


A black and white photograph of two polo players in action. The player in the foreground is wearing a dark jersey with the number 4, a light-colored helmet, and sunglasses. He is leaning forward, holding a mallet, and riding a dark horse. The player in the background is also wearing a helmet and sunglasses, and is riding a dark horse. The background is blurred, suggesting a fast-paced game.

SEYMOUR SLOAN
IDEAS THAT MATTER

**LUXURY 2020: THE TRENDS
THAT WILL SHAPE THE FUTURE
LUXURY MARKET**

A black and white photograph of three men in suits. The man on the right is in the foreground, looking slightly to the side. The man on the left is in the foreground, looking directly at the camera. The man in the background is slightly out of focus, also looking forward. They are all wearing dark suits, white shirts, and dark ties. The background shows a blurred city street with buildings and trees.

“I think there is something about luxury - it's not something people need, but it's what they want. It really pulls at their heart.”

Marc Jacobs

WE ARE WITNESSING A TRANSFORMATION IN THE LUXURY MARKET, CREATING OPPORTUNITIES FOR THOSE PREPARED TO ADAPT

The slowing luxury market in Asia has alarmed many luxury brands that had predicated future growth on improved prospects in Asia. In fact, a fundamental rethink is required around what the future looks like for luxury brands.

At the heart of the challenge is the need for luxury brands to identify the products and services they can provide credibly to their consumers. In a changing market, brands cannot stretch to selling everything. They face challenges from new entrants, focused on narrow but well-defined niches, snatching market share from existing brands. It is this clarity of purpose that has shaped the need for existing brands to reexamine their identities to compete.

Looking ahead to 2020 we see this as the ideal time to build the luxury brand of the future. This is the time to learn, recruit and implement the capabilities required to compete in a future market where traditional luxury norms become less relevant.

In conversations with leading luxury executives across 6 key regions we discussed the issues they faced approaching 2020. In addition, we spoke to leaders in complementary industries to identify potential blind spots for the luxury market heading into 2020. Below is a summary of these discussions combined with our own internal analysis to provide a view on what we think the main issues are for the luxury market.



POLITICAL INSTABILITY, SLOW ECONOMIC GROWTH AND INCREASED COMPETITION CREATE A CHALLENGING LUXURY MARKET, REQUIRING NEW APPROACHES

A CHANGING MARKET

We are witnessing a significant correction in the luxury market, one that has confounded many executives. It has meant that growth plans developed in the boom years must be hastily rewritten. Falling sales, falling margins, increased competition and sluggish global growth create the conditions for the retrenchment. With global growth forecasts appearing lukewarm at best, executives must confront new realities when developing market strategies.

Where Asia, particularly China, was the engine for luxury growth through the global recession, it now becomes the biggest source of concern.

LVMH, global leader in the sector, saw sales drop by 3% in Asia, excluding Japan, in the third-quarter of 2014. While Japan provides promise as a source of growth, it is still limited by a weak Yen. The protests in Hong Kong highlight the instability that is affecting wider confidence in Asia. However, what has dealt the biggest blow to sales is the Chinese government crackdown on corruption.

With increasing numbers of state officials receiving custodial sentences for corruption the corporate 'gifting' culture that fuelled the luxury boom has receded, further deflating the luxury market. As a result, China's richest spent 15% less overall in 2013 than they did in 2012, according to the Hurun Report, and 25% less on gifts overall.

The common view from market analysts is that China will contract as a market and now is the time for luxury brands to reconsider their expansion plans in China.

Of equal concern is the lack of large stable markets that can be exploited. Between Russia, Brazil, Indonesia and Nigeria each is beset by varying degrees of economic and political instability and as such, luxury brands are looking at a retreat to traditional markets among the developed economy. While this is a limit on potential growth, it provides greater revenue stability.

Luxury brands, in the search for lower risk but faster growth, may look at countries such as Turkey and Mexico that provide attractive opportunities in rapidly advancing economies. As an example, luxury spending in Turkey has grown by over 30% in the last four years.

As the market contracts and luxury brands retrench, two significant paths will emerge. Established brands will engage in stiffer competition with each other. In such situations it is likely that both prices and margins could fall. In addition, we are likely to see the creation of challenger brands in the markets, and segments, existing players retreat from. In these markets the successes of the future will develop. With favourable access to manufacturing facilities, business experience and large domestic markets, the progress of challenger luxury brands will be an interesting area to observe as we head towards 2020.

