



White paper on China's freshly brewed coffee industry

Deloitte China
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Preface

Affected by the COVID-19 pandemic and turmoil in capital markets, the freshly brewed coffee chain market in China has, over the past 15 months, experienced rapid expansion, slowed, and then a further round of accelerated growth in 2021. This white paper presents Deloitte's industry insights and viewpoints based on ongoing research into China's coffee chain market, providing a perspective and reference for coffee market investors and devotees.

Key questions¹

"Is China a 'stubborn' tea-drinking society?"

"Are Chinese consumers willing to pay for a fancy coffee experience, beyond just the coffee itself?"

"Is coffee supply coverage in China not the problem – but is it merely a lack of demand?"

"Do coffee chain brands in China pay excessive attention to Chinese consumers' functional demands?"

"Are 'third space' and convenience stores the main viable business models?"

Key points in this white paper

"Chinese consumers, especially those living in 1st- and 2nd-tier cities, have developed a habit of drinking coffee"

"Chinese consumers drink coffee for various reasons, have rising functional demands, and are paying more attention to the quality of coffee"

"There are numerous coffee shops in China, mostly independents. They are expected to improve their quality and scale up their chain-store operations"

"Through differentiation strategies, emerging freshly brewed coffee chains are favored by consumers in 1st- and 2nd-tier cities, and have taken the lead in seizing market share from large chain brands"

"If overly dependent on subsidies during early development, 'fast coffee' brands will face challenges in the sustainability of their business models if their coffee products are not recognized by target consumers"

"Small coffee shops that combine convenience, various flavors, and varying prices are expected to quickly penetrate the 'fast coffee' space, and boutique brands that specialize in products and customer experience are expected to dominate 'slow coffee'"

¹ Note: Key questions are cited from the industry research report issued on 31 January 2020.

Chapter 1

Do Chinese consumers habitually drink coffee? Do they only drink coffee to socialize and find personal space?



Key points

Chinese consumers, especially those in 1st- and 2nd-tier cities, have developed a habit of drinking coffee.

Chinese consumers drink coffee for various reasons, have rising functional demands, and are paying more attention to quality.

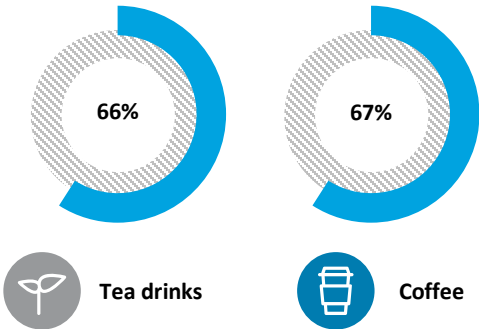
Current situation of coffee consumption in China

As the first markets penetrated by coffee culture, 1st- and 2nd-tier cities have seen coffee consumption by habitual coffee drinkers reach the same level seen in mature markets. While developing a habit of drinking coffee, consumers are constantly increasing their frequency of coffee consumption, resulting in coffee gradually changing from a “trendy drink” to a “daily drink”.

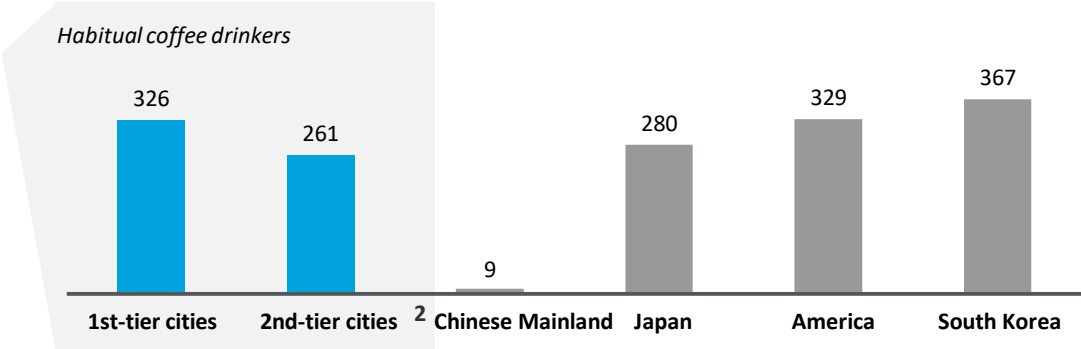
1st- and 2nd-tier cities have a coffee penetration rate of 67% which is equivalent to their tea penetration rate. Consumers show a growing acceptance of coffee and are cultivating a habit of drinking coffee. Although consumption of coffee per capita in the Chinese Mainland is nine cups per year, much less than in America, South Korea, and Japan, habitual coffee drinkers in 1st- and 2nd-tier cities consume an average of 300 cups a year, near the level of mature markets.

Of habitual coffee drinkers, more than 50% are constantly increasing their coffee consumption, thereby developing a coffee drinking habit. Consumers in 1st-tier cities, in particular, are becoming more dependent on coffee, and are now more likely to consume more cups of freshly brewed coffee. Driven by 1st-tier cities, coffee marketing education will extend to other cities, and coffee will change from a “trendy drink” to a “daily drink”.

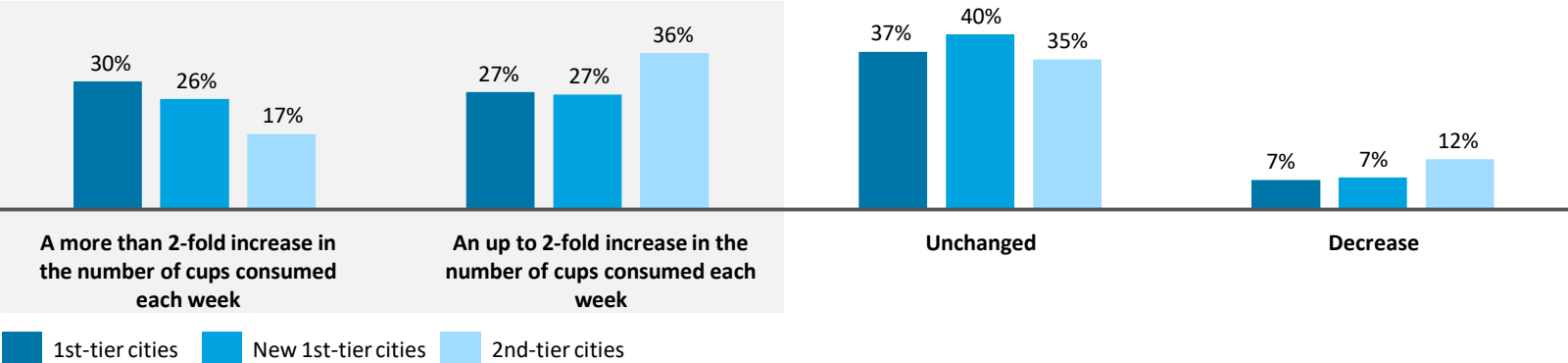
Penetration rates of tea drinks and coffee in 1st- and 2nd-tier cities¹



Consumption of coffee per capita by country/region
Unit: cups/year



Change in consumption of coffee (current vs. 1st year of drinking coffee) by city tier

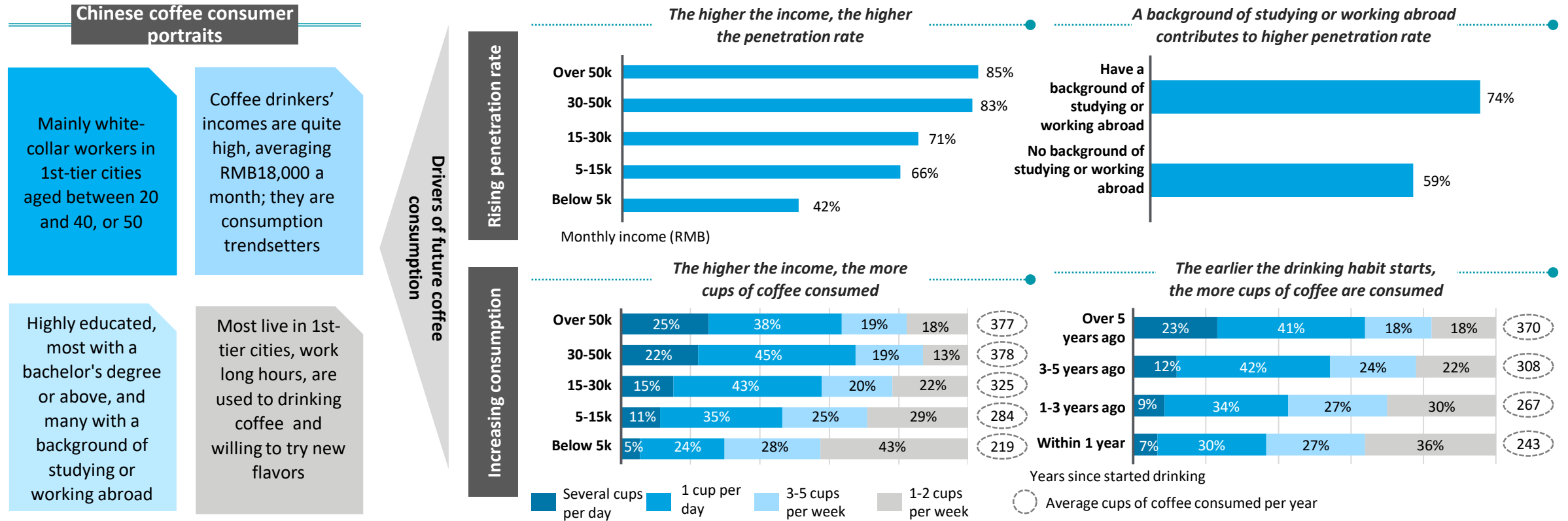


Note: 1. The respondents are white-collar workers in 1st- and 2nd-tier cities, and the penetration rate refers to the proportion of habitual tea/coffee drinkers (consuming more than one cup each week) among total consumers. 2. 1st-tier cities here include 12 new 1st-tier cities surveyed and eight established 1st-tier cities.

Source: Consumer survey, Deloitte’s research and analysis © 2021. For information, contact Deloitte China.

Chinese coffee consumer portraits

Currently, coffee consumers in China are mainly white-collar workers in 1st-tier cities aged between 20 and 40; most have a bachelor's degree or above and have a high income. The cohort of potential coffee consumers in China will continue to increase as the wider population becomes better educated and their disposable incomes increase.



China's has more than 83 million people aged between 20 and 40 with a junior college degree or above, versus 36 million with a bachelor's degree or above. Potential coffee consumers will continue to increase as they become better educated and have more disposable income.

Source: China Population Statistics Yearbook, consumer survey, Deloitte's research and analysis

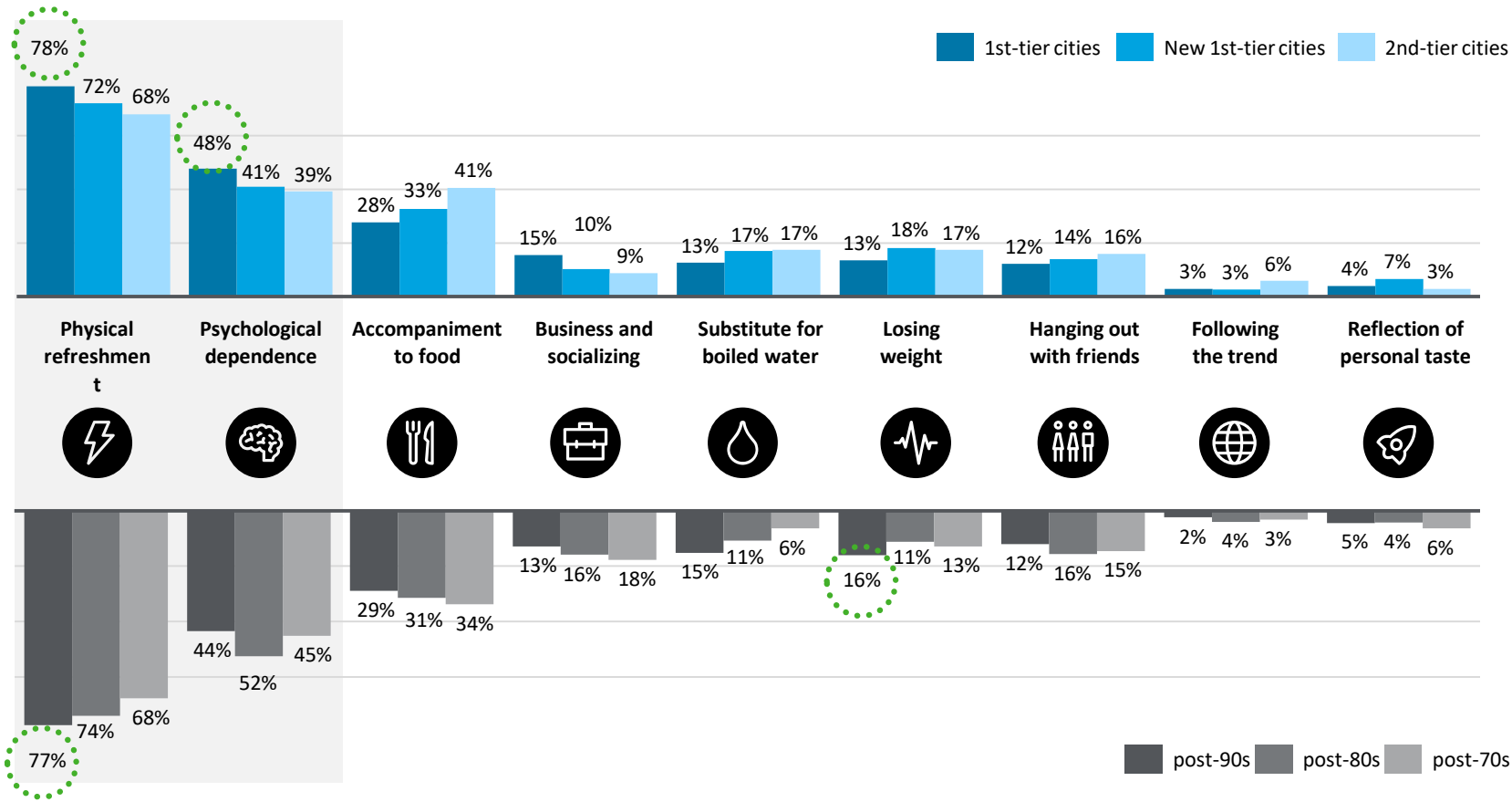
Purposes and scenarios of freshly brewed coffee consumption in China

The reasons why Chinese consumers' consume freshly brewed coffee have changed from drinking coffee to socialize to functional demand, wherein drinkers become dependent on coffee physically or psychologically. Consumers in 1st-tier cities drink coffee to refresh themselves as they face greater stress at work, making physiological needs the major reason for coffee consumption.

The reasons why Chinese consumer consume freshly brewed coffee have changed from drinking coffee to socialize to functional demand. The top three reasons include physical refreshment, psychological dependence, and as an accompaniment to food. Most consumers become dependent on coffee physically or psychologically as they develop the habit of drinking coffee, so coffee is increasingly seen in daily work and life scenarios.

