EXECUTIVE INSIGHTS

Stress-Testing 'Look Good, Feel Good'

HOW BEAUTY AND PERSONAL CARE SPEND CHANGES IN INFLATIONARY AND RECESSIONARY TIMES

Today's inflationary environment persists at historic highs. Over the past 12 months, the consumer price index rose roughly 8%-9% in contrast to around 2%-3% over the prior decade.[1] Measures to combat inflation and bring it back under control are expected to center on interest rate hikes. This type of contractionary policy change is likely to dampen consumer spending and could steer the U.S. economy into a recession. In fact, numerous economists believe that a recession will hit in 2023,[2] though predicting the exact start and end date of a recession is, of course, impossible.

Once we enter recessionary territory, one might assume that the beauty and personal care (BPC) market will decline unilaterally across categories. However, a downturn in the economy has historically been linked to an uptick in beauty sales — a finding affectionately termed the "lipstick effect." For example, during the 2008 recession, the cosmetic industry was not only resilient but in fact grew.[3] To explain this observation, different studies put forth varying reasons, though these converge around an intuitive truth: Small investments in self-care are on trend because, recession or no recession, "look good, feel good" holds.

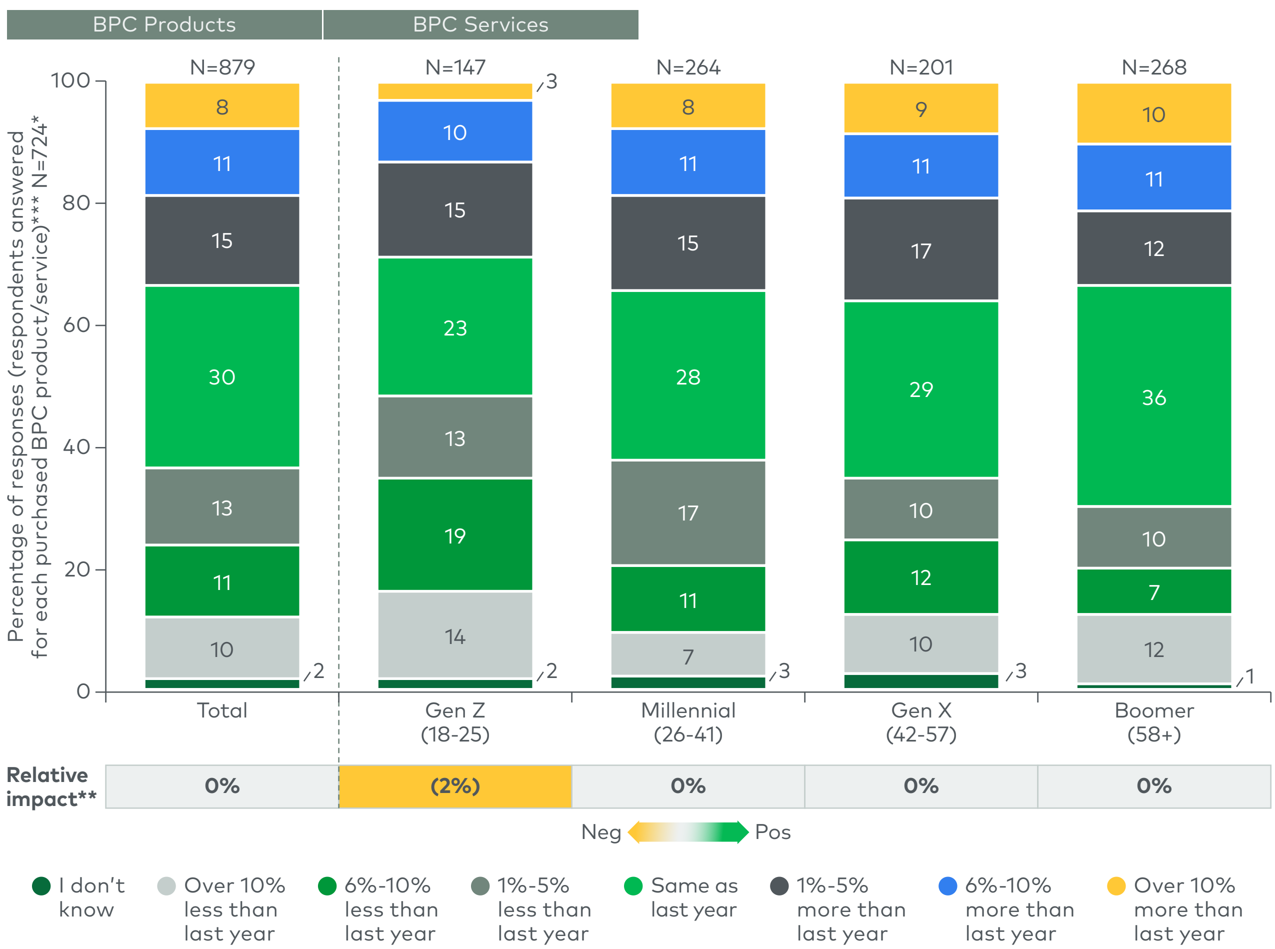
Despite such historical trends favoring BPC performance in challenging economic periods, many consumers are indicating that climbing prices in 2022 have changed the way they shop for BPC products and services. Understanding how different consumers are reacting to the current environment and how they may react to a recession is essential for BPC companies. Drawing on an August 2022 survey of 724 U.S. BPC consumers, we'll explore how inflationary pressures are affecting category spend and how a recession may add to this effect. We'll also unpack which segments of spend are most at risk and end with a brief discussion of how brands can best weather a period of inflation and potential recession.

