The State of Fashion

Beauty

McKinsey & Company

BoF


7h30m

The State of Fashion: **Beauty**

May 2023

This special edition is part of a series that *The Business of Fashion* and McKinsey & Company are publishing to complement our annual State of Fashion report. While the main report analyses the shifts shaping the global fashion industry in the year ahead, the special editions focus on specific sub-sectors, verticals, geographies and topics. For this edition, the authors have chosen to analyse the outlook for the beauty sector through 2027.

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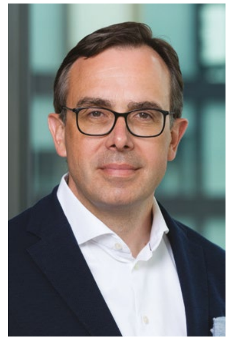

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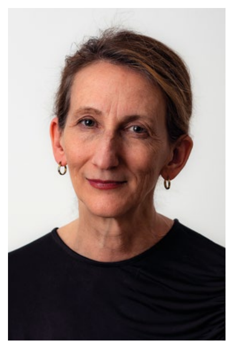

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EXECUTIVE SUMMARY

The New Face of Beauty

What is beauty? It's a question philosophers have pondered for centuries. And now it's increasingly one being asked across the beauty industry. A convergence of factors means brands and retailers are confronting deep shifts in what once was a relatively straightforward business of helping people look good.

Before this decade is over, today's $427 billion beauty industry[1] will have reshaped itself around an expanding array of products and markets. Consumers, particularly younger generations, will be spurring this reshaping, as their own definitions of beauty morph while their perceptions of everything from their role in sustainability to the importance of self-care evolve. Brands and retailers will also change, seeking greater agility and adopting multichannel operating models. They will be doing this as competition in an already crowded market continues to intensify across all categories — skin care, makeup, fragrance and hair care.

This special edition of The State of Fashion by *The Business of Fashion* and McKinsey & Company explores the global beauty industry through a set of key dynamics impacting brands and retailers in 2023 and beyond. The report uses market intelligence, insights from industry executives and other experts, and proprietary analysis to identify top business opportunities, while also providing both price segment- and category-wide retail sales forecasts over a five-year period to 2027. To enrich this report, McKinsey also conducted a global survey capturing the shopping behaviours and preferences of consumers in six core beauty markets.

The big takeaway is that the beauty market is expected to continue demonstrating the resiliency it has cemented in recent years, showing that time and time again it can withstand — and even thrive profitably and grow — amid economic turbulence, while other consumer sectors struggle. It's now an industry that everyone from top-tier financiers to A-list celebrities wants to be a part of, with good reason. McKinsey estimates that by 2027, the global beauty industry will record over $580 billion of retail sales, growing at 6 percent per year.

How the industry reaches that figure depends on brands' and retailers' ability to navigate the dynamics that this edition of The State of Fashion explores: new geographic hotspots; the burgeoning luxury opportunity; the route for emerging brands to scale; the evolving landscape for mergers and acquisitions; the steady rise of wellness-related beauty; and the complexities of the Gen-Z

beauty consumer.

First and foremost, geographic diversification is more essential than ever. It was only recently, for example, that brands could focus their footprints on the industry's two top countries — China and the US. Both markets will remain mighty forces for the industry — with China estimated to reach approximately $96 billion by 2027 and North America approximately $115 billion. But in both markets, various factors mean growth will be harder to come by for individual brands. However, there is a silver lining: other countries and regions are ready to step into the limelight, including the Middle East and India. Brands can also find opportunities by targeting consumers with products and services in the top tier of the pricing pyramid: luxury beauty has the potential to grow from around $20 billion today to around $40 billion by 2027.

By 2027, the global beauty industry will record approximately $580 billion of retail sales, growing at 6 percent per year

The next few years will also be a period of reckoning for some brands that until recently had carved out niches for themselves and whose reputations were built on disruption. These challenger brands have begun treading the same bumpy path as other small and medium-sized brands in their quest for scale. For sure, a beauty brand's trajectory to $20 million in annual sales will continue to be quite different from the one to $250 million or $800 million, especially with the vast number of brands entering the industry.

However, brands highlighted in this special edition that have successfully broken through barriers to growth show how the rulebook for scaling can be rewritten, with a laser-sharp focus on building out international footprints and channels and smart funding considerations. Mergers and acquisitions might have a role to play here. As in recent times, conglomerates and financial investors alike will pursue deals to invest in promising brands. But deal-making will be different in the near term. Megadeals will likely be few and far between in response to both market turbulence as well as the need for brands to demonstrate an ability to grow profitability with innovative product pipelines.

Another dynamic driving beauty's future circles back to the question of what beauty is. It's front of mind for many beauty consumers, and for that we can thank Gen-Z. This generation, today's teens and twentysomethings who will represent a quarter of the world's population by 2030, has outsize influence over the industry given, for example, their command of social media channels to voice likes and dislikes, influence older generations of consumers, and challenge mainstream views of what constitutes a beautiful person.

Beauty's definition will continue to broaden to encompass much more than the lipsticks, face masks and perfumes associated with the sector as consumers seek to look and feel good. Nowhere will this be more evident than in beauty's steady march into wellness. As part of today's $1.5 trillion global wellness industry, wellness-inspired products — from ingestible supplements to sleep aids to lotions made using ancient medicinal traditions — have already captured the attention of consumers as well as retailers embracing greater self-care and mindfulness in our post-pandemic daily routines. The melding of wellness and beauty is only expected to become more pronounced, with McKinsey expecting compound annual growth of 10 percent to 2027 for the wellness industry.

Ultimately, the years ahead will offer all the right ingredients — from agile channel mixes to consumers eager to explore new products — to propel the industry. For beauty leaders, it will be a unique time to flourish, with strategies that reflect a new face for beauty.

INDUSTRY OUTLOOK

Firing up Beauty for the Next Era of Growth

The global beauty industry will generate estimated retail sales of around $460 billion this year, a figure that is projected to increase to approximately $580 billion by 2027. With many beauty companies already recapturing their pre-pandemic lustre, the industry is expected to defy the downward pressures holding back other parts of the consumer sector in the short term.

But being part of that growth will require brands and retailers to deploy more sophisticated strategies than they did during the years preceding Covid-19's upheaval. From intensifying competition to distribution channel pressures, times are changing. Beauty players that thrive amid these shifting pressures will be those that demonstrate a deep understanding of their unique value propositions as well as of their communities, with an ability to tirelessly lean into rapid innovation and product cycles.

Geography Lessons

Competition for wallet share will likely play out across more countries and regions than in previous years, and at different speeds.

For example, China will likely remain a major market for beauty, but its compound annual growth rate is expected to slide to around 8 percent between 2022 and 2027, from 12 percent between 2015 and 2019. China will account for around one-sixth of global beauty retail sales by 2027, at $96 billion. The prestige segment holds the greatest potential in the country. Worth around $17 billion in 2022, the segment has an expected CAGR of around 10

Exhibit 1

In our analysis, we have broken the beauty market down into six price segments

	Skin Care		Fragrance		Colour Cosmetics	
	Price Point	Illustrative Brands	Price Point	Illustrative Brands	Price Point	Illustrative Brands
Ultra Luxury	$3,000+	La Prairie*	$5,000+	Guerlain*	$1,000+	n/a
True Luxury	$200–3,000	La Mer	$250–5,000	Byredo	$100–1,000	Clé de Peau
Prestige	$80–200	SK-II	$100–250	Dior	$60–100	Yves Saint Laurent
Entry Prestige	$40–80	Shiseido	$70–100	Hugo Boss	$45–60	Bobbi Brown
Masstige	$20–40	Kiehl's	$45–70	Kenzo	$25–45	Clinique
Mass	<$20	Nivea	<$45	Revlon	<$25	E.l.f.

* Selective offering

Note: Brands are non-exhaustive

Source: McKinsey analysis, press search

percent to 2027. China's luxury segment is smaller — approximately $4 billion in 2022 — but could see similar growth in the years to come. The greatest absolute growth will likely be in skin care, which will reach approximately $62 billion by 2027, up from around $45 billion in 2022.

Regionally, North America is poised to gain importance as a growth engine, accounting for $85 billion of the industry in 2022 and expected to reach approximately $115 billion by 2027. Notably, fragrance and hair care, worth $14 billion and $19 billion respectively in 2022, are expected to power the region with a CAGR of around 7 percent each over the five-year period.

Asia is another key region. Today, Asia Pacific, excluding China, is beauty's biggest regional market, bolstered by Japan and South Korea, and will reach an estimated $151 billion in retail sales by 2027 from approximately $110 billion in 2022.

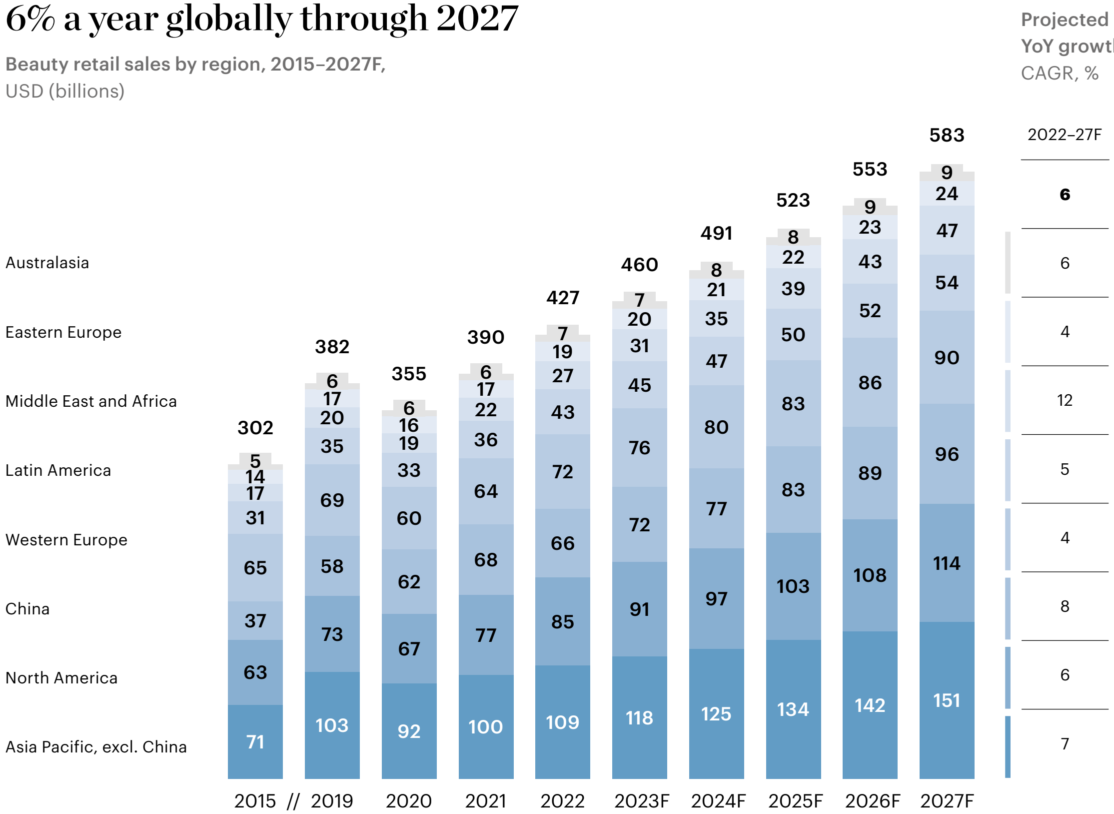
Europe, another regional stalwart representing about $90 billion in 2022, is expected to reach at least $115 billion by 2027. Similar to other parts of the world, consumers in both Western and Eastern Europe are trading up, with the increase in prestige spending experienced during the pandemic expected to continue driving high-end segments.

Growth opportunities in other markets are emerging as well. For instance, with an expected CAGR of 12 percent to reach $47 billion by 2027, the industry in the Middle East and Africa will continue to benefit from various regulatory and structural changes in select countries, including a lifting of foreign ownership rules that will ease entry into the region for global brands. India is also positioning

Exhibit 2

Beauty retail sales are expected to grow 6% a year globally through 2027

Beauty retail sales by region, 2015–2027F,
USD (billions)



Source: Forecasts for global beauty recovery by region, category and channel reflect McKinsey perspective, based on Euromonitor historical (released in April 2023), MGI macro-economic scenarios, consumer research, comprising fragrance, colour cosmetics, skin care and hair care

itself for growth, with an expected CAGR of 8 percent to reach $21 billion by 2027, thanks in large part to shifting demographics and strong economic prospects helping to expand per capita spending on discretionary goods. Meanwhile, Latin America will likely continue to shake off the pandemic's impact to return to growth, with CAGR between 2022 and 2027 rising to 5 percent to reach $54 billion.

Category Check-in

Skin care, fragrance, colour cosmetics and hair care are all expected to power ahead at a combined global CAGR of 6 percent between 2022 and 2027.

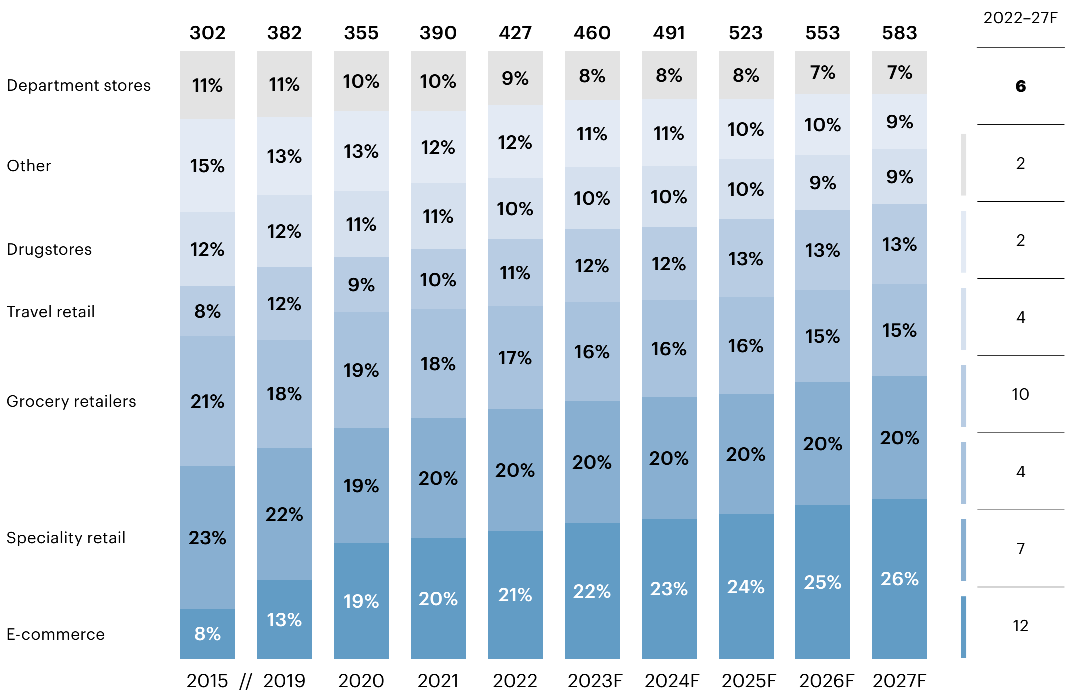
Skin care, at around 45 percent of the sector's total market value, remains beauty's largest category. With an expected global CAGR of 6 percent, the category will grow from $190 billion in 2022 to $260 billion by 2027, with gross margins of between 50 percent and 70 percent. Innovation has been, and is expected to remain, a large driver in skin care growth, with brands increasing their focus on science-driven efficacy claims. Conglomerates have long dominated the category in key markets in Asia and North America, although challengers are also a source of competition. While mass is expected to remain the largest sub-segment, the greatest growth could come from luxury and prestige, with a CAGR of 11 percent and 7 percent over the five-year period

Exhibit 3

E-commerce is set to represent a quarter of the beauty market by 2027

Beauty retail sales by channel, 2015–2027F,
USD (billions)

Projected YoY growth,
CAGR, %



Note: Percentages may not add up 100 due to rounding.

Source: Forecasts for global beauty recovery by region, category and channel reflect McKinsey perspective, based on Euromonitor historical (released in April 2023), MGI macro-economic scenarios, consumer research, comprising fragrance, colour cosmetics, skin care and hair care

respectively, reflecting the overall "premiumisation" of the category.

Fragrance — with global sales of around $70 billion in 2022 — is expected to see a CAGR of 7 percent, reaching close to $100 billion by 2027. The category is highly profitable, with margins of up to 90 percent in the luxury sub-segment and 80 percent in other sub-segments. Fragrance is expected to benefit from increasing penetration in China, where it accounts for less than 3 percent of the total beauty market. The category also has room to grow in the US, where it accounts for 16 percent of the total market, compared to Western Europe's 26 percent. Mass and masstige segments will likely wane as consumers upgrade to higher-end segments, particularly niche fragrance brands. With increasing premiumisation, prestige fragrance has an expected CAGR of 8 percent and luxury fragrance 13 percent over the five-year period.

