Exploring the Chinese Personal Care Market

Day 2
Today’s Presentation

- What is the current landscape of the Chinese personal care industry?
- What trends are occurring within personal care products?
- Which ingredients are key in China?
- Where are the opportunities for ingredient suppliers in China?
Kline & Company is a leading management consulting and market research firm, active within chemicals and related industries.
Today’s Presentation

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The 2008-2009 had limited impact on the global personal care market, with China’s retail market developing rapidly.

Retail Sales, 2004 - 2010

- China, CAGR: 10.0%
- Rest of World, CAGR: 4.3%
Europe remains the largest region, but is losing share to developing markets, in particular China and Brazil

Manufacturers Sales, 2005 - 2010

Regional Growth 2010 - 2015

- India
- China: > 7%
- Latin America
- C&E Europe: 4-5%
- Middle East & Africa
- North America
- Japan: < 2%
- Western Europe
Skin care is the largest and fastest growing product class globally.
Manufacturers’ sales of cosmetics and toiletries in China were $18.1 billion in 2010, an increase of 9.6% from $16.5 billion in 2009.
Today’s Presentation

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- Which ingredients are key in China?
- Where are the opportunities for ingredient suppliers in China?
Highlights: *Skin Care in China*

- Skin care accounts for about 37% of the personal care market in China growing at 10.2%
- Market developments include:
  - Consumers preference for multifunctional products
  - Increasing male awareness of using skin care products on a daily basis
  - Developing market for baby skin care products which is growing rapidly
  - Development of the sunscreen and whitening products segment
  - Anti-aging and whitening properties products are moving from the facial treatment category into other areas such as hand and body products.
  - Organic, natural, or products containing Chinese herbal medicine are becoming popular as they are believed to be safer
Highlights: Hair Care in China

- Hair care accounts for about 27% of the personal care market in China growing at 8.8%
- Market developments include:
  - Reduction in margins due to over-supply of hair care products
  - Limited difference between the brands which leads to consumer promiscuity
  - Increased consumer experimentation based on increased purchase power and fashion trends
  - Consumers prefer products that have a good efficacy and are gentle to the hair, such as products based on Chinese herbs and medicines
  - Developing popularity of multifunctional products
  - Perming remains fashionable, while straightening is typically done at home using mass market products.
Highlights: *Color Cosmetics in China*

- Color cosmetics accounts for about 12% of the personal care market in China growing at 13.9%
- Market developments include:
  - Increase in woman’s awareness and understanding regarding using color cosmetics
  - Increasing foreign brands entering the Chinese color cosmetics market, mainly focused on high-end products
  - Consumers opting for products with additional skin care effect, such as lipstick with nutritious effect, foundation cream with purifying and oil-control effect
  - Consumers are also increasingly attentive of health issue and prefer natural or less harmful products in China
Highlights: Oral Care in China

- Oral care accounts for about 14% of the personal care market in China growing at 6%
- Market developments include:
  - Toothpaste and toothbrushes are the main products sold in the Chinese oral care market, accounting for about 97% of sales
  - Development of specific categories for example baby toothpaste, toothpaste for whitening, etc
  - Toothpaste with multifunctional effects is increasingly popular
  - Natural products hold a solid share in the market
  - Toothpaste with Chinese herbal medicine is an advantage for Chinese local brands
Services are becoming increasingly important in China

- **Professional Skin Care**
  - The professional skin care market in China reached CNY 8.3 billion (USD 1,228 million) in 2010, up 10.6% from 2009
  - The number of beauty institutes in China increased in 2010 as the spa industry recovered from a resurgence in the economy
  - Chinese traditional medical services have become popular in the Chinese professional skin care market, especially with beauty institutes carrying local brands.
Services are becoming increasingly important in China

- **Salon Hair Care**
  - The professional hair care market in China reached CNY 4.4 billion (USD 650 million) in 2010, up 6.7% from 2009
  - The margin on skin care services is higher than hair care services, which has led to an increase in the number of hair salons within beauty institutes
  - Local brands for salon hair care products are growing slower than foreign brands due to their lack of innovation and recognition
What are the challenges for the Chinese personal care market?

- Chinese personal care market is oversupplied and the competition is fierce

- International brands occupy the leading position in the high-end personal care market. Demand for high-end products will continue to grow due to increased availability

- Despite consumers desire for natural products based on Chinese herbs and medicines, price is still a major factor in the decision making process

- Most Chinese consumers prefer value-added/multi-functional products

- The demand for sunscreen and whitening products grows faster than anti-aging products or skin moisturizers products these years

- International brands have greater market share in Tier I cities, such as Shanghai, Beijing, with most local brands focusing on Tier II and Tier III cities
Over the next decade, two types of economies will drive China’s growth – the richer coastal provinces will resemble developed economies; and inland provinces will repeat the growth miracle.

