plating to serving; after customers place orders, robots in the kitchen are assigned the orders and begin preparing dishes. After food preparation, a different set of 'server' robots then deliver the plates to the dining areas for customers to pick up.

With the increasing prevalence of smart devices and rapid growth of the so-called "lazy economy", more and more people are turning to smartphones to address most of their daily needs. Rising Internet penetration in the catering industry and growing influence of the Internet on consumers' buying behaviors have made going online a key trend. In 2018, the total number of Internet users in China reached 830 million with 820 million using mobile devices -- representing 98.6%, a sharp increase from 75% in 2012. Local consulting group iResearch projected that by 2021, all Internet users in China will go online using mobile devices. This is set to further facilitate the growth of online-to-offline (O2O) catering, providing customers with on-demand and convenient food delivery services.





What the Experts say

Services consumption becomes a new force driving economic growth

Following more than three decades of rapid growth, China's economy is becoming more consumption-driven and service-oriented. Our experts believe the burgeoning middle-class, in particular, will play a critical role in driving services consumption growth in the coming year. Currently, China has over 400 million middle-income earners. With increasing income levels seen as one of the major drivers of services consumption, the government is striving to deepen reform of the income distribution system in a bid to increase lower-paid group incomes while expanding the size of middle-income earners. Such initiatives are expected to further unleash the potential of domestic consumption and fuel demand for quality services in travel, culture, sports, healthcare, senior care, education and other sectors. Moreover, the ongoing consumption trends towards personalized, diversified and quality products and services will further unleash massive services consumption opportunities in 2020.

For the future, the services sector will continue to be a major powerhouse sustaining China's economic growth, while services consumption will become a new force driving the country's economic transformation.

Digital transformation speeds up modernization of the catering sector; pursuing high-quality growth is key

Technology advancement is driving change and growth in the catering industry. From concierge robots, service robots and smart cooking machines to facial recognition technology and automated restaurants, new advances have greatly facilitated digital upgrading and transformation in the industry. Our experts expect that new technologies, better service experiences, intelligentization and digitalization will become the factors shaping the future development of the catering industry, while mobile technology, automation and smart stores will become key pillars leading further digital transformation. All these are set to speed up the catering industry's modernization and shift towards high-quality growth.

While China's catering industry is moving towards high-quality development, it is important for market players to enhance food safety and focus more on providing healthier food options, while better adapting to local communities' growing demand for personalized, diversified and made-to-order food services. Restaurants that feature local and specialized cuisines and are able to respond to changing customers' needs are expected to see the fastest development.

04

Transformation of consumer market and circulation sector accelerates; creates a stronger domestic market



China's consumer market has maintained solid growth momentum in recent years, signalling its key role in facilitating the country's high-quality economic growth and pushing forward supply-side structural reform. "Creating a stronger domestic market" is a priority for China's economy and a major theme highlighted in the country's annual Central Economic Work Conference held 19-21 December 2018. Since then, the government has unveiled a number of measures to boost domestic consumption and increase investment on a rational basis.

Meanwhile, with ongoing consumption upgrading in China, commercial enterprises are making vigorous efforts to transform and innovate. Some companies are actively tapping lower-tier cities and rural markets – which are set to be the major drivers of growth in China over the next decade, while others are enhancing high value-added offerings such as carrying out product innovation, developing and nurturing brands.



China's determination to create a strong domestic market marks an important step for the country to achieve sustainable economic growth, while providing the needed impetus for business growth. This is important amid mounting uncertainties in the global market.

Wang Xiaodong, Professor and Dean, Department of Trade Economics, Renmin University of China

Government unveils new measures to boost consumption

In 2019, China unveiled a series of measures to boost consumer spending, as part of its initiative to expand the domestic market. In March 2019, the General Office of the State Council released a notice to adjust the working/ non-working days for the Labor Day Holiday, enabling companies and schools to enjoy an extended four-day break beginning 1 May 2019. Later, in August 2019, the State Council listed 20 measures to help improve domestic consumption, from relaxing/ eliminating restrictions in car purchases to encouraging the development of the night-time economy and developing community retailing to renovating pedestrian shopping streets. These measures aim to balance and optimize supply and demand in the commercial sector, while adding various experiential and technological elements to enhance service quality and attract more customers.

The development of the night-time economy is an example; the government has encouraged businesses and local governments to stimulate night-time consumption by turning night markets into food, shopping, entertainment, sports, tourism, exhibition and performance venues. Additionally, the development of community retailing leverages the advantages of "Internet plus" to provide a variety of quick and convenient services to neighborhood residents. Meanwhile, in August 2019, the General Office of the Ministry of Commerce published the *Standards for Renovation and Upgrading of Pedestrian Shopping Streets (2019)*, highlighting the specific requirements for renovating pedestrian shopping streets, such as improving transportation, enhancing

facilities, expanding retail formats, enhancing consumption scenarios, providing smart services and launching a variety of other activities.

Circulation sector steps up efforts to transform and innovate

Tapping lower-tier cities and rural markets; further rolling out omni-channel strategies

With rising incomes and improved accessibility, lower-tier cities and rural markets are poised to be key drivers of China's consumption growth. Increasing numbers of leading retailers and e-commerce operators are actively tapping the smaller cities and rural areas. Alibaba's initiative provides such a case. In 2019, the company gave unprecedented priority to Juhuasuan, its group-buying and flash-sale platform, repositioning this as the top destination for consumers from smaller cities and townships. Alibaba also hosted the "99 Juhuasuan Shopping Festival", a 10-day shopping event from 1 September 2019, offering deep discounts for one million items of merchandise and giving out cash dividends, coupons and other incentives. Similarly, JD.com's group-buying platform JD Pinguo (rebranded as JD Jingxi in September 2019) recorded strong sales for JD.com's "618 Shopping Festival", with tier-2 and below cities particularly showing outstanding performances. Additionally, Suning.com is leveraging its smart retail platform Retail Cloud with its technology, logistics and supply chain capabilities to provide support for small- and micro- companies in towns and counties.

Introducing new business models and retail formats

To cope with the ever-changing retail environment and better satisfy new customer needs, many commercial enterprises are stepping up efforts to reinvent their businesses and introduce innovative business models. For instance, more and more companies are engaging in social commerce. They hire popular Internet key opinion leaders (KOLs) to market and sell their products. Some companies are setting up intellectual property (IP) stores and pop-up stores to cater to consumers' growing demand for constant innovation, while others are tapping the "singles economy" – an increasingly rising trend in China – by offering more single people-friendly products and services. Moreover, the concept of the "first store" economy is trending. Recently, some global brands set up their first stores in China and have generated widespread interest among Chinese consumers.

Developing private labels

With consumers increasingly searching for high-quality and value-for-money products, foreign retailers including Walmart, Carrefour and 7-Eleven as well as domestic retail and e-commerce operators such as Yonghui Superstores, Better Life Group, JD.com and

Suning.com are making robust efforts to launch their particular private labels. In a cooperative mode, China Ants Alliance, a voluntary chain store association comprising over 30 chain store members, has developed nearly 30 private label products under three product categories, namely food, paper and cleaning products. Many of these retail chain stores reportedly took an active role in product development and dealt directly with suppliers and manufacturers, thereby strengthening supplier-retailer relationships.

