



PRACTITIONER PAPER

A proposed strategy for introducing moderately priced American brand merchandise in China

Brand
merchandise in
China

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Abstract

Purpose – The purpose of this paper is to provide a path forward, for the marketing mix elements, to be adopted by a US retailer entering the moderate brand market in China.

Design/methodology/approach – A number of recent studies focusing on the Chinese retail market, especially the apparel market, are examined. In light of these, the best method of progress for US retailers operating and/or intending to operate in China is formulated.

Findings – The emergence of the Chinese market is coupled with demographic, economic, cultural and technological factors as well as consumers' highly positive perceptions of Western brands seen as status symbols that have attracted foreign investors. However, when entering the market consideration should be also given to structure of retail environment, brand image, distribution formats and positioning efforts recalling that the Chinese market is relatively brand-uneducated and diverse. Based on the information obtained emphasizes that diversity is the key in defining the market and limited localization should be the main concern of product mix.

Originality/value – This paper serves as a comprehensive guideline as it provides an overview of the Chinese market in addition to detailed strategies for US investors entering into China. It combines carefully studied opinions and viewpoints of experienced observers of the marketplace. The author contributes over 30 years of experience in the textile, apparel and retail sectors. Recommendations are provided for US retailers aspiring to serve this market by differentiating their marketing mix.

Keywords China, Retailing, Product mix

Paper type Research paper

Introduction

China's economic size is comparable to western European countries with a GDP growth rate predicted for about 8 percent for the coming five years. This fact coupled with a population base of 1.3 billion people makes China the most desirable of emerging economies world over to have a market in China. Though the buying power of the Chinese middle class is still a fraction of their western counterparts', Chinese society is creating the right atmosphere for launching a moderate US brand in China today.

The purpose of this paper is to provide a path forward, for the marketing mix elements, to be adopted by an US retailer entering the moderate brand market in China. The approach used to write this paper is based on a review of the current literature as analyzed by the writer's over 30 years of industry experience and observations. Most academic papers study events from scientific method, but observation and intuition are important factors in the apparel industry. Therefore the studied literature is of a



secondary nature and the analysis is of first hand knowledge. The conclusions drawn therefore are based on anecdotal experience. This paper provides a method to be followed for those engaged in practical business relations with the Chinese consumer. The paper does provide literature, of a secondary research perspective, that shows that the environment for the introduction of a moderate brand does exist. The paper's intent is not to prove that Chinese consumers are prepared to purchase a moderate brand, as this is already in the literature:

China's \$1.4 trillion economy is the sixth largest in the world and the GDP is forecasted to grow 7.9 percent over the next five years twice that of the US Prospects for overall retail sales are for strong growth. Between 2001 and 2005 the retail market is expected to increase by 28 percent, reaching RMB 4,600 billion (\$555.98 billion) (Sharett, 2004).

In particular, retail-clothing market is very promising. In 2001, clothing urban retail sales reached to RMB 557.48 billion whereas the corresponding figure in 1995 was lower by 73 percent (Tredre, 2003).

As far as the spending patterns are concerned, the future trend is also similar. "According to Euromonitor International, Chinese consumers' total disposable income is expected by 2009 to grow by one third, while monthly earnings will increase to 921 renminbi from only 660 last year."

Goldman Sachs also notes that 4.5 million Chinese already enjoy annual purchasing power in excess of \$30,000 (Niemi and Weilheimer, 2005).

China current scenario for setting up market place

Not until 1992, foreign retailers were able to enter the Chinese market (Shen, 2002). The liberalization of retail industry paved the way for investors to establish their enterprises to cater to the most populous customer market of the world. "As at the end of 1997, only 18 joint venture retail enterprises have been approved by China's central government but more than 200 have been established with the approval of the local authorities. The 18 joint venture retail enterprises are located within the first tier cities and the special economic zones, and they enjoy certain privileges not accorded to those approved by the local authorities" (Wong and Yu, 2002).