Where does this leave **colour cosmetics**? Following a sharp drop during the pandemic, the category is expected to make a comeback in the next few years. After contracting — due to the pandemic, among other factors — at a CAGR of 1 percent between 2019 and 2022 to $80 billion, colour cosmetics will deliver 6 percent CAGR up to 2027, to more than $105 billion, with a generally even distribution across price segments. Brands, particularly those in the

Consumers are interested in adding products to their regular home beauty routines. More than half of consumers globally use three or more brands for skin care, hair care and fragrance, while one-third use five or more brands for cosmetics.

mass segment that rely on lower price points, should use the coming years to focus on profitability. With products in the category exhibiting lower average spend per order and requiring higher sampling expenses, this generally has resulted in the lowest average gross margins in the industry of between 45 percent and 60 percent.

As for **hair care**, the $90 billion category today spans a broader product spectrum than traditional personal care shampoos and conditioners, which has helped it gain a greater presence in the beauty industry. Brands have an opportunity to benefit from a premiumisation and the "skinification" of hair, as consumers adopt multi-step hair care routines much as they have been doing with skin care. This includes an array of specialist products, creating a white space in beauty that traditional brands as well as new entrants can tap into, particularly given that consumers are more open to experimenting with buzzy, innovative products in hair care than in other categories. Hair care is expected to see the highest CAGRs in prestige and entry prestige, at around 11 percent and 8 percent respectively. Premiumisation in hair care also extends to adjacent products such as hair drying and styling devices. Hair care's expected CAGR of 6 percent over the five-year period (excluding devices) will drive total retail sales to $120 billion, with gross margins of between 50 percent and 60 percent.

Consumer Drivers

Industry growth strategies will need to reflect a shift in consumer behaviours with regards to hair, skin and body care. Consumers today are interested in adding products to their regular home beauty routines. More than half of respondents to McKinsey's 2023 global consumer survey said they use three or more brands for skin care, hair care and fragrance, while one-third use five or more brands for cosmetics. At the same time, the survey — which canvassed shoppers across four generations in six countries (the US and China as well as the UK, Germany, France and Italy) — found approximately 40 percent of consumers indicated that they are loyal to brands they trust, while 69 percent said they like to try new products at least every six months. Certainly, consumers are diversifying within categories — in hair care, for example, consumers are expanding into specialised products for certain hair types, as well as scalp treatments, serums and oils.

Given consumers' openness to trying new products, category opportunities are evolving and could provide entirely new growth avenues. Consider wellness: consumers are broadening their definition of beauty to a more holistic concept, encompassing a broad range of products, including probiotic skin care, supplements, beauty devices and home wellness. The shift towards wellbeing is also changing the profile of influencers in the space. While influencers and celebrities, as well as family and friends, continue to be a significant source of inspiration for beauty, shoppers also report being highly influenced by recommendations from doctors and dermatologists, according to the global consumer survey.

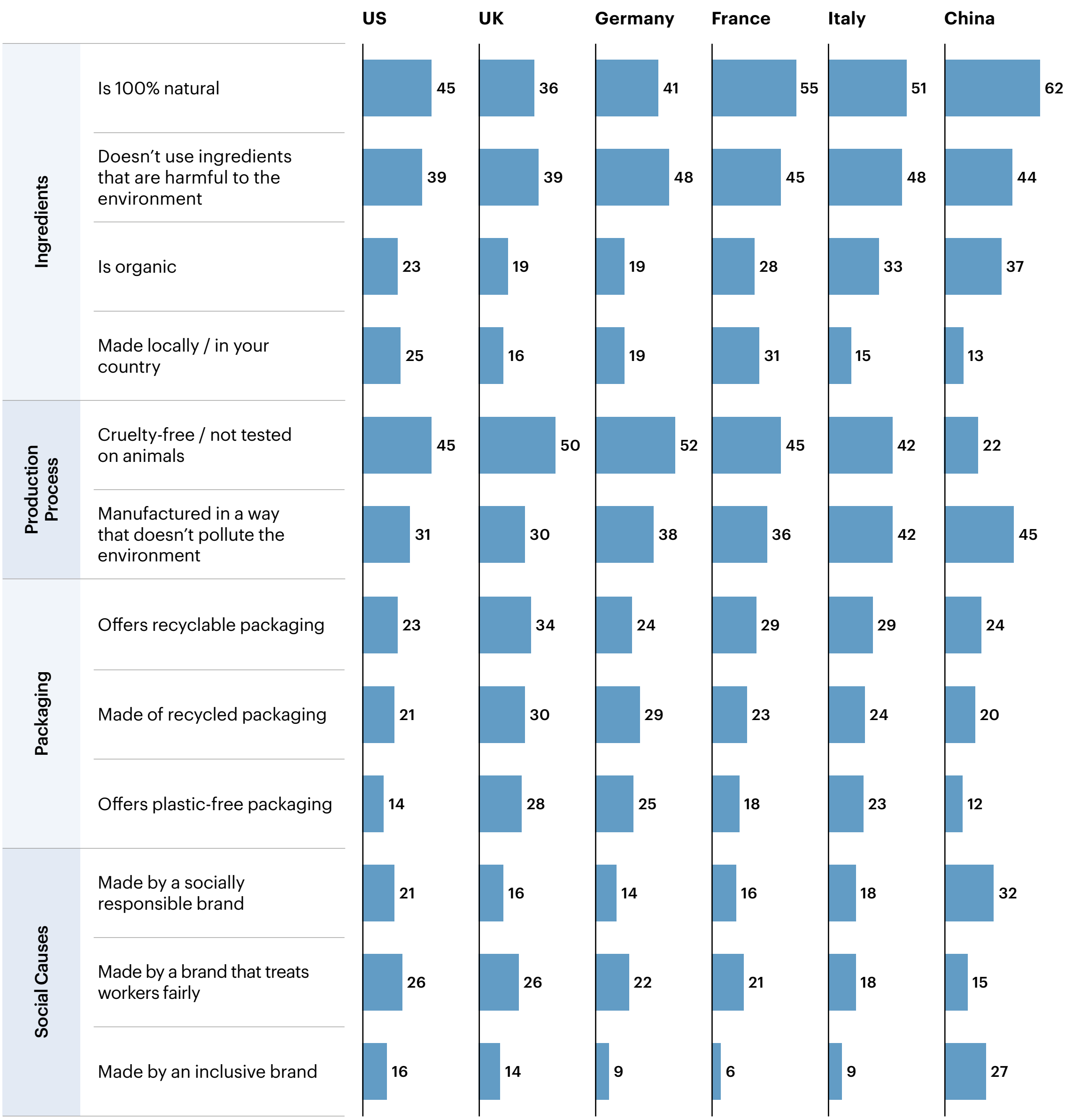
Across all these products, sustainability will be an overarching priority for many consumers. But

Customer wearing a hyaluronic eye mask. Getty Images.

Exhibit 4

When it comes to sustainable products, beauty shoppers are looking for different qualities across geographies

The most important aspects that make a beauty product sustainable, top five choices, % of respondents[1]



1 Q: Think about what makes a beauty product sustainable in your mind. Which of the following parameters are the most important? Please select up to five

Note: Choices ordered from most important to least important by share of global respondents within each category

Source: McKinsey Beauty Consumer Survey 2023, n=12,010, sample to match general population 18+ years there are multiple aspects of sustainable beauty products that players will need to consider. When McKinsey asked beauty consumers what aspects of sustainability matters most to them, the top overall responses were: the absence of ingredients that harm the environment, 100 percent natural formulas, and production that is cruelty-free and does not test on animals. But there were nuanced differences across the countries surveyed that brand strategies must factor in: Chinese respondents placed more emphasis on natural ingredients and environmentally friendly manufacturing, while those in the West also placed a high value on cruelty-free production. Overall, the focus on sustainability is most prominent among Millennials and Gen-Z, with more than half of the age groups reporting a willingness to pay more for beauty products from a sustainable brand.

Channel Mix and Match

Consumers' embrace of e-commerce has defined beauty distribution around the world in recent years, and for good reason. Between 2015 and 2022, global e-commerce sales grew at a CAGR of 20 percent, with significant uptick during the pandemic. By 2022, digital shopping overtook speciality retail as the largest individual sales channel worldwide, accounting for around one-fifth of the industry's overall total.

At a country and regional level, beauty's distribution patterns are unfolding in different ways. E-commerce remains the largest channel in the US and is on track to represent around $45 billion in sales by 2027. Continued investment in beauty from e-commerce giant Amazon is boosting the online retailer's influence in the market; Amazon is starting to reposition itself as a discovery channel rather than a replenishment platform.

The e-commerce heft of the US, however, is overshadowed by that of China. Digital sales in the country have gained share and now represent over 40 percent of the market, increasing to around $55 billion by 2027, when close to 60 percent of beauty sales in the country will be digital, driven by livestreaming and social commerce. While Tmall, China's single largest sales channel, is expected to plateau, growing 2 percent annually in the five-year period, sales on social media platform Douyin (known as TikTok in Western markets) are expected to grow 11 percent.

In the rest of Asia Pacific, as well as in Western Europe, beauty's growth through 2027 will be more evenly distributed across all sales channels, including speciality and drug stores. Hypermarkets and discounters are also investing in mass and masstige beauty in the US and Europe, with Walmart, for instance, expanding its offering in relevant markets.

It is now clear that the beauty sector moves fluidly across physical and digital sales channels. Between 2022 and 2027, global e-commerce beauty sales will grow at an approximate CAGR of 12 percent, while physical retailers can expect a CAGR of 7 percent in speciality retail and 4 percent for drugstores and grocery stores.

Consumers now expect a mix of distribution channels. Both online and in-store channels are popular sources of beauty inspiration across regions and age groups, as McKinsey's survey shows, with respondents ranking online and in-store as among the most preferred channels, at 40 percent and 45 percent respectively.

Beauty's Siren Song

The industry's attractiveness has not been lost on large, non-beauty businesses — including luxury megabrands that are launching beauty brands of their own, setting up funds and incubators, or acquiring established brands that offer differentiating products, large fan bases and a finger on the pulse of the next big thing.

Beauty has cemented its reputation as a stand-out industry given its proven resiliency and ability to consistently deliver high margins. But there's another element that brands and retailers must not overlook — the enormity of the opportunities that emerging segments and sub-segments have to offer, from wellness to ultra-luxury, as well as geographically in, for example, the Middle East and India. Amid all this, profitable and sustained growth over the coming years will hinge on turbocharged innovation. Brand portfolios need to adapt to rapid product lifecycles, with "hero" products no longer the primary way to win with customers. Competition is intensifying, as is consumer desire to put to work a full range of beauty products that help them to look and feel their best.

The State of Fashion: **Beauty**

01.

The New Growth Map

Beauty's international growth blueprint of the past decade needs a refresh. China, though still a powerhouse, can no longer be the sole growth engine for brands. The US, which will continue to be the biggest market in the world, will increase in importance for the industry even as competition for market share intensifies. Other markets, notably the Middle East and India, may offer a range of ways to offset those challenges.

India and the Middle East are emerging as hotspots, with retail sales growing to $21 billion in India and $47 billion in the Middle East and Africa by 2027

02.

Wellness Awakens

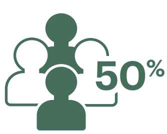
A new definition of beauty is reshaping the market as consumers shift their objectives from aesthetic perfection to holistic wellbeing. Brands can tap into emerging wellness sub-categories — from sleep to sexual intimacy to ingestible beauty — to upgrade their existing products and expand their portfolios, provided they do so with credibility and authenticity.

Today's $1.5 trillion global wellness industry is projected to grow at a compound annual rate of as much as 10 percent between now and 2027

03.

Decoding Gen-Z

As Gen-Z grows up, brands must adapt, finding new ways to speak their language. This may require retiring traditional ways of doing business — from marketing to product development — and rethinking assumptions about this diverse, digitally savvy and demanding generation that prioritises value and efficacy when choosing their beauty brands and products.



Nearly 50 percent of Gen-Z consumers say they research beauty products extensively before purchase

04.

The Scale Imperative

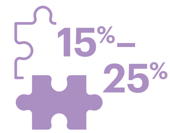
For many emerging beauty brands, the early days of getting up and running has been the relatively easy part. Now, they need to confront the greater challenges that continuing their growth trajectories entail. In an industry that has become overcrowded, geographic and channel expansion will likely be critical for gaining further market share.

Of a group of 46 brands with global retail sales between $50 million and $200 million in 2017, only 4 surpassed $400 million 5 years later

05.

M&A Recalibrated

In the short term, beauty merger and acquisition activity may not deliver as many megadeals as seen across the industry in the past, but the deal-making will continue to be buoyant. The potential benefits for buyers and sellers remain as strong as ever, playing a pivotal role in strategies focused on international growth, innovation and competitive product portfolios.



Beauty brands' average EBITDA margins are around 15 percent to 25 percent, making them attractive to deal-makers

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The New Growth Map

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KEY INSIGHTS

- China, the world's second-largest beauty market at about $65 billion, will continue to grow at an 8 percent CAGR over the next four years, though economic and other challenges are prompting brands to seek growth in alternative markets.
- At roughly $77 billion, the US market is expected to come into sharper focus, but hyper-segmentation and a diverse channel strategy will be required.
- India and the Middle East stand out as emerging hotspots with underserved consumers open to local and foreign brands.

History will not repeat itself — at least, as far as the global dynamics in beauty are concerned. Over the last decade, the growth strategies of many beauty brands consisted of targeting just a handful of countries, with particular emphasis on China. That playbook is no longer as effective as it once was — fast-changing structural economic challenges, geopolitical developments and competitive headwinds are just a few of the factors that will impact how brands develop their strategies, region by region.

China's C-Beauty Play

Nowhere are shifting conditions more pronounced than in China, beauty's biggest growth engine in the 2010s. Foreign brands once raced to capitalise on the country's burgeoning beauty market and, for many, it became their main driver of growth. But in recent years, select brands, from South Korea's The Face Shop to Dubai's influencer-backed Huda Beauty,[2] have ceased operations in the country entirely, or like L'Oréal, have been adapting their local strategies. Brands that have yet to enter the country are weighing whether they can be part of China's beauty market, which is projected to reach approximately $96 billion by 2027 from around $65 billion currently.

Florasis makeup palette. Florasis.

Economic challenges in the country are part of the reason why brands in China are not expecting unconditional growth. Since 2020, Covid-19 policies that restricted shopping and travel, combined with a deepening property market crisis, decelerated China's economic growth trajectory. In turn, businesses across a range of sectors have had to readjust their growth models.[3] The beauty industry has not been insulated from these pressure points. For instance, The Estée Lauder Companies reported that its Asia Pacific net sales declined approximately 16 percent in the second half of 2022, with much of the decline attributed to China. Over the same period, total net sales fell by 16 percent and 1 percent at the Amorepacific Group and Coty respectively, with both corporations citing China's performance as a contributor.[4] While China's economy is expected to weather the turbulence, economists say it will no longer deliver the double-digit growth that attracted foreign brands over the last decade.

Increasingly, foreign brands of all sizes can expect heightened competition from local companies, primarily in mass and masstige beauty, which represent around 60 percent of the market. Such "C-beauty" brands have targeted digital strategies and affordable price points and promotions; they also operate with tight margins, or even unprofitably. As such, they are putting pressure on the margins of foreign competitors while also gaining market share — approximately 50 percent of Chinese consumers said they regularly buy domestic brands.

While local players are growing in prominence in colour cosmetics, hair care, and mass to masstige skin care, foreign brands offering premium skin care continue to have significant appeal, owing to the allure of established foreign labels in the category and limited number of domestic brands. The category is expected to record a 10 percent CAGR over the next four years.

Meanwhile, the outlook for fragrance is particularly buoyant in China. As a $2 billion market, fragrance is underdeveloped compared to other parts of the world and could more than double by 2027. The category's CAGR is expected to be approximately 18 percent. Consumers have already begun wearing perfume more often, and in some cases, are seeking out differentiating brands.

Premiumisation will also fuel fragrance growth. Niche foreign entrants, like Paris-based Diptyque and Stockholm-based Byredo, could be big beneficiaries of this growth. The key will be for brands to build on their expertise to develop scents tailored to local sensitivities while leveraging department stores for distribution.

Foreign brands in China will need to readjust their operating models within the country, creating a localised strategy that factors Chinese traditions and consumer behaviour into each aspect of operations, from how products are made to how they are marketed, taking into consideration the increasing importance of livestreaming and social selling. Foreign brands could also consider decentralising operations and providing local teams with greater authority to craft strategies. For some brands, M&A with local players may make sense, including taking minority stakes, as L'Oréal did with Chinese luxury fragrance start-up Documents in 2022.