There are naturally exceptions to this. Some industries such as Luxury hotels, motoring and jewellery are affected by global macroeconomic trends, but seem better capable of weathering some of the microeconomic factors shaping the luxury market. The lack of natural substitutes and difficulty in counterfeiting are enormous pluses. Often the lead time in product development and completion means they are less immune to the boom and bust cycles that might affect fashion and drinks brands to an extent.

Luxury brands have to consider what lower margins mean for their business models. In high-level terms it will be the tension between big and small corporate structures. Margin protection shapes the next three years of competition as growth slows.

Looking at the conglomerates, their model is built on being able to synergise costs, use their buying power and the ability to cross-subsidise the less successful brands. However, these models are predicated on sustaining high margins with the stronger brands supporting the weaker brands.

At lower margins, even a reduction of 5% limits the scope of cross-subsidy, and at this point the conglomerate model may have to be revisited. It may be the case that the under-performing brands are better served as standalone entities or as part of other organisations. We expect such questions and issues to become pressing concerns, particularly as the appetite for M&A among the luxury conglomerates is still strong. We expect there to be changes in brand composition and alignment.

If we are looking at a future of smaller conglomerates then we could see groups such as Inditex take the divested brands and using their supply chain and infrastructure, use the acquired brands to reposition themselves further up the value chain. By 2020 we expect the upper levels of mass market brands either acquiring or competing with the lower level luxury brands as differentiation between the two reduces.

All of the above are driven by customer behaviour that has not changed this fast or significantly in a generation. Understanding these currents of change will allow brands big and small to realign their business to the new reality. Failure to do so could prove fatal to some brands.





"Technology will be more and more a merging factor and not a differentiation point. The key things will be more working on the design, materials and services part."

Max Pogliani - Vertu

ADAPTING TO RAPIDLY CHANGING CUSTOMERS WILL SHAPE FUTURE SUCCESS

THE CHANGING LUXURY CONSUMER

The future will herald customers for whom, all aspects of luxury are transparent and as such, will increase their expectations of luxury brands. The future will be about customers demanding more impact and quality for their money. This will be shaped by a number of important trends that are not only creating better informed customers but also, more demanding customers. Below we discuss these trends along with the impact they will have on the luxury market.

THE TRAVELLING CONSUMER – We are now in a globally integrated luxury market. Travel is a core element of luxury customers and this has fundamentally changed the buying experience for many consumers. The traditional model for luxury retailers had been to adopt variable pricing strategies, seeking to exploit the varying sensitivities to price in different markets.

International travel is challenging that model. In particular, Chinese travellers are embracing travel and buying the majority of their goods internationally. They avoid the high domestic prices and taxes, and often gain access to products well ahead of their release in China.

Chinese consumers now purchase more luxury goods abroad, often visiting New York and Paris to buy handbags and pens. Today, more than 60% of Chinese luxury goods are bought outside of the country. It is a similar picture in Brazil and Russia, with countries now actively wooing the wealthy elites to shop in their countries, which is particularly true in the luxury real estate market.

This creates two problems for luxury brands. There is the natural impact on margins as customers' shopping patterns move from high-cost to low-cost markets. Secondly, customers demand the European level of service and engagement in their home markets, which is driving cost upwards. Brands are now having to rebalance their pricing models, in addition to reshaping their location footprint to optimise return on capital.

By 2020 it is likely that luxury brands will operate with much leaner international footprints. We will see a retreat for many brands, driven by the desire to save cost. Instead, brands across all product classes will seek to offer more to their customers at higher price points, in a smaller number of locations. This assists in maintaining margins but in also, offering the international consumer a consistent high-level of experience.

THE DIGITAL CONSUMER – It is impossible to overstate how much digital technology has changed the world, and luxury is no exception. In high-level terms, digital technology has given consumers greater access as well as greater information around both luxury goods and the wider luxury lifestyle.

This greatly aids penetration for luxury brands and also, creates awareness and desire among customers. Current estimates put the volume of luxury sales influenced by digital at anywhere between 30-45%. As such, digital is an area nobody can ignore. By 2020 we see the share of luxury e-commerce reaching 10% of all sales, driven by a greater desire for speed and convenience.

However, digital poses a challenge that the luxury industry is getting to terms with; around what the luxury digital experience looks like. Creating a differentiated offering on platforms that are about universal access is difficult.

The luxury e-commerce experience is proving somewhat of a conundrum. In the next five years, brands will get a stronger sense of how customers wish to engage with them on digital platforms.

We see digital serving two main functions. Firstly, brands will use digital platforms to communicate messages around the luxury lifestyle, with this form of indirect marketing serving to stimulate aspiration and demand.

