

The Contributing Factor to Success and Risk for Warehouse Club in China

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ABSTRACT

In recent years, the warehouse club had become a popular spot for Chinese consumers. The warehouse club possess many differences with the prevailing form of retail which are supermarket Chain and wet market. The paper aims to understand how changes in Chinese market changes combines with some of warehouse clubs' characteristic that contribute to its rapid growth and some potential risks those warehouse club should manage to neutralize. The paper analyzes the trend on digitalization, consumption upgrade and demographic change in China and gather facts from multiple studies and reports on Chinese retail and warehouse clubs to sort out the factors that contribute to the success of warehouse club in China. The further studies could pore into each of the factor and see what strategy could underpin the long-term growth of the warehouse club store.

Keywords: Retail, Warehouse club, digitization, demographic changes, consumption upgrade.

1. INTRODUCTION

The warehouse club retail mode had developed in American for many years. Sams club opened its first store in 1996 in Shenzhen. After years of development, the total numbers of stores of Sams club in china had already reached 21, those stores are mainly plotted in tier1 and tier2 cities. The rate of increase of Sams club store had surged after 2014 at a rate of 18.85% CAGR[1]. This trend indicates that warehouse club mode is gradually mature in China. The income level of China had surged during the recent decades, and the warehouse club store market is expected to expand continuously in the following years. Seeing this trend, many local retail giants are ambitious to enter and compete in this emerging market. As a result, it is very important to understand the factors that boost the success of the warehouse club in China, so those local second movers could learn from the experience of those mature examples like Sams and Costco and keep pace with them in the future. This article argued that the success of existing warehouse club are results from the combining effects of major changes in Chinese consumption market and individual strategy that respond to these changes. The three characteristic changes in consumption market, namely, rise in small sized family, prevalence of consumption on mobile and overall consumption upgrade

in China. The internal factors like sophisticated internal factors including excellent supply chain management [2], well-conceived membership fee mode, ample products with clear segmentation and promote hit products on social media to create social buzz which could attract new customers[3]. However, there are also some potential risks for those companies when the big trend keeps evolving. The consumers' need for better digital experience and pursue for fresh and healthy diet should be attended to as well. The warehouse club may need to develop its localized strategies and swiftly satisfy the new needs of changing customers. The following paragraph will discuss the trend and success factors in detail.

2. ANALYSIS

2.1. The major trends in Chinese market

2.1.1. Consumption upgrades

The First external factor is the consumption upgrade in China. After the reform and open in 1979 and joining the WTO in 2001, The average disposable income of Chinese residents who live in towns had steadily grown over the years and had reached 47412 CNY in 2021[4]. The rise in the income is followed by the change in consumption structure. People gradually shift from basic need consumption to industrial product consumption and

finally to development and enjoyment consumption[5]. The retail sectors are a good example for consumption upgrades. For example, people's awareness on food safety had urged the retail industry to provide better products. More strict sterilization process and exclusion of unhealthy ingredients from the food productions. And customer in some first tier and second tier cities are more than willing to pay a premium on foods in pursue of better products. The supermarkets need to pay extra attention to the mix and selection of SKUs to satisfy customers.

2.1.2. Pandemic and digitization

The second external factor is the outbreak of the pandemic around the globe. The complexity of the supply chain is more unpredictable than ever. The demand is unclear and the declining supply due to the lowered participate rate. Many people are staying out of labor market for the obligation for care taking and fear of pandemics [6]. Additionally, the risk in the delay of shipments also adds to the complexity. From another perspectives, the pandemic also accelerates the digitization trend around the global and especially in China. The consumer habits had shifted more towards online after the pandemic. To be more specifically, the mobilization in consumption, using mobile devices to perform daily consumption, is growing rapidly. According to the data of the Chinese statistical bureau, the people access to internet via mobile devices had already reached 0.986 billion. This foundation had deeply integrated with the growing delivery infrastructure and forge the new map of Chinese retails. All retail participants should attend to this trend.