The popularity of homegrown brands will continue to rise across makeup, hair care and skin care, spurring competition over the next few years. The country's level of growth potential will vary for foreign brands, whose portfolios will need to be increasingly segmented and tailored to national preferences and reflect consumers' shifting purchasing behaviour.

Doubling Down in the US

The US's $77 billion market is expected to be the biggest growth driver for many multinational beauty brands over the next few years. Its sheer size has long made it a magnet for major brands, and this is unlikely to change.

US consumer sentiment did take a knocking in 2022 and the start of 2023 as pandemic-era stimulus payments wound down, and inflation and interest rates rose amid a looming threat of recession. Nonetheless, sales across all beauty categories and price points appeared to shrug off these pressures and continued growing.[5] US beauty sales are now projected to grow 6 percent annually to over $100 billion by 2027.[6]

The country is a fertile environment for beauty players in hyper-segmented markets like boutique fragrance, or with distinct value propositions, such as makeup brands accommodating particular skin conditions or complaints. But low barriers to entry and trend-obsessed consumers have fuelled intense competition over the last decade. Now, achieving meaningful and profitable scale is proving difficult for many in this increasingly fragmented market. In skin care alone, the number of small and mid-sized players has mushroomed, with at least 500 brands generating annual sales of less than $200 million. Of the 30 or so brands recording more than $200 million annually, the vast majority are owned by large conglomerates.

At the same time, big brands that have not had a significant presence in North America may start expanding their regional footprints. Wholesale distribution will likely play a significant role for these and other brands, requiring updated distribution strategies that reflect recent wholesale disruption.

Not so long ago, US wholesalers had clearly demarcated strategies to serve distinct consumer bases. For example, beauty retailer Sephora and department stores like Neiman Marcus focused on the premium market, while pharmacies and mega-store Ulta Beauty handled mass and masstige markets, respectively. But beauty shoppers have begun buying across price points since they no longer

Premiumisation will also fuel fragrance growth. The key will be for brands to build on their expertise to develop scents tailored to local sensitivities.

Exhibit 5

Beauty is projected to grow across all regions, with substantial growth in all categories in the Middle East and Africa

Projected sales growth by region and category,
USD (billions), growth to 2027, and CAGR, 2022–2027, %

Largest absolute growth
Smallest absolute growth

	Asia Pacific excl. China	China	North America	Western Europe	Middle East and Africa	Latin America	Eastern Europe	Australasia
Fragrance	4.6 12%	2.9 19%	4.5 6%	6.1 6%	5.4 11%	3.9 5%	1.1 5%	0.6 9%
Colour cosmetics	7.2 6%	5.3 10%	6.7 6%	3.0 4%	3.7 11%	1.7 5%	0.8 4%	0.7 7%
Hair care	4.1 4%	4.3 7%	7.2 7%	3.1 4%	6.1 12%	2.8 4%	1.1 4%	0.3 4%
Skin care	26.2 7%	17.1 7%	10.9 6%	5.5 4%	4.7 12%	3.1 5%	1.5 5%	0.9 6%
Total	42.1 7%	29.6 8%	29.3 6%	17.7 4%	19.9 12%	11.5 5%	4.5 4%	2.5 6%

Source: Forecasts for global beauty recovery by region, category and channel reflect McKinsey perspective, based on Euromonitor historical (released in April 2023), MGI macro-economic scenarios, consumer research, comprising fragrance, colour cosmetics, skin care and hair care

associate quality with price as they once did. As a result, mass and premium brands are increasingly sold at the same stores.

To help address this shift, Ulta Beauty has partnered with Target, while Sephora has sought out big box player Kohl's to expand its reach.[7] Instead of segmenting retail by price point, brands are moving even more tactically when deciding both where to scale and where to build engagement. Sun care-focused skin care brand Supergoop!, for example, brought its most popular — and lowest priced — items to Ulta Beauty in 2022, while selling top-tier products at Sephora, without diluting its proposition.

Expanding through direct-to-consumer plays will be key to building or defending market share. One path forward for brands with sufficient capital is to develop physical experiential spaces. Glossier, for instance, has nine experiential stores in the country including its New York flagship, which serve as effective storytelling vehicles.

Adding More Markets to the Mix

While China and the US remain key markets, global brands should consider widening their global aperture. Two markets capturing the attention of many beauty players, albeit for very different reasons, are India and the Middle East.

India's $14 billion beauty market is compelling for a number of reasons, not least its robust longer-term economic prospects. By 2027, the beauty market is expected to be worth $21 billion. This is leading many brands to assess the country differently than

While China and the US remain key markets, global brands should consider widening their global aperture. Two markets capturing the attention of many beauty players, albeit for very different reasons, are India and the Middle East.

they once might have. The country, which is expected to have one of the fastest-growing economies in the world, has both an expanding middle class[8] and disproportionately large younger generation, with approximately half of its population of 1.4 billion under the age of 30.[9] Per capita annual spend on beauty, at around $10 today, is set to rise to around $15 by 2027, though may still lag more mature beauty markets like China, where per capita annual spend is approximately $40, and fully mature markets like the US with per capita spend of more than $200. Spending growth may well be driven by younger shoppers, who are already willing to pay higher prices for quality,[10] and consumers generally continuing to embrace e-commerce.

Local retailers like Nykaa and Purplle operate almost completely online, as do many direct-to-consumer brands such as Sugar Cosmetics and Bare Anatomy.[11] Much like in China, these agile, homegrown brands and platforms are carving out market share thanks to rising e-commerce penetration as well as innovative product development and locally tailored influencer campaigns.

To date, mass beauty represents the largest segment. Local and global names share the market, including Hindustan Unilever-owned Glow & Lovely and Lakmé, Beiersdorf's Nivea, and Piramal Healthcare's Lacto Calamine. While prestige brands such as Estée Lauder and Estée Lauder-owned Clinique represent less than 15 percent of the market in colour cosmetics, and even less in skin care, the prestige segment is growing twice as fast as mass and masstige. In recent years, challenger brands like Too Faced have entered India to compete alongside legacy players such as L'Oréal Paris, Estée Lauder and Clinique. While these players have little competition from local brands thus far, this could change, requiring greater agility, including localising strategies to reflect India's vast heritage of using natural ingredients in a modern way.

Meanwhile, brands can tap new opportunities in various parts of the Middle East.[12] While the beauty market in the Middle East and Africa combined is worth $27 billion, it is yet to reflect the growing wealth of consumers in the Middle East. Per capita annual beauty spend in the Middle East is around $50, compared to more than $200 in the US.

But by 2027, sales are forecast to reach over $47 billion as the market directly and indirectly benefits from a combination of factors already having an impact, including government programmes such as Saudi Arabia's Vision 2030, aiming to modernise the economy, and a growing population — both local and expat — of high-net-worth consumers.

Alongside Saudi Arabia,[13] which is projected to be the fastest-growing global economy in 2023, the other country driving beauty's growth in the Middle East is the United Arab Emirates, where household incomes are the highest in the region. In both countries, beauty ranked as the second most-popular shopping category for 30 percent to 40 percent of female shoppers, according to BoF Insights.[14] Recent regulatory changes, including a loosening of the requirements for local partners and franchises, have also made it easier for foreign brands to do business in the region.

Categories such as skin care (at $6 billion) and fragrance (at $8 billion) are expected to double in size, as both local and foreign brands expand region-specific product ranges. Homegrown brands such as Dubai skin care label Shiffa are leaning into their Arab roots and using ingredients like Iranian roses and Egyptian jasmine. Foreign brands have been looking to do the same. Christian Dior, for example, launched a fragrance and beauty boutique in the UAE in 2020 where its smoky oud perfumes are popular with local shoppers. In 2021, the brand collaborated with Dubai fashion designer Yasmin Al Mulla to create an incense burner only available in the region.

As in India, beauty players in the Middle East need to appeal to a digitally savvy consumer base, even though e-commerce adoption is relatively low in the region — representing, for example, only about 10 percent of sales in colour cosmetics — but is rising steadily.

Against this backdrop, the beauty growth map is evolving. A single playbook will no longer be effective for internationally focused beauty brands. The US is becoming more critical than ever, while growth prospects in China will be viewed through a different lens. Brands must now build strategies that place these markets within a broader context, re-assessing resource allocations as other markets provide greater growth opportunities. Arguably more so than ever, honing a brand's unique value proposition in each of these countries will be critical, and potentially require dedicating more resources to bulk up that proposition. Nuanced understandings of each market will be needed, as will speed. Ultimately, successful growth strategies will be significantly more tailored and unique than in the past.

A shopping mall in Dubai. Shutterstock.


Dior
SWAROVSKI
SEPHORA

IN-DEPTH

Beauty's $40 Billion Luxury Opportunity

By Kristi Weaver, Sara Hudson, Amaury Saint Olive and Alex Workman

Wealthy shoppers looking for exclusive beauty products and bespoke experiences have been underserved. But that may change soon. Brands entering the luxury space may find more untapped opportunities than ever.

KEY INSIGHTS

- Luxury beauty remains significantly underpenetrated relative to other consumer categories.
- McKinsey estimates that luxury beauty is an approximately $20 billion segment today and could grow as much as 20 percent annually over the next five years to more than $40 billion.
- Though luxury fashion houses are well-placed to succeed in this segment, new entrants could claim a share of this fast-growing market.

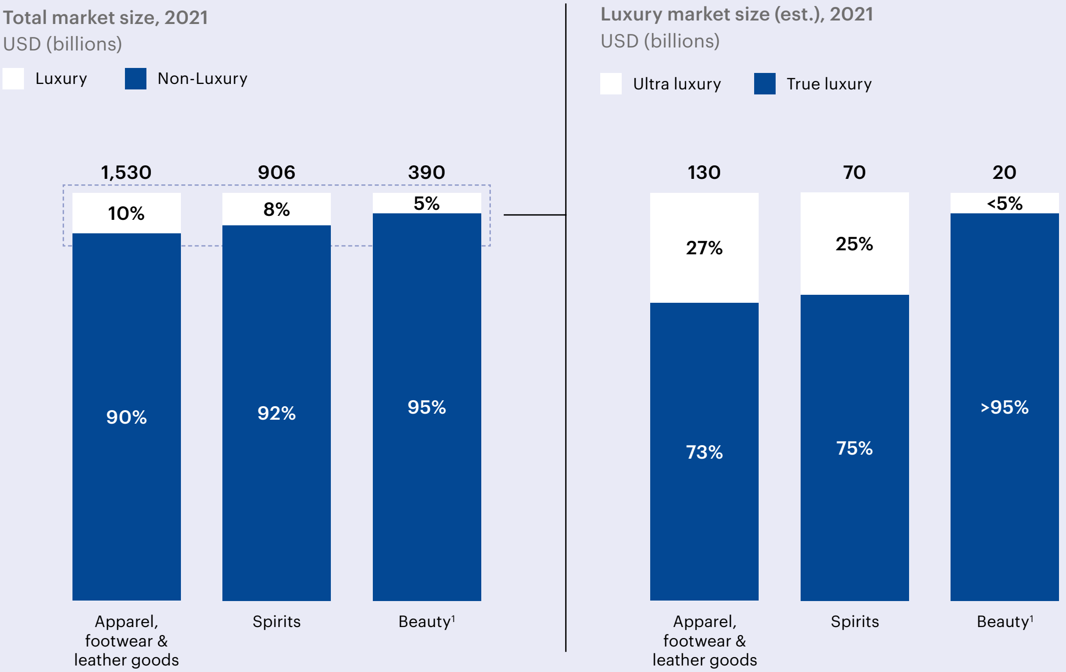
The world's wealthiest people spend more than $350 billion on luxury goods every year, allocating thousands of dollars to rare liquors or hand-crafted haute couture garments. But when it comes to beauty, luxury shoppers looking for top-tier products and experiences have limited choice. Generally, high-end beauty products simply represent premium alternatives to mass beauty, falling within the prestige category with products such as $60 lipsticks or $130 face creams. As a result, luxury shoppers' relative spending on skin care, cosmetics and other beauty items is well below what they allocate to comparable discretionary spending categories. The beauty industry now has a unique opportunity to change that.

Luxury beauty cuts across two categories. "True luxury" includes products that retail for hundreds of dollars and can generate strong profits at high volumes. Skin care brands La Mer and La Prairie cater to this space, as do niche fragrance brands like Roja and House of Creed. Meanwhile, "ultra luxury" is another level up, with products that retail for thousands of dollars. While appealing to a smaller cohort, ultra-luxury beauty can elevate a brand's reputation for exclusivity and quality. French perfumer Guerlain, for example, aims to reinforce its

Guerlain perfume bottles. Shutterstock.

Exhibit 6

The luxury beauty market has more white space than adjacent sectors, particularly at the high end in ultra luxury



1 Includes skin care, fragrance, colour cosmetics and hair care

Note: Excludes accessible luxury

Source: McKinsey analysis, Euromonitor, external reports, expert interviews, press search

artisanal history when it collaborates with artists on special editions of its signature “bee motif” bottles. The brand collaborated with jeweller Lorenz Bäumer and crystal manufacturer Baccarat to produce $25,000 versions of its bottles in 2022.[15] Similarly, Clé de Peau Beauté celebrated its 40th anniversary by commissioning jeweller Elie Top to create diamond-studded cases for its best-selling lipstick and cream that retailed for as much as $16,000.[16]

We estimate that true luxury and ultra luxury beauty combined represent an approximately $20 billion market today, with a potential compound annual growth rate of between 15 percent and 20 percent, amounting to an additional $15 billion to $20 billion in sales by 2027. The growth will be driven by both increasing consumer demand and investment from beauty brands looking to expand their offerings at higher price points.

The Luxury Consumer

The global community of high-earning and luxury clients is growing in size and spending power. The US and Europe are each home to more than 30 percent of the world’s high-net-worth individuals (with investable assets of $1 million or more) and ultra-high-net-worth individuals (with investable assets of $30 million or more), while approximately 16 percent are based in mainland China, Hong Kong and Taiwan.[17] The number of luxury clients is growing fastest in China and is expected to increase at a compound annual rate of 12 percent between now and 2027.

This wealth distribution is expected to be a factor in market growth. Erwan Rambourg, author of the 2020 book "Future Luxe: What's Ahead for the Business of Luxury," told us: "Every nationality is trading up — luxury companies understand that luxury is no longer singular, but a play on global wealth." However, he added, "Clearly, the main engines of growth for luxury over the next 10 years will still be China and America."

The world's wealthiest shoppers are attracted to status symbols, such as limited-edition products that could be considered works of art. In 2020, for instance, Hennessy created a limited-edition cognac bottle designed by architect Frank Gehry. Only 150 bottles were produced, each retailing for $17,000. The collaboration's success led to a sequel the following year, when the price of each bottle increased to $165,000.[18] Although luxury shoppers are more likely to display a rare cognac prominently in their home than they would an ornate jar of moisturiser, social media has helped bring beauty routines out into public spaces.

These shoppers are also less interested in trendy brands and products. Instead, they're seeking unique and exclusive items, which brands have started to provide. Cartier, for instance, offers luxury consumers the opportunity to co-create fully tailored scents with its in-house perfumer.

But luxury beauty brands' allure extends beyond the global elite. Consumers who are not high-net-worth individuals might still splurge on lower-priced true-luxury beauty items. For this cohort, purchases of exclusive or status-defining beauty products may be more accessible than buying haute couture or fine jewellery.

Keeping Higher Standards

Beauty players that seek to tap the true luxury and ultra luxury markets will need creativity and innovation. Go-to-market strategies will share many elements with the standard luxury playbook, which requires exceptional product quality. Luxury houses are already setting the stage for top-tier formulations. Chanel, Dior and Tom Ford have secured access to rare ingredients for their luxury fragrances, for example.[19]

Beauty brands with luxury ambitions will need to combine compelling storytelling with exceptional customer service, which can come to life through elite experiences. Alexander McQueen, for example, invited select clients to a historic former monastery in London to mark the launch of its eight-piece luxury fragrance collection in 2018. Each scent was exhibited with pieces from the fashion label's archive.[20] Dior opened a temporary luxury spa on the Orient Express in 2022 for VIP guests on their way to the Cannes Film Festival.[21] The French fashion house has also invested in estates and gardens to host special events.

As brands expand into luxury segments, they also need to tailor their offerings to local cultural expectations. Armani Privé launched an haute Oud collection exclusively designed for the Middle Eastern fragrance market, with references to the region's traditional perfumery and local ingredients.[22]

Luxury beauty brands' allure extends beyond the global elite. Clients who do not qualify as high-net-worth individuals might still splurge on lower-priced true-luxury beauty items.

"You have to adapt to local culture, which can vary tremendously," Rambourg said. "For instance, fragrances used to have very little traction in Asia, while being very popular in the Middle East with very specific scents. Localisation is very important, and with the world reopening, what you will be displaying in Paris will be different from what you show in Tokyo."

