



What the **experts** say

Ten Highlights of China's Commercial Sector 2022

January 2022

Contents

Preface **01**

About the Organizations **02**

Expert Panel Members **03**

Implications for Businesses and
Tips for Foreign Enterprises **04**

Ten Highlights for 2022 **08**

Preface

Fung Business Intelligence and the Expert Committee of the China General Chamber of Commerce are pleased to present the 19th edition of our annual Ten Highlights of China's Commercial Sector report.

2021 is a year of recovery for Chinese businesses. Even though the COVID-19 pandemic continued to disrupt economies around the world, China has brought COVID-19 largely under control, which lays the foundation for the turnaround in commercial activities and consumer spending. By the end of 2021, China's retail sales of goods have surpassed pre-pandemic numbers and the catering revenue has almost recovered to 2019 levels.

The year also saw continued evolution of pandemic-driven business models and practices. While community group buying platforms started to consolidate amid tightened regulation, the concept of "15-minute community living circles" focusing on community-based retail and local lifestyle services has received wide attention. Moreover, enterprises' digital adoption continued to accelerate, with on-demand consumer retail and home delivery and experiential retail leveraging VR and AR technologies gaining increasing popularity.

2021 also marks the fresh start of a new era with the introduction of the 14th Five-Year Plan (2021-2025), which places greater emphasis on China's domestic market (or "internal circulation"). The Chinese government rolled out a raft of supportive policies and initiatives, including efforts on improving the circulation system to further integrate rural and urban markets and to boost rural income and consumption, initiatives to develop five cities into international consumption centres, and measures to promote duty-free shopping in Hainan.

With input from more than 160 top-tier mainland experts, Ten Highlights once again identifies top trends of the past 12 months and anticipates what will shape China's commercial landscape in the year ahead.

In 2022, three significant factors will be the continued rise of China's middle class, the pursuit of green development, and the promotion of "common prosperity". Chinese consumers, led by the younger generation, are flocking into more sophisticated, high-quality, and novel products and services, especially those offered by home-grown brands. There is also a green transformation in the commercial sector. Many commercial and trade firms have started to "go green", and consumers increasingly embrace environment-friendly goods. Besides, the Chinese government is committed to expanding rural consumption and rural e-commerce. These developments will open up new opportunities for local and foreign businesses alike.

Ten Highlights is a valuable resource for global brands and retailers, and firms and individuals seeking to better understand the latest commercial trends, issues, and opportunities in China. We wish to thank all panel members on the Expert Committee for sharing their important insights, and our Fung Business Intelligence colleagues for their many contributions.

Helen Chin
Fung Business Intelligence

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 and the Renmin University Of China, 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 quasigovernment association endorsed by the State Council. The CGCC has around 80,000 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 business committees. It also supervises 40 national associations and 33 newspapers and magazines published both inside and outside China.

Fung Business Intelligence

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

Headquartered in Hong Kong, it leverages unique relationships and information networks to track and report on these issues with a particular focus on business trends and developments in China and other Asian countries. Fung Business

Intelligence makes its data, impartial analysis and specialist knowledge available to businesses, scholars and governments around the world through regular research reports and business publications.

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

Fung Business Intelligence was established in the year 2000.

The Fung Group

Fung Holdings (1937) Limited, a privately-held business entity headquartered in Hong Kong, is the major shareholder of the Fung Group of companies, whose core businesses operate across the entire global supply chain for consumer goods including sourcing, logistics, distribution and retail. The Fung Group comprises over 26,000 people working in more than 40 economies worldwide. We have a rich history and heritage in export trading and global supply chain management that dates back to 1906 and traces the story of how Hong Kong and the Pearl River Delta emerged as one of the world's foremost manufacturing and trading regions. We are focused on both creating the Supply Chain of the Future to help brands and retailers navigate the digital economy as well as creating new opportunities, product categories and market expansion for brands on a global scale.

Listed entities of the Group include Retail Asia Limited (SEHK: 00831). Privately-held entities include Li & Fung Limited, LH Pegasus, Branded Lifestyle Holdings Limited, Fung Kids (Holdings) Limited, Toys "R" Us (Asia) and Suhyang Networks.

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Implications for Businesses and Tips for Foreign Enterprises

2021 was a year of recovery and resilience for businesses after the outbreak of COVID-19 severely impacted the global economy in 2020. The Chinese government continued to introduce policies and measures to support the economy and help businesses recover throughout the second year of the global pandemic.

Meanwhile, as this was the first year of the 14th Five-Year Plan period (2021-2025), the government has also taken bold steps to boost consumption. For example, it has launched substantial policy measures to improve the circulation system. This will further integrate rural and urban markets and unlock the vast potential of the nation's rural areas. Furthermore, China is committed to reaching peak carbon dioxide emissions before 2030 and achieving carbon neutrality before 2060, which will give rise to a green transformation in the commercial sector. This will bring significant business challenges alongside new opportunities, and firms that can quickly understand and adapt to the green transformation will be more likely to succeed.

Flexibility and adaptability are key for enterprises to stay relevant and competitive in the post-pandemic era – as such, businesses should be aware of and evolve with rapidly changing market trends.

- 1 Keep up with government policies**
- 2 Explore potential in rural areas**
- 3 New consumer preferences: lifestyle services and domestic brands**
- 4 Community-based businesses: the next wave of growth**
- 5 Further strengthen omni-channel strategy**
- 6 Leverage technology and digitalization**
- 7 Compete in a new market environment**



Keep up with government policies

The “dual circulation” strategy remains a key direction for the nation’s development in 2021. The government stepped up efforts to launch policies and measures that promote domestic consumption and support the development of the commercial sector. These include plans to optimise the modernization of the circulation sector for distribution efficiency, foster international consumption centres, and promote duty-free shopping to encourage domestic consumer spending. (See Highlights 1, 2 & 4)

In addition, the government has formulated a series of policies and measures in line with the new carbon dioxide peaking and carbon neutrality goals. In October 2021, the State Council issued the *Working Guidance for Carbon Dioxide Peaking and Carbon Neutrality* which set out specific development trends for China’s commercial sector to achieve green transformation. (See Highlight 3)

Our take: Enterprises are advised to be aware of these state-led measures and policy guidelines to tap new business opportunities and government incentives. As the domestic market is expected to expand under the “dual circulation” strategy, export-oriented companies could shift their focus towards the domestic market, improve logistics capabilities, and connect with e-commerce platforms to sell their products. Enterprises also need to prepare for the green transformation of production and distribution processes by adopting “green practices” throughout the supply chain.



Explore potential in rural areas

While markets in China’s first- and second-tier cities are becoming increasingly saturated, there are distinct opportunities elsewhere in lower-tier cities and rural areas. The government has made continuous efforts to modernize China’s rural distribution system and upgrade rural commercial outlets in order to facilitate rural consumption and revitalization. Multiple provinces and regions have increased their minimum wage to ensure that people have enough money to spend – consequently, consumption power in rural areas is expected to expand quickly. Furthermore, the central government has been promoting the goal of common prosperity, which will also be beneficial for rural consumption growth in the long term. (See Highlights 1 & 2)

At the same time, the government will further facilitate the two-way flow of goods and services between urban and rural areas, such as through agricultural wholesale markets. New retail formats and business models which allow urban residents to purchase fresh food from rural areas online have been gaining popularity. (See Highlight 7)

Our take: Given the huge market potential of rural consumption, enterprises could expand their e-commerce engagement and reach out to consumers in rural areas through various channels such as social commerce and short video apps – which are popular among shoppers in rural areas. Enterprises are also encouraged to take part in online wholesale events for farm produce, such as online agricultural exhibitions, and “rural livestreaming programmes” hosted by e-commerce platforms.



New consumer preferences: lifestyle services and domestic brands

As consumption continues to upgrade, consumers are spending more on lifestyle services such as catering, travel, sports, entertainment, healthcare, and elderly services. According to government data, service-related consumption accounted for 52.5% of China's household consumption in the first half of 2021. The catering sector has also recorded stable recovery in the past year and the recovery will be further strengthened in 2022. (See Highlights 8)

Home-grown brands and products have become increasingly popular, especially among young consumers, who are more enthusiastic about "Made in China" products. The government is also striving to revitalize classic domestic brands, enhance the attractiveness of new domestic brands, and nurture several influential high-end brands in the cosmetics, clothing, home textiles and electronics sectors. (See Highlight 5)

Our take: We believe the accelerating growth of lifestyle service-related consumption will continue to unleash consumption potential and better support the country's "dual-circulation" development strategy. Enterprises are advised to reinvent and expand the range and variety of their service offerings. Businesses could also consider tapping into the domestic product market by investing in or developing private labels – popular product categories include beauty products and food and beverage products.



