

Deloitte.

Beauty Retail

A closer look at current trends impacting beauty specialist retailers



Contents

Introduction	04
Key insights	05
The beauty retailing ecosystem	06
Top 10 beauty specialist retailers	07
Top 10 health & beauty retailers	10
Market trends	14
By channel	15
By product	21
By regulation	25
Marketing trends	26
M&A trends	29
Consumer preferences	31
Key contacts	32

What trends do beauty specialist retailers currently face, and how well are retailers addressing them in order to be well-positioned for the future?

Beauty specialist retailers face a number of key trends that affect their businesses. Here, we address these trends from both a channel and a product perspective, and we identify where these retailers should focus in order to sustain their business models into the future.

We also look at marketing trends impacting beauty specialist retailers, examining them from a global perspective while assuming a regional view (Americas, EMEA, APAC).

While our focus is on beauty specialist retailers, we also consider to a limited extent other retail formats in the beauty retailing ecosystem, including health and beauty retailers (such as drugstores), department stores, and supermarkets.

We have also taken a look at the impacts of the COVID-19 pandemic on selected retailers, noticing an overall acceleration in their e-commerce activities. However, the mid- and long-term impacts in a post-pandemic world have yet to be seen.

Key insights

1. There is an increasing need for beauty specialist retailers to enhance their stores as well as their digital platforms and to seamlessly connect these channels to create an omni-channel presence.

Moving towards an omni-channel presence is critical for a beauty specialist retailer to successfully position itself.

a) Improvements in store concepts have the potential to retain customers' attention

In order to improve their store-based business, many retailers are modernising and refurbishing their brick-and-mortar stores. Beauty specialist retailers are also moving towards new store concepts that incorporate digital elements and try-on hotspots, to provide a contemporary shopping experience.

b) E- and mobile-commerce offer the opportunity to boost sales

Improving the e-commerce and mobile experience offers opportunities for beauty retailers, provided that the user experience is flawless across all channels (i.e., is easy to use, up-to-date, and informative). The primary way to achieve this is through the use of innovative technologies and tools, such as augmented reality and artificial intelligence. Consumers are demanding an increasing degree of customisation which is typically enabled through these technologies.

COVID-19 impact: In-store sales declined in 2020, as most beauty specialist retailers were forced to shut all stores temporarily. These players refocused their efforts towards enabling increased online sales. Therefore the pandemic accelerated the e-commerce expansion among beauty specialist retailers.

c) To achieve an omni-channel presence, it is vital to combine store-based concepts, e-commerce platforms, and the mobile presence, as well as social media efforts

Digital tools as a part of a modernised store concept connected to the mobile world and vice versa (i.e. try-on hotspots etc.). Beacons (Bluetooth-based hardware transmitters for interaction purposes) can provide a seamless shopping experience tailored to consumers' individual preferences. Influencers also play an increasingly important role in advertising products via social media channels, and they can combine the online with an in-store experience through such concepts as live influencer events at the store.

2. Beauty specialist retailers have to take into account the increasing consumer demand for products that are free of perceived dangerous ingredients and have not been animal-tested

Beauty specialist retailers can gain a competitive advantage if they understand prevailing product trends, including today's demand for natural, organic, cruelty-free, and vegan beauty products across a range of brands and price points. Retailers can meet these demands by partnering with both well-known brands and newcomers.

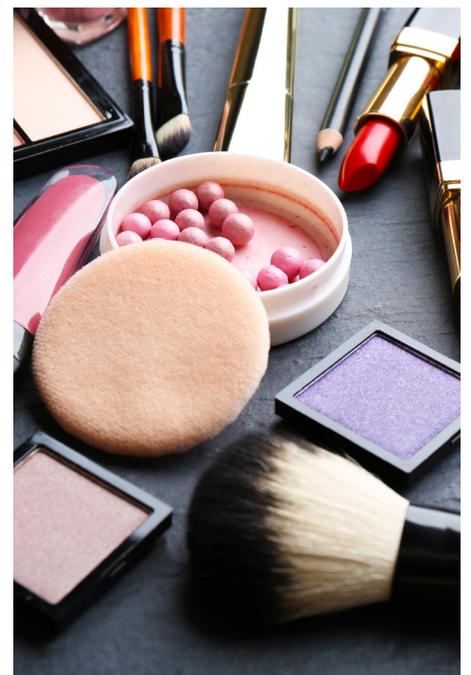
3. Beauty specialist retailers can successfully attract and retain consumers when they increase their use of digital tools in their marketing strategies

Beauty specialist retailers can increase attraction and retention of consumers when their marketing plans incorporate three main concepts: 1. Understanding the customer using data-driven marketing, 2.

using social media as a tool for optimising marketing promotions, and 3. optimising sales by applying advanced digital pricing tools and using omni-channel distribution.

4. Going forward, increased levels of M&A activity are likely with a focus on expansion in both local and new markets as well as enhancing technological capabilities

Due to the high level of fragmentation in the market, and against the background of moderate historical M&A activity, consolidation is imminent among market participants. This opens up opportunities for well-positioned players to explore local and new-market expansions through acquisitions. In addition, the increasing focus on an omni-channel approach will contribute to more technology-based acquisitions.



The beauty retailing ecosystem

Beauty specialist retailers as part of a wider beauty retailing ecosystem

This report discusses current trends impacting beauty specialist retailers (BSRs), such as Sephora and Douglas. BSRs are characterised by specific product offerings mainly consisting of cosmetics, skin care, and fragrances, positioned primarily in the premium and luxury price segments. The main BSR distribution channels are classical brick-and-mortar stores as well as an ever-increasing online presence. Players in this group do not manufacture but instead distribute products from third-party brands. Many BSRs offer their own branded products, at a price point below their main offerings.

BSRs are part of a wider beauty retailing ecosystem. To a limited extent, we will also take a look at health & beauty retailers (HBRs), and department stores and supermarkets (DSs). Other retailing formats such as direct distribution, cosmetic studios, and pure online retailers are not covered in this paper.

The beauty retailing ecosystem¹ – Beauty retailing groups discussed in this report



1. Not an exhaustive list.
Source: Euromonitor, Deloitte analysis

Top 10 beauty specialist retailers

Global top 10 beauty specialist retailers, FY18

Name	HQ	Regional presence	Stores (#)	Sales (\$m)	Sales per store (\$m)	Sales CAGR FY16-18	E-commerce sales share	E-commerce CAGR FY16-18	EBITDA margin
1. Sephora	FRA	Global	2,600	13,646	5.2	6.8%	6.7%	27.6%	n/a
2. Ulta Beauty	USA	Americas	1,174	6,717	5.7	17.6%	9.7%	47.6%	16.9%
3. Douglas	GER	EMEA	2,431	3,370	1.4	13.0%	14.8%	23.1%	7.1%
4. Sally Beauty	USA	Global	3,695	2,339	0.6	(1.1%)	2.2%	30.8%	15.0%
5. L'Étoile	RUS	EMEA	~1,000	1,316	c.1.3	10.3%		Not disclosed	
6. Sa Sa Intl.	HKG	APAC	265	1,023	3.9	2.6%	4.7%	(7.8%)	7.0%
7. Rive Gauche	RUS	EMEA	~200	572	c.2.9	11.8%		Not disclosed	
8. Mecca	AUS	APAC	~100	324	c.3.2	6.3%			7.0%
9. Ainz & Tulpe	JPN	APAC	54	220	4.1	7.0%	Not disclosed		4.1%
10. Space NK	GBR	EMEA	75	137	1.8	8.4%			10.6%

Beauty specialist retailers distribute beauty products mainly in skin care, cosmetics, hair care, body care, fragrances, and occasionally beauty nutrition and accessories. They typically sell products from various brands both through their brick-and-mortar stores and via their online channels. Manufacturers that are vertically integrated into retailing (e.g., MAC, L'Occitane) are not considered here.

1. Sephora

With over \$13 billion in sales in FY18 and 2,600 stores worldwide, Sephora, a subsidiary of LVMH, has developed into a global beauty retail powerhouse. Sephora was a pioneer of the try-before-you-buy concept. The company has developed a variety of tools such as (1) the Virtual Artist, an augmented reality (AR) technology for trying on makeup, (2) the Color IQ, a shade-matching skin scan, and (3) the Fragrance IQ, a fragrance sensory technology (InstaScent) using a dry air delivery system. In addition, Sephora increasingly offers its own branded products placed strategically in a lower price segment than the majority of its other products.

2. Ulta Beauty

Ulta Beauty generated \$6.7 billion in sales in FY18 and achieved the highest sales growth among the top 10 beauty specialist retailers (FY16-18 CAGR of 17.6%). As the top American beauty retailer, Ulta offers more than 25,000 products from approx. 500 brands across all categories. Ulta has increased its number of stores and square footage by 9%. It has focused on digital innovation by partnering with AR and artificial intelligence (AI) start-ups, resulting in a 9.7% increase in its online sales share in FY18, with a 47.6% CAGR from FY16 to FY18. For 2021, Ulta is targeting a two-day delivery for all online purchases through fast fulfilment centres in the US.

3. Douglas

With \$3.3 billion in sales in FY18/19 and a robust EBITDA margin of 7.1%, Douglas has become the leading beauty specialist retailer in Europe. The company has increased its store base significantly through acquisitions in Italy and Spain. The expansion of its e-commerce business is reflected in a sales CAGR of 23.1% from FY16 to FY18. Douglas is focused on five strategies in its #ForwardBeauty mission: (1) Upgrading and rejuvenating the brand, (2) improving the in-store consumer experience, (3) expanding e-commerce through the use of new technologies, (4) focusing on product innovation (also including own-branded products) and exclusivity, and (5) enhancing 1-to-1 marketing (CRM).

