Business of Luxury

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Strategic industry comes of age

Culture and craftsmanship have become tools to promote a business that is now acknowledged in its own right, writes *Scheherazade Daneshkhu*

At an exhibition in Paris dedicated to French *savoir-faire* in May, Frédéric Lefebvre who runs the family firm Rennotte Riot, displayed the brass mouldings, handles and decorative elements in which the bronze restorer specialises.

Based in southern Paris, this employer of 13 people that was founded in the 1880s has worked on the palace of Versailles, France's constitutional council and, more recently, on a Russian multimillionaire's aircraft. "He wanted it in the French style, so we made small bronze lion heads for the interior," Mr Lefebvre explained.

The work demands technical skills, the supply of which is dwindling. "Our work is very specialist and needs a lot of training. It's hard for me to find artisans with the right skills," he said.

Elisabeth Ponsolle des Portes, head of the Comité Colbert, the French luxury goods association, says more has to be done to encourage youngsters to pursue a career as a luxury artisan.

The association's own work with schools has revealed that students are often unaware of luxury trades, such as a fragrance "nose" or a trunk-maker, but are curious to hear more.

"The subject of training is a challenge because *savoir-faire* and quality are essential to production," she says over tea served in green and white-striped Bernardaud porcelain in her office, a stone's throw from the presidential Elysée palace. She is battling for the creation of a European register of *savoir-faire* and designated titles for master artisans. This would be similar to Japan's living national treasures list, which aims to showcase intangible cultural assets.

The debate is about more than a desire to preserve a way of manufacturing. Culture and craftsmanship have become tools in luxury's efforts to promote itself as a strategic industry able to trade on "made in Europe" labels.

Years of lobbying yielded a big breakthrough in September, when the European Commission acknowledged luxury as a sector in its own right, instead of part of another industry such as textiles, cars or leather goods.

This is described as "our first public achievement" by Armando Branchini, president of the European Cultural and Creative Industries Alliance (ECCIA), a lobby group.

For the first time, the EU's executive body had "recognised . . . the high-end industry as the pillar of cultural and creative industries", said Mr Branchini, who is also head of Altagamma, Italy's luxury goods association which created the ECCIA in 2010, together with France's Comité Colbert, the UK's luxury body Walpole, Meisterkreis in Germany and Spain's Circulo Fortuny.

In Europe, the ECCIA was pushing at an open door. In the same year, Italian politician Antonio Tajani became the European Union's commissioner for industry, and he actively solicited the sector's views.

The traditional view of luxury and fashion as an adjunct to other industries and not a real manufacturing sector "seemed absurd", said Mr Tajani, speaking to the Financial Times this year. "Fashion and tourism are two key sectors for Europe's economy; they are part of the solution to the continent's growth agenda."

Buoyed by strong demand from China in particular, Europe's luxury goods industry has grown by double digits in the last two years, while the eurozone economy has stagnated.

Luxury accounted for 3 per cent of Europe's economic output in 2010 and

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Presidential couple seeks to inspire mood of sobriety

Shopping While frugality may be the official line, Chinese tourists tend to leave such notions at home, reports *James Kynge*

From the moment Xi Jinping's aircraft touched down in Moscow in March, it was clear that the world of Chinese luxury would be sent into flux. The plane's door opened to reveal President Xi linking arms with his wife, Peng Liyuan, a famous singer, dressed in a designer navy blue overcoat with matching handbag and a light turquoise silk scarf.

Within seconds, China's tumultuous social media was in thrall. All elements of her couture – both in Moscow and later in Tanzania where she wore pearl earrings and a light Chanel-style suit with matching handbag – were scrutinised, with millions clamouring to know which brands Ms Peng had chosen. As the answers emerged, it became clear that Ms Peng had made more than just a fashion statement – she had personified Beijing's preferred vision for luxury in China.

The first lady's fashion choices were for more affordable, logo-free domestic brands, marking a sharp contrast with the prevalent Chinese taste for foreign, sometimes flashy, luxury items with famous brand names prominently displayed.

Such an attitude is intimately aligned with some of the key messages in a national campaign, launched by President Xi late last year, to promote frugal tastes and smash the scourge of official corruption.

While it may be some time before the dominance of foreign brand luxury in China diminishes, the combination of Ms Peng's allure – which some liken to the "Kate Middleton effect" – and the purposefulness of Mr Xi's campaigns are already having an impact.

Three important changes are under way: some nascent domestic brands are starting to win a wider following, domestic luxury spending is turning more furtive and the buying of luxury goods overseas by Chinese outbound travellers is booming.

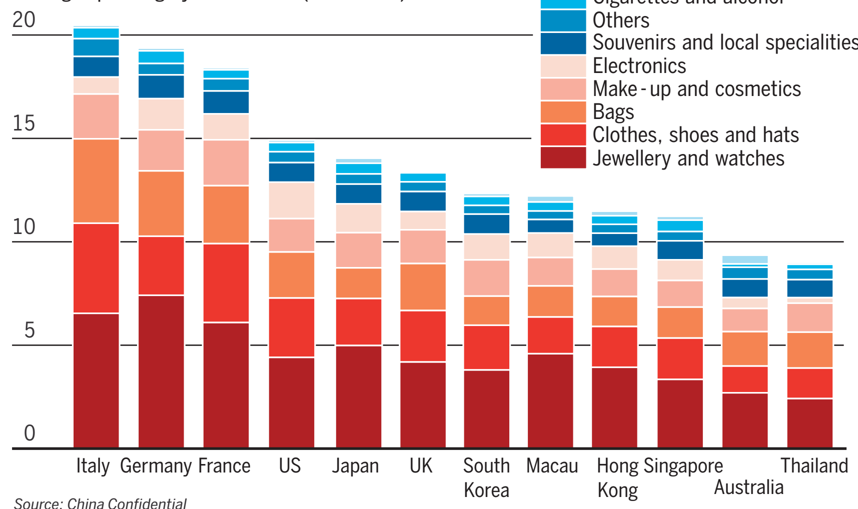
One of the brands Ms Peng chose was Exception de Mixmind, which was so swamped with interest as a result that its website crashed. Ma Ke, chief designer at Exception, has a simple philosophy that chimes perfectly with the new official zeitgeist. "Today's fashion is no longer about fancy appearances that follow trends," she was quoted by China Pictorial, an official magazine, as saying. "Instead, being fashionable should mean pursuing a return to the ordinary. Real luxury lies in the spirit a garment conveys, not a high price."

