



China's Retailers and the Coronavirus Outbreak: Lessons from the Past

For a sector already in flux, the crisis presents two
looming challenges: bottlenecks and shortages.

By Jonathan Cheng

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At a Glance

- ▶ Maintaining the trust of retailers' customers and staff will be vital as the coronavirus epidemic continues.
- ▶ Executives can use lessons from past emergencies in Asia to help them plan for an eventual recovery in demand.
- ▶ Longer term, the crisis has highlighted the need for traditional retailers to keep improving their omnichannel offering and supply chains.

While health workers heroically confront the coronavirus outbreak, Chinese business leaders and employees are aiding the fight in the background. Retail is one of the sectors playing a supporting role. Over recent weeks, we've seen retailers striving around the clock in hard-hit areas of China. Store staffers are courageously returning to work despite the risk of infection. Supply chain specialists are using all their expertise to ensure that basic necessities remain widely available. Merchants are refusing to take time off to focus on solving their own procurement issues.

As they continue to make their quiet contributions to the coronavirus response, retail management teams face two looming challenges. The first is a logistical bottleneck. Transport routes have been severely disrupted, of course, by the closure of cities for quarantine purposes, while many warehouse and logistics personnel are unable to come to work because of illness or restrictions on movement. The second challenge is imminent supply shortages, linked to uncertainty about when factories will resume production.

Managing these evolving operational complications is more than a full-time job, but at the same time Chinese retail executives can't afford to lose sight of their strategic goals. It's still unclear how the outbreak might reshape a competitive landscape already in flux. However, examining the shape of retail's recovery in two previous epidemics and one natural disaster can point to what might lie ahead both for the sector and individual product categories. Likewise, we think that viewing the crisis through the prism of some of today's key retailer models can help executives anticipate the strategic implications for their companies.

Retail's recovery in three Asian crises

We looked at the retail sales impact of the SARS epidemic in China in 2003; the earthquake, tsunami and Fukushima nuclear disaster in Japan in 2011; and the MERS epidemic in South Korea in 2015. In all three cases, there were three phases: shock, recovery and stabilization. But the timing and trajectory of each phase differed.

A month after the spread of SARS ended in May 2003, Chinese sales had bounced back to their preepidemic levels and they stabilized by July. The retail sales growth dip was much more pronounced in Japan in 2011, as was the subsequent recovery; the stabilization period was also bumpier than in

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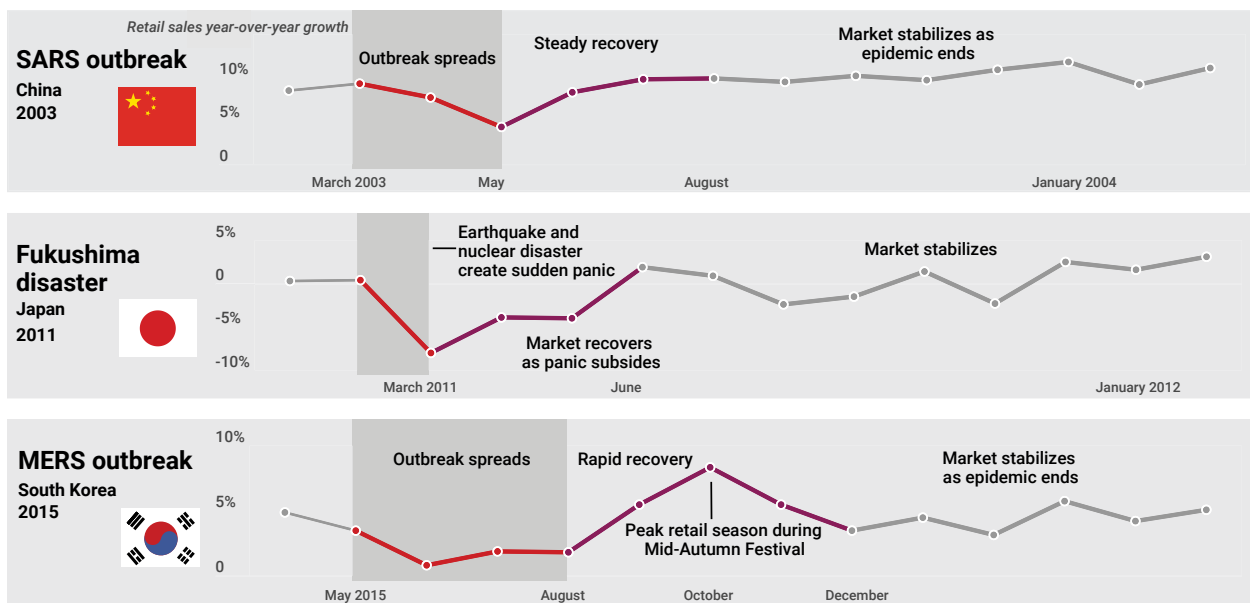
China after SARS. In South Korea, though, the rapid recovery from MERS in 2015 took retail sales growth beyond its precrisis trend, as it coincided with the Mid-Autumn Festival. The market then stabilized at a lower level, give or take some fluctuation.