B to B: production base relocation
- Inland cities will become increasingly popular as production bases
  - Intel relocated production base to Chengdu, Sichuan
  - Unilever moved its production to Hefei, Anhui

B to C: new consumption engine
- Growing disposal incomes in inland areas, as a result of government efforts to bridge regional gaps
- Massive middle-class has started to emerge in China’s inland area

Map showing coastal and inland areas, preferred production locations, and newly developed production bases.
Further, the market is very complicated with economic development clusters and city tiers, and different consumer behavior across regions.

<table>
<thead>
<tr>
<th>Tier 3</th>
<th>Tier 2</th>
<th>Tier 1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Higher presence of domestic players, two types:</td>
<td>Behaves more like developed market</td>
<td></td>
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<tr>
<td>- Well recognized national brands</td>
<td></td>
<td></td>
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<tr>
<td>- Well established regional brands targeting regional markets</td>
<td></td>
<td></td>
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<tr>
<td>Basic products may still suffice</td>
<td></td>
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<tr>
<td>Brand is important</td>
<td></td>
<td></td>
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<tr>
<td>Purchasing decision is more likely influenced by marketers</td>
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<tr>
<td>Still behaves like developing market</td>
<td></td>
<td>More consolidated – higher market share from MNCs</td>
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<tr>
<td></td>
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<td>Brand is important but value takes higher priority</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Purchasing decision comes more from sophisticated research and comparing product nuances</td>
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</tbody>
</table>

Catching up fast …
Today’s Presentation

- What is the current landscape of the Chinese personal care industry?
- What trends are occurring within personal care products?
- Which ingredients are key in China?
- Where are the opportunities for ingredient suppliers in China?
Ingredients being used within personal care play a variety of roles within a formulation

<table>
<thead>
<tr>
<th>Product Category</th>
<th>Product Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>Antimicrobials</td>
<td>Parabens, Imidazolidinyl urea, Quaternium 15, Phenoxyethanol</td>
</tr>
<tr>
<td>Conditioning polymers</td>
<td>Cationic Guar, Polyquaterniums, Proteins, Silicones</td>
</tr>
<tr>
<td>Emollients</td>
<td>Emollient esters, Natural oils</td>
</tr>
<tr>
<td>Hair fixative/styling polymers</td>
<td>Amphomer Fixative Polymers, Resyn Fixative Polymers, VP/VA Copolymer, PVP Styling and Fixative Polymers</td>
</tr>
<tr>
<td>Rheology control agents</td>
<td>Hydroxypropylmethyl cellulose, Carboxymethyl cellulose, Glucose derivatives</td>
</tr>
<tr>
<td>Surfactants</td>
<td>Acyl isethionates, Ether carboxylates, Sulfosuccinates, Alkyl polyglucosides</td>
</tr>
<tr>
<td>UV absorbers</td>
<td>Octyl methoxycinnamate, Benzophenone-3, Avobenzone</td>
</tr>
</tbody>
</table>
China has increased its share in the global ingredients market in the last 5 years.
What is driving growth of personal care in China?

- Personal care benefits from strong market drivers including:
  - Growth in population and standard of living
  - Growth in specific product categories such as lipstick, face cream and body washes
  - Strong presence of international brands
  - Developing desire for multifunctional products

### Per Capita Spend, China versus India (USD, 2010)

<table>
<thead>
<tr>
<th>Category</th>
<th>China</th>
<th>India</th>
</tr>
</thead>
<tbody>
<tr>
<td>Skin Care</td>
<td>0.6</td>
<td>0.8</td>
</tr>
<tr>
<td>Oral Care</td>
<td>0.8</td>
<td>1.7</td>
</tr>
<tr>
<td>Colour Cosmetics</td>
<td>1.3</td>
<td>0.2</td>
</tr>
<tr>
<td>Hair Care</td>
<td>1.7</td>
<td>1.3</td>
</tr>
<tr>
<td>Deodorants</td>
<td>2.6</td>
<td>0.0</td>
</tr>
<tr>
<td>Bath &amp; Shower Products</td>
<td>1.4</td>
<td>1.6</td>
</tr>
</tbody>
</table>
Volume CAGR in China is 9.6% (2010-2014), key markets such as emollients and conditioning polymers underpin this growth.
Supply of personal care ingredients in China is highly fragmented with a large number of domestic and multinational players.