Other homegrown brands gaining a profile include Shang Xia, touted as China's answer to Hermès, led by Jiang Qionger, the daughter of Chinese architect Dong Dayou, who designed the Shanghai museum. The label was acquired by Hermès in 2010 and is planning to open a first international flagship store in Paris later this year. Qeelin is a jewellery label bought by the French group PPR (which is about to change its name to Kering) in December and is best known for combining Chinese cultural motifs such as pandas, goldfish and gourds with the French craftsmanship of its co-founder Guillaume Brochard. Xander Zhou, sometimes billed as the Chinese equivalent of Yves Saint Laurent, was launched in 2007 and trades quirky variations of familiar garments, such as shoulder cut-outs on coats or jumpers.

Chinese president Xi Jinping and his wife Peng Liyuan arrive in Moscow Getty

How much did you spend on the following items on your most recent overseas trip?

Average spending by destination (Rmb '000)



Source: China Confidential

So far, the inroads made by such brands are marginal. The animating energies of the Chinese luxury market are not to be found within China at all but in a collection of overseas cities that last year attracted about 83m outbound Chinese travellers.

The World Luxury Association (WLA) estimates that of the $50bn spent by Chinese on luxury last year, some 60 per cent was overseas. In the month to February 20 (covering the Chinese New Year period), the divergent trends are striking. While an estimated $8.5bn was spent overseas, up 18 per cent from the same period in 2012, only $830m was spent domestically, down 53 per cent from a year earlier.

According to a survey of some 1,200 Chinese outbound travellers conducted by China Confidential, a research service at the Financial Times, Chinese tourists tend to leave frugality at passport control. The wealthiest 26 per cent of outbound tourists spent an average of Rmb32,628 ($5,241) on their most recent overseas trip, with shopping accounting for almost half the total (Rmb15,699). The survey was conducted in January as President Xi's frugality campaign got under way.

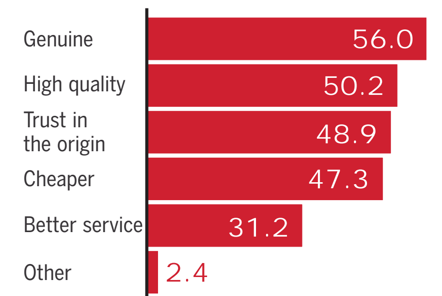
With luxury goods overseas often costing 45 per cent less than identical items at home, price is an important motivator behind the alacrity of Chinese to pick up bags in Milan, perfume in Paris, coats in London, watches in Geneva and an array of duty free products in international airports. Such sprees are often minutely planned before Chinese leave home with a long list of items that they have pledged to buy for friends, family and colleagues.

Price is not the only factor. A sense that luxury goods bought overseas are likely to be more genuine, safe and high-quality than those on sale in China ranked high among reasons for overseas shopping among respondents to the China Confidential survey.

James Kynge is principal at ftchinaconfidential.com

Reasons for buying goods overseas

Per cent



Source: China Confidential

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Anti-corruption drive makes foreign executives take note

Fight against graft

All campaigns have a finite lease although this one may last, says *James Kynge*

There is no doubt that China's campaigns to promote frugality and smash corruption are hitting sales of luxury items from watches to clothes, cars, apartments and even to private jets. What is less clear is whether the twin campaigns are likely to soften or intensify, change focus or just be quietly dropped.

The past teaches that all campaigns in China have a finite lease. The "spiritual pollution" movement of the early 1980s, the crusade against "bourgeois liberalisation" in the aftermath of the 1989 Tiananmen crackdown, the cause to promote the thought of the "Three Represents" a decade ago and several others have all served their time before falling by the wayside.

But those hoping for a swift conclusion to the current campaigns against corruption and gluttony may be disappointed. The drive to rein in official excess carries several hallmarks of real determination at the highest levels of government, suggesting that Xi Jinping, who was selected as Communist party boss last November, sees the fight against corruption as one of the defining aims of his administration.

The first of these hallmarks came in the days after Mr Xi's elevation to party boss. The man given the anti-crime portfolio in the new politburo standing committee was Wang Qishan, a former deputy premier with a strong track record for getting things done in an uncompromising manner.

The second sign of high-level resolve was the speed at which the campaign was scaled up. Already, well-publicised disciplinary action has been taken against officials caught feasting at the expense of the public purse, buying multiple high-end properties, giving expensive "gifts" to win favour, wearing luxury watches, driving premium brand cars and engaging in corrupt practises.

In addition to this hunting down of "flies as well as tigers" – as Mr Xi put it – key structural changes are under way, most notably in curbing local government abuse of the bond market and managing aspects of the shadow financial system.

Perhaps the most important indicator of the potential longevity of Mr Xi's campaign is that the public overwhelmingly supports it, thus far at least. Users of Weibo, China's version of twitter, have leapt into action, posting photographs of officials gorging themselves on fine wine at sumptuous banquets, or driving luxury cars with military number plates, wearing ostentatious luxury items and pursuing debauched lifestyles.

All this is having a sizeable impact on the sales of premium products and services. First-class airline ticket sales have eased by a tenth in recent months, the prices of Maotai, a fiery tipple favoured at banquets, have been sliding as sales plummet and, according to Shen Danyang, spokesman for the ministry of commerce, sharks' fin soup sales have dropped 70 per cent this year while edible swallow's nests, another delicacy, have dropped 40 per cent.

Luxury watchmakers, some of which have expanded rapidly in China in recent years, have seen the market soften this year, particularly at the premium end.

"All watches costing more than 1,800 francs are having difficulties in China at the moment," said Jean-Christophe Babin, when still the TAG Heuer chief executive before moving to Bulgari (see page 3). Mid-range brands appear to be more upbeat, with buying by Chinese outbound travellers in particular compensating to some extent for the drop-off in sales domestically.

> Social media users have posted photos of officials drinking fine wine or driving luxury cars

In the other areas – such as cars – foreign brands are subject to official treatment that suggests domestic rivals may stand to benefit. The ministry of industry and information technology, for instance, has published a list of 400 types of car suitable for official use. Unsurprisingly, the list is dominated by domestic and joint-venture brands. It contains glaring omissions such as Audi, Volkswagen and Toyota, the hitherto favourite choices for self-regarding officials.

Sales growth for luxury vehicles, dominated by German brands Audi, BMW and Mercedes-Benz, slowed to 4 per cent in the first quarter of this year, far below the 13 per cent annual growth in the passenger car market, according to China's association of automobile manufacturers.

BMW says it expects the slowdown to continue this year, with growth reaching high single digits – compared with 40 per cent last year – and a total of 326,000 vehicles. Daimler, owner of the Mercedes-Benz brand, is somewhat more upbeat. It still plans to add 75 dealerships in China this year to the current 262, says Hubertus Troska, Daimler's board member responsible for China.

Chinese brands meanwhile are making some inroads, mainly from government offices. In signs the frugality campaign may spell further gloom for luxury car sales, the official People's Daily newspaper recently suggested that a luxury tax would benefit society and that a tax on luxury cars, in particular, was a "reasonable" idea.