5. L'Étoile

With approx. 1,000 stores, L'Étoile, a subsidiary of Alkor & Co., is the largest beauty specialist retailer in Russia. The company grew by about 10% per year from FY16 to FY18. The retailer's strategy is focused on store expansion in Russia and on the inclusion of more premium and luxury brands in its portfolio. Interestingly, Sephora entered Russia through a partnership with the Alkor Goup in 2003 (which ended 2010) as L'Étoile was a major client of LVMH Group.

7. Rive Gauche

Headquartered in St. Petersburg and offering its beauty products only in Russia, Rive Gauche had FY18 sales of approx. \$570 million and a FY16-18 sales CAGR of 11.8%. The retailer recently introduced a new brand identity and retail concept. The company aims to further expand its store network in large shopping malls, reaching up to 240m² of floor space in each location. Rive Gauche also operates an online shop and several other sales formats (such as Beauty House, professional makeup schools, and image studios) to attract more consumers.

9. Ainz & Tulpe

Ainz & Tulpe, a subsidiary of Ain Holdings, is one of a few Asian one-stop beauty stores that is a retailer but not also a manufacturer (retailers/manufacturers include e.g. Laneige, Shiseido, Innisfree). The company had sales of approx. \$220 million and generated an EBITDA margin of 4.1% in FY18. Ainz & Tulpe is pursuing a store expansion strategy with modern formats in prime locations in the Tokyo metropolitan area. The retailer wants to improve the in-store customer experience by using displays to attract more customer traffic. Going forward, Ainz & Tulpe plans to open additional stores.

4. Sally Beauty

Sally Beauty generated annual revenues of \$2.3 billion in FY18. 81% of Sally's consolidated net sales are generated in the US, with approx. 2% of sales generated via their e-commerce channel. The retailer offers approx. 8,000 products for hair, skin, and nail care in its 3,695 stores. Sally recently introduced a new loyalty programme and implemented a two-day delivery service.

6. Sa Sa Intl.

Sa Sa Intl. Holdings Ltd. is engaged in cosmetics retail and wholesale in Hong Kong and Macau, mainland China, Singapore, and Malaysia. Sa Sa has been listed on the stock exchange in Hong Kong since 1997 and is considered the strongest player in the APAC region with sales of approx. \$1 billion in FY19. Its online presence accounted for less than 5% of FY19 sales. Sa Sa strictly manages costs by focusing on a premium assortment, reduced inventory and store size. Sa Sa's key future strategy involves e-commerce, including using WeChat to enable frontline sales staff to continuously interact with consumers.

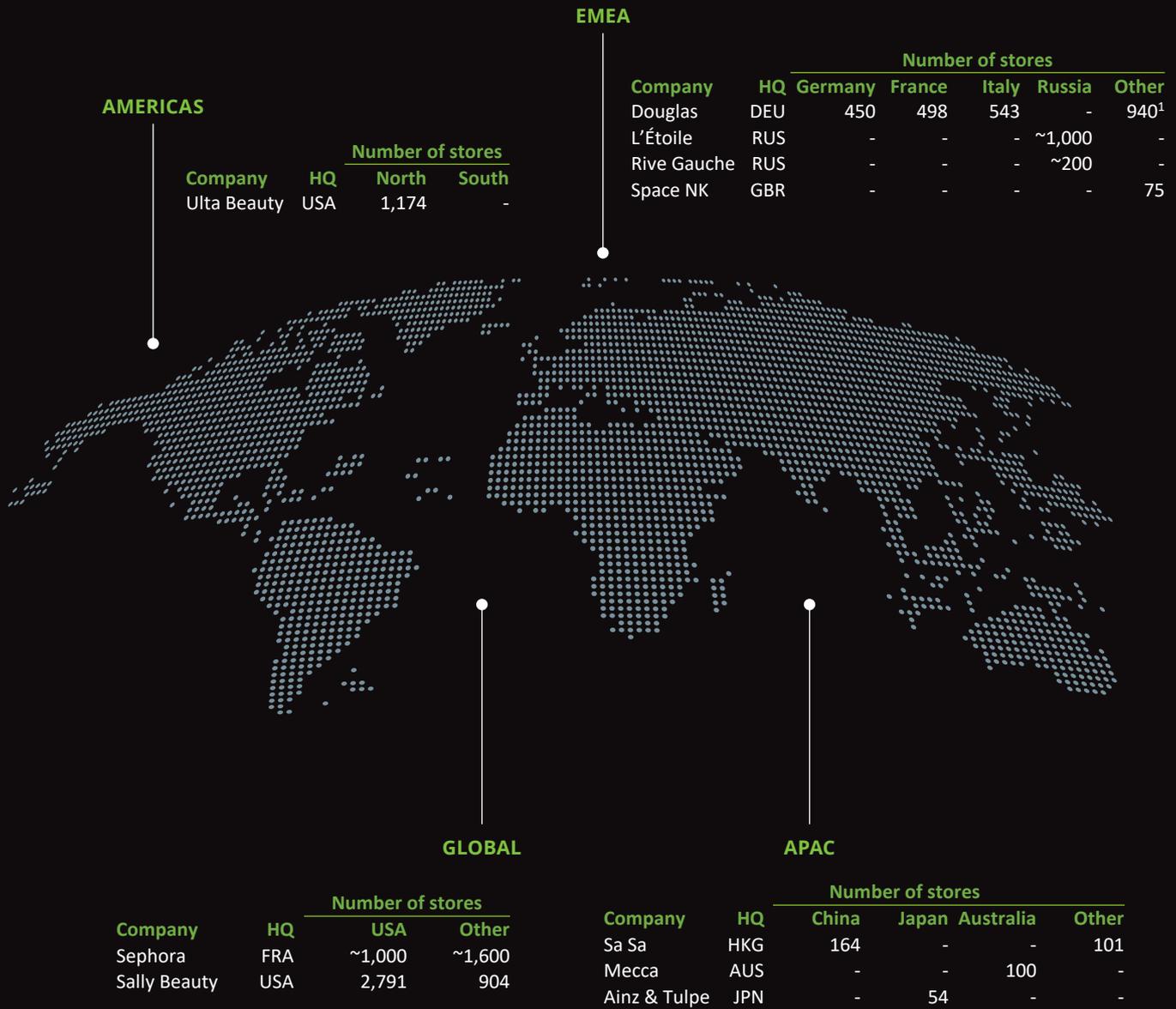
8. Mecca

Mecca comprises two concepts, Mecca Maxima and Cosmetica, with affordable to high-end products. Mecca had sales of approx. \$325 million in FY18 and grew with a CAGR of 6.3% from FY16 to FY18. The company is following an expansion strategy, targeting at tripling the space of its distribution centre to 15,000m² and investing in "mega" stores comprising 600m² store space each. Mecca is strongly present in diverse social media and other marketing formats (including a beauty festival, beauty lab, and its "Play bars" for trying products).

10. Space NK

With approx. \$140 million in sales and an EBITDA margin of 6.8%, Space NK is a relatively small competitor compared to the other companies ranked. Adyen, an e-commerce payment provider, supports Space NK with its local market expertise, enabling the company to expand faster into new regions. For Space NK, offering several payment options within an easy buying process is a strategic key to increasing online sales in times of high online-only retail competition. In addition, Space NK is working to develop more exclusive brand partnerships and more attentive customer service to ensure its premium image.

Store count of top 10 beauty specialist retailers by region



1. Other Douglas stores are mainly located in Spain, as well as in northern and eastern European countries.

Source: Annual reports, company publications, press search, Deloitte analysis

Top 10 health and beauty retailers

Global top 10 health and beauty retailers, 2018

Name	HQ	Regional presence	Stores (#)	Employees (\$m)	Sales (\$m)	Sales CAGR FY16-18	EBITDA margin
1. Walgreens Boots	USA	Global	>9,000	440,000	131,537	5.9%	6.4%
2. A.S. Watson (retail segm. CK Hutchison)	HKG	Global	~14,500	120,000	21,562	5.1%	9.6%
3. Dm-drogerie	GER	EMEA	~3,400	62,000	10,828	9.2%	4.0%
4. Matsumoto Kiyoshi	JPN	APAC	>2,000	c.3,400	5,061	1.3%	7.4%
5. Raia Drogasil	BRA	Americas	1,900	>40,000	4,254	11.9%	7.7%
6. Müller	GER	EMEA	~900	35,000	3,932	3.7%	7.1%
7. Mannings/Guardian (Dairy Farm Group)	BMU	APAC	~2,300	~23,000	3,226	10.7%	10.4%
8. Olive Young	KOR	APAC	~1,100	~450	1,509	25.3%	n/a
9. Matas	DNK	EMEA	272	2,500	549	3.1%	15.4%
10. Bonjour	HKG	APAC	~40	~900	229	(5.6%)	n/a

Like BSRs, **health and beauty retailers** (HBRs) also distribute beauty products. However, HBRs focus more on personal care products (such as hair care and body care) and sell health-related products including prescription and OTC drugs, nutrition products, vitamins and supplements, and contact lenses.

