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# Luxury apparel market in China

Visiting the big-name luxury retail outlets in fashion hubs such as Paris and Hong Kong, you will probably be amazed by the spending sprees of Chinese consumers. As China grows in economic significance, swelling pockets in the country have spurred huge demand for luxury merchandise. Today, China is the second largest luxury market in the world and the market is still growing fast. Many international luxury apparel retailers view China as a must-win market and are rushing in the market to ride this enormous growth.

While it is true that after Chinese consumers have a taste of luxury, there is unlikely to have any turning back; China is still far different from mature markets such as Japan or France. To win in this market, one has to understand its very unique features. In this issue, we will have a special focus on China's luxury apparel market, addressing the market potential, its distinctive characteristics, the competitive landscape, as well as some of the major challenges.

## I. Overview

According to the World Luxury Association, China is now the world's second largest luxury market[1] after Japan; Chinese consumers have spent over US$8 billion on luxuries in 2007. Accounting for 18% of the global market for luxury goods last year, it is estimated that China would overtake Japan and become the world's largest luxury consumer in 2015 with its share growing to 32%.

Indeed, the top lines of leading luxury groups have echoed the importance of this emerging giant. The LVMH Group announced that the revenue of fashion and leather goods from Asia region excluding Japan increased by

1 The study tracks sales of jewelry, fashion, leather products and fragrances, but excludes private aircraft and yachts

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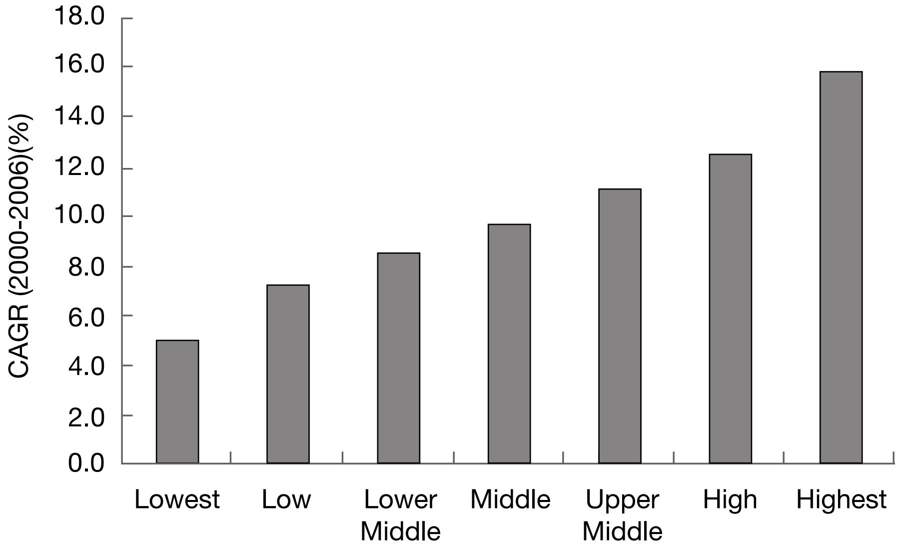
21% in 2007; and China was one of the major growth engines. The Richemont Group also saw its retail sales in China rise by 47% in 2007. Meanwhile, the PPR Group reported that revenue from its Gucci arm in China rose by a staggering 130% year on year in the forth quarter of 2007.

Consumers' trading-up has driven the prominent growth of luxury sales. According to the World Luxury Association, 13% of the Chinese population has purchased luxury goods last year. While many believe the actual number of luxury consumers in China may be smaller, there is no doubt that luxury consumers in China have reached a critical mass. Indeed, steady income growth has fuelled luxury sales in China. According to National Bureau of Statistics of PRC (NBS), residents' income has been increasing steadily in China over the past years, of which the highest income segment has shown the most impressive gains in wealth (see Exhibit 1).