Seeking M&A opportunities

In 2019, horizontal mergers and acquisitions (M&A) activities between retailers became more frequent. Differing from the past was the fact that – instead of acquisitions of local companies by foreign brands – many acquisitions were in the form of partnerships, underlining the growing strength of local players. Some notable examples include Wumei Technology Group's acquisition of Metro China and Suning.com's acquisition of an 80% stake in Carrefour China. Similarly, earlier mega deals such as Alibaba's strategic investment in Sun Art Retail Group – the parent company of RT-Mart and Auchan – and the strategic partnership between JD.com and Walmart, show the transactional alliances that retailers are keen to forge with other companies to achieve successful outcomes.





What the Experts say

Against the backdrop of growing protectionism and the increasingly complicated global environment due in part to the trade tension between China and the U.S. and the Brexit uncertainty between the U.K. and the E.U., China's determination to create a strong domestic market marks an important step for the country to achieve sustainable economic growth, while providing the needed impetus for business growth.

Since China has become one of the world's largest economic powers it is therefore a major driving force for global economic growth. Many foreign companies are setting their sights on China's vast domestic market and exploring various ways to tap the market. The second annual China International Import Expo (CIIE), for example, provides an excellent platform to connect foreign businesses with the China market. The CIIE has attracted many foreign companies, including Fortune 500 companies, to exhibit their latest products – from consumer products to healthcare equipment to heavy machinery – and demonstrate their capabilities.

Our experts believe China's circulation sector will continue to play a critical role in the growth of the domestic market. With increasing numbers of consumers pursuing a better quality of life, our experts urge commercial enterprises to step up their transformational efforts, and provide more high-quality, diverse products and services to meet ever higher consumer preferences.

05

Innovative retail formats and new business models become evident, capturing diverse and fast-changing consumer demands



China's new consumers –called “Generation Z”, and born between the mid-1990s and the early 2000s – are powering the retail market. Their distinctive consumption behavior, shopping habits and spending attitudes set them apart from their predecessors. To capture the needs of these new, young consumers, retailers and brands are actively exploring new retail concepts and practices, while adopting innovative business models such as exploring an ever-growing number of e-commerce channels, launching pop-up stores, tapping the singles' economy, penetrating local community preferences, and leveraging the so-called “first-store” economy to rejuvenate local retail markets.





Innovative retail formats and retail practices, as well as new business models will continue to emerge in 2020. Enterprises should maximize the synergies between existing and new businesses, in terms of resource allocation and operations so that they can complement each other and improve operational efficiencies.

Guo Yujin, Deputy Secretary General, China Chain Store & Franchise Association

Fast growth of new e-commerce channels: Social commerce sees explosive growth

Generation Z consumers, who are mobile-centric and socially fluid, demand more convenient ways of shopping than older generations. Their demands have prompted e-commerce players to evolve and launch new e-commerce channels to engage with them. In particular, social commerce – the use of social networks to drive e-commerce sales – is transforming direct-to-consumer transactions and the e-commerce experience. The rapid growth of social media apps, especially Mini Programs, along with the sheer amount of time spent by people – especially younger generations – on social media apps is set to fuel the growth of social commerce for years to come. As stated in a report by the Internet Society of China, more than 500 million people shopped on social commerce platforms in 2019. China's social commerce market is estimated to rise to 2,419.4 billion yuan in transaction valuation in 2022, from 547.4 billion yuan in 2018, according to iiMedia Research.

Mini Programs increasingly become an effective selling channel

Mini Programs are light-weight apps that function within another app, allowing users to open these and leave them easily, without having to install or uninstall an app. Tencent pioneered and proliferated Mini Programs in China. The WeChat Mini Program is increasingly being viewed as an effective channel for companies to capture new customers and carry out e-commerce business. According to Tencent, WeChat Mini Programs have over 300 million daily active users (DAUs). Following the success of these WeChat Mini Programs, other Internet companies and e-commerce players including Baidu, Alipay, Toutiao, Douyin and Meituan have also launched their individual Mini Programs to drive customer engagement and facilitate e-commerce sales. In one case, short video platform Douyin allowed merchants to add a Mini Program to their official

accounts : viewers can access merchants' e-commerce websites through the Mini Program while watching livestreaming videos. This provides much valued shopping convenience as consumers can purchase products without having to exit the underlying app.

Live-streamed shopping becomes prevalent

Recently, live-streamed shopping, particularly through short video platforms, has dominated the e-commerce space. Increasing numbers of brands and retailers in China hire social media influencers, or commonly known as Internet key opinion leaders (KOLs) to host broadcasts through live-streaming or short video platforms. Internet KOLs usually video themselves modeling and recommending clothes or other goods, and viewers can then purchase the items immediately from an embedded link. Examples of such popular short video streaming platforms include Douyin and Kuaishou – the former has over 320 million DAUs as of July 2019, while the latter has over 200 million DAUs as of May 2019. Some brands and retailers are leveraging these platforms' large online traffic to expand their reach in lower-tier cities. One example is Suning.com. In August 2019, Suning.com announced that Kuaishou's users could shop on its website while viewing live-streaming videos on the Kuaishou app. According to third party statistics, 54% of Kuaishou users come from tier-3 or lower-tier cities. Having direct access from Kuaishou can therefore facilitate Suning.com to penetrate lower-tier cities, which are set to be the key engine for consumption growth over the coming years.

Pop-up stores and IP theme stores or events gain in popularity, becoming effective marketing strategies

Pop-up stores continue to proliferate

Pop-up stores have become a popular distribution channel over recent years. Increasing numbers of domestic and overseas brands – and even e-commerce players – have opened pop-up stores backed by

state-of-the-art technologies, innovative marketing content as well as experiential elements to promote their products and enhance brand awareness. In April 2019, Chanel opened a beauty pop-up store in Guangzhou featuring an 1980s disco theme. The pop-up store, named “Coco Flash Club”, featured different zones, such as Mademoiselle’s Dressing Room, Jukebox and Rouge Coco Flash Lipsticks corner, while Scent bar provides exclusive cocktails inspired by Chanel’s fragrance collections; the aim is to promote Chanel’s latest beauty collections, while delivering an exciting customer experience. In June 2019, Matsushita’s Panasonic Beauty collaborated with JD.com to launch a pop-up store in Beijing to promote its new Panasonic Beauty X Series. The store not only showcases Panasonic Beauty’s latest products and technologies, but also encourages consumers to shop on JD.com.

Some industry experts warn that brands and retailers need to be rational when launching pop-up stores, as there is a fear that opening too many such stores could overstretch operational costs. Operators need to assess the efficiency of the pop-up store in converting customer traffic to actual sales. Some experts say that brands and retailers should consider using pop-up stores to sell off-price products and clear inventories, a common practice by retailers in Europe.