Relevance of HBRs in the competitive landscape of beauty retailing

Since HBR players' focus is primarily on body care products, they do not directly compete with beauty specialists. However, they are strong indirect competitors as they also sell premium cosmetics and fragrances, the predominant product categories of beauty specialists. Walgreens Boots Alliance and A.S. Watson are the two biggest HBR players, with the highest sales. Both players have a global presence and have sales that are higher than Sephora's (which ranked first place in the BSR category).

As HBR players are indirect competitors to BSRs, it would be worthwhile to

understand the HBR business strategies. Walgreens Boots Alliance is the global leader in retail and wholesale pharmacy with approx. \$132 billion in sales and an EBITDA margin of 6.4% in FY18. It has three brands in the US retail business (Walgreens, Duane Reade, and Rite Aid) and one international principal brand (Boots). The competitive advantage of a pharmaceutical retailer is primarily the reputation of trust and customer care.

In addition, Walgreens Boots Alliance has an omni-channel presence including an integrated e-commerce platform with prescription scans and refill notifications, modern stores, and new delivery models through strategic partnerships. This convenience was initially implemented to support the pharmacy brands but it has also had a positive impact on beauty retail customers resulting in an improved perception from the entire customer base.

A.S. Watson's health and beauty segment (including Watsons, Kruidvat, Trekpleister, Rossmann, Superdrug, Savers, and Drogas)

reported more than \$21 billion in sales, with an EBITDA margin of 9.6%, in FY18. In comparison to Walgreens, the Watson's brand has a stronger focus on beauty retail. In order to enhance the customer experience, the company is strategically focusing on expanding the digital presence in brick-and-mortar stores. The company also uses big data to analyse customer information to improve, simplify, and personalize the customer experience in its e-commerce platform.

HBR players understand prevailing market trends and, with a multitude of stores and employees, have a strong market presence. However, the market perception is still that they are a place to go for health products rather than for beauty products. Even though HBRs are now entering the e-commerce market, their online presence is comparatively smaller than BSR players; for example, Raia Drogasil has achieved a y-o-y growth of 163% in e-commerce sales, which only comprises 2.3% of its total sales in FY18.

COVID-19 impact on beauty specialist retailers

COVID-19 impact on top 10 beauty specialist retailers, 2020

Name	E-com sales growth	E-com customers	Store sales growth	Store change, #	Geographical impact ^{1,2}
Sephora	+70%–80% ³ Δ n/a	n/a	n/a	+64 ⁴ Σ 2,021	<ul style="list-style-type: none"> Low sales in EU Focus on CH and NA for expansion
Ulta Beauty^{5,6}	+200% Δ ~€81m	+21% ⁷	(54.0%) Δ (~€442m)	+10 ⁸ Σ 1,264	<ul style="list-style-type: none"> Reduced store expansion plans to 30 in US (from 75) and CA expansion to FY21
Douglas⁹	+40.6% Δ €238m	+41%	(15.8%) Δ (€448m)	(59) ¹⁰ Σ 2,372	<ul style="list-style-type: none"> +30% sales drop in FR and SWE
Sally Beauty⁸	+102.6% Δ n/a	n/a	(8.1%) Δ (€174m)	(42) Σ 3,653	<ul style="list-style-type: none"> Paused 'National Sally Beauty brand' relaunch (mainly US); Deferred new stores and remodeling plan
L'Étoile	n/a	n/a	n/a	n/a Σ ~1,000	<ul style="list-style-type: none"> Halted 50-new-store expansion (which was planned for FY20)
Sa Sa Intl.¹¹	9.5% ¹² Δ €2m	n/a	c.(30.7%) ¹³ Δ (~€268m)	(4) ¹⁴ Σ 231	<ul style="list-style-type: none"> Sales growth (to PY): <ul style="list-style-type: none"> HK: (33%) CN: (15%) MY: 1%
Rive Gauche	n/a	n/a	n/a	+5 Σ 240	<ul style="list-style-type: none"> Mainly focus on key cities like Moscow and Petersburg
Mecca	n/a	+400% ¹⁵	n/a	(~2) ¹³ Σ 109	<ul style="list-style-type: none"> Increased distribution centre hours to 24x7 Focus on online sales in CH
Ainz & Tulpe¹⁶	n/a	n/a	n/a	+9 Σ 64	<ul style="list-style-type: none"> Continued store expansion plans in metro areas (and shut stores in suburbs)
Space NK	n/a	n/a	n/a	(8) Σ 86	<ul style="list-style-type: none"> Closed stores in CN To close stores in US¹⁷ Focus on UK and online sales

COVID-19 impact – Key observations

1. Impact on businesses

In-store sales declined in 2020, as most beauty retailers were forced to shut all stores temporarily (mainly in EU and USA) and in-store operations were restricted after re-opening. Despite a strong increase in online sales the e-commerce business of the respective players could not fully compensate the decline of in-store sales.

2. Short-term measures

Based on the strong demand for online sales, beauty specialist retailers significantly strengthened operations of this sales channel through such measures as adjusting the supply chain infrastructure, increasing delivery speed, and shipping products from within stores.

Additionally, specific features such as virtual reality tools, online one-on-one consultations, and live-stream commerce technology were implemented to enhance the online experience for customers. Product assortments were also adjusted as a result of an increased demand, for example, for body care, hair care, and toiletries.

3. Long-term strategies

Beauty specialist retailers made a significant change to their business model to focus strongly on implementing a sustainable e-commerce business. This led to a decrease in previously planned new store openings.

Notes: (1) Data for 9M FY20 vs. 9M FY19 (2) Abbreviations for locations: SA – South America, NA – North America, US – United States, CN – China, CA – Canada, EU – European Union, SWE – southwestern Europe, FR – France, HK – Hong Kong, MY – Malaysia (3) Only for North America (4) Further plans to open 260 stores in 2021 (5) Percentages for Q2-FY20 ended Aug 20 (6) 1 € = 1.1194 US\$ - 2019 average (7) Loyalty members who make omni-channel purchases (8) FY20 vs. FY19 (9) Data for Q4 FY20 vs. Q4 FY19; refers to net growth (10) As compared to 9M FY19 (11) Period between 1st April and 30th September 2020 compared to same period of 2019; 1 HKD = €0.113951 - 2019 average (12) Turnover increase (13) Deloitte estimates (14) For period between 1st April and 30th September (15) Data for weekly visitors to the store site to pre-COVID levels (16) Data as of FY20 and Q1-21 ended July 20 (17) The company plans to close 8 stores in the US by Mar 21, currently not included in the store change data mentioned

Source: Investor reports, company publications, press research, Deloitte analysis

COVID-19 impact on beauty specialist retailers (cont.)

1. Sephora

To offset lower in-store sales, the company took a number of steps, including relaunching its “Beauty Insider” program, direct Instagram shopping, and same-day delivery in NA. Key segments that witnessed growth during COVID-19 were skin and hair care as well as fragrances.

In August 2020, Sephora mentioned plans to expand in China (to offset prolonged store closures in the EU) and NA going forward. However, from 100 stores planned only approx. 40 stores will be opened and expansion plans for FY21 in Europe have been postponed.

3. Douglas

In FY20/21, Douglas experienced an in-store sales decline of ~16% compared to FY19/20. To offset the store sales loss, the company focused on increasing its e-commerce sales during and after the COVID-19 period. This was done by (1) offering a strong product assortment, (2) implementing special services such as phone ordering (in Italy and Spain) and a lower minimum order value for free shipping in all countries, and (3) using its CRM program to support growth in first-time online buyers. As a result, online sales increased by ~41% compared to FY19/20. As Douglas readjusts its business model, its strategy “Forwardbeauty.Digitalfirst” involves a strong focus on online sales and digitization. It includes investments into a holistic digital customer journey, digitization of core processes, marketplace expansion, and supply chain changes.

5. L'Étoile

L'Étoile undertook several measures to increase its e-commerce sales (which represented only ~5% of its total sales in FY19) including (1) strong discounts, (2) exclusive online special offers (even after stores reopened), and (3) a 24x7 customer service number for online queries.

Plans to open 50 new stores in 2020 were temporarily halted.

The company introduced new antiseptic/ antibacterial products to its range.

L'Étoile also expects an increase in demand for personal care and health-maintenance products and a decline in demand for decorative cosmetics, during and after COVID-19.

2. Ulta Beauty

To compensate for the strong in-store sales decline, Ulta expanded its e-commerce activities by introducing the GlamLab virtual tool (for product comparison), curbside pickup, “Buy online pickup in store”, and “Conscious beauty” (involving products with clean ingredients), and expanded its loyalty programme. The skin and hair care segments grew.

Ulta plans to further expand its digital business, making it a larger percent of its total sales (which currently sits at ~20% annually). Going forward, the company plans to expand its presence in the US (~30 stores in FY20, compared to ~75 stores slated pre-Covid for FY20) and enter the Canadian market by mid-FY21.

4. Sally Beauty

Due to the lockdown, Sally's in-store sales declined by 18% (~US\$301m) as of 9M FY20 (to PY). The company focused on increasing its e-commerce revenues by (1) launching ship-from-store capabilities (to offer expedited shipping), (2) introducing curb-side pick ups in NA, (3) introducing a credit card program for customers, and (4) advancing its merchandising transformation efforts. This led to an increase of US\$84m (or 168% growth) in e-commerce sales.

During the lockdown, the *hair colour and salon supplies & accessories* segments exhibited sales growth.

Sally paused its expansion plans including (1) a national Sally Beauty brand relaunch, (2) new stores and store remodels, and (3) a JDA merchandising system implementation.

