Building brands in China

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Chinese shoppers love brands but don't purchase them consistently. Market research shows the way forward.

Serving the new Chinese consumer

An epic battle is under way for the hearts and minds of China's consumers, residing as they do in the world's fastest-growing market. Companies commit vast resources to build brands, with few assurances. And as some Chinese become sophisticated shoppers, tens of millions of less experienced but no less avid consumers are joining the fray every year. A sharper understanding of the differing needs and diversity of the Chinese consumer can give foreign and domestic companies an edge in building strong, profitable brands.

Over the past decade, retail purchasing has grown by about 13 percent a year. The rush to stake a claim has led to a proliferation of brands from new entrants and established players alike: a typical hypermarket in China may offer around 40 brands of shampoo and conditioner (compared with 15 in the United States) and more than 20 different toothpastes (compared with 9). The available selection of big-ticket products is also rapidly expanding. In 2000, there were 9 automotive brands on the Chinese market and by 2005 there were more than 40; during the same period, the number in the United States remained steady at about 45 to 50.

Meanwhile, marketing expenses have soared, as brands compete for exposure in this crowded market. From 2002 to 2004, advertising spending increased by 50 percent a year, on average, across all consumer product categories in China. Rapid growth seems set to continue in most of them.

The appeal of China to marketers is clear. The country offers a giant pool of first-generation consumers, a clean slate on which to etch brand images. So far, no true power brands—those with high customer loyalty, such as Coca-Cola in the United States or Mercedes-Benz in Germany—have emerged. The situation is much like the United States in the early 20th century, when more than 100 automobile brands vied for attention, for example. Only a few emerged as winners.

McKinsey is compiling and analyzing data from the market to understand what drives the behavior of Chinese consumers and how they compare with shoppers in other countries. Last year we interviewed about 6,000 people in 30 cities, from sprawling Shanghai to semirural towns and cities, covering all income levels except the poorest households. The breadth of cities and consumer segments represented in the survey accounts for about 90 percent of the country's gross domestic product, 80 percent of its disposable income, and 60 percent of its population. In addition, to gather comparable data from developed countries, we conducted an online survey of consumer attitudes in the United Kingdom and the United States, representing a full range of ages, incomes, and regions.

Our findings demonstrated that the Chinese infatuation with brands does not generate the loyalty companies enjoy in developed markets. Although consumers may show a strong preference for certain brands, companies have generally been unable to translate such responses into increased market share or to extract a price premium. Going a step deeper, in our consumer interviews we explored the motivations behind this behavior; we observed, for example, that many Chinese consumers are highly value conscious and continually interested in trying new offerings.

Complementing our efforts on the ground, the McKinsey Global Institute (MGI) has taken a broader approach, examining the likely growth of China's urban consumer classes over the next two decades. Their model suggests the rapid growth of a well-off middle class, as the migration to the cities continues and incomes rise across the board. Companies fixated on serving the wealthiest urbanites will miss the emergence of an overwhelming upper middle class of 520 million shoppers, with spending power that will dwarf all other segments.

We describe and analyze our findings from these research efforts in the article that follows along with the other articles in this package, including "Marketing to China's hinterland," "Understanding China's teen consumers," and "The value of China's emerging middle class." In addition, we present the views of Jean-Luc Chéreau, president of Carrefour China, and Steve Gilman, Asia CEO of the home-improvement chain B&Q. These veterans of retailing in China discuss how they have approached Chinese consumers, adapted to the market, and grown.

The streets of China's cities are alight with neon touting brand names from all over the world. Consumers eagerly trawl these markets, picking up Nike shoes, Samsung mobile phones, Haier home appliances, and many other top-label products. Our research shows that the Chinese consumer is enamored of brands. In categories such as consumer electronics and food and beverages, more than 80 percent of the respondents to a survey1 said that they buy name brands at least occasionally. What's more, 69 percent would buy more branded gear if they had enough money, as compared with about 57 percent in the United Kingdom and the United States.

For marketers, the problem is that despite this infatuation with brands, Chinese consumers don't consistently buy the same ones or even those they prefer. Price differences and point-of-sale marketing vehicles can change a consumer's behavior in a heartbeat. Asked to choose among three leading television brands—two foreign and one domestic—49 percent of the survey respondents said they would pick Sony if prices were similar. But our analysis shows that a Sony premium of just 10 percent over the price of a TV from Changhong (a leading domestic brand) could make about a third of the people who say they prefer Sony choose its Chinese rival instead. In developed markets, companies that enjoy the level of brand preference that Sony TVs garner in China can routinely charge price premiums of up to 40 percent. And consumer electronics had some of the highest brand preference and loyalty scores among all the categories in our Chinese survey.