As consumers in 1st-tier cities face greater stress at work, they drink coffee to reenergize and are becoming more dependent on coffee. The new-generation of consumers born after 1990, the main consumer group, drink coffee for two main reasons: they need coffee to refresh themselves at work as they are in their prime working age, and young people prefer coffee to lose weight as they are strongly health consciousness and seek weight loss and wellness.

Main reasons for consuming freshly brewed coffee



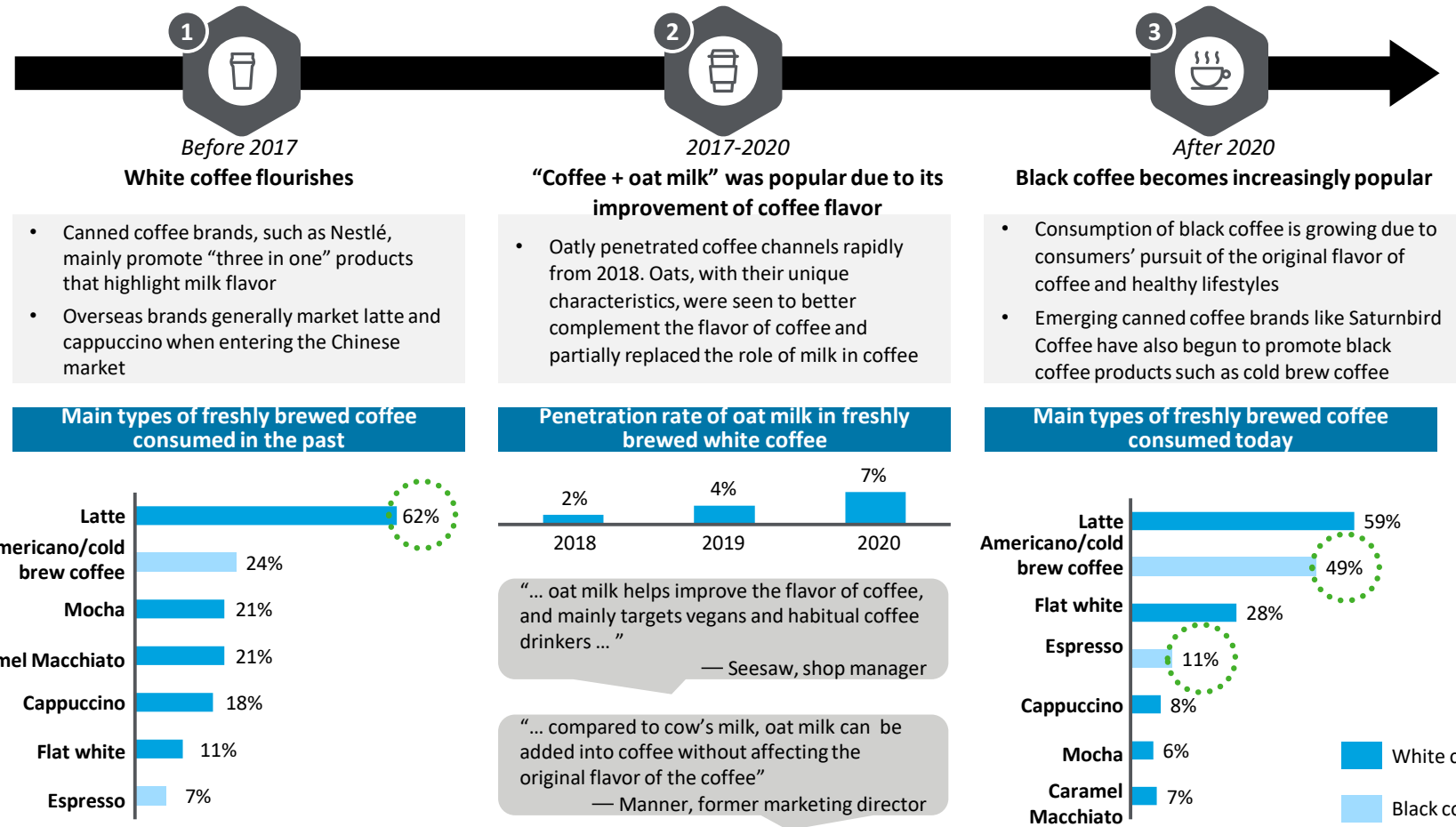
Source: Consumer survey, Deloitte's research and analysis

Chinese consumers' habit of drinking freshly brewed coffee

As Chinese consumers gradually develop the habit of drinking freshly brewed coffee, they are paying more attention to the flavor and quality of coffee, and gradually shifting their preference from white to black coffee.

Chinese consumers' habit of drinking freshly brewed coffee has undergone three stages. Before 2017, Chinese consumers did not have strong consciousness towards coffee consumption, and preferred white coffee flavored with additives. Overseas coffee brands generally marketed latte, cappuccino, and other types of white coffee when 1st entering the Chinese market, to cater to consumers' tastes. As a result, latte became the most popular coffee drink among Chinese consumers. From 2017 to 2020, the efforts of internet coffee brands like Luckin Coffee and Coffee Box to develop the market meant Chinese consumers began to develop a coffee drinking habit, pursue different coffee flavors, and favor combinations of coffee and new food materials as a result of rising health consciousness.

More coffee drinkers are now willing to try light roast coffee. Meanwhile, as consumers continue their habit of drinking coffee, they are becoming more sensitive to coffee flavors. Pour-over black coffee such as Americano, which largely retains the original flavor of coffee beans and has different tastes, is gaining popularity and has an increasing penetration rate. Black coffee looks set to become a new trendy drink.



Chapter 2

Is China's freshly brewed coffee supply market saturated? Do emerging freshly brewed coffee chains stand a chance?



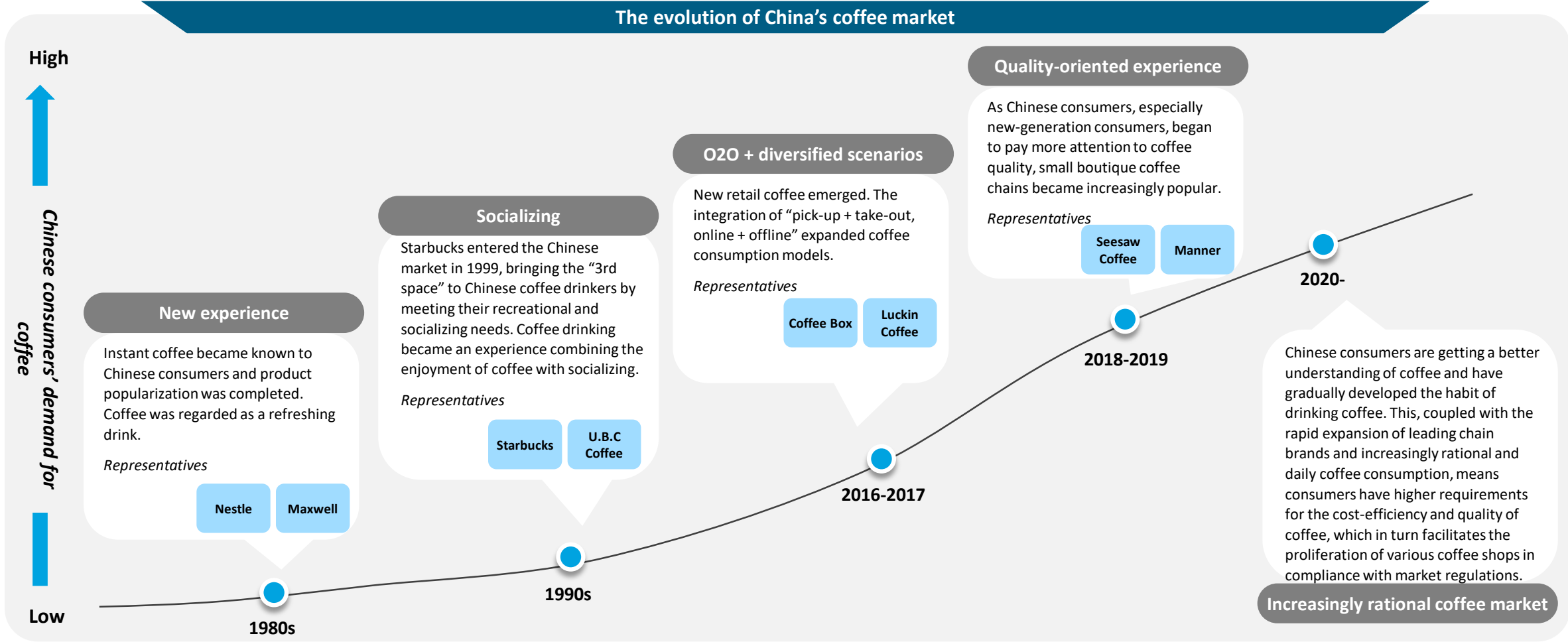
Key points

There are numerous coffee shops in China, most of which are independent and expected to improve their quality and scale up their chain-store operations.

Through differentiation strategies, emerging freshly brewed coffee chains are favored by consumers in 1st- and 2nd-tier cities, and have taken the lead in seizing market share from large chain brands.

The evolution of China's coffee market

With the further infiltration of coffee culture, Chinese consumers moved from trying coffee as a new experience, to drinking coffee to socialize, to pursuing quality. As the coffee market in China becomes increasingly mature, diversifying consumer demands have led to a proliferation of coffee shops.



Source: Deloitte's research and analysis

The competitive landscape of China's freshly brewed coffee market – number of shops

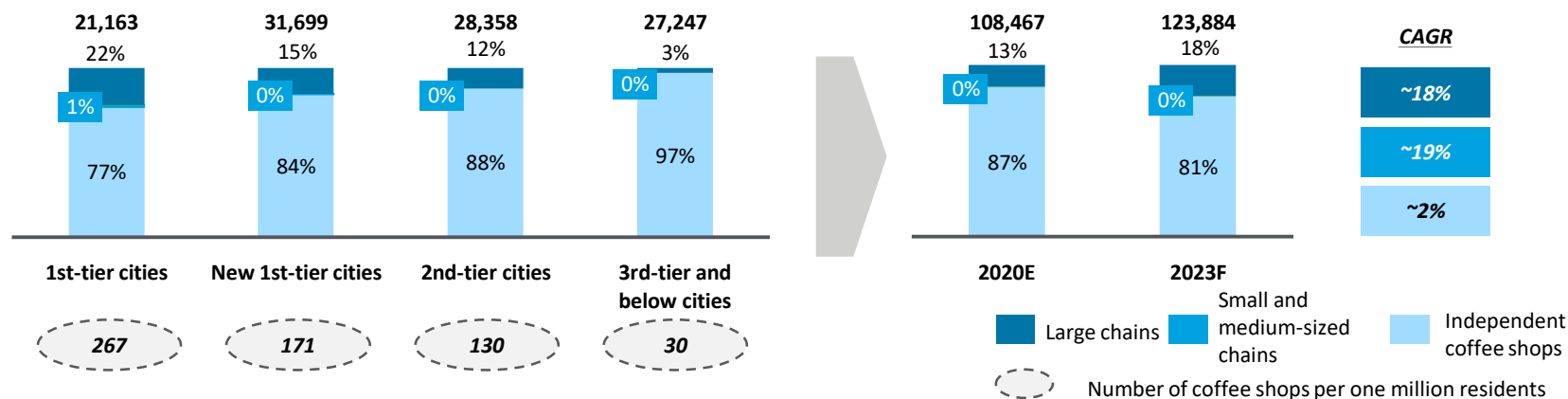
There are nearly 110,000 coffee shops in China, mainly in 2nd-tier and above cities, with a low rate of chain-store operations. The number of coffee shops will increase steadily. At the same time, the rate of chain-store operations will rise further with the continuous expansion of leading brands and the higher requirements of consumers for coffee products.

At the end of 2020, there were 108,000 coffee shops in China, 75% of which were in 2nd-tier and above cities. Based on the expansion plans of leading brands like Starbucks, as well as other factors such as the pandemic and changes in the competitive landscape, the number of coffee shops in China is expected to increase at a CAGR of 5% over the next three years to 123,000 by 2023. Cities at all tiers will see comparatively steady increases.

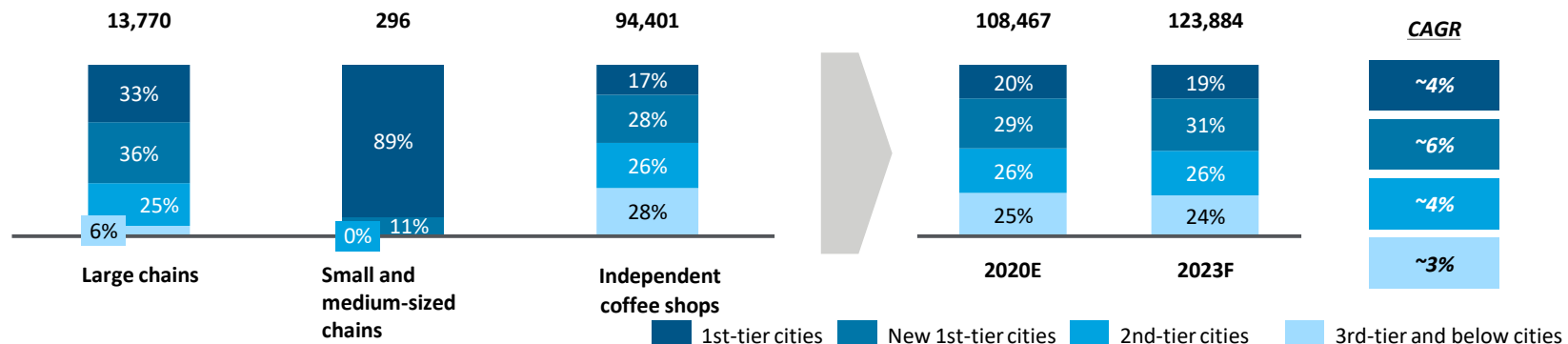
The coffee shop market in China shows a low rate of chain-store operations, with chain brands accounting for merely 13% of total coffee shops. In 3rd-tier and below cities, independent coffee shops account for as much as 97% of stores. In these cities, most chains are old cafés such as U.B.C Coffee and C.straits Cafe and are not particularly well-known brands; less than 1% of stores are boutique coffee shops such as S.Engine Coffee.

As leading brands continue to penetrate lower-tier cities and consumers' requirements for coffee products rise, chain brands will gradually replace vintage independent cafés and chain-store operations will proliferate. Local chain brands springing up in established and emerging 1st-tier cities are harbingers of the trend in lower tier cities.