Inflationary impact

A generational lens

According to our survey, Gen Z consumers (18-to-25-year-olds) have been impacted by inflation the most, with rising prices resulting in a net reduction in BPC spend for the group (see Figure 1). Given Gen Z's earlier career stage and associated lower income compared to other generations, this isn't surprising. In contrast, other generations report no impact of inflation on their BPC spend, in aggregate. This finding may prove problematic for newer beauty

Figure 1
Estimated impact of inflation on BPC spend by generation



*Survey question: How much has the recent rise in inflation impacted your average monthly spending on BPC products and services when comparing your average monthly spend today vs your average monthly spend last year?
**Average change calculated by taking a weighted average of respondent answers (e.g., 1%-5% less than last year was treated as (2.5%), 10+ coded as 15%)
***Percentages may not add to 100 due to rounding
Source: L.E.K. survey and analysis

brands trying to break into the industry as Gen Z consumers are more likely to try new items than other generations.[4] On the flip side, established brands that have a sticky, older target consumer may be better positioned to weather the storm.

The disappearing middle ground

In response to rising inflation, masstige and prestige brand consumers say they have reduced BPC spend slightly more so than mass consumers (see Figure 2). Masstige and prestige shoppers may more readily trade down to mass products when facing heightened economic constraints. By buying lower-priced products, these consumers may be able to purchase more feel-good beauty products despite rising inflation.

Figure 2

Estimated impact of inflation on BPC spend by consumers of each brand price tier (compared to last year)

