



From Financial Crisis to Supply Chain Advantage: An Analysis of Luckin Coffee's Strategic Transformation

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Abstract. This paper delves into how Luckin Coffee, in the face of a financial crisis, achieved a strategic brand transformation by optimizing its supply chain management strategies. The study reveals that supply chain management played a pivotal role in ensuring the quality of raw materials, production efficiency, logistics distribution, and relationships with suppliers, among other aspects. Through close collaboration with suppliers, investments in state-of-the-art roasting factories, and the optimization of logistics distribution systems, Luckin Coffee successfully regained the trust of the market and consumers. Furthermore, Luckin Coffee enhanced user satisfaction and brand loyalty through product innovation and the application of digital technologies. The insights from this research offer valuable references and lessons for other enterprises facing similar challenges.

Keywords: Coffee supply chain; Supply chain management; Financial crisis; Strategic transformation; User satisfaction.

1 Introduction

In the current era of globalization, supply chain management has increasingly become a core element determining the success or failure of enterprises [1]. Especially in the food and beverage industry, various aspects such as the quality of raw materials, production efficiency, logistics distribution, and relationships with suppliers have profound impacts on a company's competitiveness [2]. Luckin Coffee, a rapidly rising coffee chain brand in China, has implemented supply chain management strategies that have significantly contributed to its success, warranting an in-depth investigation [3].

In recent years, the rapid expansion of Luckin Coffee in the Chinese market has garnered widespread attention [4]. However, its financial fraud incident in 2020 dealt a severe blow to the brand's image [5]. Faced with such a significant challenge, how Luckin Coffee leveraged its core supply chain competencies for redemption, regaining the trust of the market and consumers, became a focal point of interest in both the industry and academia [6].

This paper aims to thoroughly analyze how Luckin Coffee, through its supply chain management strategies, ensured the quality and stable supply of raw materials, constructed state-of-the-art roasting factories, and closely collaborated with suppliers to

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achieve a strategic brand transformation [7]. Through a case study on Luckin Coffee, this paper hopes to offer valuable insights and lessons for other enterprises facing similar challenges [8].

2 Research methodology

This study employs the case analysis method to comprehensively investigate the self-redemption strategies adopted by Luckin Coffee, focusing on its core supply chain competencies in response to the "financial fraud" incident [9]. The specific steps are as follows:

(1) Data Collection: Relevant literature and online resources were consulted to gather information related to Luckin Coffee's "financial fraud" incident and its subsequent self-redemption efforts [10].

(2) Case Analysis: Based on the collected data, the specific circumstances of Luckin Coffee's self-redemption using its core supply chain competencies after the "financial fraud" incident were analyzed, and the key factors contributing to its success were identified [11].

(3) Conclusion Synthesis: Throughout the analysis, various pieces of information were systematically organized, leading to the derivation of pertinent conclusions.

2.1 Research design

This study possesses an exploratory objective, investigating how Luckin Coffee, following its "financial fraud" incident, capitalized on its supply chain strengths for self-redemption, turning losses into profits upon re-entry into the market post-delisting [12]. Utilizing a case study analytical approach, this research offers an in-depth exploration of Luckin Coffee's actual sales scenarios. Case studies facilitate insights into real phenomena, enriching empirical descriptions and theoretical development. In other words, this method elucidates in detail how Luckin Coffee leveraged its supply chain advantages for self-redemption. Moreover, case studies enhance the understanding of the interplay between theory and empirical research, being apt for theoretical construction while retaining the flexibility for innovative theoretical development.

2.2 Data Collection and Analysis

This research predominantly employs secondary data collection. Given practical, financial, and reputational considerations, this data enables us to compare the developmental status of various metrics across Luckin Coffee outlets at identical time points. To ensure the credibility and reputation of the data quality, authoritative third-party sources were utilized to circumvent source and researcher biases. These multi-sources encompass industry development reports and survey-based data, such as archived data, public reports, coffee industry research reports, China's Coffee Industry Blue Book, and business wire news. The data collection process involved searching for

pertinent information about the case company via search engines, with data from each case saved as documents, eventually consolidated into a database.