Number of coffee shops in China by city tier¹ (at the end of 2020)



Number of coffee shops in China by type of business¹ (at the end of 2020)



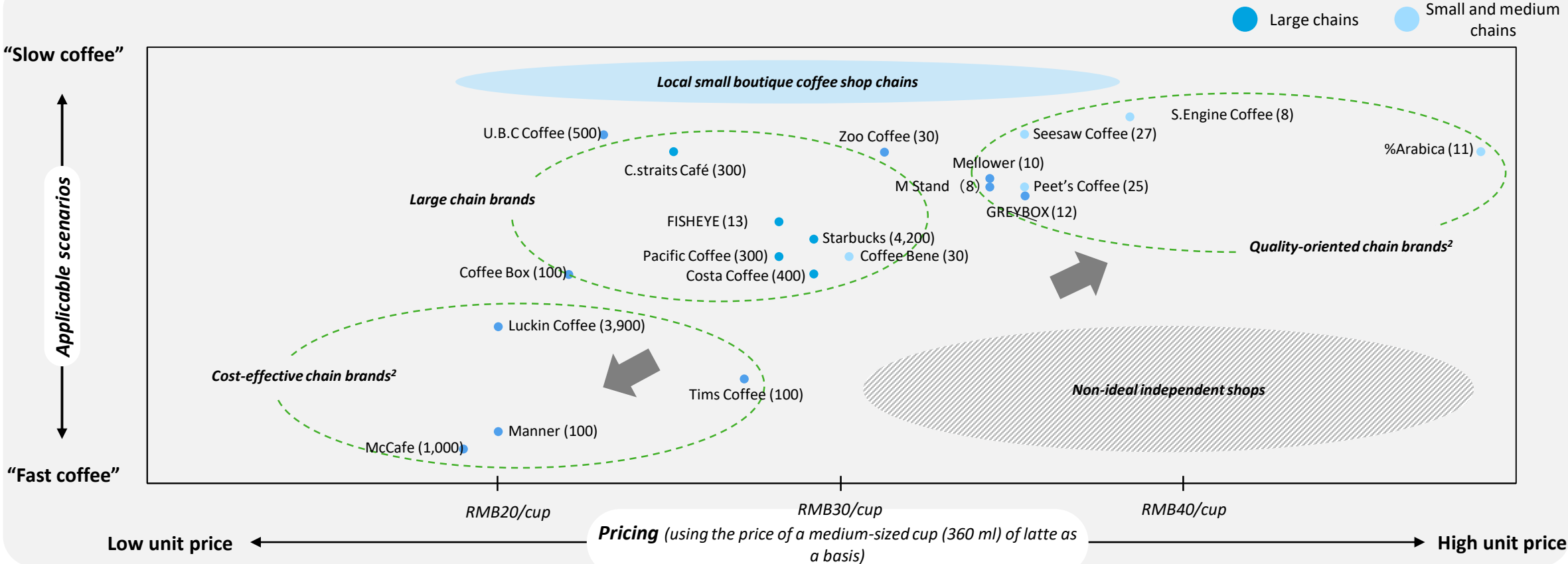
Note: 1. "Large chains" refer to freshly brewed coffee brands with more than 100 outlets in China, and "small and medium-sized coffee chains" refers to freshly brewed coffee brands with 2-100 outlets in China.

Source: Consumer survey, Deloitte's research and analysis

Future trends in China's freshly brewed coffee market landscape

Leading freshly brewed coffee brands in China are mostly large chain brands featuring comprehensive product ranges and can cater to both “fast” and “slow” coffee needs. In established and new 1st-tier cities, cost-effective brands catering to “fast coffee” needs and boutique brands catering to “slow coffee” needs are capturing the market.

The competitive landscape of leading brewed coffee brands in China¹



Note: 1. Because most brands do not disclose their number of outlets, the number of outlets is approximate data as of the end of 2020. Coffee Bene, Zoo Coffee and Coffee Box all had more than 100 outlets before 2019, but now have less than 100 after closing some outlets due to poor performance. 2. “Cost-effective chain brands” refers to those that sell products at a price lower than the average unit price of freshly brewed coffee and make low price or cost-efficiency their core selling point. “Quality-oriented chain brands” refers to those that sell products at a price higher than the average unit price of freshly brewed coffee and have the quality of coffee beans and pour-over coffee as their core selling points.

Source: Consumer survey, Deloitte’s research and analysis

Positioning of emerging independent freshly brewed coffee brands in China

Emerging freshly brewed coffee brands are focusing on one or more key dimensions, such as flavor, cost-efficiency, shop style and design experience, to differentiate themselves from large traditional chain brands.

In addition to scaling up chain-store operations, emerging freshly brewed coffee brands are striving to differentiate themselves from large chain brands. They are increasingly popular and well received in the market.

Large traditional chain brands like Starbucks have become comparatively mature and standardized in terms of product portfolio and shop style after years of operations and improvements, and can cater to people's dietary and spatial needs in various scenarios. Emerging brands, through more refined positioning, are endeavoring to differentiate themselves from large chain brands by focusing on specific value propositions, such as more exquisite flavor or trendy brand image and décor. In doing so they have successfully helped meet the more diverse demands of today's consumers – especially young consumers – for freshly brewed coffee.

For example, %Arabica, whose unit price is much higher than that of Starbucks, boasts superior quality based on higher-quality coffee beans and a better grinding process, coupled with its eye-catching “%” logo and lasting popularity through social media marketing, which attracts young consumers' curiosity and desire to be on-trend. Manner, which focuses on freshly brewed coffee products, specializes in coffee flavor and supply chains, and its price and flavor have been well received by consumers.

Positioning and shop image of independent freshly brewed coffee brands in China

Starbucks

- **Brand positioning:** mid-to-high end freshly brewed coffee products of all kinds, acting as a “3rd space”
- **Product portfolio:** a full range of products including freshly brewed coffee, tea drinks, baked food, and snacks
- **Shop strategy:** Most Starbucks coffeehouses are medium and large outlets (over 50 m²) with a unified style; Starbucks Reserve outlets, which have started business in recent years, incorporate more art and experience elements
- **Shop image:** American-style shops – a “3rd space”

Manner

- **Brand positioning:** cost-effective freshly brewed coffee products
- **Product portfolio:** mainly sells freshly brewed coffee products, with a handful of tea drinks, and has recently launched bakery products
- **Shop strategy:** Most Manner coffeehouses are small (less than 50 m²) without too much décor or 3rd space, and are centered on a take-out model
- **Shop image:** small “take-out” shops

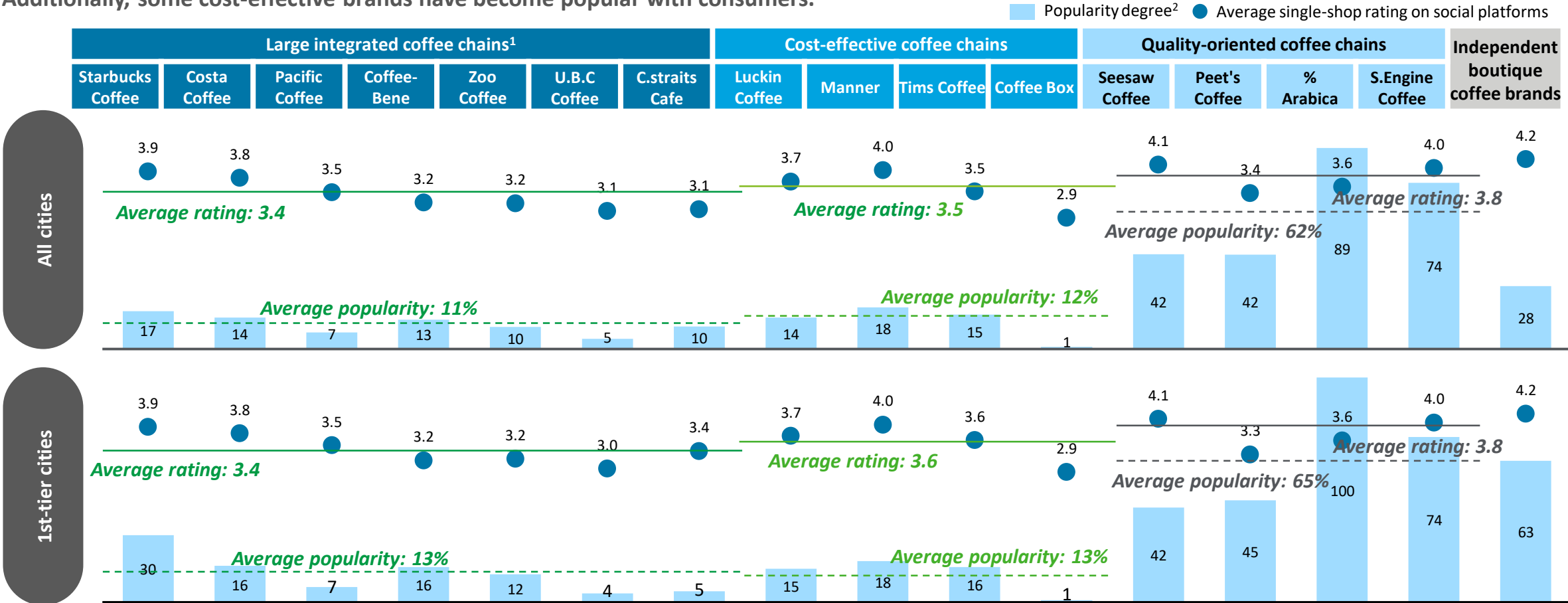
%Arabica

- **Brand positioning:** high-quality and good-looking freshly brewed coffee products
- **Product portfolio:** mainly sells freshly brewed coffee products, with a handful of tea drinks and bakery products
- **Shop strategy:** Most %Arabica coffeehouses are large (over 50 m²), spacious and bright with an “Instagrammable” style; it creates must-visit sites through art installations and other decorations
- **Shop image:** creative Instagrammable large shops

Source: Deloitte's research and analysis

Popularity of leading freshly brewed coffee brands in China (1/2)

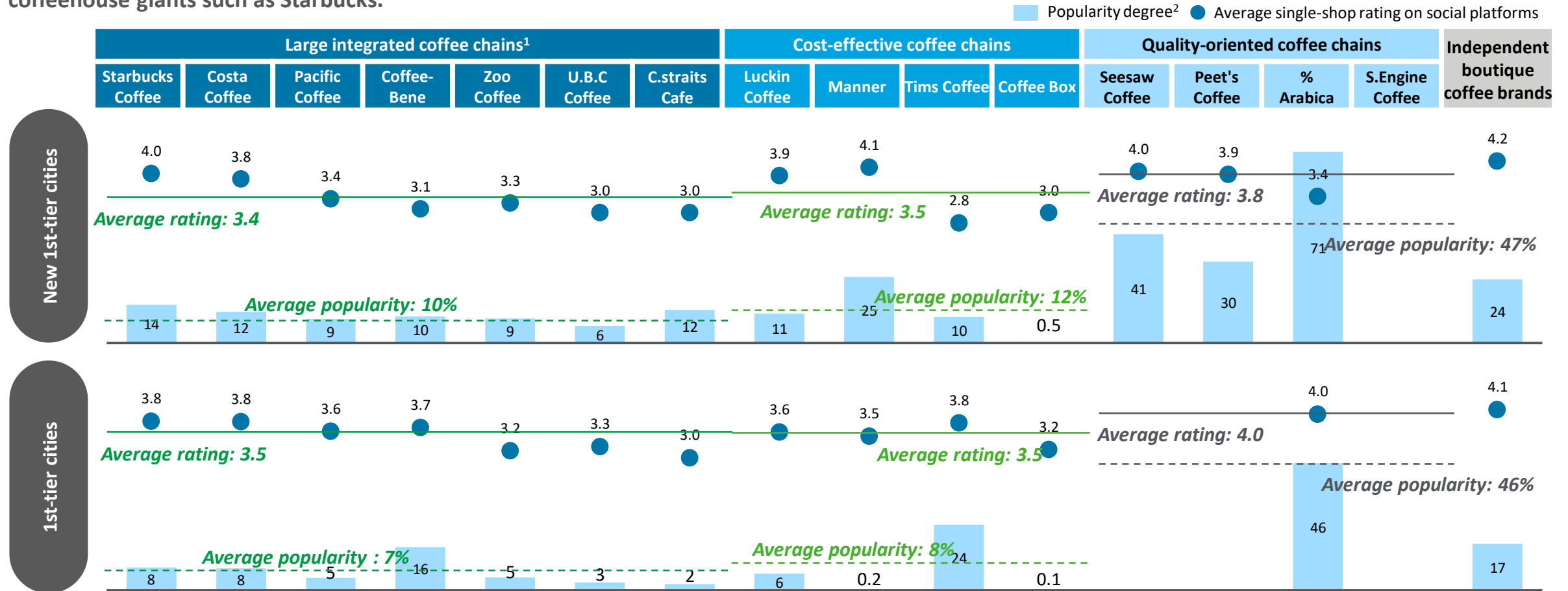
Over recent years, quality-oriented brands like %Arabica have been gaining in popularity in 1st-tier cities where trendy shops tend to open first. They have become more popular and well-received than large coffee chains like Starbucks by locals, who are increasingly keen on boutique coffee brands. Additionally, some cost-effective brands have become popular with consumers.



Note: 1. Leading brands with independent coffee shops are selected for comparison; Coffee Bene, Zoo Coffee and Coffee Box are regarded as “failed” large integrated coffee chains for the purposes of this analysis. 2. Popularity is derived from the proportion of reviews for each brand as a percentage of total reviews of all brands on social platforms.
Source: Deloitte Analytics Institute, Deloitte’s research and analysis

Popularity of leading freshly brewed coffee brands in China (2/2)

Compared to 1st-tier cities, consumers in new 1st-tier cities and 2nd-tier cities are less keen on freshly brewed coffee brands due to the distribution of outlets, but also speak highly of emerging, cost-effective brands and independent boutique coffee brands, with equal or even more rave reviews than coffeehouse giants such as Starbucks.



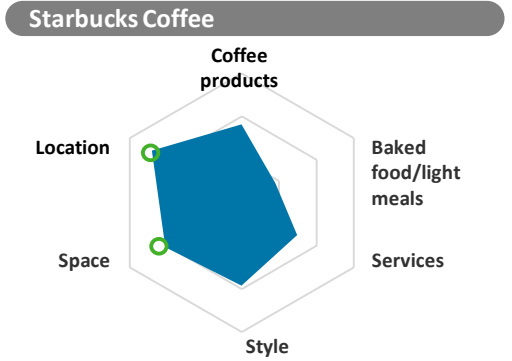
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Source: Deloitte Analytics Institute, Deloitte's research and analysis

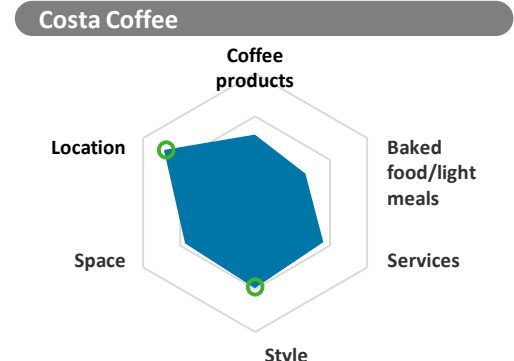
Impression of leading freshly brewed coffee brands in China (1/2)

Large coffee shop chains look to cater to a variety of consumption scenarios to capture a broad market. Consumers tend to pay attention to their "fast coffee" and "slow coffee" attributes, and consider their location, space and atmosphere as important evaluation indicators.