Chinese consumers often change their minds at the last minute, responding to in-store promotions or a salesperson's suggestion. Of our respondents, 65 percent said that they often leave a store with a different brand than the one they intended to purchase. Just as many said they almost always buy what's on sale, even if it's not their favorite brand.

Such attitudes toward price and in-store promotions create a transactional relationship between consumers and brands. No matter what brand preferences a consumer takes into a store, there's no certainty about which brand will actually get the nod. The result is a roller-coaster ride: market share in China can rise abruptly and then plummet. In 2002, for example, Motorola and Nokia commanded about 40 percent of the Chinese market for mobile-phone handsets. By 2003, despite a very strong reputation among consumers, their combined share had dropped to less than 30 percent as buyers switched to cheaper domestic brands. By 2005 Motorola and Nokia had regained market leadership. Several factors influenced the shift, but the speed of the change is a clear sign of the fickle attitudes of China's consumers and the difficulty of turning preferences into revenues.

Brand loyalty, it seems, is not only generally low but also varies considerably from one product category to the next in ways that could surprise companies accustomed to developed markets. Loyalty scores in China, for example, are about 50 percent higher for consumer electronics than for fast-moving consumer goods such as soft drinks and personal-care items. US consumers, by contrast, are much more loyal to sodas and other everyday purchases than to consumer electronics. One reason for the difference is that the price of a television, say, represents a greater share of a family's income in China than in the United States. Lower-priced products give the Chinese room to sample a broader selection of newly available offerings, and the wide range of products encourages experimentation rather than loyalty, while in developed markets the novelty has worn off and consumers have already settled on their favorites.

Given the flexible attitude of many Chinese consumers, how should marketers build their brands? Our research revealed the potential of point-of-sale marketing techniques. We also found that many consumers respond to appeals that highlight functional attributes (such as performance features) for some products and to nationalistic appeals for others. Knowing which button to push, and when, could encourage greater brand loyalty.

The importance of point-of-sale marketing

Advertising revenues at CCTV, China's national television network, more than doubled from 2000 to 2005, jumping to 12.4 billion renminbi, from 5.29 billion. The problem is that many Chinese consumers are tuning out this bombardment of marketing messages and now resist them even more fiercely than people in Western markets do. To give one example, in 2004 Chinese television viewers left the room or changed channels 72 percent of the time when ads were aired—more than viewers in other major countries—compared with 42 percent in 1999.2

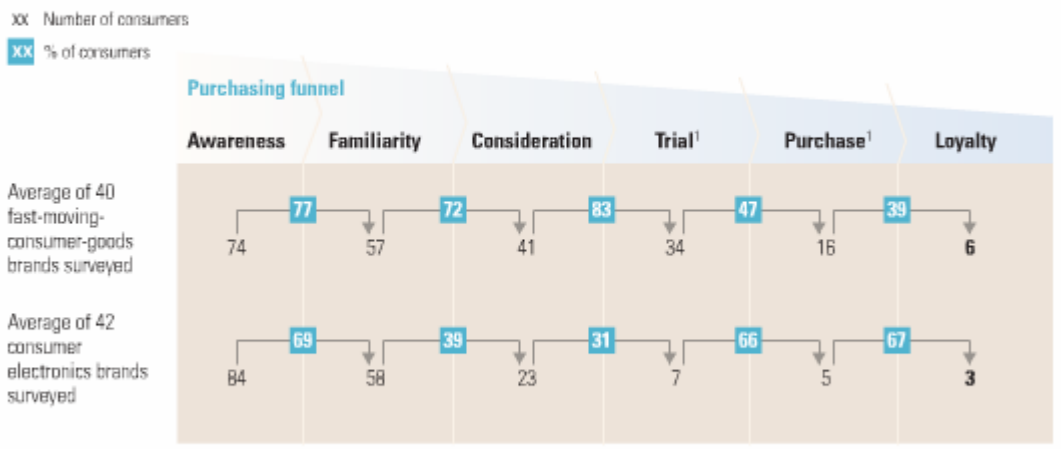
Companies must advertise in the mass media, but they can do more. Our research shows that many Chinese consumers make up their minds just before they get to the cashier and can be swayed at the last moment. While there is substantial variance by product category, in general companies should consider rebalancing their approach to marketing, with a greater emphasis on below-the-line approaches, such as price promotions and in-store demonstrations, than they might have in developed markets.

We looked at 40 domestic and foreign brands in fast-moving consumer goods such as soda, diapers, and toothpaste. On average, only about one in three consumers who considered buying a brand currently uses it. The falloff was even steeper in the consumer electronics category: on average, fewer than one in four consumers who considered purchasing a brand actually owns it (exhibit). In both cases, the current use rate was much lower than companies have come to expect in developed markets. High prices cause some of this leakage, but our study shows that last-minute switching explains much of it. Even if consumers consider themselves loyal to a brand, salespeople can get them to put a different one into their shopping baskets up to half of the time. In some cases, we have seen the influence of salespeople outweigh advice from medical professionals.