### Exhibit 1: Growth in Household Disposable Income, 2000-2006




| | | | | | | | |
|---|---|---|---|---|---|---|---|
| **% of population** | 10 | 20 | 20 | 20 | 20 | 10 | 10 |

*Source: National Bureau of Statistics of China, PRC*

Exhibit 2 demonstrates the number of individuals with personal wealth over US$ 1 million by Hurun Report, a leading luxury business portal in China. The huge number of China's very rich is a definite plus for the country's luxury sector.

### Exhibit 2: Number of individuals with personal wealth over US$ 1million, 2007

| Personal wealth (US$ million) | No. of individuals |
|---|---|
| 1 | 500,000 |
| 5 | 150,000 |
| 10 | 35,000 |
| 100 | 2,000 |
| 1,000 | 50 |

*Source: 2007 Hurun Report research*

The burgeoning middle class[2] is another major force to be reckoned with. It is estimated that the number of middle-class Chinese has reached 80 million in 2007, accounting for 6.15% of the population. The shopping list of this increasingly affluent class has extended beyond basic necessities. As people aspire to achieve higher quality of life, the appeal of luxuries is quickly finding resonance among the country's high flyers.

# II. Distinctive features of China's luxury apparel market

China's luxury market has just begun to take off. To win in this marketplace, enterprises must grasp its many distinctive features.

## 1. China's luxury market is predominately male-driven

The profile of luxury consumers in China is vastly different from overseas. Chinese luxury market is predominately male-driven. According to Merrill Lynch, China is the only market in the world where men consume much more luxury than women. Besides, the luxury consumers in China are much younger than their western counterparts. Male aged between 25 and 40 are the major consumer group, as opposed to those generally aged between 40 and 70 in Western markets. Young professionals, entrepreneurs, businessmen and celebrities are the major consumers. However, with the rise of female consumerism in China, marketers should not ignore the potential of female luxury market.

## 2. Consumers are less sophisticated and less brand-savvy

Compared to many developed economies, China's luxury market is not yet mature. Chinese luxury consumers tend to be less sophisticated and less brand-savvy; and many of them have a typical "show-off" attitude towards luxury purchase. Strongly influenced by "face", Chinese luxury consumers want to be recognized. Designer labels that are highly recognizable by the public such as Louis Vuitton or Gucci are often regarded as must-haves by first-time luxury buyers. Furthermore, luxury items with highly visible features such as prominent logos, though seldom do well outside China, are often the bestsellers in the country.

Nonetheless, as luxury retailers beef up their presence in China and increase their marketing efforts, we expect Chinese consumers to gain more exposure and grow in their acceptance toward a wider range of luxury brands.

## 3. Luxuries without hefty price tags win strong appeal among the aspirational Chinese consumers

Despite having the strongest income growth in the world, the buying power of most Chinese consumers is still considerably lower than foreign counterparts. Affordable luxuries thus are winning strong appeal for those aspiring for better lifestyle and yet with limited spending power. Understanding that many middle-class Chinese are willing

2 The NBS defines middle class as households with an annual income ranging from 60,000 yuan to 500,000 yuan. It estimates that the proportion of middle class in China will expand to 45 percent in 2020 from 5 percent in 2005.

to save to pay for higher-priced items, a number of luxury players in China are tapping into this market through the offering of lower-priced alternatives. For instance, Hermès in China now offers bracelets and mobile phone accessories to give Chinese consumers affordable access to luxuries.

## 4. Gift-giving culture promises huge business opportunities

Another distinctive feature of China's luxury market is corporate gift giving. To demonstrate their courtesy and build good rapport (guanxi), Chinese business executives often offer gifts such as apparel, accessories or watches to their key clients and business partners. It is estimated that business gifting accounts for around 50% of China's luxury consumption. The gift-giving culture promises huge business opportunities for luxury apparel retailers in China.

## 5. Regional differences in consumer mentality play a role in shaping China's luxury market

China is a country with many different economies. While everybody would tell that wealth in the country is concentrated in the Pearl River Delta, the Yangtze River Delta and the Bohai-Rim region, huge differences in consumer mentality across the regions also play a role in shaping the luxury market. Marketers must go beyond the statistics.

