Unmasking the secrets of Chinese beauty

A peek into China's skincare consumption trends and winning tips to thrive in the world's largest skincare market.

OC&C
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uncommon sense

This market is as challenging as it is attractive

Unmasking the secrets of Chinese beauty

At US$22 billion, China has the largest skincare[1] market in the world, and it's also one of the fastest growing regions among major skincare markets. Furthermore, since China's skincare spending per capita is still very low compared to that in other major markets, there is plenty of room for growth.

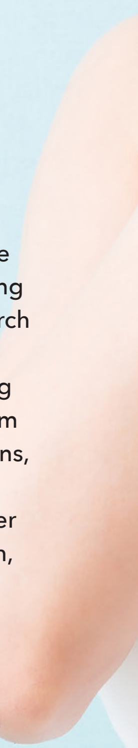
China has a long historical tradition of developing beauty treatments from natural herbs and oils, rice water and powdered pearls. As Chinese women have gradually shifted to modern cosmetics, they have maintained a high degree of sophistication in their skincare consumption habits. Also, as their needs rapidly evolve, they are increasingly demanding, always curious about the latest trends and technologies, and eager to trade up to better products and brands.

But this market is as challenging as it is attractive. On the one hand, the market is incredibly crowded and competitive – the battle among international giants from Europe, the US and Asia is fierce. These international brands are still dominant, but local leaders are quickly catching up, with new brands popping up continuously.

On the other hand, with consumers' growing sophistication and thirst for innovation, brand loyalty is now nothing but wishful thinking.

To capture the exceptional market opportunities in China, brands need to adopt highly customer-centric strategies. From our research, there seem to be three golden rules: 1) Keep product offerings relevant, 2) Engage with millennials and post-millennials through Key Opinion Leaders (KOLs) 3) Balance physical and digital retailing for a perfect mix of experience and convenience.

In order to better understand Chinese skincare consumers and their changing behaviour, OC&C conducted a research project in late 2017, which included an online quantitative survey covering 2,800 female skincare consumers from 20 Tier 1-3 cities across China's regions, complemented by several consumer focus group discussions and a number of in-depth interviews. In the research, we assessed consumers' general preferences, key buying factors and changing behaviours in the skincare category. We also measured their perception of different brands from a variety of perspectives. This report shares some of the key findings arising from this research. More in-depth analysis is available on request.



[1] In this report, "skincare" refers to facial care products only, excluding colour cosmetics and fragrances

JIAYI'S STORY:
It's been four years since Jiayi graduated from university and started to work in the human resources department of a large multinational corporation in Shanghai. As someone who follows fashion and beauty trends closely, she is devoting much of her income to beauty products – and quite a lot of her time as well. She follows a number of beauty KOLs on Wechat and Weibo, which she checks regularly. From time to time, she also flips through the "Little Red Book", the social shopping app, but she only occasionally reads beauty magazines.

Most of Jiayi's skincare products come from two brands – Shiseido and Fancl, which she has shortlisted (after extensive research and reviews) to be the most suitable for her skin type. Sometimes she also tries other products recommended by her favourite beauty bloggers, but most of these products become one-off purchases, as they tend not to meet her high expectations.

She started using moisturising cream after she graduated from high school at the age of 18 and her spending on skincare has grown over the years since then. At 25, she is increasingly concerned about her skin and is considering further upgrading her daily routine. She is still in the research phase to find the best products for her skin.

"Since I am now 25, moisturising and whitening are no longer sufficient. From now on, I think I should start using an anti-ageing serum and a sunscreen every day. I have to invest more to keep my skin flawless." – Jiayi

A powerful quest

Jiayi is not an exception. Our survey showed an overwhelming desire to spend more year-on-year across all age groups and income levels. Over 88% of our survey respondents indicated that they increased their skincare spending in the last year.

This increased spending is happening along three dimensions: Trading up to better (more expensive) products within the same brand, trading up to better (more expensive) brands, and increasing the number of skincare steps in the daily beauty routine.

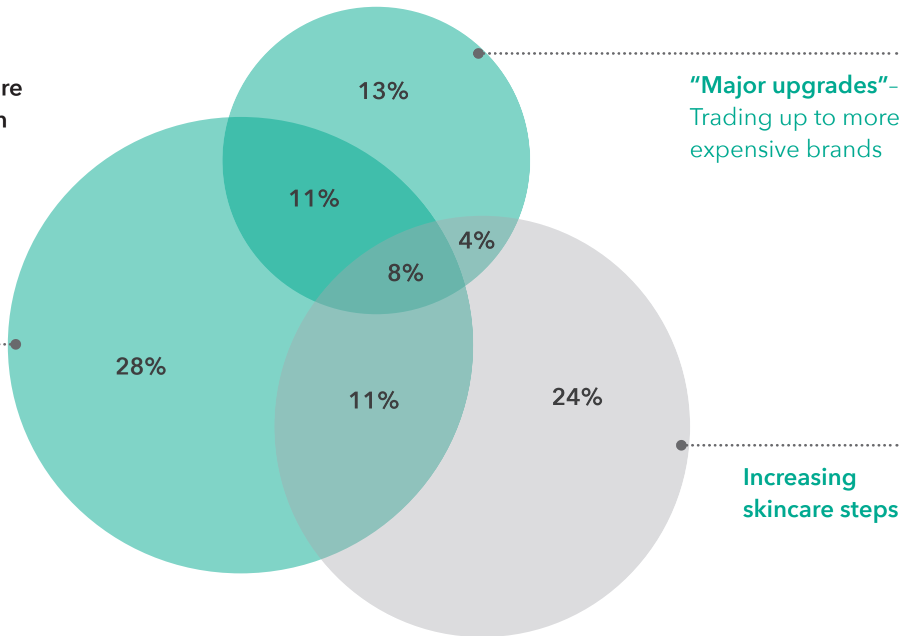
Premiumisation is a major trend – 58% of survey respondents claimed that they traded-up to more expensive product lines within the same brands last year, while 36% of respondents upgraded to more premium brands.

And consumers are trading up with clear reasons! As many as 39% of the total respondents claimed that better ingredients and improved functions were the key reasons for their decision to switch to more premium lines or brands in the last year.

Chinese women are also adding more steps to their daily routine. To the basic use of a facial cleanser and a moisturising cream, they have added the application of a toner, an eye cream and a serum. Around 70-80% of the respondents also use makeup remover, mask and sun cream on a daily basis, which adds up to an average of six to seven steps as daily skincare routine. Some of our survey respondents were following up to nine steps in their daily skincare routine, especially the more "mature" women above 30 years old.

