The Anchoring Effect on Luxury Goods Consumption among the Chinese Middle-Class

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Abstract. The Chinese Middle-Class, defined as households with annual incomes ranging from ¥300,000 and ¥1.5 million in first-tier cities, has become a significant consumer demographic for luxury goods. An uncommon phenomenon is that rising prices fuel consumer demand in the luxury goods market in China's burgeoning middle class. This research attempts to investigate the anchoring effect in this phenomenon by combining the perspective of psychological and behavioral. By recruiting 200 participants from China's first-tier cities, the treatment group and control group with the variation of price increase and public and private settings are designed to explore its influences on decisions about luxury purchases. The expected finding can provide valuable insights for both consumers and luxury brands by conveying the complex interplay between economic behavior and social influence in Chinese luxury market.

Keywords: Chinese Middle-Class, Luxury goods, Anchoring effect, Consumer behavior

1. Introduction

1.1. Overview

The middle class has long been recognized as a pivotal segment of society due to its significant population size. There are over 33.2 million Middle-Class households in China, accounting for 11% of the total population. The Chinese Middle-Class are defined as the urban residents with an annual household income ranging from ¥300,000 and ¥1.5 million in first-tier cities, and exceeding ¥200,000 in other Chinese cities" [1]. These households are primarily concentrated in first-tier cities such as Beijing, Shanghai, Guangdong, and Shenzhen. Therefore, the Middle-Class can be seen as the backbone of Chinese society and they demonstrate considerable purchasing power, particularly for luxury goods. Recent reports from leading luxury brands also indicate that one of the main consumer demographics for luxury goods is the middle class [2].

Luxury markets in China have shown promising growth in recent years. According to Bain & Company, the size of China's luxury market tripled from 2017 to 2021. Although the growth rate experienced a decline in 2022 due to COVID-19, it quickly rebounded in 2023 with a yearly growth rate of 12% [3]. PwC predicts that by 2030, China will become the largest luxury market in the world, with a projected market size of $148 billion [4]. Furthermore, the Middle-Class in China demonstrates significant purchasing power for luxury products despite their high and increasing prices. This phenomenon is noteworthy as it contradicts the standard economic law of demand, which states that an increase in price leads to a decrease in the quantity demanded.

However, the law of demand does not seem to apply in the luxury consumption market in China. Despite annual increases in the price of luxury products, there continues to be a high demand from consumers who eagerly wait in line at luxury stores to purchase these already expensive items. When traditional economic principles fail to explain this phenomenon, it is likely that psychological factors are at play. For example, similar to the development of the middle class in Western countries, the rising Middle-Class in China also exhibits a strong desire for improved quality of life and social status, which may contribute to their obsession with purchasing luxury goods regardless of escalating prices. Therefore, we aim to utilize Behavioral Economics' anchoring effect as a framework for exploring the underlying psychological motivations driving this behavior among Middle-Class consumers in China.

1.2. Research contribution

The research aims to contribute to the existing literature in the following ways. Firstly, we will combine psychological and behavioral perspectives to analyze potential results and provide suggestions for both consumers and luxury producers. Secondly, we will fill in the research gap by connecting the Chinese Middle-Class with luxury goods consumption, which has not been addressed in current research. Finally, we will design a scenario experiment with questionnaire for pre-test to exam whether anchoring influences the decision-making of the Chinese Middle-Class when it comes to consumer decisions.

1.3. Paper structure

The remainder of this manuscript is organized as follows: Section 2 comprises the literature review, encompassing an analysis of existing literature pertaining to the Chinese Middle-Class and luxury goods, as well as the identification of research gaps. Section 3 details the methodology, outlining our experimental design in-depth. Lastly, Sections 4 and 5 present the conclusion, incorporating potential findings, results analysis, and recommendations.