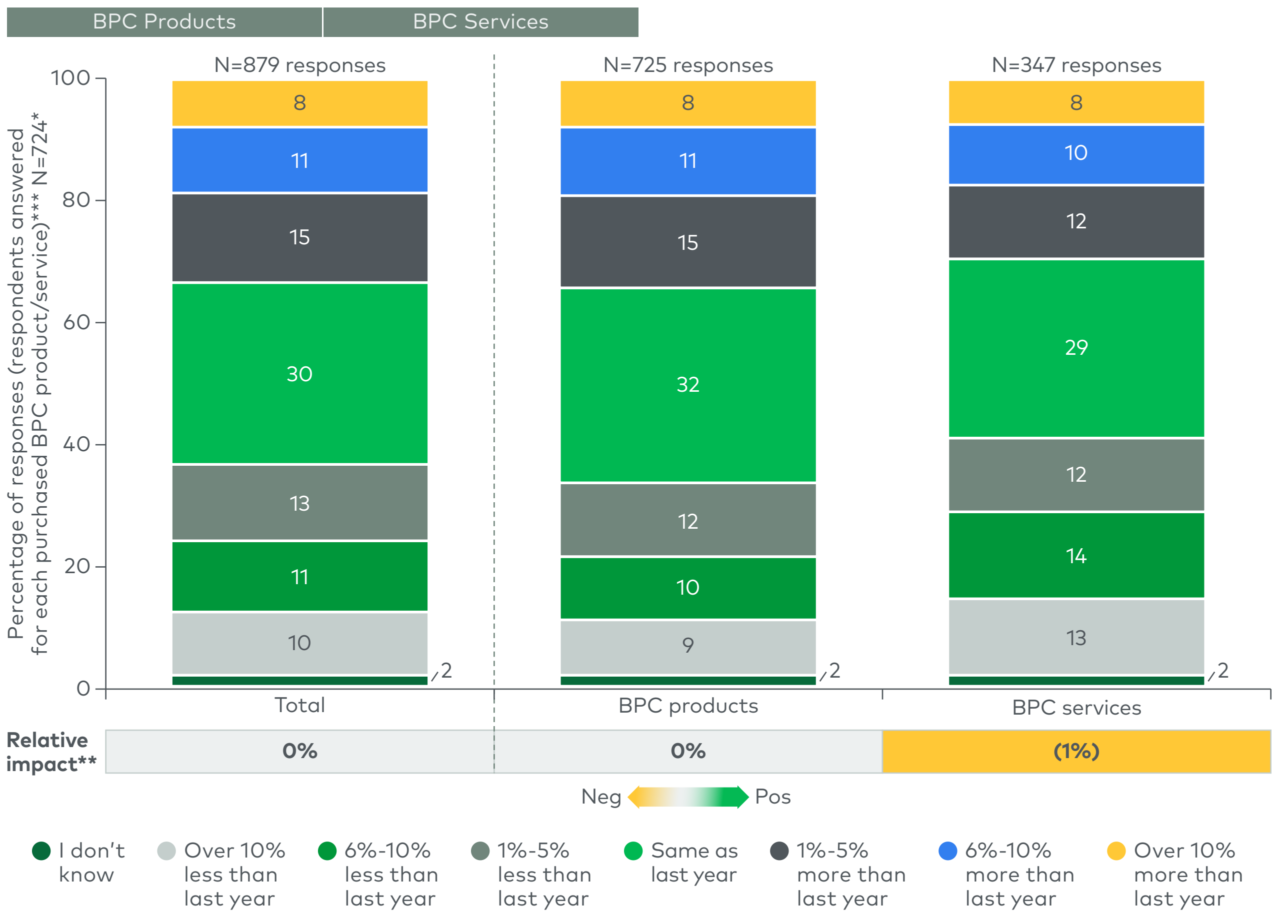
*Survey question: How much has the recent rise in inflation impacted your average monthly spending on BPC products and services when comparing your average monthly spend today vs your average monthly spend last year?
**Average change calculated by taking a weighted average of respondent answers (e.g., 1%-5% less than last year was treated as (2.5%), 10+ coded as 15%)
***Percentages may not add to 100 due to rounding
Source: L.E.K. survey and analysis

Products versus services

Consumers report their BPC product and service spend together remain roughly unchanged (see Figure 3). But a closer look reveals a slight reduction in BPC services spend. A few reasons may account for this. Services often have higher prices. Certain services may be more discretionary to some consumers, whereas the daily beauty routine at home is not. Labor challenges in select service categories may also have made it harder to get an appointment

Figure 3

Estimated impact of inflation on BPC spend on products vs services (compared to last year)



*Survey question: How much has the recent rise in inflation impacted your average monthly spending on BPC products and services when comparing your average monthly spend today vs your average monthly spend last year?
**Average change calculated by taking a weighted average of respondent answers (e.g., 1%-5% less than last year was treated as (2.5%), 10+ coded as 15%)
***Percentages may not add to 100 due to rounding
Source: L.E.K. survey and analysis

Breaking the results for services down further, consumers report their spend on nail services, hair services and massage services has dipped slightly. Nail services may be the easiest service to substitute with at-home products or treatments. Hair removal is the only category where consumers indicate no spending reduction due to inflationary pressures, perhaps because it's more functional than a luxury or self-care service.

