

Moving towards true omnichannel

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With online shopping on the rise, retailers in Hong Kong are smartly remodelling their businesses towards an omnichannel strategy to provide consumers what they desire – a seamless shopping experience. Given an impulse to innovate during the latest retail market downturn, brands are investing more in their ecommerce operations and adopt in-store digitisation tools to integrate online and offline channels in order to capture the loyalty of increasingly demanding customers. Thanks to improved market conditions, Hong Kong's retail market has ended 2017 on a positive vibe with overall retail sales growing 1.8% YOY from January until November 2017. While prime retail rents dipped another 5% YOY in 2017, we expect a slight recovery on first-tier high-streets in 2018. Based on the growing confidence in the overall retail market, particularly spurred by continuing expansion of premium accessories, lifestyle apparel, cosmetics and F&B, we foresee retail sales to rise by 4-5% YOY in 2018.

Forecasts



Demand

International mid-market fashion and lifestyle brands are thriving, new F&B concepts continue expansion, luxury watches and jewellery demand continues slow recovery.



Rent

Overall high-street rents in key districts fell by 5% in 2017. In 2018, we expect a slight rise of 1-3% YOY, while second and third-tier high-streets will likely remain under pressure in H1.



Supply

We expect 1.38 million sq ft (128,600 sq m) of new retail space to come to the market in 2018 in core retail districts.



Retail Sales

Retail sales grew 5.7% YOY in October and November 2017 combined. A key contributor was the jewellery and watch sector. We expect overall retail sales growth of around 2% YOY in 2017 and accelerating growth of 4-5% in 2018 and 2019, respectively.



2018 High-Street Retail Rents Projection

District	QOQ	2017YOY	2018F
Overall Rental Index*	-0.9%	-5%	+2%
Central	-3.4%	-8%	+2%
Causeway Bay	-0.6%	-4%	+2%
Tsim Sha Tsui	-0.7%	-4%	+3%
Mong Kok	+1.4%	-5%	+5%

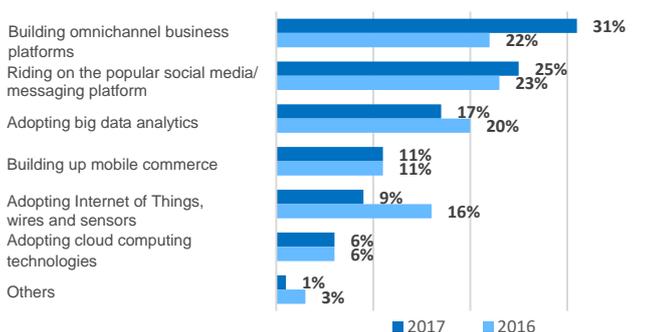
Index: Nov 2011 = 100. * Street level shops on key street segments
Source: Colliers

Development of integrated sales channels in retailer focus

2017 has marked a revival of Hong Kong's retail market. After a downturn lasting three years, prime retail streets and shopping centres appeared much busier, especially during the holiday season. Despite tourists significantly contributing to overall retail sales, local consumers have been a major driving force for the market upturn, with private consumption expenditure expanding notably by 6.7% YOY in Q3 thanks to strong job and employment conditions. A robust ongoing recovery in inbound tourism numbers has further fuelled the upswing. To cater to the likes of both the local audience and tourists, major shopping centres have been revamping their tenant mix and reducing shop sizes to create a broader and balanced selection featuring more lifestyle brands and F&B. Swire for instance, has doubled its F&B offerings in Pacific Place since mid-2016. As shopping centres are turning into hubs for leisure activities, adding elements such as F&B, entertainment and sports and lifestyle brands is inviting consumers to spend more time in malls.

Apart from this development, retailers are aware of the rising online shopping trend and the potential profit growth arising from it. Alibaba's 'Double 11', China's largest e-commerce festival illustrates the extent of changing consumer habits. First introduced in Hong Kong in 2016, Alibaba reported that this year Hong Kong ranked second in terms of cross-border transaction volume; representing an indicator for the growing popularity of online shopping. Companies are reacting and are upgrading their online presence. A recent CEO survey conducted by KPMG and YouGov¹ illustrates these initiatives, as 62% of responding companies plan to increase ecommerce investments by more than 10% in the next twelve months, while 52% invested 10% more and beyond in the past twelve months.

