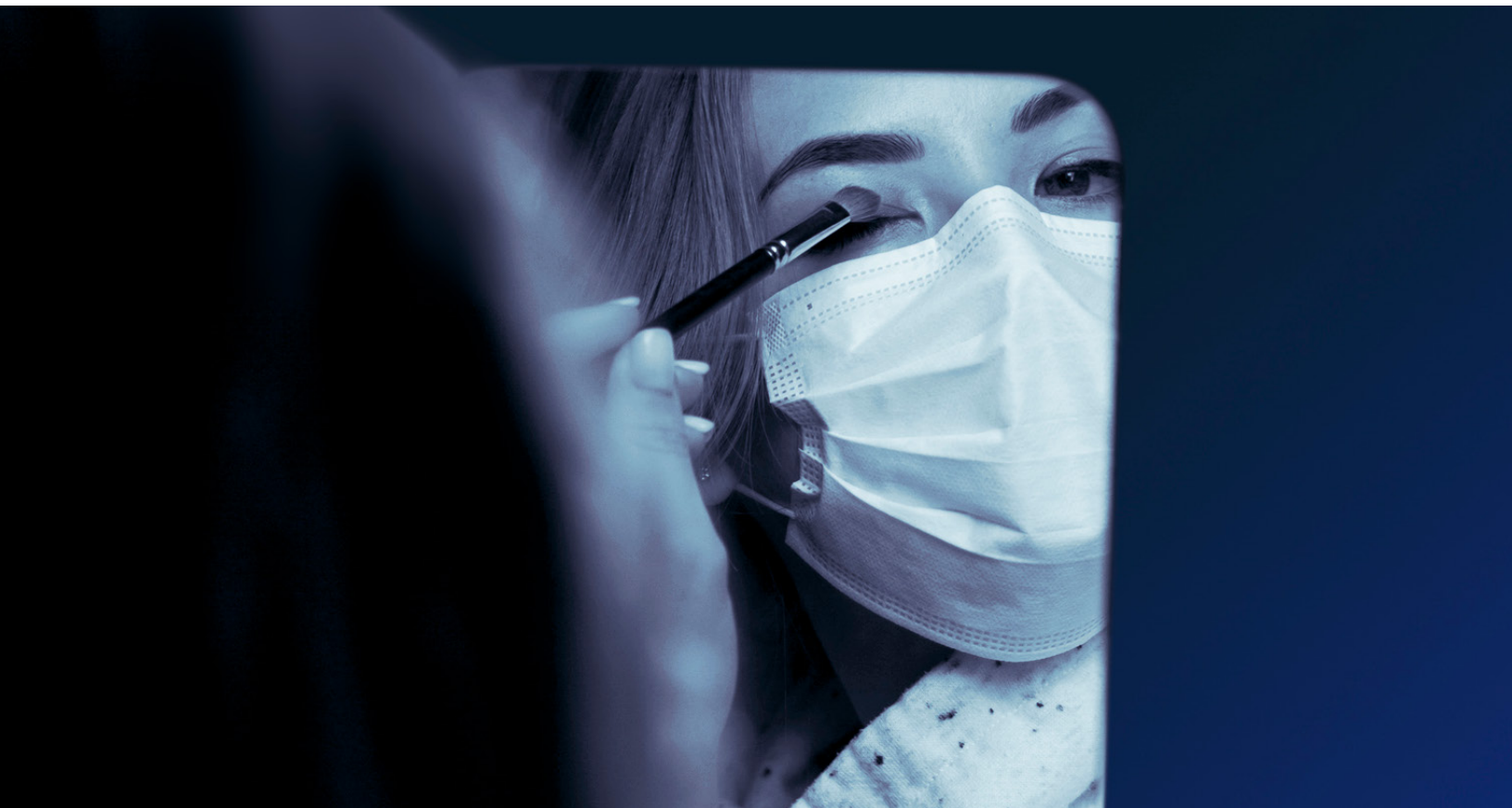


Consumer Packaged Goods Practice

How COVID-19 is changing the world of beauty

The beauty industry has been resilient in the past. Could this crisis have a different outcome?

by Emily Gerstell, Sophie Marchessou, Jennifer Schmidt, and Emma Spagnuolo



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The global beauty industry (comprising skin care, color cosmetics, hair care, fragrances, and personal care) has been shocked by the COVID-19 crisis. First-quarter sales have been weak, and there have been widespread store closures.

