

China Consumer

IMF expert call: destocking coming to an end but structural challenges remain

Industry Overview

Not yet at a turning point

We hosted a call with an IMF expert Mr. Tang Li, the founder of a baby specialty chain store in Central China. The discussion confirmed our concerns on the structural industry decline, peaking premiumization, and channel margin erosion. The expert believes that potential rebound in newborn babies in 2024 might not be as significant as the market hoped for. He also sees inventory destocking is coming to an end, but channel price could take time to recover given industry decline and competition. Market share shift is key to watch, as international brands' localization strategy could be bearing fruit.

Birth rate & market outlook: expect market decline in '24

In 2023, only 9.02mn of babies were born in China, according to NBS. This suggests a 5.6% YoY decline, or a 39% decline vs. 2019. (Some channel checks might suggest a lower number). Market is expecting a newborn rebound in 2024, given delayed pregnancy, low-base, and increase in wedding registrations. However, the expert believes rebound might not be significant, given structural demographic headwinds (fewer females at childbearing age), cautious income outlook, and different views on 2024 lunar calendar (some see the year of dragon as auspicious while others argue 2024 is a year with no "Beginning of Spring", in solar terms). IMF industry declined by mid-teens% in 2023. He foresees that 2024 should continue to see decline, albeit potentially at a slightly more moderate rate.

Channel feedback: de-stocking vs. margin/price pressure

Channel dynamics remain mixed. The expert observed that inventory returned to a healthy level at 1.5-2 months and old GB products should be cleared out by mid-2024. However, retail prices (incl. discounts) further trended down. Mainstream price in the expert's region dropped from RMB180-300 in mid-2023 to RMB150-250 given competition. This puts more pressure on channel margin. As a result, distributor/retailer GPM dropped to 5-15%/6-10% (c.10% below pre-COVID). With continued industry decline and competition, price might struggle to recover in the near term.

Competition: market consolidation vs. heavy investment

Competition remains heated, as companies rushed to clear out old GB standard products, according to the expert. The new GB implementation pushed out smaller brands, accelerating industry consolidation. Channel also underwent consolidation, he noted that 30% of baby stores closed in 2023, bringing total store count to 120-150k (vs. 300k in 2019). It becomes crucial for IMF companies to partner with sizable offline stores for customer acquisition. However, as market consolidates, share gain could come at the expense of higher marketing investment. Leading brands lowered their target growth in 2024, but they remain committed to investing heavily in the channel for share gain (to offset industry decline), according to the expert. Local brands' share gain slowed, as leading international brands adopted more effective localization strategy and started penetrating into lower tier cities.

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Terms:

IMF: infant milk formula

NBS: National Bureau of Statistics

GB: guobiao (China's infant formula registration standards)

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