IP theme stores or events flourish in China

Recently, increasing numbers of retailers in China have worked with different intellectual property (IP) characters, cartoon and animation production companies or brands, aiming to open theme stores or launch IP character exhibitions. Similar to pop-up stores, these stores or exhibitions leverage content, entertainment, social opportunities and unique consumption scenes to connect with customers. Shanghai New World Daimaru launched its first Captain Tsubasa exhibition in China in summer 2019. Captain Tsubasa is a renowned Japanese football comic series originally created in 1981 and is one of the most popular IP characters in Japan, China and many other countries. The exhibition was a great success; it attracted large numbers of visitors from the Yangtze River Delta region and other inland regions to attend. Other examples of IP theme exhibitions that have attracted widespread attention include Beijing Xidan Joy City’s collaboration with Popeye the Sailor in launching an exhibition during June 2019 to celebrate its 90th anniversary and it also launched the Garfield Summer Fiesta exhibition at Guangzhou International Grand City. These IP character marketing events were able to help retailers create brand awareness and prolong the time

customers spend in-store, as well as assist retailers to establish their uniqueness and differentiate themselves from their peers.

Tapping the growing singles’ economy

The population of single people in China is rising rapidly amid a growing trend for delaying or opting out of marriage. According to the National Bureau of Statistics of the PRC, the population of single people in China has exceeded 220 million. This demographic shift is bringing huge business opportunities for retailers and services providers. To tap the potential of the rising singles’ economy, some commercial enterprises have launched different goods and services to target the singles population – from hot pot dishes for one person in the catering sector to mini Karaoke boxes in entertainment to single travel services and to smaller home appliances for single person apartments. According to data from Tmall, the sales of mini microwave ovens and mini washing machines increased by 980% yoy and 630% yoy, respectively in November 2018. Some companies have revamped store formats and adjusted their merchandise mix to cater to singles demands for high-quality, customized products and services, as well as unique shopping experiences.

Developing new consumption scenes for community retailing

Community retailing has seen rapid development in China over recent years and has become a major focus for commercial enterprises. Some retailers have proactively launched new retail formats, such as one-stop community centers that integrate retailing with lifestyle and public services, aiming to cater to the daily needs of local communities and to provide convenience to nearby residents. In July 2019, Rainbow Department Store launched its first community center which provides retailing and catering services, as well as other daily life-related services, facilities and community activities. Chang’an Shopping Mall in Beijing has also announced that it will transform its original department store into a lifestyle services-oriented center and outlet; the new mall is scheduled to re-open for Spring 2020.

Other retailers have launched smaller-format stores in communities – particularly small-scale fresh food supermarkets with a typical store size of around 300-500 sqm – to provide shopping convenience for residents. Some of these stores also serve as warehouses for online orders and provide quick home deliveries – usually within 30 minutes. Yonghui Superstores has opened around 400 Yonghui Mini

stores as of June 2019 as a supplement to its major hypermarket business. Alibaba's Freshippo supermarket chain (commonly known as Hema supermarkets) opened three Hema Mini stores in Shanghai from June to September 2019, targeting mainly small families in communities. Freshippo aims to open more Hema Mini stores for the future in lower-tier cities, especially in those rural areas without large Freshippo stores.

Some industry insiders believe that smaller-format stores not only act as a supplementary retail format for larger stores, but also provide a totally differentiated consumption scene for individual consumers and groups. Moreover, some smaller-format stores also serve as pick-up points in communities; this helps reduce logistics and delivery costs. The lower investment costs for small-sized stores enable them to achieve higher same-store efficiencies than larger-sized stores. That said, to stay relevant in the market, retailers need to strengthen their positioning in the community and differentiate themselves from other similar small retail formats.

“First-store” economy becomes a new consumption driver for local markets

Recently, the term “first-store” economy has created considerable interest in China. The “first-store” economy refers to when a specific area, city or region uses its competitive advantages to attract global or domestic

brands to open their first flagship stores there, bringing in foot traffic, unleashing consumer spending and boosting growth in the area or region. Shanghai, Beijing and Chengdu are seen as particularly attractive for brands to set up their first stores. Local real estate consultancy firm RET reported that 589 retailers opened their first stores in Shanghai in 2018; 328 retailers opened their first stores in Beijing in 1H19; and 371 retailers opened their first stores in Chengdu in 1-3Q19.

It is worth noting that the “first store” is usually of a unique nature, and is capable of promoting retail innovation, demonstrating new technologies, offering new experiences, and catering to new consumer demands. In August 2019, Costco opened its first China store in Shanghai and drew large crowds of visiting shoppers. Its unique business model also provided insights for retailers hoping to tap the membership store sector.

Meanwhile, some cities that have distinctive, sectoral or industrial advantages can attract companies to open their first stores. To illustrate this, Hangzhou, being a world-recognized technology hub, has attracted several Internet companies to open their first offline stores in the city. Alibaba opened its “Tao Style” specialty store in the city in March 2019 and NetEase opened its “NetEase Kaola Flagship Store” in January 2019. This has further strengthened Hangzhou's position as an “Internet city” and facilitated its technology cluster.



What the Experts say

Our experts believe that innovative retail formats and retail practices, as well as new business models will continue to emerge in 2020. Companies must pay close attention to the evolving market landscape and fast-changing consumer behaviors, adjusting to cater to new consumer demands. At the same time, enterprises also need to constantly examine their internal operations to ensure they have the capital and talent to carry out innovative business transformations. Finally, enterprises should maximize the synergies between existing and new businesses, in terms of resource allocation and operations so that they can complement each other and improve operational efficiencies.

06

Digitalization becomes the “new normal”; a revolution in the circulation industry facilitates reconstruction of production processes



In 2019, digitalization has become the battlefield in the business arena, especially embracing retail and innovation. Having tasted the initial advantages brought by the digital economy and big data analysis, enterprises are more determined to embrace digitalization and technology innovation. However, as consumers become increasingly wary of the hyperbole surrounding new consumption scenes as well as questionable retail formats and market copycats, some enterprises have started to pursue more intensive, provable digital transformation. In particular, retailers and other customer-facing enterprises have the advantage of collecting first-hand consumption data and practically-grounded market intelligence; they utilize big data to perform predictive analytics and generate forward-looking insights. Alibaba, JD.com and Suning are among the enterprises that have employed digital tools and technologies to develop algorithms and advanced analytics while building powerful data platforms.

Digitalization on the retail side is also able to drive digital and technological upgrades in the upstream. It will first set off to revamp the wholesaling system, then accelerate digitalization in factories and logistics companies, and finally revolutionize the entire circulation industry. In the longer term, digitalization is becoming the “new normal” in the commercial sector. This will not only enhance distribution efficiency and productivity but will also reshape the processes of production.



In today's demand-driven era, digitalization in the circulation industry is expected to drive the adoption of smart manufacturing. This will not only enhance distribution efficiency and productivity but will also reshape the processes of production.

