

CHINA 2014

A NEW ERA IN CONSUMPTION

nielsen | 尼尔森

About Nielsen

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INTRODUCTION

Welcome to the dawn of the niche-growth era in China.

The mass-growth era, which featured year after year of double-digit GDP growth, is no longer a key theme of Chinese economic growth. Instead, what we see now is a more stable and healthy growth as an outcome of government adjustment.

As China becomes a more mature market, with 7.6 percent GDP growth in 2013 and an expectation of a similar rate for 2014, opportunities are arguably as plentiful as they ever were – if you know where to look.

In fact, from a consumer perspective, we are ushering in a new age: As China shifts away from an investment-led economic model to one driven by the population at large, consumers are taking the reins on consumption.

The country is in the midst of a massive recalibration with considerable opportunity for smart, agile competitors who keep up with the transformative changes to come.

It's time to take a master class on Chinese consumers – to really understand them – in order to compete and win in this new era.



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LESSON 1:

THE POWER OF FUTURE TIER 1 CITIES

Bigger is not always better.

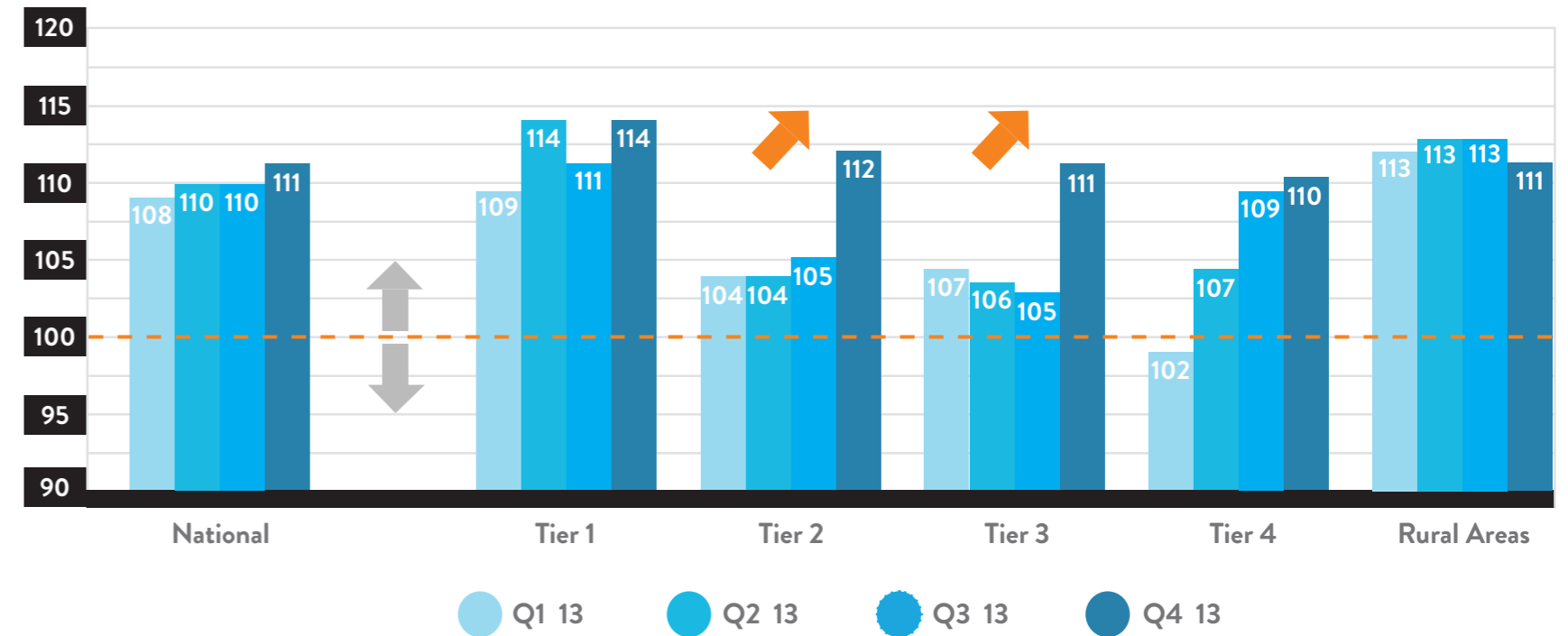
Look beyond the big prizes to find real value right now: It's the up-and-comers, those just beneath the Tier 1 cities, that are offering the greater opportunity.