Secondly, digital will be a sales and service channel for those customers unable to visit a store, particularly in the case of an emergency purchase. Unlike other market sectors that are driven by reducing unit cost, the e-commerce imperative is not as great for luxury brands. However, success in digital is a pillar for overall success.

THE SOCIAL CONSUMER - A growing area of the digital landscape shaping luxury awareness is social media. With hashtags such as, #OOTD (Outfit Of The Day) we are in an era where we are sharing our luxury experiences. Platforms such as Facebook, Twitter and Instagram are overcome with images of dinner at Corrigan's, nights out at The Box, shopping on Fifth Avenue, hotel Stays at the Connaught and the latest purchase of an Aston Martin. Aggregated, these images have increased global brand awareness and at the same time stimulate desire to acquire these products and services.

Successful brands are already targeting key social media influencers to drive their brand messages. In the coming years, and as analytics improve, brands will be able to identify the key targets and also measure both direct and indirect consumer impact.

What we will see with digital is a decoupling of the purchase decision from the purchase process and luxury brands must excel at both phases.

Brands must be aware that customers have high expectations of their luxury experiences, rewarding those that understand and deliver them while ignoring those that do not. The journey to 2020 will be a return to the core values of luxury; exclusivity and individualism. There will also be a move towards localisation; bringing cultural diversity to the luxury market.

THE FLIGHT TO EXCLUSIVITY - Market growth over the last seven years has broadened brand access, allowing new customers to access previously unobtainable brands. This has been a significant success for brands across the luxury spectrum that were able to tap into years of latent demand. However, we are approaching a slowing of this initial surge in luxury demand.

Customers will look beyond traditional brands and products for their luxury consumption and this change will be driven by a number of factors. Customer research identified three issues focused on the following areas:

Overexposure – Brands need to manage the balance of satisfying demand without spreading the brand too thinly. Ownership of certain brands no longer brings the impact of old due to broader exposure. There is, and will be, an appetite for something different in the luxury experience. We are seeing a retreat by some brands now as they realised that they have likely overstretched themselves. There is also an indirect effect from counterfeiting. Fake products do negatively impact legitimate brand values, with some brands are being hit harder than others as they have outsourced manufacturing to the Far East. We will see a retreat from many brands as they focus on fewer, but higher value items.

Harmonisation of the Customer Experience – As much of the luxury value-chain has been outsourced to common providers; the luxury purchasing experience has coalesced around similar themes across most brands. This convergence has resulted in an experience that one customer called 'generic, almost lazy.' There is an appetite for more diverse customer experiences along with a more individual customer experience.

The winners of the future will create novel experiences, but will also ensure that their offering evolves and remains current and relevant, adapting to changing customer tastes.

The Lack of Local Identity - Customers in emerging markets, particularly early adopters, who have consumed luxury goods for an extended period, now seek products that better represent their culture and heritage. Some customers have identified the feeling that they are buying into a culture that is not theirs.

This is an opportunity for new brands, in emerging economies, to add to the luxury landscape. It is the largest area for potential growth that is yet, unexploited. With these trends set to intensify, the future focus will be a greater customer desire for exclusivity. High-value luxury customers will continue to use big ticket purchases to define their status and to shape identities. As such, luxury brands will need to make the customer feel special again.

Luxury brands must embrace this and redesign propositions and customer experiences across: products, pricing and distribution. The ability to deliver a unique proposition will enable brands to charge premium prices while delivering tangible exclusivity.

INCREASED INDIVIDUALISM - The last seven years have seen customer-centricity correctly become the dominant principle when designing a business model. The logical extension of that will be moving towards customer empowerment, freeing the customer to shape their outcome. Chiefly, this will involve an emphasis on product customisation and in some cases, full customer design. It also extends to multi-channel distribution and servicing allowing full channel flexibility.

Currently, many brands allow customisation across a number of core features, but it is likely that the super-wealthy will seek to engage the design staff at the concept stage. In such cases, the customers would lack any sensitivity to price making such an approach viable. The flow could also work in reverse with designers pitching designs to the top-tier customers on an exclusive basis.

For high-value customers, creation in conjunction with leading brands will represent the ultimate in luxury. In a market where purchasing decisions are increasingly similar, this will be a powerful differentiator. It will rebalance the relationship back towards the brand as the customer aspires to be sufficiently valuable to gain preferential access.

LUXURY WITH MANY FACES - Two key trends that will increase as we head towards 2020 are; the increase in designers from emerging markets in leading roles within luxury brands and the emergence of luxury brands in emerging markets. The initial stage will arrive when a critical mass of designers from emerging markets working in the leading brands.