On the product side, spend on personal care and hair and skin products has been particularly sticky despite inflation. Consumers report no change in spend relative to last year. They report some decline in their makeup/color cosmetics purchases, a not unexpected finding given that people are working from home more. Consumers that purchase makeup/color cosmetics tend to prefer prestige and masstige brands more than they do for other BPC products (excluding perhaps skincare), which skew more heavily toward mass brands.

Recessionary impact

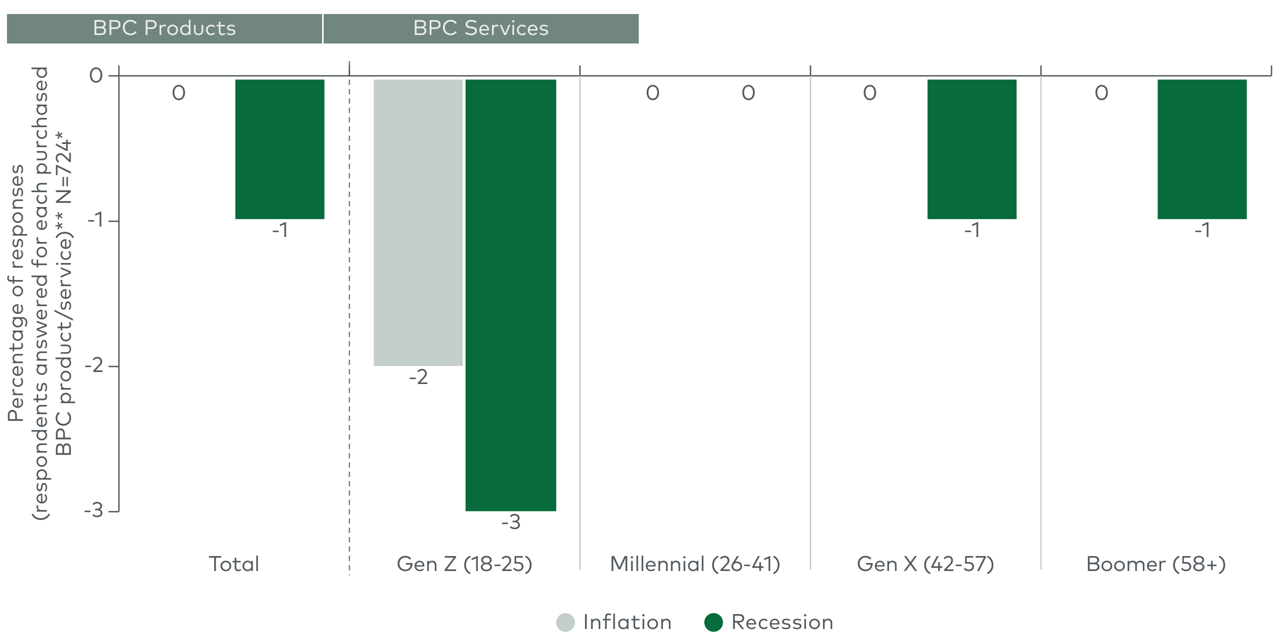
Our survey next evaluated how a future recession would further impact consumer spending in the BPC industry.

Mighty millennials

Gen Z is most likely to reduce BPC spend during a recession, just as they have done in the face of inflation (see Figure 4). But Gen Xers and boomers also expect to reduce their BPC

Figure 4

Estimated relative impact* of inflation vs recession on BPC spend by generation



*Survey questions: How much has the recent rise in inflation impacted your average monthly spending on BPC products and services when comparing your average monthly spend today vs your average monthly spend last year? If there were a recession, what impact do you expect it would have on your average monthly spending on beauty and personal care products and services compared to today?
**The number of respondents as it relates to inflation vs. recession for each generation is Total (879 vs 814), Gen Z (147 vs 117), Millennial (264 vs 247), Gen X (201 vs 197), and Boomer (268 vs 254)
Note: Average change calculated by taking a weighted average of respondent answers (e.g., 1%-5% less than last year was treated as (2.5%), 10+ coded as 15%)
Source: L.E.K. survey and analysis

spending, if only slightly, should a recession occur. Millennials appear most recession-resilient, citing no anticipated changes in their overall BPC spending in an economic downturn. This is possibly attributable to millennials having already weathered multiple financial crises.[5]