Consumer confidence is surging in Tier 2 and Tier 3 cities: up seven and six index points, respectively, in a single quarter (between Q3 and Q4 of 2013).

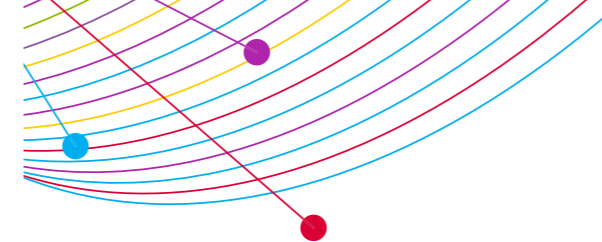
When you look at the numbers that make up the consumer confidence index score, Tier 2 and Tier 3 consumers reported a healthy boost in their willingness to spend (up 15 percentage points in Tier 2 and 7 percentage points in Tier 3); personal finances; and particularly job prospects (up 10 percentage points each, in Tier 2 and Tier 3).

CONFIDENCE SOARS IN TIER 2 AND TIER 3 CITIES

Consumer Confidence by City Tier



Source: Nielsen Q4 2013 China Consumer Confidence Report



Combining these trends with projected population changes, it's clear that the cities headed for Tier 1 status are poised to be the new powerhouse of the Chinese economy.

These demographic changes are hitting at an interesting time because they intersect with the broader trend of premiumization.

As you already know, today's Chinese consumers are growing more individualistic than their parents. They are looking for products that are new, exciting, and offer convenience for their busy lives. With higher levels of disposable income, they're striving for a better quality of life, and they enjoy the feeling of indulgence. They are upgrading.

What's different now? The playing field is changing, and it's transforming the game.

The growth, optimism and buying power of Tier 2 and Tier 3 cities are accelerating the premiumization trend into a scale never seen before in China.

Companies that understand these changes have a definite advantage in unlocking growth. Whether it's FMCG (fast-moving consumer goods), autos or other durables, it's all about serving personalized, customized needs with new products and product upgrades.

GROWTH, OPTIMISM, AND BUYING POWER





LESSON 2:

LOOK FOR GROWTH DRIVEN BY INDIVIDUAL CONSUMERS

At the core of sustainable growth is the shift from an export/investment-driven economy to one driven by personal consumption.

In 2008, domestic consumption made up about 35 percent of growth. Today, it makes up 50 percent.

There has been a transformation beginning over the past two years: It's not only the government driving consumption. It's individual consumers.

The trend is clear – as is the opportunity for those who get in front of it before that number reaches 60 percent or 70 percent.

Consumer confidence is another piece of this equation. Overall, China ended 2013 on an historic high index score of 111, with trend lines going up on job prospects and willingness to spend.

How will those willing spenders divide up their budgets?

The key to unlocking growth is to remember the importance of individualization in consumption. If we think about consumers' needs – from functional to emotional, from basics to self-realization – quality and safety are the primary concerns.

Other consumption trends to remember:

- **Advanced technology can justify a premium price, especially among early adopters and trendsetters.**
- **Gifting is a key driver of consumption, as part of the culture of paying respect, filial piety and favor exchange. It is a vehicle for expressing identity – and premium products have an edge with these purchases.**
- **Self-reward is a strong motivator for premium purchases, as consumers satisfy a need for indulgence**

This is a proven approach – so what is new here? Again, as in Lesson 1, the game is changing.

As China recalibrates toward a consumer-led economy, there are plenty of wins to be had for those who rethink their approach.



LESSON 3:

HEALTH AND ENVIRONMENTAL CONCERNS ARE EVOLVING

Health concerns have been a driver of purchasing behavior for some time.

Nielsen's Global Survey on Saving and Investment Strategies shows that 64 percent of Chinese respondents are actively saving for future potential health issues, compared to 34 percent who plan to save in the future. The survey was conducted in August and September 2013, but the results reflect a wider phenomenon.

These concerns can prompt consumers to pay more for better products, such as infant formula, healthy food products, and most notably health supplements.

In the past three years, health supplements have moved to the top of the gifting list during Chinese New Year, overtaking fruits, liquor and tobacco. Average spending on health supplements in big cities is seven times that of other over-the-counter products.

