China Retail - 2019

SPOTLIGHT
Savills Research

China 20 Retail Cities

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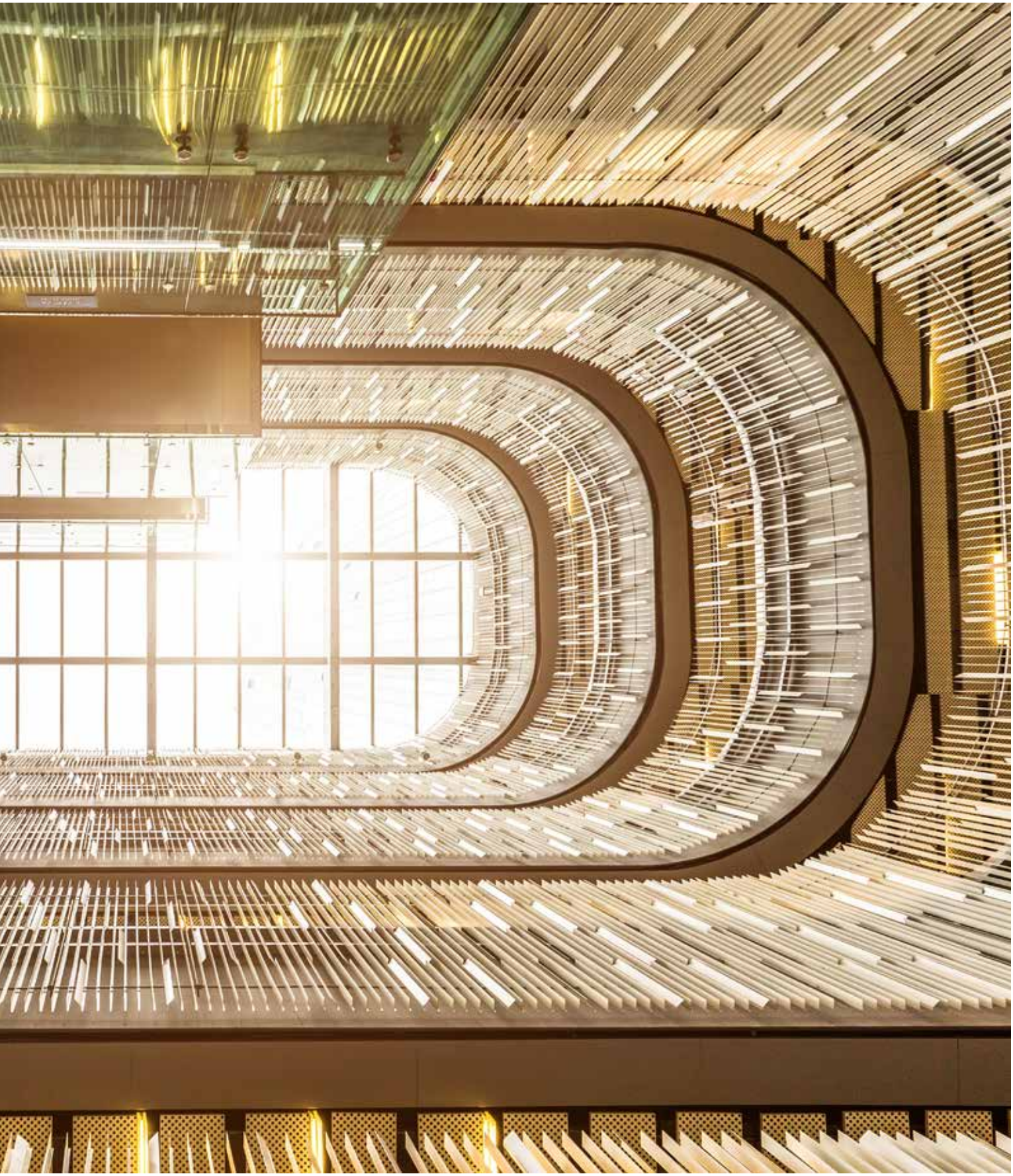


China 20 Retail Cities

This Publication

This document was published in August 2019 and utilises economic data through to the end of 2018 where possible. Store numbers represent the situation as it was at the end of June 2019.

Savills China Retail Cities study was first published in 2014, and uses 16 indicators to determine leaders under two categories: the "economic index" is based on a city's macroeconomic and demographic data, while the "retailer index" is based on the number of stores in the city operated by 50 selected international brands. The indicators are weighted and aggregated to give a final score for each city.

Contents

> China is the second-largest retail market in the world. Global retailers are going to need to pay much more attention to the changes in consumption patterns and innovations that are originating in China. The market will likely become even more competitive as domestic brands continue to grow and mature and learn from overseas experiences before bringing back their new retail know-how and combining it with their innate China knowledge.

Noise & mixed signals

Despite a slowing economy, consumer confidence remains close to an all-time high; luxury consumption continues to recover though purchasing levels of some large ticket items have shown signs of weakness. Diverging performance indicators seem to abound in the current market. Let's have a look at some of the possible reasons.

Lowest growth vs largest market

China became the world's second-largest economy back in 2010. Since then, retail sales growth has slowed from 18.4% in 2010 to 9.0% in 2018, which is largely explained by an increasingly broader base of comparison.

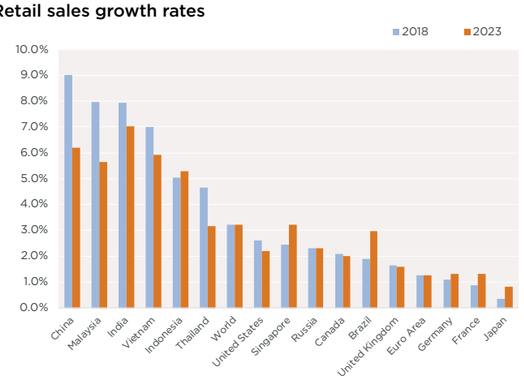
Growth of 9.0%, although close to a ten-year low, is still significantly higher than the other major economies. Given its large market size and current growth rate, China is set to overtake the US as the largest retail market in the near future, with retail sales expected to hit USD5.3 trillion in 2019. China's role in the global apparel industry has rapidly transformed from producer to consumer. In 2005, 71% of the apparel produced in China was exported. The figure dropped to just 47% in 2017 with more products staying onshore.

Despite its slowing growth rate, consumption is playing an increasingly large role in economic growth, with final consumption expenditure contributing 76% to overall economic growth in 2018—up from just 45% in 2010. Final consumption expenditure now accounts for 39.4% of the overall economy. As returns from new fixed investments continue to dwindle and parts of the manufacturing sector relocate to lower-cost Southeast Asian countries, domestic consumption is increasingly seen as the new engine for sustainable economic growth.

