

## “New Retail” Business in China

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New companies and industries have been emerging one after another in China, such as drone business, bicycle-sharing, and startup companies in Shenzhen, under different rates of growth. Recently, China’s largest e-commerce company and its counterparts, Alibaba have established the idea of “New Retail”, an integration of online and offline shopping experience, and they are rapidly expanding this new business model across the country. This article will explore China’s “New Retail” business trend, along with the strategies of relevant companies, and will discuss the future direction and how Japanese companies can seize this growing opportunity.

### 1. Introduction

In recent times, China’s e-commerce (EC) companies have been accelerating their investment in conventional retail sectors such as brick-and-mortar stores. Alibaba, China’s largest EC company, has planned to expand its fresh-food supermarket chain business, known as “Hema Fresh,” from 60 stores to 100 stores in 2018. This indicates that Alibaba is determined to further step into offline retail on top of current EC business. The other two Chinese EC giants Tencent and JD.com are also making similar moves, aggressively entering the offline retail by opening various types of offline stores, such as fresh-food supermarkets and convenience stores. Today, China’s offline retail market is a major battleground for IT related companies, e-commerce, and traditional brick-and-mortar retailers fighting each other for more market share.

The factors behind this trend include the slowdown of growth in e-commerce and the maturity of offline retail. The EC share of total retail sales in China is higher compared with other developed countries. However, it is said that such growth is slowing down recently. EC companies are facing an urgent need to find growth opportunities other than their EC core business. On the other hand, looking at current offline retail market in China, rising challenges of increasing labor costs and other issues are forcing companies to restructure their business such as cost structure reform through the use of IT technologies. For IT related companies, the new business model creates bright business opportunities. Alibaba’s transformative “New Retail” strategy

is said to be a new business model different from any present e-commerce platform offline retail.

This article thus explains the mechanism of “New Retail” by case study of Alibaba and Tencent-JD.com alliance business strategies. Then, it will discuss the possibility of future structural changes in China’s retail sector and explore business opportunities for Japanese companies in China’s “New Retail” industry.

## 2. What Is “New Retail”?

“New Retail” refers to a new business type that is different from traditional online or offline channels. This is a concept introduced by Jack Ma from Alibaba. At the Alibaba Computing Conference in 2016, Mr. Ma said that EC would be replaced by “New Retail”, an integration of online, offline, and logistics, in the next 10 to 20 years. However, he did not give a clear definition on “New Retail”, and the term is interpreted in various ways. However, if we consider carefully, “New Retail” could be viewed as a retail business model that uses artificial intelligence (AI), big data, and other technologies to heighten consumer buying experience and improve business management and operation efficiency.

More specifically, “New Retail” can improve consumer buying experience in the following three aspects. The first is an “easier and more convenient” purchase experience. In “New Retail”, there are no borders between the online and offline worlds, allowing merchants to offer the same price in both markets. Therefore, unless the customer want to take product home immediately, he or she can order it online later and has it delivered to their desired location. This seamless blend of online and offline experience helps busy customers to avoid waiting in long queues and return home with heavy bags of groceries.

The second is to ease consumers’ “food safety concerns”. While e-commerce is becoming more widespread today, many customers would still prefer hand-selecting their food to ensure they are in good quality and freshness. In that case, they can visit physical stores to check on the products and choose to purchase immediately or online later. This brings convenience to them as product discovery and product purchase need not to be done at the same time. By providing hand-selecting experience to customers, offline stores help to address the “food safety concerns” raised in EC platform purchases. Thus, it can be said that one of the strengths of “New Retail” is that the merge of online and offline shopping environments cooperatively improves consumer buying experience.

In addition, recent trends prompt companies to attach product tags and labels to provide more product information such as place of origin and manufacturing date. Simply scanning the tag, consumers can know more about the food quality and freshness, easing their concern for food safety matters when shopping online.

