

Chinese consumers: Revisiting our predictions

As their incomes rise, Chinese consumers are trading up and going beyond necessities.

by Yuval Atsmon and Max Magni

In 2011, we tried our hand at predicting the ways in which, in the decade to come, Chinese consumers would change their preferences and behaviors.¹ This article takes stock of those predictions.

Why check in now? One reason is we're about halfway to 2020. Another is a comprehensive new McKinsey survey,² which follows nearly ten years of previous research that includes interviews with more than 60,000 people in upward of 60 cities in China. Along the way, we've bolstered our own team's data on consumer preferences and behavior with a number of complementary analyses and models, including McKinsey's macroeconomic and demographic studies of Chinese urbanization and income development. We've also interviewed academics to draw out the major trends shaping the course of the Chinese economy, such as its rapidly aging population, the growing independence of women in society, and the postponement of critical life milestones, such as marrying and having children.

¹ See Yuval Atsmon and Max Magni, "Meet the Chinese consumer of 2020," *McKinsey Quarterly*, March 2012, McKinsey.com.

² See "Here comes the modern Chinese consumer," March 2016, McKinsey.com.

We've done it all with the abiding belief that companies getting ahead of the trends can build their brands and offerings to fit a rapidly evolving set of consumer needs in China. Deeper and more nuanced understanding of Chinese consumers can help reveal fresh opportunities—for new entrants and incumbents alike—and signal those areas where established players may need to be more wary.

Looking back nearly five years on, it is plain that Chinese consumers are evolving along many, though not all, of the lines we'd predicted. While geographic differences persist, Chinese consumers are, on the whole, more individualistic, more willing to pay for nonnecessities and discretionary items, more brand loyal, and more willing to trade up to more expensive purchases—even as their hallmark pragmatism endures.

EVOLVING GEOGRAPHIC DIFFERENCES

Much of the research we described five years ago highlighted the vast differences we found among consumers in China's various cities and regions. Just as it was then, generalizing about Chinese consumers continues to be almost as difficult (and maybe as foolish) as it is to generalize about European consumers.

We predicted these differences would remain—and even grow more significant, especially in the consumption patterns and tastes that relate to discretionary items. To help companies better tailor their go-to-market approach, we grouped most cities in China into clusters based on their similarities, including their geographic proximity and the transportation infrastructure that connects them.

As the economic structure in each of the 22 biggest city clusters has evolved—and as each of them has been affected differently by the recent slowdown of China's economy—significant differences, for instance, in consumer confidence, do indeed persist between these clusters.

For instance, some 70 percent of consumers in the Fuzhou–Xiamen city cluster, which lies on the coast across from Taiwan, said in our latest report that they are confident their income will significantly increase over the next five years. In that same report, the Byland–Shandong city cluster, which lies on the coast between Beijing and Shanghai, was comparatively pessimistic, with only 33 percent of its consumers expressing such confidence.

Furthermore, when our latest survey compared the consumers in the Shanghai area to those around Beijing and Hangzhou, certain spending attitudes also showed marked differences. For example, brand loyalty increased much faster in Shanghai (24 percent increase in three years versus just 7 percent in Beijing and 9 percent in Hangzhou), as did the willingness to pay for better or healthier products.

GROWING DISCRETIONARY SPENDING

Despite geographic differences, there are broad similarities among Chinese consumers. These mirror the general trends economists have found among consumers around the world as economies develop. The general tendency is for consumers, as they earn more, to spend a lower percentage of their income on food, a little more on healthcare, and even more on travel and transportation, as well as on recreational activities. It was no great stretch then, in our report five years ago, to predict a significant shift in consumption from necessities and seminecessities into discretionary categories.

Sure enough, our new survey shows Chinese consumers following the anticipated pattern. When we asked how they plan to increase spending as their income increases, dramatically fewer consumers said they will increase it on food (46 percent in the latest survey, compared to the 76 percent who said they would do so three years earlier).

Responses trended slightly up for healthcare products (from 16 percent to 17 percent), and increased for travel (from 14 percent to 23 percent) and leisure (from 17 percent to 25 percent).

ASPIRATIONAL TRADING UP

In our previous predictions, we also argued that as the income of Chinese consumers grew, they would aspire to improve their quality of life by not only spending more on discretionary items, but also by shifting their spending to more expensive items in the same categories.