There are various factors that have influenced the Chinese market in terms of having a foreign brand entry of which some of them are:

- *Demographic factors.* The urban population increased from 19.4 per cent to 36.2 percent while the rural population fell from 80.6 percent to 63.8 percent during the period 1980-2000. It is expected that the urban population ratio will rise further dramatically in the near future due to the migration driven by increasing job opportunities generated by foreign investment and opening of the market (Kwan *et al.*, 2003). So the US products, which are slightly on the higher side, will have a good market for their products in the years to come.
- *Economic factor.* There is a significant income disparity between regions. The highest household income is found in the south and coastal regions while it is close to national average for the southwest, northeast and middle south regions and below the national average for the north and northwest regions. (Kwan *et al.*, 2003). This helps to decide as to where the target market for the US brands will likely bloom in a few years. Another fact is that the wealthy class in China – the vital few – residing mostly in Shanghai, Beijing and

Guangdong was comprised of 2.8 million households in 2000. However, 24.1 million households were classified as middle income segment as their annual income ranged between RMB 10,000 to 30,000 (Tredre, 2003).

- *Cultural factors.* Chinese consumers are not fashion innovators (Kwan *et al.*, 2003). So the main fashion hubs like US and European countries can export fashion to China, as the present scenario demands that.
- *Technological factors.* Many retailers are still in the process of incorporating information technology in their operations (Kwan *et al.*, 2003). Therefore companies from other countries with good financial backup can venture into the market as brings out a revolution of technology.
- *Natural factors.* The Chinese consumer is also known to prefer clothing of high natural fiber content rather than synthetic fibers. This makes makers of natural fiber fabrics from other countries to export to China (Kwan *et al.*, 2003).
- *Consumers.* As the Chinese consumer is becoming more sophisticated and demanding, different trends are emerging in different markets. For example, though consumers in Beijing, Shanghai and Guangzhou all prefer imported foreign apparel brands in comparison to local ones Guangzhou customers are more selective and open to new products; Shanghai consumers are more cautious and price is an important consideration in their purchases; whereas Beijing consumers are more emotional and receptive to advertising messages (Kwan *et al.*, 2003). In fact, a number of studies conducted on apparel consumer behavior and consumer market segments in China have indicated that target customer profile of foreign made/branded apparel goods would be “younger aged, female, residents of Shanghai or Guangzhou, higher levels of education, and higher incomes” (Dickson *et al.*, 2004).
- *Political networks.* According to Kwan *et al.* (2003) having good relations and connections with influential people in the government bureaucracies is advantageous to foreign apparel retailers trying to gain approvals for establishing and running their retailing networks in China. This becomes more important considering the diverse regulations within the country. It only allows retailers with an annual sale upwards of \$2 billion and \$200 million in assets, to enter the market with a Chinese partner as a joint venture retailing company. However, with its accession into the WTO, China is expected to be relaxing some key restrictions applicable from January 2005 onwards. First, restriction on full-ownership and geography will be eliminated. i.e. a foreign company can establish a 100 percent foreign owned company anywhere in China, subject to central government’s approval (Ni, 2004).

Table I shows the US current exports and imports to China for an understanding about the business possibilities in various fields.

Factors influencing consumers on foreign brands in China

- (1) *Market structure.* China’s nascent retail market is highly fragmented, the leading retailers, particularly department store retailers, have a very small share of the overall market. The trend is to develop chain stores and form bigger

Table I.
US trade with China, top
10 exports and imports
2003 (\$ million)

Item	US exports to China		US imports from China	
	2003	Percent change	2003	Percent change
Electrical machinery and equipment	4,782.6	21.1	31,039.8	47.3
Power generation equipment	4,639.6	12.9	30,043.1	18.2
Oil seeds and oleaginous fruits	2,877.4	213.5	17,399.9	12.3
Air and spacecraft	2,451.2	-28.5	13,670.4	21.8
Medical equipment	1,594.0	26.6	11,144.8	3.5
Plastics and articles thereof	1,247.5	25.4	9,156.8	22.5
Iron and steel	1,213.9	105.4	5,440.6	13.8
Organic chemicals	1,105.3	78.3	4,779.9	15.3
Cotton	769.3	401.6	3,855.5	24.6
Copper	652.3	104.1	3,386.9	17.8
Total all exports to China	28,400.0	28.5	163,300.0	22.3