Community-based businesses: the next wave of growth

The outbreak of the pandemic has gradually reshaped consumers' shopping habits. People are increasingly turning to their local grocery stores, convenience stores and supermarkets, driving the development of community-based businesses. In light of this, the central government has been actively promoting the "15-minute community living circle" concept. The goal is to establish local community centres in neighbourhoods and provide residents with comprehensive services that meet their daily needs within walking distance. An increasing number of community malls will be upgraded to become one-stop "retail + lifestyle" destinations, encompassing retail shops, restaurants, hairdressers, laundry shops, clinics, elderly care facilities, etc. (See Highlight 6)

Our take: Accelerated urbanization in China will continue to fuel demand for community-based retail services. Enterprises looking to enter the market should expand the variety of their service offerings. Enterprises should also take local residents' demographics, habits and consumption abilities into consideration when making business decisions. Small and medium businesses will have more opportunities in the community, as their owners tend to interact with their neighbours and know more about the neighbourhood.



Further strengthen omni-channel strategy

With the convergence of online and offline retail, omni-channel retailing will continue to dominate the sector. Since 2013, China's e-commerce market has been the largest in the world – despite a slowing growth rate, the market still held steady in 2021. New business formats such as livestreaming e-commerce and social commerce have become well established by now, gaining more popularity among young people. However, physical stores remain the most important touchpoint for consumers, and China's brick-and-mortar retail showed signs of positive

recovery in 2021. Sales of supermarkets, convenience store and shopping malls all picked up in 2021. In-store interactions between salespeople and consumers are crucial, as they allow for relationship building and provide personalized customer experiences. In response, many enterprises are proactively refining their omni-channel retail strategy, aiming to provide a seamless online-to-offline shopping experience. (See Highlights 2 & 10)

Our take: Enterprises are expected to focus their efforts on further integrating online and offline retail operations in the future. Given the popularity of livestreaming e-commerce and social commerce, enterprises are encouraged to try their hand, which could win over more diverse consumer groups. Meanwhile, they also need to enhance their offline services and improve customer retention by adding more experiential elements or introducing new technologies in their offline outlets.



Leverage technology and digitalization

The pandemic highlighted the importance of digitalization for business development. In response, many businesses have accelerated their digitalization efforts in order to better adapt to dynamic changes in the market – chain stores, shopping malls, and even traditional wet markets are undergoing digital transformations. Innovative technologies such as cloud computing, Internet of Things, blockchain, 5G network and smart supply chain have been rapidly developed and applied. The government has also introduced a series of measures to encourage wider adoption of new technologies within the commercial sector. Internet industry giants have launched several assistance programmes and platforms targeting SMEs' digital transformations to assist small- and medium-sized retailers that lack funding and technological support. (See Highlight 9)

Our take: The rise of discerning consumers is driving evolutions in retail models and operations. To keep up with the rapidly evolving commercial landscape, retail businesses are expected to ramp up their efforts in digitalization and innovation, apply technologies which could improve their operation efficiency, and introduce new business models and formats to stand out from competitors.



Compete in a new market environment

To ensure fair competition and promote healthy industry development, the central government has tightened regulations within several sectors. In February 2021, Chinese authorities issued new anti-monopoly guidelines directed at internet platforms, which prohibited a wide range of anti-competitive practices such as offering below-cost services, signing exclusive distribution agreements and using technology and algorithms to manipulate the market. Five leading community group-buying platforms were fined for improper pricing. Many of these restrictions have been laid out in China's latest draft amendments to the *Anti-Monopoly Law*. These regulatory measures are not solely targeted towards tech giants or e-commerce platforms, but rather aimed at ensuring a fair market environment overall. (See Highlights 6 & 10)

Our take: Under these new regulations, China's e-commerce industry will enter an orderly development phase with a more level-playing field. New entrants and SMEs are expected to benefit from these changes and gain more opportunities. Companies could also spend more time on innovation and development and delivering better value to customers in order to stand out. Companies are also advised to stay informed of regulatory changes which could affect their operations.

Ten Highlights of China's Commercial Sector 2022

01

Promoting **common prosperity** through high-quality development of the **circulation sector** and increasing rural consumption

04

China to develop **international consumption centres** and promote **duty-free** industry

02

Consumption upgrading continues as the consumer market steadily rebounds after COVID-19

05

China is embracing local **home-grown brands**, fuelled by young consumers' increasing spending power

03

Commercial sector aims for comprehensive **green transformation** to support China's carbon dioxide peaking and carbon neutrality goals



06

Community-based businesses gradually transform into one-stop “retail + lifestyle” destinations



08

China’s catering market sees stable recovery with accelerated digitalization and innovation efforts



09

Continuous innovation and digitalization drive further transformation and reforms in the retail industry



07

More resources allocated towards building a modern rural distribution system and further integrating urban and rural markets



10

Business environment for physical retail is improving; e-commerce enters an adjustment phase

01

Promoting common prosperity through high-quality development of the circulation sector and increasing rural consumption





What the experts say

Coordinated urban and rural development to promote common prosperity

Chinese President Xi Jinping announced at the National Poverty Eradication and Commendation Conference on February 25, 2021 that China has completely eradicated extreme poverty. Since China's reform and opening up in 1978, it has lifted 770 million people out of poverty. By the end of 2020, the final 98.99 million rural residents living under the current poverty line were also lifted out of poverty, whilst all 832 impoverished counties and 128,000 impoverished villages have been removed from the poverty list. China is committed to narrowing the urban-rural development gap and promoting balanced regional development under the framework of common prosperity. The government will continue to promote rural revitalization in areas that have escaped poverty and improve the circulation system to boost rural consumption

Government will continue to promote high quality development of the circulation sector

In accordance with the new "dual circulation" development strategy, building a modern, efficient, and competitive circulation sector is an important strategic task during the 14th Five-Year Plan period. China will fully utilize its resources to nurture a strong domestic market, expand domestic demand and boost consumption. Both the central and local governments will focus their efforts on promoting high-quality development of the circulation sector by implementing hardware and software upgrades. The government will deepen supply-side structural reforms, better integrate the roles of the market and the government in resource allocation, invest in infrastructure and technology to optimize distribution efficiency, promote innovation and the application of new technologies, and encourage innovative business models. In addition, the government will also accelerate

the modernization of the circulation sector in rural areas to help promote rural consumption and rural revitalization. In particular, the government will focus its efforts on improving the logistics, wholesale and retail systems to further integrate rural and urban markets.

Expanding rural consumption and promoting e-commerce in rural areas

Consumption remains a key pillar of China's economic growth, and the most rapid consumption growth is happening in rural areas with large populations and increasing income. By the end of 2020, the annual per capita disposable income for rural residents exceeded 17,000 yuan, up significantly from 5,919 yuan in 2010. Rural residents have lower living costs and they are often less burdened by mortgages and rent than their urban counterparts, which leads to higher consumer confidence.

The Chinese government has announced a series of policies to support the development of rural consumption, given its huge market potential. In particular, the government is working on expanding rural consumption and upgrading informatization services and related infrastructure, as well as promoting e-commerce in rural areas. New e-commerce business models such as livestreaming e-commerce and community group buying have opened up new markets and distribution channels for agricultural products, lowered the barriers for agricultural products to reach urban consumers, and created employment opportunities for local farmers and workers while increasing their income. Major e-commerce enterprises such as Alibaba, JD.com, and Pinduoduo have all expanded their engagement in rural areas. Meanwhile, most villages and townships in China have established express delivery outlets, which have sped up the distribution of goods between urban and rural areas.

Q&As

Q: What are some of the key directions for developing the circulation sector in 2022?

Key development directions of the circulation sector in 2022 include:

- Embracing digitalization and leveraging technology to optimize business operations and improve operational efficiency, with the goal of cultivating globally competitive circulation enterprises.
- Upgrading infrastructure and establishing logistics delivery centres to improve and optimize distribution networks between rural and urban areas, which will in turn facilitate the flow of goods.
- Tapping into the consumption potential in rural areas by building new commercial outlets and transforming existing family-owned shops into chain stores.

Q: What measures has the government implemented with regards to improving the quality and efficiency of trade logistics?