2.1.3. Demographic changes

According to the 7th national demographic census in China, the population that aged over 60 take up almost 18.7% of all populations[7]. In addition the average size of family had fallen to 2.62, compared with 3.10 in 2010, the family size in china had shirked a lot. These changes will likely lead to changes in consumption patterns and generate new needs in the Chinese markets. For example, small sized package food may be more preferred by customers and inconvenient elder consumers may conduct more purchases remotely and rely on delivery to fulfill some of their basic needs.

The following paragraph will analyze the warehouse club's action and rule out how these strategies and actions adapt to the major market changes, gaining the warehouse club competitive advantages.

2.2. The internal strategies

2.2.1. Supply chain management

The first internal contributing factor is the strong supply chain management ability of these warehouse club

stores. These stores commonly adopt a minimum SKUs strategy. In each category, the brand will on only select 3-4 items[1]. The statistic showed that the number of items per categories in Sams club is only 15.5% percent compared with other supermarket counterparts [2]. Compared to its tradition supermarket counterparts, the management cost on inventory costs could thus be reduced. The warehouse stores also manage upstream to include suppliers into their own system, to filter out the risk of fluctuation in supplies. In addition, the adoption of their own brand's products also helps to squeeze out the profits that originally captured by suppliers. With this mix of the supply chain management strategy, those warehouse club stores can provide goods to customers with a relatively low price while remain good quality. And this ability also acts to partly immune the company from the uncertainty of the global supply chain fluctuation caused by pandemics and give company agility to the changing consumer needs.

2.2.2. Membership fee model

The second factor is the membership fee model of warehouse club. This model helps the warehouse club to identify its target customers and provide best services to this limited number of people. The McKinsey 2021 retail report divide Chinese consumers into four categories which are the Golden family, Moonlighters, Super savers, and 996 professionals. Worth noticing is the golden family and 996 professional's categories. The golden family aged from 35-54 and taken up 40% of the population, they are willing to pay a premium for quality, experience, and service when shopping for groceries. The data indicates that the target customer of those warehouse club is already abundant in China. Successfully transform those potential customers could drive new growth for those warehouse clubs. The warehouse club stores in China normally locate their stores in the outskirts of tier1 and tier2 cities. This Choice of location had matched the targeted customers group and rise the sunk costs for shopping for customers. Considering the long distance to the warehouse club store, the consumption for every trip will be larger than the consumption in normal supermarkets. According to the report of CMS, the average consumption per purchase for customers had surpassed 1000 renminbi in newly opened HEMA X membership store in Shanghai. And, in American and other western countries, the membership fee of warehouse club stores takes up large proportion of its revenue. Withholding the trend in China and experience in other countries, the promotion of membership fee income may continue to grow in the coming years.

2.2.3. Avoidance of competition on fresh market

The third factor is most of the food items that provides by warehouse clubs are frozen products and processed foods. Though after years of supermaketization, the wet

market is still a strong force in fulfilling consumer's need for fresh foods [8]. Other player includes community group buy also add complexity in this domain. Company in the initial stage need to invest heavily, sometimes through brutal price war to attract and maintain new customer. The proportion of fresh food in the warehouse clubs are relatively small compared to the traditional markets. The warehouse club stores' products lay more emphasis on the instant or pre-processed foods. This emphasis may cater the 996 professional's category in McKinney report. People in this category are normally age 18-34, and they lived in tier1 city. They take up about 10% of the market, they have strong purchase power and may have limited time to go to the supermarket. The survey showed that these group of people go to supermarket once a week. They also have habits to purchase all necessities in one stop. The warehouse club's pre-processed and comprehensive collection of necessities could satisfy these people's need. However, one thing worth notice that the increasing pursue of the healthy diet and pursuit of fresh foods may add complexity to the problems and it will be discussed in the later part of the article.

2.2.4. Social network effect

The final factors that largely contribute to the success of the warehouse club in China may relate to the strong social network effect. Nowadays, the social networking apps are act as vital channels to promote the product and establish images for companies. With the momentum of tick-off challenges conducted by KOL and KOC on the social media, some hit products like roast chicken in Sams club had gain massive social buzz on the internet. Those iconic hit product with low price and good quality successfully build positive impression in potential customers' mind. Many new members are attracted to the store through online channel. By wisely maneuver and enhance the online and especially social media touchpoints, the warehouse stores can attract new customer with limited expenses on advertisements.