An even more pronounced hourglass effect

Consumers anticipate a larger negative impact on BPC spend in a recessionary environment than in our current inflationary one (see Figure 5). Masstige brand consumers expect the steepest decline in BPC spend in a recession compared with mass or prestige brand shoppers. Even mass shoppers say they expect to reduce BPC spend very slightly in a recession (unlike in an inflationary environment, where mass shoppers slightly increased BPC spend). Despite the feel-good effects of buying them, BPC products and services can ultimately be cut from a

Figure 5

Expected recessionary impact on BPC spend by consumers of each brand price tier (compared to last year)

*Survey question: How much has the recent rise in inflation impacted your average monthly spending on BPC products and services when comparing your average monthly spend today vs your average monthly spend last year?
**Average change calculated by taking a weighted average of respondent answers (e.g., 1%-5% less than last year was treated as (2.5%), 10+ coded as 15%)
Source: L.E.K. survey and analysis

budget if consumers' disposable income is severely limited. However, both mass and prestige brand shoppers indicate roughly unchanged BPC spend. As a result, the hourglass effect holds true in both inflationary and recessionary periods.

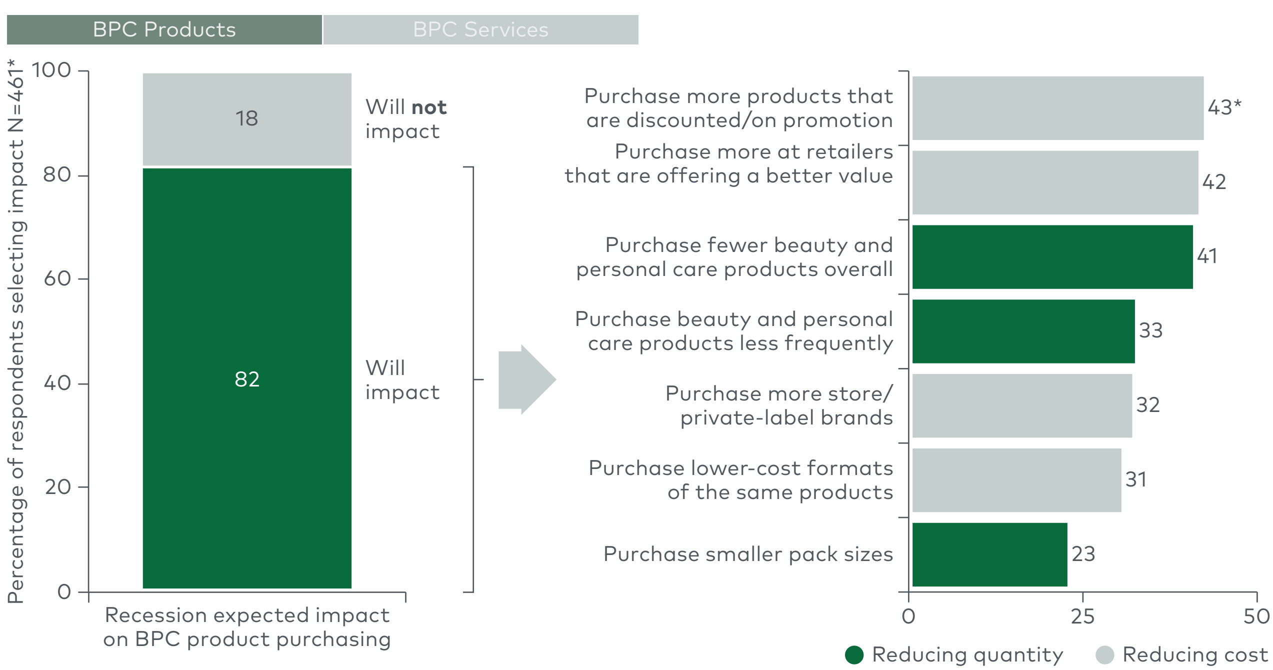
Products over services, once again

Just as consumers cut back on BPC services more than products during inflation, they expect to do the same in a recession.