In necessity categories such as food, for example, we predicted consumers would be willing to spend more for healthier versions of the same products—for instance, that olive oil would grow much faster than less healthy (and less expensive) oils. In seminecessity categories like apparel, we predicted people would buy more special-occasion and premium brands. We anticipated that the strongest beneficiaries of these changes would be in the more discretionary and aspirational categories, such as skincare and automotive. So what has happened so far?

Premium categories have really accelerated. Comparing cosmetics purchases between 2011 and 2015, 44 percent of consumers have traded up their purchases, compared with 4 percent who traded down. Even for rice, 25 percent of consumers traded up versus 3 percent who traded down. Automotive was not included in our survey, but sales data from the Traffic Management Bureau of the Ministry of Public Security in China suggest significant trading up. In 2011, 51 percent of the renminbi spent on cars by Chinese consumers were for autos cheaper than 100,000 RMB. These sales accounted for only 43 percent of the market. Cars selling for 100,000 to 250,000 RMB grew twice as fast with a compound annual growth rate (CAGR) of 19 percent versus 9 percent. And cars with price tags between 250,000 and 400,000 RMB grew the fastest of all, with 23 percent CAGR.

EMERGING SENIOR MARKET

In 2011, we observed a big generational difference between consumers in their late 50s and early 60s, who were very conservative spenders, and all of the age cohorts younger than them.

We predicted that by 2020, as the needs of consumers over the age of 55 changed along with their economic confidence, their spending habits would follow suit, making this age group worth pursuing by consumer-product companies. If anything, we underestimated the speed and force with which this trend would unfold.

By 2015, the 55–65 age group had started to shift even faster than the rest of the population. For example, 52 percent of the people in this age group showed a preference for premium products, compared to just 32 percent in 2012. They leaped from being the most conservative age group to the one most likely to trade up. Similarly, the preference for famous brand names among these older buyers jumped by more than 20 percent, fully closing the previous difference among cohorts. As Exhibit 1 shows, these older consumers don't shy away from indulgences, and they have grown more likely to use the Internet to research their purchases, even if they still do so less often than younger consumers.

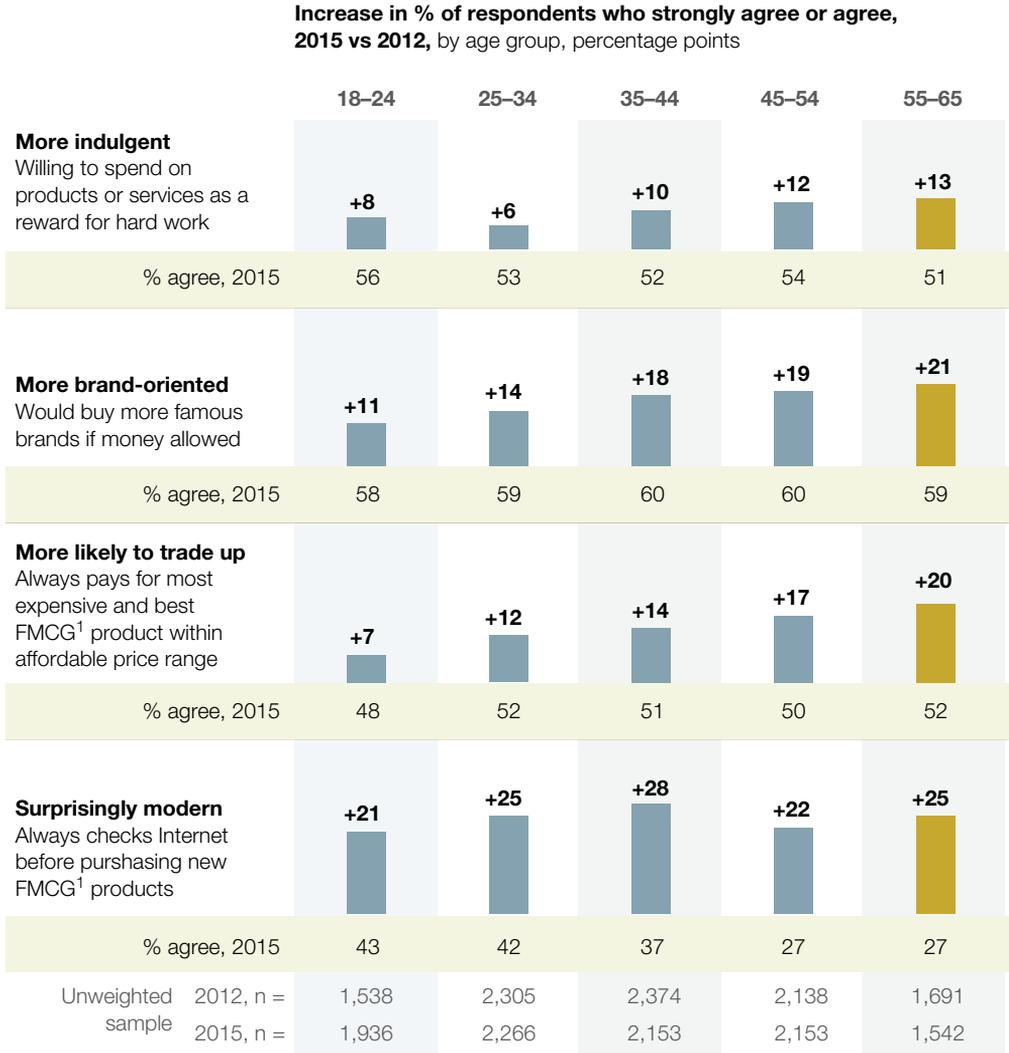
That said, the upper age group has remained more pragmatic and cost conscious than any other age group, as we discuss in the following section.

