Innovative localization of Costco Paid Membership Model in China Based on PEST Analysis

Murong Ren[1, a], Litian Wang[2, b]

[1]School of Accounting, Shanxi University of Finance and Economics, Taiyuan, China

[2]Faculty of International Trade, Shanxi University of Finance and Economics, Taiyuan, China

[a]Evelynshurmr@163.com, [b]1608572977@qq.com

Keywords: Trade Economy; Costco Paid Membership; Localization Improvement; Pest Analysis

Abstract: Costco Shanghai Minhang store has undergone a transformation from boom to the gradual " Membership cards return ", attracting attention from a host of people. This paper makes an in-depth study of it, comparing Costco Shanghai Minhang store with other supermarkets that have already adapted to the Chinese market, and comes to the conclusion the reason why it has encountered the "Membership cards return" in China. Besides, this paper proposes an improved approach to localize Costco's paid membership income model in China based on PEST analysis, that is, to apply it to Chinese convenience stores.

1. Introduction.

Costco, the largest member-owned warehouse supermarket chain in the United States, opened China's first store in Shanghai on August 27th, 2019. Since its opening, Costco Shanghai Minhang store has been so welcomed by Chinese consumers that business was suspended five hours after the first day due to a large number of customers. Within a week, however, the situation had changed, with customers lining up to cancel their membership cards. The contrast leads us to think about how the paid membership revenue model could work in China.

2. Analysis of Causes.

2.1 Direct Causes.

The direct reason for the Costco " Membership cards return " is the decline in discount rates. For example, the famous MaoTai whose price is 1,498 yuan is no longer on sale. The two bottles of whole frozen milk that originally sold for 32.9 yuan have been adjusted to 53.9 yuan. Naturally, it would be less attractive to consumers. The contrast between the boom and "Membership cards return" suggests that the boom before is just a sign that Chinese consumers are acknowledging Costco's low prices, rather than an recognition of the Costco's brand and the business model. So there's still some fundamental reasons behind this.

2.2 Root Causes.

According to the theory of consumer purchase behavior, consumer's consumption habit is one of the important factors that affect consumer's purchase behavior. The shopping habits of Chinese are very different from those of Americans. As a result, we believe that consumer shopping habits are the root cause of " Membership cards return ".

2.2.1 Chinese Consumers' Preference for Fresh Produce.

American consumers often go to the supermarket and buy a large quantity of food to store up for a long time. But in China, consumers prefer smaller batches of fresh food. When Walmart first entered the Chinese market, it tried to package and sell meat to Chinese consumers, but they rejected it. Later, Walmart adjusted its business strategy to present the meat as fresh as possible to consumers, and made localized improvements to adapt to the Chinese market, which was recognized by Chinese

consumers. Thus, the Chinese people's preference for fresh food can be seen.
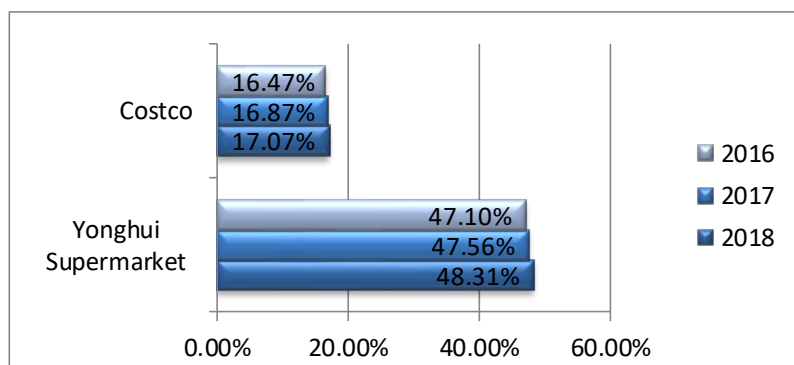

Figure 1. 2016-2018 Comparison of Fresh Food Percentage of Sales.