The Ministry of Commerce and eight other departments have jointly issued the *Notice on Issuing the Special Action Plan for the High-quality Development of Trade Logistics (2021-2025)*, which calls for accelerating the modernization of the industry and further improving the quality and efficiency of logistics services. Key tasks include building efficient urban and rural logistics distribution systems, expanding distribution channels and services to rural areas, promoting the integration of regional trade and logistics, reducing operation costs by improving the level of standardization in logistics services, and developing new business and logistics models.

Q: What measures have been implemented to boost rural consumption?

Business activities in rural areas have developed rapidly, playing a key role in poverty alleviation and rural revitalization. The Ministry of Commerce and 16 other central government departments jointly released a policy document in June 2021 to stimulate rural consumption through logistics and infrastructure improvements and building efficient distribution networks between urban and rural areas. It is important to ensure that industrial products can be distributed from urban to rural areas, while agricultural products can be distributed from rural to urban areas. The government will also improve the consumption environment in rural counties and townships by establishing commercial services and logistics centres, upgrading rural distribution outlets, transforming family-owned shops into chain stores, expanding express delivery services, promoting digitalization and innovation of rural businesses, strengthening rural e-commerce, and expanding the availability of high-quality goods and services that are suitable for the rural market.







02

Consumption upgrading continues as the consumer market steadily rebounds after COVID-19



What the experts say

Retail sales continue to recover in 1-3Q21

China's economy continued to recover from the COVID-19 pandemic in 2021. Consumption accounted for more than half of the gross domestic product (GDP) and its share continues to increase. Final consumption accounted for 64.8% of China's GDP growth in the first three quarters of 2021, making it the biggest driver of growth for the Chinese economy.

Since the outbreak of the pandemic, the central government and local authorities have implemented various policies and measures to encourage consumption and revitalize the consumer market, and these efforts have delivered remarkable outcomes: in the first eleven months of 2021, total retail sales of consumer goods rose by 13.7% year-on-year to 39.96 trillion yuan. This was also an 8.2% increase compared with the same period in 2019 pre-covid.

However, the year-on-year growth rate of retail sales has fallen significantly from 34.2% in March to 12.1% in June, and further down to 2.5% in August, as regional COVID-19 cases in July and summer floods impeded further growth. Retail sales showed signs of stabilizing in September and October, bouncing back with year-on-year increases of 4.4% and 4.9%, respectively. Our experts estimate that overall retail sales will grow by 12.5% yoy in 2021.

Trend of consumption upgrading continues; omnichannel retail strategy remains as the main focus of retailers

Consumption upgrading remains the main theme for China's consumer market in 2021. Demand for high-quality and advanced products and services is increasing. In the first 11 months of 2021, sales of jewelry, cultural products and office supplies, as well as communication appliances surged 34.1%, 20.2% and 16.3% yoy respectively, higher than their annual growth prior to the pandemic.

Online retail sales of goods jumped 15.4% yoy to 11.9 trillion yuan from January to November, accounting for 23.7% of total retail sales, which indicates consumers' increasing reliance on e-commerce. The integration of online and offline channels has become an undeniable mainstream trend for retailers. Physical stores are proactively refining their O2O strategies and providing a seamless omni-channel shopping experience for customers. They have also added more experiential elements in their stores, such as family and children-related facilities as well as art and culture exhibitions, to attract more customers. Meanwhile, new business models such as social commerce and livestreaming e-commerce continue to boom and are expected to gain further momentum in 2022.

Domestic consumption will be further encouraged in 2022

Our experts believe stable employment levels is crucial to consumption growth. According to the outline of the 14th Five-year Plan, China will implement an employment-first strategy, increase employment opportunities, and help low-income groups increase their income. China's urban unemployment rate held steady in November from the prior month at 5%, slightly lower than last year's 5.2%. Meanwhile, the central government has been promoting common prosperity and seeking to expand the size of the middle class, which will be beneficial for consumption growth in the long term. In addition, the integration and adoption of technologies to improve services and manufacturing processes will further help improve market supply, for example, contactless payment and the use of robotics and AI can better engage and serve customers. Meanwhile, more measures in line with the "dual circulation" strategy to expand the domestic market and encourage consumption are expected from the government. Overall, our experts forecast that the growth rate of retail sales will be at least 6% in 2022.





Q&As

Q: What are the measures that have been implemented by the government and e-commerce operators to encourage consumer spending?

To ensure people have money to spend, local governments regularly adjust minimum wages, in consideration of inflation and rising living costs. Multiple provinces and cities, including Shanghai, Zhejiang, Hubei, Xinjiang and Beijing, have increased their minimum wage.

Meanwhile, e-commerce platforms have hosted online shopping festivals to attract consumers with huge discounts. KOLs and brands actively launched special livestreaming shows during these shopping festivals to interact with customers and boost sales. Alibaba's e-commerce platform Tmall reported that its total transaction volume during 2021's Double 11 shopping festival hit 540.3 billion yuan, representing an 8.45% year-on-year growth.

Q: How has the offline retail sector performed?

Despite the rising trend of e-commerce and mobile shopping, retail sales of physical stores in China still accounts for more than 70% of the total retail sales of consumer goods. In the first three quarters of 2021, retail sales in convenience stores, supermarkets, professional stores and specialty stores grew by 14.5%, 6.2%, 17.1% and 19.8% year-on-year respectively.

With the upgrading of store infrastructure, increase in categories of products offered, and innovative experiential factors offered in-stores, we expect to foresee that offline sales will continue to grow in 2022, especially in the high-end and luxury sectors where consumers often prefer to shop in person. Luxury sales, in particular, are expected to rise as international travel restrictions are likely to continue into 2022.

Q: How has the auto sector performed in 2021?

Auto sales are a significant driver of retail sales. China's auto sales saw seven consecutive months of decline from May to November, after a strong rebound earlier in the year, due to a global chip shortage and surging raw material prices. The decline in auto sales has resulted in the slowdown of overall retail sales growth. According to data released by the China Association of Automobile Manufacturers (CAAM), improvements in the automotive supply chain slowed the year-on-year sales decline from 11.5% in October to 9% in November.

Furthermore, Chinese consumers are increasingly willing to buy new energy vehicles (NEVs), which are seen as more economical and eco-friendly. According to the CAAM, in spite of the global chip shortage and supply chain pressures, sales of NEVs – comprised of mainly electric and hybrid-powered vehicles, reached 2.157 million from January to September 2021, up 1.85 times from the same period in 2020.

03 Commercial sector aims for comprehensive green transformation to support China's carbon dioxide peaking and carbon neutrality goals





What the experts say

China is pushing for green development and has set clear carbon dioxide peaking and carbon neutrality goals

China is committed to reaching peak carbon dioxide emissions before 2030 and achieving carbon neutrality before 2060. It means extensive and profound economic and social changes involving new concepts, new standards, new technologies, new practices, new business models, etc will be made. During the process, it also requires joint practical efforts from various communities and sectors. The commercial sector is a key component of China's economy, and thus, plays a crucial role in achieving these goals.

A series of policies and measures were formulated immediately after the carbon dioxide peaking and carbon neutrality goals were set. Upcoming policies regarding circulation, consumption, and trade are expected to promote the increasingly green operation of physical and online stores; increase the supply and sales of green products; influence store structure design, store energy saving standards, commodity packaging methods, waste treatment, logistics, consumption philosophies and shopping concepts. The "green" label is expected to become an industry standard for commercial enterprises. These revolutionary changes will bring significant challenges to commercial enterprises alongside new opportunities. Firms that have a better understanding of green transformation and act quickly to seize on opportunities will have a better chance of success in this new competitive landscape.



Commercial sector has embraced green transformation

The commercial sector has already undergone several green changes. Green shopping malls have been built using sustainable materials and technologies, and energy-saving equipment and facilities have been installed in malls. Low carbon and environmentally friendly measures have also been implemented in e-commerce operations, particularly during the Double 11 online shopping festival. Logistics and express delivery companies are adopting "green practices" throughout the supply chain from warehousing and packaging, to distributing and recycling processes. Catering firms have been adopting the "green, low-carbon and healthy" philosophy in their business practices. They have been advocating for "clean plates" (eating all the food ordered), serving dishes in smaller portions, and initiating research and development on more environmentally friendly, natural, and healthy ingredients.