FIGURE 1: DRIVERS FOR INCREASING SKINCARE SPENDING (% OF RESPONDENTS, N = 2,581[1])

75% of the respondents claim that they upgraded to either **more premium lines** or **more premium brands** in the past 1 year



1.Those who are spending more - Q22: What has been the predominant change in how you spend money on skincare products in P1Y?

Source: OC&C skincare proposition survey (2017), OC&C analysis

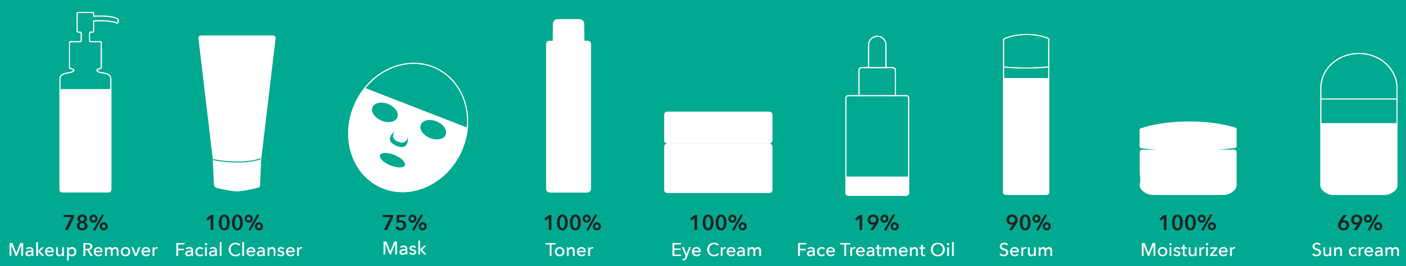
Premiumization
Increasing skincare steps

Research maniacs

More than 90% of surveyed respondents indicated that they conduct extensive research before they buy skincare products and online plays a critical role in this research. There are huge amounts of information on skincare brands across multiple channels in China. Third-party E-commerce websites such as T-Mall and JD are the main channels for browsing across brands and offerings, while social media also plays a critical role in building brand awareness and helping consumers develop product and brand knowledge.

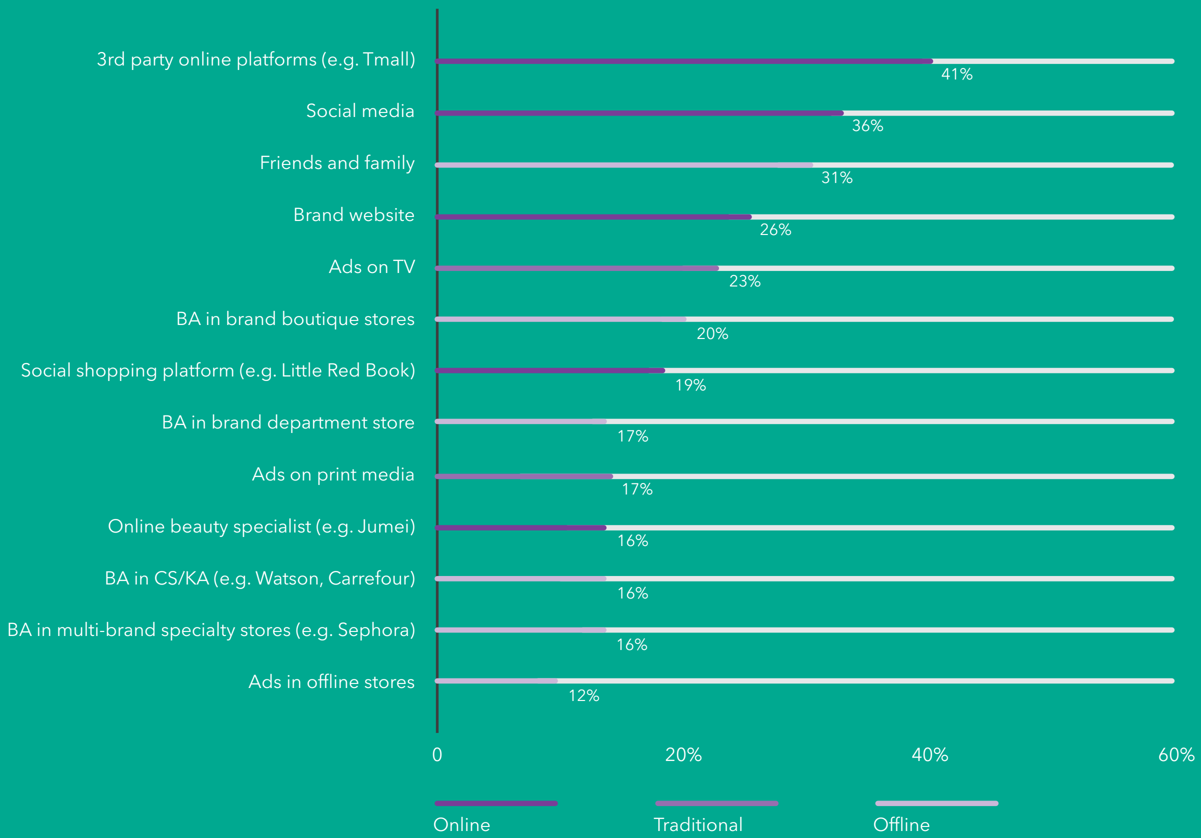
FIGURE 2: TYPICAL SKINCARE PROCESS[1] (% RESPONDENTS TAKING THE FOLLOWING STEPS, N = 3,050)

In addition to regular skincare steps, the use of home skincare tools has quickly gained popularity over the past few years . This is NOT covered in our survey



1.Q: Which steps does your daily skincare routine include?
Source: OC&C skincare proposition survey (2017), OC&C analysis

FIGURE 3: TOP INFORMATION SOURCE FOR SKINCARE PRODUCTS (N = 3,050)



1.Q: What are the top 3 information sources you use to do research/collect information before purchasing skincare products?
Source: OC&C skincare proposition survey (2017), OC&C analysis

Cracking the consumer behaviour code

So, in an environment where consumption habits and the competitive landscape are so rapidly evolving, what does it take to succeed? Here are a few tips from winners in the world's largest skincare market:

Stay relevant: The rules for a successful product offering

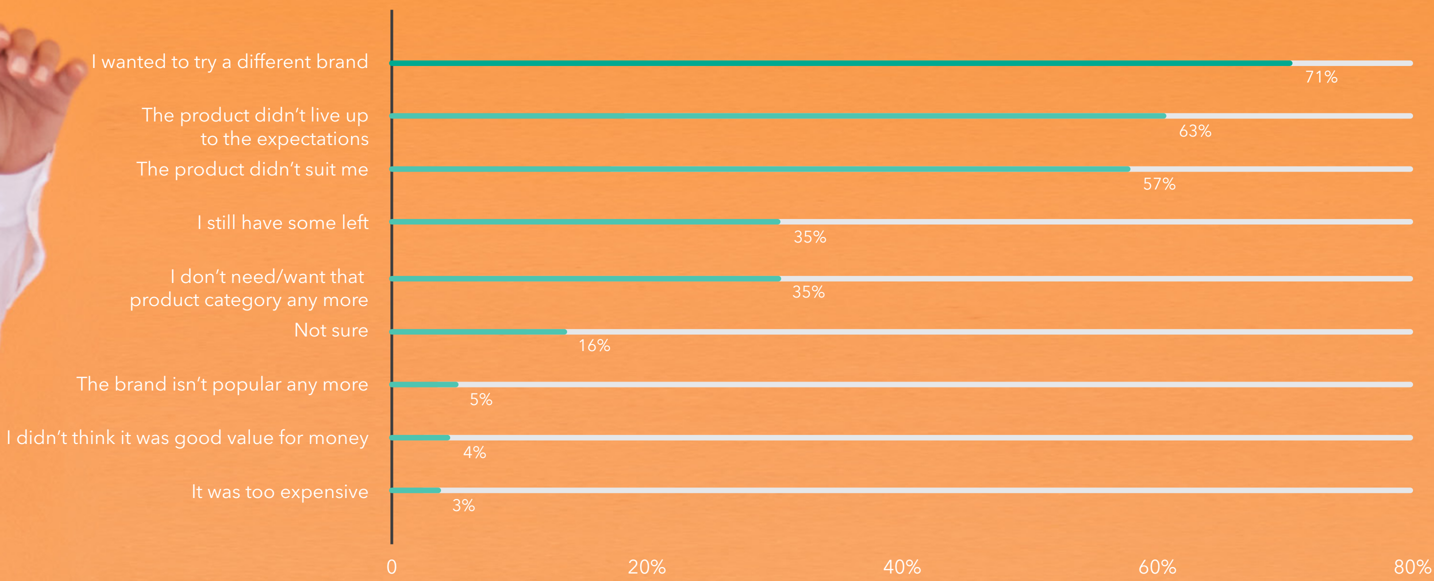
RULE #1:
START WITH A "STAR PRODUCT"

It's never easy to retain a customer in skincare market. Among all survey respondents, 22% have dropped a certain brands in the past one year, and the main reason was: "I want to try a different brand". Skincare consumers are always curious and tempted to try out the new products and concepts that are trendy in the market. For example, "anti-pollution" is one of the industry buzzwords that emerged in 2016. A while before that, there was a "snail beauty" craze made popular by the South Korean beauty brands. Another buzzword that has stuck around longer is the "natural and organic" concept, with industry advocates such as Jurlique and Origins.

However, brands' most successful products are always their long-standing "star products". Some of the most renowned and best-selling skincare products have decades of history. For example, SK-II's legendary Facial Treatment Essence was introduced in 1980; Estee Lauder's Advanced Night Repair, or "Little Brown Bottle", as it is lovingly referred to by consumers, was introduced two years later in 1982. Even for the relatively younger brand Laneige, their iconic product "Laneige Sleep Mask" also has 15 years of history.

More often than not, the first product through which consumers learn about a new brand is an iconic product, and that is usually the product that helps convert and retain customers. It is therefore critical for brands to build a strong star product, as it helps drive both customer acquisition and loyalty, while creating strong brand value in the long term.

FIGURE 4: REASONS FOR PRODUCT SWITCH (% OF RESPONDENTS WHO SWITCHED BRAND IN THE PAST YEAR, N = 1,557)[1]



1. Q: You mentioned that you purchased the below brands before but not in the P1Y, what's the most important reason? Sample size is associated with the number of brands that respondent has answered
Source: OC&C skincare proposition survey (2017), OC&C analysis

> Brands' most successful products are always their long-standing "star products". Some of the most renowned and best-selling skincare products have decades of history

RULE #2:
SPECIALISTS RATHER THAN "ALL-IN-ONE"

Consumers prefer brands that offer targeted and customised products, both in terms of function and skin type catered for. Compared to all-in-one products, they have much stronger faith in more specialised products, which are deemed "more professional / effective", while – according to consumer focus group participants – "multi-functional all-in-one products seem to be weaker in each function and do not have a clear proposition."