Most Important Digital Innovation Strategies for the next Two Years for Hong Kong Companies



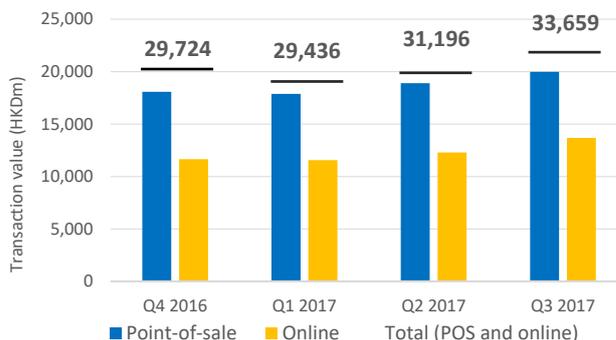
Source: KPMG and GS1 Survey analysis 2017

With the digital revolution expanding its footprint in retail, success of individual brands will depend on the retailer's capability and speed of adaptation. A revamped online presence alone doesn't do the trick as customers increasingly expect a seamless shopping experience with the same services in every sales channel. Major consultancies including McKinsey² and Accenture³ support our view that the growing demand for a frictionless brand experience makes an integration of online and offline channels necessary. Smart retailers are changing their operation models and integrating channels via an omnichannel strategy to capture the new customer demand. This so called omnichannel strategy creates seamless convergence between online, mobile and offline sales channels where customers can start their shopping journey in one channel and finish it in another while having access to all promotions and loyalty points across channels. Given the benefits for retailers and the customers, we expect more brands to make use of its merits. KMPGs survey shows that, recognising its importance, building omnichannel business platforms is the most important digital innovation technology for the coming two years for companies surveyed.

In-store digitisation as enabler to bridge offline and online

The adoption of a digital strategy with AI powered data analytics tools is a key enabler for a seamless integration of online and physical retail. IoT applications that help with inventory management, such as automated inventory tracking in real time as suggested by Fung Global Retail⁴ is an effective tool for improving customer experience as it can help retailers to predict future purchases and therefore optimise stock. We found that mobile payment apps can function as a facilitator for an omnichannel strategy. During the 'Golden Week', Alipay e-wallet users conducted eight times more in-store transactions overseas than in 2016, with Hong Kong topping the list for in-store cross-border payment

Development of mobile payment via HKD denominated e-wallets in Hong Kong



Source: Hong Kong Monetary Authority

transaction volume, according to local news. Thanks to an expanding mobile payment network and promotions seen during Alipay's newly launched international 'Double 12 Festival' in Hong Kong, where discounts were also offered to local Alipay users, e-wallet use by local consumers picked up noticeably. Data from the Hong Kong Monetary Authority supports our findings, showing that since the roll out of SVF licences in 2016, the transaction value of mobile payments via HKD denominated e-wallets in physical stores rose by 10.6% from Q4 2016 to Q3 2017, while jumping more than 17% for online mobile payments. Feeling the pressure to catch up with competing mobile payment platforms, Octopus has recently introduced a QR code payment trial, reported by local newspapers. We expect that the acceptance of e-wallets among local residents is likely to accelerate further if Octopus decides to expand the new feature.

Further applications include Smart Screens as seen at Tmall's pop-up store in Hong Kong's airport during 'Double 11'. Customers could pick up products equipped with Bluetooth and a screen automatically displayed product information. By logging into their Taobao account users could buy the products online by using mobile payment via QR code. Furthermore, mobile payment can be used in staff-free future-stores, as already in operation in China and other countries. For instance, the Chinese company BingoBox said in an interview with SCMP that it plans to roll out its unmanned convenience stores in Hong Kong where customers enter by scanning a QR code and pay with their e-wallet by scanning RFID tag equipped products. Showcasing its new strategy featuring omnichannel functions, Abercrombie & Fitch is enabling customers to place and pick-up online orders and to return items purchased online in its new store in Harbour City. Looking forward, we foresee an increasing number of brands using different in-store digitisation tools to deliver improved consumer experiences through sales channel integration.