We can see this trend spreading beyond Tier 1 cities, with consumers in Tier 2 and Tier 3 cities more concerned with personal health for the first time.

Just as health and wellness concerns can spread to new population groups, the range of concerns is also expanding.

For example, take a look at new sentiment about environment-friendly cars. The pervading belief was that price will keep Chinese consumers from caring about environmental concerns when it comes to autos.

However, this too is changing:

- **Nielsen findings indicate a growing desire for green vehicles, with purchase intention rising from 15 percent in 2012 to 29 percent in 2013. In particular, intentions rose for gasoline hybrids (from 10% to 19%); diesel hybrids (2% to 5%); and plug-in hybrids (1% to 4%).**
- **Reasons for such demand growth are mixed: Lower fuel cost and environmental friendliness are the top two reasons for consumers to consider a green vehicle. Increased traffic and air pollution concerns are further shifting consumers' interest from conventional vehicles to green ones.**



LESSON 4:

POLARIZATION OF CHANNELS - GROWTH IN BOTH E-COMMERCE AND TRADITIONAL TRADE

E-commerce has been a fast-growing channel, and will continue to be so – as modern trade, particularly hypermarkets, try to counter with an increased online presence of their own.

In addition to the digitalization of channels, we still see strong growth in traditional trade. Even though modern trade is growing, traditional trade will continue to be an important part of the retail landscape – serving millions in lower-tier cities with rising incomes who are looking for places to spend their money.

Both traditional trade, best represented by self-service grocery stores, and e-commerce are continuously to grow in lower-tier cities, filling gaps from modern trade and meeting consumers' increasing demand. Lower-tier cities have yet to see large-scale, organized modern trade development.

Compared with offline, retail sales via the emerging online channels have been growing rapidly in China over the past few years.

And smaller-format, specialty modern trade stores are pulling customers away from hypermarkets. At specialty stores for young mothers, sales of infant formula grew 15 percent in the last 12 months. During the same period, skin care product sales jumped 23 percent at cosmetic stores.

LOWER-TIER CITIES HAVE YET TO SEE LARGE-SCALE, ORGANIZED MODERN TRADE DEVELOPMENT



LESSON 5:

MOBILE TAKES A HUGE LEAP

Smartphone penetration among mobile users in China jumped to 72 percent in 2013 – up from 50 percent just one year ago.

This trend extended beyond the Tier 1 and Tier 2 cities, with high penetration rates in Tier 3 and Tier 4 cities as well as less dense urban areas. Among white collar workers and students, penetration percentages are in the high 80's. And even farmers are making the switch: with about one-third choosing smartphones.

Android is the OS Leader



How are consumers using their smartphones? Sending messages and consuming content are the top uses.