Starting in 2018, a series of tax cuts (individual income tax and import duties) as well as VAT reductions have been rolled out to boost the economy and general consumption. At the same time, the new e-commerce law, which came into effect in January 2019, should better regulate online cross-border transactions and — in combination with stricter customs checks — should stem the flow of daigou products and generate more consumption within China's borders.

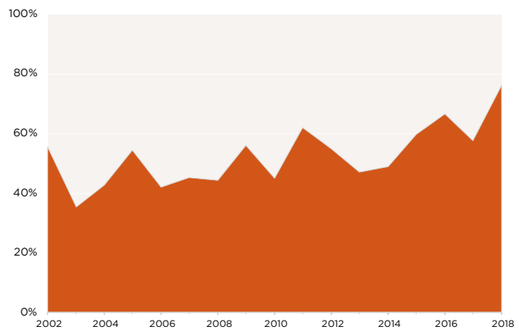
China is an enormous country made up of lots of markets, with some of them more mature than others. The spread of the internet and e-commerce has narrowed the gap to some extent but is hard-pressed to remove all the differences between different areas in China. Leading cities such as Shanghai and Beijing are much more open and accepting of international concepts, and are therefore often the first port of call for many international brands. Lower-tier cities remain much trickier. Local consumers might be able to afford the price point, but retailers will still need time to reach reasonable scale. Finding a suitable local partner is indispensable for international retailers wanting to make inroads in these local markets.

Retail sales growth rates



Source Focus Economics; Savills Research

Consumption expenditure's contribution to GDP growth



Source National Bureau of Statistics; Savills Research

Consumption vs housing price

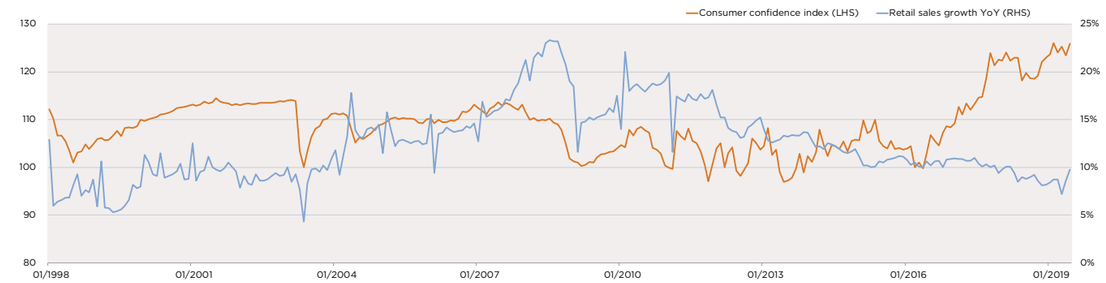
A variety of factors are at play behind the slower retail sales growth. Aside from the larger base of comparison, many observers point to increasing household debt levels, which could be weighing on household finances.

While rising residential prices won't necessarily fuel consumer spending, they could have a positive impact on homeowners' consumer sentiment. The same cannot be said for those yet to get on to the housing ladder; those who are saving up and going into debt to buy their first place; or those who want to upgrade their current premises. In recent years, house prices have been steadily increasing in many cities, making homeowners feel wealthier although this does not necessarily mean having more discretionary spending money. This dichotomy could also help explain strong consumer confidence but slowing retail sales growth.

Falling house prices seldom help to increase consumption levels. The Chinese government plans to shore up market confidence by stabilising residential prices and buying more time for sustainable housing initiatives, such as long-term rental apartments, to take hold. At the same time, the government is making efforts to boost consumption through tariff and VAT cuts as well as individual income tax deductions. There is also speculation that the People's Bank of China might consider lowering interest rates in the near future from what is still one of the highest rates for any major economy. If interest rates do fall, it could reduce debt pressure on households and encourage discretionary spending.

Short-term loans are typically associated with consumer expenditure, e.g. credit card bills, while longer-term loans are typically mortgages. In China, growth in long-term loans has been outpacing short-term loans but gradually stabilised in early 2019, a development that might indicate short-term loans are on an upward trend. As the effects of tax cuts start to play out, and domestic demand continues to be encouraged, consumer market performance is expected to improve over the second half of 2019.

Consumer confidence index and retail sales growth, Jan. 2009-Jun. 2019



Source People's Bank of China; Savills Research

Staples vs discretionary

There are concerns that discretionary spending will be affected by stock market volatility or the financial de-risking and economic reforms taking place amidst an intensifying trade dispute. However, while overall retail sales recorded slower growth in the first four months of 2019, the performance of discretionary categories was not particularly different from that of staple products.

A slowing economy and the ongoing trade dispute could pressure the Renminbi to weaken further against the US dollar. This scenario might convince Chinese consumers to stay home and make more purchases domestically rather than on overseas trips. The increased revenue could partially offset the negative impact on discretionary spending, though it could also cause inflation of imported goods.

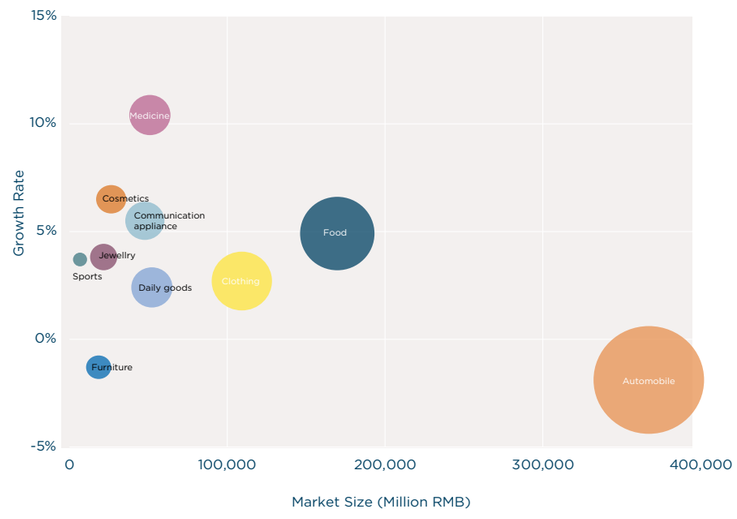
Should overseas expenditure revert to China's shores, the domestic luxury market will likely be the biggest winner. A weaker currency, in combination with a reduction in import duties and personal income taxes, as well as the reduction of structural price discrepancies between markets will likely lead to more luxury purchases within China's borders. According to Bain & Company's estimates, Chinese consumers could make 50% of their luxury purchases domestically by 2025, up from just 27% in 2018.