Actor Huang Xiaoming attends Mercedes-Benz China fashion week opening Getty

Top executives play game of musical chairs

Economic slowdown has led to hirings and firings as owners seek innovative yet experienced leaders, reports *Elizabeth Paton*

The stagnating eurozone, a global tourism slowdown plus a crackdown in China on ostentatious gift-giving have all taken their toll on sales and profits for many of the world's biggest luxury brands.

This has led to a stream of hirings and firings, as companies search for innovative yet experienced leaders who can conquer emerging markets, size up growth opportunities and navigate the merry-go-round of the mergers and acquisitions world.

Here are some of the industry's high-profile managerial and creative appointments of the past year.

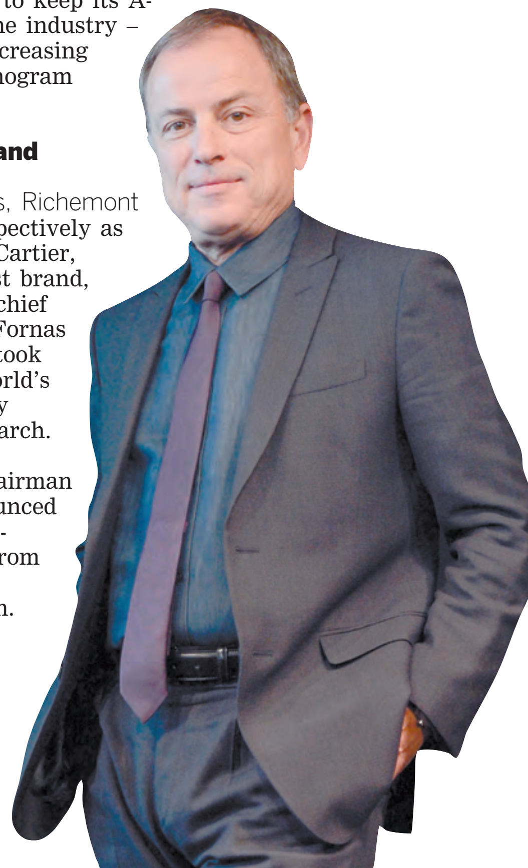
Jean-Christophe Babin
Chief executive, Bulgari
This charismatic former Procter & Gamble executive spent 12 years running TAG Heuer until his move within the LVMH stable to Bulgari in February. Widely credited as the force behind an impressive reversal of fortunes at the Swiss watch brand, the 51-year-old stepped in at the Italian jewellery house to replace Michael Burke (see profile below). Mr Babin is expected to raise the global profile of the business – but he will be keen to avoid another scandal like the one encountered in March, when Italian police seized €46m worth of Bulgari assets, including the jeweller's flagship Roman store, in a probe of alleged tax evasion prior to its €3.7bn acquisition by LVMH in 2011.

Anna Wintour
Artistic director, Condé Nast
Condé Nast's most high-profile employee (pictured right) cemented her position as jewel in the managerial crown at the US publishing house with this March appointment. The editor-in-chief of *American Vogue* – at one stage touted as President Barack Obama's next UK ambassador thanks to her political fundraising talents – will now oversee creative and personnel development across all publications. The new position reflects recognition of how valuable Ms Wintour is to the company – and the efforts it will make to retain her. But the fact her experience lies predominantly in print – not digital – has led some elsewhere to question the move.

David Chu
Chief executive, Georg Jensen
This Taiwanese-US design guru is best known as the founder of Nautica, the US lifestyle brand he sold for $1bn to the VF Corporation in 2003. Mr Chu was initially appointed chief creative officer of Georg Jensen, the Danish luxury label, following its acquisition by Middle Eastern investment house Investcorp in November 2012. In March, he became chief executive and is expected to spearhead growth through expansion in Asia.

Pierre Denis
Chief executive, Jimmy Choo
The go-to shoe brand for Hollywood starlets, socialites and businesswomen alike has had a torrid time of late. After the abrupt departure of both founder Tamara Mellon and chief executive Joshua Schulman, the former boss of John Galliano arrived in July to oversee a transition from an A-list accessories choice to lifestyle powerhouse. New owner Labelux – the privately owned holding company controlled by Joh. A Benckiser – will be wanting results. A diversification into areas such as fragrance and eyewear is presumably intended to act as a stepping stone for younger consumers to buy more expensive leather goods.

Michael Burke
Chief executive and chairman, Louis Vuitton
This 27-year LVMH veteran (pictured below) had stints of increasing seniority at Christian Dior, Fendi, and Bulgari before unexpectedly stepping in to lead Louis Vuitton in December after his predecessor Jordi Constans retired due to ill health. The French-born Mr Burke understands LVMH inside out, having worked with chairman Bernard Arnault since before the group was created. The brand faces slowing sales in core Asian and European markets and is putting the brakes on global expansion, shifting focus to its leather goods sector. The brand, which analysts estimate makes up to 70 per cent of all €7bn sales for LVMH's fashion and leather division, needs to retain exclusivity and craftsmanship to keep its A-lister position in the industry – tricky given the increasing ubiquity of its monogram logo.



Bernard Fornas and Richard Lepeu
Co-chief executives, Richemont
Stepping down respectively as chief executive of Cartier, Richemont's biggest brand, and group deputy chief executive, Messrs Fornas and Lepeu jointly took the helm at the world's third largest luxury conglomerate in March. Two months later, Johann Rupert, chairman and founder, announced he would take a 12-month sabbatical from September while promising to return.

Björn Gulden
Chief executive, Puma
The former professional football player was poached from Danish jeweller Pandora in April to run Puma, Kering's core sports-lifestyle brand. Kering, currently in the process of changing its name from PPR, seeks to reposition itself as a luxury and lifestyle group, areas where it sees the strongest growth. Mr Gulden will have his work cut out when he assumes his position in July. A turnround in fortunes is required at the German sportswear maker which has seen plummeting sales and a drop in net income of a third so far in 2013.

> Candidates must be able to conquer emerging markets, and navigate mergers and acquisitions

Stéphane Linder
Chief executive, TAG Heuer
This Swiss national was appointed to manage one of the brightest stars in the LVMH constellation in May after more than two decades at the brand. The one-time head of R&D has experience firmly rooted in product. He introduced both the sunglasses and *haute horlogerie* ranges to the TAG Heuer portfolio. Most recently head of the North America division, Mr Linder will focus on developing the womenswear collection, entering emerging markets beyond China and consolidating in-house manufacturing capacity with the aim of increasing self-sufficiency.

Alexander Wang
Creative director, Balenciaga
After Nicolas Ghesquière's 15-year tenure ended abruptly last November, parent company Kering spent just six weeks searching for a successor. Step forward the 29-year-old princeling of New York downtown cool (pictured right) who pioneered off-duty sports luxe with the eponymous label he launched in 2007 after dropping out from Parson's art college. Now overseeing 32 collections a year between the two brands, Mr Wang's monochromatic, highly structured first offering for the French design house in February was met with approval from those gathered on the front row. It is still unclear as to whether his sharp deviation from Balenciaga's rigorous *haute mode* heritage can translate into increased sales.