Regardless of the region, beauty brands have an opportunity to adapt distribution. While some wholesale retailers, such as luxury department stores, can serve as appropriate partners, direct-to-consumer may be a better option for brands seeking to retain control of clients' entire experience and ensure an elite shopping journey. Some brands will be able to leverage their existing boutiques, while others may need to open dedicated beauty locations. Traditional speciality beauty retailers that want to participate in luxury beauty's growth will also need to invest in new retail formats to attract top clients.

Who Can Win?

Though shoppers are eager to try new brands, the luxury segment will be challenging for completely new players that don't already have credibility. Success is possible, however, if new brands bring a creative proposition as well as a compelling origin or product story. British perfumery house Roja, known for using rare ingredients, launched directly into the luxury space in 2011 and offers bespoke services that can exceed $31,000.[23] London-based artisan perfumer Electimuss, founded in 2015, draws inspiration from Ancient Rome.

Established luxury brands with a track record of creativity, quality and status are well positioned to target luxury beauty. Fashion brands, especially the luxury megabrands, are particularly credible, as they can leverage their reputation for craftmanship as well as their existing relationships with wealthy clients. In addition, megabrands, such as Dior and Chanel, can maintain and leverage their high-volume prestige beauty lines while introducing elevated ranges that cater to top spenders.

Designer and luxury fashion labels launched prestige beauty divisions in the 2010s, building profitable businesses by offering an accessible entry point into their brands. While few have looked beyond the mid-market consumer, many luxury fashion brands are reprioritising their beauty strategies. Expanding on its prestige fragrances, Gucci launched the luxury Alchemist Garden collection, while Versace introduced luxury Atelier Versace scents. In 2023, Kering announced plans to form a new beauty division that is expected to address true luxury and ultra luxury.[24]

To ensure the credibility of beauty lines across both luxury and prestige, megabrands will face a delicate balancing act. Brands will need to carefully consider which categories are most suitable for luxury expansion.

"Fashion to colour is an easier move than, say, fashion to skin care," said Vanessa Goddevrind, chief operating officer of luxury skin care brand 111Skin. "Skin care and hair care products will be a more challenging jump for some brands, as top clients expect high levels of efficacy in those categories."

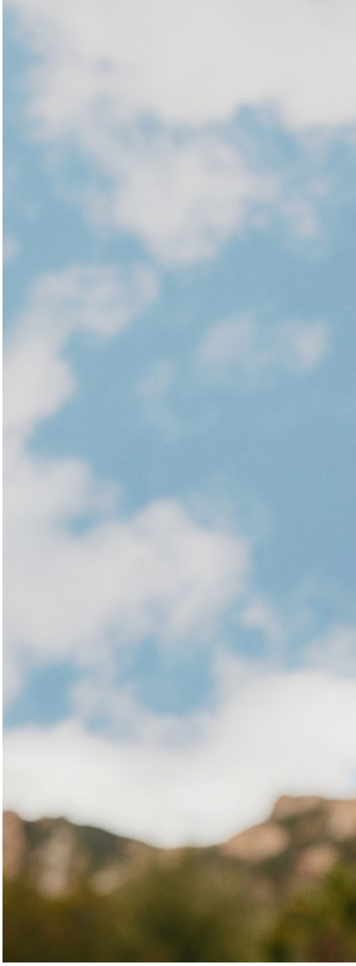
Established prestige beauty brands can more easily tap the luxury skin care market, especially if they already have a reputation for efficacy. Similarly, luxury hotels are well placed to expand into luxury beauty products, as are high-end wellness clinics and spas that offer clients a combination of beauty, wellness and medical services. Aman, a collection of 34 luxury resorts, released a luxury skin care line in 2018 with packaging designed by architect Kengo Kuma. The skin care line connects to the global resorts via natural ingredients drawn from Aman destinations around the world — for example, sea buckthorn oil from Bhutan and vetiver from Indonesia.

As beauty brands and luxury houses embark on what could be a transformative journey, capturing the attention and trust of luxury clients will require creativity and innovation, as well as a razor-sharp understanding of affluent clients. Venturing into a largely untapped market, the sector's most innovative and credible players will build competitive advantage as they establish themselves as the reference points for the sector and its underserved customers.

An ultra-luxury Clive Christian perfume. Getty Images.

02. Wellness Awakens

A new definition of beauty is reshaping the market as consumers shift their objectives from aesthetic perfection to holistic wellbeing. Brands can tap into emerging wellness sub-categories — from sleep to sexual intimacy to ingestible beauty — to upgrade their existing products and expand their portfolios, provided they do so with credibility and authenticity.



KEY INSIGHTS

- Today's $1.5 trillion global wellness industry is projected to grow at a compound annual rate of as much as 10 percent to 2027, according to recent McKinsey research.
- Traditional beauty players need a crystal-clear understanding of how expansion into wellness-inspired products can align with their expertise as well as their consumers' needs and interests.
- In addition to retail stores, spas and hotels can provide testing grounds for wellness products.

There once was a time when beauty brands had little doubt where their growth opportunities lay: creams, lotions, lipsticks and other products that promised to improve how customers looked — younger, glamourous, polished. Aesthetic perfection took centre stage.

That's no longer enough for many of today's shoppers. For them, beauty products still must fulfil traditional aesthetic needs, but also improve how they feel — both physically and mentally.

A vast array of products and categories now fall under the umbrella of wellness-inspired beauty. Products might, for example, include ingredients once only associated with homeopathy or natural remedies, or even ancient medicinal traditions. Products can also come in the form of ingestible supplements, devices — such as LED face masks and microdermabrasion tools — and products improving the atmosphere of homes.

For beauty players newer to this part of the industry or looking to expand further into wellness sub-categories, the journey should begin with a careful exploration of why and how new products, marketing or partnerships can make strategic sense.

Why Now?

Since the late 2000s, the self-care concept has captured public attention and spawned a wave of mainstream wellness products and services. This was particularly true in developed markets like the US, where wellness products from high-profile, celebrity-driven start-ups, such as Gwyneth Paltrow's Goop and Amanda Chantal Bacon's Moon Juice, helped fuel interest in the space and erode taboos around topics such as sexual intimacy. The Covid-19 pandemic only furthered consumers' interest in health and wellbeing.

Worth at least $1.5 trillion today, the global wellness industry is set to grow at a compound annual rate of between 5 percent and 10 percent

Moon Juice supplements. Moon Juice.

to 2027.[25] The US is the largest wellness market, worth approximately $450 billion in 2022. China is a close second, at $350 billion to $400 billion, with significant untapped demand. Meanwhile, the wellness market in Europe, at $130 billion, is relatively small, but is expected to expand by close to 10 percent annually.

A global consumer survey that McKinsey conducted in early 2023 sheds light on regional opportunities for wellness-inspired beauty, while also highlighting regional differences.[26] For example, consumers in China use spa services more frequently than their counterparts in Europe, whereas home wellness products such as scented candles are particularly popular in the US, and used by up to 70 percent of US consumers, compared with about 40 percent in China. Overall, the majority of survey respondents from the US, China and five Western European markets said they plan to increase spending on wellness products and services in the year ahead, perhaps a reflection of the rising profile of the "conscious consumer," who focuses on natural ingredients and sustainability.

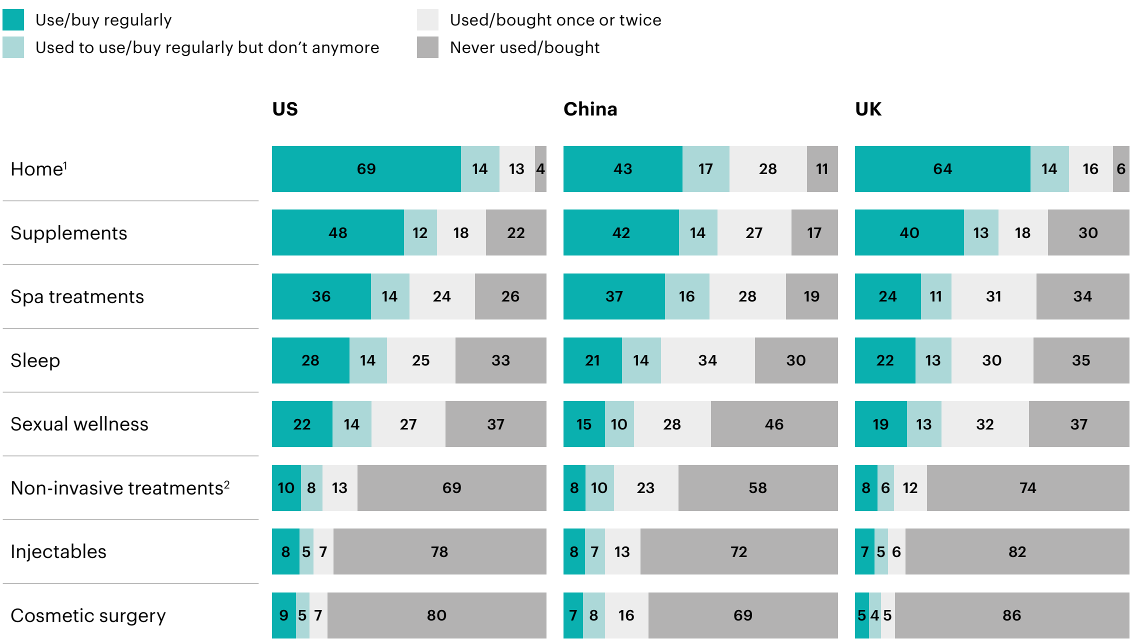
Consumers' understanding of wellness today is both broad and nuanced. As a result, wellbeing is extending beyond the day-to-day to include not just diet and fitness, but also mindfulness, mental health and sleep quality — in addition to beauty products. Beauty shoppers are educated and want to learn more about ingredients, while seeking out brands that align with the beauty philosophy they embrace: looking good *and* feeling good.

Brands, in turn, are responding, often with product portfolios that go beyond "clean" marketing and labelling by blurring the lines between wellness and beauty. For example, ayurvedic beauty brands such as Soma Ayurvedic and Ranavat aim to meet consumers' growing interest in ancient healing systems. This shift extends to more traditional cosmetics players, too: Lady Gaga repositioned her

Exhibit 7

Home products, supplements and spa treatments are the most popular wellness offerings

Use and purchase frequency of wellness product categories,
% of respondents by country



Q: What is your experience with the following beauty or wellness products and services?

1 e.g. scented candles, home fragrances

2 e.g. laser, chemical peels, microdermabrasion

Source: McKinsey Beauty Consumer Survey, March 2023

Sample sizes: US 2,096; China 1,914; UK 1,945; Germany 2,014; France 2,020; Italy 2,023

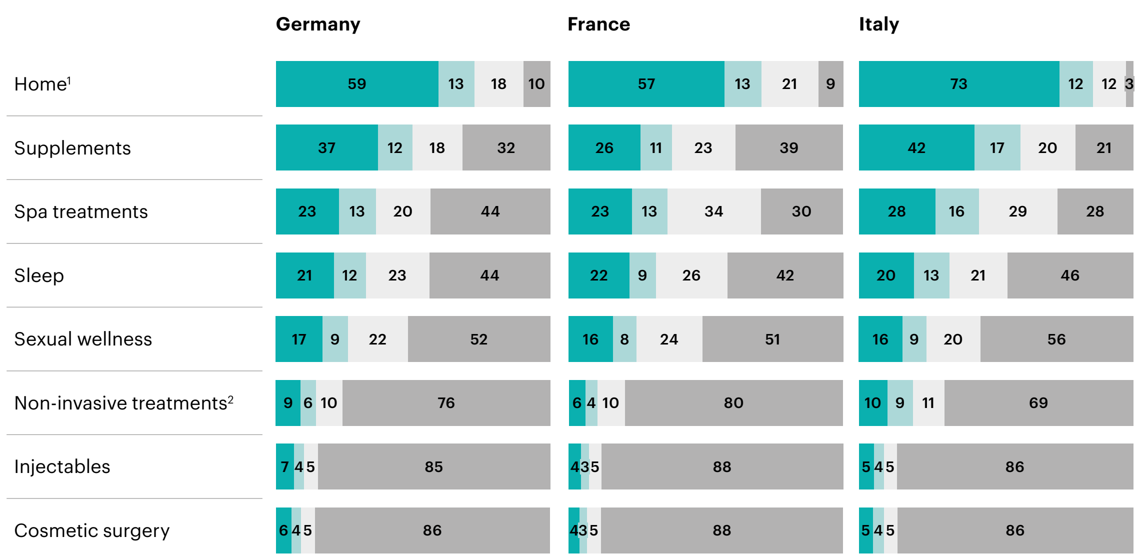
skin care-orientated cosmetics brand Haus Labs in 2022, emphasising natural ingredients such as argan oil, vitamin E and arnica, a homeopathic staple used to help reduce skin irritations.

Where to Grow

The scope of wellness-inspired beauty products is vast, with certain sub-categories already indicating potential opportunities for certain brands. For example, nearly 30 percent of McKinsey's survey respondents said they regularly use sleep-related products and services. For traditional beauty brands, this may be an opportunity to leverage expertise and consumers' trust in skin care and fragrance lines to launch pillow mists, eye masks and body lotions that promote tranquillity and better sleep. Marketers for beauty service providers such as spas can specifically highlight the sleep benefits of certain treatments.

For example, Rituals, a Dutch brand launched in 2000 and now sold internationally, seeks to enmesh wellness into its home, body and beauty products. The brand offers sleep-focused lotions, serums, diffusers and even sleep masterclasses on YouTube. Additionally, Rituals' product range expands across everyday living; it now offers candles and bath salts, drawing on self-care practices popular in Asia. The company's product lines and messaging seem to have particularly resonated during the pandemic, with its revenue exceeding $1 billion by 2021.

Sexual wellness is an area garnering increasing



attention. Having long been taboo or confined to specialist retailers in many markets, products ranging from vibrators and lubricants to intimate washes and sexual health-promoting supplements can now be found at retailers such as Sephora and Ulta Beauty. Approximately 20 percent of McKinsey's global survey respondents said they use such products today.

Maude, Dame Products and Unbound are all start-ups specialising in sexual wellness; one of the newest entrants is Playground, a line of personal lubricants that counts celebrity Christina Aguilera as co-founder, brand adviser and investor.

As for distribution, Bloomingdale's, Saks Fifth Avenue and other department stores have introduced intimate care sections on their websites and have announced plans to add them to their physical stores.

Sub-category considerations for brands should include both customer interest and brand expertise. For instance, ingestible beauty-related supplements are regularly used by approximately 40 percent of survey respondents; yet this is a sub-category likely better suited to brands with a fitness or nutrition focus, or brands with a science-based approach to beauty. Such supplements today encompass more than vitamins, and include adaptogens cultivated from herbs, roots and other plants, beverages and snacks made with antioxidants — and even intravenous drips.

Whatever the segment, traditional beauty brands will need to determine which, if any, wellness sub-categories they can move into credibly in the eyes of consumers.[27] Not every brand can expand into every part of wellness. For example, highly specialised products, such as those focused on sports or oral care, may be too narrow and incompatible with the overall brand.

Credible storytelling will need to be combined with an attractive value proposition — a combination that Uma Oils, for example is aiming to capture. Entrepreneur Shrankhla Holecek launched her face, body and aromatherapy oils business in 2016, drawing on her experience growing up in India and helping with her family's centuries-old business that harvests essential oils. Uma Oils' beauty and wellness collections are in keeping with ayurvedic tradition and include niche products such as navel therapy oils.

Uma Oils' body balm. Uma Oils.

Product Launch Pads

With each and every wellness launch, brands should assume customers will expect endorsements from wellness practitioners, dermatologists, biologists or other authoritative sources, particularly given the use of novel, science-based ingredients, with which many consumers may not be familiar.

A clear strategy incorporating wellness will be crucial for retailers. In recent years, department stores and other retailers across price segments have begun including wellness sections in their physical and online stores.[28] Ulta Beauty's "Wellness Shop" now includes superfood-infused products, spa-at-home offerings and intimate care; Sephora is following a similar path. Retailers expanding into wellness have relatively few boundaries within which to curate and cement credibility among shoppers, while becoming conduits between consumers and brands. In the years ahead, beauty retailers could become a testing ground for emerging sub-categories by providing well-defined sections within their stores for discovery and entertainment.

Other physical spaces — such as spas, hotels and clinics — can also tap into wellness, including in collaboration with one another or with fashion brands. In 2021, for example, Dior opened a spa in LVMH's Cheval Blanc Paris hotel, offering treatments using Dior's professional skin care products. Brands can position such services as more than a massage or facial, but rather as a self-care ritual that offers customers a transformative mind and body experience.

Brands that understand the advances in the wellness space, their ability to leverage expertise in a unique and credible way, and the influence of wellness on traditional beauty products are likely to gain a competitive advantage in the market as holistic beauty becomes a new benchmark for quality among global consumers.[29]

The Cheval Blanc Paris hotel. Getty Images.