(Source: Company Financial Statements)

By comparison, Yonghui supermarket fresh food income is much higher than that of Costco, indicating that Costco's guidelines on fresh food are not adequate for Chinese consumers.

2.2.2 Chinese Consumers' Preference for Supermarkets in Busy Areas.

Traditional Chinese supermarkets are often located in busy areas or near residential communities. And in recent years, Chinese people have become busier and more time-consuming, which makes Chinese consumers demand more convenient shopping. But Costco often operates in the suburbs far from the city, which is not in line with Chinese spending habits.

Table 1 compares the locations of Shanghai's famous retail supermarket with those of Costco's minhang store in Shanghai. In this table, the number of malls within 2km and the number of banks within 1km are used to measure the prosperity of the lot

Table 1 Comparison of the Prosperity of the Location of Shops.

Supermarkets	Shopping Malls within 2 km	The Number of Banks within 1 km
Walmart (Shanghai Jiangqiao Store)	13	23
Century Lianhua Supermarket (Pudian Store)	29	87
Carrefour (Wuning Store)	26	97
Costco (Minhang Store)	3	0

As showed in Table 1, by comparison, it can be seen that representative supermarkets choose prosperous areas. Nonetheless, Costco is located on the outskirts of Shanghai. The inconvenience of the location, coupling with China's traffic congestion and high population density, Costco Shanghai Minhang store will have a hard time attracting customers over the long term without Innovative localization. Table 2 shows the population density of the United States and China.

Table 2 Population Density in China and the United States.

Indicators	Population Density Per Square Kilometer		Indicators	Population Density Per Square Kilometer	
Years	China	The United States	Years	China	The United States
2007	140.38	32.88	2013	144.58	34.55
2008	141.1	33.24	2014	145.32	34.81
2009	141.8	33.54	2015	146.06	35.06
2010	142.49	33.82	2016	146.85	35.32
2011	143.17	34.06	2017	147.67	35.55
2012	143.87	34.31	2018	148.35	35.77

2.2.3 Chinese Consumers' Shopping Preferences.

According to AC Nielsen, Chinese consumers tend to shop more frequently, spend less on a single purchase, and prefer different shopping channels. Costco's products are packed in large quantity, while it's rare in China to stock up on anything, especially food. In addition, one of Costco's key ways to achieve "good quality and low prices" is to streamline the SKU, which on average have only 3,800 active SKU across all co-branded and homemade products in Costco stores. Costco only offers one or two SKU per small category. Chinese people are accustomed to choosing between large number of types of goods. For the same kind of goods, they always compare carefully before buying. So whether Costco's SKU reduction and mass production strategy can continue in China is also a worth considering question.

We can see that there is a big difference between Chinese consumers and inherent business model of Costco. Costco's long-term growth in China will be tough if it don't adapt to the fact.

3. Paid Membership Model in China's Local Improvement Model Based on PEST Analysis.

After the previous analysis, we can conclude that only through the localization improvement, paid membership model in China can develop. Therefore, based on the PEST analysis method, this paper puts forward a kind of localized improvement model in China-Application of paid membership model in Chinese chain convenience stores. Chain convenience store is a kind of small retail store which is located in a residential area, school or business area, and mainly deals in instant goods or services, and is characterized by "convenience". Compared with the large-scale supermarket, the convenience store has strong convenience in the distance, time and service. In order to make analysis more scientific, we use the PEST analysis method to analyze the external environment of the localized improvement model of the paid member model of Costco in China

3.1 Political Environment Analysis.

In recent years, China has issued many policies to promote the development of chain-convenience stores, as showed in figure 3.

Table 3 Relevant Policy Support.