3. DISCUSSIONS AND FURTHER IMPLICATIONS

Despite the success factors discussed above, some potential risks for warehouse clubs should be considered as well. With the trend in the market, three questions emerged. Firstly, with more small sized family, could the big package mode of warehouse club store continue to survive. Secondly, amid in the digitalization trend, how could the warehouse club adapt to new technologies and maintain competitive advantage versus counterparts in community group buy and supermarket chain that in constant iterations. Thirdly, with the consumption upgrade trend, consumer may prefer fresh food, how could warehouse club respond to it. The article will

briefly explain these questions and give some projected solutions.

3.1. Big package versus small packages

As stated in the introduction part, the average family size in China had already below 3, many of the family are considered as small sized families. As a result, the need for small, packaged food may start to soar in the future. However, the warehouse club stores' products mainly packed in large packages which is contradicted with the trend. To tackle this problem, the warehouse club could not simply change all the package to smaller size. For the big package also help the company to reach scale economy and lower costs of products. The warehouse club could maintain the big package while also design products related to proper storage of the foods and provide customer with more guidance on how to store the food properly. Or alternatively, the company could include separate small packages inside the big packages, so the problem may be relived. However, this solution is merely from the perspective of food preservations, there are more pain spot could be found relating to large packages and corresponding measures should be designed as well.

3.2. Embrace the digitalization in retail

The mobilization and digitalization of the retail will be huge trends that must take into consideration. The digitalization linked goods delivery is yet prevalence in all warehouse clubs. So, there is still space for further improvement. To compete with other form of retails, the warehouse club need to ponder what is its uniqueness strength in the combination of retail and digitization. One may argue that the warehouse clubs are normally located in the rural area of the city which means longer delivery times. This argument may have some ground, but if take the unique membership model of warehouse club stores into consideration, the selective customer will ease the burden of delivery and give warehouse club an advantage in deliveries. The real question is that how warehouse clubs could reach the same efficiency of picking and packing with its counterparts in multiple times larger spaces. To tackle this dilemma, automation could be adopted in the warehouse clubs. And the warehouse club could consider upgrade its warehouse characteristics and evolve to online store plus warehouse mode. But whether this model is cost benefit and accepted by local consumers in China still need further analysis and testing.

3.3. Healthier diet and better foods

The pandemic had raised peoples' awareness towards health. Reflected in diet, people include more fresh foods and nutritional ingredients into their diet structure. The processed food in the Sams that rich in salt and calories may not welcomed by consumers that are growing

conscious. The competitors who have already experienced in selling fresh foods may outperform warehouse clubs in the future. The handy reaction to this trend is to redesign the nutrition proportion for some of the products. Reduce salt, sugar and fat in the foods and emphasis low carbon elements on the package may help.

4. CONCLUSION

This article mainly focused on the trend of growing warehouse club industries in china. after the analysis of big trends in Chinese consumption market and the strategies and tactics of some warehouse club stores, the subtle linkage could be found. This article argues that the tactics and strategies of the warehouse club store accurately respond to major trends in China and thus gain continuous growth during the recent decades. The excellent supply chain management prowess to mitigate the fluctuation brought by pandemics, the membership model that clear grasp targeted customer segmentations and the social network marketing that cater to the digitalization trends are all great examples. Additionally, with those trends persist to exist in the next decades or two. Company should also possess a long-term horizon and plan in advance. Some of the noticeable changes are need for smaller packages, deeper involvement in digitalization and healthier foods. The possible limitation is that pertinent data on warehouse club stores in China is limited, which make evaluation of relative strength of different factors challenging. So based on this, more qualitative studies could be conducted on exactly the strength of these factors. In the meantime, the warehouse club store is still a relatively young form of retail in china, it may need more years to truly found its optimal integration with the Chinese market, how the warehouse

club store reached a symbiosis status with other forms is also a topic worth investigating.

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