EXECUTIVE INTERVIEW

Ulta Beauty: Looking Inside a Big Bet on Wellness

By Priya Rao

Chief Merchandising Officer, Ulta Beauty

The "skinification" of hair, sexual wellness products and better-for-you ingredients are just some of the ways wellness has infiltrated beauty. Ulta Beauty's **Monica Arnaudo** shares why she believes we are at the precipice of a changed industry — one that values mind, body and spirit.

As the beauty category continues to outpace the global economic outlook, conglomerates, retailers, brands and investors are looking for even more opportunities to evolve. And right now, there is no greater growth vehicle within the segment than wellness. Whether it is the "skinification" of colour cosmetics and hair, or the debut of sexual wellness products in the beauty aisle, companies are willing to stretch the traditional limits of the category and firmly say beauty and wellness are one in the same, according to Monica Arnaudo, chief merchandising officer of Ulta Beauty.

For its part, the US beauty retailer has been on a journey to ensure its offering keeps pace with the changing definition of beauty, underscoring that products and services can and should make people not just look good, but feel good. From first introducing its wellness concept in its bath and body assortment in 2018, to later developing full wellness sections within stores that today include more than 150 brands, consumers would be hard pressed to not find products and services that enable them to take "better care of themselves."

Over the last five years, the beauty industry has become enamoured with wellness and themes like 'beauty from the inside out' and self-care. Where have you seen the biggest changes in terms of product development, brand positioning and marketing?

The reality is that beauty, as a stand-alone category, is a feel-good category, and wellness is all about feeling good. There's always been a bit of a blurring between the two. The catalyst for this really came more to the fore because of what transpired during the pandemic when people really were focused on taking better care of themselves.

We saw that really start in skin care. People started adding more products to their routine and spending more time on their routines. It evolved to hair. If you think about the product piece, we really started to see an evolution of more scalp treatments and more masking as it relates to hair. Then, of course, it eased into more of a do-it-yourself routine.

And here we are today. The amazing thing for the beauty industry in total is that people haven't changed their routines. The consumer, and especially the beauty enthusiast, is still spending that amount maintaining their routines in skin and hair; and now they're spending more time in makeup again because they're not home, they're out — they're back in the workplace, they're going to weddings, they're going to events, they're travelling, they're taking vacations.

While that was going on, there were other things being discussed — for example, the importance of taking care of our mental health. There is definitely an association with beauty and how it can help with that because beauty does really help people feel better.

When you think about the marketing and the language, we saw an influx of communication about taking better care of yourself and spending time in that way, which completely ties into wellness — 65 percent of consumers connect beauty and wellness and, actually, for the beauty enthusiast, that's 72 percent.

Where has Ulta Beauty been in the category historically and what is your strategy going forward?

Historically, we played in the category that I would describe as everyday care, in things like deodorants and oral care and bath and body products. Then we launched the wellness shop in 2021. … We wanted to create something that crossed categories, was very easy for our guests to shop. We offered products that were very accessible, and a range of products. We really wanted to focus on the areas that we knew our guests had interest in.

We went about five years ago from more of the everyday basic care to laying out these five pillars, which everyday care is a part of. We added supplements and ingestibles, so that was pillar number two; relax and renew, this is where during the pandemic we really saw people leaning more into this space; and spa at home, again, people taking time during the pandemic. Then we launched intimate wellness at the end of Q3 of 2022, online only, and this was definitely a space that, again, we knew that our guests, especially the younger consumer, wanted to have a place to shop where they could learn about the products. It was a comfortable place for them to explore.

We started with about 400 stores and now we're in 800 stores and we've got the wellness shop online.

When you think about brand partners, what do you look for?

It always starts with the guest and where we might have opportunity. Then, when we are looking at a specific brand, and this is the piece that crosses categories: are they fulfilling a need, is there a founder involved, what is the authenticity? I think of Love Wellness and the need that was there for easy-to-relate-to supplements and ingestibles that were solution-orientated, focused on things like bloating, for example.

We also look for a founder who's highly engaged and wants to build the business with us. ... We've been on a journey of listening to our consumer and meeting various brands in this space. Our emerging brand team reviews so many new brands every year, hundreds upon hundreds, so we've seen a lot more in wellness.

What about the blurring of the categories? We are already seeing things like oral wellness now and products that you may have found in the drugstore aisle being elevated and positioned as wellness, like supplements.

It will continue to blur because, to your point, we're seeing it across multiple categories. ... People are moving beyond defining beauty through societal standards towards individual qualities like confidence and self-acceptance that radiate an aura of beauty, and beauty products play a role in every step of our mental health journey.

We define wellness as for the mind, body and spirit.

There used to be a negative connotation of mental health. Now it's so much more acceptable. It's okay to talk about maybe having anxiety, and things like this.

How important is it to bring that global perspective of wellness, like traditional Chinese medicine or ayurveda or the origins of K-Beauty, to stores and beauty retail?

It's extremely important because in order to fulfil our guests' desires, we have to take a holistic view. Our studies show that 41 percent of people globally believe that wellness is more of a communal and societal issue than an individual goal. So again for us, it's our responsibility to look at it in a holistic, global way and, to your point, maybe look at some of these remedies that come out of Asia, in general, that's an important piece of it. We need to have a global perspective.

We will see luxury brands delve more into wellness or wellness brands take more of a luxury approach.

Ulta Beauty recently expanded its luxury assortment. How do you see luxury intertwining in wellness today and in the next three to five years?

Luxury is a segment of the business that has continued to grow. Even when you think about what transpired during the pandemic and when maybe people were pulling back a little bit on their spend, they were not pulling back in luxury beauty; that was actually an area where they were leaning into more. The other aspect that has propelled luxury beauty is the influx of social media, especially TikTok. We know that 80-plus percent of Gen-Z and Millennials will buy a luxury beauty product if they see it on TikTok, on social media.

A little over a year ago we launched Chanel No1, which was not only tied to Chanel, but luxury fashion. The other cool thing about that brand is that it was taking a clean, conscious approach. ...

Wellness will probably be interconnected with luxury and perhaps we will see either existing luxury brands delve more into wellness-type products or wellness brands take more of a luxury approach.

To target that type of consumer, there's so much more room to go into spas, or whatever La Prairie does in its clinics. It just seems like the sky is the limit there.

That's such a good point because what else do you think of when you go to a spa? You think, 'I'm going to a spa to take good care of myself, to feel better,' and that's what wellness is all about, and you want to have luxurious products when you do that.

An Ulta Beauty store. Getty Images.

Do you think wellness will become — or maybe it already is — a top revenue driver for yourself and for other players in beauty?

Because we're optimistic about the growth potential and the growth that we're seeing currently in the brands in the assortment that we have, I think it will continue to be a growth driver for us. We have more than 150 brands that touch wellness [and] have about 600 brands in our assortment in total.

Do you think we're going to get to a place where the terms 'beauty' and 'wellness' are interchangeable?

Yes, absolutely. Based on all our insights, I think we're there.

You did hit on something that we also learned in our insights, and it is such a big part of beauty and wellness; it's about how you feel about yourself – it's not always the external – I look in the mirror and because of this ... It's that I feel this way. Beauty is there to enhance, it's there to help you feel even better, but so much of it is internal.

This interview has been edited and condensed.

03. Decoding Gen-Z

As Gen-Z grows up, brands must adapt, finding new ways to speak their language. This may require retiring traditional ways of doing business — from marketing to product development — and rethinking assumptions about this diverse, digitally savvy and demanding generation that prioritises value and efficacy when choosing their beauty brands and products.

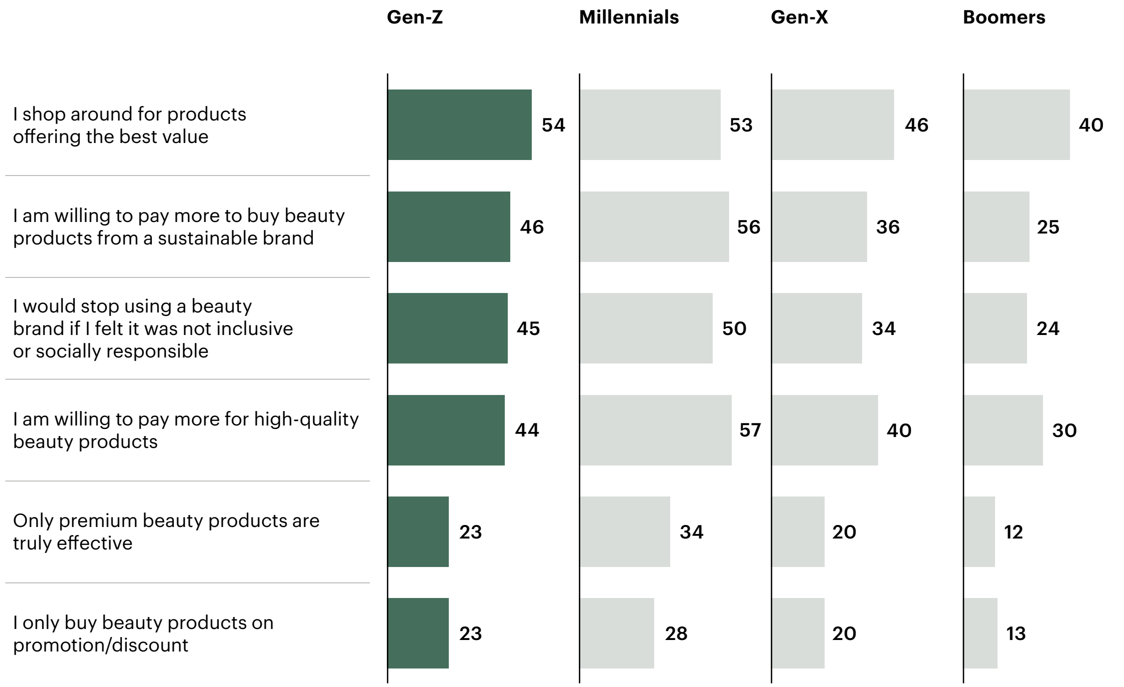
KEY INSIGHTS

- Gen-Z shares some similar priorities with Millennials when it comes to their beauty habits, with a focus on authenticity and diversity, and a desire to shop for beauty in stores in addition to online.
- Nearly half of Gen-Z consumers said they research beauty products extensively before purchase, with a similar share learning about product ingredients and benefits beforehand, according to new research from McKinsey.
- Gen-Z is more loyal than many brands think. Even as they desire to try new products, nearly 60 percent are willing to keep buying from their favourite brands.

Exhibit 8

Gen-Z seeks out beauty products offering the best value

Agreement with statement,
% of global respondents



Q: Please indicate if you agree with each of the following statements.
Sample sizes: Gen-Z 1,947; Millennials 4,333; Gen-X 3,952; Boomers 1,778

Source: McKinsey Beauty Consumer Survey, March 2023

More than any other cohort, Gen-Z is deeply connected to beauty. And why wouldn't they be? These digitally savvy teens and twentysomethings, born 1996 to 2010, have been engaged in the category from a young age, thanks to technology at their fingertips connecting them with influencer- and celebrity-founded product lines, and "Get Ready with Me" videos on TikTok and YouTube. They are more willing than older cohorts to experiment with makeup, skin care and hair products, perhaps because of how quickly beauty's viral trends spread on social media. According to McKinsey's 2023 global consumer survey, 45 percent of Gen-Z respondents said they try new brands every two to three months. For brands that hit the mark, though, Gen-Z shoppers show high levels of loyalty, with close to 60 percent willing to stick with their favourites, compared to around 50 percent of older generations, making the generation worth investing in.

Gen-Z has outsize potential to drive the beauty market's growth. By 2030, when they will represent a quarter of the world's population, their income will reach $33 trillion. This will exceed that of Millennials, born 1980 to 1995, by 2031.[30] Gen-Z individuals are also opinion leaders — much more so than the generations that preceded them. Studies by the National Retail Federation, as well as First Insight and the University of Pennsylvania's Wharton School, show that Gen-Z exert substantial influence over the purchasing behaviour of older cohorts,[31] with close to 90 percent of parents stating that their children influence their buying decisions.[32]

Close to 40 percent of Gen-Z consumers prefer gender-neutral beauty products, compared to around 30 percent of older generations.

Gen-Z beauty consumers. Pexels.

Yet Gen-Z is not a monolith: the youngest Gen-Z individuals are just in their teens, while the oldest have jobs, rent and bills to pay. Largely because of both their age and the fast-evolving digital world that they are so firmly part of, Gen-Z's preferences are in flux as they figure out exactly who they are.

So how can beauty brands get ready? Knowing who Gen-Z is today — and how quickly their preferences can change — is critical for consumer industries like beauty. That starts with interpreting the hallmarks already evident across this generation while questioning widely accepted attributes.

Gen-Z Wants It All

Unlike their predecessors, Gen-Zers do not want to make compromises. Millennials initially drove much of the mainstream interest in diversity in the beauty industry. Yet, as the most diverse generation to date when it comes to gender, ethnicity, sexual orientation and more,[33] Gen-Z is more adamant that brands, products and marketing stand for something beauty products. Bigger brands have adjusted their playbooks to keep pace with this shift. YSL Beauté, for example, launched Nu Collection, a genderless skin care and makeup line, in 2021 and tapped American rapper and singer Lil Nas X as one of its ambassadors in 2022.[35] Armani Beauty, meanwhile, created Gen A, a collective of next-gen international actors including Maude Apatow, Jonathan Daviss and Lili Reinhart to appeal to a younger clientele.

At the same time, brands are more frequently working with male, transgender or non-binary models for traditionally female-orientated product ranges such as makeup. One example is Shiseido's partnership with brand ambassador and transgender actress Hunter Schafer.[36] McKinsey research shows that Gen-Z men in Asia already embrace makeup products, with around one third using makeup regularly, while in the US and key European markets, between 5 percent and 10 percent of male respondents use makeup.

To cement Gen-Z loyalty, companies must

Gen-Z is adamant that brands, products and marketing stand for something and reflect their values.

and reflect their values relating to topics ranging from mental health to climate change, while also acknowledging their diversity.

Young shoppers, for example, seem to connect to Selena Gomez's Rare Beauty brand in a way that extends beyond its products. The American singer and actor's outspokenness about her own mental health issues has helped to portray the brand as a safe space for Gen-Z. The brand launched the Rare Impact Fund to give people access to mental health resources and held workshops during the pandemic for consumers to connect with one another.[34]

Meanwhile, Gen-Z brands like Topicals and Eadem are addressing skin issues typically found among consumers of colour, such as hyperpigmentation and dark spots, deepening the beauty industry conversation around skin tones that was started by brands like Rihanna's Fenty Beauty.

McKinsey's survey shows that close to 40 percent of Gen-Z consumers — compared with about 30 percent of older generations — prefer gender-neutral therefore develop and communicate authentic brands that connect with Gen-Z on an emotional level.