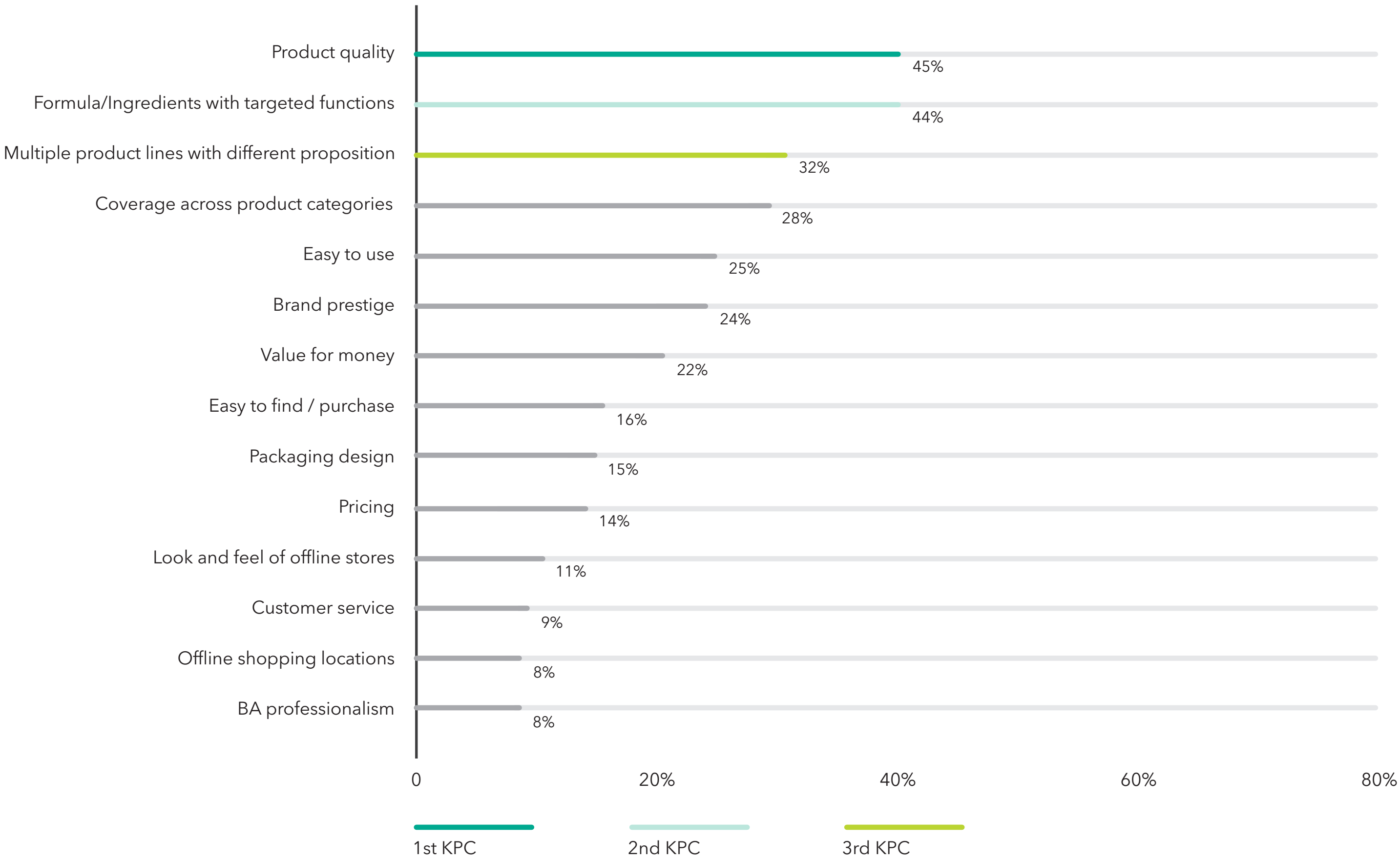
Key function focus / expectations mentioned by respondents include moisturising, oil control, pore refining, and whitening / brightening. Compared to their western counterparts, Chinese female consumers place a stronger focus on whitening, as white skin is preferable to tanned skin in Chinese culture.

RULE #3:
FULL SETS AROUND THE 'STARS'

Consumers have a growing appetite for product sets. Roughly 75% of the respondents have a growing tendency to choose skincare sets from specific brands rather than mixing & matching multiple brands. This is partially driven by the fact that product sets usually offer favourable discounts on price and come with gifts when purchased. These are considered to be the key reasons for choosing sets by c. 40% of the respondents. On a similar level of importance as the drivers for using sets, some consumers believe that using products from the same series brings out the best results. It is common for consumers to stick to using sets under one or a couple of brands, while trying out single products from other brands.

Star products, usually high value items, are the key trigger for consumers to start using the sets under specific brands. Structuring product sets around star products is therefore a smart way for brands to effectively drive sales and create loyal customers.

FIGURE 5: KPC IN SKINCARE SHOPPING (% OF RESPONDENTS SELECTING EACH FACTOR AS TOP 3 KPCS, N = 3,050)[1]



1. Q: What are key factors you will consider when you make a purchase in skincare?
Source: OC&C skincare proposition index (2017), OC&C analysis

Engage with millennials and Generation Z consumers

RULE #4
THE EARLIER THE BETTER:
Our survey found that Chinese women start using skincare products earlier and earlier.

A quarter of Generation Z survey respondents (those born in the 1990s) claimed that they started using skincare products as early as 18 years old, and 90% of them before they were 20 years old!

Meanwhile, roughly 80% of millennials (born in the 1980s) claimed that they started to purchase their own skincare products before they were 20 years old; while this percentage was only 70-75% for those born in the 1970s.

Our survey also showed that Chinese women form their knowledge of skincare treatment through experimentation and brand-switching mostly before they reach the age of 25, and then settle into a more loyal consumption pattern of their preferred brand set around the age of 30.

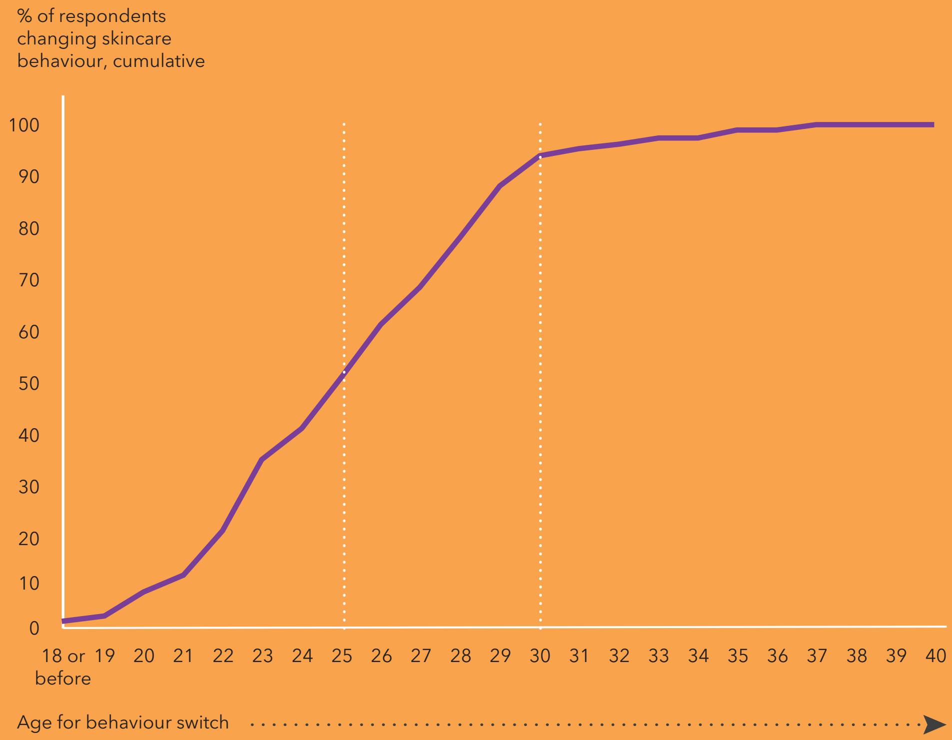
This means that brands have to make sure they educate Generation Z and catch Millennials at an early stage of their skincare discovery journey.

