WWD

FASHION

Luxury Goods Growth Seen Slowing for Next Decade

● Boston Consulting Group predicts that over the next 10 years global sales of luxury goods will grow by single digits, around 4 percent a year, compared with an average of 9 percent over the previous decade.

BY GORDON SORLINI

MILAN — The luxury slowdown is set to continue for years ahead.

That's the forecast from Boston Consulting Group, which predicts that over the next 10 years global sales of luxury goods will grow by single digits, around 4 percent a year, compared with an average of 9 percent over the previous decade, as Asian consumers rein in spending. Antonio Achille, partner and managing director at BCG, also said sales quality will be different: previously growth came in tandem with store openings, while in the future, Achille said, growth will be like-for-like, in stores opened for at least one year. Brands will focus more on "working intimately with the consumer and improving conversion rates" — in other words, turning more window shoppers into paying customers.

"Hermès is going to open only one store next year, and it will be in Asia," he said.

But organic sales growth poses challenges; for example, the rising costs of rents in particularly popular cities, like New York, Paris, London and Milan, Achille pointed out at the "7th Luxury Summit: Il Vero Lusso È Il Made In Italy" ("Real Luxury Is Made in Italy"), a conference organized Wednesday by Il Sole 24 Ore.

Achille also explained that for Italian luxury goods makers to continue to "win" consumers in the future they must focus on "made in Italy" authenticity and create "emotional connections" with their customers so that they can turn into brand ambassadors, generating positive buzz through word of mouth.

Authenticity is, and will remain, a key driver of many Italian luxury goods makers' sales, but other traits are just as important. Michele Norsa, chief executive officer of Ferragamo SpA, said that reading the market — not just in terms of understanding consumers, but in macroeconomic and geopolitical terms as well — is also fundamental. "The ability of companies to react rapidly to — or anticipate — changes where their consumers are is one of the winning characteristics of this moment," he said.

Challenges are numerous: traffic in stores isn't increasing, retail costs are growing and there are wage pressures in emerging market economies.

Norsa explained that flat store traffic doesn't mean sales are flat; in fact, he said that stores get more actual buyers because they enter Ferragamo shops already determined to buy what they saw online. Also, motion detector technology has improved. "If once a lady entering a store with her dog would have counted as two people," Norsa said, "now that doesn't happen anymore."

The ceo is also a true believer in travel retail, for it gives the brand visibility. "Being a globally visible brand increases its desirability and value to consumers, it makes it friendlier: being known is similar to being friends," said Norsa.

Gian Giacomo Ferraris, ceo of Gianni Versace SpA, said that after the restructuring the company went through when he arrived at the helm in 2009, the group's success has been based on its strategy of "emphasizing our distinctive traits." He added: "The Versace brand has a creative voice, a genius, which was Gianni and with his death this was lost a little... We found the strategy of emphasizing our distinctive signs and this is driving growth."

Ferraris said that "from the first day, the company's obsession has been to appeal to younger consumers" and a strong digital presence is key to that. The market seems to be responding positively: Ferraris said that over the past five years sales have grown at about 16 to 18 percent a year and today the company's earnings before interest, taxes, depreciation and amortization is about 13 percent of sales. Ferraris said he thinks the company — which had 2014 sales of 550 million euros, or $620 million at current exchange rates, "is a brand which has to have the potential to reach 1 billion euros, or $1.1 billion." A good part of this growth will come from new stores. Versace currently operates 120 locations. The need for cash to accelerate the group's retail expansion — with stores opening in Japan, South Korea and Mexico — was the driving force behind the firm selling a minority stake to Blackstone last year.

By 2017, Ferraris said he sees Versace reaching sales of around 800 million euros, or $903 million, in revenues and a stock market listing could take place in 2018.

While size and scale certainly matter, family-owned Kiton feels secure in its high-end tailoring business model, with growth in the high single-digit range (8 to 9 percent in 2015), the firm's ceo Antonio De Matteis said.

He pointed to the company's investments in human capital — it has an internal tailoring school — as a key to its success. "To grow we need to train a new generation of tailors," De Matteis said, adding that the average age of tailors around the world is 65 to 70 years old. "In Kiton, thanks to our school, the average age is 35 years. This gives us a sense of tranquility, for we know what our children — who are already in the company — have at least another 20 years of tailoring skills available in the company."

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> — Luca Solca, Exane BNP Paribas

Investing in human capital isn't cheap: De Matteis said that the cost per employee of the company averages about 40,000 euros, or $45,000 at current exchange, a year, as compared to some 27,000 euros, or $30,000, a year at other luxury-goods makers. While the company manages to make about 20,000 jackets a year (around 85 a day), the executive said that with tailored products "you can't grow exponentially."

Kiton, known for its men's wear, is successfully — if slowly — breaking also into women's wear. De Matteis said this is becoming an important part of the business and now represents around 10 percent of revenues, growing 25 to 30 percent annually.

Accelerating in women's wear is also a strategy being followed by Santoni, the high-end shoemaker's ceo Giuseppe Santoni, said. "Already 30 percent of our sales are to women, but the potential is much higher," he said, pointing out that while male customers are extremely faithful to the brand, women's is opening "interesting scenarios."