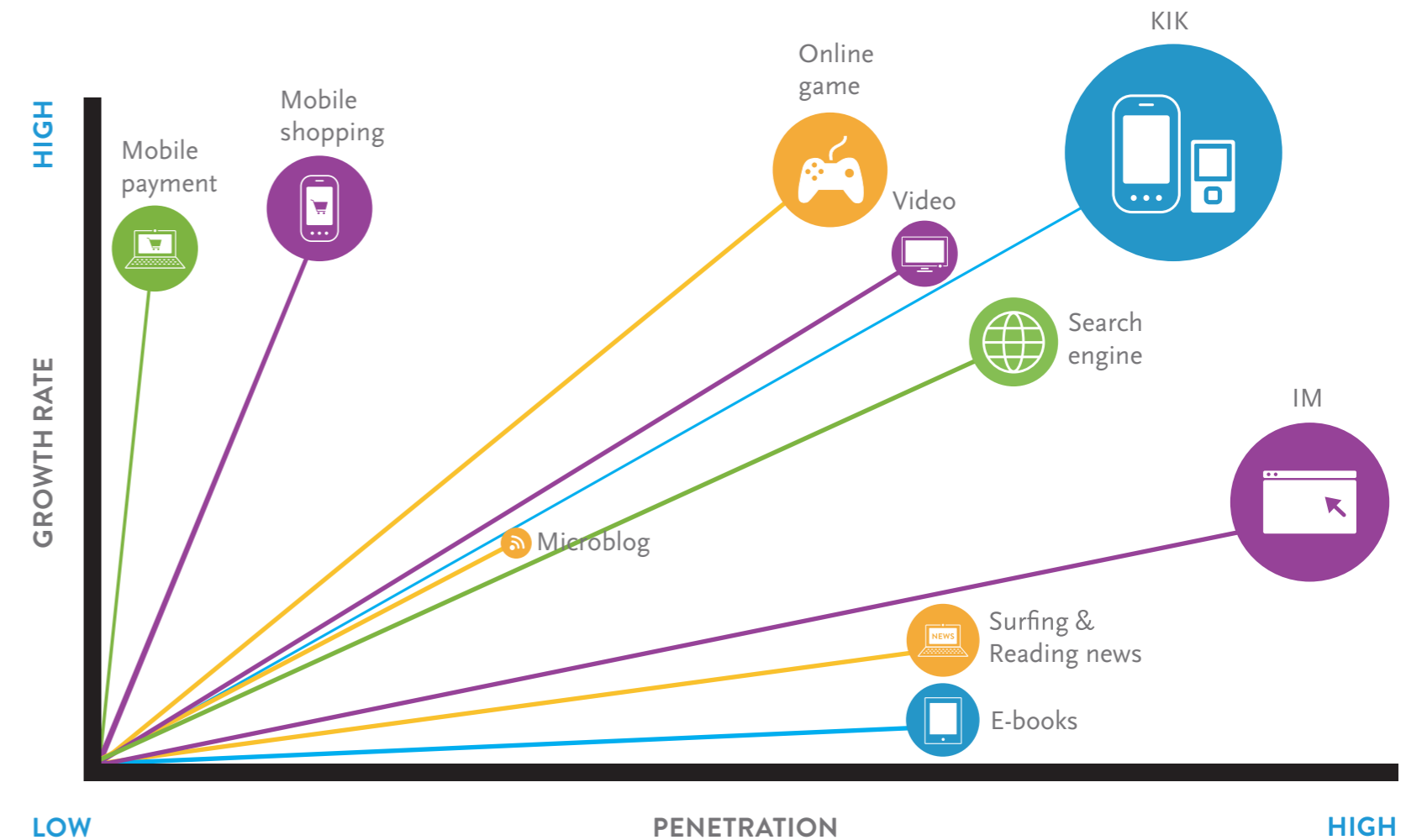
WeChat, an instant-message app launched by Tencent in January 2011, already has more than 600 million registered users, making it one of the fastest-growing new applications in China's Internet history. The penetration of WeChat among Chinese consumers surpassed 30 percent in 2013, with a year-on-year growth rate of more than 1,000 percent.

Born as a communication tool and viewed as a mobile Facebook-type platform, WeChat has begun to move into Weibo's territory as WeChat has been leveraged more and more as an owned media platform. Companies use it to extend their reach to more among Chinese consumers through official WeChat accounts, as they did with Weibo.

In addition to being avid mobile communicators, Chinese consumers show a distinct openness toward mobile payments.

They have the highest level of confidence around the world in using payment cards on a mobile device, according to *Nielsen's Global Survey on Saving and Investment Strategies*. More than 70 percent of Chinese respondents said they felt comfortable shopping online and using their payment cards on either a smartphone or a tablet, as long as their personal information is protected.

THE MOBILE GROWTH LANDSCAPE

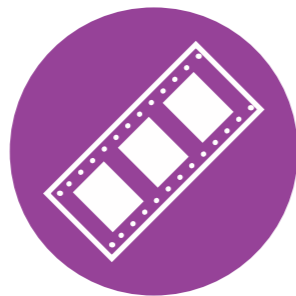


Nielsen research on mobile users in China in Q4 2013 (2,000 samples).
Interview methodology: CATI (computer-aided telephone interview).

Third-party payments are a key area of growth – whether through “Alipay” (affiliated to one of China’s most influential e-commerce sites) or via social media platforms such as Tencent’s WeChat.

The trend is picking up speed. Tencent’s recent “red envelope” campaign – which enabled users to send a mobile version of a traditional cash gift in a red envelope – was the hottest game among Chinese mobile consumers during the 2014 Spring Festival. Tencent said 75 million “red envelopes” were sent on January 30 and January 31 using cards linked to WeChat payment accounts.