THE STILL-PRAGMATIC CONSUMER

Back in 2011, even as we were predicting changes in the behavior and preferences of Chinese consumers, we also saw ways in which their essential pragmatism would likely stay the same. For instance, we anticipated that

Exhibit 1

Chinese consumers in their late 50s and early 60s are shifting their buying behavior.



¹ Fast-moving consumer goods.

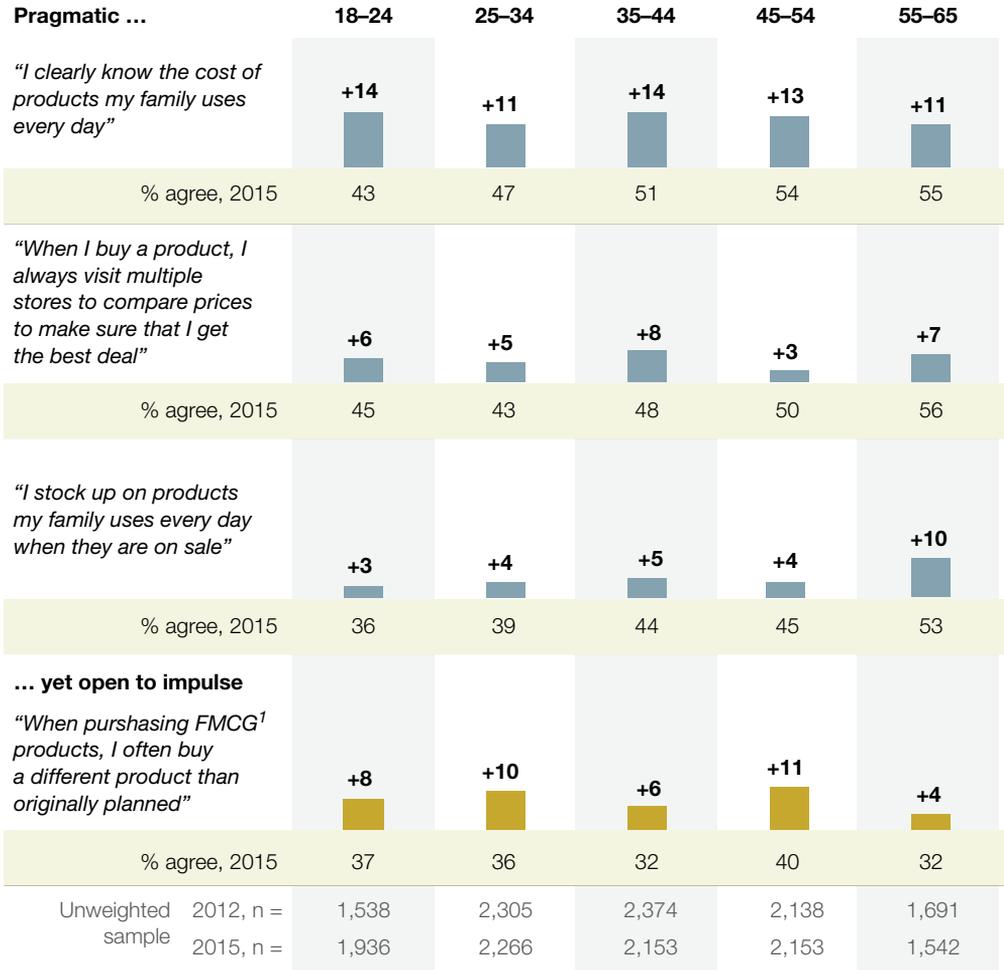
Source: McKinsey 2012 and 2015 China consumer surveys