The industry has responded positively to the crisis, with brands switching their manufacturing to produce hand sanitizers and cleaning agents and offering free beauty services for frontline response workers. At the same time, the industry's leaders have a responsibility to do their best to ensure that their companies survive. The global beauty industry generates \$500 billion in sales a year and accounts for millions of jobs, directly and indirectly. Lives come first, but livelihoods also matter.

This article examines the likely effects of COVID-19 on the beauty industry over the next three to six months. Then it explores how the crisis could fundamentally change the industry in the long term—and how retailers, strategic players, and investors can adapt. In many cases, it draws from the results of a McKinsey Global Consumer Sentiment Survey that took place in early April.

The short-term outlook for the beauty industry

Beauty may be in the eye of the beholder, but there is little debate when it comes to the long-term attractiveness of the global beauty industry. Not only has it grown steadily, it has created generations of loyal consumers. During the 2008 financial crisis, spending in the industry only fell slightly and fully bounced back by 2010 (Exhibit 1).

Even though the economic magnitude of the COVID-19 pandemic on brands and retailers will be far greater than any recession, there are signs that the beauty industry may once again prove relatively resilient. In China, the industry's February sales fell up to 80 percent compared with 2019. In March, the year-on-year decline was 20 percent—a rapid

rebound under the circumstances. In a variety of markets, consumers report they intend to spend less on beauty products in the near term (largely driven by declines in spending on color cosmetics) but more than they will in other discretionary categories, such as footwear and clothing (Exhibit 2). Noting the uptick in lipstick sales seen during the 2001 recession, Leonard Lauder of the European cosmetics family coined the term “lipstick index” to describe this phenomenon. The principle is that people see lipstick as an affordable luxury, and sales therefore tend to stay strong, even in times of duress.

McKinsey has explored nine scenarios for the economy over the next few years, based on epidemiological trends and the effectiveness of economic-policy decisions. Based on the scenarios most expected by global executives and current trends, we estimate global beauty-industry revenues could fall 20 to 30 percent in 2020. In the United States, if there is a COVID-19 recurrence later in the year, the decline could be as much as 35 percent (Exhibit 3).

We looked at the beauty industry's recovery against each scenario, considering two key factors: where and how beauty products are being sold and what is being purchased.

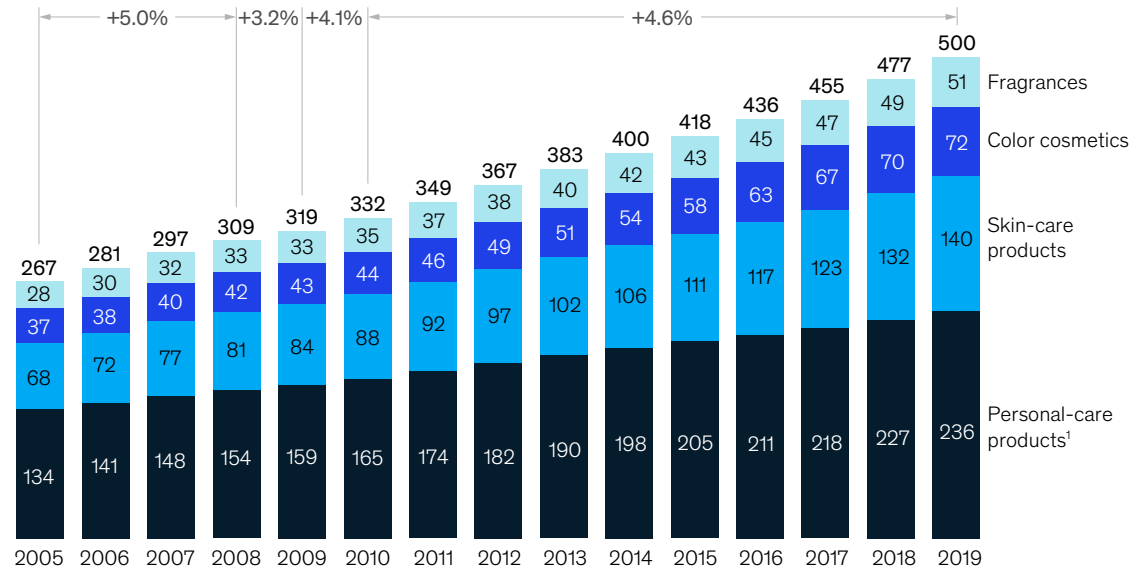
Where and how beauty products are being sold