Retail sales are accelerating

Good consumer sentiment and increased consumption has steadily helped overall retail sales return to positive territory in 2017, growing 1.8% YOY from January until November. A rise in mainland Chinese tourists and local demand spurred medicine and cosmetics sales which grew 4.8% YOY in the same period. Sa Sa reported an increase in average sales per transaction for both local and mainland customers in its recent interim report, indicating the strength of consumer spending power.

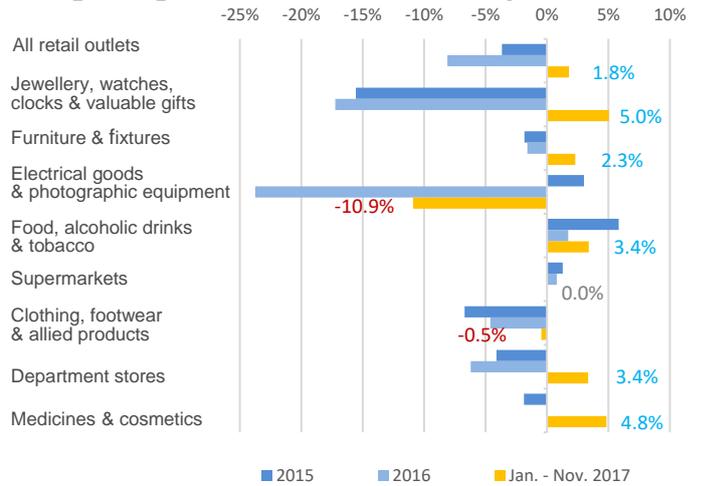
Demand for premium watches and designer jewellery rather than luxury jewellery has also been fuelling the recovery of this subsector, sparking cautious optimism among retailers. Improved jewellery and watch sales results of 5% YOY until November were partially attributed to rental savings. Despite its relatively slow recovery, the jewellery and watch sector remains one of the main contributors to overall retail sales. The sales decline for electrical goods, and clothing and footwear narrowed substantially. Based on this upturn we expect the recovery course to continue over 2018 with a 4-5% YOY sales growth.

Mild rent recovery for first-tier high-streets in 2018

In 2017, overall high-street retail rent decline narrowed to 5% YOY, a strong improvement compared to the slump of almost 18% YOY we recorded at the end of 2016. Despite rental decline remaining with 0.9% QOQ at the same rate as in Q3, there have been some notable improvements on a district level. Several first-tier high-streets across districts, except for Central, recorded a positive QOQ growth in Q4. Mong Kok, led by stronger rents on Sai Yeung Choi Street South, returned to positive territory, with rents edging up 1.4% QOQ.

In 2018, we expect a more stratified rental market with a widening rental gap between first-tier, and second and third-tier high-streets within the same district. Favourable rents on first-tier high-streets are driving demand. Instead of large flagship stores, retailers are favouring smaller sized shops ranging from 1,000-5,000 sq ft (93-465 sq m) which can emphasize innovative store concepts and fit-outs that create a more personal and themed atmosphere. Based on the robust demand for prime locations, we believe overall high-street rents are set to increase by 1-3% YOY in 2018, led by stronger rents on first-tier high-streets. However, second and third-tier high-streets will remain under pressure and are likely drop by a lower single-digit in H1 2018.