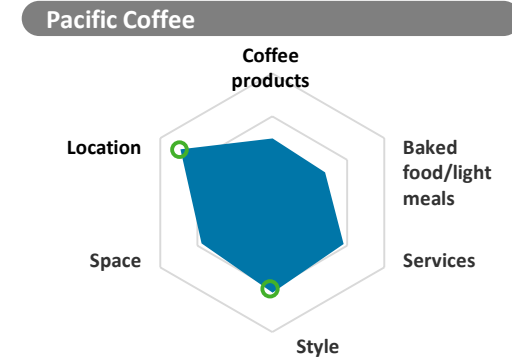
Radar charts based on consumer reviews



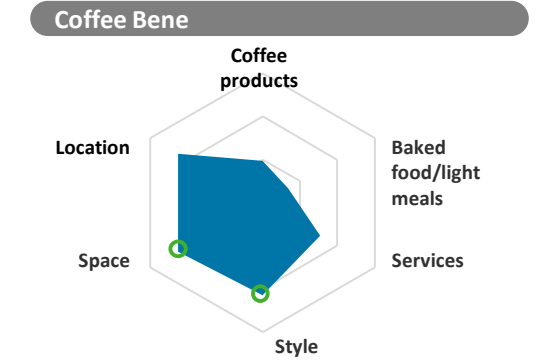
Starbucks coffeehouses are highly convenient and most are located in *upscale hotels, shopping malls, office buildings* and other areas within a five-minute walk from the surrounding population; its "3rd-place" concept is deeply rooted in people's minds.



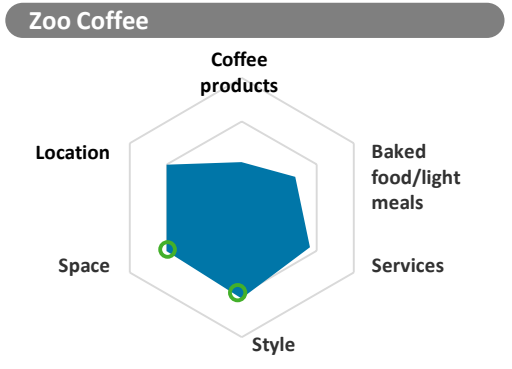
As an authentic British coffee brand, the *British Christmas family atmosphere* Costa creates in its outlets is highly regarded by consumers.



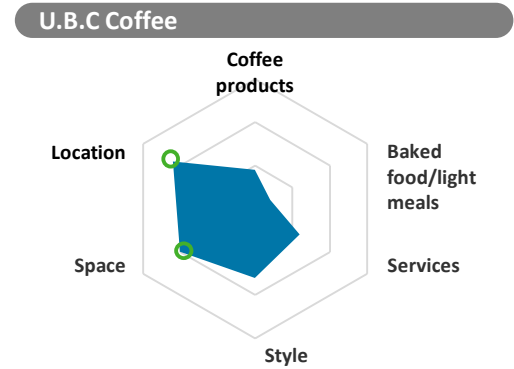
The brand positioning of Pacific Coffee is *more "business"-orientated*, and its outlets are preferred by white-collar workers as a place for business negotiations.



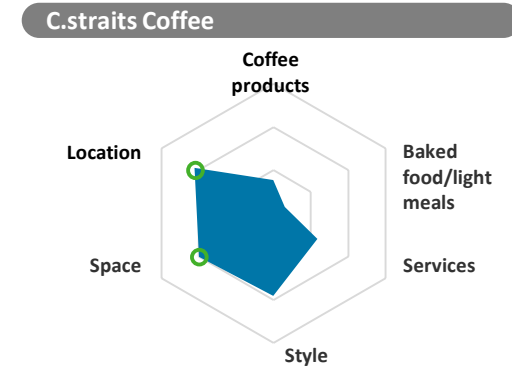
Coffee Bene has become popular thanks to the *Korean drama craze*, and its outlets are decorated in a *romantic Korean style* for fans to experience Korean culture.



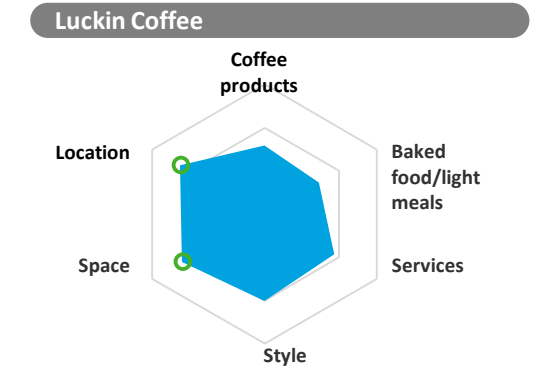
Zoo Coffee is a Korean brand with a *zoo culture* as its theme. It displays large plush animal toys to highlight this theme and impress consumers.



As an old brand that focuses on *Chinese and Western light meals*. Consumers do not think highly of its coffee quality and light meals, but pay more attention to its *spacious and comfortable environment*.



As an *upgrade brand of U.B.C Coffee*, C.straits Coffee also focuses on Chinese and Western light meals. The quality of its coffee and light meals are also not well regarded by the public, and consumers enjoy its outlets more for the *gathering space* they provide.



As an *Internet coffee brand*, Luckin Coffee uses the "takeaway + subsidy" model to focus on *price performance and convenience*, while developing *flagship shops and premium shops with a sense of space*.

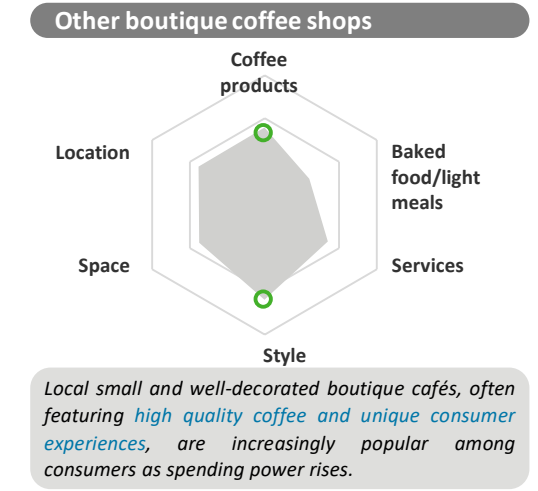
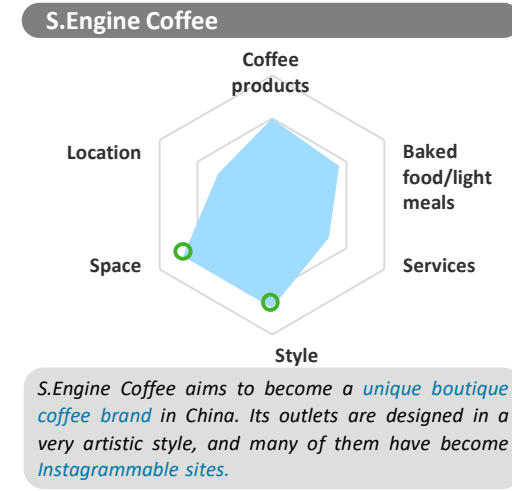
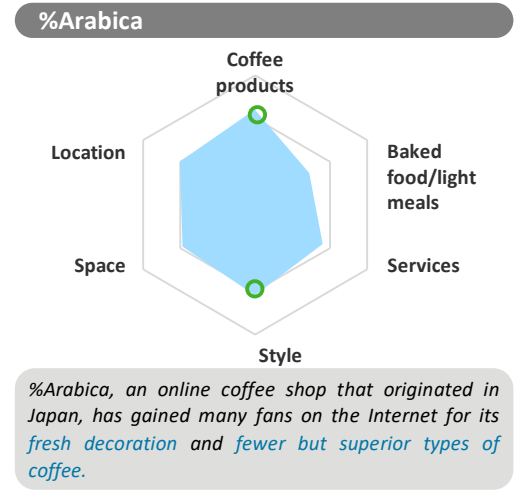
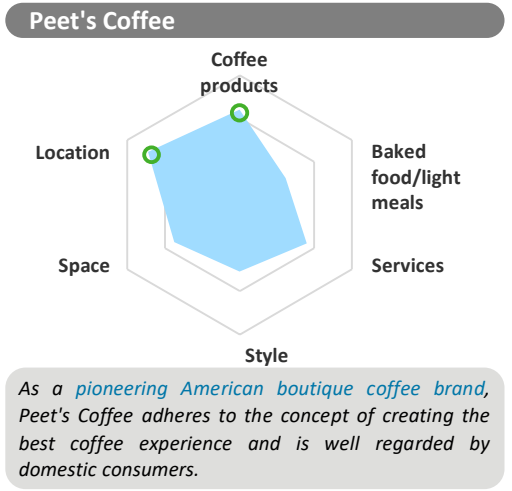
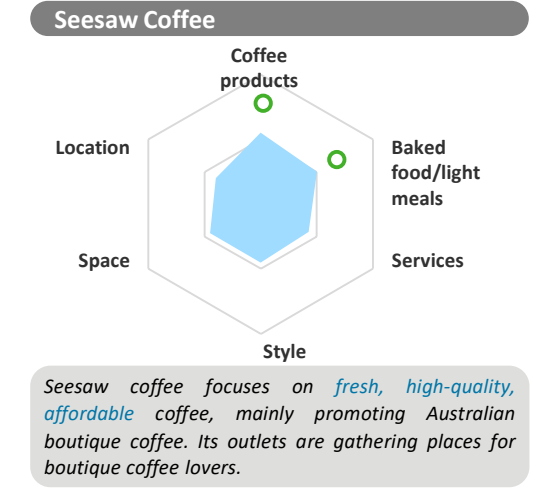
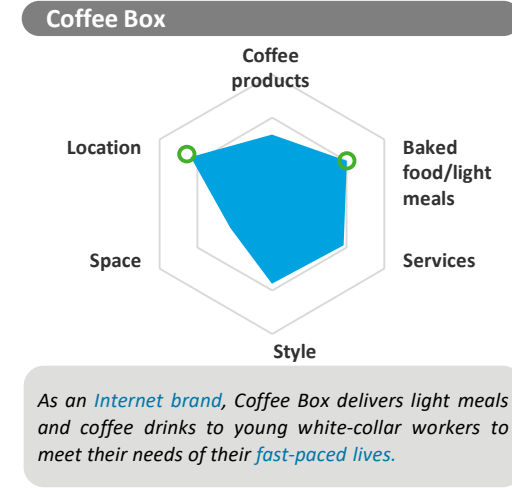
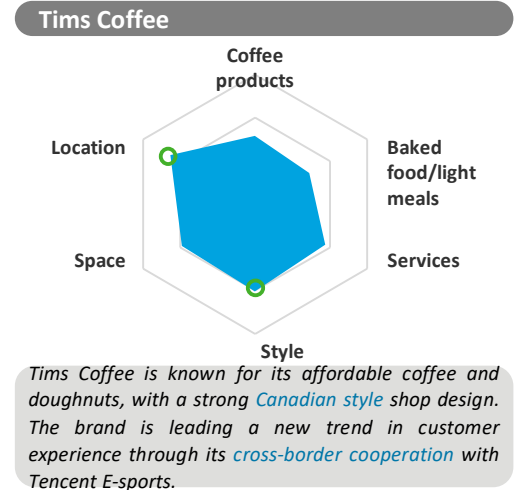
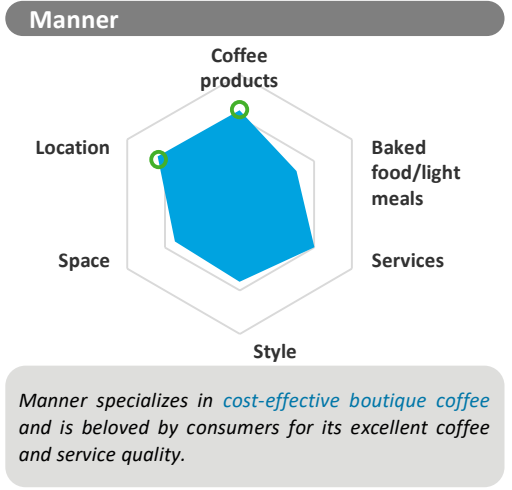
Source: Deloitte Analytics Institute, Deloitte's research and analysis

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Impression of leading freshly brewed coffee brands in China (2/2)

For coffee brands that focus on cost efficiency, consumers are more concerned about the convenience of buying ("fast coffee"), while for boutique coffee chains, consumers place more emphasis on high quality coffee and unique design while enjoying "slow coffee".

Radar charts of consumer reviews



Source: Deloitte Analytics Institute, Deloitte's research and analysis

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Consumer evaluation of leading freshly brewed coffee brands in China (1/2)

Large integrated coffee chains such as Starbucks Coffee, Costa Coffee and Pacific Coffee have great reputations on the whole, but their coffee flavors and environment fall short of consumer demands; U.B.C Coffee, C.straits Coffee and other older cafés are more likely to be regarded as restaurants by their customers who express dissatisfaction with their dishes.

■ Coffee products ■ Baked food/light meals ■ Services ■ Atmosphere ■ Space ■ Location