Prioritising Value and Efficacy

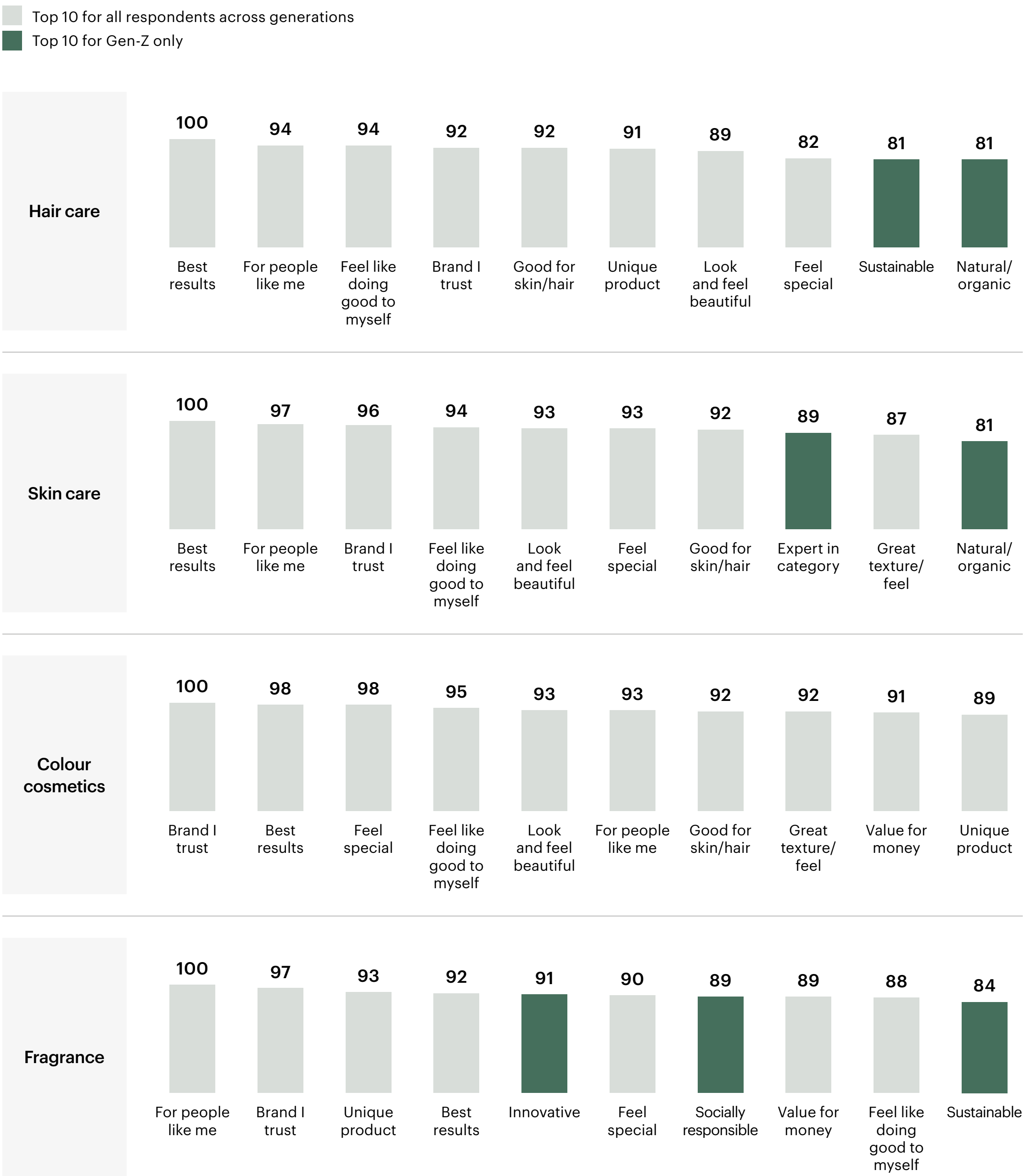
Similarly to Millennials, close to half of Gen-Z report checking product ingredients and doing extensive research on their benefits before purchasing, compared with one-third of Gen-X (born 1965 to 1979) and one-fifth of Boomers (born 1945 to 1964). However, Gen-Z does not equate higher price points with quality like their older counterparts: one in two Gen-Z consumers report shopping for the best value for money and fewer than one in five consider products from premium beauty brands to be effective, compared with about one in three Millennials.

The Ordinary is a favourite among younger shoppers, in part because of its transparent strategy for product and price.[37] The brand makes clear to consumers that its products have the same ingredients as other, more expensive lines.

Exhibit 9

Gen-Z prioritises products that deliver the best results from brands they trust and values sustainability more than older generations

Top 10 purchasing criteria for Gen-Z by category,
% of global respondents



Sample sizes: Gen-Z 1,947; Millennials 4,333; Gen-X 3,952; Boomers 1,778

Source: McKinsey Beauty Consumer Survey 2023

Bubble Skincare's overnight hydrating mask. Bubble.

Even when the skin care brand raised prices in 2022, it explained why, citing the rising cost of raw ingredients, packaging and shipping, as well as cost-of-living increases for employees.

Brands should not shy away from their mass or masstige positioning. For example, marketing for Bubble Skincare, a Gen-Z line launched in 2020, underscores the products' affordability. Yet, while Gen-Z is driving growth in the mass and masstige segments, beauty brands can also find success with premium products if they can justify higher prices and do not rely on premium positioning alone by demonstrating additional value. Nearly half of Gen-Z respondents report being willing to pay a premium for products if they are higher quality. On top of this, 46 percent are willing to pay a premium if they consider a brand to be sustainable. These figures may increase along with Gen-Z's spending power.

Being Real and In-Person

Gen-Z generally prefer unfiltered aesthetics which speak to their demand for authenticity. Unlike Gen-X and Millennials when they were in their teens and twenties, who prioritised brand reputation and experiences respectively, younger shoppers today want realness and relatability. Indeed, while Millennials generally aspired to a singular ideal of beauty — coining the term "Instagram face" — Gen-Z values authentic self-expression and want to be part of a brand's story. In essence, the term "community" has higher stakes for Gen-Z than any other generation.

E.l.f. has been quick to involve younger shoppers in its brand story, so much so they were the inspiration for the US brand's first television advert promoting its primer, which aired during the Super Bowl in 2023. E.l.f. chief marketing officer Kory Marchisotto said fan interest in the product — generated on TikTok and other social media platforms where Gen-Z congregates — drove the TV strategy: E.l.f. fans called the primer "sticky jam," "sticky slime" and "space glue," among other monikers, which was why actress Jennifer Coolidge, the star of the ad, found herself in "sticky situations" in the slapstick commercial directed by "White Lotus" creator Mike White.

Indeed, Gen-Z is the first digitally native

Jennifer Coolidge in E.l.f.'s Super Bowl advert. E.l.f.

generation. Its use of social media has propelled brands such as skin care label CeraVe, which did not necessarily set out to target the generation but found success on TikTok as users and influencers highlighted the brand's lower-cost but effective products.[38]

Yet Gen-Z is not as digitally fixated as some believe. While 50 percent of Gen-Z respondents said they are most likely to learn about new products from social media personalities, particularly on TikTok, 41 percent also cited brick-and-mortar stores as an important channel — roughly the same percentage as older survey respondents.

When Gen-Z individuals shop in stores, they have a clear sense of what the experience should be, with more than 85 percent citing high levels of service — such as customised skin and hair diagnostics — and pleasant store environments as very important purchasing factors.

Retailers are adjusting the brands they stock accordingly. Ulta Beauty was the most popular destination for beauty purchases for US Gen-Z in 2022 largely due to its stock of Gen-Z favourites, according to a survey by Piper Sandler.[39] Meanwhile, Sephora dedicates shelf space to popular Gen-Z brands with in-store categories like "Hot on Social Media," showcasing products that have gone viral among the online beauty community, which the retailer nurtures through partnerships with influencers and key opinion leaders.

For both brands and retailers, staying attuned to Gen-Z — even while targeting other generations — will be a critical piece of any growth puzzle. Building a meaningful, authentic and collaborative connection with this cohort can help inform where and how to best direct a business's focus, from pricing strategies to product lines to marketing. This will require brands to ensure their products encapsulate meaning beyond their material value. Above all, beauty leaders must ensure their brands grow and mature alongside Gen-Z, while also being seen as a positive force for change and innovation in how Gen-Z experiences beauty.

EXECUTIVE INTERVIEW

Topicals: Connecting With the Multidimensional Gen-Z Shopper

By Diana Pearl

Founder, Topicals

Olamide Olowe has written her own playbook ever since founding her skin care label, Topicals, for connecting with Gen-Z consumers through mental health advocacy and by opening a conversation with her brand's fans.

For many beauty brands, figuring out how to connect with Gen-Z is akin to deciphering a foreign language.

But not for Olamide Olowe, the founder of US skin care label Topicals. As a member of the generation herself, the 26-year-old has built a company on many of the principles that matter most to Gen-Z consumers: mental health advocacy, racial inclusivity, and an open dialogue and feedback loop between consumer and brand. These competitive advantages have resonated with not just consumers, but also investors. She's the youngest Black woman to raise over $2 million in venture capital funding, having raised $14.8 million as of April 2023, and has her sight set on making an effective product for all types of chronic skin conditions, for Gen-Z and beyond.

Along the way, she's discovered for herself what the power of community really means for a beauty brand. She likens a brand's community to a country's citizens, in which loyalty should run both ways. "You feel like it owes you something, but you also feel like you owe it something," she says.

As a Gen-Zer yourself, and a Gen-Z founder, what do you think that this generation of consumers is really looking for from their beauty brands?

Good product is table stakes. Gen-Z, because they're more cash-strapped [than older generations] are not just spending money on any and everything. They really want to know that it works. Reviews, before-and-afters, are really important to this customer.

On top of that, storytelling is essential. Gen-Z really loves messages that are nostalgic, messages that … just remind them of a simpler time. They've democratised a lot of things, and the stories they want to hear in efforts to democratise beauty are more inclusive. They're stories that tell narratives around the LGBTQ+ community, around Black and Brown consumers, around differently abled consumers. That's really amazing, because now instead of beauty looking singularly, it looks multidimensionally.

As a Gen-Z founder, what do you think is the most common misconception about your generation?

I always say that Gen-Z is a psychographic, not a demographic. The internet is the great equaliser because people are sharing ideologies across generations. I know people who are over the age of 50 who act more Gen-Z sometimes than my little brother, who is 20. I don't think that the way that Gen-Z approaches businesses or interacts with experiences is relegated just to a specific age.

The misconception that a lot of people have around Gen-Z is that they're fickle. I think Gen-Z is probably one of the most loyal demographics, but they're loyal to what they believe is true. There are a lot of things that aren't as true as people think that they are. That is why people think, like, 'Oh, Gen-Z changes their mind,' or, "Price is the only thing that really impacts Gen-Z," because people will figure out how to pay for certain things.

What mistakes do you see businesses make when they try to connect with Gen-Z?

They try to be everything to everyone. You have to be everything to one. My one is people with chronic skin conditions, people who love culture, people who are really community-orientated, people whose mental health has been an issue for them as it relates to their skin condition. Those are very specific things that I look for in my customer.

People may not be all of those things; they may fall into one of the buckets. But I was super adamant about who it was that I was serving, and because of that, I'm able to tailor my marketing, and I don't [share] deluded stories and messages across the chain, across the stack. I tell very specific stories, and it may not resonate with certain people, but that's okay.

Some brands aren't supposed to get big, because if they get too big, they then lose the niche. When a brand is no longer in touch with anyone, it becomes a dying cash cow, where there's a tonne of revenue but no innovation and no growth, because they can't pick one message to speak to because they believe it alienates another core [customer].

What role does TikTok play in curating Gen-Z's beauty tastes, and what sort of role does TikTok play in your own business?

To me, it's almost like Google 2.0, because it has a visual element, and the information is being presented by everyday people.

It's done really well for us in


FADED

just spreading awareness about what we do at Topicals, not just our products, but also mental health advocacy. It's been really important and interesting to see how people have taken our products and used them not just as a medium to show people before-and-afters or treatment on skin conditions, but also as an opportunity to have open conversations.

We know that we're not going to solve the issue of mental health, but we want to at least open up the conversation.

Do you think brands should experiment with emerging platforms? You never know what's going to be the next TikTok.

There are so many shiny objects and so many new things that are constantly launching, where you're like, 'Should I jump on this? Should I not do this?' Brands never want to be left behind, but you also have limited resources. What people don't realise is … there's only so much you can do with a limited budget and a small team. Especially for a lot of the indie brands that are really driving innovation in the industry, you have to choose certain things.

If you are the first on some of these platforms, you have to do a lot of the groundwork. But I think you should be in touch. We have a community programme of over 4,000 members called Topicals Insiders; they run the gamut of age and where they live in the United States and their backgrounds. They keep us super hip and young.

Community has become such a buzzword. How do you think that brands can really connect authentically with Gen Z?

Everyone just thinks, 'If I get a cheap product or a quick, cool, viral-type product, then I'll build community,' but community isn't followers and it's not customers, although they can overlap. A community is a citizenship to your brand world. If you are an American citizen, you feel pride to be an American. If you're French, if you're Nigerian, if you're Middle Eastern … you feel a sense of entitlement to that country. You feel like it owes you something, but you also feel like you owe it something. Citizenship is really important.

So what language do you speak [when communicating with those citizens]?

Topicals has been really adamant about not using negative language as it relates to your skin. Quite literally, the citizens of the Topicals world are called "Spottie Hotties" because, for us, we just make fun of what people have made fun of us for, this idea of having spots or not having clear skin.

What would be your advice be to the next crop of Gen-Z founders, and particularly Gen-Z founders of colour?

People need to understand that VC is rocket fuel. If you're not building a rocket, if you don't want to build a business that's going to be doing north of $50 million to $100 million in sales in the next five to seven years and you don't want to dedicate your life to that, there are — and we should be creating more — other ways to fund businesses.

It's important to understand what you're walking into when you take venture capital. Do you want to build a very, very big business, and are you ready to sell this business, part ways with this business in five to seven years, or is this something that you want to keep in your family forever? Or do you want optionality?

If you want optionality, I would say you just don't take VC and you take other types of capital until you've then decided VC is the route for you. I do think more founders, Black founders, should have access to VC capital as well, if that's what they've decided. Raise with a plan to execute, and execute like you'll never raise again.

What is next for Topicals? How do you see the business continuing to grow and connect with new audiences?

We're going to continue to innovate in different skin conditions; we want to create products for every skin condition that exists.

Our goal is to continue to donate money. We've donated $100,000 since our inception to different mental health causes. … By 2026, we want to have educated 10,000 skin care professionals on the connection between skin health and mental health, which is called psychodermatology, and on skin of colour.

Fifty percent of dermatologists say their medical school training didn't prepare them to treat skin of colour. So our hope is to also educate professionals. Over-the-counter skin care is great, but having an aesthetician or a dermatologist also look at your skin is part of this toolkit.

This interview has been edited and condensed.

Topicals eye mask. Topicals.

04.
The Scale Imperative

For many emerging beauty brands, the early days of getting up and running has been the relatively easy part. Now, they need to confront the greater challenges that continuing their growth trajectories entail. In an industry that has become overcrowded, geographic and channel expansion will likely be critical for gaining further market share.

KEY INSIGHTS

- In a group of 46 brands, each with global retail sales of between $50 million and $200 million in 2017, only four surpassed the $400 million mark five years later.
- Material growth for young brands will require a laser focus on expanding their channel mixes, regional footprints and — at a later stage — categories.
- Challengers, owing to their sheer number, pose a threat to the market share of incumbents.

Fenty Beauty products on display. Getty Images.

The first wave of digitally innovative independent brands burst onto the beauty scene in the early 2000s and disrupted an industry long dominated by conglomerates and brick-and-mortar retailers. To grab market share, these challengers used a combination of tactics to their advantage: direct-to-consumer selling, low-cost marketing, outsourced product development and a focus on underserved consumer groups to shake up beauty's status quo.

But many of these challengers have been unable to build on their early momentum. Some of the buzziest brands of recent years haven't grown much: in a McKinsey analysis of 46 brands that launched after 2005, each with global retail sales of between $50 million and $200 million in 2017, only four had surpassed $400 million in sales five years later.

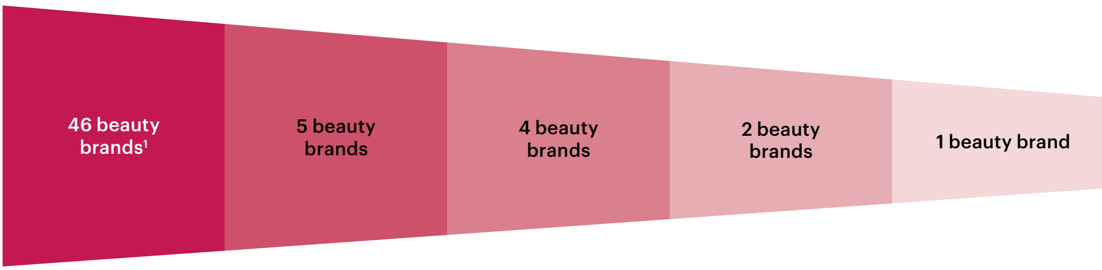
One critical reason for the slowed momentum is that the market is now highly saturated with competition from all sides. Legacy brands have taken a page from the newcomers' book, updating product portfolios and marketing, with considerably more capital. At the same time, indie brands are launching at a rapid clip. All this has created an even more challenging environment than when early disrupter brands got their start.

Tellingly, the four brands that have scaled beyond $400 million are based in the world's largest beauty markets: Fenty Beauty and The Ordinary in North America, and Winona and Adolph in China.[40] While Fenty Beauty and The Ordinary went global early

Exhibit 10

Very few new beauty brands have scaled sufficiently to surpass $400 million in global retail sales

Beauty brands founded in 2005 or later by annual revenue after five years of business



$50M–$200M in sales in 2017	$250M+ in sales in 2022	$400M+ in sales in 2022	$750M+ in sales in 2022	$1B+ in sales in 2022
Addiction	Winona	Winona	Winona	Winona
Botanist	Fenty Beauty	Fenty Beauty	Fenty Beauty	
Bulldog	The Ordinary	The Ordinary		
Jimmy Choo Parfums	Adolph	Adolph		
KeraSys	Harry's			
Nature Republic				
New York Color				
Tony Moly				
TS Shampoo				

1 Includes skin care, hair care, colour cosmetics and fragrance brands founded in 2005 and later that generated between $50-$200 million in global retail sales in 2017

Note: Brands are non-exhaustive

Source: Euromonitor, April 2023

in their lifecycles, Winona and Adolph have stayed focused on China. Adolph headed into the hair care market, where Western conglomerates have long had a strong presence, launching its prestige shampoos in 2013. Dermatology-focused Winona, founded in 2010, zeroed in on sensitive-skin products tailored to common ailments in China.