6. Sa Sa Intl.

Due to the lockdown (and low tourist presence), Sa Sa's store sales declined by 33% in HK and 5% in CN. Further, in FY20, the company's e-commerce sales via its own channels declined by 35% (to PY). However, its e-commerce sales via third party platforms (WeChat, Boutir, etc.) saw a 5% growth (to PY).

Initiatives to boost e-commerce sales during COVID-19 included (1) personal online stores, (2) strong discounts, (3) sale via social commerce sites, and (4) a click-and-collect service in MY.

Post COVID, Sa Sa plans to focus only on organic growth of its existing store network in MY and HK, and open new stores only in specific locations in CN (such as Chengdu, Chongqing, and Shanghai).

COVID-19 impact on beauty specialist retailers (cont.)

7. Rive Gauche

During this period Rive Gauche focused on strategies to improve its e-commerce sales including (1) higher discounts via loyalty cards, (2) bonus programs for exclusive brands, and (3) online order and in-store pick-up options.

After lock-down, strategies to boost in-store sales included (1) expansion of “client day” offerings (specific brand-related events at stores offering make-up demonstrations, discounts, free loyalty cards, etc.) and (2) store-specific discounts.

Rive Gauche opened 5 new stores across Russia (of which 3 were in Moscow) and plans to continue its geographic expansion in key cities in Russia.

9. Ainz & Tulpe

Ainz & Tulpe did not shut all of its stores in Japan; it mainly restricted in-store hours (for most stores).

In May 2020, the company launched its official web store (which was planned pre-COVID) and together with its new mobile app (launched in October 2019), Ainz & Tulpe was able to mitigate in-store sale losses due to COVID-19.

Other measures included (1) price reductions for specific in-house brands, (2) website-specific sales, and (3) new store opening discounts.

The company closed 6 stores in suburban areas and opened 15 new stores in urban metropolitan regions, including Sapporo, Tokyo, Osaka, and Hakata.

8. Mecca

In order to compensate for the loss of in-store sales, Mecca introduced various programs such as (1) Mecca Live and Mecca TV (to allow customers to chat with customer service teams, broadcast interviews, etc.), (2) virtual consultation and shopping services via video calls for a fee, (3) a purchase via phone and collect in-store service, and (4) increased content output on digital platforms. Weekly visits to its online store grew by ~400% during the first phase of the crisis. Sales of skin and hair care products reported strong growth while sales of fragrances and home fragrance grew moderately.

Additionally, Mecca also increased its distribution centre hours (in Melbourne) to 24x7 and switched all deliveries to “priority shipping” status.

10. Space NK

Space NK announced plans to temporarily close stores in the UK, and to permanently shut all its 8 stores in China (and only focus on its web store sales in the country). Additionally, in June 2020, the company announced plans to shut all 8 of its owned stores (by March 2021) in the US and focus on wholesale sales in the region.

During the first phase of the lockdown period, Space NK announced several new online initiatives to boost e-commerce sales such as (1) online consultations via booking for a fee, (2) virtual events via Zoom meetings, (3) curbside pickup for deliveries, and (4) its SpaceLive platform for live-streamed beauty classes.

The company reported that there was higher demand for hair care and treatment, bath and body products, and lipstick during and after the first COVID-19 wave, whereas the sales for fragrances and foundation dipped.

Key market trends in beauty retail



CAGR 2018-25F of selected product-based trends



Sources: Organic Soil Association, Allied Market Research, Grand View Research, retailer's websites, Deloitte analysis

Trends in e-commerce are heading towards digital tools and advice

Beauty retailers are innovating their e-commerce platforms by introducing new tools in the digital sphere. Their main goal is to promote a more seamless and convenient user experience. However, consumers still prefer frequenting physical stores, so is that they can try on products, match the colours to their skin tone and compare textures. Currently, when customers purchase products on the internet, they only buy ones they know. In order to increase the number of products purchased on the internet, BSRs are introducing augmented reality (AR) and virtual reality (VR) to their e-commerce platforms.

AR product try-on is one of the most popular e-commerce trends among beauty retailers

With the rise of e-commerce, beauty specialist retailers have introduced AR makeup try-on tools on their mobile apps to address the above-mentioned shortcoming. These tools recognise the users' facial appearance and let them apply makeup products of their choice, mimicking a realistic full-face look. The systems recognize small motions so that quick head movements do not impair the program's quality, and even face-obscuring barriers like glasses don't hinder the experience. The user thus receives a realistic picture of the final look and is able to directly add their favourite products to the shopping cart. With further advancement of AR technology, this trend is expected to rapidly gain popularity.

For example, Sephora offers a live 3D experience on its app with Virtual Artist and Pocket Contour. Target offers Beauty Studio, A.S. Watson has the Magic Mirror and Alibaba offers YouCam Makeup on its Tmall Flagship Store 2.0. There are many other retailers that also offer AR makeup try-ons, mostly in cooperation with ModiFace or YouCam and social media platforms such as Facebook and WeChat.

To bring online customers offline into stores, some retailers offer large screen AR try-on stations at select stationary locations. Additional mechanisms to combine virtual and store based shopping include "click & collect" and "click & reserve" on many retailers' websites.

Data gathered by PerfectCorp, owners of the AR makeup try-on app YouCam Makeup, shows that customers using the app are 1.6 times more likely to purchase beauty products and spend 2.7 times more money on beauty products than those who don't use the app.

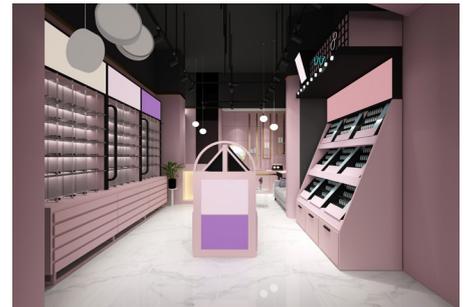
Another trend, which is still in its initial stages, is the establishment of virtual stores based on VR. Alibaba, for example, opened a VR shop with Tmall Flagship Store 2.0 to attract Gen Y and Z consumers.

Virtual beauty advice is increasingly offered via online chats and apps

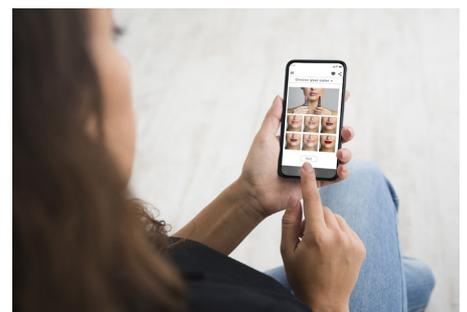
Many retailers are increasingly incorporating virtual beauty advice tools via online chats or members-only social platforms (e.g., Sephora's Beauty Insider

Community). This offers consumers an enhanced shopping experience by providing quick, convenient and free advice from experts. Examples of retailers that offer beauty chats or beauty advice are Target, Jumei, and Takaski. Sephora's Pocket Contour Class, which is a face contouring instruction app, uses AR to provide beauty advice.

Examples of virtual product try-on



In-store



App

Stores become modern and premium

Beauty specialist retailers are increasingly modernising their brand towards a more high-end look. Many retailers have even refurbished their stores towards “instagrammable” flagship stores. These stores include beauty displays for AR make-up try-on, attractive product placements, and many other touch-and-feel experiences. The goal is to enhance the customer’s omni-channel experience for many exclusive brands. Retailers are aiming to make in-store experiences more enjoyable and informative than their websites and apps.

Modern, refurbished stores are located on high streets and offer in-store events

As brick-and-mortar stores are gradually losing sales share to e-commerce platforms, retailers are continuously searching for ways to attract more customers into their stores. One option is to modernize and refurbish stores by integrating more appealing interior design, creating a luxurious atmosphere and presenting sculptural displays. Touch-and-feel corners also help customers to try on new products. Some retailers have established “concept stores” that focus on digital components and offer a more curated retail experience for their customers.

Digital innovations are increasingly used to create a personal and enhanced consumer experience, resulting in more connected stores

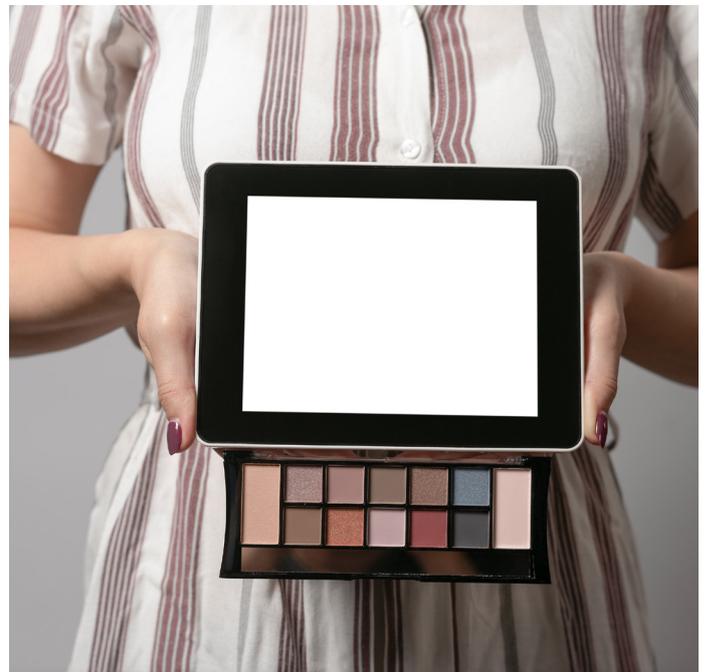
Digital innovations, such as the widely used augmented reality (AR) tool, are being increasingly applied in many selected stores. Using AR, a large in-store display can augment a customer’s face with their selected make-up choices.