Within retail categories, demand variations during and after a crisis tend to follow three patterns (see figure below). The first applies to staples such as fresh food and baby care products; demand in these cases tends to spike during the emergency because of panic buying, before resuming a more stable rhythm. Other products also see a spike in a crisis, but with a much steeper decline in demand when normality returns as hoarded items are gradually used up. Categories affected in this manner include health-protection items such as disinfectant or hand sanitizer, as well as home cleaning products. Then there’s a third group that follows a “dip and rebound” pattern as shoppers defer purchases during the crisis and then return in droves when safe. Clothes and cosmetics are among the products subject to this sudden release of pent-up demand.

In our experience, consumer preferences can also be skewed by a crisis—and not just temporarily. Fresh produce tends to become more important, benefiting retailers that offer a compelling fresh assortment at keen prices in the most trying circumstances (and beyond). Food and product safety also rises up the list of consumer priorities, rewarding retail brands that have consistently projected an image of quality and reliability.

Above all, loyalty can be reinforced or broken at moments of extreme social stress. In the aftermath of Hurricane Katrina in 2005, for instance, the calm efficiency of some US retailers was a notable help

Retail markets typically dip during a crisis, but eventually stabilize



Sources: China National Bureau of Statistics; Japan Ministry of Economy, Trade and Industry; South Korea government statistics

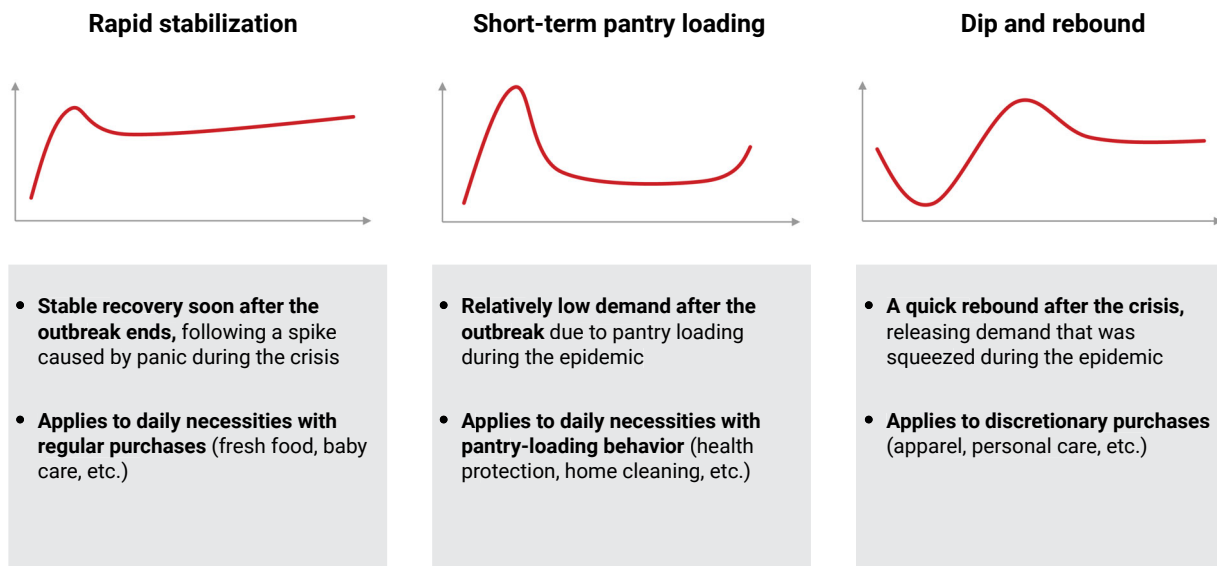
to the relief effort. Similarly, after the 2011 Fukushima disaster, convenience stores deepened their bond with grateful Japanese shoppers by rapidly resuming operations with supplies of basic goods.