Brendan Mullane
Creative director, Brioni
The former Givenchy menswear designer was appointed a year ago, six months after Kering bought the iconic Italian brand in a bid to gain a better foothold in Asia's booming menswear market.

Stefano Pilati
Head of design, Ermenegildo Zegna
After failure to renew his Yves Saint Laurent contract made way for *enfant terrible* Hedi Slimane, the highly capable Mr Pilati arrived at Zegna in January. The brand is enjoying success in China and has begun expanding in sub-Saharan Africa (see article on page 6).

Alasdhair Willis
Creative director, Hunter
The dashing entrepreneur and husband of designer Stella McCartney took the creative helm of the British manufacturer best known for its Wellington boot in February, as it expands rapidly under controlling shareholder Searchlight Capital Partners.

Alessandra Facchinetti,
Creative director, Tod's
With high-profile if shortlived stints at Gucci and Valentino, Ms Facchinetti appears equipped to take on operations at the Italian accessories company.

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Stock markets compete with buyouts

Listings Share offerings are more attractive to strong managers, says *Rachel Sanderson*

When Milanese jeweller Pomellato wanted to raise funds to expand into Asia, its first choice was a listing on the Milan stock exchange. In April, though, it opted for a buyout from French global luxury goods group PPR, soon to be renamed Kering.

The decision by Pino Rabolini, Pomellato's founder, to sell his business to the French instead of selling shares on the bourse, underlines a dynamic animating the luxury goods industry. Amid rapid consolidation and fierce competition to acquire independent luxury brands, the world's stock exchanges must fight to gain attention.

"Stock exchanges are actually competing with Kering and LVMH," says Claudia D'Arpizio, head of the luxury goods practice of Bain, the consultancy.

Luxury goods companies have been among the most successful listings of the past three years. Michael Kors launched US fashion's biggest ever initial public offering (IPO) in 2011. Prada, which listed in the same year, has become a star attraction of the Hong Kong exchange. Shares in cobbler-to-the-stars Salvatore Ferragamo and cashmere casual wear label Brunello Cucinelli more than doubled in value in the past year on Milan's exchange.

Bankers say they expect a healthy IPO pipeline this year. US sportswear brand Vince is looking at an autumn offering, according to Reuters. In Italy, lingerie-to-accessories group Carpisa Yamamay and sportswear brand Moncler will consider a listing this year, say executives.

Meanwhile, bankers say several prominent unnamed European and US brands look to follow the example of New York-listed Coach. This year it is making a secondary listing in Hong Kong to boost its profile among Chinese investors and consumers.

Luca Peyrano, head of continental Europe, primary markets for the London Stock Exchange Group, says in Italy, the richest territory for independent luxury brands with potential to expand internationally, there is no shortage of companies suitable for a debut on the bourse.

An annual study by consultants Pambianco in association with the Milan stock exchange identifies 100 Italian luxury, fashion and designs firms ready to list on the bourse, including Dolce & Gabbana, Armani, Ermenegildo Zegna, Calzedonia, Yamamay, Twin-Set, MaxMara, Only the Brave, Loro Piana, Missoni and Moncler.

Mr Peyrano says the LSE Group, which runs the exchanges in London and Milan, is in "close discussions" with five or six of them.

Nonetheless, the conversion rate for IPOs remains low compared with the number of luxury goods firms changing hands, according to bankers. This is not least because industry leaders, private equity funds and new investors from emerging markets are also in the chase giving the owners of luxury brands plenty of options to get the best valuation.

Ms D'Arpizio says many entrepreneurs are keeping the door open to an IPO and another option – a "dual track" process – up until the last minute as they seek the best valuation, particularly amid volatile equity markets.

Moncler is a one-time IPO candidate that actually changed its mind. Management had pursued an IPO in Milan in 2011 but a day before the roadshow was due to start, the private equity owners, Carlyle, decided to sell their stake to Eurazeo, another private equity group, amid concerns about the value it would gain in a volatile market.

Bankers were also doubtful that Moncler's business – spanning luxury outerwear to lower priced apparel – would command the valuations of a pure luxury company. As a result, Eurazeo is considering listing Moncler in the autumn but may restrict the listing to the luxury brand and split off its lower-margin retail business in a bid to command a higher valuation.

The IPO route remains most attractive for those entrepreneurs with a strong leadership record and who do not need or want a big conglomerate like Kering or LVMH to provide managerial advice. The success of Miuccia Prada and Patrizio Bertelli, the wife and husband team behind Prada, has underlined its potential.

Bankers see Ermenegildo Zegna, a family-owned group with €1.3bn in sales in 2012, as a potential IPO candidate in this vein. Chief executive Gildo Zegna, however, repeatedly denies that he is interested in listing.

Claudia Parzani, a partner and co-head of the luxury goods practice at lawyers Linklaters who advised on the Ferragamo IPO, points out another advantage of taking the IPO route, especially in Italy. "Listing is a way to overcome the traditional Italian reluctance to [pursue] mergers," Ms Parzani says. "For a niche company wanting to expand, they can list in order to raise capital and then be in a position to take over rivals."

Ringing the bell: Michael Kors launches initial public offering Getty

> 'A niche company wanting to expand can list to raise capital and then take over rivals'

Private equity Deals follow shift in consumer spending

Six years after the height of private equity's interest in luxury fashion was marked by Permira's acquisition of Valentino Fashion Group, investment firms seek fresh opportunities in the high-end sector's more modestly priced competitors.

In the last six months, buyout groups have made a handful of deals in the so-called contemporary market, or companies that offer fashion-led but accessibly priced clothing, often manufactured offshore.

Here growth has been fuelled by a shift in spending preferences since the financial crisis.

Tory Burch, the womenswear brand, welcomed two investment firms at the start of the year to help with its expansion.

The fashion house, which sells totes to tunics, has built a loyal following with budget-conscious women in the nine years since its launch from Ms Burch's kitchen table.

Having already taken the US market by storm, the company is looking to open more stores in Europe, the Middle East and Asia.

General Atlantic and BDT Capital Partners, the new investors, say they will support the company's push abroad.

Patricia Hedley, managing director at General Atlantic, says: "In many cases, the real appeal of working with us is when a company has global aspirations."

Citing experience and expertise from prior investments in Asia, General Atlantic says it can give Tory Burch critical knowhow in areas such as supply chain management and marketing.

Other companies that have brought in private equity investors since November include New York lifestyle brand Rag & Bone, French ready-to-wear lines Sandro and Maje, upmarket denim maker True Religion and womenswear group J Brand.