Other tools offer beauty recommendations such as skin care diagnostics and tutorials that can be combined with the advice of an in-store makeup expert. For example, Sephora offers Color IQ, a tool that analyses the skin tone. Color IQ provides guidance in choosing the correct makeup shade by evaluating the customer’s skin tone via a number-coding device.

In some concept stores, such as Sephora, visitors are greeted through large welcome screens, and employees are equipped with iPhones for mobile point-of-sale purchases instead of cash registers.

With these tools, retailers can connect the store-based shopping experience with their mobile-app-based browsing and purchasing offerings.

The “Sephora to Go” app shows online reviews and ratings of products that have been scanned in the store via a barcode. Within the app, Sephora has incorporated a “store mode” using beacon technology which consumers can use to navigate over a product to obtain relevant and useful messages.



Stores become modern and premium (cont.)

Stores offer exclusive, trendy brands that underline individualism and a conscious lifestyle

Exclusive, trendy brands are typically positioned in the premium price segment. These are often marketed by social influencers, some of which promote the clean-beauty movement. An example is the product series “Kylie Skin” by Kylie Jenner, the Instagram influencer with around 165-million followers. The products are cruelty free, gluten free, vegan, paraben free, sulphate free, and dermatologically tested. Another celebrated beauty influencer on Instagram is Huda Beauty. Her beauty products, named “HudaBeauty”, are also available at renowned retail chains worldwide. Thus, exclusive brands and an extended assortment encompassing conscious brands are a key strategic focus for the majority of retailers to attract more customers.

Beauty treatments are increasingly offered in stores

Beauty treatments are now also offered by some beauty retailers. Ulta offers personalized in-store services by licensed professional stylists who customise hair, skin, brow, and makeup services in accordance with the customer’s needs and wishes. Sephora offers facial treatments, makeup, and brow services as well as specific beauty advice with tips and tricks for their customers. Beauty treatments and makeup services are also available at selected locations of Douglas.

The variety of delivery and payment methods in stores increases

Customers are now able to choose from different delivery and payment methods. The click & collect-method offered by A.S. Watsons, Ulta, Douglas, and others supports the needs of customers who are not at home during regular delivery times. Sephora introduced the “Flash” program which promises two-day delivery with an annual enrolment fee of \$10, a model comparable to Amazon’s Prime subscription.



Deep dive: Skin colour scans in stores



Beauty shoppers' pain point

Searching for a matching colour tone is a pain point for most beauty consumers. This search is made even more difficult by the facts that brands occasionally optimise their colour assortment and alter their colour codes, makeup shades are not consistent across different brands, and shoppers' skin tones can vary seasonally. All of these circumstances lead to consumer confusion and the inability to maintain the same shade for a considerable period of time.

Sephora's Pantone Color IQ test to the rescue

Even though e-commerce sales are continuously rising for retailers, brick-and-mortar stores still generate the highest sales share. Industry pioneers are constantly working on solutions to make the in-store experience more seamless and exciting for consumers who are, for example, confronted with the difficulty of finding the correct foundation. To address this challenge, a partnership between Sephora and the colouring specialist Pantone has emerged. The collaborators developed and patented a scanning device that allows consumers to scan their skin to identify their skin colour/tone. Consumers

receive a Pantone Color IQ number and are then able to match their skin tone with various make up brands offered by Sephora. A range of product suggestions are offered to support customers in their selection process. This foundation-matching innovation had a strong impact on the cosmetics industry.

Transcending in-store and e-commerce channels

The Sephora-Pantone Color IQ system invites consumers into stores and then provides the results digitally, frequently coupled with product suggestions. This process enables buyers to make purchases both offline and online.

Similar to the Color IQ system, other retailers have established their own touchpoints that attract shoppers into their brick-and-mortar stores in order to test the retailers' innovations, such as those using augmented reality concepts. Consumers typically receive their results digitally. This customer-centric omni-channel approach of merging various sales channels has become important for retailers globally in their efforts to attract more consumers into their stores and balance out the growth ratio of in-store and e-commerce sales.

Deep dive: Beacons as the new digital in-store experience



The rise of the beacon

Over the past decade, the retail industry has seen major technological developments focusing on effective POS marketing or information transfer to customers. As wireless connectivity has become more important, traditional technologies have been surpassed by beacons.

Beacons communicate with mobile devices via apps. Stores equipped with beacons are able to send their consumers notifications about personalised offers and promotions. These notifications are sent out based on a customer's location in the store, and they simultaneously provide valuable data to the store operators.

Beacons have increasingly gained attention since Apple's introduction of iBeacon in 2013. The underlying technology uses a Bluetooth Low Energy (BLE) transmitting device consisting of a Bluetooth module and various additional sensors and systems that transmit data within a

specified range, typically 70 metres. Beacons can be classified according to their protocol type (iBeacon, Eddystone, etc.).

Retail as the largest application market for beacons

End users of beacons encompass a wide array of industries, in particular the retail and transportation industry. Other prominent end user markets include real estate, education, and hospitality.

With a market size of US\$969 million in 2018, the retail sector accounted for ~53% of the global beacon market (US\$1,834 million) and has the highest penetration within the beacon market.

Application areas within the retail segment

With the emergence of e-commerce and the widespread combination of different channels towards an omni-channel approach, retailers have searched for ways to improve their marketing efforts. Many large corporations, such as Sephora,

conducted beacon technology pilot trials which proved the effectiveness of the technology, inducing many other retailers to quickly adopt this technology.

Beacon usage and benefits differ from retailer to retailer. The most common usage remains as an advertising tool, providing shoppers with more appropriate, personalised messages at the right time and the right location. The technology can also be used by store operators to collect data that can provide valuable insights into their consumers' behaviours, allowing them to further optimise the consumer experience. Beacons also support consumers by maximizing their app usage. Beacons cost less than traditional marketing tools which is an additional benefit to retailers.

Americas: The pioneer of the beacon market

The Americas are a pioneer in the beacon industry with a global sales share of ~44% in 2018, closely followed by the EMEA region which accounts for ~40% of the market. Both regions are expected to lose market share by 2026 to the fastest growing region, APAC (projected to grow with a CAGR of ~69% between 2016 and 2026).

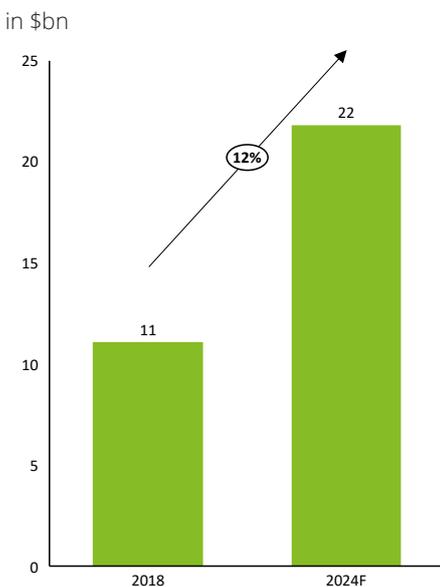
The global rise of natural and organic cosmetics

The natural and organic cosmetics market is undergoing a major shift due to changing consumer perspectives and needs. As consumers' health and environmental awareness is increasing, there is an observable trend towards natural and organic products and ingredients as well as eco-friendly packaging (recyclable and refillable). Both the awareness of well-being and the desire for outer beauty contribute to the higher demand for these products.

Researchers assume an annual increase of ~12% from 2018 to 2024 in the use of certified natural and organic products,¹ with a corresponding increase in the global market for these product from \$11 billion in 2018 to \$22 billion in 2024.²

Beauty brands are not legally obligated to be certified; for example, products with 1% or less of such ingredients may still carry the label "organic".

Global market size of natural and organic cosmetics



1. Organic Soil Association. 2. Persistence Market Research.

Source: BIS Research, press research, retailer websites, Deloitte analysis

Growth drivers have different magnitudes

One of the main growth drivers for natural and organic cosmetics is inner **stress**.

Consumers search for products that help them to sleep, be calm, and stay mentally healthy. A study of the Organic Soil Association shows that 83% had a better feeling in regard to their health if using an organic product.

Another strong driver is product **quality and efficacy**. Consumers perceive that organic products are as or even more effective than non-organic products.

Natural and organic products are based on the usage of natural **active ingredients**. Examples of popular active ingredients include ground coffee in skin scrubs, and seaweed snail slime and bee venom in skin care.

These ingredients are especially used in **K-beauty products** (Korean beauty cosmetics) with a market size of \$9.3 billion in 2018. Between 2019 and 2026, the K-beauty market is anticipated to grow by a CAGR of 11.3%, leading to an expected market size of \$21.8 billion in 2026. Around 70% of the total market share is situated in the Asian-pacific region, where wellness and health are emphasised in skin care routines. Other Asian countries, such as Japan (**J-beauty**), have a similar ingredient focus in cosmetics.

Global **pollution** is leading to a rise of skin sensitivity and premature ageing due to oxidative stress. Demand is increasing for botanical products with high levels of natural antioxidants which help protect the skin against free-radical damage by supporting the self-reparation of the skin.

Examples of natural and organic cosmetics by retailers' own labels



Cruelty-free, vegan and halal cosmetics are trending globally

In 2019, Douglas launched a clean beauty concept which focuses on healthy ingredients (using no silicones, parabens, sulphates, or mineral oils) and on those that are cruelty-free. This was in response to an increasing trend among customers of healthy and conscious lifestyles.