The third is to offer a “pleasant” purchasing experience. As consumers can place orders online and get home-delivery, brick-and-mortar stores do not need to keep large amounts of inventory. Instead, they can offer a space where customers can “experience” products in various ways. For example, apart from food tasting and trying clothes on, brick-and-mortar stores can offer channels to enhance consumers’ product knowledge. In this way, not only do they offer a place where consumers can buy products, but also create a pleasant shopping environment.

The above seem to be beneficial to consumers. However, they are already having similar practices, buying in offline retail stores and EC sites according to their own shopping habits. For example, bulk purchase of beverage and regular items with known quality are purchased online.

Therefore, what is exciting about “New Retail” is that retailers can also enjoy great benefits and business opportunities from the integration of online and offline shopping environments. More specifically, by analyzing data collected from consumers’ online and offline purchases, they are able to present the best merchandizing mix at stores, selling the right product to targeted customer group and expand sales. As retailers do not need to keep large amount of stocks, they are of better inventory cost control and more resources for marketing activities to drive online and offline sales. In this respect, we can tell that the use of technologies is crucial in “New Retail.”

Concerning the “New Retail” strategies in China, two IT company groups—one led by Alibaba and one by the Tencent-JD.com alliance—are currently taking the lead. Chapter 3 will further analyse their moves in “New Retail.”

### **3. Specific Measures for “New Retail”**

Alibaba is the pioneer in “New Retail.” As aforementioned, it has been expanding its offline retail business using “New Retail” strategy, in which its fresh-food supermarket chain, “Hema Fresh,” plays an important role here.

Hema Fresh is a new business model functioning as a supermarket, EC warehouse and restaurant. Not only can consumers get their shopping done, but they can also place orders online via a mobile app and have products delivered to their homes. The store also serves as a warehouse for EC. As for the merchandising mix, adequate products are displayed at the store with adequate quantity, using big data calculations, which also helps reduce inventory management costs. Furthermore, they have established dining areas in each store. Consumers can buy seafood, have it cooked on-site and enjoy at the dining space. In this way, “Hema Fresh” stores offer customers a unique purchasing experience that is quite different from ordinary supermarkets, resulting in sales per unit area four or five times of the latter. The success in Hema Fresh stores proves that “New Retail” is a new and effective business model.

Not only does Alibaba operate stores under its own brand, it also actively invests in existing retail companies. For example, it invested USD 700 million

in department store chain Intime Retail in 2014 and RMB 28.3 billion in home appliance retailer Suning in 2015. While Alibaba did not made aggressive moves in the past, it has been accelerating their investment pace since 2016, making an additional investment of HKD 19.8 billion in Intime Retail in 2017. In addition, it has entered into a strategic alliance with Bailian Group, one of China's largest retailers, and has invested HKD 22.4 billion in Sun Art Retail Group, a large supermarket operator. Alibaba has been fully penetrating offline retail market across China with "New Retail" model, rapidly integrating offline retailing and e-commerce platform.

Apart from Alibaba, JD.com, the second-largest EC company in China, introduces its "Borderless Retail" strategy and is rapidly moving to expand into offline retail as well. This "Borderless Retail" strategy aims at eliminating boundaries between online and offline shopping environments and improving customers buying experience, which is very similar to Alibaba's "New Retail" strategy. Under "Borderless Retail", JD.com has been opening new stores one after another, such as automated convenience, grocery stores, and "7Fresh," a new fresh-food supermarket chain, and via trial & error, JD.com is seeking for an optimal store model.

Tencent, China's largest internet company and the biggest shareholder of JD.com, also started to break into offline retail market by investing RMB 4.2 billion in major supermarket operator Yonghui Superstores in December 2017. Later, Tencent and JD.com jointly invested in China's Bubugao, a major retailer, and Wanda Group, a leading real estate company. Tencent also formed a three-company capital and business partnership with a Chinese arm of French company Carrefour and Yonghui Superstores. Tencent is accelerating its business moves. While Tencent got a late start, it has been heavily investing in retail business, striving to earn a place in the sector in cooperation with JD.com.