Each is looking to its new partners to help with its growth, while offering the investors a potentially lucrative opportunity to profit from the sector's rise.

Aspirations: Patricia Hedley

Investment firms have eyed opportunities in the rapidly expanding contemporary market following the recent success of companies such as J Crew and Michael Kors, which raised $944m from an initial public offering in 2011 on the US market and recently did a secondary offering.

Fashion insiders say the contemporary market's growth has come as high-end, designer-luxury brands focus on their wealthiest customers with high-margin accessories, shoes, bags and fragrances.

This has created an opening for brands to fill the void for consumers, left behind by luxury brands, who still seek sleek apparel but do not want to spend as much for the styles.

The labels have also benefited from the rise of online shopping, where customers around the world can interact with the brands before shops are opened near them.

Andrew Rosen, chief executive of Theory and Helmut Lang at Fast Retailing, the fashion group behind rapidly expanding retailer Uniqlo, says creative designers working with brands must remain at the heart of an enterprise for it to stay successful after outside investors are brought in.

"These companies need more than just money. They need founders and visionaries that can build the business in an ever-changing marketplace. They need a good leader," Mr Rosen says.

Along with his role at Fast Retailing, Mr Rosen has invested heavily in the contemporary market with stakes in Rag & Bone, Alice + Olivia and Gryphon.

"At the end of the day, it is about the products and who is running them. The founders and visionaries of these companies are critically important," Mr Rosen adds.

"When you look at the Michael Kors story, the group that founded it is still there. The same is true at Tory Burch."

With private investors multiplying, the contemporary market has so far taken a different direction than the luxury sector, which is dominated by LVMH and PPR.

Fast Retailing is the closest thing to such a consortium as it owns J Brand and French womenswear company Comptoir des Cotonniers, in addition to the companies run by Mr Rosen.

As dozens of designers and labels vie to be the next success story in the contemporary market, investors can afford to be picky. "We look for . . . companies that are established with some history, where there is something unique . . . so that it's not a me-too product," says Sandra Horbach, managing director at Carlyle. The private equity group was said to have expressed interest in Sandro and Maje before buyout group KKR acquired a 65 per stake in a deal valuing the French labels at €650m, including net debt. "In the sector, the brand itself is really important," adds Ms Hedley. "The brand name, the fact that it is in the know and the fact that people have an affinity to it are all significant."

Arash Massoudi

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Consumers push big names to account for supply chains

Manufacturing

How products are created can make or break a brand, reports *Rachel Sanderson*

After successfully completing the listing of a third of his luxury business in Milan last year, Brunello Cucinelli, Italy's self-styled "King of Cashmere", paid each of his 700 employees a special bonus of €6,300.

The payout, mostly given to knitters and weavers based in his headquarters in a hill top hamlet in Umbria, was the latest example of what Mr Cucinelli calls his philosophy of "humanist capitalism".

The former chartered surveyor has built his business for 30 years on the idea of fostering traditional Italian artisanship and paying his workers above an above average wage. "Luxury consumers want to know, or will want to know, that their goods are made humanely," Mr Cucinelli maintains.

Where once Mr Cucinelli was in a minority that is no longer the case. As logos have gone out of fashion and industry surveys routinely find consumers unhappy with customer service in luxury goods stores, experts say the entire concept of luxury is now centred on artisanship. Manufacturing is king and can make – or break – a brand.

"The only source of luxury is who makes the product. This is luxury today," says Stefania Saviolo, a luxury goods industry expert at Milan's Bocconi university and head of its masters in fashion programme.

This shift in consumer taste can be clearly seen in the sales of luxury brands today.

The marques where sales are growing sharpest are those perceived by consumers to be based on artisanship and manufacturing excellence such as Hermès, Chanel, Bottega Veneta, Céline and Brunello Cucinelli.

At Hermès, sales rose 22 per cent in 2012 to €3.5bn outpacing a rise of about 10 per cent for the market at large. Operating profits at Bottega Veneta rose 47 per cent to €300m.

At Cucinelli sales rose 15 per cent in 2012. Shares in the company have doubled in value since it listed a year ago, making Mr Cucinelli, 59, a billionaire.

While the shift in taste away from logos and towards artisanship is in part a reaction to the financial crisis in the US and Europe bringing the curtain down on an era of "bling", analysts point out that the main reason is Chinese tastes.

"Most Chinese and Japanese luxury consumers still associate the Made in Europe label with superior quality but increasingly feel the prices need to be justified not just on the basis of 200 years of history but also the transparency of the supply chain," says Thomas Chauvet, head of European luxury goods research at Citi.

As Luca Solca, head of luxury research at Exane BNP Paribas, points out, "luxury goods are all about China". Chinese have become the largest consumers group by far with a quarter of the market. As a consequence, the industry is adapting to meet their demands.

The exception to the rule is Prada. The Milanese fashion house reported in its prospectus to its 2011 IPO that it made about 20 per cent of its collections – clothing to shoes to handbags – in China. It also uses manufacturing in Turkey and Romania.

That choice appears to have had no effect on its sales. These increased 29 per cent in 2012 driven by sales to Asian consumers at home and Chinese tourists shopping in Europe. Analysts have come to the conclusion that consumers desire to have Miuccia Prada's designs outweighs manufacturing bias towards Europe.

> 'Customers still associate Made in Europe with quality but feel prices must be justified'

By contrast, Gucci and Bottega Veneta, the star brands of the Kering group (the new name for PPR) put unrivalled emphasis on the ethics of their manufacturing process. They have an environmental profit and loss account in an attempt to show consumers the social and environmental impact of their supply chain.

It is an issue that most particularly pertains to Italy, where the majority of the world's luxury goods – from leather goods to textiles to ready-to-wear – are made. Italy's dominance in manufacturing luxury goods is in part because much of the traditional artisanship has been lost in France and the UK.

Bottega's woven *intrecciato infilato* bags are made in Vicenza, in north-eastern Italy. Here Bottega has invested in developing a manufacturing cluster, including a school, to preserve the artisan skills it needs to meet surging Chinese demand for styles such as its Cabat, with a starting price of €4,800 for a nappa leather version.

Marco Bizzarri, chief executive of Bottega Veneta, says "consumers are much more careful now about what they buy and they are going back to luxury roots, where the product is everything".

He adds: "This is not a marketing gimmick. Companies that are based around their product are the strongest ones now."

Mr Bizzarri says preserving Bottega's Made in Italy artisanship is key because many of its artisans are the sons of former artisans and "we cannot replicate this model abroad". But in such as Vicenza, he says, there is another advantage: "It is a small district, a small cluster. The flows of information are so quick that they create innovation. This would never happen if we were sending prototypes around the world."