For instance, consumers in the north eastern provinces generally place heavier emphasis on "face" and they look for prominent logos and extravagant features; whereas consumers in the south eastern regions tend to be more subtle and sophisticated. Consumers in Chengdu demonstrate another example of how local differences come into play. While income in this western city is not particularly impressive, Chengdu consumers are known for their resemblance to the US consumers who have a natural urge to spend; the city's luxury market flourishes.

## 6. Mainlanders shop overseas for luxuries

The pricing of luxury merchandise in mainland is generally higher than overseas markets because of higher tax and duties. With increasing income, Renminbi appreciation against the US dollars and easing travel restrictions, more and more Chinese consumers shop for luxuries abroad. Hong Kong is one of the favorite destinations for luxury spending due to its proximity to the mainland. According to China Economic Monitoring & Analysis Center, 49.7% of the wealthy people cited Hong Kong as their most desirable shopping destination. We also witness many luxury retailers such as Louis Vuitton and Cerruti 1881 setting foot in Macau this year as new casinos have attracted new waves of Chinese tourists.

# III. Competitive landscape and movements of major players

## 1. Dominance of foreign players in the luxury market

Foreign players dominate China's luxury apparel market. As Chinese luxury consumers tend to favor brands that can be easily recognized by others, super-brands have a stronghold. Brands such as Louis Vuitton, Chanel and Gucci are the biggest winners and they enjoyed tremendous success in China.

Meanwhile, domestic brands are virtually absent in China's luxury scene. However, some domestic players have strived to move up the value ladder and hoping to get a place in the premium market. For instance, NE·TIGER (東北虎), which claimed itself to be China's first luxury apparel brand, has set up studios in the States, France, Italy and Russia to work on design innovation. Jefen (吉芬) is another example, and it has stepped out of China and was invited to Paris Fashion Week in 2007. Though, we should admit that these domestic brands have only minimal presence in the luxury segment. There is still a long way to go for domestic players to rival their foreign counterparts.

## 2. Retailing network of luxury apparel retailers

To translate opportunities into profits, many apparel luxury retailers have embarked on or planned for retail network expansion in China. In Exhibit 3, we demonstrate the retail network of selected apparel retailers in different Chinese cities. The cities are ranked in the order of respective competitiveness complied by the authoritative Chinese Academy of Social Sciences in 2007. Those cities higher on the list are often viewed as with higher development potential and denote stronger economic influence. Some interesting facts about luxury apparel retailers in China can be found.

**Exhibit 3: Sales locations of selected apparel retailers in China**

| Rank | City | A.Testoni | Altea | Aquascutum | Armani | Bally | Brooks Brothers | Burberry | Canali | Celine | Cerruti 1881 | Dunhill | D'Urban | Ermenegildo Zegna | Gianni versace | Gieves & Hawkes | Givenchy | Gucci | Hugo Boss | INTERMEZZO | Kent & Curwen | Lanvin | Longchamp | Louis Vuitton | Prada | Salvatore Ferragamo | Tod's | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 1 | Shenzhen 深圳 | 2 | 1 | 3 | 1 | 3 | | 2 | 2 | 1 | 3 | 2 | 3 | 2 | | 1 | 1 | 1 | 4 | 1 | 4 | 1 | 1 | 2 | | 2 | 1 | 44 |
| 2 | Shanghai 上海 | 2 | 1 | 8 | 12 | 6 | 6 | 3 | 4 | 2 | 8 | 8 | 9 | 6 | 2 | 9 | 3 | 4 | 8 | 5 | 9 | 1 | 4 | 1 | 1 | 3 | 3 | 128 |
| 3 | Beijing 北京 | 3 | 4 | 4 | 4 | 4 | 4 | 3 | 5 | 1 | 7 | 8 | 9 | 6 | 3 | 10 | 3 | 5 | 8 | | 7 | 1 | 1 | 3 | 3 | 6 | 1 | 113 |
| 4 | Guangzhou 廣州 | 1 | | 4 | 1 | 2 | 1 | 3 | 1 | 1 | 3 | 1 | 3 | 1 | | 1 | 1 | | 2 | 1 | 1 | 1 | | 1 | 1 | | | 31 |
| 5 | Wuxi 無錫 | | | | | | 1 | | 1 | | | 1 | | 1 | | 1 | | | 2 | | 1 | | | | | | | 8 |
| 6 | Suzhou 蘇州 | | | | 1 | 1 | 1 | 1 | | | 2 | 1 | 2 | 1 | | 2 | | 1 | 3 | | 2 | | | | | 1 | | 19 |
| 7 | Foshan 佛山 | | | | | | | | | | | 1 | | | | | | | | | | | | | | | | 1 |
| 8 | Qingdao 青島 | 1 | | | 1 | 1 | 1 | 1 | 2 | 1 | 1 | 1 | 1 | 1 | 1 | 1 | | 1 | 2 | 1 | 1 | | | 1 | 1 | 1 | | 22 |

