Responding to crises and changing consumer behaviour

How the retail sector can overcome challenges and capitalise on new opportunities

Impact and challenge of the coronavirus (Covid-19) outbreak on the retail industry

On January 25, 2020, the first day of the Chinese New Year, commercial streets that were crowded in previous years were deserted. Shopping malls, restaurants and fashion stores were closed due to the outbreak of the coronavirus. Meanwhile, Alibaba’s new retail supermarket Hema has been busy sorting, packing and launching products online. According to a report released by Hema, the supermarket put 500,000 packaged vegetables and 80 tonnes of bulk vegetables on both its online and offline shelves in Shanghai on 28 January. The supply of online vegetables has tripled in Beijing. Large quantities of vegetables were also launched online in Guiyang. MissFresh, another new retail supermarket player, has reported a 321 per cent increase in transaction volume nationwide during the first to fourth day of Chinese New Year compared to the same period last year. New and existing users poured in, and the sales per order increased by about 30 RMB, totalling more than 120 RMB per ticket.1 Also, traditional community retail stores, fruit stores, supermarkets and pharmacies were busy as citizens stocked up on groceries and face masks.

The impact of the coronavirus outbreak on different retail formats are quite different. On the one hand, retailers that rely on customer footfall (such as traditional shopping malls and department stores) have taken a considerable hit. On the other hand, emerging community shops and online shops are increasing their trading volume and attracting a mass of new customers. However, these retailers also face supply chain challenges due to traffic controls, limitations of cross provincial procurements and a lack of delivery capacity.

Under such circumstances, it is inevitable the retail industry has been significantly affected by this black swan incident, and it remains to be seen how quickly the industry can recover. However, by the same token, the coronavirus outbreak may introduce new opportunities to the retail industry.

1 [Hexun.com] https://baijiahao.baidu.com/s?id=1657883555581666077&wfr=spider&for=pc
Economic recovery after the coronavirus outbreak

Referencing the SARS outbreak in 2003, macroeconomic conditions in the second half of the year rebounded with double-digit growth after the outbreak. Given that the service sector accounted for 42.5 per cent of GDP in 2003 and more than 50 per cent now, GDP is more dependent on consumption which may lead to a slower recovery compared to the SARS outbreak in 2003.

For the retail industry, the growth rate of total retail sales of consumer goods dropped to 4.3 per cent at the peak of the SARS epidemic, and recovered rapidly once the outbreak was over. Although the coronavirus outbreak is more widespread than SARS, we remain optimistic about the recovery of consumption when the virus is under control, based on the continuous development of new retail and the resilience of the Chinese economy.

For retail firms, this outbreak has demonstrated a lack of crisis preparation. The continuous growth of the domestic retail industry has made many businesses neglect crisis prevention and risk mitigation. The industry could learn lessons from Japan, where natural disasters occur frequently. In 2017, seven major convenience stores and supermarkets, including 7-eleven, ITO-Yokado, Familymart, LAWSON and Aeon, were designated as public authorities, meaning they would assist the government in the event of a disaster. Even before this decision, retailers in Japan, following the East Japan and Kumamoto earthquakes, had begun experimenting with ways to provide disaster relief to local citizens. These stores are equipped with 48-hour emergency power supply, food and daily necessities. They also share disaster relief information with local government and medical authorities. In 2016, 37 supermarkets owned by Aeon were transformed into such stores. Aeon plans to increase the number of such stores to 100 by 2020.

Crises can give rise to both challenges and opportunities, with unforeseen events playing a big role in the transformation and reshaping of the retail industry. The current outbreak is undoubtedly a major blow for brick-and-mortar retail businesses which require large footfall. Many retail enterprises are facing significant cash flow pressures. If the outbreak and the related downturn in consumer confidence do not improve in the first or even the second quarter, many businesses may not survive. However, this will create opportunities for M&A or investments by the industry’s leading firms, as well as online businesses. At the same time, traditional offline retail enterprises will actively seek help regarding sales digitalisation, business transformation and assortment diversification, greatly accelerating integration.

So how do brands, distributors and retailers deal with the crisis and recover from it?

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2 [News.sohu](http://m.sohu.com/a/154143167_99904663)
How can the retail industry quickly restore business and build long-term capabilities?

First, in the short term, companies must keep a tight control on costs. A flexible management approach will be essential to control labour costs, rental costs and the non revenue-generating areas of the business. In addition, business hours can be shortened, which together with a commensurate reduction in salary costs, can keep cash flow at a reasonable level. Meanwhile through this crisis, it is necessary for big brands and retailers to build long-term relationships by helping upstream and downstream enterprises.