Social media influencer Kylie Jenner, who has over 165 million followers on Instagram, introduced a skin care line called Kylie Skin. Its products are vegan, cruelty-free, gluten-free, sulphate-free, and paraben-free. In alignment with its clean beauty concept, the Douglas Group launched this brand in 2020, and it now ranks among its top-ten skin care brands.

Rising demand for cruelty-free products that are not tested on animals

Unilever offers cruelty-free products with its Suave brand. Suave has an accreditation from People for the Ethical Treatment of Animals (PETA) which validates that alternatives to animal testing are used for these products.

Estée Lauder is also ending animal testing in cosmetics through the expansion of partnerships with Cruelty Free International and Humane Society International. This means that Estée Lauder will no longer directly test products on animals, nor will they ask any third parties to do so.

Despite these initiatives, finding cruelty-free and vegan cosmetics at retailer stores is still rare. However, this is anticipated to change in the future.

Halal cosmetics finds interest among Muslim consumers, especially in the APAC region

The demand for halal cosmetic products is increasing among the 2.4 billion Muslim consumers worldwide. The development of these products is still in the beginning stages. Halal cosmetics are produced without the use of pork, dog, or alcohol ingredients in accordance with Islamic requirements. Halal is not only applied in the product itself but also in the packaging, manufacturing, and distribution methods.

According to Grand View Research, the global halal cosmetics market had a size of ~\$23 billion in 2018 and is projected to grow with a CAGR of 12.3%, reaching \$52 billion by 2025. The large worldwide Islamic population will be willing to pay a premium for halal-certified beauty products, strengthening the demand over the forecast period. Skin care is anticipated to be the strongest growing product segment of the halal cosmetics market, followed by makeup products.

In the ASEAN region, consumers are becoming more interested in halal products. A recent report (by TechSci research) regarding the Saudi Arabia Halal cosmetics market reported a growth level of 15% annually in the past five years for the halal beauty market and projects comparable growth in the future.

The variety of halal beauty brands is limited as this market segment is still a niche, with many Muslim women still not aware of halal cosmetics.



CBD skin care is gaining interest among consumers

CBD skin care products are an innovation in the cosmetics industry. CBD is an ingredient from the cannabis plant. The three primary species are sativa, indica, and ruderalis. Cannabis contains over 110 cannabinoids with different effects, but only two of them are largely known – THC (tetrahydrocannabinol) and CBD (cannabidiol). THC has psychoactive effects, while CBD is used to combat anxiety, chronic pain, and mood disorders.

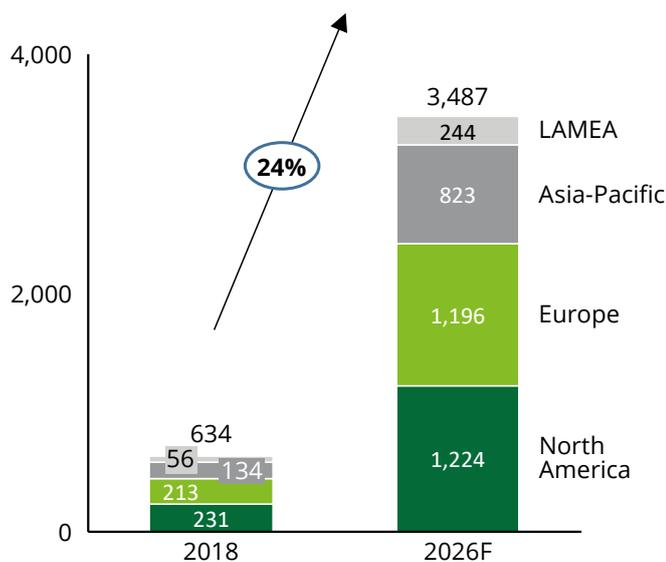
The effects of CBD skin care are diverse

Used as a topical agent, CBD can counteract free-radical damage and reduce inflammation. CBD anti-aging creams are said to diminish wrinkles, skin dullness, and ruddy skin tones.

Key players in the production of these products include Kiehl's LLC, Cannuka LLC, Leef Organics, Medical Marijuana Inc., Lord Jones, Kapu Maku LLC, and Endoca LLC. Other players in the value chain are L'Oreal, Kana Skincare, Cronos Group, CBD Biotech, Nordic Cosmetics, and Estée Lauder.

The distribution of CBD products via retail channels highly depends on the regulatory status in each market.

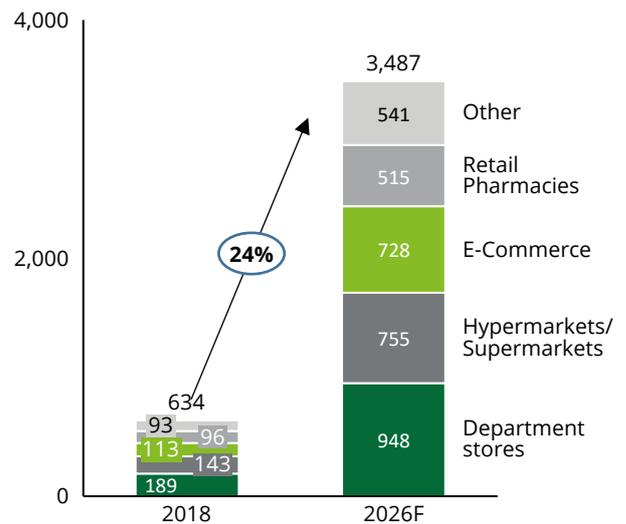
The global CBD skin care market by region, in \$m



The global CBD skin care market is fragmented and growing strongly

The global CBD skin care market shows high growth potential in North America, Europe, and Asia-Pacific. Thus, the market is of increasing interest for beauty retailers' brick-and-mortar and e-commerce platforms.

The global CBD skin care market by distribution channel, in \$m



The global CBD skin care market was valued at \$634 million in 2018. It is expected to grow to \$3,484 million by 2026 (CAGR of 24.8%).

Some retailers in the Americas and EMEA already sell CBD skin care, such as CVS (Mediterra), Walgreens (Sagely Natural), Sephora (Lord Jones, Saint Jane), Avon (Green Goddess), Rossmann (Canobo), and Douglas (SYS). Other retailers, especially in APAC, are expected to follow when regulatory hurdles are cleared in the near future.

- In Singapore, using or selling cannabis products is severely penalized.
- Japan and Hong Kong allow products that contain no traces of THC.
- In China, the use/sale of topical CBD products do not incur specific penalties. India has no formal ban or permit for CBD use.

Beauty retailers are aware of the growing men’s skin care segment

According to Allied Market Research, the men’s personal care market was worth \$134 billion in 2018 and is expected to reach \$166 billion in 2022. Asia-Pacific has the strongest growth levels in this market. Skin care for men is currently the fastest-growing segment given a strong demand for anti-aging creams, exfoliants, eye creams, tinted moisturizers, SPF products, and masks.

In China and Korea, male skin care is booming. Male makeup in China is pushed by key opinion leaders who have millions of followers on social network sites, such as Weibo.¹

The US male personal care and grooming market is expected to grow by 23.9% between 2018 and 2024.² Male-specific bio-based cosmetics and personal care products have been gaining traction which is an attractive opportunity not only for producers but also for retailers. Mass retailers are beginning to dedicate more shelf space for men’s grooming products.

Males prefer to shop for beauty products online

According to GlobalData research on US male consumers in November 2018, around 53.4% of American men feel uncomfortable buying cosmetics and personal care products in beauty retailer stores like Ulta and Sephora, as these are perceived as places for women.

Although men recognize that BSRs are convenient shops to buy personal care and grooming products, they are most comfortable buying these products online or at mass retailers such as Target or drugstores like Walgreens. Men (63.5%) are more likely to shop online than women (39.3%).³

Men have a strong brand loyalty and switch less among different brands

Interestingly, men are not as experimental as women, which results in stronger brand loyalty and less brand switching.

They are more interested in technical and scientific information than in the emotional feelings a product can evoke. Also, they prefer multi-purpose products (e.g., 3-in-1 shampoo) over many single-function products.

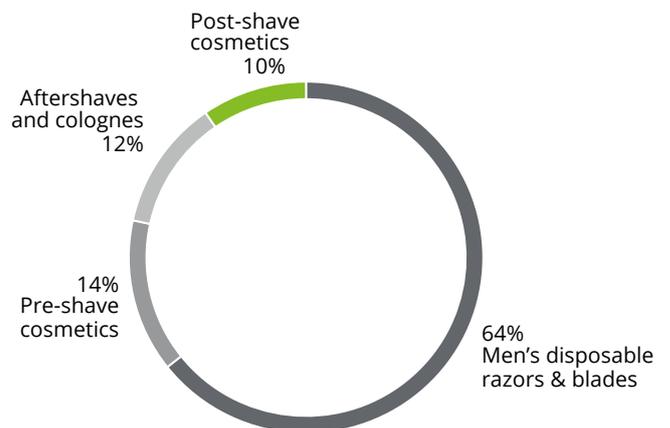
Men’s grooming trends are similar to those of women for specific beauty products

According to the US Chamber of Commerce, five key trends in men’s grooming can be forecast:

1. Wellness and fitness cosmetics
2. Natural and organic products
3. Hair grooming innovations
4. Moisturizing/anti-aging skin care
5. Gender-neutral products⁴

Social media influencers have changed the perception of male skin care – it is no longer a taboo topic. However, men’s disposable razors and blades still have a much larger market size (\$11,684 million in 2018) than cosmetics, depicted below as pre- (2018: \$2,564 million) and post-shave cosmetics (2018: \$1,746 million).