| Rank | City | A.Testoni | Altea | Aquascutum | Armani | Bally | Brooks Brothers | Burberry | Canali | Celine | Cerruti 1881 | Dunhill | D'Urban | Ermenegildo Zegna | Gianni versace | Gieves & Hawkes | Givenchy | Gucci | Hugo Boss | INTERMEZZO | Kent & Curwen | Lanvin | Longchamp | Louis Vuitton | Prada | Salvatore Ferragamo | Tod's | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 9 | Tianjin 天津 | | | | | 1 | 1 | | 1 | | 1 | 1 | 3 | 1 | 2 | 1 | | 1 | 3 | | 2 | | 1 | 1 | | 1 | 1 | 22 |
| 10 | Hangzhou 杭州 | 1 | | 1 | 2 | 1 | | 1 | 1 | 1 | 1 | 2 | | 2 | 1 | | | 1 | 1 | | 1 | | | 1 | | 1 | 1 | 20 |
| 11 | Dongguan 東莞 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 12 | Ningbo 寧波 | | | | | 2 | | 1 | 1 | | 1 | 2 | | 1 | | 1 | | | 2 | | 1 | | | | | 1 | | 13 |
| 13 | Dalian 大連 | 1 | 1 | | 1 | 1 | 1 | 2 | 2 | | 2 | 2 | 2 | 2 | | 2 | | | 2 | | 2 | | | 1 | | 2 | | 26 |
| 14 | Jinan 濟南 | | | | | 1 | | 1 | 1 | | 1 | 1 | | 1 | | 1 | | | 2 | | 2 | | | | | 1 | | 12 |
| 15 | Xiamen 廈門 | | | | | | 1 | 1 | 1 | | | 2 | 2 | 1 | | 1 | | | 2 | 1 | 2 | 1 | | 1 | | | | 16 |
| 16 | Nanjing 南京 | | | | | | | 2 | 1 | | 1 | 2 | | 1 | 1 | | | | 2 | | 1 | 1 | 1 | 1 | | 1 | | 15 |
| 17 | Zhongshan 中山 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 18 | Changsha 長沙 | | | | | 1 | | 1 | 1 | | 2 | 2 | | 1 | | 1 | | | 2 | | 2 | | | | | | | 13 |
| 19 | Shenyang 瀋陽 | 1 | | | 1 | 2 | 1 | 2 | 3 | 1 | 3 | 3 | 3 | 3 | 1 | 2 | | 1 | 3 | 2 | 2 | | 1 | 2 | 1 | 2 | 2 | 42 |
| 20 | Changzhou 常州 | | | | | | 1 | | | | | 1 | | 1 | | | | | 1 | | 1 | | | | | | | 5 |
| 21 | Wuhan 武漢 | | | | 1 | 2 | 1 | 1 | 2 | | 2 | 2 | 2 | 1 | | 2 | | | | | 3 | | | | | | | 19 |
| 22 | Yantai 煙台 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 23 | Zibo 淄博 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 24 | Weihai 威海 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 25 | Chengdu 成都 | 1 | | | 1 | 1 | | 1 | 1 | 1 | 1 | | 2 | 3 | 1 | 2 | 1 | 1 | 3 | 2 | 5 | | 1 | 2 | 1 | 1 | 1 | 33 |
| 26 | Fuzhou 福州 | | | | | | | | 1 | | 1 | 1 | | | | | | | 1 | | 1 | | | | | | | 5 |
| 27 | Anshan 鞍山 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 28 | Hefei 合肥 | | | | | | | | | | | 1 | | 1 | | | | | 1 | | | | | | | | | 3 |
| 29 | Nanchang 南昌 | | | | | | | | 1 | | 1 | 1 | 1 | | | 1 | | | 1 | | 1 | | | | | | | 7 |
| 30 | Nantong 南通 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 31 | Changchun 長春 | 1 | | | 1 | 1 | 1 | 1 | 1 | | 1 | 1 | 1 | 1 | | 1 | | 1 | 1 | | 1 | | | | | 1 | | 15 |
| 32 | Zhuhai 珠海 | | | | | | | | | | | 1 | | | | | | | | | | | | | | | | 1 |
| 33 | Shaoxing 紹興 | | | | | | 1 | | | | | | | | | | | | 1 | | | | | | | | | 2 |
| 34 | Harbin 哈爾濱 | 1 | | | | 1 | | 1 | 1 | | 4 | 2 | 3 | 1 | | 4 | | | 1 | | 5 | | | | | 1 | | 25 |
| 35 | Xuzhou 徐州 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 36 | Tangshan 唐山 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 37 | Xi'an 西安 | 1 | | | 1 | 2 | | 1 | 2 | | 2 | 2 | 2 | 2 | 1 | 2 | | 1 | 2 | | 3 | | | 1 | 1 | 1 | 1 | 28 |
| 38 | Yangzhou 揚州 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 39 | Shijiazhuang 石家莊 | | | | | | 1 | | 1 | | 1 | 1 | 1 | 1 | | 1 | | | 1 | | 1 | | | | | | | 9 |
| 40 | Ordos 鄂爾多斯 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 41 | Chongqing 重慶 | 1 | | | 1 | 1 | 1 | 1 | 1 | | | 1 | 1 | 1 | | | | | 2 | | 1 | 3 | | | | 1 | | 16 |
| 42 | Taizhou 台州 | | | | | | | | | | | 1 | | 1 | | | | | 1 | | | | | | | | | 3 |
| 43 | Wenzhou 溫州 | | | | 1 | 1 | | 1 | | | | 3 | | 2 | | | | | 3 | | | | | 1 | | 1 | | 13 |