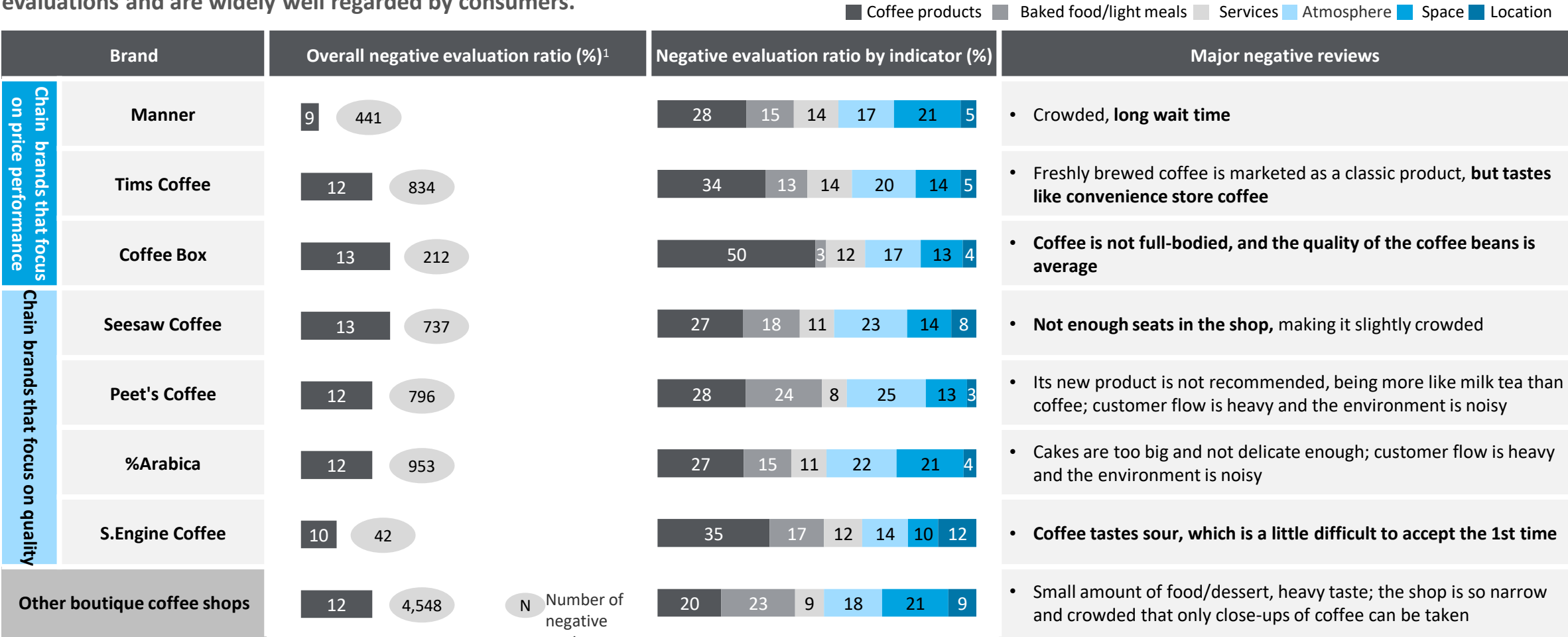
Brand		Overall negative evaluation ratio (%) ¹	Negative evaluation ratio by indicator (%)	Major negative reviews
Large integrated coffee chain brands	Starbucks Coffee	12 (4,463)	18 15 24 25 13 4	<ul style="list-style-type: none"> Noisy and crowded: waiters are not hospitable enough and even a little impatient
	Costa Coffee	12 (3,244)	29 13 18 22 14 4	<ul style="list-style-type: none"> Americano tastes so-so: the overall decoration is simple, and tables and chairs are not very comfortable
	Pacific Coffee	11 (2,930)	33 10 18 21 15 4	<ul style="list-style-type: none"> Latte/Mocha coffee tastes light: many people hold business meetings here and occupy seats for a long time
	Coffee-bene	13 (730)	28 21 16 22 9 3	<ul style="list-style-type: none"> Coffee tastes light: cakes are not fresh enough; the lighting is not so good
	Zoo Coffee	12 (1,287)	29 17 12 23 15 6	<ul style="list-style-type: none"> Coffee tastes bad: seats are densely packed, the lighting is dark, and the animal dolls are a bit worn out
	U.B.C Coffee	17 (1,287)	11 30 21 26 9 3	<ul style="list-style-type: none"> Slow to serve and the dishes have a strong smell; obsolete environment with outdated decoration and a lack of atmosphere
	C.straits Coffee	17 (889)	11 36 21 20 8 4	<ul style="list-style-type: none"> Overcooked steaks, and the dishes have a strong smell; outdated decoration, heavy smell of cigarettes
Luckin Coffee	13 (663)	N Number of negative reviews	40 17 15 16 9 3	<ul style="list-style-type: none"> Latte and Americano are not mellow enough; coffee tastes strange, in a difficult to describe way

Note: 1. The proportion of negative keyword mentions in the total number of positive and negative keyword mentions on social media platforms.

Source: Deloitte Analytics Institute, Deloitte's research and analysis

Consumer evaluations of leading freshly brewed coffee brands in China (2/2)

The overall reputation of emerging chain brands that focus on price performance and quality is comparable to that of the large integrated chain brands. Several brands that do better in cost efficiency, coffee quality or environment, such as Manner and S.Engine Coffee, have a lower proportion of negative evaluations and are widely well regarded by consumers.



Note: 1. The proportion of negative keyword mentions in the total number of positive and negative keyword mentions on social media platforms.

Source: Deloitte Analytics Institute, Deloitte's research and analysis

Chapter 3

What are the core issues that coffee chain brands can face during rapid growth?

What kind of business model can quickly seize future market share?



Key points

If overly dependent on subsidies in their early development stages, the sustainability of the business models of “fast coffee” brands will face challenges if their coffee products are not well regarded by target consumers.

Small coffee shops that combine convenience, various flavors, and varying prices are expected to quickly penetrate “fast coffee” scenarios, and boutique brands that specialize in products and customer experience are expected to dominate “slow coffee”.

Freshly brewed coffee consumption scenarios and channels in China

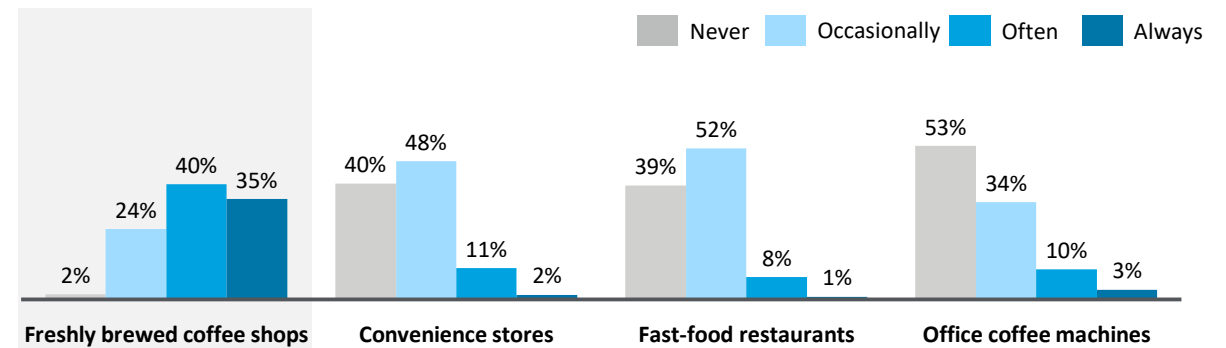
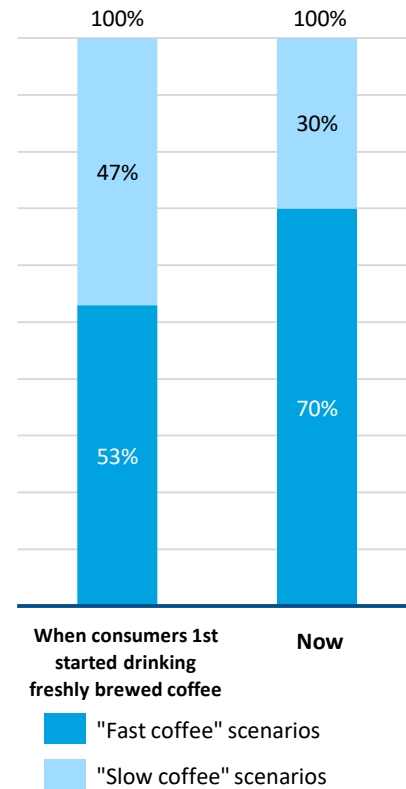
With the rapid expansion of coffee chains such as Starbucks and Luckin throughout lower-tier cities, Chinese consumers are gradually developing the habit of drinking coffee, especially in "fast coffee" scenarios where channels such as convenience stores and office coffee machines have emerged. However, coffee shops are still the main channel, and the main reason consumers enter freshly brewed coffee shops is still to buy coffee or other drinks.

Due to the fast-paced work environment in 1st- and 2nd-tier cities and Luckin's cultivation of consumers' coffee drinking habits over the past three years, consumers have gradually become habitual coffee drinkers, and the proportion of coffee consumption in "fast coffee" scenarios has gradually increased. "Fast coffee" scenarios now account for 70% of consumption of freshly brewed coffee.

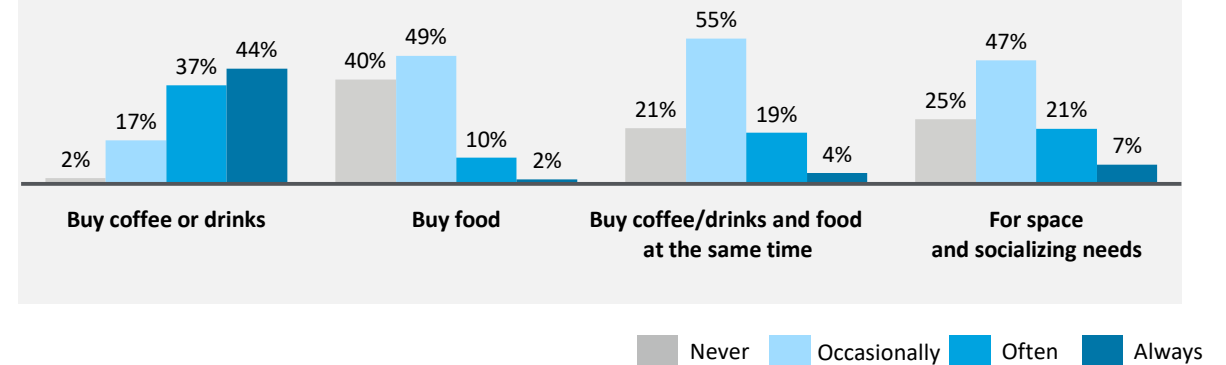
In response to consumers' need for speed, channels such as convenience stores and office coffee machines have gradually emerged and penetrated some unique scenarios. For example, people can have coffee when they buy breakfast in convenience stores or work overtime in the office. These channels have successfully occupied a position in the market for freshly brewed coffee.

At present, freshly brewed coffee shops are still the main freshly brewed coffee channel, since different coffee shops can meet consumers' different time and space requirements. Consumers mainly enter coffee shops to buy coffee or drinks, and some people buy food, but few people buy food only. More than 20% of consumers frequently visit coffeehouses for space and scenario-based needs only, with consumers regarding coffeehouses as a "3rd space".

Consumption scenarios and locations



The main reasons consumers enter freshly brewed coffee shops



Source: Consumer survey, Deloitte's research and analysis

Considerations of Chinese consumers when choosing freshly brewed coffee

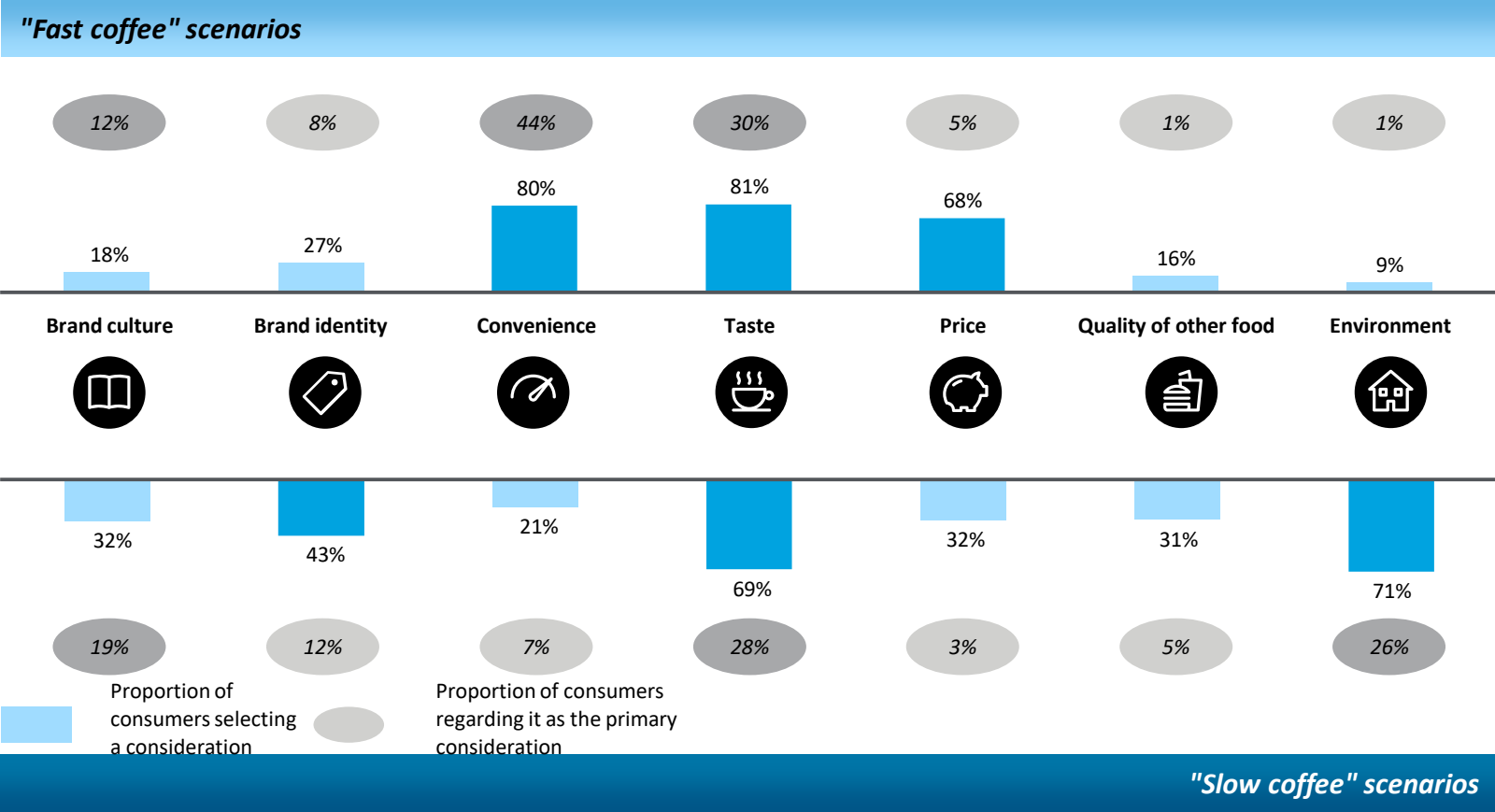
Despite diversified consumption scenarios, the taste of freshly brewed coffee is the main factor consumers always consider. In addition, "fast coffee" scenarios attach more importance to convenience and price, while "slow coffee" scenarios pay more attention to brand identity and the coffeehouse environment.

The consumption scenarios of freshly brewed coffee are becoming increasingly diversified. Influenced by time requirements and purpose, consumers have different considerations when choosing freshly brewed coffee in different scenarios. But whether they are enjoying "fast coffee" or "slow coffee", taste is always a factor.

In "fast coffee" scenarios, consumers' top three considerations are taste, convenience and price. Although 44% of consumers think convenience is the primary consideration, they still strongly consider taste.

In "slow coffee" scenarios, consumers' top three considerations are environment, taste and brand identity. Taste is still an important factor, with 28% of consumers viewing it as such. Besides taste, in "slow coffee", "3rd space" concept-based scenarios like doing business, socializing, enjoying leisure time and taking photos are consumers' main demands. As a result, the values of a coffee shop itself, including its design, comfort level and brand identity have become key considerations.