Mobile is also turning big city taxis into battlegrounds, with Alibaba and Tencent offering incentives to both drivers and customers to use their apps, as a way to expand Alipay and WeChat bases.



LESSON 6:

MEDIA LANDSCAPE CONTINUES TO SHIFT

Television is undoubtedly the biggest player, dominating ad spend and enjoying double-digit growth right now.

But online's influence is growing, and social media – in a country where the WeChat platform alone has 600 million users – has become a powerful tool for engaging with consumers.

Year-over-year growth in the overall advertising market reached 9.8 percent in 2013, compared to 0.9 percent in 2012.

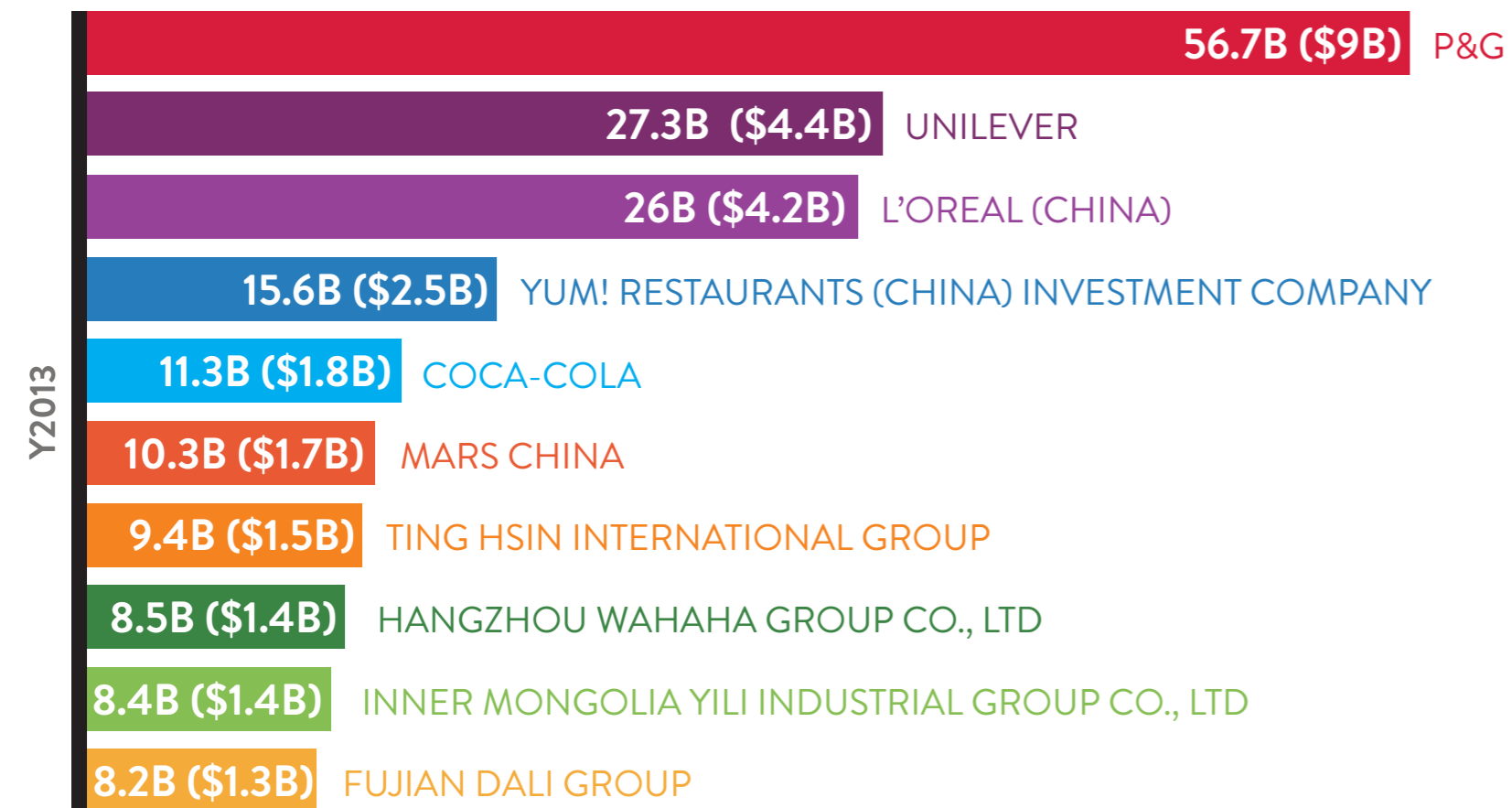
Among the four traditional advertisement formats, television remains the leader with 12.3 percent growth in 2013. It is also the only traditional advertisement format whose year-over-year growth rate surpasses the overall market. Radio grew slightly, at 3 percent, while ad spend for magazines and newspapers declined 1 percent and 9 percent, respectively.