| Rank | City | A.Testoni | Altea | Aquascutum | Armani | Bally | Brooks Brothers | Burberry | Canali | Celine | Cerruti 1881 | Dunhill | D'Urban | Ermenegildo Zegna | Gianni versace | Gieves & Hawkes | Givenchy | Gucci | Hugo Boss | INTERMEZZO | Kent & Curwen | Lanvin | Longchamp | Louis Vuitton | Prada | Salvatore Ferragamo | Tod's | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 44 | Zhenjiang 鎮江 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 45 | Zhengzhou 鄭州 | | | | | 1 | | 1 | 1 | | 1 | 2 | | 1 | | 1 | | | 1 | | 1 | | 1 | | | | | 11 |
| 46 | Jiaxing 嘉興 | | | | | | 1 | | | | | | | | | | | | | | | | | | | | | 1 |
| 47 | Baotou 包頭 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 48 | Hohhot 呼和浩特 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 49 | Panjin 盤錦 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 50 | Quanzhou 泉州 | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| 52 | Taizhou 泰州 | | | | | | | | | | | | | | | | | | 1 | | | | | | | | | 1 |
| 56 | Taiyuan 太原 | 1 | | | | | | 1 | 1 | | 1 | 2 | 1 | 1 | | 1 | | | 1 | | 1 | | | | | | | 11 |
| 62 | Jinhua 金華 | | | | | | | | | | | | | | | | | | 1 | | | | | | | | | 1 |
| 65 | Kunming 昆明 | | | | | 1 | | 1 | 1 | | 1 | 2 | 1 | 1 | 1 | 1 | | | 1 | 1 | 1 | | | 1 | | 1 | | 15 |
| 76 | Lanzhou 蘭州 | | | | | | | | | | | | | | | | | | 1 | | | | | | | | | 1 |
| 78 | Ürümqi 烏魯木齊 | | | | | 1 | | | | | 1 | 2 | | 2 | | 1 | | | | | 1 | | | | | | | 8 |
| 80 | Zhanjiang 湛江 | | | | | | | | | | | | | | | | | | 1 | | | | | | | | | 1 |
| 88 | Haikou 海口 | | | | | | | | | | | 1 | | | | | | | 1 | | | | | | | | | 2 |
| 90 | Nanning 南寧 | | | | | 1 | 1 | | | | 1 | 1 | 1 | | | 1 | | | 2 | | 1 | | | | | | | 9 |
| 111 | Guiyang 貴陽 | | | | | 1 | 1 | | 1 | | 1 | 1 | 1 | | | 1 | | | 2 | | 1 | | | | | | | 10 |
| 143 | Dandong 丹東 | | | | | | | | | | | | | | | | | | 1 | | | | | | | | | 1 |
| n.a. | Sanya 三亞 | | | | | | | | | | | | | | | | | | | | | | | | | | 1 | 1 |
| Total | | 18 | 7 | 20 | 30 | 40 | 27 | 34 | 42 | 9 | 55 | 69 | 54 | 51 | 14 | 53 | 9 | 18 | 80 | 14 | 68 | 9 | 11 | 20 | 9 | 29 | 12 | 802 |