In most major beauty-industry markets, in-store shopping accounted for up to 85 percent of beauty-product purchases prior to the COVID-19 crisis, with some variation by subcategory. Even online-savvy American millennials and Gen Zers (those born between 1980 and 1996) made close to 60 percent of their purchases in stores (Exhibit 4). With the closure of premium beauty-product outlets because of COVID-19, approximately 30 percent of the beauty-industry market was shut down. Some of these stores will never open again, and new openings will likely be delayed for at least a year.

Exhibit 1

The global beauty-industry market has been consistently resilient.

Global beauty-industry retail sales, \$ billion



Note: Figures may not sum to listed totals, because of rounding.

¹ Includes bath, hair-care, men's shaving, oral-care, shower, and adults' sun-care products; deodorants; and depilatories.

Source: Euromonitor

Here are several ways beauty-product sales are changing:

- **Increased online sales are not offsetting the decline in in-store sales.** Some beauty-product brands and retailers with inventory and shipment operations ready to scale up are reporting e-commerce sales twice as high as their pre-COVID-19 levels. Overall, we think 20 to 30 percent growth will be more typical. Sephora's US online sales are reportedly up 30 percent versus 2019;¹ as were Amazon's beauty-product sales for the four-week period ending April 11. In China, McKinsey research has seen online revenues for beauty-industry players rise 20 to 30 percent

during the outbreak. These figures are in line with what beauty-product consumers are reporting in McKinsey COVID-19 Consumer Pulse Surveys.

- **Beauty-product sales at essential retailers are down.** While brick-and-mortar drugstores and mass-market and grocery stores remain open, their customer traffic and revenues have plummeted. The Boots UK drugstore chain reported its overall sales fell by two-thirds between March 25 and April 3, 2020, with beauty-product revenues contributing to the decline. Surveyed UK consumers say they expect to spend around 50 percent less on beauty products than usual in the next two weeks.

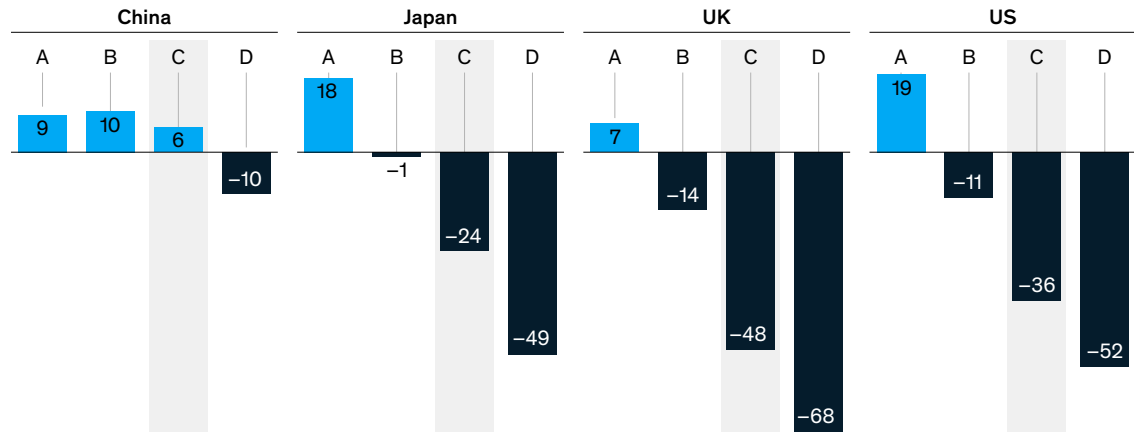
¹ Priya Rao, "How Sephora is incubating the 'next guard' online," Glossy, April 14, 2020, glossy.co.