Ongoing efforts required to translate goals into concrete plans and actions at the business level

Green transformation is well underway, but the concepts of green transformation, as well as that of carbon dioxide peaking and carbon neutrality, are still relatively new to practitioners. In fact, there is currently no global consensus on what these concepts mean and how to efficiently operationalize them in practice. Therefore, commercial enterprises should put continuous efforts into exploring how to translate these goals and concepts into concrete plans and actions in their respective sectors. Such efforts should also be supported by favourable governmental policies. It is expected that government policies regarding circulation, consumption and trade can provide a clearer guidance on green transformation, such that they can carry out green transformation and carbon emission reduction in a structured and efficient manner.

Q&As

Q: What are some of the green transformation practices that have been adopted in the retail and catering sector?

Tmall announced its Double 11 carbon reduction plan during the Double 11 online shopping festival, alongside launching special online stores that offered 500,000 green products. It also issued 100 million yuan in subsidies to encourage green consumption.

Intime Department Store is building its first green shopping mall and leveraging its digital retailing capabilities to experiment with green operations, green services, and green supply chains. In November 2021, Intime Department Store launched its first Green Consumption Festival, which included green forums and encouraged the use of paperless receipts.

In addition, food delivery platform Meituan, in conjunction with many catering brands, began using customized, recyclable cutlery in its delivery services.

Q: What are some of the key green transformation development trends in the commercial sector?

The central government issued a number of policies and measures to achieve the goals of carbon dioxide peaking and carbon neutrality. In October 2021, the State Council issued the *Working Guidance for Carbon Dioxide Peaking and Carbon Neutrality* which set out specific development trends for China's commercial sector to achieve green transformation:

- Commercial enterprises will be encouraged to integrate green and low-carbon concepts in their corporate culture and establish internal green management systems.
- Commercial enterprises are encouraged to participate in the construction of green certification and standard systems, apply for green product certifications and promote the consumption of green and low-carbon products.
- The development of green logistics and integrated multi-dimensional transportation systems will be accelerated. Rail and water transportation (which generate lower carbon dioxide emissions per journey) will play a more important role in reducing energy consumption and carbon dioxide emissions in the transportation sector. The efficiency of road transportation will be further improved, primarily by increasing roundtrips to reduce empty runs. The organization of passenger transportation will be further optimized and transportation resources will be further integrated to ensure higher efficiency.
- The international trade sector will incorporate more trade policies aimed at establishing a green trade system and reducing the exports of energy-intensive and high-emission products. We will see the import and export of more high-quality, value-added, technologically advanced green products, as well as more imports of energy conservation and environmental protection services.





04

China to develop international consumption centres and promote duty-free industry





What the experts say

As one of the three key drivers of growth, consumption remains the biggest contributor to China's economic development. According to the 14th Five-Year Plan, the central government will develop international consumption centres across the country that can compete with global consumption centres such as New York, London, and Paris. Meanwhile, the government will also promote the development of the duty-free industry to boost domestic consumer spending.

Consumption continues to drive China's economy during the 14th Five-Year Plan period

Over the years, consumption has become a key driving force of China's economy amid its broader economic transformation. The consumer market has rebounded strongly since the beginning of 2021. As China's middle class continues to expand and their disposable income increases, there is an increasing demand for more sophisticated, higher-quality products and services. There has also been a strong surge in spending on high-value products such as cosmetics, jewellery, home electronics, automobiles, as well as travel and entertainment.

According to data from the National Bureau of Statistics, total retail sales of consumer goods reached 31.8 trillion yuan in the first three quarters of 2021, up 16.4% year-on-year. Meanwhile, the contributions of consumption to GDP and GDP growth continue to increase. In the first three quarters of 2021, final consumption expenditure accounted for 64.8% of China's GDP growth. According to forecasts by the China Institute for Reform and Development, China is expected to become the world's largest consumption market during the 14th Five-Year Plan period.

Cultivating international consumption centres

With the State Council's approval, China's Ministry of Commerce announced in July 2021 that Beijing, Tianjin, Shanghai, Chongqing and Guangzhou will be the first batch of cities to be developed into international consumption centres that will match their global counterparts in terms of competitiveness, influence and reputation.

Efforts will be made to attract and pool global companies, brands, goods and services, alongside the development of home-grown domestic brands, new consumption landmarks, and new consumption models.

In addition to these five cities, more than 20 cities in China, including new first-tier cities such as Hangzhou, Nanjing and Chengdu, as well as second- and third-tier cities such as Shenyang and Taiyuan are also striving to position themselves as international consumption centres.

Our experts believe that establishing international consumption centres will play a key role in stimulating domestic consumption, upgrading supply, increasing competitiveness, and enhancing China's reputation as a global consumption market.

Duty-free shopping to play a prominent role in boosting domestic consumption

In June 2020, China released the *Overall Plan for the Construction of the Hainan Free Trade Port (FTP)* to facilitate trade and investment and establish the Hainan province as a globally influential duty-free trading centre. An integral part of the initial construction of the Hainan FTP is enhancing duty-free shopping policies to stimulate domestic consumption and redirect overseas travel spending back to the domestic market. The government has enhanced duty-free shopping policies by raising duty-free shopping limits, reducing restrictions on the number of purchases, expanding the variety of duty-free goods offered, as well as offering different collection methods for duty-free goods. With the introduction of new policies and measures, China's duty-free market shows strong signs of growth heading into 2022.

Q: What is the positioning and respective areas of focus for the first five cities that were selected to be cultivated into international consumption centres?

The first five cities that were selected have a clear positioning in terms of cultivating themselves into international consumption centres with the following key areas of focus:

City	Key Areas of Focus
Shanghai	Shanghai will position itself as a global consumption/ shopping destination, offering top-tier goods and services and attracting international brands to hold their global launches in the city
Beijing	As China's capital city and an international tourism destination, Beijing will leverage its rich history and culture to build multiple consumption landmarks, cultivate new brands, promote digital consumption, and develop cultural, tourism, sports, education and medical consumption
Guangzhou	Guangzhou is a city with strong consumption and manufacturing power. As one of the core cities in the Guangdong-Hong Kong-Macao Greater Bay Area, Guangzhou will leverage its proximity with Hong Kong and Macao to develop itself into an international metropolis
Tianjin	Tianjin is an important industrial and commercial centre, and a major transport hub in northern China. The cultural and tourism industry will play a significant role in promoting the city to consumers
Chongqing	Chongqing will build itself into a globally renowned city for shopping, food, exhibitions, tourism, and culture, as well as promoting the cultivation of local brands and services with its own characteristics

Q: How has the duty-free market in Hainan performed after the implementation of the new offshore duty-free policies?

According to data from the Hainan Provincial Bureau of Statistics, in the first three quarters of 2021, Hainan's duty-free sales amounted to 41.7 billion yuan, an increase of 118% year-on-year. About 7.3 million people made duty-free purchases, up 116% year-on-year, and a total of 38 million pieces of duty-free goods were purchased, up 96% year-on-year.

Q: What are the key amendments to the offshore duty-free policies implemented in Hainan effective July 1, 2020?

Duty free policies in Hainan pre & post July 1, 2020

	Before July 1, 2020	After July 1, 2020
Annual duty-free shopping quota	30,000 yuan per person	100,000 yuan per person
Duty-free limit for a single product	8,000 yuan	Unlimited
Product categories of duty-free items	38 categories	45 categories
Products subject to limit on purchase quantity	All products were subject to a limit on purchase quantity	No limits on purchase quantity except for cosmetics, mobile phones, hand-held radiophones and alcoholic products
Eligible operators	Only offshore duty-free operation license holders	All qualified operators for duty-free goods in China





05

China is embracing local home-grown brands, fuelled by young consumers' increasing spending power



What the experts say

Chinese domestic brands and products have become increasingly popular over the past few years, especially among young consumers, as their spending power is rising and they have taken up more of the consumer base in China. For a long time, Chinese manufacturers have mainly been serving the export market and manufacturing for Western brands. Now we are seeing rising demand for home-grown domestic brands.

