

Etsior Monthly Opinion 15 July 2010 China growth benefits consumer sector (*)

One question that came up at the time of the 2008-2009 financial crisis and of the global slowdown of the economy was if China, with its large population and 10%+ growth rate, could compensate for the consumption decrease observed everywhere else. The answer was that of course China had a growing share of its population benefitting from reasonable buying power, but that this had not yet spread to all.

So what are the perspectives for consumer oriented companies now benefitting from the overall growth of the Chinese economy and of the creeping reevaluation of the Yuan?

The first factor is that it looks like the Chinese government wants to *rebalance the economy in favor of the private consumption* and in disfavor of investment. Exports should recover after a difficult (-3.9%) 2009. Other factors are also very important such as:

- **Urbanization:** the urban population is expected to grow at a 2% rate, adding up about 20M people each year. This is a major factor for consumer spending growth which triggers changes in consumption habits.
- **Middle class:** a growing number of people are reaching the middle class category. An estimated 40M people is adding to this group every year, and they are the most avid consumers, not hesitating to spend more for brands and good quality products. The middle class annual disposable income is in the 10 to 15k\$ range.
- The **young generation** (single child) is using internet and is buying more and more on line.

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Our selection is always put in the macro-economical perspective to exploit the short to medium term market trends.

Brands appeal a lot to this generation and brand status is very important, when brand loyalty is quite low.

- Marketing costs are high and advertising expenses also. The overall size of packaged consumer goods is over € 100B in China. This is a very fragmented market, the Food sector being the most fragmented one, especially outside of the main very competitive cities (Beijing, Shanghai). More opportunities arise in tier 2 and 3 cities.

Who are those global companies that could benefit the most from these trends?

First say is that China represents the largest consumer group (CG) market in the world with its 1.3 b population. Though China is really on the growth, one should not forget that more or less its GDP is at the level of the German one, of course with a 10%+ annual growth.

Global CG companies really get 2 to 6% of their sales from China, which represents a huge potential.

Among the best positioned global CG companies, **L'Oreal** is quite interesting in the fastest growing markets with its leading market share (m.s): Skin care (16% m.s), Color cosmetics (33% m.s) and derives 4.7% of its global sales from China.

Unilever, deriving 3.5% of its sales from China is also well positioned with strong positions in Laundry Hair and Soups.

Other companies like **Beiersdorf** (5.7% of global sales) and **P&G** (6.2% of global sales) will also benefit from a strong position and growth in China.

We care for you!

(*) Source: JP Morgan Cazenove –Views from China – 15 June 2010

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