*Source: Li & Fung Research Centre, respective company websites*

*Note: The 50 most competitive Chinese cities are shown; the cities afterwards without the presence of selected luxury retailers are omitted.*

### (1) Luxury apparel retailers generally have more sales location in top cities; inland provincial capitals are also the chief targets

As shall be seen in Exhibit 3, most of the luxury retail locations are located in China's most competitive cities. Top-tier cities such as Shanghai, Beijing and Shenzhen are the most attractive to luxury apparel retailers. Shanghai, viewed as China's fashion capital, has allured the largest number of players to set foot in. Indeed, the city is of strategic importance to many luxury apparel retailers for its strong showcase effects in China.

Some cities further lower in terms of overall competitiveness have also attracted quite a number of luxury retailers. In fact, as wealth in China trickles into other lower-tier cities, major inland cities that can easily accessed by surrounding cities and counties have also entered luxury retailers' radar screen. In particular, inland provincial capitals such as Xi'an in Shaanxi, Taiyung in Shanxi and Kunming in Yunnan where business and tourist activities concentrate are retailers' chief targets.

### (2) Male-oriented luxury players have more extensive footprints

As observed, the number of retail sales locations of male-oriented luxury brands is significantly higher than those female-oriented brands in China. These male-oriented luxury brands also have more aggressive expansion; they are usually the first movers into less developed Chinese cities. This is consistent with the fact that China's luxury market is predominately male-driven, which gives a natural boost to brands such as Ermenegildo Zegna, Gieves & Hawkes, Cerruti 1881, Dunhill and Hugo Boss.

## 3. Specialty outlets and department stores are the chief distribution channels

Luxury players are hugely image-conscious. To achieve stricter control on shopping environment and to ensure a good mix of high-quality adjacencies, they spend huge efforts on retail site selection. Most of the luxury merchandises are sold through concession counters in high-end department stores and specialty stores in upscale shopping malls and hotels in China. And according to Jones Lang LaSalle, retailers increasingly look for larger retail spaces to build their flagship stores. Competition for super-sized duplex stores with huge facades is particularly fierce as luxury retailers are keen to raise visibility in this increasingly competitive market.