This trend is becoming more evident in luxury shopping malls. Luxury shopping malls in first- and second-tier cities maintained annual sales growth of 10-20% over the past two years, outperforming the market average. In the meantime, luxury brands are consolidating stores into the best performing projects, focusing on operations at key stores while exploring online channels rather than having too many locations in the same market.

The slower retail sales growth figures can be attributed largely to declining automobile sales since mid-2018. The auto market has been affected by the sluggish economy with limited consumer credit availability as well as buyers waiting for the release of new emission standards (effective July 2019). Nevertheless, the fall in fossil-fuel car sales has been partly offset by the rising sales of new energy vehicles (NEVs). Overall, auto sales fell 12.1% YoY in the first four months of 2019, while NEV sales increased 60% over the same period.

Staple categories are also not immune from the tougher macroeconomic situation. Sales growth rates of food & beverages and daily necessities were only slightly higher than other categories. According to a Kantar survey, premium toothpaste brands and healthy juice sales posted strong growth while less innovative categories, such as diapers and chewing gum, saw sales volumes contract.

Size and growth rates of consumer goods, Jun. 2019



Source National Bureau of Statistics; Savills Research
Note The bubble size represents the monthly sales by companies above a designated size.

20 Retail Cities

Savills Retailer Index saw the least movements in city rankings in the latest five years with only Suzhou and Shenyang swapping positions, while all the other cities retained their previous ranking.

Ranking	City	Index	Ranking	City	Index
1	Shanghai	98	11	Xi'an	25
2	Beijing	87	12	Suzhou	22
3	Shenzhen	44	13	Shenyang	20
4	Chengdu	39	14	Changsha	19
5	Hangzhou	35	15	Kunming	17
6	Guangzhou	34	16	Dalian	17
7	Chongqing	28	17	Qingdao	14
8	Wuhan	28	18	Ningbo	14
9	Nanjing	26	19	Zhengzhou	13
10	Tianjin	26	20	Xiamen	12

Source Savills Research
Note Wuxi has been removed from the rankings while Xiamen has been added.

Catching up

If Shanghai and Beijing are the two largest and most important prime retail markets in China, how far behind are the other 18 cities and how close could they get to the top? In fact, the gap has already narrowed in the last three years. While most international retailers still prefer Beijing and Shanghai for their first location, they often have plans to expand to Chengdu, Hangzhou or Shenzhen within a year. If a brand has a local partner, it may even choose a second-tier city that the partner is more familiar with as its first location. For example, Champion opened its first China store in Hangzhou while Heron Preston chose Xi'an.

In 2014, Beijing and Shanghai had roughly five times the number of stores that the other 18 cities had, on average; in 2019, this has fallen to four times the number, as retailers have expanded faster in Guangzhou, Shenzhen and other second-tier cities. While cities such as Chengdu and Nanjing may have all the same brands that Shanghai and Beijing have (albeit in fewer numbers), many retailers (40% of those tracked) have yet to establish a presence in markets such as Xiamen, Zhengzhou and Ningbo.

After Shanghai and Beijing, the cities of Hangzhou, Chengdu and Shenzhen are the pre-eminent markets for the luxury, affordable luxury and mass fashion categories, respectively, with their store counts in these segments reaching almost half of that seen in Shanghai and Beijing, despite having much smaller populations.

Up and down

Tracked retailers have slowed down their expansion pace in central and western second-tier cities—the main reason why the retailer index ranking remained largely unchanged. In the 12 months to June 2019, retailers increased their average store count in central and western second-tier cities by just 5.8%, compared to 9.8% for cities in the Yangtze River Delta (YRD). A similar trend can be seen in the macroeconomic indicators, with central and western second-tier cities growing only 0.6 of a percentage point (ppt) faster than cities in the YRD in 2018 compared to 0.9 of ppt faster in 2017.

Retailers' pace of expansion in central and western regions is more discerning than before—Kunming and Chengdu recorded slower growth while Changsha and Xi'an maintained a higher pace of growth. Kunming's new projects are located mostly outside the city core, which has helped boost F&B numbers but has done less for international fashion brands. Meanwhile, Chengdu's market is already fairly mature with a full range of brands present; therefore, the impetus for continued growth is weaker.

Several landmark projects opened in Changsha and Xi'an in the last 12 months and, consequently, luxury brands have upgraded and consolidated their premises from older developments, which has resulted in an overall decrease in luxury stores. Retailers from other categories, however, remained bullish and pushed overall expansion rates above 10% in both cities.

Xi'an remains the fifth-largest luxury market in mainland China by store count despite recent adjustments. Retailers from other categories, such as affordable luxury and F&B, have been very active in opening new stores in the last year, helping to enhance the overall retail mix and vibrancy of this ancient-yet-thoroughly-modern city. As the only city that moved up the economic index ranking (now 13th), Xi'an has attracted more than one million permanent residents in the past two years, more than any other city in the rankings. The expanded workforce should provide a solid base for the city's long-term development.

Second-tier cities in the YRD reaffirmed their appeal over the last year with Hangzhou and Suzhou seeing average store growth rates exceed 10% and every retailer category notch store openings. Suzhou is the only city to have ascended the retailer rankings — while the market is diffuse, Suzhou has always been economically strong, coming seventh in terms of GDP ranking. The city is expected to overtake sixth-placed Tianjin in 2019.

Xiamen, despite coming last in the rankings, also outperformed most cities for store numbers with an increase of 11% over the last year. Considering only 31 of the 50 brands tracked have a presence in Xiamen, the city still has plenty of potential, and the opening of the 150,000 sq m Xiamen MixC in late 2018 will continue to attract new brands to the market.

Neck and neck

Hangzhou ⑤ vs Guangzhou ⑥

Hangzhou, Zhejiang's provincial capital, managed to stay ahead of Guangzhou after overtaking it in 2018, albeit by a narrow margin. Hangzhou's market tends to have a discerning consumer base that helps to attract more international brands from niche apparel, café and beauty sectors. Guangzhou, on the other hand, has recorded strong demand for supermarkets, fast food and affordable clothing, reflecting a preference for a more utilitarian lifestyle. Both cities are expecting a similar amount of new supply in the medium term, roughly one million sq m over three years, so they are likely to remain neck and neck in the retailer rankings for the next few years.