EXHIBIT 1

Relatively few people progress to the purchasing stage

Chinese consumers who moved to next stage of purchasing



[1]Trial = consumer purchased product once but does not continue to use; purchase = consumer continues to purchase, use product.

Source: Sept 2005 McKinsey interviews with ~6,000 individuals in Chinese households

Companies must get their retail execution right to improve their point-of-sale performance: well-trained and disciplined salespeople must go into stores and make sure that the retailers

understand the product, that it is getting the promised shelf space, and even that the packages on display have been dusted. In developed markets companies can rely on their distributors to do this sort of work, but in China distributors generally don't yet have the skills or influence needed for it. As a result, piled-up boxes may hide modern display racks, and layers of grime may obscure the brightest packaging.

Although in-store activities are common (and of growing importance) in developed markets, they are generally focused on a narrow range of new or improved products. In China, low labor costs allow companies to stretch their point-of-sale efforts across a broader range of products. Promotional staff in selected stores can literally put a product into the hands of consumers and explain its benefits.

The importance of function

A lot of Chinese consumers attach importance to functional attributes in many product categories. In our survey 83 percent of the respondents liked name-brand clothes because they perceived the quality to be better; by contrast only 65 percent said that branded clothes made them feel better. The gap is larger than would be expected in developed markets, where the range of functional differences among brands has shrunk over the past two decades for many categories3 and consumers are more likely to be hooked by emotional imagery such as sophistication, coolness, or just "feeling good." Why the difference? Perhaps because many products that are common in developed markets are only now being introduced to China, where consumers are still learning their value.

Many products common in the developed world are only now being sold in China, where consumers are still learning their value

Johnson & Johnson, for instance, focuses heavily on the functional benefits of its o.b. brand of tampons—using techniques such as advertisements that feature a prominent doctor explaining at length how, when, and why to use the product. Tampons (along with shampoo and cosmetics, among other products) were not available to most Chinese until the 1980s. But the rules can change quickly. In hair care products P&G is shifting its marketing for Head & Shoulders shampoo, especially in the bigger cities, from fighting dandruff to "new life for hair."

As China's consumer markets mature and the differences in quality among brands become less perceptible, emotional appeals will probably increase in importance. But the pace and extent of the change will vary widely among product categories and consumer segments. Companies will need high-quality consumer research to detect such trends.

A nationalistic streak

China is bursting with national pride, which is reflected in consumer attitudes toward domestic brands. In our survey 86 percent of the respondents claim to trust them, compared with 53 percent who trust foreign ones.4 In some categories the preference for Chinese brands is much stronger: 87 percent, for example, say that they trust local brands for food, as against 20 percent who trust foreign brands. Although all age groups express greater trust in Chinese brands than in foreign ones, younger adults trust the former relatively less and the latter relatively more—perhaps because they are more exposed to categories such as mobile phones, where foreign companies have a stronger presence. (Teens show the greatest trust for domestic brands, possibly because China's fortunes have risen rapidly during their lifetimes. See "Understanding China's teen consumers.") Global companies must understand these tendencies and tailor their brands to targeted segments or risk appearing too foreign.

Multinationals have boosted their local credentials through package and product redesigns—for instance, by offering red-bean ice cream and prawn-flavored potato chips or getting endorsements from Chinese sports heroes, such as basketball star Yao Ming and Olympic medalist Liu Xiang. Domestic companies cater to national pride by emphasizing their emergence on the global stage: for example, the Chinese computer maker Lenovo, for its Chinese-language home page, selected a world map with pictures of its PC towering over landmarks including the Statue of Liberty, the Eiffel Tower, and the Sydney Opera House. The slogan "In step with global technology" accompanies the image.

The Chinese market is a moving target, and continued change is the only thing a company can count on when planning its brand strategy. Some consumer segments will mature rapidly, especially in the biggest cities, and shoppers could quickly become loyal to specific brands. But as income levels rise across China, a continuing influx of new consumers will be first-time buyers of many products and eager to try new brands.

Meanwhile, new competitors—both multinational and domestic—will be entering the market. Only a few brands in each category will succeed in commanding premiums, which (at least for the next few years) will seem razor thin as compared with those in other markets, though volumes can be immense. Channels will also proliferate as modern retail formats spread further from the big cities and Chinese buyers become accustomed to catalog and online shopping and to direct sales.

To foster the distinct brand image and consumer loyalty that can generate higher sales and profits in the face of such fluidity, companies must continually reassess their targeted segments and marketing strategy and then focus on the factors that drive purchasing decisions. It's a tough job, but also a unique opportunity to develop and shape brands for an enormous market.

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