What brands can do now

Consumers plan to respond to the recession by purchasing more BPC products on promotion, shifting to retailers offering better value and reducing BPC purchase quantity (see Figure 6). These responses essentially amount to a consumer search for value.

Figure 6
Expected recessionary impact on BPC product purchases



*Survey question: If there were a recession, what impact would it have on your purchase of beauty and personal care products?
Note: The percentages in the right-hand side chart are reflective of the 82% of respondents who are impacted
Source: L.E.K. survey and analysis

So, how should brands respond? Here are some ideas.

Communicate value

Brands should consider the best ways to communicate their value to consumers and strengthen their value proposition. The more a company can articulate an attractive "price to perceived value" ratio to consumers, the more likely consumers will be to continue buying that product, even in a downturn. What does value mean? Brands can answer this question through greater at-home convenience, price pack architecture, or a fundamentally superior performance or experience. Defining the specific pillars of brand value is important, but so too is developing the right marketing materials to communicate these to consumers.

Further, products delivering multipurpose benefits are a popular way to unlock greater perceived value.[6] An example within the skincare/makeup space is Pretty Filter Glassy Skin Balm, a moisturizer, primer and glow creator all-in-one product from K-Beauty brand Touch of Sol.[7] In the same vein, brands can introduce bundled SKUs as a counterweight to overall fewer BPC product purchases among consumers.

Thoughtfully discount while protecting heroes

To tempt bargain-minded consumers, companies may introduce more discounts — but they must do so thoughtfully as opposed to blanket promotions. Personalized discounts based on individual spending patterns is one way to keep consumers engaged and reward them at a time when it would be especially well received.

In particular, companies should ensure that pricing of their hero (i.e., bestselling) products remains protected and accessible. For example, mass brand e.l.f. Beauty raised the price of some of its products but held the line on its $3 lipstick.[8] Retaining an entry to the brand can keep shoppers buying and ultimately lead some to build a bigger basket.

Innovate for lasting influence

A downturn will make cash king. But in beauty, innovation will always be essential for building and protecting competitive advantage. The data has turned up no evidence that cutting innovation spend in a recession improves profits, growth or market share in either the short or long term.[9] Maintaining investment in innovation is key for companies to be ready for the post-recession rebound.[10] It also signals to consumers and investors alike that a brand is in it for the long haul.[11]

For more information, please contact strategy@lek.com.

Endnotes

[1]U.S. Bureau of Labor Statistics, "CPI Inflation Calculator." https://www.bls.gov/data/inflation_calculator.htm

[2]Time, "What a Recession Actually Is — And How to Know If the U.S. Is Entering One." https://time.com/6201205/what-is-a-recession-2022/

[3]Reuters, "Sales of beauty products get boost from recession." https://www.reuters.com/article/us-beauty-sales-recession/sales-of-beauty-products-get-boost-from-recession-idUSBRE86417C20120705

[4]StyleSage, "How Can Beauty Brands Prepare For An Economic Downturn?" https://stylesage.co/blog/beauty-brands-economic-downturn/

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[6]Cosmetic Executive Women, “CPNA 2022: Today’s Wellness-Minded Consumer Solidifies Beauty’s Recession-Proof Status.” https://www.cew.org/beauty_news/cpna-2022-todays-wellness-minded-consumer-solidifies-beautys-recession-proof-status/

[7]Ibid.

[8]Wall Street Journal, “A Cosmetics Brand Defies Inflation With Its $3 Lipstick.” https://www.wsj.com/articles/the-3-lipstick-that-ignores-inflation-11663639487

[9]Wharton School of Business, “What Every CMO Needs to Know to Make Marketing Decisions During the COVID-19 Recession.” https://wca.wharton.upenn.edu/wp-content/uploads/2020/10/Wharton-Forbes-Marketing-in-a-Recession-Report-8.24.20.pdf

[10]IRI, “When Down Is Up: Building Brands in Recessionary Periods.” https://www.iriworldwide.com/IRI/media/Library/IRI_GrowthConsulting_Building-Brands-in-Recessionary-Periods_April-2020.pdf

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