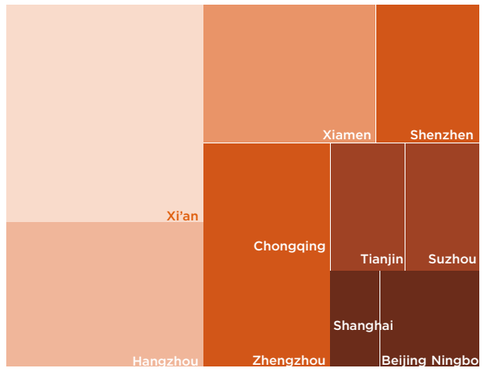
Ningbo ⑱ vs Qingdao ⑰

Ningbo comes last among key retail cities in the Yangtze River Delta. Its performance seems even more muted against the backdrop of the recent rise of central and western cities. It is worth noting, however, that the gap between Ningbo and seventeenth-placed Qingdao has been narrowing. While new stores openings in Qingdao have recently outstripped Ningbo, this is primarily a factor of available stock. Ningbo has the chance to catch up or even overtake Qingdao in the coming years as new retail landmarks are launched onto the market—namely developments by China Resources Land, New World Group and Hankyu Hanshin.

Changsha ⑭ vs Shenyang ⑬

Changsha has been rapidly catching up to Shenyang in the rankings as a result of the city's strong economic growth over the past five years (annual growth rate of GDP at 9.5%), which has created jobs, migration and wealth. At the same time, northern cities, particularly Shenyang, have been coping with a depressed economy, which has sapped consumer spending and seen a number of retailers give the city the cold shoulder.

New luxury and affordable luxury openings by city
2H/2018-1H/2019



Source Company websites; Savills Research

Brands

As more brands see their omnichannel platforms evolve, retailers are going to need to take a harder look at the cost-benefit proposition offered by brick-and-mortar stores and what role they can play in the overall development of brand awareness and engagement. Scale is not everything anymore, and consumers are demanding more from brands.

Store expansion

The evolving online and digital experiences that consumers have through mobile payments and mini-programs have bolstered consumer spending. Consequently, international brands are allocating more resources to the development of online platforms to reach a wider range of consumers. Retailers have also invested more in key flagship stores with better fit-outs, broader product ranges and experienced staff. The store experience and quality of service must be improved to create a more gratifying retail experience.

In the 12 months to June 2019, the store expansion rate of the eight retail categories tracked slowed 5.2 ppts YoY to 4.3%. Coffee store chains were the only category that recorded an expansion rate exceeding 10%.

Luxury store numbers contracted by 6.2% YoY as retailers relocated and upgraded premises to newly launched malls, consequently shuttering older existing stores in several second-tier cities last year. As ROPO (Research Online, Purchase Offline) becomes ever more common in the luxury sector, brands are increasing their engagement with consumers online while still relying on their physical stores in a few select malls to provide a wide range of products and better services.

Western fast food chains tracked in this survey grew at a slower pace in Shanghai and Beijing (1.9%) than in the other 18 cities (8%) for the first time in over four years. This, however, overlooks the fact that mid- to high-end burger and pizza restaurants (not included in the basket of brands) are most definitely on the rise in Shanghai and Beijing. Mass market fast food chains are eventually reaching saturation point in some cities and areas, and higher-income households are becoming more selective when it comes to their fast food.

Fast fashion brands grew store numbers by 4.8% over the past 12 months, with brands trying to be more creative in their product offerings and store designs as competition intensifies. H&M opened a 2,200 sq m store in Hangzhou Gonglian CC, which also stocks a range of household goods, while Inditex has opened two new multi-brand stores in Shanghai.

New entrants are also tapping online platforms as they make their first tentative steps into the China market. Urban Outfitters has been operating a Tmall store for over three years now and has recently started using pop-up stores in preparation for a potential first brick-and-mortar location. Macy's, on the other hand, has decided to leave the China market after operating a Tmall store for just two years, though products are still available through its official website.

All about health

Consumers are becoming increasingly health-conscious and aware of their impact on the environment. In recent years, the government has stepped up its campaign of environmental protection and food safety standards, and consumers have taken this a step further by differentiating not just by product safety standards but also by selecting different products and services more conducive to a healthier lifestyle. This is especially true in more affluent cities where consumers are willing to spend more on health-related products and activities. Many international brands are paying attention and have started emphasising their sustainability credentials while also focusing on health benefits, social welfare and sustainable materials.

While interest in healthy living is universal, it tends to play out differently across countries and regions. Chinese cuisines still dominate second- and third-tier cities. Consumers may accept the idea of going vegan or cooking with less oil and salt but are still not on board with Western health food concepts. Many salad bar chains learned this the hard way when they flocked into the market two or three years ago but failed when they were unable to accommodate local tastes.

The rapidly developing health and wellness market has taken on a life of its own and now incorporates new concepts and products that are shaping consumer lifestyles — from athletic underwear ranges to avocado and chia seed detox smoothies and high-intensity interval training (HIIT) courses. A noteworthy trend has been the rise of cross-sector or multi-sector retailers that seek to tap into increasingly specialised consumer groups.

F&B

Restaurants are updating their menus to include more fresh produce, innovative recipes and healthy ingredients. Some are promoting healthy concepts like in-house produce, organic food supplies, or self-service eateries.

Examples

Hotpot and burger outlets are embracing an upgrade in their food offerings through fresh, organic ingredients and better-quality meat.

Grocery

Consumers are more concerned about how sustainable and organic their produce is. "Additive-free" and "natural and organic" foods are becoming more popular.

Examples

Plant-based milk alternatives are gaining popularity. Soy milk sales recorded a faster growth than other major fast-moving consumer goods in 2018, while oat milk products are also capturing consumers' attention.

Leisure

Consumers are requiring more out of sports and fitness services. The market is fragmenting as specialisations such as spinning, yoga and dance studios and CrossFit boxes expand, supported by innovative technologies.

Examples

Social fitness app Keep has opened an offline fitness centre called Keepland in both Beijing and Shanghai. The Beijing outlet also delivers salad take-outs within a certain radius.

Fashion

Socially-conscious consumers welcome natural materials such as pure cotton and linen. Meanwhile, evolving fabric technology is also enhancing comfort and functionality.

Examples

The incorporation of new technologies in products is expanding, such as Under Armour's bioceramic underwear and Allbirds' wool sneakers.

Digging up new demand

Digging up new demand

At all levels, the government is looking at how to stimulate domestic consumption and economic growth. Beijing, Shanghai and Chengdu have all recently introduced measures, including subsidies and rewards, to attract new retailers. Nevertheless, most mainstream products and brands are already well established, and future growth will increasingly have to come from more novel and innovative brands and those that target particular niches of society.