Global male shaving toiletries market segmentation in 2018, in %



1. CosmeticsChinaAgency. 2. GlobalData analysis. 3. GlobalData consumer panel.

Source: Allied Market Research, press research, BIS Research, OneSpace, Stephenson Personal Care, CNBC, MarketLine, Deloitte analysis

Regulations and certifications

As a result of consumers' increasing awareness of products' ingredients and manufacturing conditions as well as the resulting increase in CBD, cruelty-free, vegan, and halal cosmetics, some countries have enacted regulations to set legal frameworks and certification rules for businesses serving these trends.

Some countries and regions ban animal-testing conducted for new cosmetics development

Cruelty-free cosmetics are on the rise not only in customers' minds but also in legislation around the world. Since 2013, the European Union announced a ban on the import and sale of cosmetics that contain ingredients tested on animals, and shortly after that the EFTA1 members followed suit. Europe has become a leader in the field and several non-European countries have also pledged to abandon practices involving animal testing, such as Israel in the EMEA area, India, Taiwan, South Korea, and New Zealand in the APAC region, and Guatemala in the Americas.

Other countries might not have laws as specific as those in the EU but are still phasing out animal testing processes due to national and international pressure, such as the US and Brazil. China remains a special case, as it currently has a law in force that requires imported cosmetics to be tested on animals prior to introduction to the Chinese market. However, growing awareness has led to the Chinese government requiring new cruelty-free methods of testing foreign cosmetics.

To provide transparency and help customers base their purchasing decisions on their beliefs, numerous associations are giving out certifications for companies going entirely cruelty-free. The best-known certification is the so-called *Leaping Bunny*, which is given out by Cruelty Free International and the Coalition for Consumer Information on Cosmetics and which requires companies to follow a strict set of rules. Furthermore, *Choose Cruelty Free* and *PETA* are also engaged in certifying cosmetics not tested on animals. However, some critics say that associations like PETA don't do enough to verify the trustworthiness of certified companies.

Natural cosmetics are often labelled with certifications verifying natural ingredients

Another growing certification area is in natural cosmetics, i.e., cosmetics including natural ingredients only. The leading certifications granted for natural cosmetics are *NATRUE* and the *COSMOS* standard, which have been developed in cooperation between five individual certifying organisations. There are also many regional certifiers, such as *Demeter* in the DACH region. Most certifications do not strictly require the entire product to be completely natural and allow a small fraction to be made up of certain pre-communicated ingredients. Also important in this context is the *Vegan Trademark* by the Vegan Society, which is a widely-known standard provided if the product does not include animal ingredients, an increasing trend in the beauty industry.

CBD and halal cosmetics increasingly gain attention

The use of CBD in cosmetics, a relatively new trend, depends on the prevailing legislation of each country and is not always clear-cut. In the EU, the use of hemp-derived or synthetically produced CBD in cosmetics is allowed, but member states might have further restrictions. For example, while Luxembourg allows hemp seed oils with a THC concentration of less than 0.3%, France forbids the use of CBD altogether if THC is found in the finished product. In Canada, CBD in cosmetics might be allowed if it meets certain criteria. In Japan, THC-free CBD oil is permitted, and hemp ingredients can also legally be used in China. Australia, on the other hand, prohibits the use of any kind of CBD ingredients in cosmetics.

Religious requirements have also led to regulations, especially with regard to halal products. Indonesia has passed a law requiring all cosmetics to be certified as halal, resulting in the expectation that there will be a strong demand of such products in South East Asia in the coming years.

New regulations and certifications are likely to emerge in the upcoming years.

Understanding the customer through data-driven marketing

How is marketing changing for beauty specialist retailers? Beauty retailers are increasingly using a specific marketing mix which strongly relies on digital technology.

On the following pages we outline tools and methods which help beauty retailers to

1. Understand their customers,
2. Optimise promotions via social media and
3. Optimise selling.

1. Understanding the customer: Data-driven marketing helps to identify different consumer behaviour patterns



Combining consumer-centric, innovative, and exclusive marketing activities is key in customer relationship management (CRM). This type of marketing is mostly driven by data-driven consumer insights.

One way to collect data is to profile customers through consultations and quizzes. The answers provided by the customer lead to personalised recommendations and promotions in accordance with the individual's complexion, problems, and beauty needs. AI technology also helps to derive data and to create personalised product recommendations based on collected consumer information. The information can be retrieved from past purchases and online browsing behaviour, relationships between the consumer and the product, and the buying cycle of the products. Google Analytics 360 Suite is an exemplary tool.

In China, beauty trends identified by AI strongly influence R&D and marketing. The Meitu Matrix app recommends personalised cosmetics to its users based on big data analysis. Meitu's artificial intelligence is also able to make sales forecasts, ensuring sufficient stock and fast delivery to customers.

Other beauty retailers, such as Sephora Asia, use analysis tools to manage website traffic and other marketing channels in order to ensure they have enough stock of the products that are being advertised.

Purchase patterns can also be identified with the help of machine learning. This

tool is important to understanding how users shop off- and online as well as how to create one continuous shopping journey. Another type of data-driven marketing is geo-ware (e.g. via beacons) targeting. This enables the retailer to display mobile ads to potential customers within the vicinity based on real-time location data supplied by the mobile network provider. Geo-fencing works similarly and helps to communicate with mobile devices in a specifically marked area. A geo-fence can send SMS messages, emails, and push notifications to devices.

Gathering data about consumer preferences can also be done by analysing shopping patterns via member loyalty programmes, such as the Douglas Beauty Card or the Ulta Ultimate Rewards Program. The data collected enables targeted micromarketing which includes personalised product recommendations and invitations to exclusive brands. This can lead not only to a higher conversion rate for retailers but also a larger average basket size. At Douglas, the average basket of an personally addressed card holder was 20% higher (at the end of FY17/18). At Ulta, sales to members of the loyalty programme account for 95%, targeted effectively through promotional and marketing activity. Members both shop and spend more than those who are not members.

Social media as a tool for optimising marketing promotions



2. Optimising promotions by means of social media

In addition to traditional marketing channels (such as magazines, advertising pillars, screens in public places, TV spots, and ad banners), social media is becoming increasingly important for beauty retailers. Social media campaigns are reshaping the beauty retail industry as they help retailers to engage more with their consumers. In fact, consumers increasingly trust social media as their primary information source with regard to new brands and products. Data from the 2019 GlobalWebIndex shows that consumers are 41% more likely to find new brands or products through social media. Furthermore, 47% say they discover them specifically via the social media pages of the brands. Influencer marketing on social media channels has an especially strong effect on retailer brand awareness.

There are six types of social media used globally among beauty retailers: photo sharing, video broadcasting, chat programmes, communities, influencers, and micro blogging. However, the purpose of the usage differs. Photo sharing, such as on Instagram and Pinterest, is used to introduce new products, and to present promotions, events, and competitions

to attract and retain consumers. When it comes to tutorials that explain the usage of products such as contouring palettes, video broadcasting is used. Platforms vary from region to region but can include YouTube, IGTV, Douyin (TikTok) and Facebook.

Sephora provides as good example of the use of YouTube as a tutorial platform. In 2016 Sephora had 690k followers, which has now grown to 1.3m subscribers, a CAGR of ~24%. In the tutorial videos, employees give beauty advice in a simple, approachable manner.

Video broadcasting on platforms like YouTube is used for long-form educational content. Online communities and beauty blogs created by retailers (such as the Sephora Beauty Insider Community and the Douglas Beauty Blog) help to give further guidance on products they sell.

Chat programmes such as WeChat (China), HelloTalk (Japan), KakaoTalk (South Korea), Line (Thailand), SnapChat, and Facebook Messenger are used to promote events, book reservations for beauty appointments, and implement conversational campaigns.

Micro blogging platforms such as Twitter and Weibo are used to give further information on retailers' products and promotions. Watsons, for example, was listed among the "Top 100 Annual Weibo Influence Power" in 2013, mainly publishing promotional content such as offers and vouchers on its Weibo page.

In this channel-based environment, the most important are the people who advertise for retailers – mostly social influencers. Influencers have been instrumental in changing the beauty business as they provide inspiration for consumers. Influencers generally receive products in advance of their launch in order to test them out. Their testing is then shown to the consumer who will develop an opinion which is influenced by the beauty influencer. Based on how many followers they have, credible influencers referred to as "Key Opinion Leaders" (KOL) are highly demanded by beauty retailers. Singers, actors, and other public figures (e.g., Z.TAO in China for Sephora) can also be influencers. Retailers' sales can increase when influencers recommend the product to their followers.

Selling optimisation using advanced pricing tools and omni-channel distribution



3. Optimising selling

Sales price is increasingly data-driven

The pricing for beauty products is increasingly based on extensive data analysis. Douglas, for example, uses data-driven programs such as price optimisation software from Revionics to make price adjustments in real time. It is crucial to understand how much money each customer segment is willing to pay for different product groups and brands.

This understanding depends strongly on the precise differentiation of each customer at different touchpoints (e.g. Google, review sites, banner ads, Facebook, Instagram). This makes it effective for the retailer to push personalized messages with product recommendations. Personalisation also incorporates the right distribution of special sales, promotional codes, gifts in form of free mini products, cakes or services such as photo shoots, and members-only bonus programmes in accordance with the amount, timing, and frequency of their purchases.