Source: China economic statistics

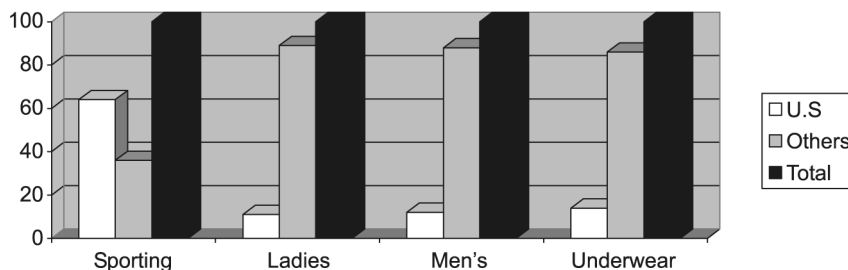
retail groups. Retailers are achieving this through a process of consolidation via mergers and acquisitions (Sharett, 2004). According to Wong (2004), one of the big international players present in China's retail environment is: Wal-Mart which already has 31 stores in 15 Chinese cities, and is planning to expand it by 50 more stores within five years. This will bring it approximately to the same number of stores as Carrefour.

China already has been identified as having a small group of very rich people, who can afford luxury brands. Ralph Lauren, Calvin Klein, Dior, Escada, Louis Vuitton etc. are only some of the luxury players with a successful presence (Li *et al.*, 2004). Currently, the share of US brands in the retail market by category is: sporting goods 64 percent, ladies wear 11 percent, men's wear 12 percent and underwear 14 percent (Delong *et al.*, 2004) (see Figure 1).

(2) *Brand image.* A survey conducted as a part of a study on "Perception of US Branded Apparel in Shanghai" by Delong *et al.*(2004) revealed that brand image gained the highest ranking for US brands. Even the lack of actual knowledge of US brands did not stop the respondents from rating American brands as high. Brand image is also closely tied to superior quality. The Chinese believe new foreign products to be superior in quality to Chinese products. Three tasks must be approached differently in Asia-Pacific markets:

- The brand name is very important. Selecting a positive or lucky sounding name in the native language is important for the brand image.
- Establishing the right image, as Asians are image conscious consumers the brand should be aspiration and associated with prestige.
- Quality perception too should be enhanced. Unless the Chinese customer is convinced that the quality being provided is at a good price they may not make repeat purchases.

It is also important to understand that in localizing the brand it is not perceived as a plus to hire Chinese designers and to manufacture the goods in the same towns they are sold. In fact when a Chinese customer buys an US brand they expect it to be representative of the US cultural experience, which is what a brand exemplifies. However, certain sensitivity to their culture and local consumer preferences should be an important part of localizing the brand for it to do well in China. US brands were rated higher than local brands for product design, exciting innovations, workmanship,



Source: Delong *et al.* (2004)

Figure 1.
US share of Chinese
apparel market

service and display of product. Especially, exciting innovations had the largest gap in perception between the Chinese and US brands (DeLong *et al.*, 2004).

- (1) *Store formats.* As Kwan *et al.* (2003), put it; most foreign branded apparel in China is generally sold through the following three intermediaries:
 - Franchised outlets.
 - Wholly owned outlets.
 - Department store concessions.
- (2) *Location.* This is another very key decision for apparel retailers in particular. Some of the areas with best potential for retail are based in Shanghai, Beijing, Tibet, Guandong, Zhejiang, Tianjin, Fujian, Jiangsu, Qinghai and Yunan. Based on 2001 data, those regions comprise the top ten locations in descending order in terms of average income levels with Shanghai reaching RMB 17,213 and Beijing RMB 15,661 compared to national average of RMB 9,465 (Tredre, 2003).