Domestic

01 Insurgent start-ups

A strong domestic economy and a government push to spur creativity and entrepreneurship combined with increased venture capital and private equity has created the right environment for start-up brands to flourish. Food & beverage and fashion have received significant interest both online and offline while new, high-quality brands in health-related sectors, such as sports, fitness and personal care, have also appeared on investors' radar.

magmode

A designer clothing brand established in 2016, Magmode closed Series C funding in 2018. The new capital is to be used to expand its network in China and explore overseas markets.

02 FMCG goes beyond supermarkets

The ongoing transformation in the traditional supermarket sector has encouraged some FMCG (fast-moving consumer goods) brands to seek alternative channels for growth; for example, securing storefronts or pop-up stores. Utilising creative design elements, brands can generate buzz and elevate their image while also attracting a new generation of consumers.

Wang Lao Ji / Wong Lo Kat

This Chinese herbal tea brand, which used to sell in supermarkets and restaurants, has opened a chain of "1828 Wang Lao Ji" stores in Guangzhou to offer fresh-brewed herbal teas and desserts.

03 Heritage culture

Reinvigorated traditional Chinese brands have been attracting more attention in recent years. According to Alibaba, traditional brands that have undergone substantial makeovers have on average seen a 30% increase in online sales. Heritage brands have an incredible opportunity to tap into consumers' fond childhood memories of brands while also resonating with young consumers by enhancing their retro image and integrating with popular culture.

White Rabbit

White Rabbit, an iconic candy brand from Bright Food Group, opened a milk tea pop-up store in collaboration with Happy Lemon. White Rabbit has also partnered with HeyTea on a limited-edition milk-candy-flavoured ice cream and bubble tea.

04 New brands from mature retail groups

The drive for new products to satiate China's growing need for diversification and personalisation has convinced domestic retail groups to look to overseas markets to buy or partner with new brands. This drive has supported the growth in China's outbound investment. According to a report by Deloitte, wholesale and retail segments accounted for about 20.8% of outbound investment in 2017.

Ahava

Israeli skincare brand Ahava was acquired by Fosun Group in 2016 and, two years later, opened stores in major Chinese cities including Shanghai and Beijing. Investment in overseas retail brands has become such an important part of the group's business that they established Fosun Fashion Group in 2018.

05 Clicks to bricks

More online brands are stepping into the world of bricks-and-mortar retail. A wide range of businesses are exploring the opportunities that come with physical platforms, whether they be single brands, online marketplaces (NetEase Koala and Xiaohongshu), workout and fitness apps (Keep), or online video platforms (iQiyi). The brands are looking to increase user stickiness and loyalty by creating an enhanced member experience and deeper engagement.

Little Red Book

Social e-commerce app Little Red Book has over 150 million users and 85 million MAU. In its official offline store, Red Home, the 400 sq m space not only introduces the platform's best-selling products but also boasts a café and home goods area to establish the brand's lifestyle credentials.

International

01 Peripheral products

As beauty, skincare, and sports and fitness sectors grow rapidly, retailers are also foraying into peripheral products. Industry leaders, including L'Oreal (beauty) and Johnson & Johnson (skincare) have been acquiring firms in related sectors, either to enhance their foothold in existing brand categories or tap into new market sub-segments. A growing number of new brands are emerging that offer beauty aids, digital accessories or specialised products.

ReFa

ReFa, a beauty device brand from Japan, opened its first store in mainland China in 2017. Aiming to provide a better consumer experience (with experiences like skin tests), it now runs stores in Beijing, Shanghai, Hangzhou and Nanjing.

02 Premium F&B

China's food and beverage industry is characterised by significant geographical differences and fierce competition. The leading cities, where affluent consumers are more open and willing to try new concepts and brands, remain very attractive to foreign brands. However, it is still important to find the right local partner to help with supply chain management and product localisation, amongst other considerations.

Shake Shack

Shake Shack, in partnership with Maxim's from Hong Kong, opened its first mainland store at Xintiandi in downtown Shanghai. Higher-end burger restaurants in the vicinity, such as Beef & Liberty, charge an average RMB80 yuan or more for a burger.

03 Tourists' favourites

You can never go wrong by paying attention to Chinese tourists' shopping trends. Brands that appeal to Chinese tourists in overseas markets are often well-received when they enter the China market. As outbound tourism matures, Chinese nationals have a better understanding of brands and products available. International brands with some rapport and understanding of Chinese consumers will also be better prepared.

Canada Goose

Canada Goose has always been popular with Chinese tourists and has built a remarkable reputation via celebrities and social media. It opened its first mainland store at TaiKoo Li Sanlitun in Beijing, along with an e-commerce business on Alibaba's Tmall.

04 Private label cosmetic

Consumers remain enthusiastic about cosmetics and skincare products, particularly the higher-end brands. Nevertheless, many brands may be new to consumers, and thus will rely heavily on consumer reviews and social media platforms (as opposed to direct marketing), which give niche products a better opportunity to gain a consumer following.

Diptyque

Diptyque is one of the pioneering niche perfume brands in mainland China. Since its mainland debut in 2014, the company now operates eight stores — three in Beijing, two in Shanghai, and one each in Chengdu, Chongqing and Nanjing.

