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China

What recession?

New brand entries, more store openings, robust growth—
China's beauty market emerges unscathed from the downturn

The recession has done little to dampen spirits in China's beauty market. US-based research group Kline & Company predicts the market will grow by 11% in 2009, just 1% less than in 2008. The selective market is seeing an even stronger performance, with sales up 20%. The top end of selective—high-priced skincare product retailing at over \$115—also continue to do well. The downsides are in color cosmetics, whose value growth fell by 3 percentage points between 2007 and 2008, according to Euromonitor and in fragrance, where the growth rate dropped from 22% in 2007 to 15% in 2008. Some manufacturers have also noted that while the impact of the recession on beauty is minimal, consumers are planning their purchases less and buying fewer products ahead of when they may need them. They are also paying more attention to value, in-store service and expertise.

The majors battle it out

As the growth rates increase, so does the battle for market share. Heavyweight P&G saw a slight decline in its market share in 2008, says Euromonitor, due to increased competition from rivals L'Oréal, Unilever, Shiseido and Beiersdorf. L'Oréal said its sales in China grew by 27.7% in 2008 and it claims to be the number-one skincare group in mass and prestige combined. Its L'Oréal Paris brand boasts the number-one spot in its distribution, while Lancôme claims a 20% share of the selective market and the top ranking in prestige skincare. L'Oréal says that it has also seen a 'phenomenal' response to Kiehl's, whose first Chinese door opened in Beijing in July.

Meanwhile, The Estée Lauder Companies (ELC) reported that in fiscal 2008 sales from China reached \$100m for the first time. The group now sells most of its major brands in the market and the Estée Lauder brand ranks number-two in prestige skincare. ELC announced that it would put greater focus on skincare and the Asia region, meaning that the group will become even more aggressive to increase its share in China. LVMH is pushing ahead with its Dior brand, which ranks number one in fragrance and make-up and number-three in skincare. As for Shiseido, it entered China in 1981 and may find the market more

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L'Oréal China luxury products division vp
Philippe Lamy

China retail

- Dept stores: 5,300
- Watsons stores: 450
- Sephora stores: 53

Source: Kline & Co, industry sources

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■■■ competitive today, but claims to have kept the early-mover advantage. The Japanese group does 28% of its overseas sales in China, claims above-average profitability there and continues to see strong success with its *Auprès* brand, which it is currently revamping; it has introduced new technology to the brand and is redesigning counters. The company hopes the revamp will increase the number of *Auprès* users from 1.2 million to 2.1 million.

Building brand awareness

Big-name brands continue to be important for Chinese consumers, as there is still a risk associated with buying lesser-known lines and a reluctance to switch brands. According to McKinsey, 63% of shoppers enter a shop with a shortlist of favorite brands or a single preferred one and will not stray from it. "Consumers have a basket of around five brands, and it's hard to break into that. Yet there is huge pressure to keep up and so they're open to new things," says consultancy Innovatize managing director Thomas Wetherell. He adds: "If you have a good story and communicate well you can interest them. There's a lot of opportunity for niche brands or smaller firms". L'Oréal China vp luxury products division Philippe Lamy agrees: "Kiehl's resonated as it has an authentic brand story. Chinese consumers want to understand the brand and almost appropriate it." But building awareness for an unknown line in a market dominated by ■■■

China C&T sales 2003-2008 by category \$bn

Category	Sales \$bn 2008	% Change 08/07	% CAGR 08/03
Skincare	6.98	15.6	18.0
Haircare	3.50	10.3	8.5
Premium cosmetics	2.49	15.8	19.7
Bath & shower	1.94	6.1	6.7
Color cosmetics	1.81	12.4	12.1
Fragrance	0.47	14.6	19.1
Babycare	0.40	14.3	11.2
Men's Grooming	0.35	14.2	12.2
Suncare	0.35	15.8	16.2
Deodorants	0.06	12.8	16.6
Other (oral hygiene, depilatories)	4.70	-	-
Total C&T	18.09	11.8	11.9

Source: Euromonitor, retail sales price

NB: Premium cosmetic sales are additionally included within babycare, bath & shower, deodorants, color cosmetics, haircare, skincare and suncare.

Sum of sectors is greater than market size as the four men's toiletries subsectors are included in men's grooming as well as in deodorants, skincare, bath & shower and haircare.

“Some channels need to update their formats. Department stores need to redecorate and stock more fashionable brands”

Kline & Co engagement manager China
Rob Field-Marsham

China

■■■ L'Oréal, Lauder or Dior is tough. Wetherell suggests that smaller companies focus on alternative communication vehicles, especially the internet through blogs and forums. "The Chinese are doing a lot more on this than in the West, and you can create share this way," he notes. Chinese government statistics say there were 20 million Chinese bloggers, and 180 million internet users in 2008 and this figure is expected to reach 500 million by 2020.