Not only a decision on what markets or regions has to be made but also where they will be located in those markets. Some of the options are as follows:

- (1) *Street front store or upscale shopping centers in downtown areas.* These stores enjoy a very high traffic volume due to their easily accessible locations. A good example of an upscale shopping center is Plaza 66 in Shanghai. Some of the notable brands sold there are Escada, Loewe, Chanel, Laurel, Trussardi, Lagerfeld, Hugo Boss, Dior, Dunhill, Agnona, Fendi, Nautica, and Mac& Jac. These are mostly located in high-level business districts in the largest cities. They target fashion conscious customers who have high incomes and high levels of taste.
- (2) *Multi-level malls located close to the city.* A good example is the Grand Gateway Mall in Xujiahui district-Shanghai. Some of the brands sold there are Braxton, Jockey, V-one, Giordano, Chic a porter, Kuhle, and Harmony. These malls are located in major cities and market most types of apparel goods in multiple price ranges to satisfy the needs of a broad range of customers.
- (3) *Joint discount superstore.* This format caters to budget level price levels and offers a variety of merchandise. They offer consistent low selling prices, one-stop shopping with low operating costs, customer service, and low profit margins with high sales volume. These are a good choice to sell commodity or seasonal goods in an intensive market coverage strategy. Wal-Mart and the very popular Carrefour are prime examples of this format. Some typical brands sold through this channel are: Gold tree, Polo Club, OK Man, Orado, Conch, and Kaka.
- (4) *Manufacturer wholly owned flagship stores.* Manufacturer owned stores provide the Chinese manufacturer with a way to vertically integrate forward with retail stores. These could be either specialty stores or chain stores acting as their own factory outlets. Opening a flagship store has become an effective means to promote the owner's brands. It is seen as an effective way of attracting the customer's attention in China. The Youngour Flagship store in Nanjing Road-Shanghai, owned by one of the two biggest Chinese menswear companies

exemplifies an example for this type of store format (Li *et al.*, 2004) (China: Garment Industry and Consumer Market, 2002).

The following figure combines fashion forwardness and price aspects of different retail formats in China (see Figure 2).

Strategy for US brand to market in China

Based on the study conducted by DeLong *et al.* (2004), and the other research studied on the Chinese consumer market and the US brands, the following marketing mix can be drawn to be adopted by the US retailers in China.

Product mix

Currently there is no serious presence established by a moderate American brand in the Chinese market. However, as was found by DeLong *et al.* (2004), most of the middle class Chinese consumer is very enamored and eager to emulate the western lifestyle. The moderate brands can emphasis the “Americana” origin behind their brands and position it to cater to the desire for genuine western lifestyle/brands at much more affordable price points in comparison to designer brands. The design process should not be localized; however, merchandising should take into account the local preferences in terms of colors and sizing. Continual innovation and newness should be maintained in the store along with good service. It should be noted that the moderate price points though much lower in comparison to the designer goods price points will still be an expensive buy for the Chinese customer. Hence to begin with the brand should enter with an exclusive distribution catering only to the rich, little rich segment in the big cities. As brand awareness is developed amongst the Chinese consumer base and the