FIGURE 6: AGE WHEN CONSUMERS STARTED TO PURCHASE SKINCARE PRODUCTS THEMSELVES BY AGE GROUP (N = 3,050)[1]

1. Q: What age were you when you first purchased a skincare product for yourself? (age)

Source: OC&C skincare proposition survey (2017), OC&C analysis

FIGURE 7: AGE WHEN CONSUMERS CHANGE SKINCARE BEHAVIOURS[1] (% OF RESPONDENTS CHANGING SKINCARE BEHAVIOR, CUMULATIVE)



1. Q: You mentioned that, compared with previously, you tend to use product sets from selected brands rather than mix & match from many brands by yourself / you tend mix & match from many brands by yourself rather than use product sets from selected brands. When did you start to make that switch?

Source: OC&C skincare proposition index (2017), OC&C analysis

RULE #5: HIRE THE RIGHT KOLS TO INFLUENCE AND INSPIRE

Chinese Millennials are known for their digital savviness in the world's most advanced digital ecosystem. Generation Z consumers will take this to the next level, with an even higher level of expectations related to brands' presence and activity on social networks and digital-enabled services.

In this environment, Key Opinion Leaders (KOLs) have great power. Most of our survey respondents indicate that they are positively influenced by KOLs, with Generation Z customers being the most receptive and responsive group.

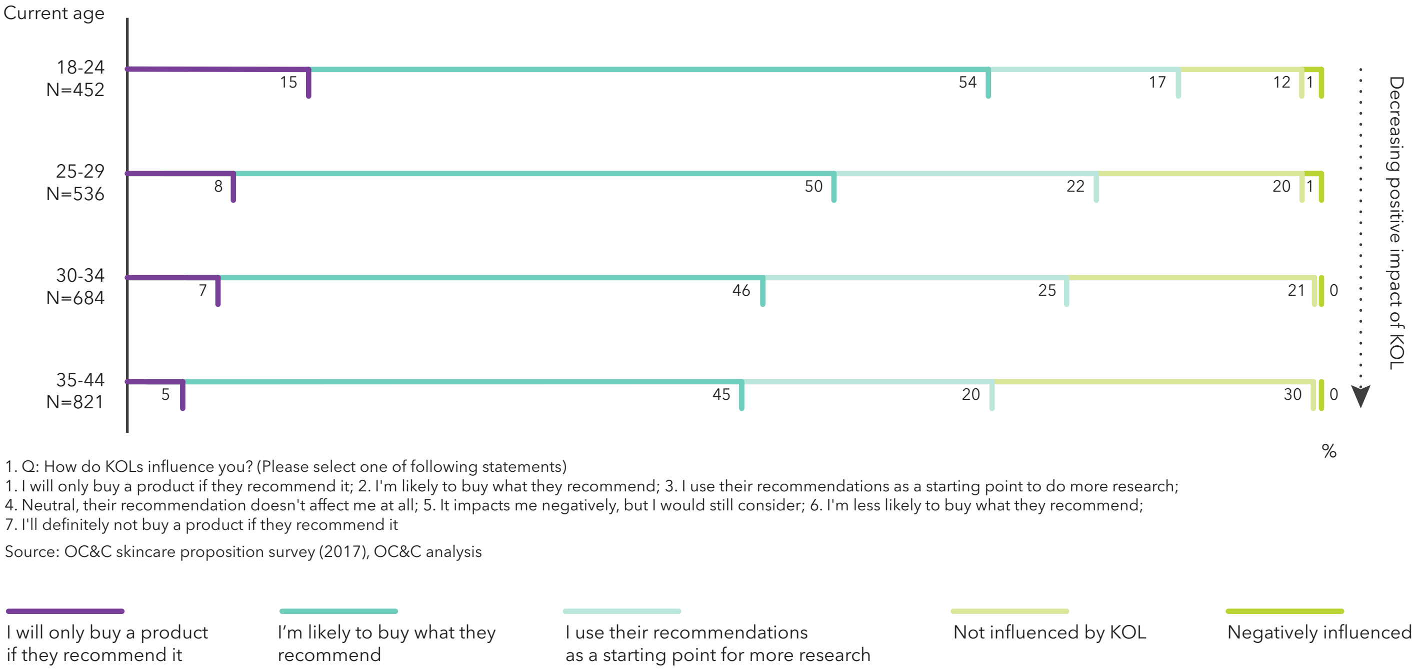
Likewise, KOLs were mentioned as part of the top three preferred marketing approaches by survey respondents in every age group.

Among KOLs, celebrities have been the most effective. Most of China's younger generation consumers have their own favourite idols, ranging from Chinese actress Yang Mi or singer Lu Han, to Korean boys' band The Bangtan Boys. The fan economy has transformed the way brands interact with consumers. Cosmetic brands, among other categories such as fashion and apparel, have been collaborating closely with top idols to leverage their influence on younger generations.

For example, one of the leading local cosmetic brands Chando started a collaboration in 2016 with TF Boys, a teenage Chinese pop band and it is not uncommon for cosmetic brands to work with male artists, targeting their strong female fan base. Chando's product line, which was endorsed by TF Boys, doubled their sales during the tracked period in 2017 vs. 2016.

Chinese beauty bloggers are the second most influential group of KOLs for skincare products. Consumers tend to keep themselves updated on content posted by these professional bloggers, and are more likely to purchase after repeated exposure from them. For example, 50 famous beauty bloggers were invited to do a 20-minute livestream video for the recent launch of a new L'Oréal Paris lipstick, resulting in 10,000 units being sold in two hours on its T-mall flagship store alone. Marketing collaboration with these KOLs, while effective, can be very costly: Papi Jiang, a phenomenal internet celebrity, sold her first video ad for an astonishing 22 million RMB last year.