Domestic brands continue to enhance competitiveness

Chinese consumers are flocking to home-grown brands, seeking new, innovative, high-quality and cost-effective products. According to a report jointly published by internet giant Baidu and a research institute under People's Daily, interest in domestic products has soared by 528% compared to 10 years ago. In the past, foreign brands were favoured over domestic brands for their quality and design. In recent years, home-grown brands have enhanced their competitiveness by improving product quality, engaging in material innovation, and enhancing their design capabilities. For example, local down apparel brand Bosideng has teamed up with top international designers to lead new fashion trends. It also has taken part in various major international fashion weeks. Sportswear brand Li-Ning has launched a clothing line inspired by its founder Chinese Olympic champion Li Ning's gymnastic career in 1990s, which aims to take consumers down memory lane and evoke a strong feeling of nostalgia. Beauty brand Florasis incorporates traditional Chinese culture, launching the Chinese Miao Ethnic Minority Silver Limited Collection with strong elements of Eastern culture which has attracted much attention among consumers. Maia Active, an athleisure wear maker, has stated that their products are specifically designed based on body measurements of Asian women and therefore offer Chinese customers a better fit and added comfort compared to its Western counterparts. Some successful emerging and

upcoming brands in the small home appliances industry have increased their appeal by developing aesthetically appealing products which are of comparable quality to international brands but with significantly lower price points, meeting the needs of consumers who prioritize value-for-money products.

Brand promotion via innovative marketing strategies

Besides paying attention to the latest trends and rapidly launching new products, domestic brands have adopted various marketing promotion strategies through different channels to reach their target customers. Social media, in particular, has significantly changed the way Chinese consumers shop online. The increasing importance of social commerce is mainly linked to the influence of celebrities, Key Opinion Leaders (KOL) and Key Opinion Consumers (KOCs). They are arguably the most powerful form of advertising, as they strongly influence young consumers' purchase decisions. Beauty brand Perfect Diary was able to gain widespread coverage and establish a strong foothold in the beauty market by closely collaborating with celebrities, KOLs and KOCs.

Meanwhile, collaboration with other well-known brands is another common marketing strategy adopted by domestic brands. White Rabbit, a famous candy brand that many Chinese consumers grew up with, has collaborated with brands in various sectors. It has launched milk-scented perfumes, body lotions, lip balms and many other products. Most of these collaborations have seen great success. In Shanghai, people even waited at a pop-up store for four hours to purchase a White Rabbit bubble tea. Sports brands also engage in marketing by sponsoring local sport stars participating in international sports games. For example, Chinese weightlifting champion Lyu Xiaojun donned gold Anta shoes in the Tokyo Olympics, generating a lot of buzz on China's social-media channels.



Young consumers drive growth of China's domestic brands

Young consumers are the main target audience of domestic brands. Post-90s and Generation Z (Gen Z) are gradually becoming the core driving force of consumption growth. According to data from Tmall, the post-90s and post-00s groups made up over 45% of consumers during the Double 11 online shopping festival in 2021, and the number of post-00s consumers increased by 25% compared with the same period last year.

Unlike previous generations, post-90s and Gen Z consumers grew up when the country's economy has been taking off and catching up quickly with its western peers. They have strong and genuine confidence in their national identity, which makes them less likely to blindly admire foreign brands and are more enthusiastic about "Made in China" products. According to a report published by CBNDATA and Tmall.com, the number of new home-grown domestic brands that were launched on Tmall in 1H20 doubled the number for the whole year of 2018. Meanwhile, over 100,000 new domestic brands were launched on Tmall from 2018 to 2020.

Q&As

Q: What are some of the initiatives mentioned in the 14th Five-Year Plan to promote home-grown brands?

The latest Five-Year Plan underscores a commitment to the “dual circulation” strategy for economic development. The government will build up a strong domestic market and continue to promote and strengthen the development of domestic brands. Specifically, the government will protect and revitalize classic and time-honoured brands (colloquially known as Laozihao), enhance the influence and competitiveness of domestic brands, and nurture a number of high-end influential brands in the cosmetics, clothing, home textiles and electronics sector.

Q: How are domestic brands leveraging KOL marketing to approach consumers?

The most common way brands engage in KOL marketing is to encourage user-generated content or to pay a KOL to use ready-made promotional materials. User-generated content usually involves a KOL reviewing the product or creating some form of content to promote the brand. Some KOLs in more popular niches have millions of followers as they have built their reputation for being experts in a certain area or category. Their followers value their opinion highly. If they positively mention a product or use it, followers are likely to try it and may even become regular customers.

Q: What are some of the consumer characteristics of Gen Z consumers?

Gen Z consumers usually have a strong individualistic streak. They are tech-savvy and enjoy researching and comparing products before making an actual purchase decision. They are also less attached to brands and are constantly on the lookout for innovative and novel products. They highly value user experience, aesthetics and quality. They are not as price conscious as their previous generations and are willing to pay for what they like and value.



06

Community-based businesses gradually transform into one-stop “retail + lifestyle” destinations





What the experts say

Community-based businesses to provide more lifestyle services

The outbreak of the COVID-19 pandemic and the rapid development of e-commerce in China have gradually reshaped the way consumers purchase daily necessities. In the post-pandemic era, people prefer to shop online or visit nearby grocery stores, convenience stores and supermarkets. As such, the demand for community-based businesses is rapidly growing.

Currently, most community-based businesses in China are small- and medium-sized retail stores and restaurants. But their functions should be more than that: community-based businesses should not only meet residents' basic needs, but also provide services in education, leisure, entertainment, medical care, and other fields. China's community-based businesses are moving in this direction – there is plenty of room for growth and significant opportunities.

Our experts foresee that an increasing number of community malls will become one-stop “retail + lifestyle” destinations. They also suggest that the services and facilities in the community malls should be planned according to local residents' demographics, habits, and consumption abilities. For example, communities with an aging population should be allocated more elderly service facilities, while younger communities should have more education and entertainment facilities.

Multiple cities to establish 15-minute community living circles

The central government has been actively promoting the “15-minute community living circle” concept – meaning that within a 15-minute walking distance, residents can access comprehensive lifestyle, work and study-related services.

In July 2021, the General Office of the Ministry of Commerce, together with 10 other government departments, issued the *Guidelines for the Building of 15-minute Urban*

Community Living Circles. According to the Guidelines, the goal is to build thousands of 15-minute community living circles in hundreds of cities before 2025, with a target satisfaction rate of at least 90%. Local governments will lead the development of the 15-minute community living circles by increasing the investment of public resources while bringing in diverse business and social entities.

Government policies to promote healthy development of community group buying sector

A new approach which combines the elements of social e-commerce and community business has gained increasing popularity with consumers. Dubbed community group buying, the model allows a group of consumers in the same neighbourhood to order fresh produce and groceries in bulk via apps or WeChat mini programs at discounted prices, and pick up the goods in the community.

The COVID-19 pandemic further accelerated the growth of community group buying as consumers opted to shop online in order to reduce the risk of infection. The market size of China's community group buying industry reached 72 billion yuan in 2020, up 112% year-on-year. According to iiMedia Research, the industry is expected to exceed 102 billion yuan by 2022.

To ensure fair competition and promote healthy industry development, the central government has tightened regulations within the community group buying sector. Unethical practices such as predatory pricing, using excessively low prices to lure customers, posting misleading product information, and data-driven price discrimination will be prohibited. Many of these prohibitions are also laid out in China's latest draft amendments to the *Anti-Monopoly Law*. In March 2021, China's State Administration for Market Regulation imposed administrative penalties on five leading community group-buying platforms for improper pricing, including Chengxin Youxuan, Duo Duo Grocery, Meituan Youxuan and Nicetuan.

Q&As

Q: What are the main forms of community-based business?

Business Forms	Services provided	Service radius
Commercial outlets usually located on ground floors of residential buildings	Basic retailing facilities	Within 300-500 metres
Shops and booths located on major business streets within a community	Retailing and lifestyle service facilities meeting basic needs such as convenience stores, restaurants, and banks	Within 1 kilometre
Community business centres composed of ground floor shops, business streets and other ancillary facilities	Shopping malls providing comprehensive retailing, catering, entertainment and leisure facilities	Within 3-5 kilometres

Q: What services are provided by community-based businesses?

Services provided by community-based businesses can mainly be divided into two categories:

- Services that meet people's basic needs, including convenience stores, wet markets, breakfast stalls, cleaners, hairdressers, print shops, repair shops, pharmacies and express delivery service points.
- Services that improve people's quality of life such as restaurants, bookstores, fitness centres, nurseries, elderly care facilities, training and education facilities, flower and gift shops, coffee shops, and pet service providers.

In addition, the central government has been promoting public welfare in the community by encouraging high-income individuals to contribute more to society via donations. Local governments are setting up community recycling stations and second-hand stores, which could reduce the financial burden of low-income families and provide employment opportunities. The community recycling network can also promote the concept of environmental protection by gaining more public support for the green movement and instilling a green culture within the community.