Diversity will manifest itself in a wider range of product ideas and marketing approaches. With the experience from leading brands available, these designers will branch out to build brands in their native markets. Using the organisational knowledge married with local cultural awareness, this generation of designers will develop challenger brands that will redefine specific market segments.

An excellent example is Osklen, a Brazilian brand that is now looking for investment to expand its range of luxury sportswear abroad. It presents a different proposition to European brands, but as Brazil develops and Brazilians travel, it represents an opportune moment to expand.

THE CHANGING LUXURY CONSUMER – The world is changing beneath our feet. Modern day successes are often technologists, often very young, and are creating a new definition of luxury. One only has to look at Mark Zuckerberg to see how the corporate wardrobe is changing. Slowly, the bespoke suits, briefcases and watches are ignored in favour of casual items with a distinct absence of brand names.

Instead, luxury purchases are on bigger-ticket items such as travel, cars and in many cases property. We are seeing a generation chastened by the excesses of the previous decade. An interesting change is the increasing significance of sustainability when considering purchasing decisions. Even luxury brands will have to demonstrate both environmental and social responsibility. As we move towards 2020 there will be a greater requirement for luxury brands to be exemplary citizens.

Another rising trend is the desire for authenticity. Ten years ago, you could find a takeaway van in most British cities selling a range of food that was unlikely to be healthy for you. However, the rise of street food vendors has seen a change in that. They now provide a diversity of and through this, can often charge premium prices for their products.

Driven by the increasing need for authenticity – the feeling of closeness between creator and consumer – street food vendors are able to charge a premium for their products. This desire for authenticity is seeing the rise of local brands, musicians, hotels, in fact, anything where the consumer feels intimacy with the brand.

As this trend rises through the mainstream, luxury brands must be ready with products and services that have that authenticity. It is also a natural return to the essence of luxury - the idea of the artisan hand crafting products with passion.

THE LUXURY START-UP - Another potential development is further subdivision of the luxury brand into micro niches, serviced by the challenger brands lacking the capital or desire to compete with the luxury conglomerates. By attacking specific niches, they reduce the barriers to entry and can better tailor their proposition to their target audience.

We are witnessing a boom in such brands. From Adrien Sauvage's eponymous label, Aaron Dash with MrDash, Dymant in Paris to Lux-Fix, brands are exploiting niches that only small and nimble operators can exploit.

We believe there are, and will be, opportunities for luxury start-ups. It has never been easier to start these brands. They can opt for a very lean manufacturing process, outsourcing all but the core elements to scale much more quickly than a traditional company that manufactures everything. They don't need a big marketing team to reach the customer in today's market. For example, Leonard & Church is a start-up direct to consumer watch manufacturer. They aim to deliver the same high-quality handmade watch quality offered by established brands at far smaller mark-ups.

They may not carry the same weight as decades-old brands - they don't have to in order to be a profitable and sustainable business in today's start-up-friendly culture.

On a larger scale, the lustre of well-established brands is fading away - and it is especially true for brands that sell high-end products. The factors highlighted in this paper create a climate where new entrants, offering the same quality but with a better overall customer experience, can succeed.





**“Some people say culture
trumps strategy, but I don’t
believe that’s true, strategy
emerges from culture.”**

Milton Pedraza - The Luxury Institute

FUTURE SUCCESS WILL ARISE FROM INTERNAL CHANGE. FUTURE LEADERS ARE ACTING NOW

SUCCESS FROM WITHIN

The driving force of success will be from the internal changes that luxury brands make to remain relevant, responsive and adaptable. The ultimate aim is to remain closer to the customer and to deliver on their expectations.

CHANGE STARTS AT THE TOP – Strategy will move away from linear 1, 3 or 5 year plans to an iterative approach, where the overarching vision and strategic goals are agreed, but revisited quarterly or biannually. Executives must review their goals regularly, accounting for the changing competitive landscape as well as evolving consumer habits. More importantly, goals must be reviewed in light of the behaviour of competitors and new entrants.

Strategy is now a chess game between competitors, with brands responding to every market move in real-time. Heading towards 2020 luxury brands will remodel their business architecture to deliver agility and responsiveness to meet customer needs. Those responsible for strategy formation and execution will require the capability, aptitude and tools to monitor market movements as close to real time as possible. In addition, they will need decision making processes that emphasise speed of response in order to react to opportunities as they arise.

CHANGING BUSINESS STRUCTURES – The future of the luxury market will still be driven by the creative inspiration that has underpinned the market from its earliest beginnings. The big change now is in the execution of the vision. Organisational structures will need to evolve and with it, we expect to see an increased importance of the commercial roles.