The beauty players that have defied growth challenges offer lessons for other brands on the critical steps to achieving scale: channel expansion across brick-and-mortar retail and online, and disciplined category expansion.

Mixing It Up

Most of the brands that exceeded the $400 million retail sales mark in McKinsey's analysis significantly diversified their sales channels to grow their customer base. In the US market, for instance, they partnered with beauty retailers like Sephora or Ulta Beauty, online and offline.

There are a host of reasons why young brands need to recalibrate their channel mixes. Certainly, the pandemic played a role in amplifying digital opportunities as lockdowns essentially halted brick-and-mortar while spurring e-commerce. The case for a mix of both online and offline is now strong: McKinsey's 2023 global consumer survey found that among respondents who buy beauty products online, 36 percent visit the retailer's physical store, and 28 percent visit other physical stores, before making a purchase online. Customers want to see, test and smell beauty products before making purchases.

Meanwhile, finding the right retail partner has been a central part of expanding a brand's reach.[41] The physical and online footprints of multi-brand retailers — which in the US, for example, include beauty players like Sephora and Ulta Beauty, big box retailers like Target and department stores — are hard for many brands to match on their own. And the choice has been widening to include other beauty retailers like Bluemercury.

In recognition of this, brands that previously sold only through online direct-to-consumer channels have begun turning to multi-brand retailers to generate sales. The seeds were already being sewn pre-pandemic: for example, men's grooming and skin care company Harry's, which launched as an online pure play, forged short-term partnerships with J.Crew, Barneys and several barbershops before selling its products in Target, Boots and other retailers. "It gave us the conviction that people wanted to experience our brand in a retail environment," co-founder and chief executive Jeff Raider told *The Business of Fashion*. The brand now generates more than $250 million in annual sales. More recently in 2023, Glossier, which also expects to exceed the $250 million annual sales threshold this year,[42] entered Sephora as part of a new strategy to spur sales growth.[43]

Controlling the Trajectory

Beauty upstarts have long known that finding and articulating their unique selling point can make or break their businesses. But today, getting it right is far more complex than it once was amid competition from a growing number of brands. Inclusive imagery, influencer partnerships and ingredients transparency are table stakes, not differentiators. Brands must offer shoppers a clear, unique value proposition, rather than playing copycat. For example, Winona identified white space in China, developing and marketing products in collaboration with dermatologists and other science and medical professionals, drawing on its hometown of the Yunnan province in southwestern China, which is known for its medicinal species of plants.

The international expansion timeline is also critical. For independent brands, pace of growth can be a challenge. Expand abroad too quickly and a brand risks spreading itself too thin and losing focus; grow too slowly and competitors might race ahead. In the case of US-based drugstore skin care brand CeraVe, it focused on growing domestically for 10 years and began selling internationally only after it was acquired in 2017 by L'Oréal.[44] Yet even today, the brand generates most of its $1.3 billion in retail sales in North America. To be sure, brands that are headquartered in smaller markets will likely need to consider international expansion sooner.

The most successful emerging brands wait until they reach significant scale to expand their product range, focusing initially on only one main category. Makeup brand Fenty Beauty, for example, which now exceeds $500 million in sales, launched its first skin care items three years after its initial debut when it had reached over $400 million in annual retail sales. It leveraged its reputation for inclusive makeup shades for its first small expansion into genderless cleansers and serums, prioritising skin care items closest to its core makeup range. Similarly, Hourglass Cosmetics expanded its colour range into skin care with a limited assortment of products in 2014, 10 years after the brand was founded. It wasn't until 2021, during the pandemic, that the brand further leaned into skin care by introducing new products to the portfolio.

The most successful emerging brands wait until they reach significant scale to expand their product range, focusing initially on only one main category.

Fuelling Growth

While securing investment from corporates or other investors makes it more likely that a brand will

A Sephora store in China. Shutterstock.

achieve scale, there are no guarantees. According to McKinsey research, out of a group of 78 recently founded global beauty brands that secured venture capital, private equity or another type of investment above $2 million between 2010 and 2015, 56 percent still generate less than $100 million in annual retail sales today, despite many having been acquired by corporates or financial investors — while 31 percent have gone out of business.

Arguably, some of the toughest decisions start-up founders and their executive leadership teams face as they aim to fund their transition from niche start-up to established player involve when and whether to sell a minority or majority stake in the business. The UK makeup brand Charlotte Tilbury, for instance, secured a minority investment from Sequoia Capital Partners in 2017 to widen distribution, including expansion into the Middle East, and saw sales grow by more than 30 percent year on year. In 2020, it sold a majority stake to privately owned fashion and fragrance conglomerate Puig to accelerate international and product expansion. Even with the reported $1 billion-plus deal with Puig, Tilbury holds a minority stake and is chairman, president and chief creative officer of the brand, with Demetra Pinsent, the brand's original chief executive, remaining.[45]

Even after a sale to a conglomerate or other large investor, challengers and their new parent companies need a plan to help ensure the original essence of the brand is not lost or overshadowed by other corporate priorities. When Procter & Gamble's beauty division bought Mielle Organics at the start of 2023, Monique Rodriguez, a Black businesswoman who co-founded the US textured hair care brand with her husband Melvin in 2014, took to social media to assure followers that product formulations would not change. According to P&G at the time of the deal announcement, the brand, like others in its beauty division, would operate as an independent subsidiary, while focusing on expanding into underserved Black communities.

Independent brands will need to lean into innovation and tactically build out their channel strategies, international footprints and product lines to find themselves in a virtuous cycle of growth. In such a fast-moving sector, brands that fail to scale may find themselves running to standstill. Beauty is too crowded and competitive to support the plethora of brands coming to market over the long term. Ultimately, only a select group of newcomers will be able to establish themselves among the industry's leading brands in the years to come. Yet incumbents cannot be complacent: while only a few challengers achieve significant scale, the sheer volume of independent brands in the industry is chipping away at the market share of larger players — which means the latter must continue to innovate and consider strategic mergers and acquisitions to stay ahead of the curve.

EXECUTIVE INTERVIEW

Byredo: Putting a Niche Fragrance Brand on a Path to Growth

By Tamison O'Connor

Founder, Byredo

Byredo is one of the big success stories of the luxury fragrance industry, hitting €120 million ($130 million) in annual revenue before its acquisition by luxury group Puig. Founder **Ben Gorham** breaks down how indie labels can flourish in a crowded market.

In a crowded and competitive beauty market, patience can pay off for indie brands looking to achieve both scale and longevity, says Byredo founder Ben Gorham, who spent years laying the groundwork for the recent explosive growth of the high-end fragrance label he founded in 2006. The Stockholm, Sweden-based company's journey was a slow burn: while the brand operated in key global markets from the outset, its growth potential was limited in the early days thanks to its distribution strategy built on scarcity, with Gorham carefully controlling product supply to keep Byredo aspirational.

The strategy, however, helped catapult Byredo to commercial success, with the brand hitting €120 million ($130 million) in annual revenue in 2021 before selling a majority stake to Spanish fashion and beauty group Puig in May 2022. More importantly, after 17 years on the market, Byredo remains a cult and coveted name in beauty.

While the landscape has changed dramatically since Byredo's early days, making the jump from niche player to established global name is still within reach for other start-ups, Gorham says: a diversified distribution channel mix, disciplined category expansion and creating relevance in an authentic way can all form part of a winning formula.

Why was 2022 the right time for Byredo to bring on investment from a big strategic partner?

When I look at the strategic phasing for the company, it's been more in relation to distribution strategies, cash flow needs, the complexities of globalisation — so the investments that I needed to establish subsidiaries — and then marketing. I've been at it for 18 years. It's become clear that the brand and the company have gone through very challenging phases.

I set out to create a global brand from the beginning. In retrospect, at times we may have spread ourselves a little bit thin; operating in every quarter of the globe is complex. When you talk about beauty, you're also talking about being in stock, you're talking about logistical challenges, you're talking about regulatory [considerations], you're talking about regional preferences, you're talking about culture.

The challenges that stood in front of us when we partnered with Puig were very much about development and production, so quality at scale. Puig being vertically integrated brought a great opportunity for us to lower our cost of goods but also improve the quality of our products. Puig is one of the few fragrance experts within these larger conglomerates.

How would you characterise your approach to being a global brand today?

It's continuing this idea of thinking global and acting local. Communities is a word that's been thrown around a lot, but I think it's something that people truly need to focus on. They need to understand the smaller ecosystems. For Byredo, even though we have this global footprint, we're almost taking a step back in becoming local experts.

For small beauty brands, a big distribution partner like Target or Sephora can have a huge impact on scale, but Byredo has chosen a different route. How do you think the distribution game has changed for indie brands?

Byredo comes from fragrance, so a lot of our structures were built on a fragrance business. A lot of the potential chains or distribution partners were not doing huge volumes in fragrance. The other thing to remember: today we have a diverse channel mix. That helped us navigate the pandemic, but it's also helping us navigate skyrocketing [customer] acquisition costs, digital marketing and the turn of social media, the complexities of influencers, the downward turn of American department stores. Our diverse channel mix was how we were able to pivot.

We made a choice at Byredo to identify the clients and then meet them where they are. The reality is that we live in an omnichannel world and customers are online and they're in retail stores and they're in wholesale doors. Out of inclusion and for practical but also philosophical reasons, we decided to be in those places and do our best to compete in those places. Direct-to-consumer was this idea that you owned the customer and you did that through a variety of ways — one of them being digital online and the other one, social, but also retail.

I think for most direct-to-consumer brands, the opportunity lay in digital scalability because retail is costly and personnel-intensive. What really changed is

that this was a direct-to-consumer relationship through digital marketing acquisition costs. It turns out that social media is also like a wholesale channel — the only difference is that Google is the wholesaler as opposed to Neiman [Marcus].

It's also what caused a lot of hiccups for the direct-to-consumer brands [because] that specific wholesaler increased their price overnight, three nights in a row. Sometimes when I speak internally about some of the complexities I see there [I say] it is the equivalent of your landlord coming on Monday and raising the rent and then coming back on Wednesday and raising it again. So to build or hinge your business on one of these channels as they continue to evolve is dangerous.

Byredo leveraged scarcity and its reputation as a niche player to maintain allure among consumers and build desire. But that's notoriously difficult to scale. How do you strike the balance between niche and mass appeal, especially when you're growing fast or you're part of a bigger group?

It's the eternal dilemma: how to control supply and demand, and to your point, at scale how do you still maintain the desirability of a brand? Defining what that scale is — I don't necessarily think it's about numbers. I think it's about perception.

For us, it's been focussing on authenticity and quality. Scarcity was one of the pillars of luxury culture. But I think with the "marketisation" of luxury and

Byredo's first makeup collection. Byredo.

fashion, authenticity and quality are the things that are going to take you beyond that.

If I approach it as a consumer myself, the brands and the products that continue to be in my life are the ones that qualify under those two criteria: being authentic and being [high quality]. I can find scarcity in other parts of my life if that's important.

How do you see this evolving?

Scarcity is a very interesting tool. We're still living in an era of rapid growth and a lot of brands are still very interested in growing things very fast. We took a very long-term approach, which in retrospect was painful for many years because it obviously requires patience. You're probably saying no more than you're saying yes to things, you appear to be leaving a lot of things on the table. But I think brands have an opportunity today to pace themselves a little bit. I am a huge advocate for seeing the journey as more of a marathon.

Byredo's roots are in fragrance, but you recently expanded into makeup and there's a skin care launch in the works. What role does category diversification play when you're thinking about scale?

We entered into fragrance without any background in the category, with no expertise. We kind of employed this idea that it could be done differently in a unique way. Part of that philosophy was to be executed in makeup from a purely creative place. I think what's different today than 18 years ago when we started is that we have a large group of clients and customers. Part of what we do today is to embrace that as our community. I think being a three-axis beauty brand is partly what people expect, but it also caters to the beauty needs of our community.

The reality is that if you want to compete with the truly big groups or big brands, you need to play in all three of these axes. You can use them so that they benefit each other. Today we speak to a much younger clientele — primarily women — when it comes to makeup. A lot of these makeup customers have in the last year transitioned into becoming fragrance customers. In parts of Asia, skin care drives the beauty market. Skin care becomes the way to reach the larger group of people, so it can have different strategic purposes.

But for the sake of Byredo, it's just a natural evolution and something I kind of considered from day one that we would be more than one thing.

How do you maintain desirability, especially when you're a brand that's been around for a while and is competing with even bigger players and newer buzzy start-ups?

It's maybe the most important question, it's one that we discuss daily. I funnel it down into creating relevance in an authentic way. The evolution of a brand is its ability to stay alive and stay relevant.

Relevance is work. It's speaking to people in a way that they understand, with how they're living and where they're living and what is going on in the rest of the world. So even though we were timeless in our approach, and our products are borderline iconic at this point, the narrative has to evolve as the customer evolves. We have to continue to tell stories that are relevant to the way people live.

A few years ago, you started seeing the world come around to this idea of diversity and that was people trying to create relevance to something that was important to the world. We also saw that the people that were doing it in a less authentic way didn't succeed in creating relevance. So, it's an open-ended answer because it's going to be different for everybody, but I believe the combination of timelessness and current relevance, how you do that is how you stay alive.

This interview has been edited and condensed.

Scarcity is a very interesting tool. We're still living in an era of rapid growth and a lot of brands are still very interested in growing things very fast.

05.
M&A Recalibrated

In the short term, beauty merger and acquisition activity may not deliver as many megadeals as seen across the industry in the past, but the deal-making will continue to be buoyant. The potential benefits for buyers and sellers remain as strong as ever, playing a pivotal role in strategies focused on international growth, innovation and competitive product portfolios.

KEY INSIGHTS

- Beauty is expected to remain one of the most attractive consumer categories for M&A, given the sector's overall resiliency and strong margins.
- Amid a more challenging economic environment, competition for the most attractive targets will heat up and target assets will undergo greater scrutiny.
- Conglomerates will likely seek out smaller, but higher-quality assets to fill gaps in their portfolios or modernise product lines to stay competitive.

Drunk Elephant products. Drunk Elephant.

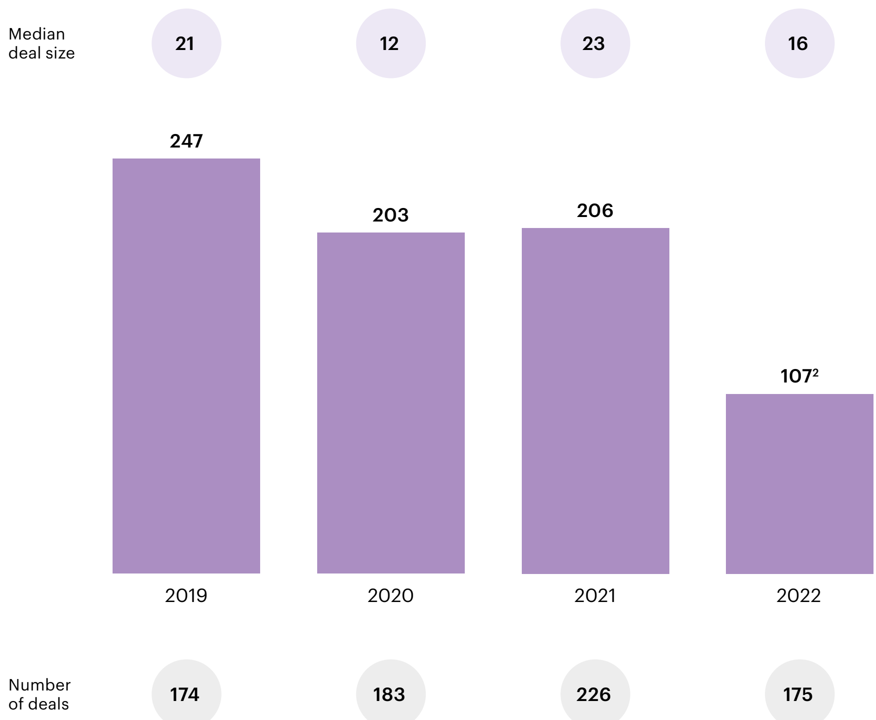
Barring a financial market meltdown, beauty M&A is unlikely to lose its sheen any time soon. Both corporate and financial investors have good reason to gravitate towards beauty, a consumer category that continues to prove its attractiveness thanks to hefty amounts of resiliency and strong gross margins, despite economic headwinds. But competition for the most attractive assets will likely be intense. Deal partners on both sides of the table will need to recalibrate their expectations for deal success.