Ding Junfai, Former Vice Chairman and Research Fellow, China Federation of Logistics & Purchasing

Key digitalization trends for 2020

Digitalization is set to remain a key theme for China's commercial sector. Our experts foresee a number of trends for 2020.

Big data analytics further optimize inventory management

Increasing numbers of retailers and e-commerce platforms will leverage data analytical tools, comprehensive communication networks and information systems to optimize targeted marketing and inventory forecasting. In fact, inventory management has long been a "pain point" for retailers. Traditional retail businesses used to rely on experienced merchandisers to make market forecasts and procurement decisions. With the advent of big data analytics and information tools, retailers can identify potential consumers more precisely, analyze previous procurement and sales figures, make accurate estimations and minimize unsold inventory. Alibaba's LST (Ling Shou Tong) platform helps over a million small retailers to 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.

Digitalized information systems enhance connectivity in franchising systems

Digitalized information systems could enhance connectivity and accelerate the expansion of retail chain. Due to geographical barriers, retail franchisors find it difficult to synchronize with their franchisees. Through digital price tags, distance monitoring, data sharing and membership profiling, as well as other technological support, franchisors can disseminate information quickly to franchisees, improving the unity of store image and products. Franchisees can retain some flexibility and make management decisions according to the local consumption environment. This would attract more franchisees to businesses and fuel offline expansion. Take Jiuxian, a B2C (business-to-customer) e-commerce operator that sells imported and China-sourced wine, as an example. The company has been actively expanding its offline presence in recent years; it adopts an online-to-offline (O2O) business model which directs its online clients to wine tastings and pickup in offline stores. With digitalized information systems, Jiuxian is able to recruit many franchisees to cope with its rapid offline expansion plan while at the same time maintaining the quality and authenticity of its liquor products across all franchised shops. It was reported that Jiuxian opened 500 and 1,000 new shops in 2018 and 2019 respectively while aiming to operate over 10,000 shops in five years.

Digitalization facilitates the development of private labels

Digitalization enables seamless upstream-downstream connectivity and shortens the process from factory to consumer, making it easier for retailers to develop private labels and offer distinctive products. In the past few years, increasing numbers of retailers and e-commerce operators have launched their own private brands or set up self-operated platforms: Suning.com created Suning Jiwu, JD.com founded Jingxuan and Jingzao and Alibaba launched Taobao Xinxuan. Alibaba's Freshippo supermarket even implemented a three-tier private label strategy, 'Blue label' for everyday goods, 'Emperor Xian' and 'Gold Standard' for premium offerings, and 'Black Label' for rare or unique goods. With digitized supply chains in place, these companies can share real-time consumer insights with manufacturers and their factories, ensuring they produce what consumers want. Moreover, with greater control over product design and supply chains, retailers and e-commerce operators can offer high quality goods at lower prices. Private labels help promote stronger customer recognition as well as loyalty and pursuit of profitable growth. This trend is expected to continue into 2020.





What the Experts say

Having witnessed the transformational effect of retail brought by digitalization, our experts believe that digitalization will spark yet another transformative cycle in wholesale and logistics, eventually deepening the reform and upgrading of the circulation industry. The extensive use of technologies and improved synergies throughout the supply chain will definitely accelerate the process. Meanwhile, the government has put more focus on promoting digitalization in commercial industry and launched major supportive policies over recent years. For instance, the General Office of the State Council issued the *Opinions on Accelerating the Development of the Circulation Industry to Boost Consumption in August 2019 and the Opinions on Promoting Collaborative Development of E-Commerce and Courier Logistics Business* in January 2018. The Ministry of Commerce has also published relevant policies and provided further guidance regarding digitalization in the circulation industry.

Our experts maintain that digital technologies have empowered retailers to take up some of the functions of wholesalers. As retailers receive real-time consumer data, they can synchronize these with manufacturing data on their digital platforms and initiate timely sales and marketing decisions. Digitalization is set to further drive the integration of retailers and wholesalers while redefining their roles in supply chains.

In today's demand-driven era, our experts further foresee digitalization in the circulation industry driving the adoption of smart manufacturing. Increasing numbers of retailers now use digitized

supply chains which can incorporate real-time sales data into product design and production. This facilitates the development of an agile and smart manufacturing system that can support quick prototyping, design and testing, as well as fast iteration. As customization and personalization have become the dominant retail trends, factories need to develop digitalized capabilities around data mining, predictive analytics, task modularization, material and process planning as well as product life cycle management to improve production efficiencies. Smart factories will have a much higher chance of thriving in this new retail era.

Finally, our experts warn that digitalization is a double-edged sword. On the one hand it eliminates labor-intensive jobs and creates mass unemployment but on the other hand, it generates new job opportunities in relation to e-commerce, online trading, supply chain management and logistics. Nonetheless, it is believed that the benefits of digitalization outweigh the disadvantages. Our experts cite the fact that the launch of some agricultural e-commerce platforms facilitated the distribution of agricultural products from rural to urban areas, while generating additional incomes for poverty-stricken villages. Some e-commerce operators have also provided technological know-how and channels for low-income individuals to start their own businesses. Although digitalization has its risks and challenges, it is inevitable and indispensable for China to embark on a digital transformation journey to sustain economic growth and boost consumption upgrading.

07

Renovation of pedestrian streets facilitates consumption upgrading; trend for coordinated development between commerce, tourism and cultural businesses



A city is usually associated with one or more of its most famous commercial or shopping streets which best represent its level of prosperity and character. A well-designed commercial or shopping street usually boasts a range of commercial businesses that can address different customer needs as well as facilitate consumption upgrading, uplift the city's image and drive economic growth.

Since the economic reforms of 1978, China's pedestrian commercial streets (or pedestrian streets) have experienced two separate waves of development. The first took place amid large-scale and rapid urbanization in 1999 and the second against the background of the global financial crisis in 2008-2009. With state-led measures in place, our experts expect to see another wave of pedestrian street renovations and upgrading in 2020.

That said, there remain several issues with pedestrian street development in China. A major problem is the imbalance of development between coastal and interior regions. While some tier-1 cities feature a number of well-developed, globally renowned pedestrian streets, many cities have no well-developed pedestrian streets for shopping or other activities. Some city planners are either not aware of, or have paid little attention to, the role of pedestrian streets in shaping a city's image and promoting its quality of life. The government has needed to take the lead in developing pedestrian streets across the country.



Pedestrian street renovation work will accelerate in 2020 and the trend for coordinated development between commerce, tourism and cultural businesses will become more prominent. Pedestrian streets can become city landmarks while also boosting consumption upgrading and facilitating commercial sector transformation.