Like Kiton, the company offers a tailor-made service for its top customers, with three shoemakers dedicated to serving some 200 Santoni clients around the world. (The company is also a supplier of leather straps to Swiss watchmaker IWC.)

For high-end women's wear maker Ermanno Scervino, growth will continue to come through a focus on product sophistication and retail expansion. Toni Scervino, the firm's ceo, said Scervino has always believed in "made in Italy out of vanity: we liked only that which was made in Italy. We are based in Florence for the beauty of the place but also because in Tuscany there are artisanal skills and a tradition of women's tailoring, which is talked little about because in Italy you talk mostly about men's tailoring."

The company is investing in building up its retail network, including debuting in the U.S. with a store in Miami's Bal Harbour mall.

While the focus at the conference was on the highest end of the luxury pyramid, Luca Solca, head of luxury goods at Exane BNP Paribas, offered a different view of exclusivity. Pointing out that investors — not consumers — in luxury want growth, he said: "In the industry there is a conviction that the higher you are the better. In reality, to be successful you have to have a large business. I tell clients, 'Don't buy exclusive companies, buy big companies that create the perception in consumers of being exclusive'. You have to combine exclusive image with large dimensions, for this is a world where fixed costs — be it labor, distribution — are very high. Many people think Chanel and Hermès are exclusive. But then look at the facts and you see that both sell many accessibly priced products."

Solca also said that firms are going to have to learn to be much better at managing themselves, especially now that China — a top driver of luxe sales in recent years — is slowing. "Over the past 10 years, if you remove the contribution of Chinese luxury buyers — both in China and abroad — the market has grown by 2 to 3 percent annually. Since we are entering a moment when sales in China are slowing — in part because brands have limited capacity to open new stores, in part because consumers are spending less — errors are easier to spot and so you have to make less mistakes."

BUSINESS

Jobless Teens Seen as Key Challenge in Mideast

● A Chalhoub Group study warns dependency on oil is another threat to the Gulf's retail market.

BY RITU UPADHYAY

DUBAI — Can a retail market driven by abundant consumption — and a "build it they shall come" mantra — last for generations? Not unless the Persian Gulf addresses two key challenges: dependency on oil and youth unemployment, according to a report from Chalhoub Group, one of the Middle East's largest luxury retail conglomerates.

The Gulf economies are still largely reliant on exports of oil and gas, which account for more than 33 percent of the gross domestic product and 84 percent of government revenue across the Gulf Cooperation Council. Those earnings give the region some of the highest GDPs in the world, but it also has a very high youth unemployment rate, with numbers approaching 30 percent in Saudi Arabia.

Those are the questions posed in a new white paper from family-owned Chalhoub, entitled "Luxury in the Gulf: A Sustainable Future?"

"We believe in this region and its potential and we want to make sure that our group is still here in the next 60 years," said Anthony Chalhoub, co-chief executive officer of the Chalhoub Group, which marks its 60th anniversary this year.

With rapid growth comes inevitable environmental impact. The United Arab Emirates has one of the highest ecological footprints per capita in the world, according to the World Wide Fund for Nature — and this is not going unnoticed.

The region is home to several large-scale sustainability projects. Alongside China and South Korea, two of the largest "eco-city" projects can be found in the United Arab Emirates: Masdar City in Abu Dhabi and Desert Rose in Dubai. According to the report, "these cities are master plans of a new vision of social and environmental harmony, which will reshape social principles of living."

Creating a culture of sustainability has become a priority for luxury consumers in the region. Emirati teens are spending six times more on average than global teens, according to research by AMRB and TRU.

Research done by Chalhoub Group shows the affluent GCC consumer spends on average $2,400 per month on beauty, fashion and gifts. They also have high expectations of the brands when it comes to corporate social responsibility, with 83 percent of respondents saying they expect the shops they buy from to engage in environmentally friendly activities. Yet 68 of consumers feel brands do not care enough about the environment and the community.

It is rare to find a Gulf national working in retail, dominated by foreigners on work visas. Yet the luxury sector could offer a major outlet for the region's youth, if they can be prepared to enter the job market, the report suggests.

"We have adopted education as a key channel to facilitate the development process, believing that it is the first and foundational step in understanding how to address today's social and environmental challenges in the region," said Patrick Chalhoub, also co-ceo of Chalhoub Group.

The report calls for more educational opportunities for potential employees and insists corporate entities should be held as accountable as governments for creating sustainable employment solutions. Such programs already exist in many sectors from telecom to hospitality in the GCC.

The Chalhoub Group has an Emirati and Saudi graduate program, which offers an accelerated retail learning experience by rotating fresh university graduates through different roles and business activities in the company. The company says it plans to increase recruitment for its Emirati graduate program.

Chalhoub held out hope the report highlights the challenges facing the fast-developing region. "Our sustainable engagement strategy was created to raise awareness, and we believe that by combining our individual efforts, we will be able to contribute to the region's sustainable future," added Patrick Chalhoub.