Top three considerations for choosing freshly brewed coffee in different scenarios



Source: Consumer survey, Deloitte's research and analysis

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Chinese consumers' preference for freshly brewed coffee brands

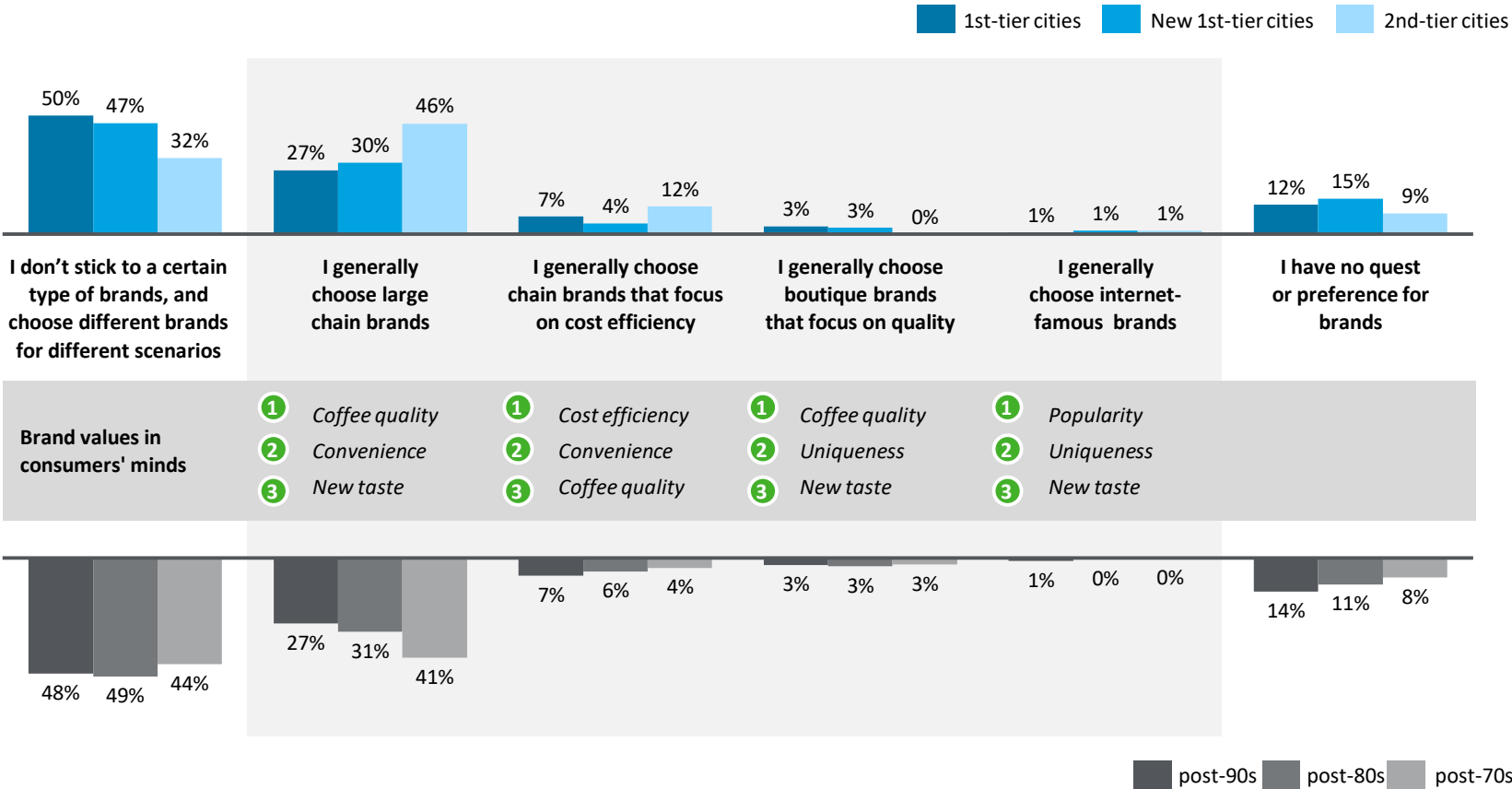
Nearly 50% of consumers will switch between freshly brewed coffee brands depending on the scenario. Older consumers and those in lower-tier cities tend to choose large chain brands for quality and convenience, while these values are less favored in 1st-tier cities and among younger people.

Consumers don't usually frequent the shops of just one freshly brewed coffee brand. Nearly 50% of consumers buy coffee from various brands for different reasons.

Coffee quality and convenience are still the main reasons people choose large chain brands such as Starbucks Coffee and Costa Coffee, but these factors are much less important in 1st-tier cities and among post-90s consumers than they are in 2nd-tier cities and among consumers born post-70s. The coffee market in 1st-tier cities is more scattered and diverse, and post-90s consumers are more receptive to new things. The current value propositions of large chain brands will carry less weight with the future consumer groups, given increased market competition.

Consumers view cost efficiency as the main appeal of chain brands, coffee quality as the key selling point of boutique brands, and popularity as most important factor in internet-famous brands.

Consumers' quest for freshly brewed coffee brands



Source: Consumer survey, Deloitte's research and analysis

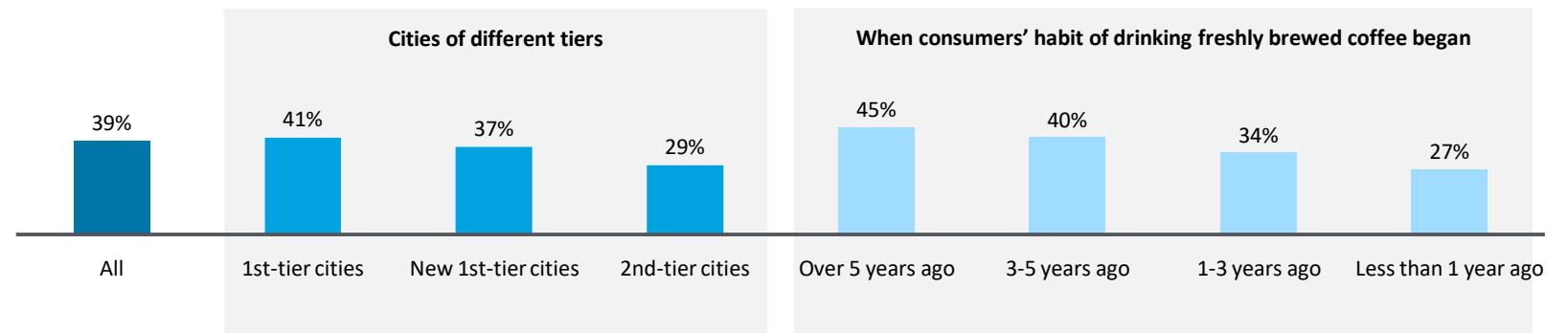
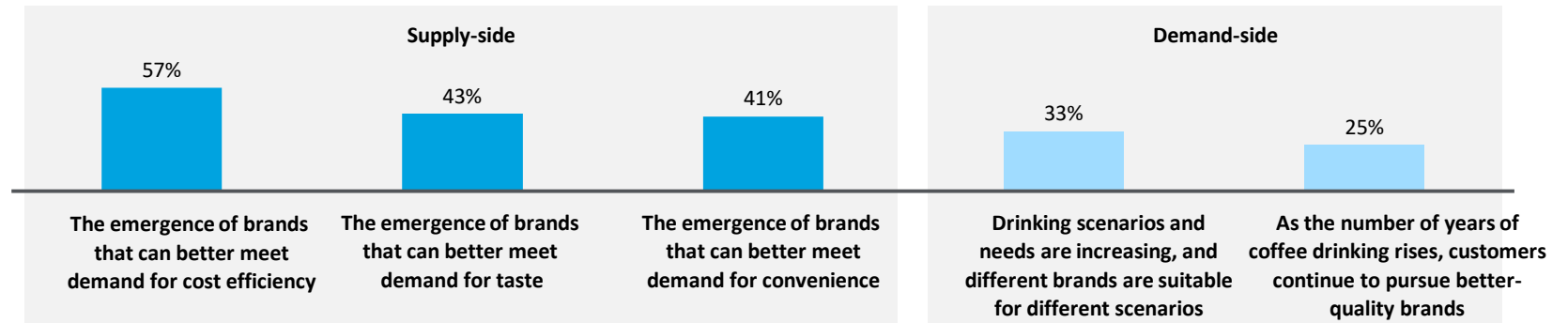
Chinese consumers' brand loyalty

With more choices available and changes in demand, consumers are willing to change their choice of coffee brand. In particular, consumers living in 1st-tier cities and who have been coffee drinkers for longer will sometimes spontaneously seek higher-quality freshly brewed coffee brands.

With an increasingly diverse range of options in China's freshly brewed coffee market and continuous changes in demand, consumers tend to favor different brand preferences at different times. Supply-side and demand-side factors create the cycle of consumers constantly trying new brands, falling in love with a certain brand, and then replacing their past favorites with better brands. The continuous emergence of more cost-effective, better-tasting and more convenient freshly brewed coffee brands is driving consumers to change their preferences.

New and old brands are accelerating their rollouts in 1st-tier cities, which are the main arenas of coffee brand competition. 41% of consumers in these cities have changed their most frequent brand of freshly brewed coffee since they 1st started drinking, more than in other types of cities. At the same time, with the further cultivation of coffee drinking habits, rising incomes and a growing cohort of coffee connoisseurs, consumers will spontaneously look for freshly brewed coffee brands with better quality (better taste and a more trendy culture).

Reasons for changes in the most commonly consumed freshly brewed coffee brands



Proportion of respondents who have changed their most commonly consumed freshly brewed coffee brand

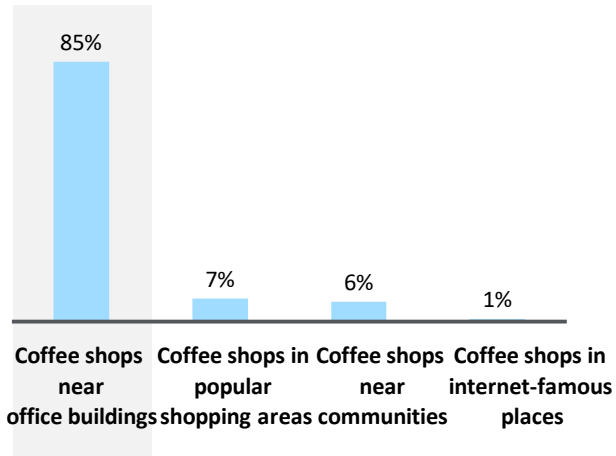
"Fast coffee" scenarios – shop type preference

In "fast coffee" scenarios, consumers tend to buy freshly brewed coffee in office buildings or nearby cafés; they are more sensitive to price, and have less demand for support services other than take-away.

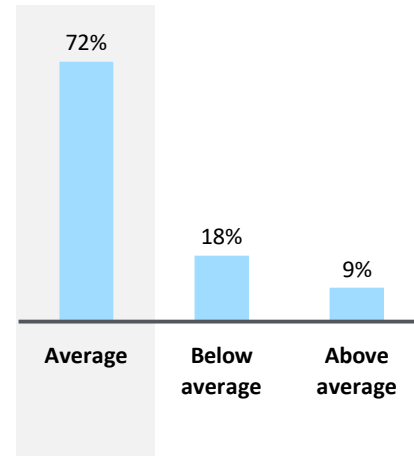
Consumer preference for brands and shop types in "fast coffee" scenarios



Location

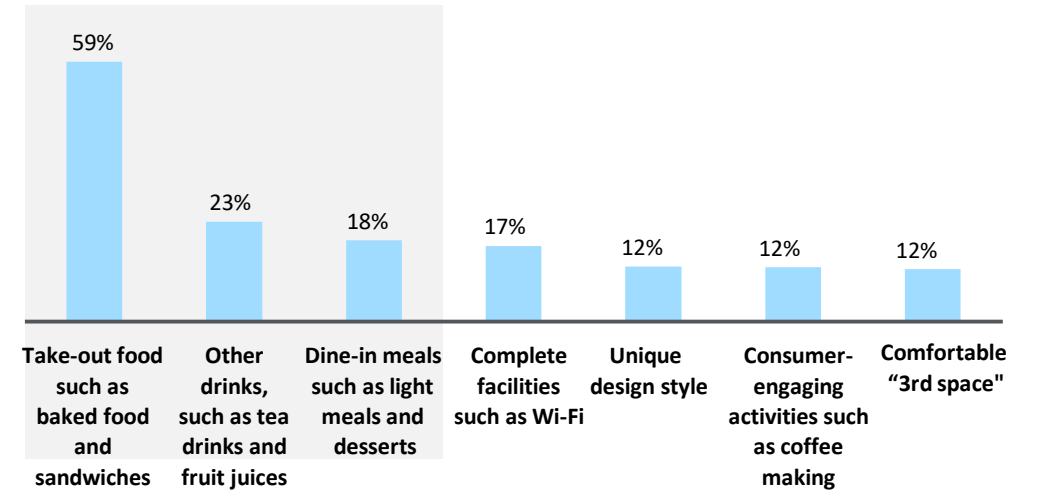


Price



Products and services other than coffee

80%
Proportion of consumers who need other products and services



In "fast coffee" scenarios, coffee drinking has more rigid demand – meeting consumers' needs for refreshment during the working day. As a result, on one hand, consumers have higher requirements for immediacy and quickness, so coffee shops near office buildings are usually their 1st choice. On the other hand, the relatively high frequency of "fast coffee" consumption constrains consumers' willingness to pay for high-price products to a degree, making them more likely to choose cost-effective coffee. In addition to coffee, consumers mainly favor basic food and drinks such as fast food, and pay little attention to cafés added value, such as overall style and environment.

Source: Consumer survey, Deloitte's research and analysis

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White paper on China's freshly brewed coffee industry

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"Fast coffee" scenarios – a single-shop economic model for freshly brewed coffee

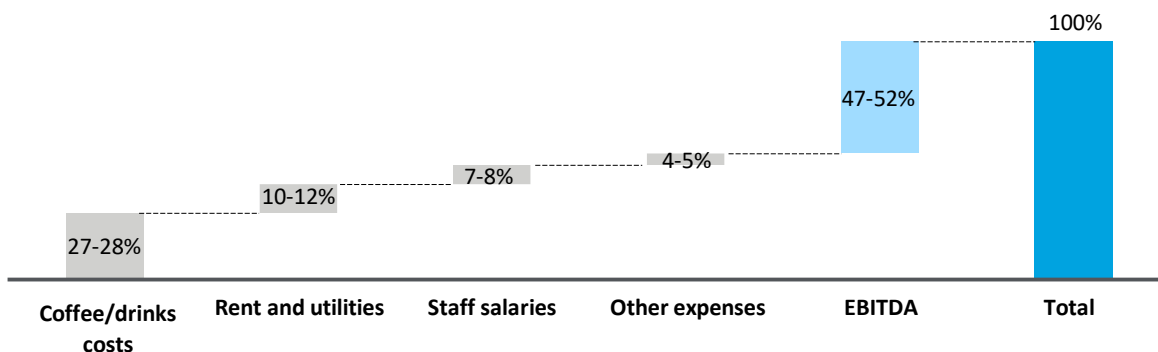
The small shop model of providing only coffee and drinks is suitable for "fast coffee" scenarios. Quality brands can quickly expand and multiply outlets by focusing on price performance, taste and other values consumers are most concerned about to achieve profitability and recover their investment quickly.