TV spending is expected to continuously grow, however at a more modest rate of single to lower double-digit growth, while online will grow at an average of 30 percent to 40 percent per year. Current Internet penetration is 45.8 percent, with 618 million Internet users in China.

**GROWTH OF THE OVERALL
ADVERTISING MARKET
REACHED 9.8% YOY IN 2013,
COMPARED TO 0.9% 2012**

TOP 10 ADVERTISERS IN 2013

Over the past decade, multinational fast-moving consumer goods giants like Procter & Gamble, Unilever, Coca-Cola and L'Oreal have been perennially atop the list. But local giants like state-owned carrier China Unicom and privately owned Hangzhou Wahaha Group are catching up to the multinationals. And local pharmaceutical companies are also heavy ad spenders – best represented by Harbin Pharmaceutical Group.



Source: Nielsen CCData

* Values listed in RMB and USD

** Value is based on the rate card rate. Real spending may be lower.

As for mobile, even though China has the most mobile users in the world, the market for mobile advertising has not yet become a reality. Industry estimates indicate that the growth rate will be high over the next two years, but ad spend will remain relatively small.

However, the influence of social media – powered by mobile – is already sizable. And it's growing.

The rapidly changing social media environment in China, best represented by Weibo and WeChat platforms, is creating opportunities for marketers to engage with consumers – making the coming years a crucial era as social media opens up doors for brands.

For social success in China:

- **Make your content and format mobile-friendly, and leverage the platform for your marketing activities. Social media is going commercial.**
- **Use third-party influence to leverage key opinion leaders to raise your digital reputation.**
- **Go beyond city tiers to customize your social strategy for different priority audiences: Social media is increasingly fragmented and location-based.**
- **Leverage the power of Chinese Internet culture by working from the grassroots level to best connect with your consumers.**



LESSON 7:

LOOK TO THE YOUNG – AND THE OLD

Chinese consumers consistently rank among the most avid savers in the world.

But the desire to save competes with the desire to provide for children's needs. With a new family planning policy on the horizon, there may be fewer one-child families – and more mouths to feed.

Spending on children's education ranked in the top three uses of spare cash, according to *Nielsen's Chinese Consumer Confidence and Spending Intentions Report* for Q3 and Q4 of 2013.

Meanwhile, *Nielsen's Global Survey on Saving and Investment Strategies* shows that nearly half of Chinese respondents (49%) are actively engaged in saving for their children's future (including both education and other living expenses), exceeding the global average of 34 percent. For those who are currently saving, 16 percent allocated the highest contribution each month for achieving this goal.

Similarly, caring for the growing aging population presents another strain on most families' budget.

China is predicted to be the world's most aged society by 2030, with a higher proportion of people above the age of 65 than anywhere else in the world, according to a Chinese Academy of Social Sciences report. In 2010, people over age 60 made up 12 percent of the population. By 2050, that number is expected to jump to more than 30 percent.

Brands that can leverage the desire to provide for China's children and its aging population may be able to tap into those healthy savings accounts.

CHINA COULD BE THE WORLD'S MOST AGED SOCIETY BY 2030



LESSON 8:

BANKING AND FINANCE NAVIGATE CHANGING WATERS

The financial industry has more information about its customers than ever.

How can they use this knowledge to connect with current customers and market effectively at the same time?

This question becomes more urgent with the recently announced reform to deregulate state-owned banks: Competition is only going to intensify.

With many more banking channels available today, consumers are engaging across multiple points. If it's not seamless, they may seek other providers.

To fuel growth, it is crucial to navigate consumers' needs:

- **Match the right consumer with the right products, whether it's through cross-selling or acquiring new customers.**
- **Look at which touchpoints can emotionally connect and build loyalty with customers, and execute your strategies flawlessly.**
- **Think digital – especially mobile.**

There is no question, e-commerce is beginning to penetrate the finance industry.