Q: What are some of the key government policies aimed at the development of community-based businesses?

The central government has issued a series of policies and regulations in recent years to regulate the operation of community-based businesses. The industry has been receiving more attention and resources and will become an important platform to increase employment and promote domestic consumption.

Issuance Date	Policies and measures	Key points
November 2016	Opinions on Advancing the E-Commerce in Communities and Promoting Convenience Consumption by Residents	Explicitly requires enhancing the level of informatization, standardization and regularization of community-based businesses; promotes the innovative development of community-based business
March 2020	Implementation Opinions on Promoting Capacity Expansion and Quality Improvement of Consumption and Accelerating the Formation of a Strong Domestic Market	Promotes the development of community living services, convenience stores, community groceries and other community-based businesses; calls for broader property management services and the construction of commercial districts aimed at improving community convenience
August 2020	Opinions on the Action of Strengthening Weaknesses in Urban Residential Community Construction	Supports the building of convenience business service facilities; encourages small stores to provide diversified services; guides chain stores to provide quality services for their local communities
May 2021	Opinions on Promoting the Construction of 15-minute Urban Community Living Circles	Introduces the plan to select a list of 30 districts in certain cities as the pilot 15-minute community living circles

07

More resources allocated towards building a modern rural distribution system and further integrating urban and rural markets





What the experts say

Rural commerce plays an important role in forming a strong domestic market and facilitating China's dual-circulation development. Narrowing the urban-rural consumption gap, supporting rural consumption, and strengthening distribution networks between rural and urban areas are some of the Chinese government's key tasks during the 14th Five-Year Plan period.

Modernizing rural distribution system and upgrading rural consumption

The government has made continuous efforts to modernize China's rural distribution system and upgrade rural commercial outlets in order to facilitate rural consumption and rural revitalization. In June 2021, 17 departments, including the Ministry of Commerce, jointly issued the *Opinions on Strengthening the Construction of the County-Level Commercial System to Promote Rural Consumption* (the Opinions).

According to the Opinions, China's county-level economy has developed rapidly in recent years, making a positive impact on poverty alleviation and rural revitalization. However, county-level commercial development is still lagging behind due to inadequate infrastructure and logistics support and insufficient supply of goods and services. In order to tackle this issue, a campaign will be launched during the 14th Five-Year Plan period to improve the rural business system. In regions where conditions are satisfactory, chain stores and logistics distribution centres will be established in all counties; commercial and trade centres will be established in all towns and townships; and express delivery services will be made available to all villages by 2025. In addition, the government will continue to facilitate the two-way flow of goods and services between urban and rural areas and promote rural consumption upgrades by improving rural distribution networks, upgrading commercial facilities, strengthening the cultivation of county-level commercial enterprises, enhancing distribution efficiency of agricultural products, digitalizing rural supply chains, improving the quality and variety of goods, and the shopping environment and consumption experience for rural consumers.

Agricultural wholesale markets continue to improve, with new innovative business models gaining popularity

The government has emphasized the importance of ensuring stable supplies and prices of agricultural staples such as vegetables and meat. During the COVID-19 pandemic, agricultural wholesale markets played a strong role in maintaining supply and price stability. Going forward, the markets will continue to transform and upgrade through service informatization, standardization and digitalization, which will allow them to better meet consumer needs. Meanwhile, new retail formats and business models for purchasing fresh food, such as fresh food supermarkets, fresh food convenience stores and fresh food e-commerce platforms have gained popularity in rural areas as they are able to meet changing consumer demands. The pandemic, in particular, has greatly increased demand for purchasing fresh food online. Community group-buying platforms have also become popular. This new model has improved distribution efficiency and lowered distribution costs for suppliers, while offering attractive discounts and convenience to consumers.

Accelerating digitalization of agricultural markets

New information and communication technology has continued to transform China's agricultural markets. Information systems and high-speed internet have facilitated real-time data sharing for better coordination and collaboration of supply chain activities. Meanwhile, consumers are paying more attention to the quality and safety of agricultural products. Cloud computing and blockchain technology have enabled the construction of reliable traceability systems which are able to capture key information along the supply chain to better detect and prevent quality issues and fraud. Meanwhile, supply chain digitalization has also improved the performance and efficiency of cold chain logistics, which is critical for distributing fresh food. For example, blockchain, cloud computing, and tracking sensor technologies have enabled real-time monitoring of temperature changes along the logistics chain, so suppliers can intervene in time if necessary.

Q&As

Q: What are the development trends of agricultural wholesale markets in 2022?

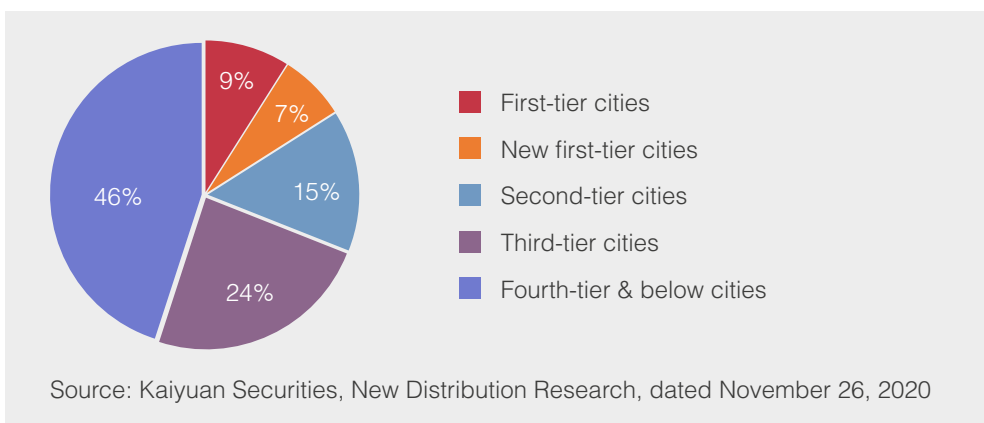
Our experts predict that agricultural wholesale markets will continue to digitalize, which in turn will enhance efficiency. Meanwhile, agricultural wholesale markets will move from a rental business model to a “rental plus self-operated” business model. Some agricultural wholesale markets have been actively working towards standardizing and branding fresh farm produce. Upgraded agricultural wholesale markets are expected to play a significant role in connecting farmers with consumers in urban areas, resolving mismatched supply and demand for agricultural products, and raising income and living standards for rural residents.

Q: What measures have the government implemented to promote cold chain logistics?

The General Office of the State Council recently issued a development plan to promote the cold chain logistics sector during the 14th Five-Year Plan period. The Plan will address major bottlenecks in the development of cold chain logistics by investing in infrastructure, upgrading facilities and equipment, promoting the application of information and communication technology, improving regulatory standards, cultivating talent, and strengthening the international competitiveness of domestic cold chain logistics enterprises.

Q: Why is community group buying more popular in lower-tier cities?

Community group buying is more common in lower-tier cities, especially in third-tier and below cities. Lower-tier cities have more tight-knit neighbourhoods. People in lower-tier cities tend to interact more with their neighbours and are keener on participating in social shopping experiences. Consumers in lower-tier cities are also more price sensitive – they are more likely to look for deals and value-for-money products. According to a report from Kaiyuan Securities and New Distribution Research, around 85% of group leaders for community-based group-shopping platforms are based in second-tier cities and below.







08

China's catering market sees stable recovery with accelerated digitalization and innovation efforts



What the experts say

China's economy is on a steady trajectory for recovery as it enters the 14th Five-year Plan period in the post-pandemic era. While the COVID-19 pandemic has brought significant challenges to the catering sector, 2022 will bring new opportunities for growth and development.

Catering businesses overcome challenges

While the pandemic has largely been brought under control at the national level, the effects of COVID-19 could still be felt in 2021 with various regional outbreaks causing setbacks for the catering industry at a crucial moment in its recovery. Catering businesses have faced pressures from all sides – rent prices, labour costs and cash flow shortages – which have forced them to adapt and innovate in order to survive. New offerings such as online ordering takeaway and delivery services, retail product sales, new dishes and set menus have all helped businesses through these challenging times.

Catering industry sees stable recovery and further development in 2021

During this turbulent period, catering businesses have also actively heeded government advice to strengthen pandemic prevention efforts and use major holidays to carry out promotional activities. Steady demand and consumer confidence have played an important role in boosting the market, reinforcing stable recovery and further development of the catering industry. As such, despite various setbacks, the industry as a whole has seen steady growth from January to October 2021, with a 25.7% year-on-year increase in revenue. By heeding government advice and remaining resilient and resourceful in the face of the pandemic, the industry has managed to encourage spending and strengthen its overall recovery.