"Fast coffee" brand single-shop economic model¹

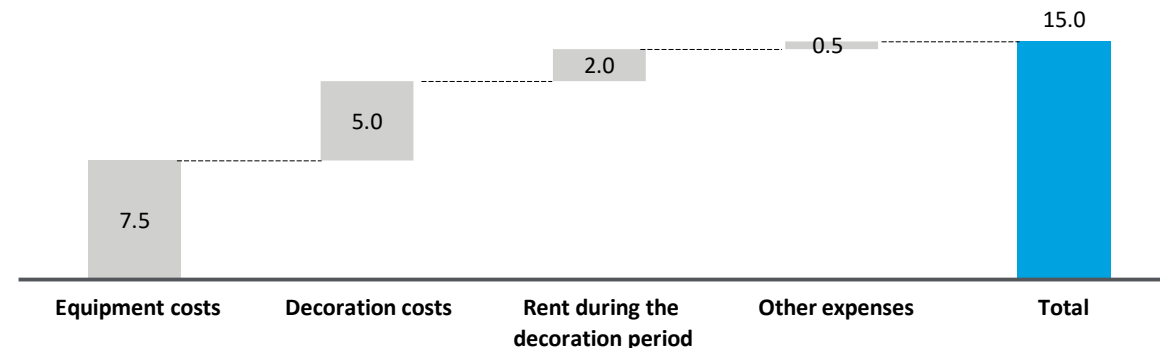
Schematic diagram

Average monthly sales of mature shops	RMB150,000-180,000	Average monthly EBITDA	RMB70,000-80,000	Single-shop area	5-10 m ²	Climbing period	1-2 weeks	Average monthly sales per unit area	20,000-25,000 yuan/m ²	Investment return period	2 months
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Single shop profit (%)



Single shop investment (unit: RMB10k)



"Fast coffee" scenarios do not require a coffee shop to provide spaciousness or atmosphere, and a small shop of 5-10m² is sufficient to support freshly brewed coffee supply. Locations with large customer flow but relatively cheap rents, such as subway station exits or alleyways around popular shopping areas, are better choices.

To improve average transaction value, coffee shops in "fast coffee" scenarios do not need to overly focus on other products such as baked food and light meals, because these will lower gross margin and are more suitable for large shops where consumers tend to spend more time.

Note: 1. Taking coffee shops in popular shopping districts in Shanghai as an example.
Source: Deloitte's research and analysis

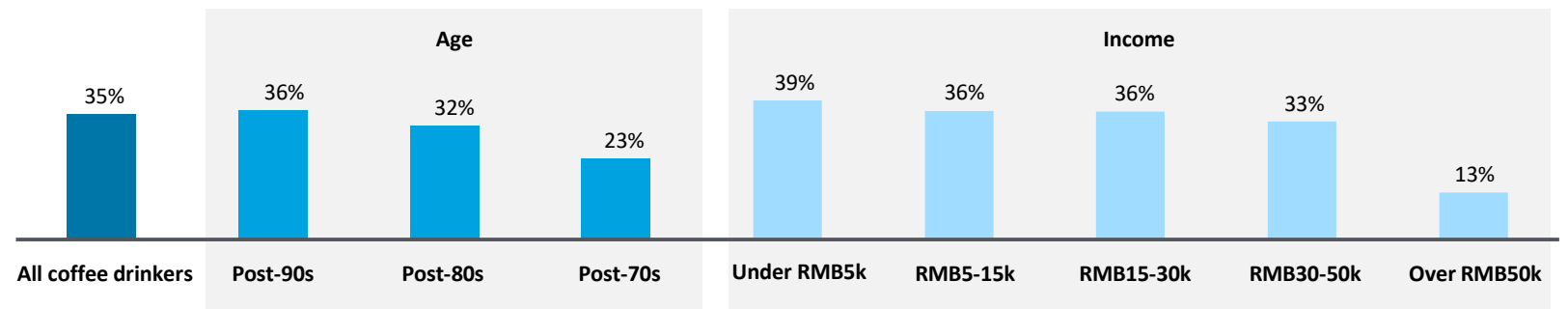
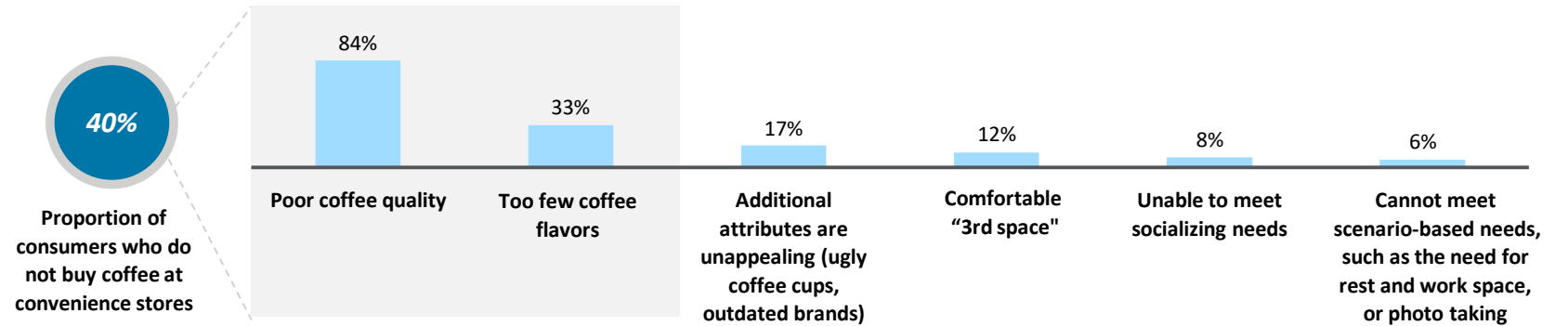
"Fast coffee" scenarios – convenience store coffee

In "fast coffee" scenarios, convenience stores will have an impact on freshly brewed coffee shops. Consumers who have been drinking coffee for a longer time attach more importance to coffee quality, while younger, lower-income customers are more concerned about functionality and price performance, and will be the main consumers of convenience store coffee.

In "fast coffee" scenarios, 60% of consumers buy freshly brewed coffee in convenience stores due to their greater convenience and lower prices, and 40% do not choose convenience store coffee because of its poor quality and limited flavors. Since Japan's top three convenience stores, Family Mart, Lawson and 7-Eleven, launched their own coffee brands in 2011-2013, coffee has become an important product for convenience stores, playing a role in attracting customers and enhancing customer stickiness. Consumers usually buy breakfast or lunch with a cup of coffee, without spending extra time and energy. This has an impact on freshly brewed coffee shops that are not as densely distributed as convenience stores are.

In the future, convenience store coffee will secure a stronger place in the market. 35% of consumers will more often buy coffee at convenience stores in future. Younger and lower-income people, who are more concerned about the functionality and price performance of coffee, will be the main consumers in convenience stores.

Reasons for not buying coffee in convenience stores



Proportion of consumers who will buy coffee at convenience stores more often

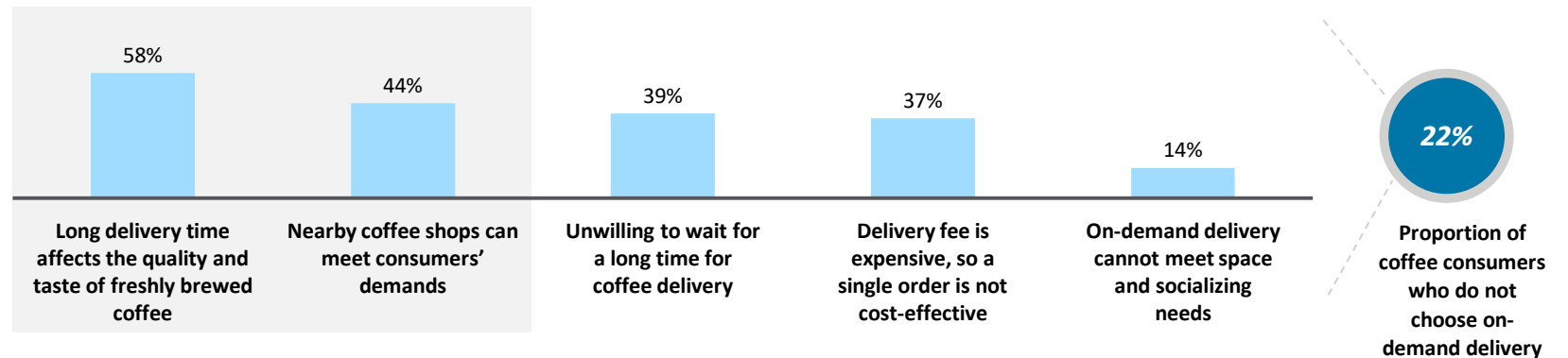
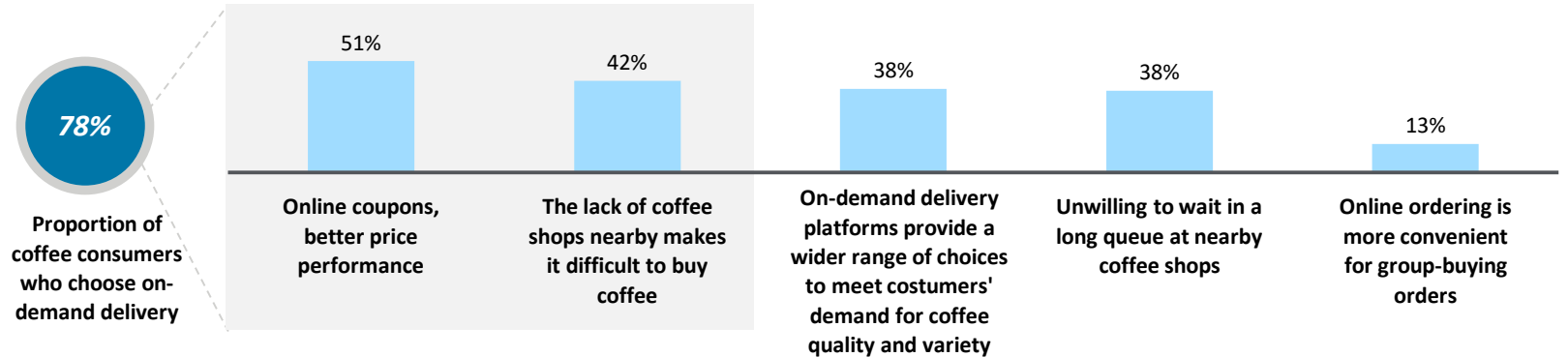
"Fast coffee" scenarios – on-demand coffee delivery

With the gradual disappearance of online discounts, buying coffee online is losing its advantage in price performance. Meanwhile, due to the less-favored taste of takeaway coffee, and further rollout of cost-effective or high-quality coffee brands, on-demand delivery is unlikely to have a disruptive impact.

In recent years, as the industry's new breakthrough point, coffee delivery business created many new coffee consumption scenarios. 78% of consumers would buy freshly brewed coffee through on-demand delivery platforms. Most consumers tend to choose coffee delivery for its online discounts and convenience. With the gradual disappearance of online discounts, and additional delivery and packaging fees, buying coffee online will lose its advantage in price performance.

Deliveries inevitably affect the quality and taste of freshly brewed coffee. With a further understanding of coffee, consumers will be more willing to buy better quality coffee and might no longer choose coffee delivery once there are enough cafés near to them that can meet their demand for price performance or quality. In other words, consumers' loyalty to coffee delivery is not high, and with the further rollout and expansion of quality coffee brands, on-demand delivery is unlikely to have a disruptive impact on the existing pattern.

Reasons for choosing on-demand coffee delivery



Reasons for not choosing on-demand coffee delivery

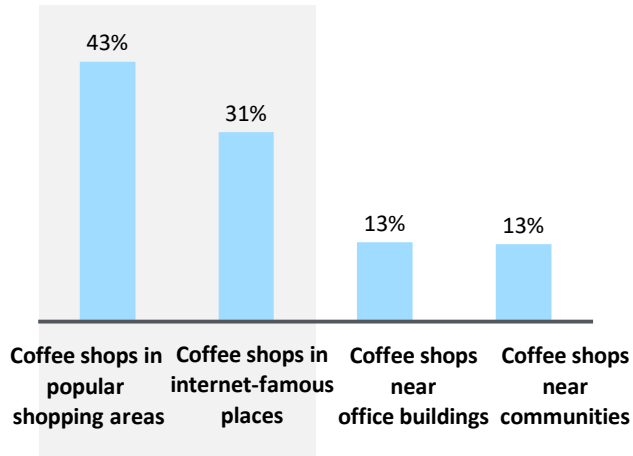
"Slow coffee" scenarios – shop type preference

In "slow coffee" scenarios, consumers have lower requirements for convenience and are willing to pay higher prices for coffee products. They also have high requirements for food and environment, including the quality of baked food and desserts, comfort and interior design.

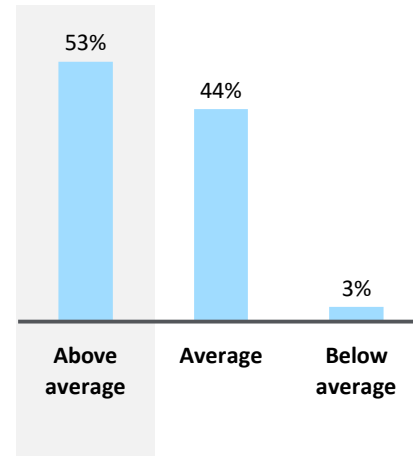
Consumer preference for brands and shop types in "slow coffee" scenarios