Furthermore, this study adheres to stringent validity and reliability standards. To achieve construct validity, this research employed triangulated secondary data sources, integrating multiple sources like company annual reports, business reports, blogs, and news articles. The collected textual data was integrated into the literature and underwent rigorous thematic analysis. Additionally, we favored third-party data and authoritative reports to minimize over-reliance on internal case data, thereby enhancing the research's reliability.

3 Results

3.1 Enhancing Product Innovation and Retaining User Engagement for Value Creation

Internet enterprises typically adopt a "freemium model" to attract users, profiting through value-added services. Sole reliance on this model, however, struggles to retain long-term user engagement. To ensure sustained user participation, businesses must continually innovate and elevate consumer satisfaction. Taking Luckin Coffee as an example, they implemented a "cashless" strategy, conducting all orders online, thereby amassing vast consumer behavior data. However, given its limited scope for product innovation, Luckin primarily lured repeat purchases through pricing strategies. Despite Luckin's emphasis on its "technology-driven, data-centric" approach, the lack of product innovation and user services challenged the retention of young user loyalty.

After its delisting, Luckin Coffee began prioritizing digital technology for product innovation to enhance user satisfaction. They endeavored to bridge product innovation with consumer preferences, using detailed data operations to guide new product development and iterations. By deeply understanding domestic consumers' coffee taste preferences, Luckin focused on innovative product R&D, consistently launching best-selling items. This strategy gradually established economies of scale, benefiting its business expansion. Concurrently, Luckin Coffee adopted a combination of direct operations and franchising, effectively expanding its presence in lower-tier markets.

By leveraging the emerging retail model of mobile internet and big data technology, Luckin Coffee has positioned itself as an entity that provides consumers with cost-effective coffee beverages. In recent years, the company has consistently launched highly popular products, thereby establishing a certain scale advantage in the competitive coffee market.

In terms of their approach to product operations, Luckin Coffee emphasizes SKU innovation for its coffee beverages, frequently launching best-selling items, thereby amplifying brand influence. They prioritize the R&D of innovative coffee beverages, laying the groundwork for future success. As a domestic coffee brand, Luckin possesses a deep understanding of the general public's coffee taste preferences, which is reflected in their focused efforts towards innovative coffee beverage R&D. This renders their product line richer than other domestic coffee giants. In the year of 2021

alone, Luckin Coffee introduced a remarkable total of 113 new products, further strengthening their groundwork for future best-sellers.

3.2 Refining Cost Structure and Resource Integration to Enhance Core Competitiveness

To enhance its core competitiveness, Luckin Coffee implemented measures to adjust its cost structure and integrate resources. Although initially proclaimed as an asset-light model, Luckin effectively adopted an asset-heavy strategy by rapidly expanding its directly-operated stores. However, this resulted in escalating financial pressures in 2019, as the excessive fixed costs were incongruent with its intended asset-light positioning. Consequently, Luckin undertook strategy adjustments to address this issue, which involved the closure of some directly-operated stores and the introduction of a franchising model in third and fourth-tier cities. By 2022, franchise stores constituted over 30% of the total, contributing to 16.4% of Luckin's revenue. This strategy not only mitigated Luckin's fixed costs but also facilitated additional market expansion and optimization of its logistics network.

The new retail concept emphasizes the deep integration of online, offline, and logistics to better meet customer needs. Considering the complexity of the coffee supply chain, Luckin Coffee strengthened its proprietary supply chain, establishing automated production bases and planning a roasting factory in Kunshan. Additionally, Luckin harnessed digital technology to optimize its operations, such as using intelligent dispatch systems for automatic order allocation and scheduling, real-time sales and inventory monitoring through automated inventory management systems, and an intelligent supply chain management system to enhance procurement efficiency.

In terms of store operations, Luckin Coffee's best-selling products ensured the profitability of individual stores, supporting its rapid store expansion. This strategy gradually established economies of scale. Simultaneously, combining direct operations and franchising, Luckin effectively expanded into lower-tier markets, as shown in Fig. 1.

Luckin Coffee's beverages have garnered widespread acclaim, propelling the brand to a dominant position in the market. This leadership has enabled Luckin to elevate the average selling price of its beverages while sustaining daily sales growth in its directly-operated stores. Such consistent profitability within individual stores has laid a robust foundation for its rapid store expansion, as shown in Fig. 2.