In this chapter, we have reviewed investment cases of Alibaba, the Tencent-JD.com alliance, and other Chinese IT companies in retail business. From the above measures, we can see that many offline retailers in China now have capital ties or business partnerships with either Alibaba or the Tencent-JD.com alliance, and the integration of online and offline channels has been progressing rapidly in China's retail industry (Fig. 1). From here on, both groups will continue their business and investment expansion, leading to a further acceleration in online/offline integration.

In the next chapter, we will discuss the potential future of "New Retail", with a focus on Alibaba and Tencent.

#### **4. The Future Direction of the "New Retail" Sector**

Conventional B2C retail business approach, in which companies sell products to consumers, has been the mainstream way of retail business. Companies conduct various researches to understand consumer behavior, and make business decisions from manufacturing to shop product display

based on the findings. The direction of business flow has always been from companies to consumers.

In contrast, “New Retail” suggests a reverse flow of business, a C2B approach, by optimizing big data. Consumers are the initiators. Data of their purchasing record and habits are collected via various channels, allowing companies to manufacture, procure, and provide personalized products and services for each customer. By analyzing various data obtained from consumers, companies can get insights to introduce more new products, and form a new business.

In this way, Alibaba and Tencent could further facilitate the evolution of the data-based C-to-B retail business model with their advanced IT technologies. One example is to link membership information to EC platforms operated by Alibaba or JD.com. Usage of mobile payments such as Alipay and WeChat Pay provided by these two companies are ubiquitous. By leveraging on the services, companies can obtain personal purchase data and analyze them. IT companies with a wealth of data are developing “New Retail,” and this will not only integrate online and offline environments, but also have the power to dramatically change current retail eco-system.

**Fig. 1: Retail-related businesses owned by Alibaba and Tencent**

Alibaba	VS	Tencent-JD.com
Intime Retail Bailian Group Sun Art Retail Group Sanjiang Shopping Club Lianhua Supermarket New Hua Du Supercenter	Supermarkets Department stores Shopping malls	Yonghui Superstores Carrefour Rainbow Supermarket Bubugao Wanda Group Walmart
Suning	Home appliances	JD Home
Hema Fresh stores	Fresh food	Super Species 7Fresh
F2 Tao Cafe Tmall Corner Stores	Convenience stores Automated stores	JD convenience stores Unmanned supermarkets
Ele.me Koubei	Life services	Meituan-Dianping JD Daojia
Easyhome Zhidashudian	Others	HLA

Source: Prepared by Mizuho Bank Industry Research Department based on information from the official websites of Alibaba, Tencent, and JD.com, as well as other available information

## **5. Conclusion**

Retail industry in China is about to undergo a great transformation. So far, many Japanese companies might have a perception of strong selling ability of China’s EC companies across the country. There is no doubt that Alibaba, Tencent, and other companies tapping into offline retailing can help increase sales of fresh food products, and China will become more attractive as the designated export market for Japanese companies.

On the other hand, Japanese companies can see Chinese EC companies not only as distributors but also as pioneers in the “New Retail” industry, or real retail business operators. Aeon Delight, a Japanese company offering facility management services, has then established a joint venture with Deep Blue Technology, an affiliate of Alibaba Group, in March 2018 in order to improve user convenience, by opening automated stores etc. The company announced that they would like to expand their business to Japan and ASEAN countries in the future. This move might show that Japanese companies can utilize Chinese EC companies’ cutting-edge retail technology to expand their business in Japan and other countries. It is quite a new understanding of Chinese EC companies compared to the past.

In view of the current Chinese economy, the U.S.-China trade war seems to show no obvious signs of ending. Amid such situation, it is expected that China will focus more on driving economic growth by expanding domestic demand. Retail industry in China will offer great business opportunities not only for Chinese companies but also for many foreign retailers, including Japanese companies. This article has introduced investments of Alibaba, Tencent, and JD.com etc. in “New Retail”, and the blooming development of this retail revolution, and hopes to provide some important insights to Japanese enterprises when they are considering stepping into China market.

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