Catering industry continues its digital transformation

China's catering industry has witnessed continuous rise in living standards and consumption capacity over the years, and remains indispensable for creating employment, promoting consumption, and supporting the Chinese economy. The year 2022 will become a milestone for the digitally-empowered development of the industry. In accordance with the 14th Five-Year Plan, China must focus on increasing domestic demand to support the dual circulation strategy. Under the guidance of the national policy, the catering industry should focus on high-quality development and digitalization in order to further stimulate demand and increase consumption.



Q&As

Q: How is the government supporting the recovery of the catering industry?

In September 2020, the State Council issued the *Opinions on Accelerating the Development of New Modes of Consumption Led by New Business Formats and Models*. This document calls for increasing efforts to integrate online and offline consumption, optimize the development environment for new modes of consumption, and increase policy support for new modes of consumption. In 2021, the national policy will continue with expanding domestic demand, building a new development pattern fuelled by domestic and international dual circulations, and support the continued recovery of the catering industry which will once again become a key driver of consumption.

Q: What are the key post-pandemic consumer demands regarding the catering industry?

In post-pandemic era, consumers are more health- and safety-conscious than ever. This means higher standards for nutrition, food safety and hygiene across the industry. As such, catering businesses should focus on improving governance, increasing accountability for catering service providers, and enhancing consumers' overall sense of security and satisfaction towards food safety. The pandemic has also normalized new consumption models such as online ordering, contactless delivery, and retailing of ready-to-cook and ready-to-eat products. In order to encourage spending, businesses should also look at opportunities to upgrade their offerings: supply-side reforms, regional cuisine, heritage protection and cultural tourism, the night economy, etc. have all become new business opportunities to promote catering consumption.

Q: What is the most important industry development trend?

Supply chain improvements through innovative technologies have a promising future. The catering industry should accelerate the digitalization process by adopting technologies such as big data, AI, and the Internet of Things (IoT) across the supply chain. This will effectively reduce labour costs and improve risk management, which will in turn shift the focus from increasing scale and speed to improving quality and efficiency. This newly modernized catering industry will be able to better meet the increasing consumer demand for personalization, customization and experiential consumption.

Q: What is the most important industry development trend?

Sustainability:

At the United Nations General Assembly in September 2020, China announced its goal of reaching carbon emissions peak by 2030 and achieving carbon neutrality by 2060. The catering industry can support this goal by actively working towards industry-wide green development. This includes improving standards and evaluation systems, exploring approaches to environmental protection, introducing clean and renewable raw materials, improving equipment and facilities, reducing energy consumption, and advocating for healthy diets and low-carbon lifestyles. customization and experiential consumption.

Food waste:

In light of the sustainability issue, the Chinese government has also taken steps to reduce waste in the catering industry. The *Law of the People's Republic of China on Anti-Food Waste* was enacted in May 2021, followed by the *Food Conservation Action Plan* in October. In 2022, the catering industry should respond by strengthening operations management, improving the anti-food waste systems, improving industry standards and service standards, proactively reminding consumers to order appropriate meals, offering smaller portion sizes, providing information on food quantities and specifications, and cracking down on food waste violations.





09

Continuous innovation and digitalization drive further transformation and reforms in the retail industry



What the experts say

Retail businesses continue to innovate their business models

Driven by technological innovations and changes in consumer demand, an increasing number of retailers have adopted innovative and digital tools to support their businesses. Many new retail formats and models have emerged in China in recent years such as on-demand delivery business, livestreaming e-commerce, experiential shopping, and unmanned retail stores. In the initial stages of business development, companies usually focus their efforts on expanding their business and gaining market share. Upon reaching a certain level of business maturity, they must begin to explore a sustainable model to retain consumers and generate profit. Our experts believe that enterprises will continue to innovate and experiment with new retail formats and business models to stand out from the competition.

Digitalization of large retail chain stores to improve efficiency

A number of large retail chain stores have started digitalizing their operations and successfully eliminated data silos between business units, improving efficiency in both of their online and offline operations. For example, convenience store operator 7-Eleven in Guangdong officially kick-started its digital transformation process at the beginning of 2020. By working with a strategic digital solution provider, 7-Eleven has transitioned to a new retail operation system based on cloud computing technology to better manage their operations. For example, real-time data synchronization between different platforms and across different devices has helped resolved inventory issues previously caused by data discrepancies,

which in turn has helped improve consumer satisfaction. Going forward, we expect that an increasing number of retail chain stores will undergo digital transformations to improve operational efficiency.

On-demand delivery businesses shift focus from traffic cultivation to profit generation

On-demand delivery businesses have become an important retail model, particularly during the COVID-19 lockdowns. The market leaders of on-demand delivery in China have adopted a low-price strategy for capturing market share. For instance, Freshippo, Meituan Maicai, Dingdong Maicai and MissFresh have successively offered delivery services with little or no additional charges. Our experts observed that in the initial stage of business development, pursuing a low-price strategy is a common tactic for attracting traffic and cultivating users. However, when the expansion rate slows down, improving product quality and service standards becomes crucial for businesses to retain customers and generate profits. For example, China Resources Vanguard is strengthening its own online business and no longer solely relying on third-party platforms. Dada Group, China's local on-demand delivery and retail platform, has teamed up with JD.com and launched "Shop Now", a jointly built business where consumers can order online and have the products delivered from the physical stores to home within an hour. Meituan has been deepening its cooperation with various offline partners such as supermarkets, convenience stores, and specialty stores and have been offering additional product categories to better meet the consumption needs and habits of its customers.

Q: How are changes in consumer demand affecting retail innovation?

According to our experts, the rise of discerning consumers is driving evolution in retail models and operations. It is difficult for traditional single-category retail stores to stand out and catch the eye of today's consumers. To attract store traffic, retailers are leveraging new technology such as VR/AR/AI to offer immersive shopping experiences to attract shoppers, especially young consumers. Shopping malls and traditional wet markets are also undergoing transformation. For example, JD.com opened its first "JD Mall" in Xi'an which includes different experiential zones, with various themes such as kids' entertainment, gourmet kitchens, etc. The shopping mall offers interactive shopping experiences and encourages cross-buying across multiple zones. Meanwhile, the refurbished "Xi'an Wet Market Cultural and Creative District", which has retained its original appearance and function of selling fresh products, has become an attractive offline leisure location for young visitors to take social media shots. The market has welcomed new tenants, such as cafes, bars and handicraft workshops, while also introducing new visual elements including wall graffiti and art exhibitions.



Q: How can small- and medium-sized traditional retailers survive in the digital era?

Many small- and medium-sized retailers have not fully implemented digitalization, as they lack the funds and technological support to develop their own digitalized systems. Some small-sized community stores and convenience stores have started to leverage the knowledge and expertise of third parties and their digital solutions to help transform their businesses. Alibaba has recently launched a digital SaaS platform known as “Aoxiang” to support small- and medium-sized businesses by offering various digital solutions to support their online and offline operations, provide consumer insights and analytics, and help improve their operational efficiency.

Q: What are some examples of digital innovation in the fresh food industry?

Qdama, a fresh produce service provider, launched an unmanned retail project named “Cai Bar” in certain communities where it is difficult to set up fresh product physical stores due to limited resources. Qdama offers pre-packaged fresh products at the Cai Bar. With its business philosophy of not selling overnight food, Qdama has set up smart refrigerators in Cai Bar and uses electronic price tags, which can adjust prices automatically and clear out all fresh products with discounts before closing time every night.