- Acquisitions that are reshaping the supply of personal care ingredients:
  - AkzoNobel acquiring Boxing Chemicals in Shandong (completion Q4 2011)
  - Rhodia acquired Suzhou Hipro in Zhangjiagang region (Q1 2011)
  - Rhodia acquired Feixiang Chemicals in Zhangjiagang region (Q4 2010)
  - Merck acquired Suzhou Taizhou Technology Development in Shanghai area (Q4 2009)
Western companies are moving in via acquisition or joint venture

Rhodia’s Acquisition of Feixiang Chemicals, 2010

- Established a footprint in China by acquiring China’s leading manufacturer of specialty amines and surfactants; Feixiang was also a top-three player in specialty amines globally
  - Amphoteric and cationic surfactant expertise
  - Realized strong top-line growth of 20%/year prior to acquisition
- Leveraging Feixiang to build a leadership position in specialty surfactants in Asia
- Targeting growth through combining Feixiang’s technologies and products with Rhodia’s market application expertise and global presence
- Committed to double the size of the acquired business in five years and develop a global amines business from its base in China

<table>
<thead>
<tr>
<th>Financial highlight</th>
<th>US$ Million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Enterprise Value</td>
<td>489</td>
</tr>
<tr>
<td>EBITDA</td>
<td>54</td>
</tr>
<tr>
<td>2010 EBITDA multiple</td>
<td>9</td>
</tr>
<tr>
<td>Capital source</td>
<td>100% cash</td>
</tr>
</tbody>
</table>

Source: Rhodia.
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Personal care is benefiting from development of the naturals segment not only in Asia, but in all regions.

Manufacturer Sales of Natural Personal Care, 2005-2010

* - Includes truly natural and natural inspired
Natural personal care sales in Asia are over USD 8.5 billion in 2010

- CAGR is about 14% since 2005

- The strong GDP growth in many economies in Asia and consumers' preference for herbal-based beauty products are the two major factors responsible for the consistent double-digit growth in the segment since 2003

- Key manufacturers in the naturals market include: DHC, Sulwasoo, Dabur, The Face Shop, etc

Personal care ingredient suppliers are taking advantage of the naturals trend with investments in China

- Opened in 2010 a new state-of-the-art production facility for alkyl polyglucoside (APG®) surfactants at its site in Jinshan, China.
Other ingredient classes are also benefiting from the naturals trend, although performance is hindering uptake.

Personal Care Ingredients by Type and % Naturally Derived

<table>
<thead>
<tr>
<th>Ingredient Class</th>
<th>% Naturally Derived</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hair fixative polymers</td>
<td>Below 10%</td>
</tr>
<tr>
<td>Specialty surfactants</td>
<td>Below 10%</td>
</tr>
<tr>
<td>Specialty emollients</td>
<td>50%</td>
</tr>
<tr>
<td>Conditioning Polymers</td>
<td>80%</td>
</tr>
<tr>
<td>Specialty Actives</td>
<td>100%</td>
</tr>
</tbody>
</table>

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So what are specialty actives? Demand for active ingredients is high in developing markets, as consumers increasingly try to combat signs of ageing.

<table>
<thead>
<tr>
<th>Active Ingredients</th>
<th>Vitamins</th>
<th>Botanicals</th>
<th>Biotechnology Products</th>
<th>Marine Ingredients</th>
<th>Proteins &amp; Peptides</th>
<th>Enzymes &amp; Coenzymes</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>• Synthetic/Nature Identical • Natural</td>
<td>• Extracts • Purified Molecules</td>
<td>• Extracts • Purified Molecules</td>
<td>• Algae Extracts • Purified Molecules</td>
<td>• Botanical • Biological</td>
<td>• Synthetic • Non-Synthetic</td>
</tr>
</tbody>
</table>
Innovation in personal care will continue to come from a variety of sources

- Food
  - Vitamins, antioxidants, actives
- Delivery systems
  - Nanoparticles, molecular films
- Chemical/polymer science
  - Fixative polymers, delivery systems
- Drug development
  - Synthetic peptides and other actives
- Wound care
  - Biopolymers, scaffolds
- Chemical Engineering
  - Molecular coupling, chemical hybrids
- Extraction techniques
  - Botanical actives
Today’s Presentation

Thank you for attending today’s presentation
This database includes eight product groups, and provides quantitative data including:

- Consumption of key personal care ingredients by application
- Supplier sales by ingredient type
- Average market pricing of ingredient
- Forecast consumption of ingredient within a five-year timeframe (2011 to 2016)

Regional Coverage:
Europe, USA, Japan, China, India, SE Asia, Brazil
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