At work: employee at a Brunello Cucinelli factory Bloomberg

Crises contained but challenges loom large

World Economy

Martin Wolf explores global growth scenarios with Gavyn Davies and Huw Pill, his partners on a panel at an FT conference today

Since 2007, the world economy has lain in the shadow of huge financial crises. Crisis engulfed the US, the UK and other western high-income economies in 2007 and 2008. From 2010, it engulfed the eurozone. Japan never fully recovered from its crisis of the 1990s. Meanwhile, emerging countries have continued to grow robustly, though concerns have grown about these countries too, not least over the ability of China to manage a transition to slower and more consumption-led growth.

So how do Gavyn Davies of Fulcrum Asset Management and Huw Pill, chief European economist of Goldman Sachs see the economic future? What might it mean for the luxury industry?

Martin Wolf *Is the world coming out of the crisis?*
Gavyn Davies Yes, though it is an arduous process, which might take another five years at least. The banking crisis is over in the US, but not in the UK or the eurozone, both of which need to implement more fundamental clean-ups.
Although central banks have contained the worst, output in the developed countries is still a long way below trend and recovery remains weak. The huge waste of human and physical resources continues.

In the longer term, the prognosis is for a gradual elimination of excess capacity, as growth recovers.
The main catalyst is likely to be a return to normal risk appetites in the private sector. With commodity prices weakening, as supply increases, global deflation is a bigger risk than higher inflation, though neither looks likely.

Quantitative easing is unlikely to be reversed soon. It will not cause inflation in the foreseeable future.

Regulation and macro-prudential policy can handle any bubbles it creates.

The incomes of people likely to buy luxury goods are likely to grow faster than the world economy
Martin Wolf

MW *What about the US?*
GD Much of the above applies to the US. Private sector and bank deleveraging has ceased, while fiscal tightening is having its maximum impact about now. Growth may accelerate to 3 per cent, by next year. This should not cause any difficulties: plenty of spare capacity exists – more than is implied by the unemployment rate, because labour participation can rise.

There are some recent signs of declining core inflation. But inflation expectations remain near to target. With expectations stable and the Phillips Curve [which shows the trade off between inflation and unemployment] relatively flat, a recovery in demand is likely to be reflected in higher real output, rather than greater inflation. The US budget position is sustainable until around 2020, after which it might need further action, notably on healthcare and, to a lesser extent, social security.

MW *What about Japan and particularly, "Abenomics"?*
GD The bold plans of Shinzo Abe, the prime minister, and Haruhiko Kuroda, the new governor of the Bank of Japan, have been a spectacular success in moving financial markets, the yen and inflation expectations. But we do not know whether they will permanently raise domestic demand or reported inflation. I am sceptical. But I do expect exports to grow.

The risk that the general rise in inflation expectations will unhinge the bond market is limited, given the huge BoJ purchases of long-dated debt. The Abe measures on structural and market reform are better than nothing, but are not likely to raise the trend rate of economic growth much. Nevertheless, the depreciation of the real exchange rate should raise Japanese growth, for a while.

MW *What about prospects for the emerging world?*
GD Many of the major emerging economies, which have enjoyed strong catch-up growth, are showing signs of exhaustion: excessive credit growth, real estate bubbles, undue reliance on high commodity prices (which may have peaked in real terms) and a need to change growth models. Furthermore, the scope for catch-up is diminishing, in some cases, including China's. With slowing growth, the possibility of shocks triggered by imploding credit bubbles and sudden slowdowns exists. Such disappointments have occurred previously.

MW *What are the big risks?*
GD The biggest risks lie in the eurozone. There are in addition, geopolitical risks, among which the greatest concern North Korea, Iran, and Pakistan, as well as a resurgence of the revolts of the Arab spring. Finally, a financial crisis stemming from a decline in confidence about government debt would be frightening.

MW *What policy measures are still needed?*
GD A further lengthy period of extreme monetary accommodation is required. On budgets, governments should try Ben Bernanke's plan of introducing long-term, legislated budget consolidation while relaxing near-term fiscal policy, through spending on infrastructure. A more symmetrical adjustment of the balance of payments is essential, with a focus on Germany and China, and probably a further downward shift in the currencies of many advanced countries, relative to those of emerging countries. The reform and recapitalisation of banking systems is unfinished business. And of course most countries need a better strategy for dealing with demographic shifts and climate change. It is a daunting list.

MW *The biggest risks then are in the eurozone. So what does Huw Pill think of its prospects? Is it coming out of its crisis?*
HP Last summer's commitment by Mr [ECB president Mario] Draghi to do "whatever it takes" to save the euro brought the acute phase of the crisis to an end. Yet, the ECB's announcement of its Outright Monetary Transactions (OMT) programme last September does not mark the end of the crisis, but rather a step in its evolution.

The tail-risk of a rapid disorderly break-up of the euro area has receded. European financial markets – not least those for peripheral sovereign debt – have rallied strongly as the OMT has gained traction and credibility, even if, as yet, the OMT itself remains untested in practice.

MW *What are the remaining risks over the next year or two?*
HP The crisis has morphed into a chronic economic malaise. The eurozone is mired in recession. Fiscal consolidation and private-sector deleveraging continue to weigh on demand. Dysfunctional capital and labour markets hinder necessary restructuring and render adjustment more costly.

A recovery in demand is likely to be reflected in higher real output rather than greater inflation
Gavyn Davies

MW *In the longer run, will the eurozone survive and, if so, what needs to be done to ensure this?*
HP The euro can survive this painful period. But emergence from the euro area's economic quagmire will not be spontaneous. It requires policy action on at least two interrelated and challenging dimensions.

First, at the national level, countries must undertake economic restructuring: improving competitiveness, correcting financial and external imbalances and fiscal consolidation are necessary elements. But they weigh on spending and confidence. In many peripheral countries, it remains an open question whether social and political cohesion can survive the pressures.

Second, at the area-wide level, considerable effort is needed to make the euro workable. Achieving this requires greater integration on various dimensions: of the financial system, of the fiscal system and of regulation. Ultimately, this will also entail sharing the relatively strong German national and fiscal balance sheets with other countries. German political and public opinion have yet to acquiesce in these transfers. And achieving that acquiescence depends crucially on the terms at which the transfers are made.

For German public opinion to accept the distributional implications of underwriting – and thereby stabilising – the eurozone, it needs to see concrete evidence of a willingness and ability to reform and consolidate fiscal positions in other countries. Germany is willing to share risks with the rest of the euro area, but only once those inherited from mistakes in the past have been significantly reduced. Meanwhile, other countries argue restructuring is politically and socially feasible only if such economic stabilisation is first achieved, on the back of greater and more visible German financial support.

In short, Germany wants reform before it provides financial support, whereas others seek that support to facilitate implementation of reform. Managing the choreography requires effective institutional and governance at the zone-wide level.