Han Jianhui, Director, China Pedestrian Street Working Committee, China Federation of Urban Commercial Outlets Construction Administration

Government policies to promote renovation and upgrading of pedestrian streets

In recent years, the government has indeed stepped up support for the development of pedestrian streets. In December 2018, the Ministry of Commerce (MOFCOM) published the *Notice on Carrying out Renovation and Upgrading of Pedestrian Streets*, proposing to develop a number of world-class pedestrian streets. The Notice also confirms the government's decision to commence a pilot project to renovate and upgrade the first batch of 11 pedestrian streets, such as Wangfujing pedestrian street in Beijing, Nanjing Road in Shanghai, Jiefangbei pedestrian street in Chongqing, Kuanzhai Alley in Chengdu and Hubin Road in Hangzhou. The first phase of renovation work on these pedestrian streets was carried out in 2019, with some positive results. Statistics from the MOFCOM revealed that in the first half year of 2019, these 11 pedestrian streets recorded 450 million visitors and 61.2 million yuan in sales, up 19.9% yoy and 12.6% yoy, respectively.

In August 2019, the MOFCOM published a more detailed proposal, the Plan for Promoting the Renovation and Upgrading of Pedestrian Streets, which states clearly its goal to develop between 30 and 50 demonstrative pedestrian streets in municipalities and capital cities across the country and achieve a 30% increment in visitor traffic and sales within three years. In the same month, the General Office of the State Council issued the *Opinions on Accelerating the Development of the Circulation Industry to Boost Consumption*, providing

further directions for local governments regarding the upgrading of pedestrian streets. The Opinions encourage local governments to provide support in infrastructure, transportation, information exchange and social credit ratings so that the quality and management efficiency of pedestrian streets can be improved. The government will also expand the scope of the pedestrian streets' pilot project.

While the list of the second batch of pedestrian streets has yet to be released, some local governments have already announced sending staff training and reserve budgets to upgrade transportation infrastructure, security measures, public facilities, roads and lightings on pedestrian streets in 2020.

Cross-sector integration facilitates coordinated development of pedestrian commercial streets

Some pedestrian streets in China have recently shifted to a development model which focuses on the integrated development of commerce, tourism and culture-related businesses. Many industry experts believe these industries can complement each other, enabling them to achieve synergies and enhance efficiency. Cross-sector integration can also make pedestrian streets more vibrant with a variety of shopping, dining and cultural elements; the upgrading of streets, attracting more businesses (to set up stores) and customers (to shop and spend time) may also be further facilitated. Renovation and upgrading of Hubin Street in Hangzhou provides a good illustration.

Case study: Hubin Street in Hangzhou

Hubin Street is located at the heart of the central business district of Hangzhou, a city that has a rich history and culture, and houses the global headquarters of Alibaba. The street has maintained annual through-traffic of 50 million people and a 10% growth in total retail sales of consumer goods for the past five consecutive years. In the hope of becoming the Chinese version of the renowned Avenue des Champs-Élysées in Paris, five months of renovation work has been carried out on Hubin Street in 2019. The work was completed in time for China's National Day golden week beginning 1 October 2019.

The renovation of Hubin Street has driven an upgrade of businesses there. Of the total 257 shops on the street, two-thirds underwent store revamps and upgraded business operations and services. For instance, a traditional dim sum shop revamped its storefront and interior by featuring South Song Dynasty decorations. The shop had been making between 40,000 and

50,000 yuan in daily sales in 2018 but sales have risen by between 20% to 30% following renovation and reached 100,000 yuan during the 2019 National Day holiday. Additionally, the Lianhua chain supermarket on Hubin Street took the chance to upgrade both its hardware and software. It allocated part of the store for a new catering business in which young people can put on ancient costumes, enjoy tea and do live-streaming on social media. Lianhua equipped its store with self-checkout kiosks, omni-channel services and a traffic tracking management system powered by Internet of Things (IoT) and artificial intelligence technologies. Other neighboring stores also added new retail elements or made efforts to provide better shopping experiences.

The renovation exercise has allowed Hubin Street to successfully attract several brands to set up their first stores there, including the Nio Automobile and Kaola's offline flagship store, Netease Yanxuan's offline store, as well as the new retail partners of the Yangtze Delta Region Institute of Tsinghua University.





What the Experts say

Our experts maintain that city planners need to have a thorough understanding of the strengths and characteristics of their cities before deciding on development plans for their pedestrian streets. Plans should balance the needs of mass and niche markets, offer both daytime and night-time attractions as well as satisfy local and international tastes. Our experts also highlight the need to integrate commerce, tourism and culture into the development of pedestrian streets and to promote cross-sector cooperation and interaction. They urge businesses to tap the emerging markets presented by women, families and kids as well as the elderly to offer a diversity of services tailored to all these consumer groups.

A good pedestrian street should provide sufficient open space for walking and physical activities. At the same time, it should be easily accessible by car and public transportation in order to draw consumer traffic. Therefore, it is important to build sufficient parking spaces near pedestrian streets and connect them with the transportation network. Our experts believe that it is not necessary for pedestrian streets to follow a traditional linear design. With growing traffic and sales, businesses on the main pedestrian street can naturally extend to nearby streets and alleys. The pedestrian areas can also evolve into becoming blocks or circles, with different zones and complementary functions.

To enhance the uniqueness of pedestrian streets, our experts urge urban developers to introduce new business formats and exclusive brands relevant to their streets. While large brands can draw traffic and uplift the image of these streets, emerging brands need the chance to experiment and grow. In addition, leisure and catering facilities should contain local features. Shops and facilities, along with some historic preservation and older architecture on the streets, are expected to attract more customers and generate increased foot traffic.

Finally, our experts believe that pedestrian street renovation work will accelerate in 2020 and the trend for coordinated development between commerce, tourism and cultural businesses will become more prominent. Pedestrian streets can become city landmarks while also boosting consumption upgrading and facilitating commercial sector transformation.



08

Community retailing shifts towards services; “last-100-meter” retail gains attention



Community retailing has been developing rapidly. Formerly focused primarily on product sales, this has since 2019 started to transform and upgrade towards more life-related services, particularly aiming to promote welfare and convenience for local communities.

Indeed, the development of community retailing gained unprecedented support from the government in 2019. In August, the General Office of the State Council issued the *Opinions on Accelerating the Development of the Circulation Industry to Boost Consumption*, highlighting the need for community-based services to cater to local daily needs. The Opinions also set out several specific tasks, including establishing an “Internet plus community” public services platform, creating and improving a number of public services centers, and coordinating various lifestyle services targeting residential communities such as housekeeping, elderly care, community education, healthcare and sports.

Some local governments have also stepped up efforts to support community development. As an example, in September 2019, the Department of Commerce of Jiangsu provincial government issued the *Guiding Opinions on Promoting Consumption in Communities and Facilitating the Development of Community Retail*. The Opinions highlight six major initiatives to support the growth of community retailing, namely developing retail chains, introducing more brands, developing new business models, promoting the development of new retail formats such as e-commerce, facilitating convenience consumption and strengthening the coordinated development of services businesses devoted to communities.



Community retailing is shifting towards providing more life-related services. Many government-backed community malls and neighborhood commercial districts are expected to open in different communities in the coming year. These malls and commercial districts aim to provide a full range of services for neighborhood residents.