Products are distributed via omni-channel

In the past, a multi-channel approach has been perceived as a single online and offline presence. But smartphones and the exploding internet penetration have created a much more tech-savvy customer whose mobile and online purchases have increased rapidly in recent years. Beauty retailers began quite some time ago to combine product placement. Sephora combined its traditional and digital marketing divisions in 2013. In 2018, Sephora went even further by merging its in-store and digital retail teams to create one omni-retail department.

Omni-channel retailing combines mobile, brick-and-mortar and e-tailing, requiring retailers to rethink their business models. Convenience is the key in this context. Being available as a beauty retailer any time and anywhere, i.e., on all the media channels the target customer is using. It should be a seamless and preferably fully integrated user experience that puts the customer in the centre of all commercial channels and uses data generated from each channel to continuously improve the customer's experience. This requires significant development of the retailer's backend systems, its website, and its mobile app.



M&A trends

The following summarises the recent M&A transactions among beauty specialist retailers as well as health & beauty retailers. The common theme in this rather moderate M&A activity is mainly to expand into other markets acquiring established players (e.g., Douglas acquired Limoni & La Gardenia Beauty in Italy and Bodybell in Spain) or to invest into technology firms to attain the goal of an omni-channel presence (e.g., Ulta acquired QM Scientific, and Douglas acquired Parfümerie Akzente). In the future, we expect an increasing number of acquisitions based on the high fragmentation of the market throughout all regions. Acquisitions will mainly follow the same trends:

1. Expansion in home and new markets and **2. expansion of technological capabilities supporting an omni-channel approach.**

Selected M&A transactions by the global top 10 beauty specialist retailers

Year	Target name	Target Nation	Acquirer name	Acquirer nation	Transaction value (\$m)	Rationale
2020	Podrzhka (90%)	RU	L'Étoile	RU	<100	Expansion of footprint by ~250 stores in Moscow and the Moscow region as well as in St. Petersburg and other major cities in Russia
2019	Niche Beauty (51%)	DE	Douglas	DE	n/a	Expansion for exclusive, international cosmetics trend products in the luxury segment with a portfolio consisting of 6,000 products of 200 brands
2018	Parfümerie Akzente (majority stake)	DE	Douglas	DE	n/a	Strengthening of its European e-commerce business by acquiring the leading independent retailer of premium beauty products (parfumdreams)
2018	QM Scientific & GlamST (100%)	US	Ulta Beauty	US	n/a	Two technology companies (AI and AR) to evolve the customer experience with a strong technology emphasis across the business
2017	Limoni & La Gardenia Beauty (100%)	IT	Profumerie Douglas	IT	n/a	With LLG running the most extensive beauty and perfumery network in Italy, Douglas is strengthening its business in another core market in Europe
2017	H. Chalut (100%)	CN	Sally Beauty	US	8.8	Expansion of footprint in Quebec, Canada, with a 21-store professional-only distributor of beauty supplies
2017	Bodybell (100%)	ES	Douglas	DE	n/a	Expansion of business in Spain with one of the leading Spanish perfumery chains offering selective and mass beauty products
2017	Perfumerias IF (100%)	ES	Douglas	DE	n/a	Expansion of the Spanish business with strong presence in the North of Spain (103 stores) to achieve a better market position in this attractive region
2016	Ile de Beaute (100%)	RU	Sephora/	US	n/a	Increase of stake to become sole owner
2016	Peerless (100%)	US	LVMH	US	23.9	Stronger presence in the Midwestern region of the US through distributor of beauty products with 15 stores
2016	Ile de Beaute (65%)	RU	Sally Beauty	US	n/a	Entry into the Russian beauty and cosmetics market by acquiring a stake in one of the leading retailers

Selected M&A transactions by the global top 10 health and beauty retailers

Year	Target name	Target Nation	Acquirer name	Acquirer nation	Transaction value (\$m)	Rationale
2020	Cocokara Fine Inc. (100%)	JPN	Matsumoto Kiyoshi	JPN	n/a	Aiming at industry-leading position in the drugstore and pharmacy segment (final merger envisaged for 2021)
2019	Kosmolet A/S (100%)	DNK	Matas	DNK	21	Product expansion by adding a large make-up brands (Nilens Jord) in Denmark to the private label portfolio of Matas
2019	Niceshops GmbH (26%)	AUT	Müller ¹	GER	n/a	Acquisition in Austria's largest e-commerce group in order to expand Müller's omni-channel strategy towards higher online retail activities
2019	Drogaria Onofre (100%)	BRA	Raia Drogasil	BRA	n/a	Expanding drugstore footprint in Brazil with the 50 stores of Drogaria Onofre (held by CVS Health)
2017	Kozmo d.d. (100%)	HRV	Müller ¹	GER	n/a	Strengthening Müller's presence in the Croatian market by acquiring the drugstore chain Kozmo from the previous owner Konzum d.d., a Croatian retailer



1. Handels GmbH & Co. KG

Source: Mergermarket, Company publications, Deloitte analysis

Regional comparison of consumer preferences

Beauty retailers face different consumer preferences in the various regions considered in this report. A high-level examination of various studies (PiperJaffray, Third-i, Cosmetics Europe) reveals these differences.

European consumers consider cosmetics and personal care products an enhancement to their quality of life

According to research conducted among 4,000 consumers across 10 EU member states¹ in 2017, 71% of respondents stated that cosmetics and personal care products are important or even very important to them. In addition, 72% explained that these products improve their quality of life. The same opinion was provided across all age groups, and by a higher share of women. Respondents reasoned that personal care products provide them with a good health and personal hygiene which constitutes one of the most important factors of achieving a good quality of life. European consumers valued innovation as important for achieving product quality and efficacy. Their sources of information about quality and efficacy are primarily product packaging, websites, friends and family, and among the Gen Y and Z, social media was also mentioned.

American consumers between 20 and 40 years old count on online influencers and consider brick-and-mortar stores as “in”

An average American teenager spends \$318 per year on skin care, cosmetics and fragrances. Around 80% of this age group search for new beauty brands and trends with the help of online influencers. Approximately 65% use their friends as

a source and 33% consult beauty retailers directly. In addition, 90% of American teens prefer to shop in-store instead of online, exhibiting that brick-and-mortar stores of beauty retailers are actually an “in” place to linger. In Spring 2019, female American teens ranked Ulta and Sephora as their favourite beauty retailers.

Consumers in APAC countries, except for Australia, value brands and quality over price

In a 2016 survey conducted among 12,000 residents of the APAC countries, four out of five respondents said they valued brands and quality over price. This preference was particularly high in Indonesia. Hong Kong residents spend the most on cosmetics, with 29% spending at least \$130 per quarter. This spending amount is three times the regional average, as only 11% of all respondents spend more than this amount. The lowest spending was in the Philippines, with 74% of respondents spending less than \$40 per quarter.

Approximately 62% of the above respondents buy brands they trust rather than those that have been recommended. Around 40% of Chinese consumers purchase products that have been recommended by friends, relatives or colleagues, which is more than twice the regional average (19%). In regard to age, 70% of respondents over the age of 45 value brands that they trust over recommendations from third parties. Interestingly, 38% of women from APAC countries between the ages of 18 and 44 use skin whitening products. These products are very popular by beauty specialist retailers in the APAC region.

1. France, Germany, UK, the Netherlands, Italy, Spain, Denmark, Sweden, Poland, and Bulgaria.

Source: PiperJaffray, YouGov, Third-i, Cosmetics Europe, Deloitte analysis

Key contacts



Karsten Hollasch
Consumer Business Leader –
Deloitte DCE

Tel: + 49 211 8772 2804
Mob: + 49 177 8772 804
Mail: khollasch@deloitte.de



Silvio Ritz
Director Financial Advisory –
Consumer

Tel: + 49 211 8772 2635
Mobile: + 49 151 5807 2464
Email: siritz@deloitte.de



Dr. Daniel Wagner
Manager Financial Advisory –
Consumer

Tel: + 49 69 75695 6268
Mobile: + 49 151 5800 2054
Email: danwagner@deloitte.de



Nora Suthoff
Consultant Financial Advisory –
Consumer

Tel: + 49 69 75695 7275
Mobile: + 49 151 1829 4736
Email: nsuthoff@deloitte.de



Sandeep Gill
Global Financial Advisory and
M&A Leader - Consumer

Tel: + 44 (0) 20 7303 3325
Mobile: + 44 (0) 7768 530 482
Email: sandeepgill@deloitte.co.uk



Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as "Deloitte Global") does not provide services to clients. Please see www.deloitte.com/de/ueberUns for a more detailed description of DTTL and its member firms.

Deloitte provides audit, tax, financial advisory and consulting services to public and private clients spanning multiple industries; legal advisory services in Germany are provided by Deloitte Legal. With a globally connected network of member firms in more than 150 countries, Deloitte brings world-class capabilities and high-quality service to clients, delivering the insights they need to address their most complex business challenges. Deloitte's more than 220,000 professionals are committed to making an impact that matters.

This presentation contains general information only, and none of Deloitte Consulting GmbH or Deloitte Touche Tohmatsu Limited ("DTTL"), any of DTTL's member firms, or any of the foregoing's affiliates (collectively, the "Deloitte Network") are, by means of this presentation, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. In particular this presentation cannot be used as a substitute for such professional advice. No entity in the Deloitte Network shall be responsible for any loss whatsoever sustained by any person who relies on this presentation.

© Deloitte LLP and affiliated entities.

Created by Core Creative Services. RITM0877765