Secondly, businesses should urgently prepare their supply chain operations for the economic recovery. From the demand side, as the outbreak hits the retail industry and consumer confidence in the first quarter and even the beginning of the second quarter, we predict that there could be “compensatory” growth. This is especially likely during holidays and the golden week period in the second half of the year, when the outbreak should ease. From the supply side, given the lack of operations in February, small and medium-sized production-oriented enterprises may shut down their business owing to insufficient cash flow. This would in turn create significant challenges in the supply of goods when the economy begins to recover in the second and third quarters. Therefore, in dealing with the crisis in the short term, we recommend that retail enterprises should proactively align with suppliers on the schedule of production and supply for the second half of the year. This may include planning with logistics partners to prepare for the rebound in consumption.

Thirdly, in the long term, it is necessary for retail companies to establish risk prevention mechanisms. Companies need to collaborate with the government, communities, banks and hospitals to establish an emergency mechanism that can help protect people’s livelihoods and reduce the inventory backlog caused by outbreak. After the Kumamoto earthquake hit Japan in 2016, four 7-Eleven plants in Kumamoto were shut down and 16 other plants in Kyushu were required to increase production to ensure the normal delivery of goods to Kumamoto stores. Goods trucks were unable to get into the affected areas at the time due to traffic congestion. However, after it was listed as a “designated public authority”, 7-Eleven had priority to reach the affected areas. In March 2017, 7-Eleven and the Tokushima government collaborated in a pilot to manage the supply plan by using convenience stores. 7-Eleven has a system called “Seven VIEW” that aggregates information about natural disasters such as typhoons and earthquakes and adjusts logistics networks accordingly. When a disaster happens, 7-Eleven can arrange supplies according to information provided by the government on traffic control and refuge locations.²

Last but not least, in line with the trend of long-term business development, enterprises can strengthen their “internal capabilities” in the following areas:

Build “omni-channel” marketing and digital retail capabilities, and continuously innovate business models. We have observed that many enterprises do not maximise the value of their online membership schemes, which are simply used for receiving orders via an app. When facing inventory backlog issues, businesses often encounter difficulties in adjusting supplies due to the lack of data. As a result, companies can leverage this outbreak as an opportunity to identify shortcomings regarding digital technology and talent. It is a chance to enable retailers to embrace technology and upskill employees to ensure they have the right talent to capitalise on opportunities presented by the artificial intelligence and the digital revolution. On one hand, retailers will be able to reach out to consumers more actively and secure their future. On the other hand, innovative business models can help reduce margin costs via investment in automation or artificial intelligence.

While enhancing their digital and online presence, companies should also plan for the future of their brick-and-mortar stores. Big data on footfall, customer profiles and shopping preferences can help retailers judge which store locations have the best long term value, and which could be replaced by online sales to improve overall sales and cost efficiency. During the offline to online transition, companies should prioritise maintaining good relationships with landlords, and focus attention on retraining employees to enable redeployment of talent to digital positions.

² [News.sohu](http://m.sohu.com/a/154143167_99904663)
Accelerate the integration of different formats and categories. For example, following the trend of “one-stop” consumption, cosmeceuticals can be added in offline supermarkets and convenience stores while general merchandise can be also introduced into pharmacies. Large hypermarkets can move towards “fragmented retail”, allowing greater customisation and helping consumers.

Improve the supply chain network and ensure all products have more than two suppliers. Supplies should be guaranteed by setting a reasonable inventory level. Given its geographical advantage, Wuhan plays such a significant role in supply chains that many companies have been affected after the city was locked down. To withstand the impact of such crises in the future, we suggest companies work with suppliers and logistics vendors to make their supply chain more flexible. In Japan, for example, after the Fukushima disaster, auto companies conducted a thorough investigation of the security of all global suppliers from tier 1 to tier 3. This action not only ensures that plants have contingency plans but also further drives the restructuring of the industry and eliminates over reliance on top tier suppliers.

Invest in digitalisation and functionalisation, reduce personnel costs and increase efficiency. We recommend that retail companies invest more in automation and artificial intelligence, such as robotic process automation (RPA), and automated replenishment systems, AI deep learning, to reduce labour costs in the long term. At the same time, the function of retails apps should be fully utilised to ensure communication among employees, suppliers and logistic vendors. Especially when crises occur, apps can be an important tool in bringing front-end store staff and consumers closer and protecting livelihood.

Finally, we urge local governments to further introduce policies on tax relief and loan preference to help enterprises survive the crisis, and be well prepared for the recovery in the second half of the year. Recently, the Suzhou, Shanghai, and Beijing governments have introduced relevant policies. For example, reducing taxes for small and medium-sized enterprises, extension of the payment period for social insurance, providing allowances for employee training, have already been enacted. Local enterprises can also actively contact relevant departments and banks for assistance.

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