05 Alternative entertainment

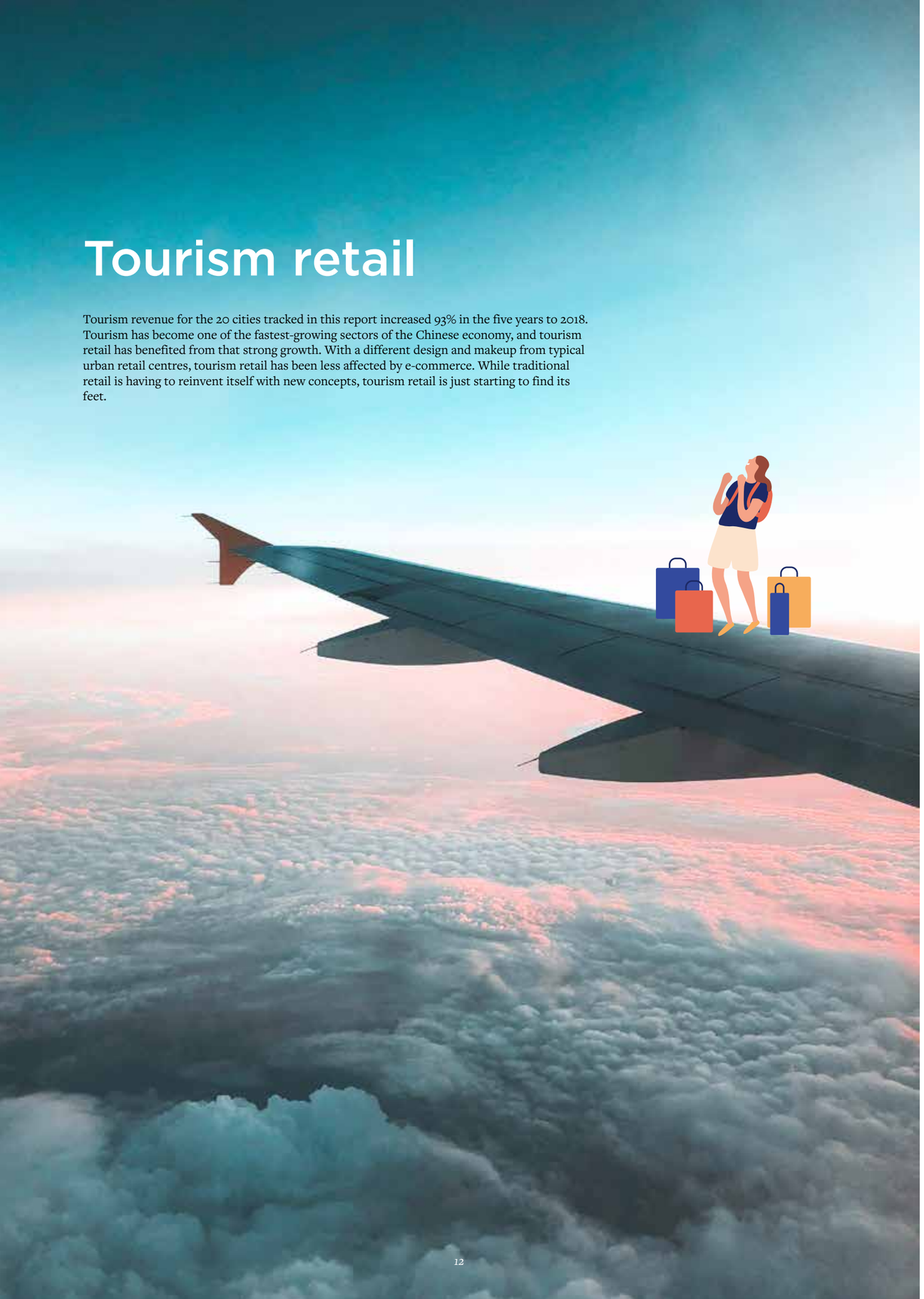
While many retail sectors have been impacted by e-commerce's rapid expansion, entertainment operators have been largely untouched as many experiences are harder to replicate. New construction and space created by vacating brands have handed entertainment operators a golden opportunity to secure great new venues on favorable terms. E-sports and other sports-related tenants are particularly hot at the moment, enjoying a groundswell of interest from consumers.

B-monster

Boxing studio B-monster has opened two stores in Shanghai, while its home market of Japan has a total of just eight. They offer a distinctive experience from your normal gym, focusing solely on high-intensity boxing workouts and featuring unique décor and a nightclub-like atmosphere.

Tourism retail

Tourism revenue for the 20 cities tracked in this report increased 93% in the five years to 2018. Tourism has become one of the fastest-growing sectors of the Chinese economy, and tourism retail has benefited from that strong growth. With a different design and makeup from typical urban retail centres, tourism retail has been less affected by e-commerce. While traditional retail is having to reinvent itself with new concepts, tourism retail is just starting to find its feet.



Duty-free stores

Duty-free stores are an important channel for Chinese consumers when it comes to overseas purchases with two-thirds of overseas luxury expenditure taking place in urban or airport duty-free stores, according to McKinsey.

There are three typical types of duty-free stores in China: 1) Duty-free stores at sea and airport terminals, which are the most common. Shanghai and Beijing airports account for nearly 80% of total revenue; 2) Island duty-free stores, typically found in Hainan. Sanya Haitang Bay International Shopping Mall has revenues comparable to that of prime malls in key cities; and 3) Downtown duty-free stores, which are far from maturity.

Duty-free stores are highly regulated in China with only a handful of companies licensed to operate stores. China Duty Free (CDF) Group is the largest operator in mainland China with approximately 80% market share. The group runs the airport duty-free stores in the four first-tier cities, and in early 2019 they announced plans to open downtown duty-free stores in Beijing, Shanghai and Xiamen.

Further expansion of downtown duty-free stores is expected in the future amid efforts to boost consumption. Nevertheless, downtown stores are likely to remain low key and present a limited range, so as not to distract too much from airport duty-free stores or luxury stores in the core retail areas.

Airport retail

In 2018, 800 million passengers passed through the airports of the 20 tracked cities, up 7% from a year earlier. As airport margins are squeezed and competition from high-speed rail travel intensifies, more airports are focusing their attention on non-aviation revenue sources. Internationally, airport retail has gone beyond meeting the basic needs of travellers with many airports offering a wide variety of quality products and services that can make layovers and check-ins much more bearable while loosening tourists' purse strings. Well-designed and provisioned spaces can also enhance the attractiveness and competitiveness of the airports as international hubs and create a positive first impression of the city or country.

Only two Chinese airports saw non-aviation revenue exceed aviation-related revenues, namely Shanghai Pudong International Airport (PVG) and Beijing Capital International Airport (PEK). Two-thirds of PVG's non-aviation revenue came from duty-free shops, while PEK's share was 45%. These airports are still highly dependent on duty-free stores, but there remains significant potential for other retail options.

Airport interior design in China has tended to be conventional and utilitarian—failing to create anything close to the consumer environments seen in international airports like Singapore's Changi or city-centre malls in Shanghai and Beijing. Mainland airports tend to be dominated by general retail and a handful of F&B tenants that are often unappealing to travellers, and pop-up stores and concept stores, while gaining popularity in city centre locations, rarely make an appearance either. There is also a distinct lack of leisure or entertainment options. One of the first and easiest steps would be to upgrade the F&B options and airline lounges.

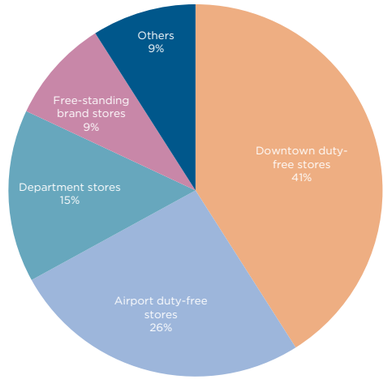
Additionally, design and planning flaws carried over from earlier phases of airport construction mean that subsequent expansions or renovations must address serious service and retail issues. Challenging as that might be, progress is starting to be made. For example, Muji's public area at Shenzhen Bao'an International Airport (SZX) T3 includes a rest area, a business area and a MUJI to GO store. The planned expansions at major airports in Beijing, Shanghai, Guangzhou and Shenzhen—totalling as much as 4.3 million sq m—represent a tremendous opportunity in the not too distant future to reshape Chinese perceptions and expectations of airport retail across the whole country.