2. Literature review

2.1. Factors influencing Chinese Middle-Class consumption

Early researchers have conducted studies to explore self-brand connections, representing the degree to which people have integrated a brand into their identity. Escalas and Bettman find that how much member group and aspiration group use affects a person's self-brand links depends on how much that person is part of a member group or wants to be a part of an aspiration group [5]. Besides, aspiration group brand use has a higher effect on self-brand connections for people with self-enhancement goals, and member group use has a higher influence on self-verification objectives for those with self-brand connections. Such findings demonstrate that consumption can be motivated by

self-needs and self-identities, while branded goods symbolize group membership and social status. However, as only undergraduate students were recruited, it remains puzzling to generalize the results to additional age groups and the Chinese Middle-class.

In another study, Zhan and He further explore psychological factors influencing the Chinese Middle-Class consumers' consumption of luxury goods [6]. The research analyzes scales collected from 359 participants in Shanghai and focuses on three main luxury products (handbags/suitcases, designer clothing, and watches) towards best-known luxury brands. It concludes that Chinese Middle-Class luxury consumption is associated with value consciousness, susceptibility to normative influence (SNI), and the need for uniqueness. To be more specific, the researchers suggest that, for Chinese Middle-Class consumers. However, luxury goods don't always have to be costly investments; buying the best-known brands offers a higher benefit/cost ratio and compliance with social influence [6]. Seeking for uniqueness is also a driver of luxury consumption, with consumer knowledge about brands as a moderator. This study identifies new psychological characteristics to analyze the Chinese Middle-Class consumption. It details the findings of Batra et al. which explored the relationship between SNI and social values and expands its effect on consumption [7].

However, minor research further explored the influencing factors of Chinese Middle-Class consumption from the behavioral perspective or a combined economic and psychological aspect as this research aims to do. Also, the value perception of luxury and identity expansion are the core topics of most psychological factor analyses; nevertheless, not enough research examines psychological factors from the standpoint of decision-making, as we want to demonstrate.

2.2. The effect of anchoring on consumption

The anchoring effect in promotional scenarios has been discussed by Chen [8]. Using questionnaires, this research recruits 209 respondents and concludes that the majority of people who shop regularly and are interested in promotion are those whose preference for promotion changes with an increase in the degree of promotion in a linear manner. The research elaborates that the anchoring effect exists in people who focus on promotion only when the degree of promotion is high enough on account of knowledge accessibility. Consumers who prioritize promotions are less likely to be affected by an increase in the intensity of the promotions in terms of their preference for the promotion form. Also, compared to discount promotions, gift promotions make the customers exaggerate the original price of the products due to the numerical effect. However, another research that explores the reference price effect suggests that the customer would doubt the quality [9]. Therefore, they would give up purchasing low-priced products which is opposite to the traditional demand theory. Due to the inconsistent results, it is still unclear about the anchoring effect in luxury consumption.

Another research explores the anchoring effect on online product pricing [10]. Proposing a pricing model based on the MNL model, the researchers find that when consumers are anchored only by sales of goods, the ideal solution is monotone in terms of the anchoring degree. When consumers are anchored by both price and sales, both factors impact their behaviors. This research emphasizes that the anchoring point and degree are important in influencing the product pricing strategy of platform enterprises, as well as consumer behaviors. This gives empirical experience to platform enterprises by price anchoring in shaping consumer cognition and behavior. However, research gaps exist in exploring the anchoring effect on luxury goods consumption. Based on previous findings, we propose the following hypothesizes:

H1: The anchoring effect will increase the purchase of luxury goods in the Chinese Middle-Class when its price increases.

H2: Anchoring effects differ in purchasing luxury goods in the context of public and private.

H3: Anchoring effects differ in luxury goods consumption in different ranges of increasing prices.

3. Methodology

3.1. Sample

The convenience sampling method will be adopted for its convenience to find related samples. The research will recruit 200 samples via an online platform, and participants will be only recruited from Beijing, Shenzhen, Shanghai, and Guangzhou to exclude the influence of the various development levels of cities on the income definition of the Chinese Middle-Class as these four cities are the representatives of first-tier cities. Participants' annual income ranges between ¥300,000 and ¥1.5 million, ranging from 20 to 60 years old. As the previous literature conducted around 200 samples to explore the anchoring effect, 200 samples are also settled to explore the anchoring effect of luxury consumption in the Chinese Middle-Class [8].

