THE DAILY CHECK-IN WITH GOLDMAN SACHS

GUEST: CHRISTINE CHO, EQUITY ANALYST, GOLDMAN SACHS RESEARCH
HOST: LIZ BOWYER, GLOBAL HEAD OF BRAND AND CONTENT STRATEGY
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Liz Bowyer: Hi, Christine.

Christine Cho: Hi, Liz.

Liz Bowyer: You cover the beauty sector, which is one of the fastest-growing consumer categories in China. When we talked last summer, you talked about the surge in China's beauty market, driven mostly by millennials and Gen Z consumers. Now looking back on 2020, how did China's beauty sector fare?

Christine Cho: The market demand has been very resilient despite COVID, and we continue to see signs of premiumization as well as a rapid digital shift. One interesting angle that we look at the China market is both the combination of onshore consumption as well as offshore consumption. If you look at onshore, basically we see cosmetics retail growing 14% YOY in 2020. So started off for 1% YOY growth in the first half and sequentially accelerated to 26% in the second half.

In the offshore, which is basically travel retail, obviously it's been quite challenged because of the travel restrictions in place. However, the Korea DFS foreign spending, which is a good proxy for the reseller activity of Chinese daigous, was down 30% year over year. So all in, onshore plus offshore consumption combined, we expect about a 1% YOY decline as a whole in 2020.

Liz: And what's your outlook for China's beauty sector in 2021?

Christine Cho: We expect another record year for China beauty consumption driven by solid offline recovery as well as ongoing online penetration. All in, you know, travel retail still remains a bit of a swing factor for 2021, but we remain hopeful as the increasing vaccinations across the globe potentially will help bring signs of recovery in the second half of the year.

So all in all, we expect 22% YOY growth in the market to 650 billion renminbi or about 95 billion US dollars in 2021.

Liz Bowyer: And what about the role of ecommerce in the beauty market, which has been such a surprise success story during the pandemic?

Christine Cho: Oh, undoubtedly, there has been a rapid rise in online penetration last year. Almost a 7 percentage point jump to 38% in 2020. And we expect a continued rise to 57% by 2025. And in fact, actually a lot of the leading brands are already deriving between 50-60% of sales from these online channels already.

I think one interesting observation is that the depth and breadth of the online penetration has been expanding notably. So for example, we're seeing consumers above the age of 40 spending more online in terms of beauty. And also we're seeing increased consumption in various categories across personal care. For example, like, body wash, hair wash, hair care, in addition to the skin care and makeup.

We also observe that consumers are using more number of online platforms to make their purchases. And this is actually a great opportunity for digital-savvy companies to reach a refined set of consumer targets as well as maximize their reach into some of the consumers that they haven't been able to reach historically. For instance, there is fairly little overlap between the personal care consumers that purchase through WeChat versus Tmall and Taobao.

Liz Bowyer: Another thing that you touch on in your research is local Chinese brands moving towards a multibrand portfolio. How are you seeing that play out?

Christine Cho: One of the key pushbacks that the Chinese local brands have received in the past is regarding their heavy reliance on single brands, which raises questions as to the sustainable growth path in the longer run, especially in light of the shorter brand cycles that we observe in the younger consumers. So for example, let's take Yatsen. They've actually expanded their brand portfolio to include seven brands across makeup, skin care, and premium skin care. And that compares to the three that they had at the end of September 2020.

And a lot of the other local companies are also pursuing similar strategies in building a multi-brand portfolio. It would be very interesting to watch how this strategy pans out and also how it impacts the overall competitive dynamics in the longer run.

Liz Bowyer: So finally, Christine, it sounds like the outlook for China's beauty sector is positive overall, but what are some of the headwinds?

Christine Cho: A shift in consumer perception and value may significantly impact the industry. So for example, in recent years premiumization has been a dominant theme in China beauty, driving growth for the industry. But I can recall a case back in South Korea in 2010 when the rise of one-brand shops and health and beauty stores drove a massive trade down in the whole overall category, bringing multi years of cosmetic spending declines despite the very stable income growth during that time.

Secondly, it's very early but I think the companies need to start thinking about increasing ESG awareness, including the environmental impact and issues like animal testing, for instance. So for example, Shanghai Jahwa, they were the first to actually issue an ESG report this February, first among the Chinese listed cosmetic companies. And we also expect a lot of the other companies to follow suit, given the increasing awareness for some of these ESG issues.

Liz Bowyer: Thanks, Christine.

Christine Cho: Thank you.