## 4. Players expand their product portfolio to appeal a wider audience

To capture the opportunities by the emerging mass affluent class in China, many luxury players have sought to launch products to cater to different levels of the aspirational curve. For instance, PORTS plans to continually expand its product lines including jewelry, fragrance, handbags and shoes in the coming years. The body wash lotion launched by Ermenegildo Zegna is another example. Marketers hoped that these items will be affordable to a much wider market in China and yet remain special.

## 5. Marketers explore more exciting marketing tools

While print advertisements in magazines and billboards are thus far the most-often-used marketing tools for luxury players in China, some marketers are also trying different promotional campaigns to impress consumers. Louis Vuitton is for instance embracing the "medium of the masses" by launching its first ever on-screen corporate campaigns via cable and satellite television channels and movie theaters. The company believes that advertisement would be particularly useful in reaching new audiences in emerging markets like China. PORTS, one of the leading luxury apparel players in the country, is on the other hand the official sponsor for the 21st Century FOX picture "The Devil Wears Prada". The film has PORTS visuals appearing throughout the movie. Fendi also presented its spring-summer 2008 collection on the Great Wall of China.

## 6. Luxury players embrace more casual elements

The luxury sector is embracing more casual elements. While luxury formals are still the mainstream among the male-oriented brands in China, luxury casuals are fast gaining popularity, particularly in the younger working population. As the country increasingly exposes to western fashion trends, luxury casuals look set to demonstrate rapid growth. As a result, many luxury brands are launching their new casual collections. Ermenegildo Zegna, for example, has launched its Zegna Sports gym kit series last fall. BMW Lifestyle, the complimentary product line to PORTS, offers mainly sporty and casual apparel items. Dunhill also has its Traveling and Recreation Series to meet the market demand.

# IV. Challenges

## 1. Investment phase can be long for lesser-known brands

Although China offers lucrative opportunities, not all the luxury brands can find gold immediately. While big-name designer labels such as Louis Vuitton and Gucci have reported tremendous success in the country, many other lesser-known luxury brands have struggled to find profit. The Boston Consulting Group estimated early last year that only one in ten luxury players in China were profitable. Morgan Stanley also suggested that it would take at least five years for most foreign luxury houses to break even in China. As mainland luxury consumers tend to look for obvious wealth symbols, we expect big-name designer brands will continue to receive strong favor.

## 2. Securing prime sites are more difficult as competition intensifies

Competition for prime retail locations is getting fierce as more and more luxury retailers embark on aggressive expansion and store enlargement plans. According to Jones Lang LaSalle, luxury retailers such as Louis Vuitton, Gucci and Fendi are competing hard for super-sized retail space in Shanghai in order to maximize visibility and offer more product lines within a single store. This undoubtedly has led to higher retail rentals for prime shopping malls. Unlike the super brands which often receive more favorable terms from landlords, many lesser-known luxury brands are now facing more frequent lease terms reviews and even relocation in mature sites as super brands take up prime spaces. Many high-end department stores are also asking for higher commissions as luxury brands chase for counter space.

## 3. Counterfeits and trademark infringement hurt retailers

Many luxury players have complained about the prevalent counterfeit problem in China. According to a report by the US Embassy in Beijing in 2004, China has one of the highest piracy rates in the world and it estimated that on average, 20% of consumer products in China are counterfeits. The multi-billion luxury industry is particularly appealing to counterfeiters. Indeed, the US authorities have in January announced one of the biggest counterfeit luxury goods operations in US history, discovering fake Chinese imports with brand names Gucci, Burberry, Louis Vuitton and Coach, worth about $100 million had they been real. Marketers are worried that counterfeits would contribute to huge revenue loss and brand devaluation.