3.2. Experimental design

A questionnaire will be distributed via the online platform to pre-test the basic information such as gender, age, and income to screen the participants that meet our demand of the Middle-Class. Later, a lab experiment will explore the anchoring effect on luxury consumption in the Chinese Middle-Class. The experiment totally has eight groups, including four treatment groups and four control groups. The four treatment groups will be as follows: Group 1.1 small price increase with public context, Group 1.2 small price increase with private context, Group 2.1 high price increase with public context, and Group 2.2 high price increase with private context. For the control group, each condition will correspond to the treatment group without anchoring information on price increases. Participants will decide on purchasing a popular luxury bag under different settled purchasing conditions.

Each subject will participate in the experiment once. Each participant will only see one scenario randomly distributed in the treatment and control groups. Participants have the right to withdraw from the survey at any time, and all the information about participants remains confidential. The result of the experiment will be kept secret and private. Each participant who completes the experiment will get ¥10 reward. The whole process will continue for 2 to 3 months and the participants' emails will be recorded for debriefing the results and counseling details about the research.

3.3. Treatment and control group scenario

3.3.1. Clarification

As the scenario is settled, a certain budget, the original price, the high final price and a small final price are settled. Luxury bags are chosen as the representative of whole luxury goods in the Chinese market. The clarification about reasons for such settlement and choice is as follows.

A budget of ¥30,000 is set based on statistics showing the annual income of the Chinese Middle-Class range from ¥300,000 to ¥1.5 million [1]. According to the McKinsey and Company report, middle-class households typically spend 50% of their income on daily necessary expenses [11]. We propose the budget of ¥30,000 representing a realistic discretionary spending amount of the Chinese Middle-Class.

The original price of the luxury bags is set at ¥20,000. The price for the small increase group is set at ¥21,000 based on market pricing of popular luxury bags in China ranging from ¥19,800 to ¥26,700 [1]. For the high-increase group, the price is set at ¥28,000, which is a 40% price increase. This price aligns with Deloitte's report, which highlights that luxury goods have seen significant price increases due to high demand and brand value [12]. The report suggests that luxury brands often implement price hikes between 20-40% to maintain exclusivity and meet market demand [12].

Luxury bags are a significant segment of the luxury goods market in China, expected to reach 9 billion USD in 2023. Also, around 68% of Chinese shoppers purchase at least one handbag per season [13]. This strong demand makes luxury bags an appropriate representation for studying consumer behavior in this research.

3.3.2. Scenario description

Treatment Group 1 is the "Small price increase with public context" group. The scenario will be described as, "Imagine you have a budget of 30,000 RMB, and you are in a luxurious, well-lit boutique with soft music playing. The store is immersed with elegance, with glass cases displaying an array of top-end luxury bags. You are surrounded by additional shoppers who will observe your decision, and a well-dressed sale with a warm smile guides you to a luxury bag that you have wanted for a long time. The bag sparkles under the light, showing its intricate design and craftsmanship. She explains that this bag is one of the most popular pieces and it was originally priced at ¥20,000. However, due to its estimated demand, the price has increased to ¥21,000."

Treatment Group 2 is the "Small price increase with private context" group. The scenario is similar as the first treatment group. However, in this group, the participants will be told alone in a private room, without observers and sales.

Treatment Group 3 will be the "Large price increase with public context" group. In this group, participants will also be settled in a public environment with the same budget and initial price as previous groups. However, the final increased price of the bag will be ¥28,000.

Treatment Group 4 will be the "Large price increase with private context" group. This group will experience a similar scene description and the same budget as the previous group, as well as the same original price and final increased price as the treatment group 3. Instead, participants in this group will be set alone.

Each treatment group will have a corresponding control group. Participants in each control group will receive the same scenario as the corresponding treatment group, but their scenario will be without the anchoring price increase information.

No matter what scenarios the participants are randomly distributed in, they are asked to rate how likely they would purchase the bag under given increased price and public/private context, with a range of 1 to 5 representing extremely unlikely to extremely likely. Given that the participants are all Chinese, the description will be translated into Chinese following the back translation principles [14].