While Mr Draghi and the ECB have an important role to play, the eurozone sorely lacks a coherent governance mechanism to deal with the deeper political and distributional challenges. The disappointing evolution of the debate on banking union over the past year provides ample evidence of this impasse.

For all the economic challenges the eurozone faces, the biggest risks to further progress are political. Risks in the political sphere – where risks to Italian governability and the forthcoming German federal elections stand out – are paramount. The biggest risks at present remain the political difficulties in facilitating and implementing necessary institutional reforms, at both national and zone-wide levels.

Europe's crisis has morphed into a chronic malaise. A solution will not be spontaneous
Huw Pill

Martin Wolf concludes: The crises have been contained, so far. But the challenges remain large, particularly in the eurozone. What might this all mean for the luxury industry? The European market is likely to stagnate, while the US market is likely to be stronger. But the rapid growth is likely to be largely in the emerging countries. The growth in incomes of people likely to buy luxury goods is also likely to be faster than that of the world economy, given the forces for ever-rising inequality.

For online coverage of today's panel and other sessions of the FT Business of Luxury summit in Vienna June 2-3 visit www.ft.com/luxury360 or join the debate on Twitter #FTBizLux13

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Where some purveyors of the good life are happy to tread

Sub-Saharan Africa A tiny elite of very rich customers has emboldened some brands to set up shop in Nigeria, reports *Xan Rice*

On a recent sweaty night at Murtala Muhammed international airport in Lagos, a Nigerian man strutted towards the boarding gates like somebody who knows – or rather hopes – that he is being watched. He was pulling a carry-on Louis Vuitton suitcase, with a smaller Louis Vuitton bag on top. His shoes were from Louis Vuitton and so were his trousers, belt, shirt and sunglasses. It was over-the-top, even by the standards of Nigeria, where some of the elite love to flaunt the luxury brands purchases in the boutiques in European capitals.

Until very recently, flying abroad was the only way for them to buy luxury goods. Now, things may be changing. In April, Ermenegildo Zegna opened a store in Lagos, the first luxury clothing brand to do so. Its setting – on Akin Adesola Street, a busy road that links the lagoon and ocean on either side of Victoria Island, the city's financial district – is not glamorous. But Zegna, which had never had a store in sub-Saharan Africa, is betting that customers more accustomed to shopping on Bond Street on or the Champs-Élysées will not mind.

Zegna is considering opening a store in Angola, which, like Nigeria, has a small but extremely wealthy elite thanks to its oil industry, and in Mozambique, the site of large new gas finds. Africa "is going to be a territory that's very important for luxury", even if the market is still at an early stage, according to Gildo Zegna, chief executive. Describing the company's strategy in emerging markets, including Africa, Mr Zegna told the FT last year that it was targeting "the top 1 per cent of the population, or perhaps even less".

Zegna's African expansion may initially seem startling – both Angola and Mozambique experienced devastating wars not long ago – but the company is not alone. Breitling now distributes its watches through wholesalers in at least a dozen African countries, including Ghana. The trend is less surprising when you look at Africa's place in the global economy. Sub-Saharan African economies are expanding faster than any other region, bar developing Asia, with the IMF forecasting growth of 5.4 per cent in 2013 and 5.7 per cent in 2014. Though many African countries are growing from a very low base – and income distribution is often very unequal – the number of wealthy, status-conscious people is rising and will continue to do so while commodity prices stay high.

For now, the only entrenched market for luxury goods in sub-Saharan Africa is South Africa, which has the continent's largest economy and a largely urban population. A recent report by the consultancy Bain noted that South Africa has 71,000 dollar millionaires, 60 per cent of the total number in sub-Saharan Africa. That is more than Saudi Arabia or the United Arab Emirates and not that far off the 95,000 millionaires in Russia. Bain estimated that by 2020, 420,000 households in South Africa would have disposable income of more than $100,000 and forecasts that the luxury goods market, worth about $1bn a year, will grow by 20-30 per cent for the next five years.

A good night: empty bottles of champagne at a Lagos nightclub frequented by wealthy Nigerians Panos

In South Africa's favour is its large number of high-end shopping malls that offer the sort of retail space attractive to international brands such as Louis Vuitton, Burberry, Gucci and Fendi, all present in the country. South Africa has its own luxury brands working mainly with leather and jewellery.

In Lagos, the continent's most populous city, with more than 12m people, there only two small malls of international standard – compared with 74 in Johannesburg – and even these may not be of a high enough standard for the likes of Louis Vuitton.

Francesco Trapani, head of LVMH's jewellery and watches division, said last year that Africa remained "a very, very small market for us". Hermès said that despite looking at South Africa, it had not yet found any suitable opportunities to do business or open a shop on the continent. Yet as Zegna's foray into Lagos shows, the amount of money sloshing around – and the appetite for conspicuous consumption – means that some luxury goods companies no longer feel content simply to wait for change.

> Nigeria was the second fastest-growing market for champagne from 2006 to 2011

According to Euromonitor, Nigeria was the second fastest growing market in the world for champagne between 2006 and 2011, by which time it had became the 17th biggest consumer of bubbly in the world, with 752,879 bottles drunk. Over the five years to 2016 the trend will continue, with only France experiencing a larger rise in champagne consumption, by volume. And it's not the cheap stuff – Moet, Veuve Clicquot and Dom Pérignon are all popular among Nigeria's elite.

Carmakers have taken note. Porsche opened a dealership in Lagos last year, a short walk away from the Zegna store. For luxury to take full flight will require the emergence of a middle-class. That said, for some luxury bosses, a narrow band of super-rich people will do for now.

Strategic industry comes of age

Continued from Page 1

10 per cent of its exports, according to consultants Frontier Economics, in a report commissioned by the ECCIA.

Luxury is one of the sectors in which Europe has a clear competitive advantage since European brands account for 70 per cent of the global market.

Emmanuel Combe, affiliate professor at ESCP-Europe, the business school, calculates that the French luxury industry had a positive trade balance of €34bn in 2011. That compared with €17bn for the French aerospace industry.

"In other words, handbags, perfumes and spirits carry twice the weight of aeroplanes in terms of commercial balance," says Mr Combe, who is also vice-chairman of the French competition authority. "That demonstrates an extraordinary force for the French economy."

As the creation of the ECCIA indicates, the luxury industry has moved beyond national frontiers to mobilise on a Europe-wide basis.

The Comité Colbert, founded in 1954 to represent *l'art de vivre française,* recently opened its membership to other European countries, including Germany, Belgium, Poland and Hungary.

"The context has completely changed," says Ms Ponsolle des Portes. "In 1954 there was no European Union.

Now, with the adoption of the Lisbon Treaty [of 2011] giving more powers to the European Parliament, the regulatory regime comes from Brussels, which we find ourselves visiting more and more frequently. We have to convince European commissioners and not only the French ministers now."