E-commerce companies are now providing some Internet financing solutions, and are luring customers away from credit cards and banks. With Alibaba and Tencent, for instance, consumers are transferring money through e-commerce where they can earn higher interest.

Another major trend is mobile payment, with traditional banks offering mobile banking through apps.

Last year's Nielsen Mobile Insight Survey showed that the average monthly spend via mobile payments was 737 RMB (\$120 USD).

Considering that 62 percent of mobile users still worry about the security of mobile payments, mobile payments have not even tapped half the market. As security worries fade, huge growth is possible.

WEALTH MANAGEMENT ON THE RISE

Rising income levels are driving demand for diverse investment and financing. In 2013, the average disposable income of Chinese urban residents surpassed 26,955 RMB (\$4,389 USD), with annual growth of 9.7 percent.

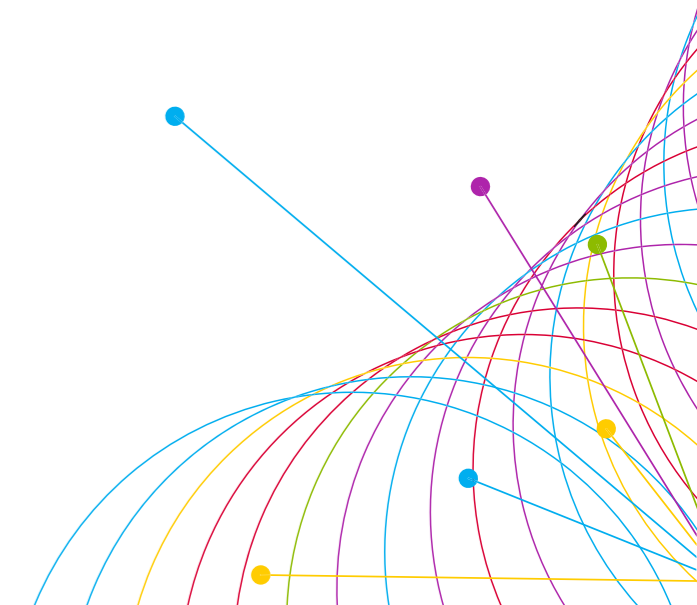
By 2012, 18 of China's banks had begun offering comprehensive financial services for the growing number of consumers with high net worth, including private banking.

Over the past two years, the penetration rate of almost every category of personal finance products has increased.

In terms of goals, nearly 10 percent of those with a high net worth (whose investment assets are valued between \$1 million and \$6.5 million USD) put "property inheritance" as their top goal for wealth management, according to a report from China Minsheng Bank. There is also interest in collection, estate, futures and overseas investment.

Affluent consumers are also heavy credit card users. The penetration rate among mass consumers is 49 percent, compared to 87 percent among wealthy consumers – and well-off clients' plastic spending is 2.5 times that of mass consumers.

RISING INCOME LEVELS ARE DRIVING DEMAND FOR DIVERSE INVESTMENT AND FINANCING





LESSON 9:

THE AUTO INDUSTRY'S GENERATION GAP

As more post-80s and post-90s generations become car buyers, the auto industry is adjusting to seismic changes in its customer base.

First-time buyers today are different than their now-middle-aged counterparts were when they bought their first cars. The new generational shift brings a pivot away from a sole focus on practicality and performance.

The post-80s and post-90s generations appreciate design and individualized features. They view their car as an extension of their identity – their personal space and a tool for their social lives – and they appreciate the newest technology.

In addition to generational issues, the customer base is transforming in another way: It's getting much bigger. And it's spreading across a wider area.

Tier 3 and Tier 4 cities are home to 55 percent of current car owners – and 68 percent of the potential car buyers in the coming year, according to the 2013 Nielsen Auto Research Report.

With this shift to regional markets outside the major urban areas, there are more first-time buyers in the lower-tier cities – potentially a significant leading indicator for further spending.

**POST-80s AND POST-90s
VIEW THEIR CAR AS AN
EXTENSION OF
THEIR IDENTITY**



LESSON 10:

WELCOME TO A MATURING MARKET

As the economy matures over the next few years, the contours of the new consumer-driven market will begin to take shape.