FIGURE 8: % OF RESPONDENTS INFLUENCED / NOT INFLUENCED BY KOL (N = 3,050)[1]



1. Q: How do KOLs influence you? (Please select one of following statements)
1. I will only buy a product if they recommend it; 2. I'm likely to buy what they recommend; 3. I use their recommendations as a starting point to do more research;
4. Neutral, their recommendation doesn't affect me at all; 5. It impacts me negatively, but I would still consider; 6. I'm less likely to buy what they recommend;
7. I'll definitely not buy a product if they recommend it

Source: OC&C skincare proposition survey (2017), OC&C analysis

FIGURE 9: TOP 3 RANKING OF PREFERRED MARKETING SCHEME BY AGE GROUP[1] (N = 2,320)

	18-24	25-29	30-34	35-39	40-44
1st	Live-streaming	Brand online marketing	KOL daily usage of the products	Drama/TV shows (product placement)	Drama/TV shows (product placement)
2nd	KOL daily usage of the products	KOL daily usage of the products	Drama/TV shows (product placement)	Events with KOL (gifting, gathering)	KOL daily usage of the products
3rd	Brand online marketing	Brand traditional marketing	Live-streaming	KOL daily usage of the products	Brand traditional marketing

1. Q: When KOLs influence you, which methods are most likely to attract your attention? Rate with 1-7, 1: least attractive, 4: Neutral, 7: most attractive
Source: OC&C skincare proposition survey (2017), OC&C analysis

"Advertorial is effective but it cannot be selling the brand too hard."

Focus Group Participants

"KOLs using the products themselves is the most convincing recommendation for me, e.g. WANG Fei using Bioderma makeup removal water."

Focus Group Participants

"I'd love to see KOL events (interaction/free gift) for fans – I always sign up for gift lottery to try out the products she recommended."

Focus Group Participants

Balancing experience and convenience

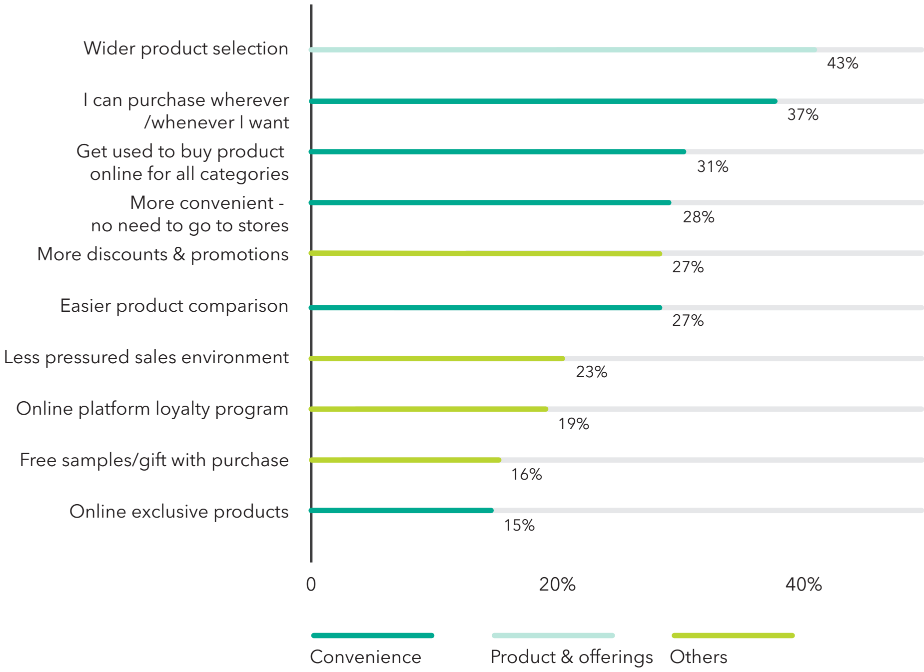
RULE #6:
OMNICHANNEL IS THE WAY TO GO

Only a generation ago, most Chinese consumers purchased all skincare products at local retail counters (super and hypermarkets for mass-market products and department stores for more premium products) where only limited options were available. Nowadays, consumers are enjoying much broader choices in more diversified channels.

Around 60% of our surveyed respondents indicated that they now shop both online and offline for skincare products, as opposed to shopping in one channel only, online or offline. This sends out a strong signal to skincare brand owners. Cross-channel shopping has become the dominant mode for skincare consumers in China, and building a seamless omnichannel shopping experience is therefore essential for a successful retail strategy.

Online is undoubtedly an increasingly critical channel for skincare product sales and internet retailing represented c. 20% of general skincare sales in 2016, surging from only 6% in 2011. The main reason for consumers to shop online is a wider selection of products. A total of 43% of all respondents indicate they shop online because of the wider brand selections available online or the convenience, while 37% indicate that they shop online because of broader brand and product selections. Consumers clearly shop online for convenience. This refers not only to avoiding time and location constraints when shopping in a physical store, but also to the ease of making product and brand comparisons.

FIGURE 10: TOP REASONS FOR CHOOSING ONLINE[1] (% OF RESPONDENTS, N = 2,953)



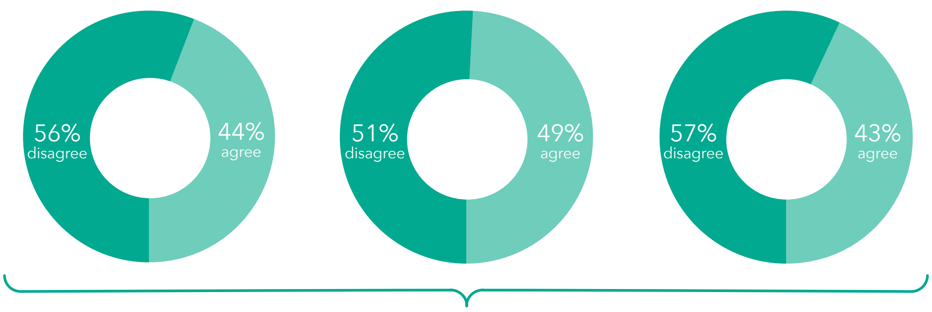
1. Q: What do you think are the main advantage for shopping skincare online?
Source: OC&C skincare proposition survey (2017), OC&C analysis

FIGURE 11: CHANNEL SELECTION BY PRODUCT TYPE (% OF RESPONDENTS, N = 3,050)[1]

"I tend to buy premium brands offline and mainstream online"

"I tend to buy more expensive products offline and cheaper ones online"