There will be a move away from the traditional Head of Creative and Head of Commercial towards a wider span of decision makers. Initially, we see the CEO, particularly in the larger organisations, being supported by the following core roles:

- Head of Strategy
- Head of Customer
- Head of Operations and
- Head of Creative

As organisations develop, more roles will become necessary, particularly as geographic reach extends. In the initial phase of development, these are the roles that will allow luxury brands across the spectrum to be closer to the customer and also, closer to the markets while simultaneously driving the internal development agenda.

INNOVATION – We are heading into a world in 2020 where marketing will be, ‘on demand.’ Customers will have access to a brand at the very point they need it. This, added to the wider technological and social revolutions, will create new opportunities for those quick enough to identify, understand and deliver on them.

To succeed at this, the main areas of Strategy, Customer, Creative and Operations have to work together to turn ideas into reality faster than the competition. They must be the leaders of the innovation agenda, pushing their brands into products and experiences that leave the mass market behind. Innovation is a vital area of leadership for luxury brands, particularly as they seek to sustain or improve profit margins.

Marketing is a clear example of where innovation is required. Internal research suggests that over 80% of marketing executives feel their analytics capabilities are insufficient to deliver the marketing experience they would like. Most executives in the luxury market identified four main areas they would like to direct their innovation:

- Product Quality
- Customer Value
- Customer Impact and
- Customer Loyalty

With 70% of customers making some element of their buying decision online, often the battle can be lost before anyone is aware. As such, innovation is about reducing the blind spots in the marketing journey. To achieve a strong innovative base, the leadership team must collaborate to identify challenges and solutions as well as providing the drive to deliver them. The luxury market is catching up, but is still behind sectors such as the tech sector that have wired innovation into their daily business routines.

MASTERING TECHNOLOGY – Technology is an area where luxury brands are playing catch up with the rest of the consumer goods market. Understanding your customers and understanding technology are two parts of the same whole. We are seeing new product and distribution categories, from wearable technology to 'showrooming,' where customers visit a store to decide on a product then seek out the best price and delivery options online.

These all require back-end technology to support them and luxury brands must now face the challenge of investing in market leading technology solutions. To achieve this, the Head of Operations must have strong technological experience and be a champion of digital solutions to drive performance. The new skills that underpin this such as, social media, analytics, 3-D prototyping with 3-D printers and customer relationship management (CRM) are scarce in the wider economy, placing them at a premium. However, luxury brands cannot ignore these new challenges as they can have a disruptive effect on the overall market. Instead, a concerted effort is required in acquiring both the enthusiasm for technology and the skills to make it happen.

MORE PEOPLE, NEW SKILLS – The ability to recruit and retain the right people lies at heart of sustainable success. In a changing market, we are seeing new skills enter, skills essential in getting the luxury industry up to speed with other high margin organisations such as Apple. Heading towards 2020, the luxury market will see an influx of skills from outside the luxury sector arriving to accelerate development.

In particular, we expect an increase in MBAs and those with experience of change programme delivery. These specialist skills will augment other core skills such as digital marketing, analytics and broader technology skills.

This could give rise to commercially driven luxury brands, where business people, with complementary skills partner with a designer to deliver lean and agile luxury brands with the disciplines of a listed company. We will see an accelerated start-up process, taking advantage of the areas where creative-led brands often struggle in order to grow rapidly.

We expect to see greater diversity in the composition of luxury brands, reflecting the reality that consumers will be looking for some cultural connection with foreign luxury brands.

Luxury brands must maximise the diversity of ideas, skills, backgrounds and influences without sacrificing quality. Diversity will allow brands access to influences and trends they may otherwise miss. It is these ideas that shape the innovative visions that define the luxury market. The businesses that can support a large degree of individualism in its products will prove the winner in the high-end luxury segment.

The business model should accommodate a division that can deliver on the customisation issues outlined above. Ideally it will be supply driven with luxury brands offering the service to the highest spending customers. This creates an incentive to increase spending. It will also fulfil the customers' desires to feel special as well as define themselves as an individual.

CONCLUDING THOUGHTS

We are facing a new model of growth as the existing luxury market matures. The splintering of the market is driven by the cultural diversity of the high-net worth market. Their needs are different and their approaches to fulfilling those differ too.

The organisations that will thrive in these changing times are those best placed to understand the new needs, as well as subtly changing existing needs, and adapting effectively to those. The two elements successful organisations must possess are, true diversity and organisational agility to react to a changing market.

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