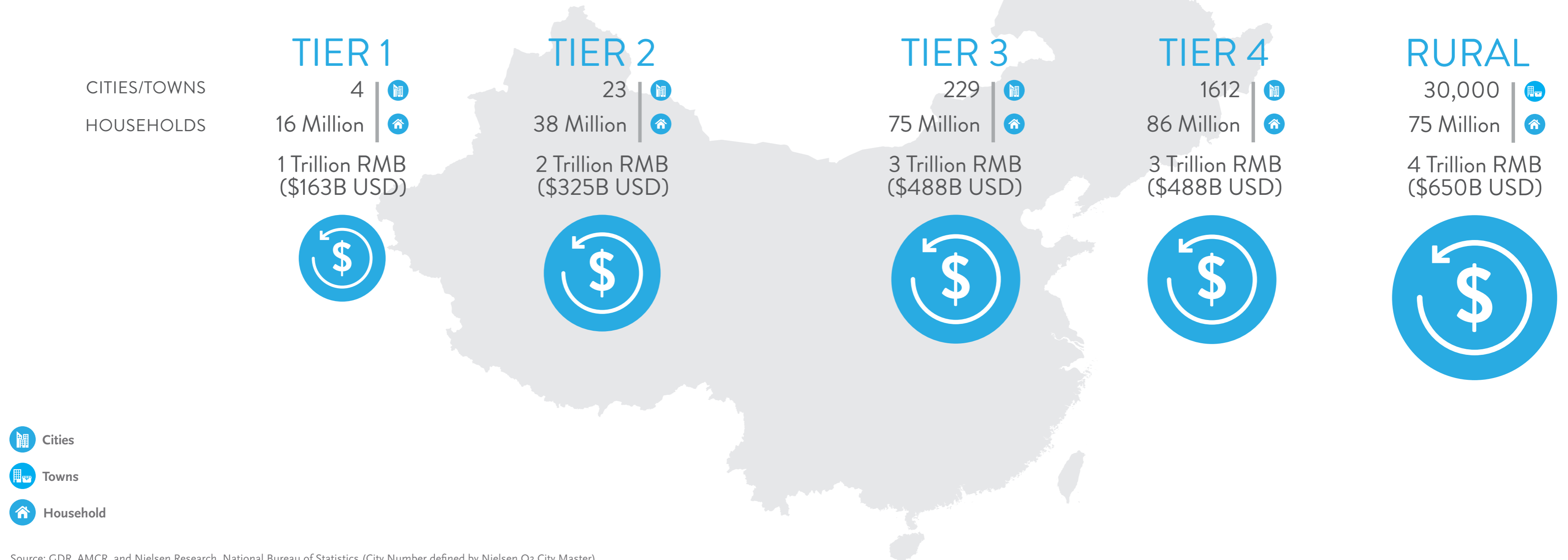
Demographic and population changes will be as important to watch as any other factor – and it is crucial to understand how they will play out in the ongoing digital revolution.

In the coming years, overall fast-moving consumer goods consumption growth is expected to be higher than GDP growth – most likely in the low double-digits, or high single-digits. Precision marketing is the best tool for unlocking value in this climate, to meet the unique demands of several key groups of consumers.

Indeed, 2014 is predicted to be the Year of Mass Consumption. But competition is expected to remain high. It's an atmosphere that requires preparation, agility and constant adjustments to be successful.

2014 IS PREDICTED TO BE THE YEAR OF MASS CONSUMPTION

CHINA: A SNAPSHOT



Source: GDR, AMCR, and Nielsen Research. National Bureau of Statistics (City Number defined by Nielsen Q3 City Master)

Nielsen China

Beijing Office

11/F, Office Tower1
(Nielsen Tower),
Sun Dong An Plaza
No. 138 Wang Fu Jing Dajie
Beijing 100006
China
Tel: 86 10 5812 9000

Shanghai Office

2/F, East Ocean Centre
(Phase II)
618 Yanan East Road
Huang Pu District
Shanghai 200001
People's Republic of China
Tel: 86 21 2326 9200

Guangzhou Office

12/F, May Flower Plaza,
No. 68 Zhong Shan Wu
Road,
Guangzhou 510030
China
Tel: 86 20 8316 4000

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尼尔森市场研究



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Or reach us at Communication.China@nielsen.com

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