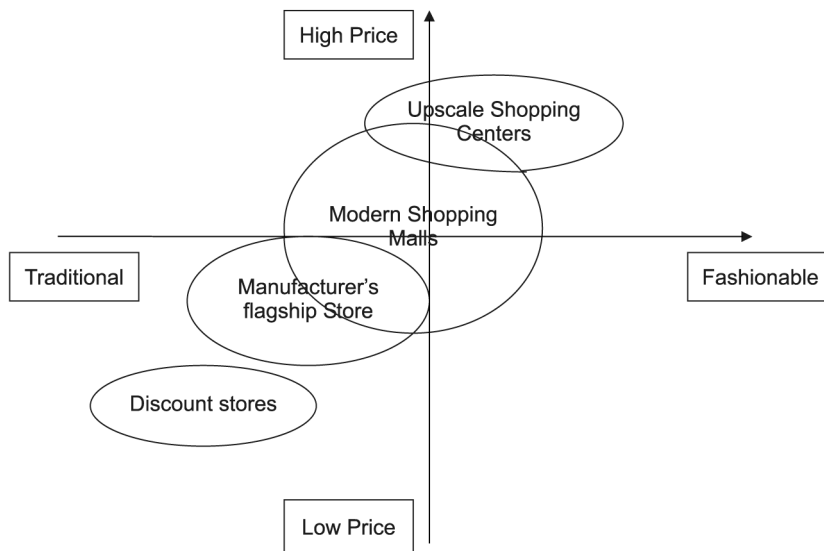


Figure 2. Schematic mapping of retail formats on price and fashion sensitivity index

Source: Li *et al.* (2004)

median income increases over time, the brands can penetrate the market more intensely and follow the same model as in the US. Establishing an upscale image will prove to be advantageous for a brand once the market reaches maturity and has penetrated fully (Thapa, 2004).

Communication strategy

Western brands are perceived to be superior (DeLong *et al.*, 2004) but not much brand awareness is there- they need to market the brand with a clear US image to it – it needs to be built and tied with the product to get the actual sales and differentiation from other western brands. However the brand will need to adapt subtly to local taste and cultural preferences.

In the initial stage, the US brand should be positioned as a premium brand in China (differing from its positioning in the US). A good example of this is the upscale image of Wal-mart in China versus the discounter positioning in the USA. In Shanghai shoppers see it as an exclusive outlet where they can buy things they did not have access to previously via other existing stores (Wong, 2004; Ayala *et al.*, 1996).

Once a critical mass point is reached in brand awareness and buying power of the consuming segment – the brand can be launched on a wider scale catering to a bigger cross section (as in the US) (Thapa, 2004).

The marketers of the moderate US brand in China should understand that the Chinese consumer prefers foreign brands believing they are of superior quality than the Chinese products (DeLong *et al.*, 2004). Hence, the moderate American brand must communicate the good/superior quality of their product repeatedly to maintain the perception gap. They should highlight the great quality, and superior product innovation and their “American origins” being offered at better pricing (than designer brands). Understanding this, the Chinese consumer is more likely to buy such a brand at a premium (in comparison to local brands) for the superior quality and design without having to buy designer brands (Thapa, 2004).

Price positioning

The Chinese consumer though eager to acquire all the new fashions is however constrained by the prices. As quoted before the urban middle class income is around \$3,500 per annum. In a survey carried out in the five big cities in China it was found that an average of 7.3 percent was spent on clothes by the shoppers there (approx \$251) (DeLong *et al.*, 2004). Clearly, affording designer brands will be very difficult for this class. However they can definitely afford multiple pieces of moderate true-blue US brands. It is to be noted, that this class is growing today and will in the next ten to fifteen years be a major consumer force. The consumer will be more likely to buy into the brand if it is projected as aspiration in addition to being a good quality US product (Thapa, 2004).

Distribution channels

Current real estate presence/format/model: as proposed in the promotion section, the brand should have an exclusive strategy in the introductory phase. Retail presence in upscale shopping centers like Plaza 66 should be established via leasing space in high profile and prestigious department stores or opening a company owned flagship store depending on the financial commitment and control on channel desired by the brand.

This will help attract attention to the brand as has been found effective with the Chinese consumer (Cui, 1998).

Once awareness has been established and the brand begins to enter its maturity stage and the consumer buying power has increased, stores in Malls (catering to better and moderate price points) can be initiated. This may be done either through franchisee stores or through company owned stores. Once the market has matured for the brand to penetrate intensively they may look to either selling through department stores or specialties stores and maintain chain of fully owned flagship stores in high profile markets to act as a model for other stores and deliver the advertising message in the key markets.

Hypermarkets have proved to be a huge success in China and were reporting a 50 percent return in the late 1990s (Chan *et al.*, 1997). Hence a presence in these hypermarkets could be also looked into in case of secondary cities, which do not have a major upscale strip mall or mall outlet. This will also improve the brands penetration into the central regions and give them access to mass market as the middle class comes of age in China in the next five to ten years.