Economies of scale have provided Luckin with a competitive edge in penetrating lower-tier markets. Such advantage is derived from the ability to cater to consumer preferences for convenience, ensuring the support of suppliers in the development of customized products, undertaking consumer education and coffee beverage promotion in lower-tier cities, as well as the optimization of its supply chain. Additionally, the presence of an expansive logistics network and a robust IT infrastructure further augment the company's operational leverage.

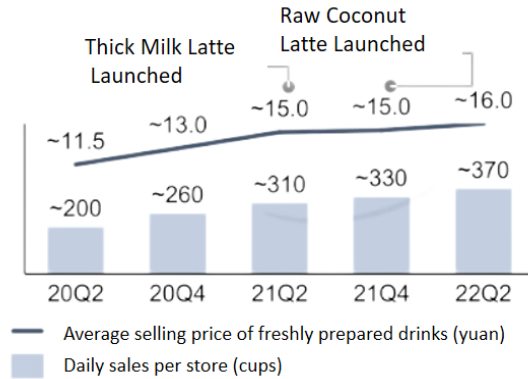


Fig. 1. Average daily sales and average price of drinks at Luckin Coffee Shops

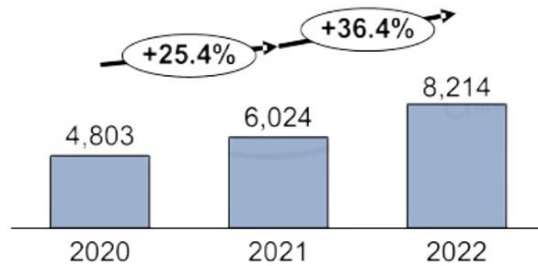


Fig. 2. Store distribution

In its expansion into lower-tier markets, Luckin has adopted a hybrid model of direct operations and franchising. In first and second-tier cities, Luckin continues to expand its directly-operated stores. In contrast, in lower-tier cities, it predominantly employs franchising and joint venture models, aligning with the consumption habits of mid to low-end markets, as shown in Fig. 3.

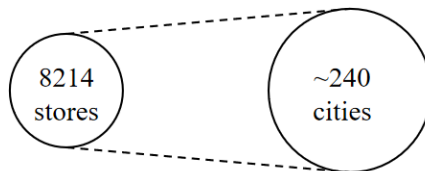


Fig. 3. Scale of Luckin Coffee Outlets

4 Discussion

4.1 Competitive Advantages of Luckin Coffee in the Industry

Luckin Coffee, with its high-quality yet affordably priced products, has challenged the domestic coffee market dominated by foreign brands such as Starbucks [13]. By adopting a new retail strategy, Luckin successfully catered to the online ordering needs of China's vast mobile user base, thereby achieving cost advantages. Luckin Coffee encompasses every aspect of the coffee supply chain, from raw material procurement and intermediate processing to final brand sales, demonstrating its comprehensive market strategy.

Deep Dive into Raw Material Procurement: Luckin sources high-quality green coffee beans from renowned plantations worldwide. Due to its large-scale procurement, Luckin has successfully established a core competitive barrier. According to data, in 2021, Luckin imported 15,808 tons of green beans, and by 2022, this figure exceeded 30,000 tons.

Self-built Roasting Factory: Luckin has established the country's first fully automated roasting base and plans to invest \$120 million in Kunshan to construct an even larger fully automated production base, expected to be completed by 2024, with an annual production capacity projected at 30,000 tons.

4.2 Competitive Disadvantages of Luckin Coffee in the Industry

Luckin Coffee expanded rapidly through extensive advertising and discount strategies. However, due to significant losses and the financial fraud incident, it became overly reliant on equity financing [14]. This could potentially lead to a break in the capital chain, subsequently affecting the company's future. To enhance its brand image and market competitiveness post-financial turmoil, Luckin adjusted its strategy, strengthening supply chain management and product quality control, and investing in advanced roasting factories.

To ensure product quality, Luckin adopted the following measures:

Strict Supply Chain Management: A rigorous system is in place to ensure that every batch of raw materials and finished products adhere to the relevant quality standards.

Quality Inspection and Monitoring: Each store is staffed with highly trained baristas and quality control personnel who conduct regular inspections and continuously monitor the overall quality of the products.

Training and Guidance: A comprehensive training program is provided to franchise stores.