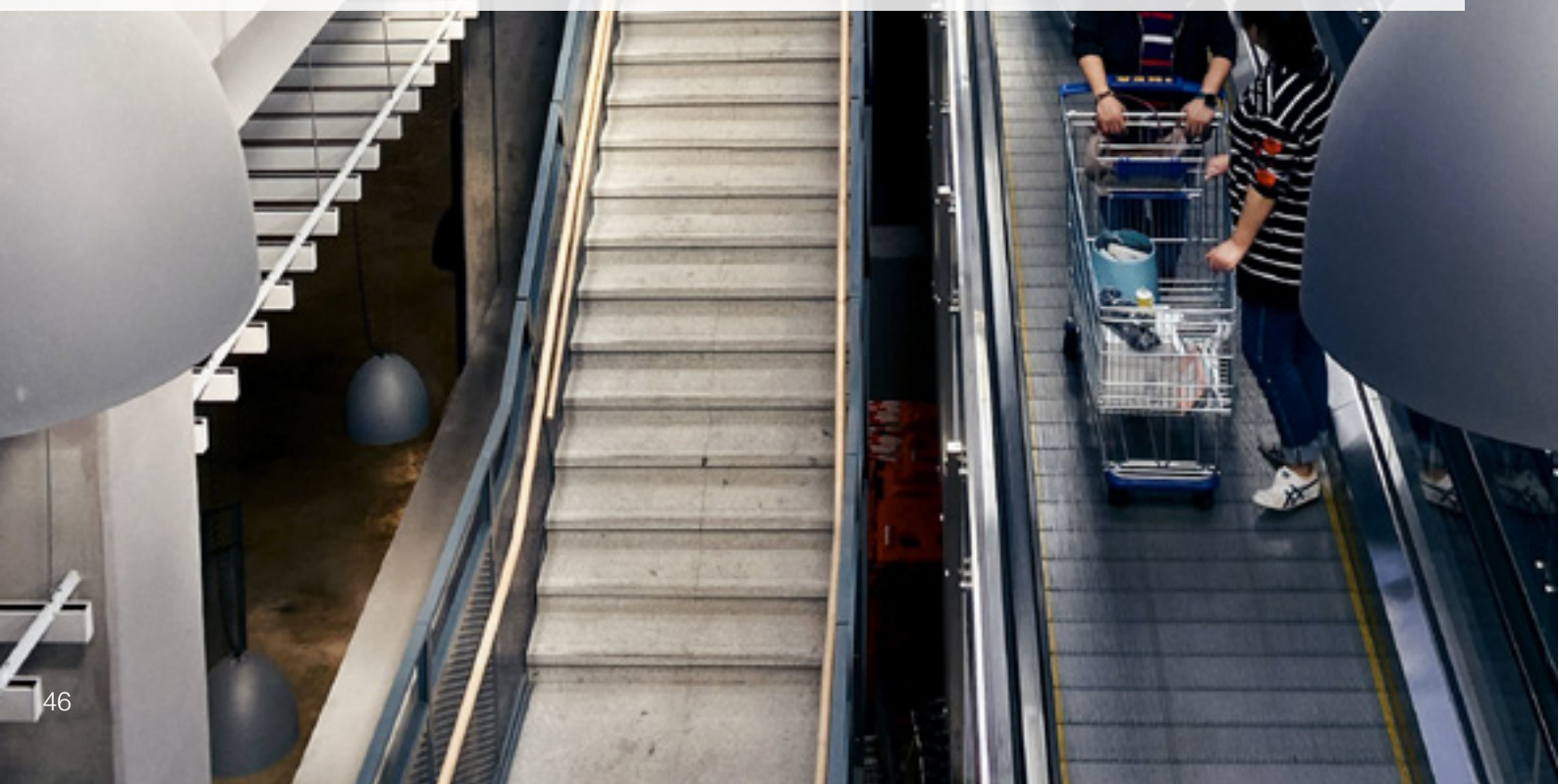
JD Fresh, JD.com’s online fresh food business, has helped traditional wet markets expand their operations online with the support of JD Logistics. Dingdong Maicai, an online grocery operator, has been leveraging big data analytics and algorithmic predictions to make more informed and accurate procurement decisions.





10

Business environment for physical retail is improving; e-commerce enters an adjustment phase





What the experts say

Physical retail shows signs of recovery

China's brick-and-mortar retail is emerging from a long winter, showing signs of positive recovery in 2021. Sales of supermarkets increased by 6.4% in the first eleven months of the year, while convenience store sales maintained its double-digit growth. Foot traffic at shopping malls has also picked up, as shopping remains a popular pastime and a genuine form of entertainment for people. High-end department stores and malls, in particular, has seen strong growth as demand for luxury products remains high, especially with international travel restrictions still in place.

Our experts believe physical retail has unique advantages over online channels. To a certain extent, the experiences that physical stores offer cannot be replicated online. Nevertheless, retailers still need to work harder than ever to attract shoppers in the post-pandemic era. They are working more closely with upstream partners in R&D, design and manufacturing to strengthen their supply chain and improve product management and service capabilities, as well as strengthening their direct sales business and developing their own private labels. These initiatives will help retailers differentiate themselves from competitors.

E-commerce growth slows down

In the first eleven months of 2021, online retail sales of physical goods reached 9.81 trillion yuan, up by 13.2% from the previous year, below the average increase of approximately 21% for the past five years. According to the *Plan for E-commerce Development during the 14th Five-Year Plan period (2021-2025)* released by the Ministry of Commerce, the Cyberspace Administration of China and the National Development and Reform Commission, China's e-commerce turnover is expected to reach 46 trillion yuan by 2025, a 23.6% increase from 2020. This is only one third of the growth rate from 2015 to 2020. Meanwhile, Alibaba's Double 11 shopping festival across 11 days generated 540.3 billion yuan in gross merchandise volume (GMV); though this was an 8.45% yoy increase, it was the lowest growth rate since the Double 11 online shopping festival was launched in 2009.

The slowdown in China's e-commerce growth rate was partly expected, as e-commerce penetration is gradually reaching saturation, especially in China's top-tier cities. By the end of 2020, the number of online shoppers reached 782 million, making up 80% of Internet users and 60% of the nation's total population. Many elderly people and rural residents have adopted online shopping during the pandemic. Meanwhile, the cost of e-commerce is also rising. Marketing and advertising fees are increasing, while storage and logistics costs remain high. All these factors have slowed the growth of the e-commerce market.

Our experts believe the slowing growth rate means the e-commerce market is maturing. Retailers should focus their efforts on further integrating online and offline retail operations in the future. Notwithstanding the above, e-commerce will continue to play a key role in China's pursuit of "high quality" growth in the next five years, especially in narrowing the development gap between urban and rural regions.

Anti-monopoly rules released to protect fair competition in the market

The central government has been enforcing anti-monopoly rules to ensure fair competition in the market and prevent monopolistic behaviors. In February 2021, the Chinese authorities issued new anti-monopoly guidelines directed at internet platforms. According to the guidelines, internet platforms will be prohibited from engaging in a wide range of anti-competitive practices, such as offering below-cost services, signing exclusive distribution agreements, engaging in price fixing, and using technology and algorithms to manipulate the market. Our experts noted that these regulatory measures are conducive to promoting a fair market environment for various market players, especially small- and medium-sized enterprises (SMEs). It is also worth noting that the anti-monopoly measures are not solely targeted towards tech giants or e-commerce platforms. Large-scale physical retailers should also abide by these regulations.

Heading into 2022, our experts are of the view that China's e-commerce industry will enter an orderly development phase. Companies should focus their efforts on innovation and development and deliver value to customers to stand out from the competition.

Q&As

Q: What are the advantages of brick-and-mortar retail?

Physical stores are the best place to showcase new products, provide new services, and test-out new business models. Consumers can inspect the products at physical stores in person. In-store displays also encourage purchases since consumers are likely to choose more items than planned, due to appealing visual displays. In addition, physical stores allow consumers to shop in groups with their families and friends, which is an experience that cannot be replicated through online shopping.

Q: How are physical retailers strengthening their supply chains?

A robust and efficient supply chain is crucial to the future success of physical retailers. Some retailers are actively developing their direct sales business and private labels. JD Logistics and SF Express have introduced one-stop supply chain management solutions to provide services including inventory management, omni-channel distribution and last-mile delivery solutions to support retailers' logistics operations. Meanwhile, our experts have observed that SMEs, especially those situated in third- and fourth-tier cities, have voluntarily come together and formed strategic alliances to build economies of scale in procurement, R&D and marketing. These alliances are particularly conducive to rural development as it reduces the development costs of individual enterprises via sharing, exchanging, co-purchasing/co-development of products and services.

Q: What punitive actions has the central government taken under the Anti-monopoly Law in the past year?

In April 2021, China's State Administration for Market Regulation (SAMR) fined the Alibaba Group 18 billion yuan after an anti-monopoly probe found that the e-commerce giant had abused its dominant market position for several years by preventing its merchants from selling on other e-commerce platforms. According to the SAMR, this practice stifles competition, hinders free circulation of goods, infringes on the business interests of merchants, and fails to protect consumer rights.





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