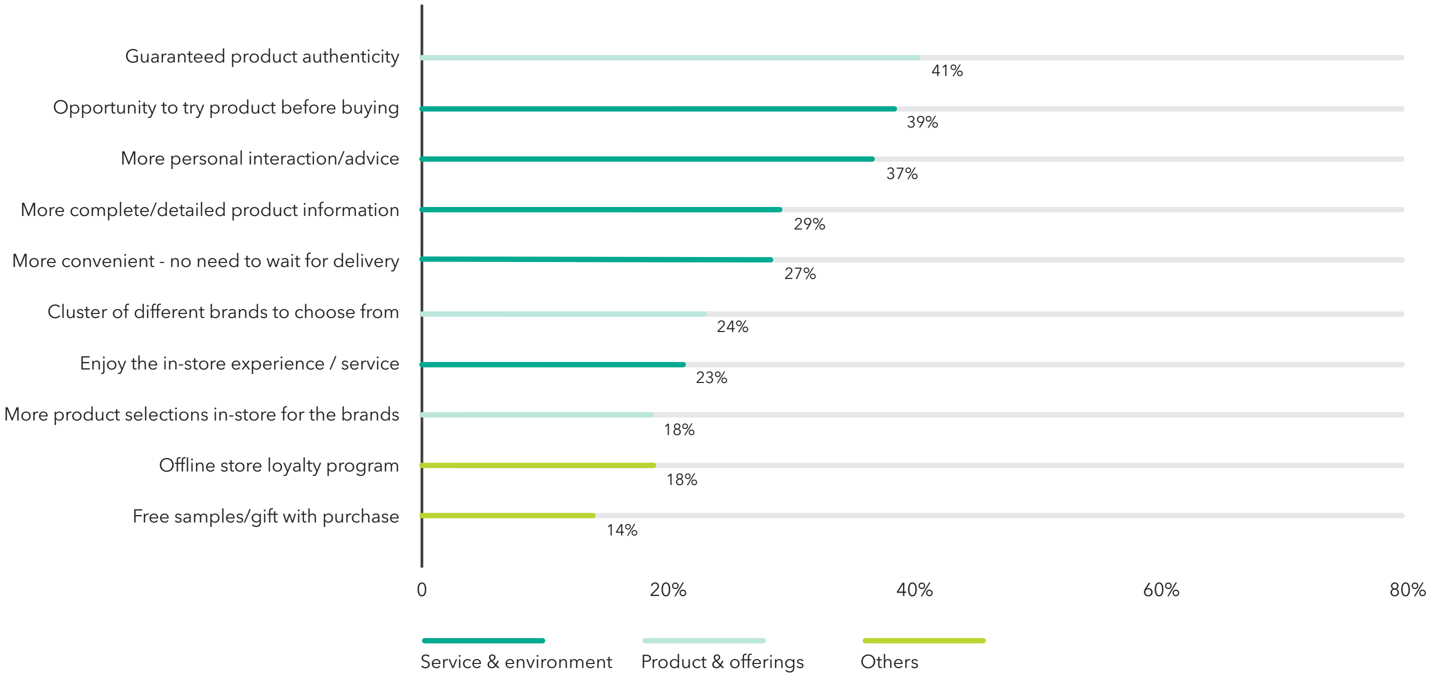
"I tend to buy smaller volumes online and full size offline"



Online is NO LONGER ONLY relevant with mass positioning brands / cheaper product categories / smaller volumes

1. Q: Do you agree or disagree with the following description on your skincare shopping and usage behavior?
I tend to buy skincare products of a premium brand in offline channel, and buy mainstream brands online (e.g. Lancôme in offline vs. DHC in online).
I tend to buy the more expensive products of a brand in offline, and less expensive products of the same brand online (e.g. serum in offline vs. toner in online).
I tend to buy skincare products of smaller volume online (e.g. 15ml, 30ml testers / combo) and full-size products offline.
Source: OC&C skincare proposition survey (2017), OC&C analysis

FIGURE 12: REASONS FOR CHOOSING OFFLINE[1] (% OF RESPONDENTS, N = 2,492)



1.Q: What do you think are the main advantage for shopping skincare offline?
Source: OC&C skincare proposition survey (2017), OC&C analysis

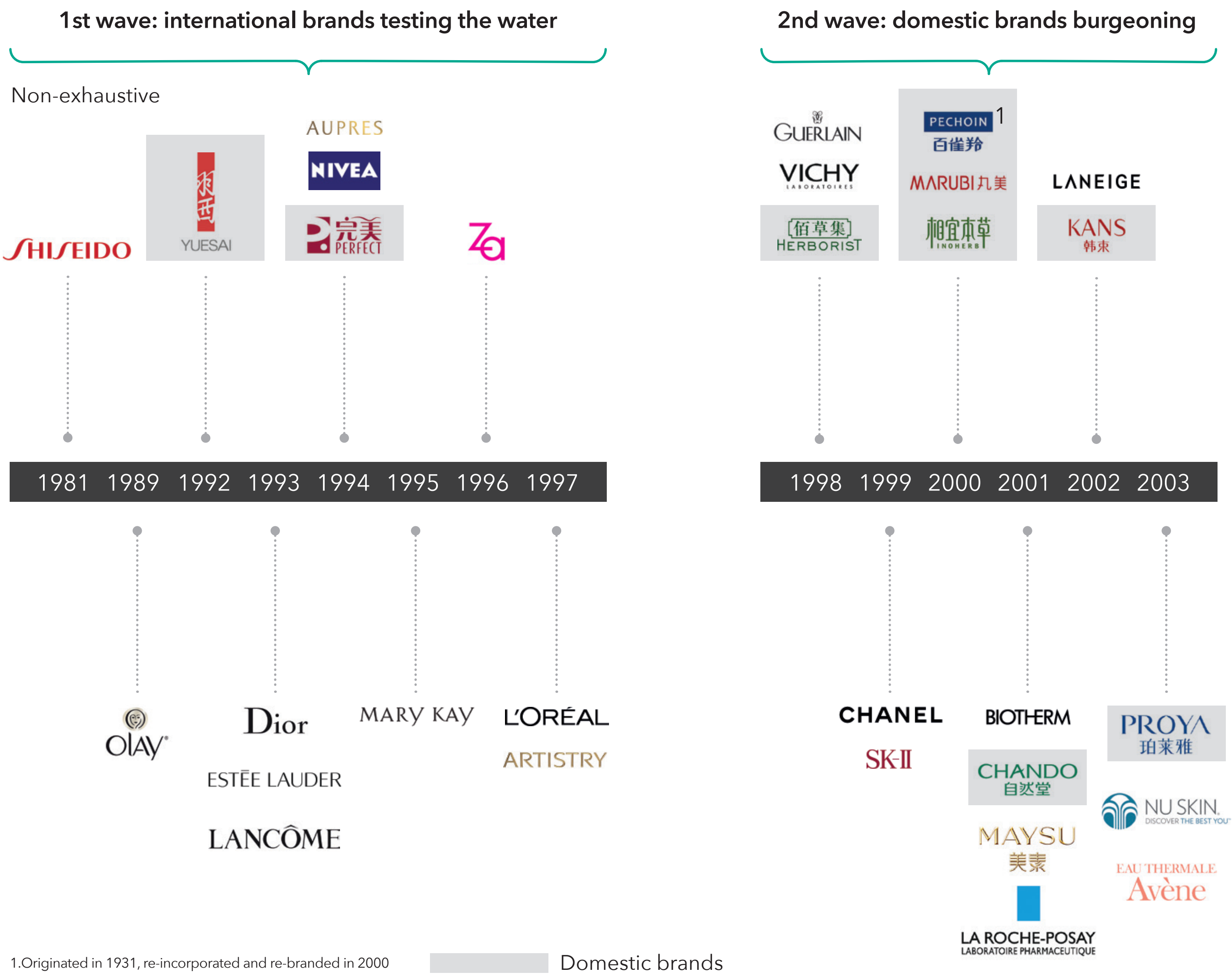
Whether brands like it or not, the online channel is no longer limited to low-value or cheap products, as consumers are ready to purchase premium skincare products online. As many as 56% of our survey respondents disagree with the statement that "I tend to buy premium brands offline and mainstream products online." Premium brands which had been very cautious about online distribution are finally catching up, for example LVMH Group's Guerlain has recently set up a store on T-mall. Meanwhile, Dior, Chanel and Estee Lauder have established independent online stores and opened Wechat brand accounts for communications.