Exhibit 2

Global consumers intend to spend less on beauty products, but other categories could fare even worse.

Expected spend per category over next 2 weeks compared with usual, net intent¹

A Groceries B Personal-care products C Skin-care products/makeup D Apparel



¹Net intent calculated by subtracting % of respondents stating they expect to decrease spend from % of respondents stating they expect to increase spend. Question: Over the next 2 weeks, do you expect that you will spend more, about the same, or less money on these categories than usual?

Source: McKinsey COVID-19 Consumer Pulse Surveys, results sampled and weighted to match general population aged ≥18 years: Apr 15–19, 2020, in China (including Hubei province) (n = 1,896); Apr 17–19, 2020, in Japan (n = 600); Apr 18–19, 2020, in UK (n = 1,005); Apr 20–26, 2020, in US (n = 1,484)

- **China shows the return to in-store shopping could be slow and differentiated.** Despite store reopenings in China starting the week of March 13 and reports of “revenge spending,” sales have not fully bounced back. As of mid-April, 90 percent of drugstores, supermarkets, beauty-product specialty retailers, and department stores in China had reopened. However, depending on the sector and type of store, traffic remains down 9 to 43 percent compared with pre-COVID-19 levels. Mall-based stores have proven slower to recover. Even after reopening, around 60 percent of large malls in China report a 30 to 70 percent decrease in sales, year on year, in the first quarter of 2020.
- **Retailers and brands are turning to promotions to bring in consumers and clear inventory.** In an uncharacteristic move, several prestige brands

are offering discounts online of up to 40 percent, competing with specialty beauty-product and department stores to capture promotion-oriented consumers. Promotions also help move unsold seasonal inventory. As beauty-product brick-and-mortar stores reopen, we expect to see more promotions aimed at reclaiming customer foot traffic.

Which beauty products are being purchased

Given the realities of working from home, physical distancing, and mask wearing, it has become much less important to wear makeup and fragrance. For prestige brands, we see 55 and 75 percent declines in cosmetic and fragrance purchasing, respectively, versus a year ago. When consumers do return to work, many will continue to wear masks, further slowing makeup's recovery. One possible exception is above-the-mask treatments. In China,

Exhibit 3

If there is a COVID-19 recurrence later this year, US beauty-industry revenue could fall by as much as 35 percent.

Monthly beauty-product sales compared with 2019, %¹



¹ Estimate based on McKinsey economic-impact scenario A1 (virus recurrence).

Source: Daxue Consulting; Earnest Research; National Electronic Disease Surveillance System Base System; "Safeguarding our lives and our livelihoods: The imperative of our time," Mar 2020, McKinsey.com; McKinsey COVID-19 US Consumer Pulse Survey, Mar 16–17, 2020; McKinsey analysis

Alibaba reported eye-cosmetic sales increased 150 percent, month over month, during the week of February 18, 2020.²

By contrast, skin-care, hair-care, and bath-and-body products appear to be benefiting from self-care and pampering trends. NPD, which tracks consumer spending and point-of-sale data, recorded that sales of luxury hand soap in France were up 800 percent the week of March 16, 2020, as the country went into lockdown.³ Zalando, Europe's largest fashion and lifestyle e-commerce marketplace, reported a boom in pampering and self-care beauty categories, including candles, aromatherapy, and detox products; sales of skin-,

nail-, and hair-care products were up 300 percent, year on year.⁴ That is consistent with results from Amazon, for which most makeup sales in the United States are showing slight declines, compared with the same month in 2019, while sales for nail-care products (218 percent), hair coloring (172 percent), and bath-and-body products (65 percent) are way up (Exhibit 5).