impulse buying would remain lower than in other countries and that value for money would continue to be an important consideration when choosing products and services. Interestingly, Chinese consumers across all age groups have, in some ways, become even more pragmatic. They're now even more likely to compare prices across multiple stores, to be more price aware, and to stock up on promotions. That said, they're now willing to buy more often on impulse (Exhibit 2).

Exhibit 2

The pragmatism of Chinese consumers has increased slightly across all age groups.

Shift in % of respondents who strongly agree or agree, 2015 vs 2012, by age group, percentage points



¹ Fast-moving consumer goods.

Source: McKinsey 2012 and 2015 China consumer surveys

THE INDIVIDUAL CONSUMER

We also predicted that as Chinese consumers aspire to a better life and trade up their purchases, they would become more discerning and gradually more individualistic. This would lead, for example, to a shift toward more healthy choices, more user-friendly products, and products and brands that better fit their personality. This could be a big opportunity for niche brands—and a threat to the mass-market brands that had won big in previous years by using

scale and ubiquitous availability, supported by the trust gained by heavy advertising.

Our latest research certainly shows a decrease in consumption in categories deemed less healthy and a willingness to spend significantly more on health and more environmentally conscious categories. It also shows consumers are more likely to spend more to indulge themselves and more likely to try new technology. While their consumption choices have become more individualistic, though, it is important to note that family values continue to be at the top of their priorities (Exhibit 3).

One area our predictions missed, however, was by anticipating that consumers, as they became more individualistic in their choices, might focus less on basic product reliability and safety. Perhaps in part because of a number of more recent food scandals, however, consumers seemed more concerned with these issues in 2015 than they were before.

THE INCREASINGLY LOYAL CONSUMER

When our team first started researching Chinese consumers, nearly ten years ago, many of us were surprised by their fickle attitude toward brands. Fewer than half of consumers tended to stick with their favorite brands, compared, for example, with almost three quarters of US consumers.

As we debated this tendency while making our predictions, we wondered if, in the clash between pragmatism and individualism, brand loyalty would

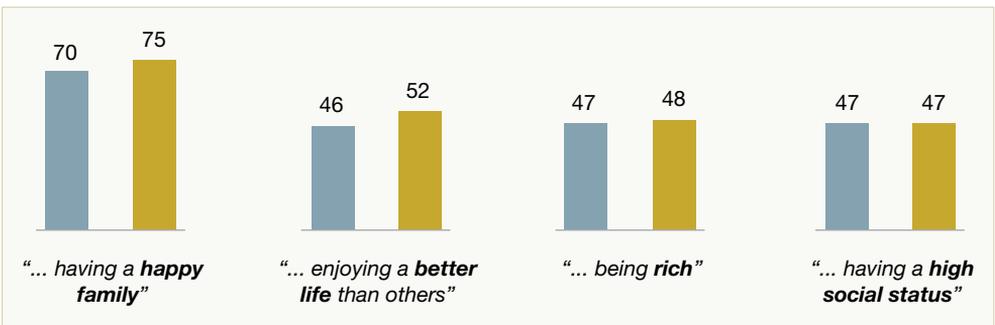
Exhibit 3

Chinese consumers' needs and values continue to center around family.