In the early stages of brand entry, mail order business should not be given emphasis due to two main reasons. As first of these was noted by (Sharett, 2004), the progress of mail order business in China was hindered by a government ban on direct selling, which was in effect during 1995 and 1998. Second, purchases mainly depend on cash economy, as “credit cards are still under-developed many cards are actually delayed debit cards. Only 100,000 pure credit cards had been issued by the end of 2000. Even though the country has a reasonably efficient postal system, lack of credit card ownership and previous restrictions make it difficult for brand growth through mail order business (Tredre, 2003) as well as e-tailing.

As discussed earlier coastal cities are the most prosperous cities in China, though transportation infrastructure is a problem in China as a whole, again the coastal regions are much better off than other regions. The second tier cities have prospered due to their proximity to the first tier cities and are well linked to them.

Due to this a US brand may want to concentrate on distributing their products on the coastal cities. It will not only allow them access to the most affluent customer with similar preferences, but also the most densely populated regions and hence a disproportionate market share. Human and financial resources can also be employed most judiciously and higher return on investment can be achieved via concentration on a more focused market and the economies of scale.

This strategy could be employed as market penetration is spread via proximity to coastal cities including all regions eventually as improved infrastructure and consumer-buying power spreads to other regions as well (Thapa, 2004).

Wong (2004) made a similar claim that “western retailers want to concentrate their distribution activities in the densely populated urban coastal areas, where the roads and other physical infrastructure are good, and disposable incomes are higher.”

Recommendations

Due to the sheer size of manufacturing and foreign trade in China, it holds obvious lure to many logistics providers. This may lead to an even more rapid development of transportation and other logistic support functions leading to a more rapid spread of business in China. More than any other developing country, China is also making huge

rapid economic strides. Even if it takes more than a couple of decades for the country to come at par with the western economies, many parts of the Chinese economy (the coastal regions most noticeably) will catch up with the west far before then. Due to its size, even a fraction of the Chinese economy will provide for very serious business for the leading goods and service providers around the world. The Chinese are willing to pay for western branded products, as they believe them to be of superior quality. Hence quality is a key factor, which must be emphasized along with innovation and better customer service. The most successful brands will be those that will project themselves as aspiration and of superior quality to other brands in the market. Accordingly, retail real estate will also play a big part in communicating the positioning of the brand to the consumer.

As noted by Wong (2004), western retailers with their superior merchandising expertise and management know-how, their ability to stock stores with compelling merchandise present it in a clean wide-aisled stores and provide service with a smile will help them with building a customer base and loyalty. A good case in example is Wal-mart. "Their stores are so good-looking to Chinese consumers that it took some time for them to be convinced that Wal-mart wasn't too expensive for them". This merchandising expertise is backed with superior technology and inventory management expertise.

Conclusions

Based on the findings of the practical industry research analysis, we recommend the following for US retailers:

- Income disparity should not be the only criteria with regards to point of market entry. Infrastructure and delivery mechanisms should also be considered.
- Noting the purchasing power factor, to begin with the brand should aim the vital few section of the population through an exclusive distribution in the big cities. Over time, customer database should be expanded to also cover the middle-income segments.
- Limited localization should be utilized meaning that as western-US-brands are favored over Chinese ones, products' "American Origins" should be highlighted coupled with special importance on color and sizing.
- Even it holds lure to cater to elderly and time conscious consumers, mail order business or internet sales should not be one of the primary distribution channels utilized by companies as they might not be profitable due to the underdeveloped credit card business and former regulations.
- As market conditions improve distribution channels should be modified to ensure that the target customer base is within reach.

Today is the right time to invest in building awareness for a brand in China. In the relatively brand uneducated market, a brand that launches itself right now, stands to gain the first movers advantage and will enjoy a stronger brand recall than other brands launched later when the Chinese retail sector is nearing saturation. This advantage will prove to be an important differentiation tool to the brands advantage when the market will have reached its full potential.

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