Zeng Lingtong, Director, China Retail Human Resource Research Center

Rise of one-stop community malls, focusing on the provision of lifestyle and public services

With the support of the central and local governments, a new type of one-stop community center emerged in 2019. Sponsored or co-developed by government authorities, these centers or malls not only focus on selling products, but also emphasize the provision of lifestyle and public services. As a case in point, the country's first demonstration project for a new-style community center – “Nanjing Shanguli Neighborhood Community Center” – was launched in October 2019. Developed jointly by Qianhong Street in Qinhuai District, Nanjing city and Sushang Zhilian Technology Co., Ltd. (the operator of Su Sun Living Mall), the community center provides various public and community services, as well as community-based retail for nearby residents. During the center's construction phase, Qianhong Street proactively reached out to different government authorities and associations – the Public Security Bureau, the Ministry of Civil Affairs, the National Population and Family Planning Commission, the Ministry of Culture and Tourism, the Ministry of National Defense and China Disabled Persons' Federation – to coordinate various services businesses. Tenants (or enterprises) operating in the center are selected through open tender, and they are responsible for the long-term operation of community retailing as well as the provision of housekeeping and elderly care services. Besides offering regular services such as catering and fresh food supermarket, the community center also has a public services as well as neighborhood police and community services points to provide convenient services for residents.

A significant advantage of this type of government-private co-developed community center project is that the government can make better use of limited space to provide comprehensive public services, while enterprises can benefit from the increase in footfall generated by more residents using public services in such “community malls”. Additionally, community malls also facilitate “easy living” by offering shoppers and residents quicker and more convenient access to shopping, dining and public services.

Establishing neighborhood commercial districts: A rising trend in community retailing

Recently, some neighborhood commercial districts have emerged to provide convenient solutions to residents' diverse, everyday needs. An example is the commercial district of Zhenguo Temple North Street in Huaxiang Town, in Beijing's Fengtai District: this is the country's first demonstration project for neighborhood commercial districts to provide public services within 15 minutes from the town center. At 1,500 meters in length, Zhenguo Temple North Street houses over 160 brand stores within 1.5 square kilometers, with over 68% of space reportedly occupied by chain stores. The aim of setting up this neighborhood commercial district is not to maximize profits, but specifically to provide goods and services that can satisfy everyday needs of neighborhood residents. Apart from restaurants and convenience stores, the district also features shops that provide comprehensive services such as hairdressing and beauty salons, laundry stores and housekeeping services companies.

“Last-100-meter” retail becomes focal point: Convenience store sector in rapid growth

Convenience stores, being a key retail format to provide “last-100-meter” services, continued to grow quickly in 2019. With positive policy support from the government, convenience chain stores are actively improving services and operational excellence, pushing forward digitalization of bricks-and-mortar stores, and advancing towards ‘smart’ operations. For instance, smart convenience store operator Bianlifeng has widely adopted technologies and digital solutions to enhance efficiency. Similarly, Dmall, a third-party online-to-offline local lifestyle services platform, has launched a new Mini OS system for its partnering convenience and small-format stores.

Along with the rapid growth of convenience stores, small-format stores and store-front warehouses (designated spaces inside stores to act as warehouses) have also seen accelerated development. Recently, some supermarket and hypermarket operators have opened smaller-size stores. Freshippo supermarket is such a case. In March 2019, the company announced the introduction of four small-format stores – Hema F2, Hema Market, Hema Mini, and Hema Xiaodian. Hema F2 stores are similar to regular convenience stores and are located in office areas in major business districts; Hema Market stores are similar to Freshippo supermarkets but without catering areas, located in city community areas as well as suburban districts; Hema Mini stores, with store sizes at about 500 square meters, have opened in suburban districts and lower-tier cities; and Hema Xiaodian outlets have opened in places lacking any Freshippo supermarket, acting as store-front warehouses and offering delivery services only.





What the Experts say

While our experts agree that the new form of community retailing – especially the one-stop community centers that provide both lifestyle and public services – have done well, these can also do better in catering to the daily needs of local communities and convenience to residents, as prescribed in official policies. There are some troubling cases. In 2019, “Guoan Community”, a community project that provides various household-related and housekeeping services as well as public services through online and offline channels, allegedly encountered financial difficulties as a result of expanding too quickly. Its first offline community center was opened in Beijing in July 2015; since then, it quickly expanded to other major cities in China with over 400 centers in 2018. Many of these have reportedly been operating at a loss, leading to large numbers of closures and job cuts in 2019. Guoan Community is said to have reduced its store openings target to 150 locations in 2019 from 100,000 planned for the year.

Community retailing in the new paradigm envisages successful cooperation between government authorities and the private sector. Development of community retailing is set to continue its growth momentum in 2020 with the gradual implementation of supportive government policies, as promulgated in 2019. More government-backed community malls and neighborhood commercial districts are expected to open in different communities in the coming year. These malls and commercial districts aim to provide a full range of services for neighborhood residents.

Convenience stores are expected to maintain strong growth in 2020. They will continue to embrace digital transformation to achieve further automation and seek to extend operations beyond mainly chain operations. Small-format stores are set to further proliferate in the coming year, well-positioned as they are to meet consumers’ increasing demand for convenience, personalization and rapid services. Meanwhile, leading regional convenience store operators will step up expansion across the country with market consolidation continuing through 2020.

09

Joint efforts to promote rural e-commerce, food traceability and poverty relief lead to mutual gains



Since 2014, China's Ministry of Commerce (MOFCOM), Ministry of Finance (MOF) and the State Council's Leading Group Office of Poverty Alleviation and Development have worked closely on pilot programs to support rural e-commerce development. Following six years in this joint effort, the pilot programs have been rolled out in all of the poorest villages across the country.

Prior to the launch of the rural e-commerce pilot programs, the central government set up food traceability pilot schemes to facilitate circulation of agricultural products, including meat, vegetables and traditional Chinese medicines. From 2010, the MOFCOM and the MOF have developed food traceability pilot zones across the country and have so far established food traceability systems in 58 cities while facilitating the circulation of Chinese traditional medicines in 18 major regions. The government has developed responsive traceability systems for distributing meat and vegetables across the country. Managed by the central, provincial and municipal administrations, the blockchain-powered food traceability systems span the entire supply chain from farms to consumers. This has enabled administrations to trace the origins of meat and vegetable products from millions of farmers and distributed by hundreds of thousands of enterprises and merchants across 58 cities nationwide.

Similar traceability systems have also been set up for circulation of traditional Chinese medicines. Operated by the central and regional administrations, these traceability systems allow users to monitor and trace Chinese herbal medicines from plantation, processing, preparation, marketing to consumption, involving activities by different parties, including millions of farmers and processing workers, as well as hundreds of thousands of enterprises and merchants across 18 cities nationwide.