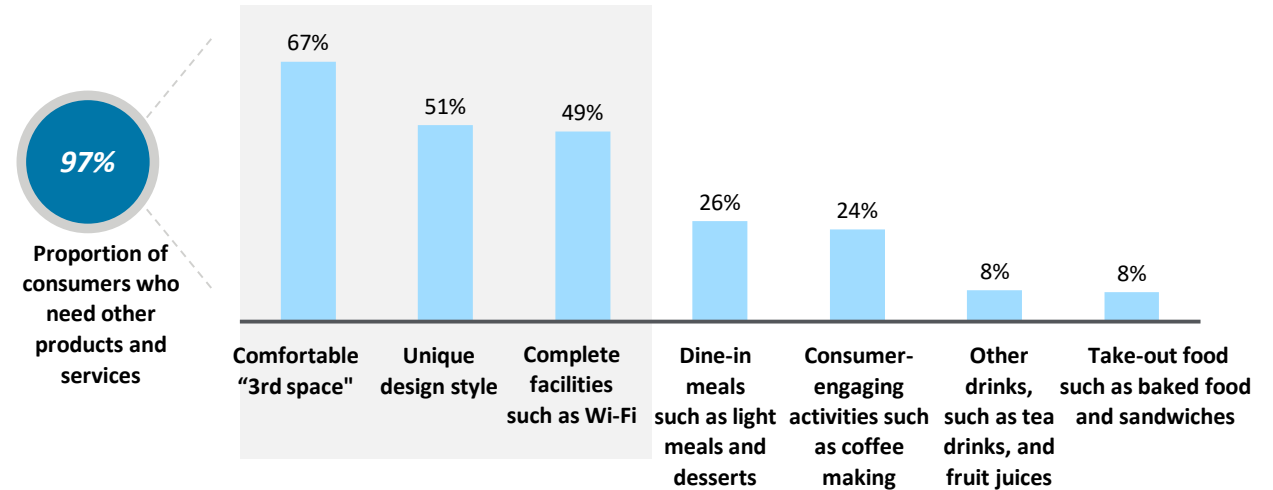
Location



Price



Products and services other than coffee products



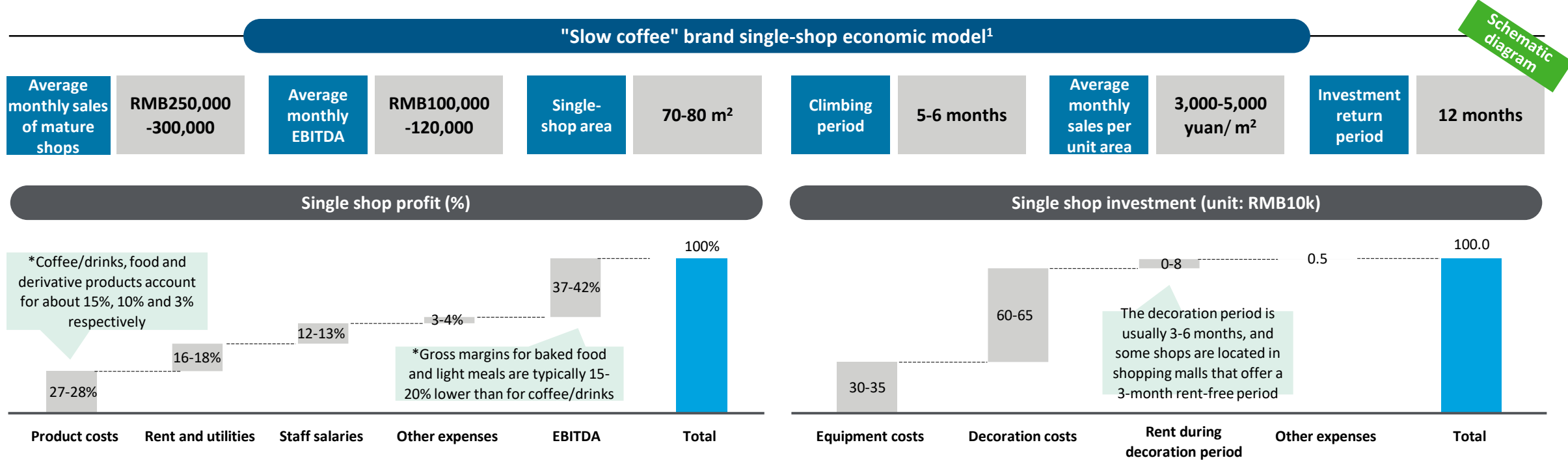
In "slow coffee" scenarios, coffee shops are a platform for socializing, and consumers pay more attention to their environment than they do to convenience, so their location is no longer as important a consideration. Coffee shops in popular shopping areas or internet-famous places will become potential consumption sites. The less frequent consumption of "slow coffee" also makes consumers less sensitive to price and willing to pay more for coffee with better quality. Cafés' comfort level, interior design and supporting facilities are also factors.

Source: Consumer survey, Deloitte's research and analysis

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"Slow coffee" scenarios – a single-shop economic model for freshly brewed coffee brands

A coffee shop catering to "slow coffee" scenarios should have a large space and provide a variety of drinks, food and other products. Compared with the small shop model, the large shop model requires a longer climbing period and higher costs, so it is not profitable in the short term and the investment return is slower.



A coffee shop catering to "slow coffee" scenarios needs to provide consumers with plenty of space and a great atmosphere, so it requires a larger area and elaborate decoration to create a "3rd space". Such coffee shops also need to offer baked food, meals and drinks to keep consumers in the shop. Although overall gross margin will decline, average transaction value will improve and revenue will increase.

Compared with the small shop model, the large shop model is more expensive in terms of rent and staff salaries, and takes some time to achieve stable customer flow, so the investment return period is longer and outlets cannot multiply as quickly.

Note: 1. Taking coffee shops in popular shopping districts of Shanghai as an example.
Source: Deloitte's research and analysis

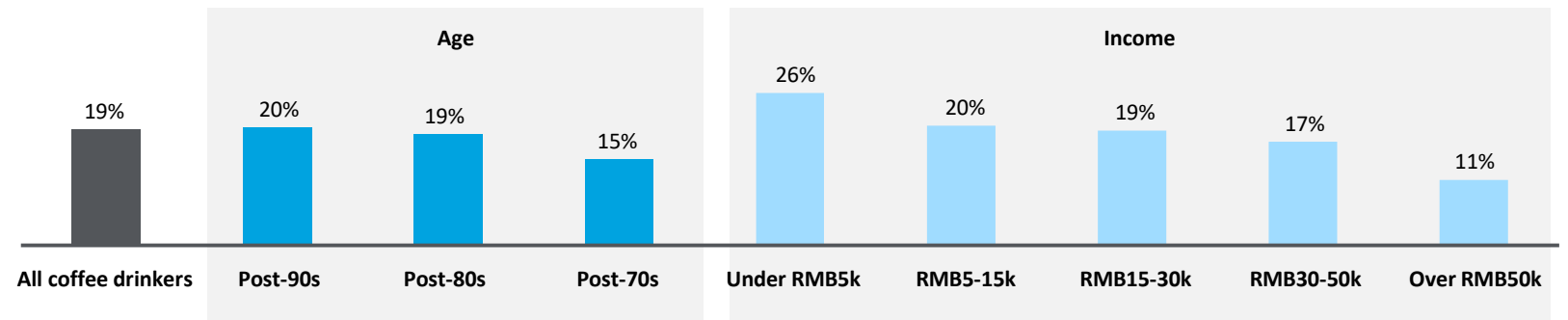
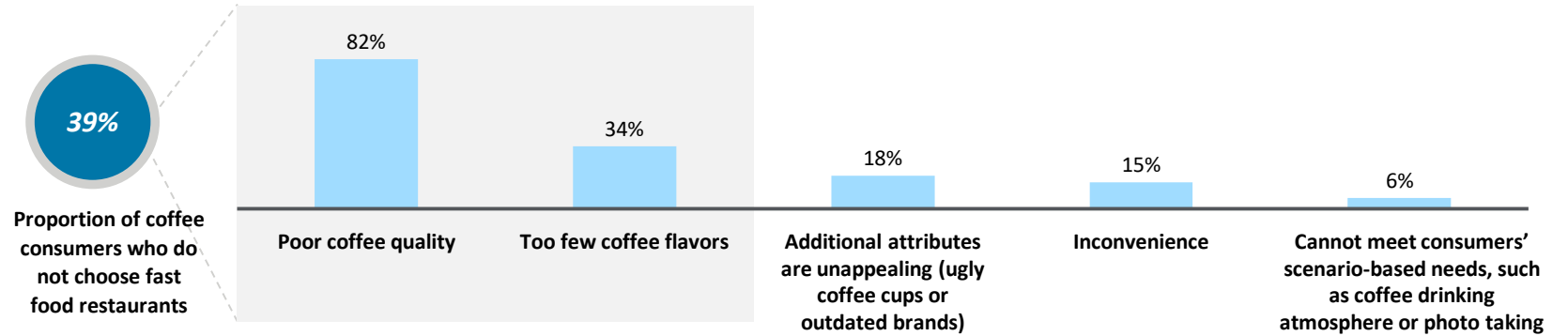
"Slow coffee" scenarios – fast food caterers

Fast food stores and coffee drinking scenarios still have a time-space mismatch. Fast food restaurants can increase the probability of consumers pairing coffee with breakfast or lunch, and reduce consumers' purchases at freshly brewed coffee shops to a degree, but they cannot meet consumers' speed and scenario-based needs.

With McDonald's and other fast food giants accelerating their coffee businesses, 61% of consumers buy freshly brewed coffee at fast food restaurants. Benefiting from a complete range of product supplies, fast food restaurants can meet the needs of consumers who wish to enjoying coffee and meals at the same time. Relying on their network of existing outlets, these coffee shops are launching a "breakfast/lunch + coffee" model. These stores may reduce consumers' purchases at freshly brewed coffee shops to a degree, poor coffee quality and limited flavors are still the core pain points of fast food restaurants. This is the main reason 39% of consumers do not buy coffee in fast food stores.

Unlike either Starbucks Coffee and other freshly brewed coffee shops, which are a "3rd space", or convenience stores, which focus on price performance, fast food caterers are committed to relatively ambiguous "in between" consumption scenarios. Only 19% of consumers will buy coffee from fast food caterers more often in the future, while younger, lower-income consumers are more willing to do so. There is still a time-space mismatch in between fast food restaurants and coffee drinking scenarios, and whether fast food restaurants will be accepted by coffee consumers in the future has yet to be tested by the market.

Reasons for not buying coffee from fast food restaurants



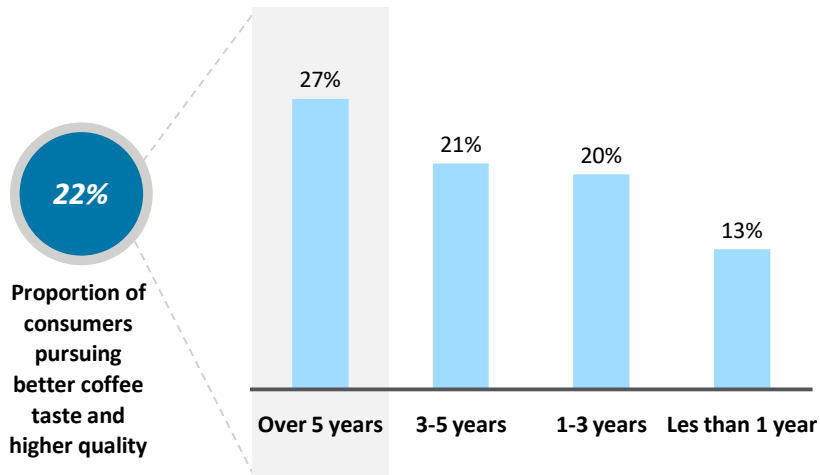
Proportion of consumers who will buy coffee from fast food restaurants more often

"Slow coffee" scenarios – independent boutique cafés

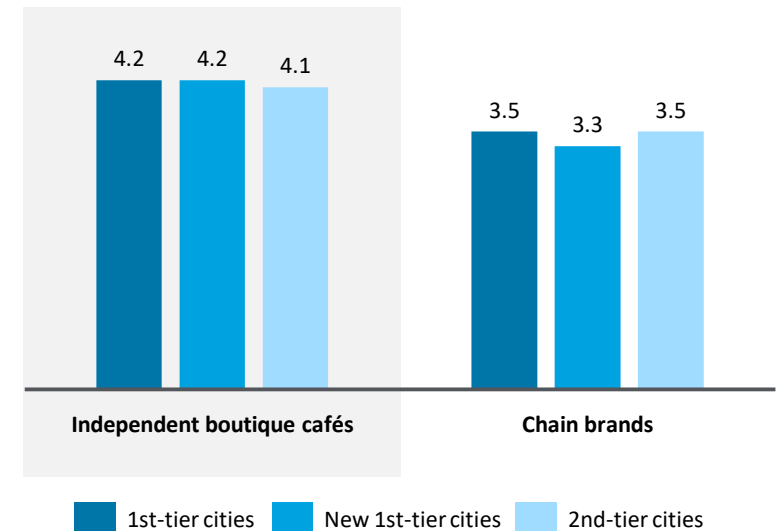
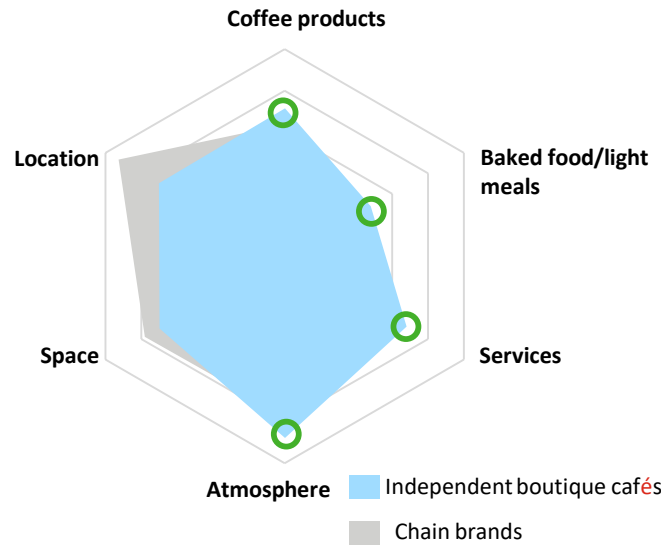
At present, young people are still the main consumers for independent boutique cafés. In addition to their unique characteristics and style, independent boutique cafés, compared to large chain brands, generally enjoy high popularity due to their coffee taste and quality and café atmosphere, which could become the core advantage for their expansion.



The pursuit of coffee taste and quality by consumers depending on how long they have been drinking coffee



Consumer reviews of independent boutique cafés¹



In "slow coffee" scenarios, independent boutique cafés are increasingly favored by consumers, especially the younger generation. The longer they have been drinking coffee, the more consumers value taste and quality. Independent boutique cafés have gained recognition in terms of their high quality services, coffee products, unique brand identities and interior design. Compared with large coffee chains, consumers have a higher opinion of independent boutique cafés. With rising incomes and the accelerated popularization of coffee culture, specializing in high-quality coffee could become the core advantage of boutique cafés.

Note: 1. Consumer evaluation includes the proportion of positive keyword mentions in the total number of positive and negative keyword mentions for each dimension of brands and shops on social media platforms, and the average single shop rating on social media platforms.

Source: Consumer survey, Deloitte Analytics Institute, Deloitte's research and analysis © 2021. For information, contact Deloitte China.

Key success factors for freshly brewed coffee brands

In "fast coffee" scenarios, brands need to pursue price performance and convenience, and adopt a small shop model to focus on coffee products and quickly multiply outlets. In "slow coffee" scenarios, brands need to focus on taste and customer experience, and provide quality food to improve average transaction value.

Key success factors for "fast coffee" scenarios



- Focus on price performance, convenience, and low unit price while ensuring the quality of coffee; make sure coffee quality differs from those of convenience stores and office coffee machines



- Adopt a small shop (less than 20m²) model, select the sites with periodic customer flow or with relatively low rent near popular business districts, and achieve profits and investment recovery quickly with relatively low investment



- Focus on the quality of coffee and other drinks, without investing too much in other products such as baked food, light meals or the atmosphere of the space

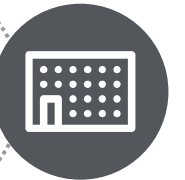
Source: Deloitte's research and analysis

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- Focus on taste and customer experience – that is, coffee quality, coffee culture, and the comfort level and uniqueness of the space and atmosphere, to meet consumers' need to "slow down"



- Adopt a medium/large shop (50-100m²) model, focus on shop design, spaciousness and comfort, while avoiding the bad customer experience of existing large-scale comprehensive chain brands or internet-famous brands



- Ensure the quality of coffee; provide a wide range of high-quality baked food, light meals and derivative products to improve average transaction value and the sales per unit area



Key success factors for "slow coffee" scenarios

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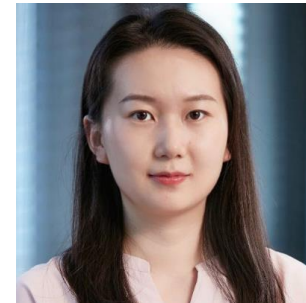
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