Outlets

From 2016 to 2018, 7.5 million sq m of outlet developments were completed; of those, just 30% were classified as tourism outlet centres — typically 50,000 to 150,000 sq m outlets in the suburbs near highways or key tourist sites. Generally, outlets have been evolving in recent years. The average size of an outlet mall has shrunk by 30% as sites have crept closer to city centres in the form of repurposed underperforming department stores. This type of retail format seems to be unique to China.

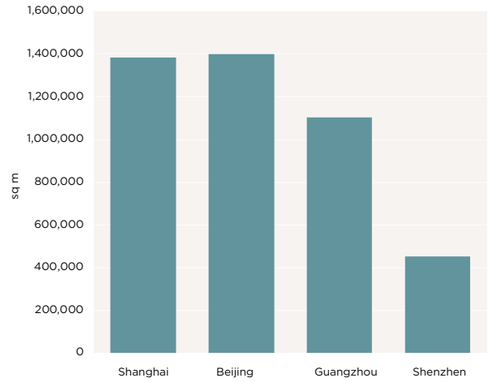
Successful tourism outlet malls in China include Bailian Outlets Plaza in Qingpu District (Shanghai), Florentia Village in Wuqing District (Tianjin), and Capital Outlets in Fangshan District (Beijing). They have become popular destinations for travellers on short breaks and weekend getaways with the catchment area limited to respective cities and neighbouring provinces. Brand selection, product range and pricing remain the biggest challenges for outlet operators whose target consumers are understandably more price-conscious than those who frequent downtown luxury malls.

Chinese overseas consumption by shopping channel



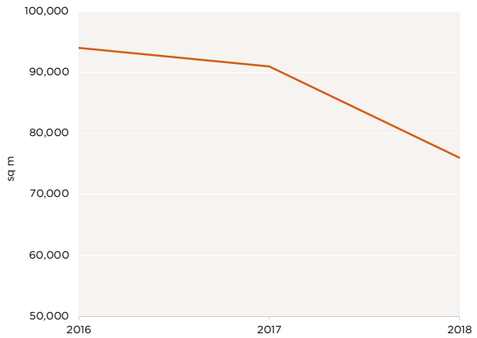
Source McKinsey; Savills Research

Expansion of key airports, 2018 to 2030



Source Savills Research

Average size of outlet malls



Source OutletsCN; Savills Research

Overseas opportunities

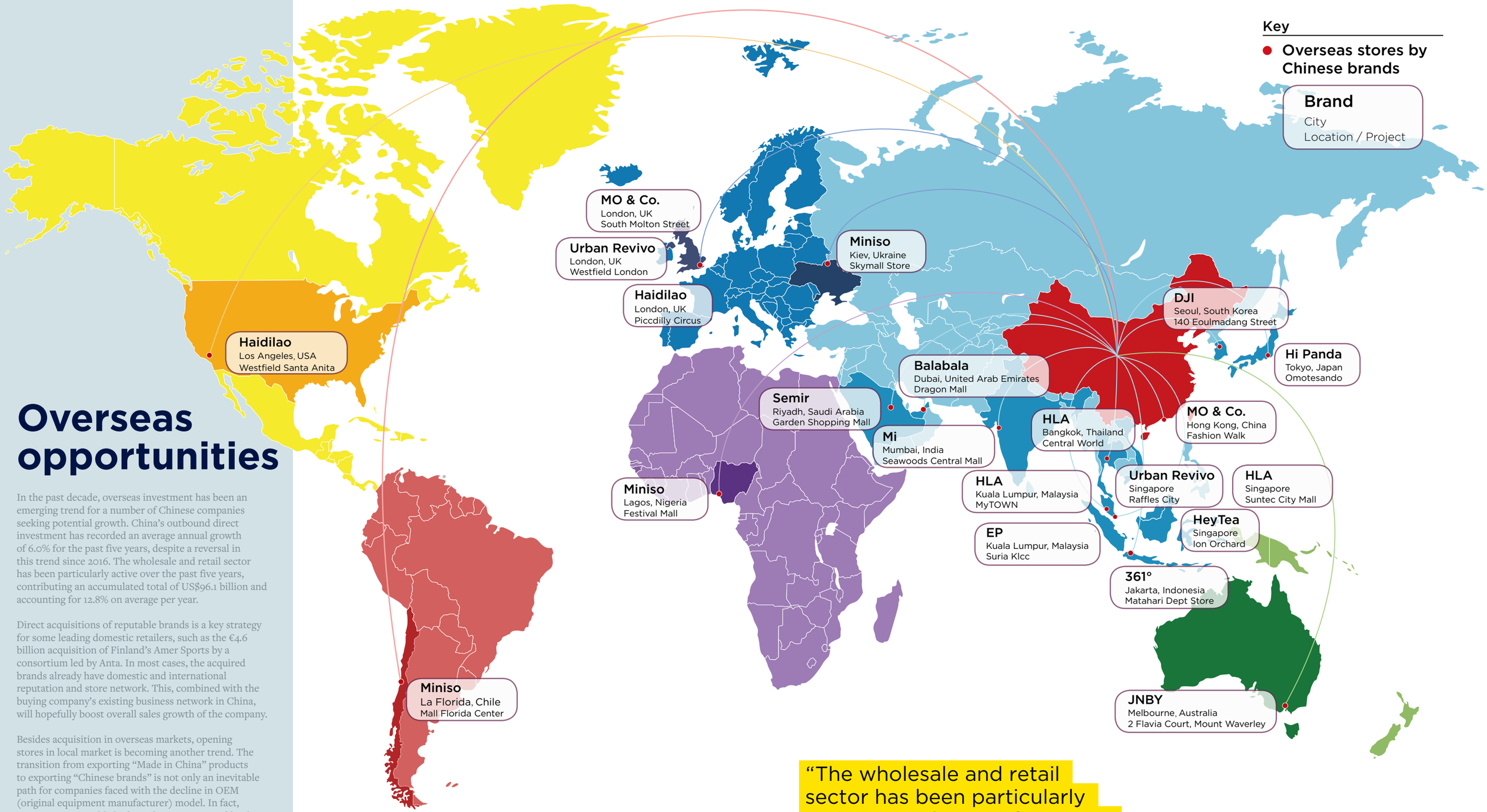
Overseas opportunities

In the past decade, overseas investment has been an emerging trend for a number of Chinese companies seeking potential growth. China's outbound direct investment has recorded an average annual growth of 6.0% for the past five years, despite a reversal in this trend since 2016. The wholesale and retail sector has been particularly active over the past five years, contributing an accumulated total of US$96.1 billion and accounting for 12.8% on average per year.