Another notable trend is the rise of do-it-yourself (DIY) beauty care. Many beauty salons have closed, and even in places where they have not, consumers are forgoing services because of concerns about close physical contact. In addition, many consumers will likely face economic difficulties after the

² Christine Chou, "Huda Beauty catches the eyes of Chinese consumers," Alizila, March 30, 2020, alizila.com.

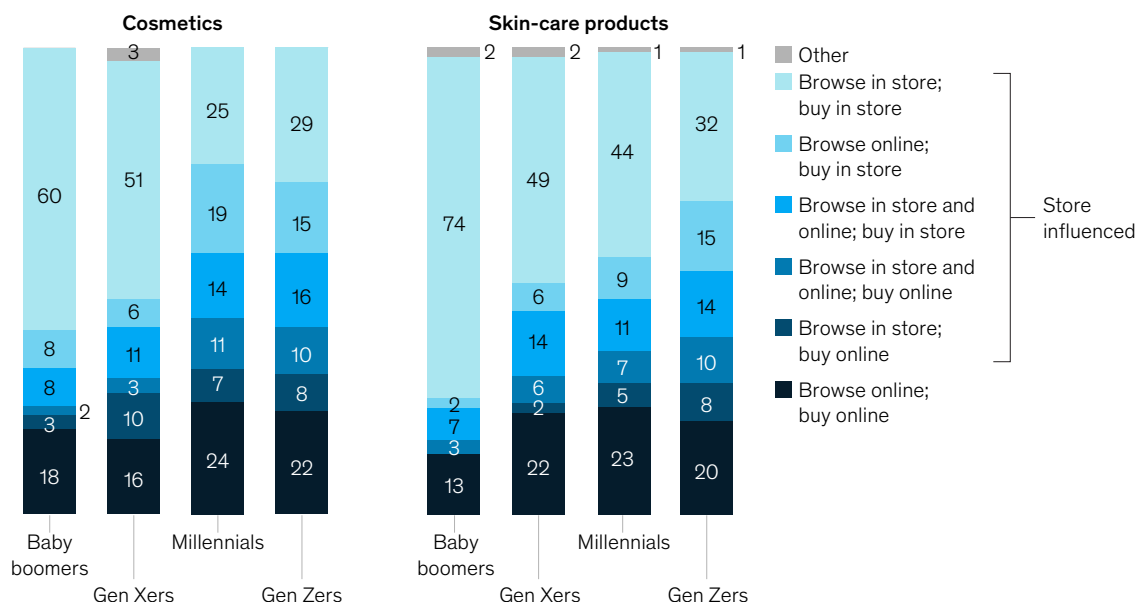
³ "Confinement: Mauvaise passe pour les produits de beauté haut de gamme ... à deux exceptions près [in French]," Fashion Network, April 10, 2020, fr.fashionnetwork.com.

⁴ "What Zalando customers are buying as they're asked to stay home," Zalando, April 16, 2020, corporate.zalando.com.

Exhibit 4

Some beauty-product sales are shifting online, but the store still has a critical role to play.

Shopping habits, by age group, % of respondents¹



Note: Figures may not sum to 100%, because of rounding.

¹ Question: How do you purchase [cosmetics and skin-care products] most often? (n = 10,000).

Source: McKinsey New Age of the Consumer Generational Survey 2019

COVID-19 crisis, given the loss of jobs and savings. In McKinsey's survey of UK consumers, 66 percent believe their finances will be affected for at least two months because of COVID-19, and 36 percent say they are cutting back on spending.

As a result, DIY hair coloring, nail care, and care in other beauty categories are finding new customers. In the United States, Nielsen reported rises in the sales of hair dye and hair clippers by 23 and 166 percent, respectively, in the first week of April 2020 versus a year ago.⁵ Sales of Madison Reed at-home hair-coloring kits rose tenfold from mid-March to mid-April.⁶ In the United Kingdom, online sales of

prestige-brand nail polish have seen double-digit growth every week since lockdown began in March. This surge in DIY nail care has some speculating that the current crisis's lipstick effect has an added dimension—the "nail-polish effect."⁷

The long-term impact of COVID-19 on the beauty industry

Some changes resulting from the COVID-19 crisis are likely to be permanent. Here are three areas in which the pandemic could alter the beauty industry in fundamental ways:

⁵ Alicia Wallace, "Walmart CEO says we're in the 'hair color' phase of panic buying," CNN Business, April 11, 2020, cnn.com.