Fortunately, the Chinese government has stepped up its efforts to clamp down counterfeiting in recent years. In 2006, the Chinese court ordered a shopping center operator, the Xiushui Haosen Clothing Company (the landlord of Beijing Xiushui Street), to compensate international brand owners for the pirated goods sold in its premises. It is hoped that the landmark ruling would curtail the sale of counterfeits. It also shows that foreign investors can now make use of legal channels to fight against counterfeits more effectively.

On the other hand, trademark infringement is another headache for retailers. China has a first-to-file trademark registration system — whatever party first registers a trademark has the right to use it, whether or not that party originated the trademark. Recognizing the value of the world-renowned brands, some unscrupulous persons have purposefully registered the trademarks in the country beforehand, hoping to negotiate with foreign brand owners for benefits. The pending case of a Wuhan businessman successfully registered the LOUYIVEITEN (the Chinese pronunciation of Louis Vuitton) trademark and logo on the mainland in 2003 is a case in point. The man has threatened to produce his own LOUYIVEITEN products and accessories if the LVMH Group does not give him exclusive franchise rights in the city.

## 4. Pseudo luxury brands mislead consumers

The huge potential of luxury businesses in China has attracted a number of so-called pseudo luxury brands. Some domestic players have presented themselves as foreign luxury brands by adopting foreign images, say having “Italian” or “French” brand names and using foreign models, in order to lure the unsophisticated Chinese consumers. This does pose challenges for luxury players, as some consumers do not know how to differentiate between real and pseudo luxury brands. However, as growingly affluent Chinese consumers now travel abroad more, it is expected that consumers will become more knowledgeable and abandon these brands eventually. Furthermore, more vigorous tenant and concessionaire selection by shopping malls and department stores would also force these brands to move out upscale retail locations in China.

## 5. Lack of management talent affects retailers’ expansion in China

The lack of management talent can possibly slow down the luxury retailers’ expansion in China. In top-tier cities where it is easier to hire well-trained personnel, staff turnover is increasingly serious as companies expand and compete for talent. In fact, China’s staff turnover rate is today the highest in Asia. Furthermore, there is also a clear shortage of sales and service personnel in luxury sector in some lower-tier cities. Luxury apparel retailers need to work their best to attract, train and retain talent.

## 6. Pressures to improve on supply chain responsiveness increase

This actually applies to luxury retailers worldwide. The increasingly competitive fashion industry is today changing at great speed. The emergence of fast fashion retailers like Zara and H&M is offering consumers with cheap-chic alternatives. Of course it is reasonable for top designer labels to have longer time-to-market, consumers will definitely appreciate shorter lead time. Adopting a hybrid model — launching new flash collections hand-in-hand with the traditional ones — may be a viable option. And given that effects of the changes in weather conditions are more profound these days, efficient supply chain models shall also help retailers manage their risks.

# V. Concluding remarks

Despite all the exciting growth opportunities, the luxury sector in China is still in an early phase of development. For luxury apparel retailers wishing to get the cream of the cake, here are a few things to bear in mind:

First of all, China is not a place for quick profit, especially for lesser-known luxury brands. Luxury retailers shall be prepared that their investment phase in China may take at least five to ten years. And given the male-driven nature of luxury businesses in the country, we believe male-oriented brands will have a higher chance of success.

To fully tap the market potential, luxury apparel retailers shall understand the psychology of Chinese consumers and meet their aspirations to be recognized. Designs that address the needs to show off shall continue to receive much more favor for some time. Luxury retailers can also consider launching different accessories items or complimentary lines with less heavy price tags to target the growingly influential mass affluent class. Nonetheless, it is prudent for players to pay long-terms efforts to educate Chinese consumers and cultivate a culture for luxury appreciation.

In the long run, luxury apparel retailers shall also consider mobilizing more resources to formulate real estate strategies and build long-term relationship with shopping malls developers and department store operators. This definitely helps them securing retail spaces, which are becoming increasingly scarce in China.

One final advice for luxury retailers that have not come to China and consider setting foot in: register your trademark early and often. Solving trademark disputes can be difficult and costly in China.

China is a market that deserves long-term commitment. We believe it is a promising land for luxury apparel retailers in the world.