In 2016, the MOFCOM and the MOF stepped up their efforts in the food traceability pilot projects in Shandong, Ningxia, Shanghai and Xiamen, and expanded the pilot projects to cover fruits, aquatic products, grain, distinctive agricultural products and other categories; the move has laid a solid foundation for the coordinated development of rural e-commerce, food traceability systems and poverty relief.



Thanks to the well complemented strengths and joint efforts of government authorities, local communities and enterprises, the development of rural e-commerce and food traceability systems has made great strides over recent years in breaking down barriers as well as promoting harmony and integration among multiple parties across entire supply chains.

Liu Haifei, Research Fellow, China Research Institute of Business Economics

Backed by advanced information and electronic communication technologies, the government's food traceability pilot projects have been launched throughout the countryside. These projects have improved the supply and demand cycle for agricultural products, enhanced food safety and quality for customers, while playing an important role in poverty reduction and agricultural modernization in rural areas. Over recent years, the rapid development of rural e-commerce and food traceability pilot projects, along with the country's poverty relief program, have supported the growth of several business models that are conducive to multiple parties across the entire supply chain. Selected examples of the business models are discussed below.

Developing rural cooperatives to achieve mutual gains

Riding on the government's pilot programs in support of rural e-commerce growth and the development of food traceability systems, local authorities have set up rural cooperatives and invited leading enterprises and local villagers to join them. With extensive government support and active participation by major enterprises, the cooperatives encourage villagers to leverage natural resources such as land, crops and livestock to build their own businesses and brands. To alleviate poverty and enable greater prosperity in the countryside, these cooperatives also provide poverty alleviation subsidies and loan services to rural villagers, enabling them to convert their own resources into new sustainable incomes and move out of poverty. Ar Horqin Banner, under the administration of Chifeng city in eastern Inner Mongolia Autonomous Region, provides a good illustration of how rural cooperatives help facilitate rural sheep trading. To boost farmers' incomes, the local government has set up

traceability systems for agricultural products and helped distribute local sheep products through e-commerce platforms, while village cooperatives have provided free support and advice to impoverished sheep farmers in such areas such as sheep breeding, epidemic prevention and product processing services, as well as offered interest-free loans to sheep farmers in need of help. With the comprehensive measures carried out by local cooperatives, along with the government's poverty relief program, incomes of impoverished sheep farmers in Ar Horqin Banner have reportedly increased significantly, with each household expected to earn 30,000 yuan annually in 2019 and be poverty-free within one to two years.

Establishing whole chain traceability systems from production to consumption

Most of the traceability pilot systems set up by the government have adopted advanced tracking technologies, including Beidou (a Chinese navigation satellite system), global positioning systems (GPS) and radio-frequency identification tracking systems (RFID), video surveillance systems, temperature and humidity sensors as well as Internet of Things (IoT)- and big data-based tracking systems. The adoption of digital traceability technologies enables the development of a whole chain traceability system which can integrate all stages of production and distribution, from planting to processing to warehousing and to transportation. Such a system can enhance efficiency, transparency and accountability across the entire supply chain, while ensuring the safety and quality of foods and other products from production to consumption. Qinghai-based mutton supplier Qilian Pasture is a case in point.

By embracing digital agriculture, the company has deployed Beidou-based satellite maps, GPS livestock collars and a remote live-stream surveillance system on its farms to collect real-time data on variables such as temperature, rainfall, humidity, livestock tracking and all stages of production processes from farm to customer. The information is accessible online through a mobile app; this can be relayed to ranchers to save time and costs of manual monitoring. Such real-time monitoring also gives consumers greater insights into farm performances in terms of production, transportation, storage and other processes.

Strengthening brand-building efforts

Currently, there are two particular ways for rural cooperatives to create brand awareness of their products. Teaming up with well-established businesses is an effective way for cooperatives to strengthen their brand building efforts and further promote revitalization in rural areas. For example, some local cooperatives in Nanjiang County, Sichuan province, have formed a partnership with the century-old drugstore Nanjing Tongrentang to provide red sage (or danshen) planting sites. As Nanjiang County is renowned for the best soil to grow high quality danshen, the partnership enables both the company and poorer farmers to generate higher incomes, creating advantages for both parties. Another brand building strategy is cultivating local brands. Developing a local brand requires more time and resources compared with forming partnerships with major businesses; yet, once brand awareness is built, it creates long-term brand value. With local government support, rural cooperatives and fruit farmers in Xi County, Shanxi province, have set up a food traceability system for its locally-produced Yulu pear fruit. The system enables them to take control of the Yulu pear production process and ensure safety, quality and regulatory compliance. By providing high-quality products, local cooperatives and fruit farmers have successfully created a strong brand image for Yulu pear products, increasing sales and market share.

Exploring new distribution channels

Most e-commerce players participating in the government's rural e-commerce pilot programs have focused particularly on distributing rural agricultural products to urban areas. To facilitate this, some e-commerce players have created distinctive packaging designs and marketed products both online and offline to reach diverse consumers. To boost consumer confidence, some e-commerce players have also developed manufacturing traceability systems to increase data visibility and transparency across the entire supply chain, providing consumers with detailed information about products they purchase and facilitating communication between consumers and manufacturers. Some manufacturing traceability systems even share information with consumers about the farmers who supplied the products.





What the Experts say

Some industry insiders maintain that the government encountered considerable obstacles and challenges during early development of rural e-commerce and food traceability pilot projects due to lack of experience, including insufficiently specialized skills and technologies. However, thanks to the well complemented strengths and joint efforts of government authorities, local communities and enterprises, the development of rural e-commerce and food traceability systems has made great strides over recent years in breaking down barriers as well as promoting harmony and integration among multiple parties across entire supply chains.

Our experts predict that the advent and proliferation of 5G technology – a massive mobile network that can provide seamless, ubiquitous, and limitless connectivity for all people and all connected things – will usher in a new era of opportunity for the development of rural e-commerce and food traceability systems, contributing to lowering the country's areas of poverty and rural revitalization.

10

Agricultural distribution channels accelerate transformation; rural issues and consumption upgrading are better addressed



The rise of the Internet coupled with changing consumer preferences has redefined China's agricultural landscape for offering, circulating and distributing produce. New distribution channels for farm produce – such as fresh food supermarkets, fresh food convenience stores and agricultural e-commerce platforms – have emerged in recent years to cater to consumers' rising expectations, particularly for shopping experiences and convenience, as well as providing access to numerous consumer cultures from different regions.

At the same time, traditional agricultural wholesale markets – actively undergoing transformation and upgrading – continue to play an invaluable role in the distribution of agricultural products to consumers in urban areas, as well as facilitating the reduction of poverty in agricultural areas. According to the National Bureau of Statistics of the PRC, the total transaction value of agricultural wholesale markets amounted to 5.32 trillion yuan in 2018, up 6.4% yoy, with the total transaction volume reaching 912 million tons, increasing by 4.83% yoy. Data from the China Agricultural Wholesale Market Association showed that the total transaction value of the top 100 wholesale markets rose 2.95% yoy to 1.9 trillion yuan in 2018, while the total transaction volume reached 290 million tons, up 1.43% yoy.