In many respects, the recalibration began in 2022. The onset of economic volatility and uncertainty last year impacted M&A: the average beauty M&A deal value in 2022 was less than half that of 2019 despite a similar number of deals taking place. Industry observers expect deal volume and average value to tick downwards in the short term, from the post-pandemic high when competition for sought-after challenger brands drove up valuations to record multiples. For example, Shiseido bought skin care brand Drunk Elephant in 2019 for $845 million, at least eight times its annual revenue of just over $100

Exhibit 11

The number of beauty M&A deals in 2022 was the same as in 2019, but were worth half the average value

Average beauty M&A deal value[1],
USD (millions), 2019–2022



1 Based on acquisitions where information is publicly available and stake acquired is 30 percent or higher

2 Includes Tom Ford

Source: Capital IQ Corporate Actions and Transactions data, February 2023

million.[46] The same year, Coty paid $600 million for a 51 percent stake in Kylie Cosmetics, with estimated annual net revenue of $177 million, which implied a 6.8 times revenue multiple.[47]

Even as market uncertainties persisted in the early months of 2023, beauty's attractiveness to deal-makers remains steady. EBITDA margins are averaging around 15 percent to 25 percent and, globally, McKinsey estimates that skin care, hair care, cosmetics and fragrance will see a compound annual growth rate of 6 percent through 2027.

Private equity and other financial investors will likely fuel deal-making as they look to add beauty brands to their portfolio companies or offload previous beauty acquisitions. These range from private equity players Advent International[48] and TSG Consumer Partners to venture capital investors such as VMG Partners, Forerunner Ventures and Lerer Hippeau.

But it's among beauty conglomerates that M&A will continue playing a particularly prominent role. Acquisitions are a necessary part of their strategy

It's among beauty conglomerates that M&A will continue playing a particularly prominent role. Of the 139 beauty deals that closed in 2022 to acquire stakes of 30 percent or more, conglomerates accounted for about 90 percent.

to increase growth and maintain their competitive edge. Of the 139 beauty deals that closed in 2022 to acquire stakes of 30 percent or more, conglomerates accounted for about 90 percent. Several of these conglomerates have also established their own early-stage investment arms, which include The Estée Lauder Companies' New Incubation Ventures and L'Oréal's Circular Innovation Fund.

For instance, Puig, owner of Paco Rabanne and Jean Paul Gaultier, announced plans in May 2022 to buy a majority stake in Byredo — the luxury fragrance brand founded in Stockholm in 2006. Though Puig did not disclose the agreed price, press reports at the time said Byredo's valuation could be as high as $1 billion.[49] A few months later, The Estée Lauder Companies announced its $2.8 billion acquisition of Tom Ford.[50]

Discerning Deal-Makers

Recent earnings have provided evidence of how acquired brands can give their new owners a boost. In the second half of 2022, for example, The Estée Lauder Companies reported skin care sales declined 20 percent year on year, which was largely attributed to two of its oldest brands, Estée Lauder and Clinique. But The Ordinary, a brand The Estée Lauder Companies bought in 2021 which is known for its lower prices and ingredient-centric philosophy, offset category declines.[51]

Conglomerates are also leaning into M&A to stay relevant and nimble in today's market that requires innovation and novelty to capture consumers' share of wallet. "M&A fills and accelerates the development pipeline. It's critical to have what will appeal to the next generation," said Nini Zhang, managing director at Bank of America's consumer and retail investment banking group.

In return, corporates can facilitate global expansion by providing access to foreign distribution networks and leveraging relationships built over decades with partners. These investors also typically already have — or possess the expertise to build — infrastructure and systems that can reduce costs, streamline processes and provide economies of scale when, for instance, negotiating with suppliers or landlords.

According to Zhang, buyers and sellers need to ask themselves, "Where can corporates take the brand using their footprint, commercial structure, capabilities over the next five to 10 years?"

Sometimes, if the answer to that question doesn't come easily, it may be better to reconsider a deal, even if it has long closed. In 2021, Shiseido carved out and sold colour cosmetics brands Laura Mercier, BareMinerals and Buxom to Advent International as part of a global strategy rethink to realign its focus on skin care, despite having acquired the brands only in the 2010s. Similarly, The Estée Lauder Companies closed makeup brand Becca Cosmetics that same year, less than five years after acquiring it for a reported $200 million. While Becca was once a beauty favourite, post-acquisition it struggled to cultivate a loyal consumer base and suffered as colour cosmetics sales declined even further during the pandemic.[52]

And as proven all too often in the past, timing is critical — as in the case of L'Oréal's April 2023 announcement of its $2.5 billion acquisition of personal care and grooming brand Aesop. Following the announcement, industry watchers observed that

A L'Oréal flagship store in Shanghai, China. Getty Images.


L'ORÉAL
PARIS

the deal would give L'Oréal a brand that has both luxury and mass appeal. The deal took place at a critical moment in Aesop's journey to cult favourite, which *The Business of Beauty* likened to The Estée Lauder Companies' acquisition of Le Labo in 2014, just when the perfumer's Santal 33 was riding a wave of popularity.[53]

What's on the Horizon?

Where does this leave target brands? While a focus on revenue generation once sufficed to make a buzzy start-up attract suitors, evidence of sustainable profitability will be front of mind for investors. Meanwhile, the strength of intangible (and sometimes hard-to-value) assets such as strong brand identities, visionary leadership or loyal customer communities could make or break a deal. Targets will also need to indicate that they have the potential to scale in new markets or categories, using storytelling or product development strategies that can resonate across markets regionally or even globally. Due diligence will also need to sense check for any incompatibility between buyers and their targets.

Meanwhile, acquirers' post-merger plans must address and mitigate common risks in such deals — like the acquired brand losing longtime loyal customers. Whether they are long-term or short-term buyers, acquirers must also incentivise management teams to stay engaged and ensure the continuity of the brand DNA as it scales.

Deal-making is at an inflection point. Ongoing economic and geopolitical uncertainties underscore how buyers and sellers must anticipate different approaches to M&A as market conditions change. Industry observers expect fewer, higher quality deals in the near term. Increasing challenges in acquiring larger brands are expected to result in a greater focus on targets earlier in their lifecycles than their predecessors. Over the longer term, beauty deal activity is likely to continue at pace or increase due to the sector's attractiveness.

"I don't think we will go back to the high-volume environment of 2021, but it will continue to be reasonably robust with a steady flow of brands coming to the market," said Cosmo Roe, partner at Goldman Sachs. "I don't see a change in valuations in the near term. Even if cost of capital is up, the truth is these categories are super competitive and there are many well-capitalised buyers."

Skin care, niche fragrance and hair care will be closely watched by buyers, due to those categories' expected growth, increased premiumisation and potential for product innovation. Private equity investors will also look beyond brands for opportunities to participate in beauty's growth, considering contract manufacturers, turnkey solution providers or ingredient suppliers.

For their part, conglomerates will seek to bring more brands into their fold, much along the lines of what L'Oréal has already been doing: prior to its acquisition of Aesop, it purchased clean skin care brand Youth To The People in 2021, and Skin Better Science in 2022, to further fill out its Dermatological Beauty division.

"We see a relatively solid pipeline of assets and in terms of size," said Goldman Sachs managing director Jelena Djuric. "The majority of businesses that get sold in the category are within $75 million to $200 million in sales; we would expect that the majority of activity will be in this range."

Overall, M&A is expected to continue with fewer, higher-quality deals at high multiples in the near term. In this environment, acquirers will need to become more sophisticated, building on experience from previous deals and sharpening their ability to identify long-term winners through increasingly stringent due diligence processes. This will require zeroing in on the few differentiated and scalable businesses and having the conviction to back them.

An Aesop store in London, UK. Shutterstock.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REDUCES FRIZZ, NOURISHES & PROTECTS
100 ml/Net 3.3 fl oz
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ALL HAIR TYPES
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EXECUTIVE INTERVIEW

Advent International: Finding the Winning Ingredients for Beauty's Deal-Makers

By Janet Kersnar

Managing Partner, Advent International

Capital flows, deal structures and even the investors themselves may change, but **Tricia Glynn** of the global private equity firm unpacks the enduring factors effective beauty deals share.

Olaplex products. Olaplex.

It's not that a major M&A-fuelled shakeout is imminent in today's highly fragmented beauty industry — market conditions may make that a moot point. But given beauty's expected growth trajectory, plenty of deal-makers are eager to pile into the sector. That doesn't worry Tricia Glynn, a managing partner and member of the consumer retail leadership team at Advent International, which today holds more than $90 billion of assets under management. According to Glynn, who joined the firm in 2016, there are plenty of opportunities for private equity investors like Advent as entrepreneurs look for external partners to help grow their businesses.

In many respects, Glynn has had an exceptional seat at beauty's deal-making table, having seen over the finish line two industry deals for the global private equity giant — to buy a majority stake in hair care company Olaplex in 2020 before floating it on Nasdaq the following year and the carve-out of three makeup brands from Shiseido Americas to form Orveon in 2021. Advent continues to be involved in both companies — according to public documents, the firm holds combined voting power in Olaplex of approximately 80 percent, while Orveon remains one of its portfolio companies with Glynn holding a board position.

For Glynn, building such long-term investment relationships begins with two must-haves: a great product and a clear understanding of the business or consumer problem that an investor can help unlock.

How does the focus on beauty deals fit into Advent's overall investing philosophy?

From an Advent perspective, we love this market. We're looking for similar things in beauty that we look for in other sectors of consumers. In each sector, we're trying to find brands that can build and grow for decades. Then our job is to unlock those brands and opportunities with capital, with global insights, with supporting the executive team to build a phenomenal culture.

To invest in the consumer field at scale, we are big believers that you can't be a contrarian. You need to be investing where the consumer is going over the next 10 to 20 years.

We think beauty is a beautiful fit inside that strategy. It's not just colour cosmetics; it's not just colour cosmetics and skin care. Now you have colour and skin and hair and wellness — beauty inside and outside. It's all still valid.

There are so many different ways to grow. Also each of these markets I'm listing are very big, so you can have more than one brand [in a portfolio] and they don't necessarily directly compete.

There are different ways to come at the beauty sector. … Olaplex, Orveon are quite different, but they show a truism of the Advent strategy: understanding the business problem or the consumer problem that's being unlocked.

Beauty and wellness is an industry that allows the consumer to invest back into themselves. There's a lot of good tailwind in it. The definition of who is willing to invest back in themselves has evolved and broadened over time [and so have] the tools which we're giving people to invest back in themselves.

Other investors — financial alongside strategic — would agree with you about beauty's opportunities, and probably explains why beauty brands have been attracting so much interest from potential buyers and investors, especially after the pandemic when access to capital was cheap and easy. What's your take? What's different from an acquirer's perspective these days?

Yes, more capital, more business generation generally speaking — that's a great thing. That doesn't bother me at all.

For a long time, there was a view that it was very, very hard to compete with the likes of the Estée Lauder's and L'Oréal's of the world. … There was the general belief, and this exists in other sectors of the economy, that the big "strategics" had the right of way. Look, they're incredible companies. They do have really talented executives and professionals out building [companies], as does P&G, as does Unilever.

But what you've seen proof of in the last three years, five years is that you can have investment strategies that are not just tied to those big conglomerates that are effective. So more buyers are coming in.

What you haven't seen yet is a rash of exits for those buyers, and ultimately you'll need to see that. Nothing is holding back exits but time. More capital has chased into the sector and all that capital will and should see exits over time, both to private owners as well as to respected consolidators in the world of beauty.

Ultimately, this category is big enough that you can invest in innovation, you can invest in the sustainability of packaging, you can invest in clean product formulas that really work. You can be efficacy-based. You have got almost all the attributes that we'd see in any consumer market that you can put to work in beauty.

In such a big and crowded market, how do you identify targets?

If I distil everything I'm saying down it is this: I'm looking for businesses where they want to inflect the line of what they're doing over the next five years. For whatever reason, they need to get outside of their conglomerate, they need more capital, the founder doesn't want to take the next step.

I'm not particularly interested in a business that was started just to be sold. I want to buy businesses where [the founders] wanted to run it their whole lives but there's [now] some reason that this next phase [of the company's growth] is better done with a minority or majority partner.

When we go about putting investments behind [those companies], we're really flexible. It can be minority capital or majority, it can be a carve-out — as in the case of Orveon; or backing a business by buying from the founder — like in Olaplex.

Speaking of those two deals — Olaplex and Orveon — how do they reflect the role investors like Advent can play in helping brands scale?

If you look at Olaplex, the product is one of the most unique opportunities I've ever seen. The product actually fixes damaged hair, rebuilds the bonds in damaged hair. When we did the original diligence work, I was blown away by the efficacy and the strength of the community. [But] there was not a lot of infrastructure that had been built underneath the brand. Supply chain rigour, procurement, talent in HR, professionals inside the firm to help it grow, a finance organisation, a marketing organisation — a long list, right?

When we completed the carve-out of the Orveon brands from Shiseido, there were three brands with incredible products and customer loyalty, [again] without the infrastructure.

One thing neither Olaplex nor Orveon has is legacy systems, or legacy processes. The marketing was built for today. The supply chain was built for today. Both companies are highly focused on innovation around product, which I think has got to be the core of any consumer-orientated company and innovation on how to speak to the customer.

I don't want to conflate these two brands too much; we happen to be a common owner of both and we own other businesses. There are similarities, but also differences — the channel strategies are slightly different, the marketing strategies they need to employ are different.

With Orveon, you kept three brands under one umbrella. Why not simply keep them separate?

We thought about that a lot. The benefit — and you see this a lot in the start-up world actually — is that you can have incredible talent around a start-up, but at some point, the appeal and size of that business only allow you to bring in so much new talent to help you grow. The heft and size we have of Laura Mercier, BareMinerals and Buxom allow the company to afford a really talented executive team that can do more. They have run bigger businesses.

The reason people joined Orveon with us — besides following the leadership of Orveon CEO, Pascal Houdayer, or besides a love for these brands — is the ability to chart a new path in the industry. I'm not a car person, but you get a brand new chassis to go plug new brands into and that can be pretty compelling.

Was the idea to eventually be able to compete along the lines

More capital has chased into the sector and all that capital will and should see exits over time.

of Estée Lauder Companies or L'Oréal? Was there a discussion about that future M&A-driven growth when you were putting together that deal?

I do think that business will continue to do M&A and bring in new brands. If we were to get all the way to the size of an Estée Lauder or L'Oréal, that would be great; that's not bad for anybody. They're incredible companies — [but] with 100-year track records behind them. I think the goal can be much more modest than that, and still be a beautiful opportunity for this business.

As you said, Olaplex has taken a different route. Its IPO makes it a bit of an outlier since there have been so few beauty IPOs. What are the pros and cons for companies like them to go public these days, or are there more realistic options for brands?

There are a lot of options for brands, but I don't shy away from the public markets. I'm still a believer in beauty IPOs despite 2022 and what we're all living through right now. Public markets have flaws, but they're good for a lot of things. ... One of the benefits of being public is that all the shareholders can benefit from the business for the very long term. You get a fairly liquid way to compensate employees with equity over the long term.

Ultimately, we felt that Olaplex could own its own destiny for longer as a public company.

Looking at the deal landscape, what are you seeing?

Debt markets are volatile, public market valuations are still down dramatically; inflation is still persistent and there are concerns about liquidity now in a way that wasn't the case [earlier in the year].

You end up with two outcomes: one, less deal flow than you had before because people don't want to sell at low prices, and two: in these times of volatility, trust really matters.

For our business, we don't need to invest every minute of every day; we are with this for the long term. I think spending real time with executives and owners and building that trust is really critical. You absolutely can still invest in these moments of time, but perhaps you do structure it differently. Perhaps there's no debt and just a liquidity facility.

We're spending time thinking about what the business really needs to be investing in right now, without worrying about 10 years from now. In other situations with plenty of liquidity, you might be able to still invest for the 10-year-away big opportunity that changes the market.

As you look across all of that, ultimately great businesses should gain share in tough times and will persist to get to the other side of all this.

This interview has been edited and condensed.

A Laura Mercier store. Getty Images.

Editor's note: This report was revised on May 31, 2023, to correct an attribution in the image caption on page 32 to Clive Christian.

GLOSSARY

Ayurveda
An ancient Indian medical system that aims to preserve health and wellbeing through a holistic approach to healing.

Clean beauty
Beauty products created without synthetic chemicals and ingredients perceived as harmful or irritating to the skin (e.g., parabens, phthalates, oxybenzone, synthetic fragrances).

Conscious consumer
A consumer who is focused on sustainability, cruelty-free production and ethical and ESG claims.

Multi-step care
A beauty routine consisting of multiple steps, including for instance: cleanser, toner, serum, moisturiser, eye and day or night cream.

Premiumisation
The trend towards more expensive, premium products for a perceived increased benefit.

Skinification
Elevation of a routine (such as hair care) to the elaborateness of skin care, e.g., nourishment and treatment of hair with specific ingredients and a range of products made for them.

Textured hair care
Products and services with special formulations designed to cater to customers with wavy, curly, coiled or kinky hair textures.

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