Being successful means ...

% of respondents who selected "strongly agree" or "agree"

■ 2012 ■ 2015



Source: 2012 and 2015 McKinsey surveys of Chinese consumers

stay low, increase, or even decline. Ultimately, we decided it would increase as the emotional benefits of brands became more important to consumers and as increased choice and availability of branded products (online and off) would allow consumers to optimize for price and convenience without changing choices too often.

Our recent research confirmed the changes we anticipated. Consumers are now significantly less likely to buy a brand that is not already among their favorites, continuing the upward trend we observed in 2011 (Exhibit 4).

THE MODERN SHOPPER

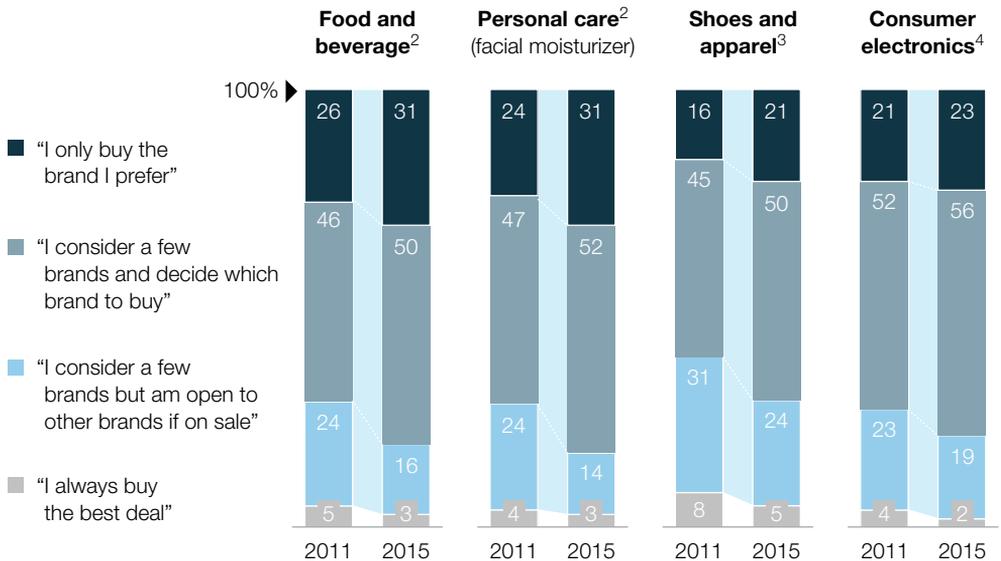
Our 2011 predictions were bullish on e-commerce, predicting that Chinese consumers would adapt their channel choices even faster than has occurred in developed markets.

Exhibit 4

Chinese consumers are increasingly brand loyal and focused on just a few brands.

Which statement best describes your shopping experience?

% of respondents¹



¹ Including common products such as beer and chocolate.

² Figures do not sum to 100%, because of rounding.

³ Including sports clothes and shoes, leisure wear, and women's shoes.

⁴ Including flat-panel televisions, laptops, and mobile handsets.

Source: McKinsey 2011 and 2015 China consumer surveys

We estimated that by 2020, online consumer-electronics purchases would jump to 40 percent, from about 10 percent. More mainstream categories would rise to 15 percent, and some categories, such as groceries (now below 1 percent), could reach about 10 percent. These changes are occurring even as the enduring pragmatism and diligence of the Chinese consumer continue to be in place. Our latest research shows that consumers of all age groups are much more likely to collect information online, even on fast-moving consumer goods, than they were just three years ago.

In 2015, online food and beverages sales (excluding fresh) reached 7.2 percent: reaching our predicted 10 percent in five years looks very likely. The online share of consumer-electronic purchases, meanwhile, has reached a whopping 39 percent in 2015, and it now looks possible that by 2020 it will be about 50 percent of overall sales.

Looking from today's perspective at our 2011 predictions, it is impressive to see the evolution of Chinese consumers—even as their most characteristic traits endure. Certainly, we'll check in on their progress as we get ever closer to the year 2020. Making predictions may be difficult, especially about the future—as US Baseball Hall of Famer Yogi Berra famously observed. But they can still provide valuable foresight for executives. 

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