Strategic implications for retailers

The disruption caused by the coronavirus comes at a time of intense change for the retail industry. Globally, Bain & Company analysis suggests that seven types of retailer are prevalent today, but not all of them will thrive, or even survive, in the future (see the Bain Brief “The Future of Retail: Winning Models for a New Era”). In China, the public health emergency may well end up exacerbating the broader trends that are already creating winners and losers. For instance, it has so far accelerated the shift from traditional store-based selling to purely digital or omnichannel retailing—just as SARS prompted upstart entrepreneurs to embrace the full potential of e-commerce almost two decades ago.

Ecosystem players are unlikely to suffer long-term damage from the coronavirus outbreak. These are digital natives that have built one-stop online shops spanning retailing, chat, entertainment, payments and a host of other services. As they avoid public gatherings, people in China have been increasingly living online within these ecosystems. True, ecosystem players have also suffered substantial short-term disruption to trading. Food delivery, for instance, has been hit by restaurant closures, while merchants trading on ecosystem marketplaces have faced supply issues. But the inexorable shift online means the strategic challenge for China's ecosystem players is likely to remain positive: maintaining service levels amid continued business growth.

Demand fluctuates after an epidemic, but tends to follow one of three patterns



Dynamic traditional retailers with a significant national or international presence (we call them scale fighters) are financially well placed to withstand the short-term coronavirus disruption. The breadth of their supplier network is likely to emerge as a strength, enabling them to get around some of the emerging bottlenecks, and they tend to have a significant enough online presence. Yet their scale can also be a source of weakness; that bulk can slow down decisions in changing circumstances, whether that be the logistical challenge posed by an unfolding crisis or a shift in consumer tastes after a crisis is eventually resolved.

Regional retail chains don't have the same capacity to absorb financial shocks as scale fighters. If they don't have an exceptionally good regional supplier base, they could also be more prone to supply bottlenecks. But the local presence and relationships built up by the sector's strongest regional players—regional gems, in our analysis—also has the potential to be an asset, particularly if they show empathy and common cause with their communities.

The challenges posed by the outbreak are even more pronounced for retail's legacy laggards—store chains that have struggled to adapt to the rise of online channels and other market changes over recent years. Legacy laggards aren't known for responding nimbly to events, have a disproportionate focus on physical store traffic and are often financially fragile, making cash flow disruption particularly threatening. That said, if they have conveniently located stores, legacy laggards could reconnect with old customers who might have been taking their continued presence for granted.

How Chinese retailers can increase their resilience

Trust will be vital now and for the foreseeable future. As the epidemic continues, relationships between retailers, their customers and their staff will likely come under further strain. Shoppers expect stores to keep products on their shelves and not compromise on quality. Even as they face mounting logistical pressures, retailers must strive to meet those expectations through proactive decision making and a willingness to make trade-offs elsewhere. Many employees need reassurance and support as they brave possible infection and take a financial hit from delayed and reduced work. That support is likely to be paid back over the long term.

The crisis has rendered current annual budgets meaningless, thanks to the short-term decline in consumer demand and increased operating costs. Retailers should quickly adjust their annual forecasts with more realistic P&L estimates and reallocate resources as needed. Yet past crises have shown how vital it is to plan for an eventual resumption of normality, even as companies scramble to manage and quantify the disruption. That's understandably hard to do (or even contemplate) when health concerns are still paramount. But when pent-up demand is released, unprepared companies can struggle to retain existing shoppers or form a lasting bond with new customers.

Other actions with a longer time frame can help retailers cope better with similar crises in the future, while reinforcing their defenses against the strategic pressures building in the sector. By stimulating demand for online shopping, the outbreak has highlighted the broader need for traditional retailers to keep moving away from a reliance on brick-and-mortar stores to an omnichannel model, for instance. Likewise, leadership teams should aspire to strengthen their supply chains by applying lessons they have learned in recent weeks—and will continue to learn during the uncertainty ahead.

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