Many agricultural wholesale markets have taken ambitious steps to transform and upgrade. These markets will play an increasingly significant role in connecting farmers with consumers in urban areas, addressing the mismatch in supply and demand for farm products, and raising rural incomes.

Zhang Juan, Director, Department of Industry, China Agricultural Wholesale Market Association

Transformation of agricultural wholesale markets starting to bear fruit

For some years, many agricultural wholesale markets have taken ambitious steps to transform and upgrade, expecting to further facilitate the distribution of products between rural and urban areas and improve rural incomes. Some of these transformation efforts have started to bear fruit with large numbers of wholesale markets starting to provide more upgraded functions and facilities.

Establishing an integrated agricultural supply chain to enhance efficiency

To enhance the formation of an integrated agricultural supply chain, some wholesale markets have put more focus on informatization, standardization and digitalization of services. These and other innovations have strengthened the functions of cold chain storage, farm produce delivery and data services, adopting new models and technologies to facilitate the development of “smart wholesale” while supporting online-to-offline (O2O) integration. All these initiatives are set to greatly enhance supply chain quality and efficiency. Such a case involved Inner Mongolia’s Shiquanshimei Co. Ltd., a food company engaged in wholesale, distribution and retail of farm products; it established an e-commerce platform in 2018 and set up a “distribution plus retail” WeChat Mini Program to support its O2O initiatives. The company also uses data analytics to achieve precision production, seamlessly connect upstream production and downstream activities, and thereby streamlining and redefining the supply chain.

Improving standardization and brand integrity of farm produce

Some agricultural wholesale markets have been actively working on the standardization and branding of farm produce. The use of blockchain technology, for instance, can improve the optimization of agricultural supply chain (by recording transactions in real time and providing up-to-date supply and demand information to farmers, distributors and consumers). Blockchain can also enhance traceability of farm produce by providing reliable information on the origins of food items and the precise journey it took from farm to table. Besides, blockchain can greatly enhance brand integrity and performance as well as operational efficiency.

Jiangsu Wuxi Chaoyang Group Company Ltd., one of China’s supply chain innovation and application pilot companies, has successfully experimented with this type of application. In 2019, Chaoyang Group created a mobile application for its e-commerce platform “Chaoyang Daojia”. Through the use of blockchain technology, Chaoyang Group’s app allows users to track foods from farm to table, find out where the foods came from and who grew them. It can also enhance food safety as well as prevent food-related frauds and scams.

Development of a regional temperature controlled agricultural distribution center is under way; accelerates building of distribution centers at points of origins

Chinese consumers’ growing demand for fresh produce has called for better cold chain storage and logistics for agricultural products. This presents a great opportunity

for the development of cold chain logistics. China's cold chain logistics sector is estimated to reach 500 billion yuan by 2020, growing at a compound annual growth rate of over 20% over the four years from 2016, according to market research institute Forward (Qianzhan) Intelligence Co. A regional temperature controlled agricultural products distribution center is expected to be built shortly, providing refrigerated production, food processing, storage and distribution services and facilities; various functions will include transaction, information sharing, logistics and fulfillment, as well as product exhibition and sales.

Meanwhile, the government's anti-poverty drive and rural revitalization strategy have not only facilitated the distribution of agricultural products to cities, connecting farmers with business and promoting rural-urban integration, but also accelerating the transformation of farm markets and agricultural product services centers – especially those servicing townships. In recent years, many local distribution centers and cold storage warehouses were built at points of origin for farm produce, in a bid to facilitate distribution of farm products, hence enhancing farmers' incomes and alleviating poverty.

Agricultural wholesale markets' clustering approach to pursuing O2O strategy, shows positive results

Some agricultural wholesale markets have worked with other similar markets to roll out O2O strategies. For example, Guangzhou Jiangnan Fruit and Vegetable Wholesale Market – the largest in Guangzhou, and a distribution center with one of the highest trade volumes for the sector in China and Southeast Asia – partnered with several other fruit and vegetable wholesale markets that include Shanghai Huizhang Fruit and Vegetable Market and Guangxi Pingxian Jiangnan Market to launch online transactional platform “Jiangnan Xianpin” in 2017. The platform leverages on the substantial resources of Guangzhou Jiangnan Fruit and Vegetable Wholesale Market to provide digitalized supply chain solutions for buyers and sellers. It has set up an online trading platform to connect sellers with potential buyers, while offering related services such as product tracing, digital order-picking and sorting, cross-docking and smart fulfilment.





What the Experts say

Our experts believe the upgraded agricultural wholesale markets will play an increasingly significant role in connecting farmers with consumers in urban areas and addressing the mismatch in supply and demand for farm products. Additionally, wholesale market transformation can also promote distribution of better rural products, contributing to income growth in the countryside. Our experts also highlight the following factors to enhance agricultural produce circulation and the development of agricultural wholesale markets.

Strong government support for the development and transformation of agricultural wholesale markets

Over recent years, the government has issued a series of policies to support the development, transformation and upgrading of agricultural wholesale markets. In May 2019, the Ministry of Finance (MOF) and the Ministry of Commerce (MOFCOM) jointly released the *Notice on Promoting the Interconnection of Agricultural and Commercial Enterprises and Improving the Supply Chain of Agricultural Products*, aiming to enhance the circulation efficiency of agricultural products, improve farmers' incomes and rural revitalization. Earlier, in January 2019, the MOF and the State Taxation Administration jointly published a notice to continue to grant property tax and urban land use tax concessions to agricultural wholesale markets and farmers' markets, in a bid to reduce the tax burden on farmers. These policies play a vital role in facilitating the distribution of products between villages and cities, harmonizing supply and demand for farm produce, and boosting product sales as well as farmers' incomes.

BRI provides a strong impetus for the growth of global agricultural trade

Given its scale and significant infrastructure development plan, China's Belt and Road Initiative (BRI) will provide new growth opportunities for the global agricultural trade. Currently, China is the world's largest importer of agricultural products. The surge in imports has been driven by rising incomes, changing consumer preferences and growing demand for fresh produce. As a result, the scope of imports – in terms of product origins and varieties – has broadened significantly. According to the Ministry of Agriculture and Rural Affairs, China's agricultural trade with BRI countries totaled US\$76 billion in 2018, an increase of 12% yoy, which is 4.3 ppts higher than the growth of China's total agricultural trade. Imports increased 16.4% yoy to US\$42.8 billion, and exports rose 6.8% yoy to US\$33.2 billion. Being one of the major trading platforms for agricultural products, China's agricultural wholesale markets are set to play a crucial role in driving the import and export of agricultural products.

Going forward, the transformation and upgrading of agricultural distribution channels will further facilitate the growth of global agricultural trade. Agricultural wholesale markets should continue to expand their global distribution channels and focus on brand incubation to streamline the agricultural trade. Moreover, they should leverage their global supply chain capabilities and adopt new technologies to tap new business opportunities.

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