Hong Kong's Retail Sales Growth by Subsector

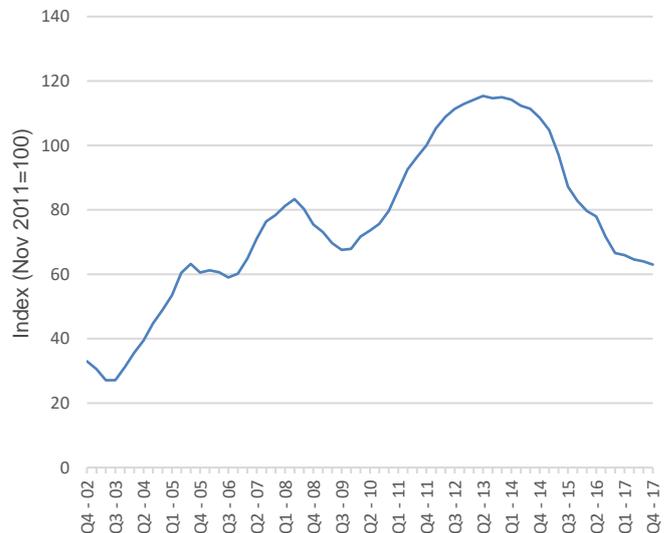


Development of Total Retail Sales in Hong Kong



Source: Census and Statistics Department, Colliers

Hong Kong High-street Retail Rental Index



Source: Colliers

- 1 KPMG 2017;
- 2 McKinsey 2017;
- 3 Accenture 2017;
- 4 Fung Global Retail 2017



Strong leasing activity of lifestyle brands and F&B concepts

Major shopping malls have offered comprehensive performances, activities, and stalls to capture the positive vibe and drive foot traffic. The variety of pop-up installations during the festive season helped boost sales and to test new brands in the market. Various developers and landlords focused on shopping centre decorations and related activities to attract shoppers during the festive season, including ballet in Pacific Place, a soft toy circus in the Landmark, and a giant Santa airship in Harbour City.

Instead of traditional luxury items, the areas of expansion in 2017 have been lifestyle, F&B, and premium accessories, with young affluent millennials as key target market. Aware of the spending power and shopping preferences of this group of consumers, young affordable international fashion and lifestyle brands have established a presence or expanded their footprint in Hong Kong. Brands leveraged the opportunity of opening shops in prime locations due to favourable rents. Major League Baseball (MLB), an international contemporary fashion apparel label, has entered Hong Kong, setting up its first stand-alone flagship store on Sai Yeung Choi Street South, Mong Kok's prime street.

The popular Swedish watch brand Daniel Wellington (DW) launched its first stand-alone flagship store on prominent Russell Street in Causeway Bay. The German sports brand Puma has also opened a new flagship store in the newly renovated Fashion Walk in Causeway Bay which is featuring numerous lifestyle brands. F&B continued to show great leasing activity backed by a continuous rise of restaurant receipt values which grew by a solid 5.1% YOY in Q3 2017. Jamie's Deli, a casual food concept by the renowned chef has opened in Harbour City, marking its first outlet in Asia, while restaurants featuring international cuisine such as Pirata Group and the Black Sheep Restaurants continued to lead an aggressive expansion in the market.

The fact that numerous retail brands across sectors are choosing Hong Kong as stepping stone to kick off their international expansion is an indicator for business confidence in the market. However, with retail disruptors on the rise, embracing new data analytics tools and technology that is integrated in an omnichannel strategy to understand customer preferences is key to providing an excellent shopping experience and long-term success. Given the growing number of technological initiatives, a sustained strong employment market together with a continuing recovery of inbound tourism, we look positively into 2018 and foresee the retail market to gain further momentum.

Selected Lease Transactions in Q4 2017

District	Tenant	Address	Floor/ Unit	GFA (sq ft)	Lease Type
Mong Kok	Xiaomi	Chong Hing Square, 601 Nathan Rd	G/F	6,208	New Lease
Mong Kok	Mannings	Grand Plaza, 639 Nathan Rd	G/F	3,500	New Lease
Mong Kok	MLB	52-54 Sai Yeung Choi Street S	G/F & 1/F	3,600	New Lease
Causeway Bay	Carl F. Bucherer	Clover Commercial Building, 58 Russell St	G/F	550	New Lease
Causeway Bay	Daniel Wellington	Lai Yuen Apartments, 59-61 Russell St	G/F	780	New Lease
Central	Nightclub	Silver Fortune Plaza, 1 Wellington St	LG/F, UG/F, 1/F & 2/F	20,119	New Lease
Central	Mercedes Me	Manning House, 38-48 Queen's Rd C	G/F & 1/F	4,797	New Lease

Source: EPRC, Colliers

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