Consumer Feedback Mechanism: Consumer feedback is collected through satisfaction surveys.

4.3 Competitive Threats to Luckin Coffee in the Industry

The domestic coffee market is fiercely competitive. Luckin's products are not proprietary, making it impossible to prevent competitors from imitating. Simultaneously, established brands like Starbucks and Blue Mountain Coffee have more experience in market operations, production techniques, and marketing strategies than Luckin. These factors could hinder Luckin's growth.

4.4 Competitive Opportunities for Luckin Coffee in the Industry

The penetration rate of freshly brewed coffee in the domestic market remains relatively low, presenting a significant opportunity for Luckin. By 2023, it was projected that the per capita consumption of freshly brewed coffee in China would grow from 1.6 cups in 2018 to 5.5 cups. At the end of June 2023, the total number of Luckin stores reached 10836, as shown in Fig. 4. Luckin has attracted a vast consumer base, through continuous promotions and quality enhancements. It has accumulated a transactional customer base of over 170 million, with an average monthly transactional customer count of 43.07 million in the second quarter. These figures indicate that Luckin has recovered from its previous financial turmoil and has once again established itself as the leader in China's affordable "quick coffee" segment.

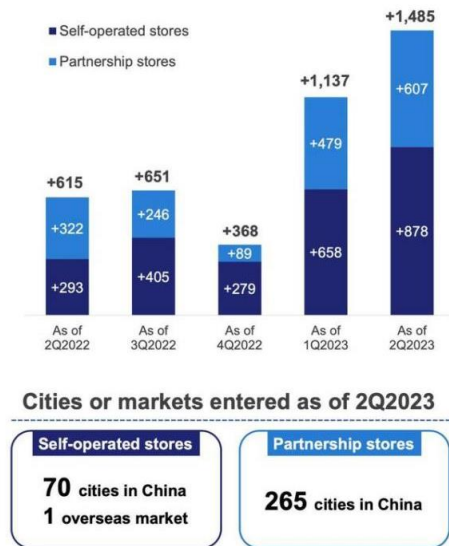


Fig. 4. Net new store openings

5 Conclusion

This study delves deeply into the pivotal role of supply chain management in the modern business environment, particularly its impact within the rapidly emerging brand, Luckin Coffee. The research suggests that supply chain management is crucial

for ensuring the quality and consistent supply of raw materials, especially in the coffee industry where inputs like coffee beans are influenced by various external factors. This implies that raw material supply can be interrupted, leading to price fluctuations. By optimizing its supply chain, Luckin Coffee not only ensures high-quality raw materials but can also navigate market price fluctuations and exchange rate changes. This provides Luckin Coffee with a stable cost foundation, enabling it to offer competitive prices in the market.

Luckin Coffee's success isn't solely reliant on raw material supply. To ensure product quality and consistency, Luckin has invested in state-of-the-art roasting factories. These factories employ cutting-edge international technologies and a complete set of imported advanced green bean processing equipment, achieving full automation from green bean processing to roasting and packaging. This not only enhances production efficiency but also ensures that every cup of Luckin Coffee meets consistent high-quality standards.

Supply chain management isn't just about production and logistics; it also involves relationship management with suppliers. Luckin Coffee has established close collaborations with its suppliers, allowing it to access the finest raw materials and ensuring supply chain stability. Furthermore, due to its large-scale procurement, Luckin Coffee can negotiate more favorable prices with suppliers, further enhancing its cost advantage.

Efficient logistics and distribution play a crucial role in the coffee industry, particularly within the fast-moving consumer goods sector. Luckin Coffee has successfully optimized its supply chain to realize efficient distribution from the factory to the store. This not only leads to cost savings in transportation but also guarantees product freshness, thereby enabling consumers to enjoy the highest quality experience.

More importantly, supply chain management provides Luckin Coffee with a sustained competitive edge, allowing it to stand out in a fiercely competitive market. Additionally, effective supply chain management aids in enhancing brand image, ensuring product quality, consistency, and timely delivery, thereby establishing a brand's reliability and high-quality image.

In conclusion, supply chain management plays a pivotal role in the success of Luckin Coffee. Through continuous optimization and management of the supply chain, Luckin Coffee's rapid market expansion and brand image enhancement have been solidly supported. This offers invaluable insights and lessons for other enterprises seeking rapid growth.

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