The internet is also fast becoming an important distribution channel. For Lancôme, the web is its third most important door. In such a vast market, e-commerce enables brands to extend their reach to where they don't yet have department-store counters and also to reach a younger consumer base.

Developing department stores

When it comes to brick-and-mortar distribution, the rapid expansion of stores continues. Department stores, which account for 90% of the prestige market, have doubled in number since 2003, says Kline & Company, and there are now some 5,300 department stores selling cosmetics in the country. The leaders in sales terms include Parkson, Wangfujing, and Dashang Group. But while the number of stores has grown, some say their offer still needs work. "Some channels need to update their formats. Department stores need to redecorate and stock more fashionable brands," Kline & Company engagement manager China, Rob Field-Marsham comments. He adds that over-investment in department stores may cause problems as retailers don't have a clear focus on a customer segment and operating costs have grown. Indeed, there is little differentiation among department stores: most carry the same brands and have similar counter designs. Parkson has been singled out for offering a new shopping experience through special promotions and other events.

An alternative distribution?

Analysts say the real point of difference will come through new types of distribution. "One channel isn't enough for the market. It'll be good when more retailers come as it speeds up market [growth], but new retailers will need to target specific consumers and be different," Lamy explains.

LVMH-owned retailer Sephora has sought to bring an alternative to the market, and has been praised for attracting a different consumer from those in department stores (essentially a younger consumer). The retailer, which now operates 53 stores in the country, has been applauded for flexibility in its brand offer, especially its inclusion of local brands and niche lines. The company is also said to have improved its service level, with stores manned by knowledgeable sales assistants (which are ■■■

China prestige color cosmetics

Ranking	Brand
1	Christian Dior
2	Lancôme
3	Chanel

Source: Industry sources

China prestige skincare

Ranking	Brand
1	Lancôme
2	Estée Lauder
3	Christian Dior

Source: Industry sources

China prestige fragrance

Ranking	Brand
1	Christian Dior
2	Chanel
3	Lancôme

Source: Industry sources

China C&T market share %

Company	Market share %
Procter & Gamble	20
L'Oréal	5
Unilever	5
Colgate	5
Beiersdorf	4

Source: Kline & Co

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■■■ now provided by the brands). However, one Chinese brand manager told BW Confidential that consumers are still not used to the Sephora-style format and that it may take a long time before they come to accept it.

Fellow chain (although not exactly a competitor), Watsons, owned by the AS Watson group, sells predominantly mass health and beauty and is home to counters for some key prestige players. It is said to have nailed the niche of consumers who want to 'buy now without spending too much'. The chain's ambitious store-opening program underlines demand for this format. The company now operates 450 stores in China and plans to open 150-200 outlets per year. The response to its loyalty card is also telling. It launched the card (which consumers buy for a small fee so as to add value to the concept), in January this year and as of May there were three million members. Given this success, AS Watson is likely to concentrate on this concept for China for now rather than launch Marionnaud there. The company opened a Marionnaud store in Hong Kong in 2008, but doesn't seem in any rush to go beyond that in the region.

What future for new formats?

In terms of new concepts, analysts are waiting for the Body Shop to move into China, although owner L'Oréal hasn't revealed plans on this front. New prestige concepts may appear in hypermarkets, which have rolled out more upscale areas for mass brands, such as Revlon and Olay. Given the traffic at these stores, Wetherell believes that if hypermarkets become more flexible with their merchandising (perhaps develop what they are doing with some mass brands) prestige players may consider going there. But even in this fast-paced market that is unlikely to happen soon. With brands enjoying double-digit growth there isn't a pressing need to seek out consumers in other distribution. For now the focus is on market-share gains, brand building, expansion beyond the main hubs, and delivering growth to companies that are seeing their business stagnate elsewhere. ■

Fragrance: to be or not to be?

Opinion is still divided on the potential of fragrance in China. The category represented 2.6% of the C&T market in 2008, or \$0.47bn in sales, according to Euromonitor. Fragrance is often bought as a gift or a novelty item or because of its brand name, but rarely for the juice. Some say fragrance will never be a big market as there is little interest in the category, and suggest that brands that want to pursue this direction should focus on 'teen perfume' or low-priced items. The category also receives little interest from retailers and distributors (who prefer to push the dominant and more lucrative skincare segment), making it difficult for fragrance companies to build brands and gain visibility. Others, however, say that there is a history of perfume in China and that fragrance will develop into a strong category there, especially as today's younger consumers become more exposed to the product. They maintain that although fragrance may be a slow (and expensive) build, the industry needs to come up with the right product mix that will appeal to this consumer.

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Innovatize md
Thomas Wetherell.