⁶ Megan Cerullo, "Sales of hair-dye kits jump as stuck-at-home workers cut off from salons," CBS News, March 27, 2020, cbsnews.com.

⁷ Sandra Halliday, "Nail care is the UK's 'lipstick effect' in Covid-19 crisis, French brands benefit," Fashion Network, April 8, 2020, us.fashionnetwork.com.

Exhibit 5

Do-it-yourself and self-care beauty products are growing quickly in the United States.

■ Do-it-yourself and self-care products

Beauty-product category	Estimated year-to-date sales, \$ million	Average price, \$	Year-over-year change, 2019–20, 4 weeks ending April 11		
			Retail sales, %	Average price, %	Retail sales, \$ million
Body wash, soap, and lotion	321	14.10	65	-11	44
Nail care	123	15.02	218	16	37
Hair care	540	18.43	27	-12	33
Men's grooming	240	25.44	56	6	28
Skin care	540	18.17	20	-14	27
Hair coloring	58	13.64	172	-3	17
Women's hair removal	74	16.15	53	-14	9
Eye makeup	82	12.30	5	-12	1
Face makeup	77	13.87	-3	-21	-1
Lip care and color	55	8.97	-15	-28	-2
Beauty tools, devices, and accessories	316	16.60	-7	-15	-6
Total beauty products ¹	2,632	N/A	28	N/A	172

Note: From Amazon results.

¹ Includes fragrances and sun-care and tanning products.

Source: Stackline

- **Digital continues to rise.** Pre-COVID-19 trends will likely accelerate, with direct-to-consumer e-commerce, such as brands' websites, shoppable social-media platforms, and marketplaces becoming more important. Across the globe, consumers indicate they are likely to increase their online engagement and spending. Beauty-industry players will need to prioritize digital channels to capture and convert the attention of existing and new customers. On the operations side, the use of artificial intelligence for testing, discovery, and customization will need to accelerate as concerns about safety and hygiene fundamentally disrupt product testing and in-person consultations.
- **The pace of innovation accelerates.** As the COVID-19 crisis has shown, the world can change quickly, bringing substantial shifts in demand. Sometimes, supply cannot catch up. Even before the pandemic, brands were under pressure to overhaul their product-innovation pipelines, inspired by the ability of digital-native direct-to-consumer brands to go from concept to cupboard in less than a month. Now, the need for speed is even greater. To achieve it, there may be a greater role for contract manufacturers, both to diversify (and thus reduce production risks) and to serve as thought partners in product innovation. There is also potential for closer collaboration—among brands and

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retailers, in particular—through data sharing and inventory pooling.

- ***M&A rises as multiples fall.*** With the COVID-19 crisis causing significant damage to the balance sheets of brands, retailers, and suppliers, many companies will need to find new sources of capital. At the same time, given the hits to revenues and the global economy, multiples could fall from precrisis levels, when some brands were trading for more than eight times revenue or 10 to 15 times earnings.

While the beauty industry may be in a relatively stronger position than other consumer categories, 2020 will be one of the worst years it has ever endured. We believe, however, that the industry will remain attractive in the long run. The COVID-19 crisis is likely to accelerate trends that were already shaping the market, such as the rise of the global middle class and the use of e-commerce, rather than mark entirely new ground. Consumers across the globe are showing by their actions that they still find comfort in the simple pleasures of a “self-care Sunday” or a swipe of lipstick before a Zoom meeting.

Even before the pandemic, the definition of “beauty” was becoming more global, expansive, and intertwined with individuals’ sense of well-being. The COVID-19 crisis is not likely to change these trends—and in that, there is reason for hope.

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