However, offline channels are still very important. In addition to the perceived guarantee of product authenticity that they offer, the main reasons for consumers to shop offline are the services and in-store experience that they seek, which cannot be provided in online channels. As many as 41% of our survey respondents chose offline for "guaranteed product authenticity" as the main reason for offline shopping. The next most important reasons to shop offline were "Opportunities to try a product before buying", "More personal interaction/advice" and "More complete/detailed product information", which were mentioned by 39%, 37% and 29% of respondents, respectively.

An increasing number of beauty brands have started to offer beauty services and experiences in their stores, such as facial treatment and makeup and some are experimenting with more innovative cross-marketing concepts such as Chanel's Coco Café.

Magnet for brands

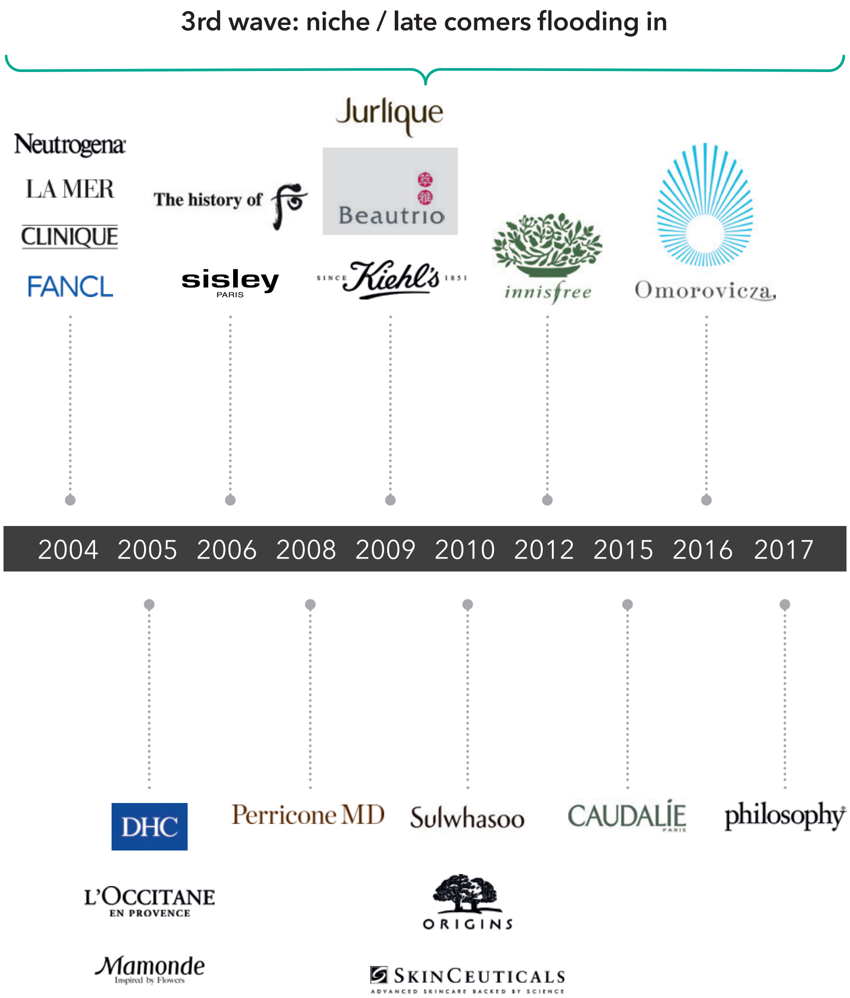
FIGURE 13: CHINA ENTRY / INCORPORATION HISTORY OF SKINCARE BRANDS



1.Originated in 1931, re-incorporated and re-branded in 2000
Source: desktop research, OC&C analysis

China's skincare market will continue to grow at a steady pace, fuelled by the rising middle class and their increasing disposable income and sophistication, and it will remain a magnet for the most ambitious international brands for years to come.

China is probably the most competitive battleground in the world, with powerful players from Europe, the US, Japan and Korea deployed at full strength. These companies have been joined by Chinese players, which have become serious challengers as they have dramatically increased their market share in recent years.



A look at the composition of China's top 10 cosmetics players over the period 2011 to 2016 illustrates this fast-evolving environment. Chinese players such as Pehchaolin, Chicmax and Infinitus, which were barely on the map five years ago, are now solid members of the top 10 club. Business models are also very diverse, with direct selling, mass channel and premium all represented in the top 10 group.

Respondents to our skincare brand survey ranked Chinese brands very highly, especially in the mass to mid-end segments, often ahead of the international powerhouses. Their success stems from their unique understanding of Chinese consumer needs and their exceptional mastery of China's digital ecosystem.

Aerial view Shanghai, China

The China prize is a big one. But the bar is being set higher and higher for those who wish to win big!

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