Relevant Policies	Launch Time	Main Content
To further promote the development of convenience stores	2018-10-10	To expand development space, optimize network layout; increase financial support, reduce operating costs; To promote the "release of supervision services" and simplify the registration process, reform business licensing and innovate the supervision model, standardize law enforcement inspections.
Notice on promoting the development of convenience store brand chain	2019-07-10	To attach great importance to the development of brand convenience store chain; Grasp the development of brand convenience store chain work program.
Opinions on accelerating the development of circulation and promoting commercial consumption	2019-08-27	To promote the development of new business forms and new modes of circulation; to promote the innovation, transformation and upgrading of traditional circulation enterprises.

The promulgation of these documents will provide policy support for the application of paid membership revenue model in Chinese convenience store chains, making the innovation mechanism more feasible.

3.2 Economic Environment Analysis.

From a macro perspective, in 2019, China's overall economic performance was stable. Despite the economic impact of the 2019-ncov pneumonia epidemic, Chen Yulu, the deputy governor of the People's Bank of China, said the economic impact of the epidemic was short term and limited, and that in the aftermath of the epidemic, the previously suppressed demand for consumption and investment will be fully released. Fundamentals of China's long-term positive and high-quality economic growth remain unchanged.

From a micro perspective, the growth rate of convenience stores in China continues to accelerate, and chain convenience stores allow more space for profit. According to the typical retail survey of the Ministry of Commerce, the sales of convenience stores in the first three quarters of 2019 increased by 6.3% year-on-year, continuing to rank first among the major retail business. According to the *Top 100 Chinese chain stores in 2018* released by the China Chain Management Association, the growth rate of convenience stores among the top 100 chains is far ahead. In 2018, the sales volume of the top 100 convenience store enterprises increased by 21.1 percent year-on-year, the number of stores increased by 18.0 percent, and 11,944 new stores were added, accounting for 62.5 percent of the total number of new stores in the top 100. With the good situation of chain convenience stores in China, the implementation of the paid membership revenue model has more room for profit.

3.3 Social Environment Analysis.

3.3.1 To Meet the Chinese Consumers' Preference for Fresh Food.

In terms of purchasing preference, the convenience store chain suitable for the Chinese market is more in line with the Chinese people's preference for buying fresh food, food and eating habits and consumption habits.

3.3.2 To Meet the Convenience Preferences of Chinese Consumers.

Many of Chinese are currently busy studying or working and have little time to shop in large supermarkets in the countryside. The "quick consumption" model is more and more favored by Chinese consumers. Nowadays, "small stores", "near-field" and "online" are the mainstream consumption trends, such as Suning small stores, Yonghui life store and other small community stores. So chain convenience store whose biggest feature is convenience, will have a better development in the future.

3.3.3 To Meet the Shopping Preferences of Chinese Consumers.

Although the chain store is small, there are basic supplies of daily life and food in them. The volume of goods in convenience store is small and medium-sized specifications, which is in line with the buying habits of Chinese consumers. In addition, there are more SKU per item in convenience stores than one or two in Costco. This gives consumers more choice. Therefore, this application model can meet the Chinese consumers' shopping habits of shopping more frequently, spending less on a single purchase, and preferring different shopping channels.

3.3.4 Demographic Impact on Retailing in the Future.

There is no doubt that China has entered the ageing society. It is predicted that by 2050, China's elderly population will reach 480 million people, and will reach 34.1% of the population. In such a social and demographic structure, the elderly will become an important consumer group of daily necessities and food, which can not be ignored. Compared with Costco and other big warehouse supermarkets, convenience stores are more suitable and safe for the elderly to consume.

Table 4 Number and Proportion of Population Aged 65 and over in China Time.