The recognition of luxury as a separate industry means that its special features and interests will be taken into consideration in future legislation, says Mr Branchini. One of those characteristics is the industry's argument that it must control the distribution of its products to protect their brand and image.

When that came under threat from internet retailers and EU competition law, the industry secured an exemption allowing it to sell its goods through specific outlets.

Now the industry's aim is to prevent regulation that promotes the free transit of goods through Europe from allowing counterfeit goods to pass unchecked.

The protection of intellectual property and a push for the opening up of export markets – especially those of Brazil and India – are other priorities, along with facilitating visas for tourists, who are big buyers of luxury goods when abroad.

> 'Handbags, spirits, perfumes, and so on, carry twice the economic weight of aeroplanes'

The industry's growth is expected to halve this year from 10 per cent last year, according to a survey by Altagamma and the Bain consultancy.

That still makes it one of Europe's fastest-growing sectors. This rising economic weight works two ways, however.

As one EU official said of a global tendency towards protectionism: "France and Italy are very negative about free trade in the Union. So if those industries that benefit from free trade . . . could be more vocal in telling their governments that free trade is good for them, it might influence government positions."

Assertive groups act to make their mark on the virtual world

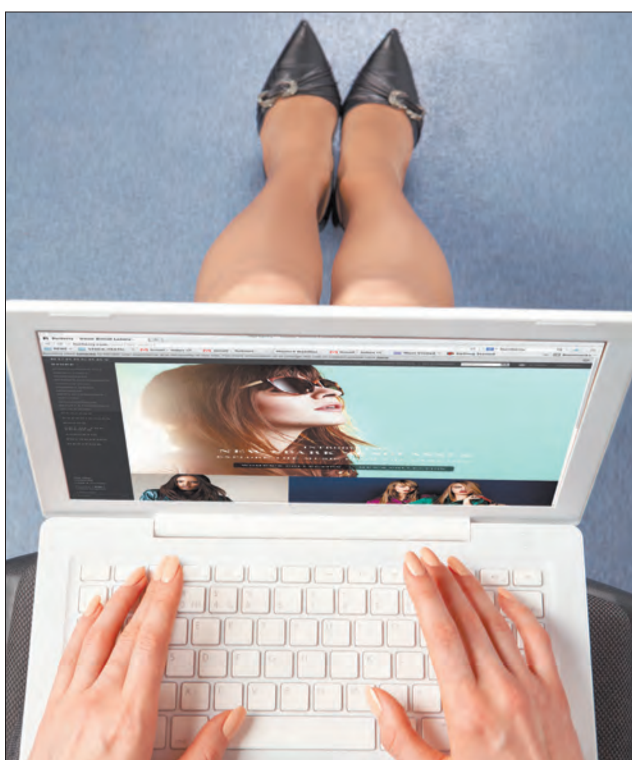
Online retailing

Strategies mirror what is happening in the physical world, says *Andrea Felsted*

From buying in franchises to reinforcing their stamp on their online presence, luxury groups are asserting control of their operations in both the physical and virtual worlds.

"Luxury groups' electronic commerce strategies mirror what is happening in the physical world," says Claudia D'Arpizio, lead author of Bain consultancy's annual luxury report.

Burberry, the British luxury group, has been at the forefront of taking control of its online presence. Burberry World, as it calls its website, includes an internet store, but also streamed catwalk shows, social networking and even specially selected music.



Shoe-in: a businesswoman views Burberry's website

PPR last year formed a joint venture with Yoox, the global internet retailer, dedicated to managing sites for a selection of Kering's brands – Bottega Veneta, Yves Saint Laurent, Alexander McQueen, Balenciaga and Sergio Rossi.

Behind the scenes, Yoox will manage the online operations of these brands for Kering, to help them more quickly develop their web-based presence.

Experts say that just as in the physical world, where luxury groups still want to sell through top end department stores, they will also want to continue to sell through the best multi-brand sites.

Sites such as Net-a-Porter, Yoox, My-Wardrobe, MyTheresa and Feelunique in beauty have all demonstrated that it is possible to sell luxury goods online. Moreover, they can reach a wider and different audience to that of standalone sites.

"The physical world of luxury is more mature than its online counterpart. Luxury boutiques set the benchmark for the offline retail experience, while with online, the situation is a bit different: we are at the beginning of a long journey," says Federico Barbieri, electronic business vice-president at Kering.

"In both the physical and digital worlds, you absolutely still need good multi-brand stores," he says. "They give the customer a broader range of products to play with. Our brands' own sites go deeper, offering the full assortment, a purer representation of the brand and integrated offline services."

Sarah Curran, founder of my-wardrobe.com, says while there may be a period of adaptation for multi-brand sites, they will continue to play an important role.

"There is an adjustment naturally . . . I think the two remain very different," she says.

With luxury brands offering more limited edition or exclusive pieces on their sites, Ms Curran says buyers at multi-brand sites will have to work harder with those brands to ensure that there is an exclusive element in the collections they buy.

To prosper, Ms Curran says the multi-brand sites, as well has having strong buying, styling and editorial content, need to provide an engaging luxury experience, from packaging to excellent customer service.

> 'In both the physical and digital worlds, you absolutely still need good multi-brand stores'

Christine Cross, chief retail and consumer adviser to PwC, says multi-brand sites, such as the websites operated by the top department stores, can provide luxury groups with extensive data about their customers and their purchasing patterns

New forms of multi-brand sites are emerging, blending online stores with editorial content.

The best multi-brand sites have "become curators rather than retailers," says Gregor Jackson, partner at gpstudio, a brand consultancy.

According to Mr Barbieri: "There is room for different online multi-brand business models. I see the new style of curated online magazines you can shop from becoming more and more popular. We all need to grow our presence in the digital space and there are many ways to do it, but it must be done in a selective and qualified way that best positions our brands to a new generation of online consumers."

Ms D'Arpizio says there have always been a small selection of physical stores – such as Colette in Paris or London's Browns – where the very fashion-oriented consumer shops.

"Now probably there are some etailers that play the same role but in a more powerful way, because they also can deliver a lot of editorial content. You have the best of both: the best of Vogue and the best of Colette on one site," she says.

Ms Curran maintains that "the multi-brand and own brands . . . can coexist online, as they do on the high street.

"No one would dream of saying 'because Burberry has opened another flagship store, Harrods or Selfridges or Harvey Nichols [will] lose sales'. No one would make that assumption. It's the same with online."

Where luxury groups may cut back their reliance on multi-brand sites is with those offering discounted luxury goods or so-called flash sales.

Outlet and flash sale sites are still expanding, says Ms D'Arpizio, because they are adding new brands to their portfolios, "but the big luxury brands are not pushing this route to market any further".

Rob Feldmann, chief executive of BrandAlley, a luxury flash sale site, says: "We have seen the high end brands we work with becoming a lot more selective about where they sell their products."

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