3.4. Variables

The treatment variable in this experiment is the variations in small and high price increases and the shift of public and private settings. The dependent variable is the consumer decision, specifically the tendency of participants will buy luxury bags. Control variables include gender, age, interest or habit of buying luxuries, and income. Participants' ages range from 20 to 60 years old, and only those with an annual family income between ¥300,000 and ¥1.5 million were included. Participants

without an interest in luxury goods will be excluded to avoid biased results. The post-experiment analysis will exclude the confounding influence of gender and age on the relationship between the anchoring effect and consumer behaviors.

4. Results

4.1. Possible results

The results are expected as follows: (i) Compared to the control group, more people will choose "likely" and "extremely likely" when the price increase is small. (ii) On the contrary, fewer people will choose "likely" and "extremely likely" when the price increase is high. (iii) More people will choose "likely" and "extremely likely" in the public context than in the private context in the condition of both small and high price increases.

4.2. Discussion

The expected result shows that more people tend to buy luxury goods when the price increase is small, while fewer consumers will purchase when the price increase is high. The tendency indicates the anchoring effect of the initial price on consumers' behavior and its effect in increasing the purchasing the luxury goods. In the group "small price increase", the increasing price of ¥1,000 is tiny compared to the initial price of ¥20,000, which can be seen as a value addition of luxury goods. However, in the group "high price increase", the increasing price of ¥8,000 is relatively much higher, which is less motivated customers to buy luxury goods. Contrary to conventional economic demand theory, the little price increase of ¥21,000 after a high initial price can be seen as a strong social identity and social standing, which further contributes to the rising sales. Such findings are consistent with the statement that self-identity will promote consumption while branded goods symbolize social status, as Escalas and Bettman suggested [5]. Also, it expands the findings of Chen and Liu et al. by exploring the anchoring effect of initial price [8,10].

As for the difference in consumers' behaviors between public and private environments, most participants will choose to buy the bag with a high increase even if they thought it is not worth ¥28,000 in public environments. In public environments, considering social image and group membership, they consume to display their wealth and enhance their image, regardless of whether the price increases are high or small. This corresponds to the finding of Zhan and He, which elaborates that a higher benefit/cost ratio and compliance to social influence offered by luxury goods are the reasons for a stronger willingness to consume in a public environment for the Chinese Middle-Class [6].

5. Suggestions

As the expected results show that the purchasing decisions of the Chinese Middle-Class are significantly influenced by the anchoring of initial price and whether the environment is public or private, several suggestions are offered for both luxury goods merchants and consumers as follows.

5.1. For luxury goods merchants

To promote sales, merchants should consider increasing the prices of goods in smaller, more frequent increments instead of implementing a large price increase at once. Applying the anchoring effect, customers may perceive each low price increase as less significant and more acceptable.

Besides, merchants should hold more brand events and incentivise consumers to purchase luxury goods in public environments. Public consumption contexts can enhance social influence and consumers' perceived value of the products, which encourages purchasing even at higher prices. Also, luxury goods merchants can highlight the uniqueness and marketing social status and identity of luxury products. This also helps justify higher prices and motivate consumers' interest despite price increases.

5.2. For consumers

When considering the purchase of a price-increased luxury item, consumers should be aware of the anchoring effect of initial price and social influence. Assessing whether the product's perceived value justifies the higher price results in more rational purchasing decisions. Although the social status and image associated with luxury goods are attractive, consumers should ponder their financial situation and long-term goals. Balancing social influence with the personal financial condition is significant for making rational and responsible luxury consumption decisions.

6. Conclusion

This research mainly explored the anchoring effect in purchasing luxury goods among the Chinese Middle-Class from a psychological and behavioral perspective. By conducting the contrast experiment, the expected results show that people are more likely to purchase luxury goods when the price increase is low, especially in the public context. Such findings not only expand the previous literature on the anchoring effect of initial price but also close the research gap by establishing a link between the Chinese Middle-Class and the consumption of luxury products and offer insightful information to both merchants and consumers. Given that the research's scenarios involving the purchase of luxury bags are restricted, future studies researching the anchoring effect can focus further on other luxury goods.

Acknowledgment

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