Direct acquisitions of reputable brands is a key strategy for some leading domestic retailers, such as the €4.6 billion acquisition of Finland's Amer Sports by a consortium led by Anta. In most cases, the acquired brands already have domestic and international reputation and store network. This, combined with the buying company's existing business network in China, will hopefully boost overall sales growth of the company.

Besides acquisition in overseas markets, opening stores in local market is becoming another trend. The transition from exporting "Made in China" products to exporting "Chinese brands" is not only an inevitable path for companies faced with the decline in OEM (original equipment manufacturer) model. In fact, many mature, established retailers are attracted by the potential growth in emerging overseas markets — at a time when the domestic physical market has been adequately served and the benefits of doing business online are starting to fade.

A presence in top global cities may also help them gain access to the world's prime retail destinations and enhance their brand profile.



"The wholesale and retail sector has been particularly active over the past five years, contributing an accumulated total of US$96.1 billion."

Digital and fashion brands lead the way

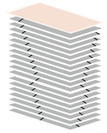
The global consumer market remains dominated by US and European brands, especially in the FMCG and traditional retail categories. Chinese companies, however, are climbing up the rankings. Chinese brands, including Moutai, Huawei, Tencent and Alibaba, took 15 spots in BrandZ's Top 100 Most Valuable Global Brands list for 2019.

Chinese brands made their first international forays back in the 1990s with home appliance brands such as Haier. Recent years have witnessed an increasing number and variety of Chinese brands try their luck outside their home market. Miniso now runs about 200 stores (including franchises) outside China; apparel brand HLA and hotpot chain Haidilao each operate over 20 overseas stores while emerging F&B brands HeyTea and Mellower Coffee are taking their first steps beyond the border.

Of the 100 Chinese brands tracked by Savills, 20 have so far already opened stores outside mainland China, while another 45 have expressed an intention to expand overseas in the near future. A quick store count shows that Southeast Asia is the most favoured destination for Chinese brands, accounting for 33% of existing stores, followed by East Asia (including Hong Kong, Macao and Taiwan) with 21%.

Digital, apparel and NEV brands appear to be the most aggressive in their expansion efforts given the advantages Chinese brands have in these sectors.

For example, while the global fashion supply chain is shifting its focus to Southeast Asia, China is still the world's largest producer of apparel, accounting for 47% of global production as of the end of 2017. In the smartphone market, three Chinese brands are ranked in the top five producers in the world, with a combined market share of 33% : Huawei (3rd), Xiaomi (4th) and OPPO (5th). In the NEV sector, Chinese electric car manufacturers are also growing aggressively — four models from BAIC Motor, JAC Motor and BYD Auto were among the top ten car models in the world by sales volume .



RMB 500,000

How much space can be leased for RMB500,000 per month?

How much space can a retailer secure in a prime retail area or high street for a budget of RMB500,000 per month? Savills data shows that average rent for China's most expensive high street is equivalent to that of prime high streets in Europe's second-tier cities, such as Preciados in Madrid or Zeil in Frankfurt. There is still a long way to go, however, when compared with the world's leading retail streets.

In areas such as West Nanjing Road in Shanghai and Sanlitun in Beijing, a retailer should be able to find a 200 sq m unit for roughly RMB500,000 per month, though available units might be even smaller in the most highly sought after projects. In the Bell Tower area in Xi'an, where rents are less expensive, the same budget would likely stretch to a 1,000 sq m flagship store. In Tokyo's Ginza or Hong Kong's Central district, however, RMB500,000 might only cover the rent for a 50-70 sq m street store, and on New York's Fifth Avenue you would struggle to find a 25 sq m location — the size of a milk tea store — at that price.

Southeast Asia markets, on the other hand, offer very competitive rents and have proved very popular with Chinese brands. The rental rates at Singapore's Orchard Road and Kuala Lumpur's Parkway Plaza are comparable to some of the top high streets in China, while more cost-efficient alternatives can be found in Bangkok, Jakarta and Ho Chi Minh City.

Prime retail areas of major world cities

RETAIL AREA		SHOP SIZE (sq m)
	Fifth Avenue (between 49th - 60th), New York	25
	Central, Hong Kong	50
	Ginza, Tokyo	70
	Collins Street, Melbourne	80
	Myeong-dong, Seoul	125
	Oxford Street, London	135
	Sanlitun, Beijing	200
	West Nanjing Road, Shanghai	230
	Pavilion, Kuala Lumpur	250
	Orchard Road, Singapore	320

Source Savills Research
Note Based on first-floor apparel and accessories store, net area basis.
Exchange rate of USD1: RMB6.8.

Drivers

Aside from the economic challenges, the enthusiasm over the past few years for "New Retail" and online platforms appears to be waning, and the market is once again returning to fundamentals, with consumers and products the defining lynchpins of success.

1. Economic uncertainty – Never a dull moment
Uncertainties surrounding the China-US trade dispute continue to weigh on China's manufacturing and export sectors. The government has recently been taking steps to shore up the economy by transforming and enhancing its financial markets and encouraging consumers to keep on shopping. Import tariff cuts on a variety of consumer goods have helped to buoy certain segments of the market while personal income tax cuts and VAT reform should continue to bolster consumer confidence and take-home pay.

While the short-term performance of the economy may be in question, the bigger picture of a transformed and revitalised economy will bolster retailers' longer-term confidence in the market.

2. Regional integration – Better together
Regional integration is a national-level strategy to boost business investment, further urbanisation and, in doing so, generate greater productivity through the efficient allocation and sharing of resources. These larger population bases, namely the southern Greater Bay Area, the Yangtze River Delta and the Beijing-Tianjin-Hebei region, will become incubators and testing grounds for new retail concepts.

3. Fierce competition – Reinvent or perish
Future retail supply is expected to be significant and will undoubtedly increase market competition. Older projects will find it hard to stay competitive without renovating current premises and continually innovating. Retailers should pay attention to larger shopping malls in emerging areas, as well as renovated boutique projects in central locations.

4. Demanding consumers – Innovation, customisation and digitisation
Market demand for quality retail brands remains robust, supported by a growing middle class and the rising influence of a younger generation of consumers. Effectively reaching and engaging with these consumers will require brands to create innovative concepts, customise products and digitise the retail experience.

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