Years	Population over 65 [10000 people]	Total Population [10000 people]	Percentage [%]
2007	10,165	131,788	7.71
2008	10,353	132,465	7.82
2009	10,600	133,126	7.96
2010	10,801	133,770	8.07
2011	11,101	134,413	8.26
2012	11,418	135,069	8.45
2013	11,781	135,738	8.68
2014	12,233	136,427	8.97
2015	12,796	137,122	9.33
2016	13,515	137,866	9.80
2017	14,342	138,639	10.34
2018	15,210	139,273	10.92

3.3.5 Strong Credit Wins Consumers' Trust.

In fact, as early as 2018, there were a number of individual supermarkets in Wuhan that operated on a paid membership income model, but suffered a " Membership cards return " in just a few months due to poor business. One of the important reasons for its failure is the trust problem. Many consumers say the stores are too small to win customers' trust and they will have to bear the cost of membership fees if they close. Therefore, the application of the paid membership income model in China has to consider the trust problem. Chain convenience stores generally have brand franchise stores all over the country, even in the same city, there are many branches. So membership cards can be used in every branch, greatly reducing consumer trust concerns.

3.4 Technological Environment Analysis.

The application of artificial intelligence makes the realization of unmanned supermarket and new retail possible. For example, JD.com convenience stores launched unmanned vending machines, the first colorful fruit box in August 2016 in Zhongshan, Guangdong, July 8,2017. "Tao coffee" officially opened in Hangzhou and so on. The application of new technology in convenience store chains will bring consumers a new consumer experience, attract consumers to shop.

4. Conclusions.

To sum up, the application of the paid membership income model in Chinese convenience stores not only deal with Costco's inadaptablity in the Chinese market, but also has ideal environment according to PEST analysis. In terms of the policy environment, the relevant laws, regulations and documents support the innovation of convenience stores. As for economic environment, China's long term economic fundamentals and high profitability in the convenience store industry have provided economic support for this application model. As for social environment, this application model is not only suitable for the consumption habits of Chinese consumers, but also in line with the current situation of Chinese society. As for technological environment, with the development of artificial intelligence, block chain and other new technologies, the advancement of convenience stores will be better. The application of paid membership income model in Chinese convenience stores not only improves the Costco paid membership income model, but also injects fresh blood into the development of Chinese convenience stores. With the support of relevant policies and technologies, it is believed that this model will bring greater convenience and benefit to Chinese consumers and contribute to the development of livelihood undertaking in China.

References

[1] Rafael Segovia. COSTCO in Mexico: What struggles for a Dignified Life are set to be in a Globalised World[J]. Media International Australia, 2004, 111(1):97-103.

[2] Kapner S. Costco[J]. 2008, 37(5):1144-1146.

[3] Woolley S. Costco? More Like Costgrow[J]. Money, 2002.

[4] Branch S. INSIDE THE CULT OF COSTCO[J]. 1999.

[5] Li Y, Zhang X. The Revenue Model of Online Third-Party Payment Based on Game Theory[C]/2008.

[6] Vali Lehdonvirta. Virtual item sales as a revenue model: identifying attributes that drive purchase decisions[J]. Electronic Commerce Research, 9(1-2):97-113.

[7] C. B. Bhattacharya. When customers are members: Customer retention in paid membership contexts[J]. 26(1):31-44.

[8] MorrisonCoulthard, Jane L. Measuring service quality and relationship marketing in a paying membership organisation : the influence of cognitive factors[D]. University of Leicester, 2005.

[9] Akihiko Kaneko. Terms of trade, economic growth, and trade patterns: A small open-economy case[J]. Journal of International Economics, 2000, 52(1):169-181.

[10] Song Yingfa, Yin Hong. Risk Study of E-Governance based on PEST analysis model[C]/The International Conference on E-Business and E-Government, ICEE 2010, 7-9 May 2010, Guangzhou, China, Proceedings. 2010.

[11] Zhang Yanjun, Yang Xiaodong, Liu Yi, Zheng Dayuan, Bi Shujun. Research on the Frame of Intelligent Inspection Platform Based on Spatio-temporal Data. Computer & Digital Engineering [J], 2019, 47(03): 616-619+637.

[12] Yi Liu, Jiawen Peng, and Zhihao Yu. 2018. Big Data Platform Architecture under The Background of Financial Technology: In The Insurance Industry As An Example. In Proceedings of the 2018 International Conference on Big Data Engineering and Technology (BDET 2018). ACM, New York, NY, USA, 31-35.