

Overview of Global and China Luxury Markets

1. Global Luxury Market

Global Luxury Market

Introduction

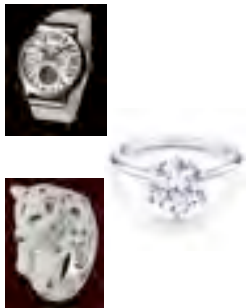
Introduction

- Luxury goods retail market started in Europe in eighteenth century
 - Paris, Milan and London have been the key fashion cities worldwide for over a century
- Japan and U.S., driven by the strong economic growth, became the top luxury market in the end of nineteenth century
- The global luxury goods retail market depreciated by the financial crisis since 2008, except the emerging markets, especially China

Definition

- Luxury brands usually have high reputation, as well as prestige brand perception, as well as high brand awareness among consumers
- The four key category of luxury goods include (i) hard luxury, (ii) cosmetics, (iii) apparel & shoes and (iv) handbag and small leather goods

Hard Luxury



Cosmetics



Apparel and Shoes



Handbag and SLG



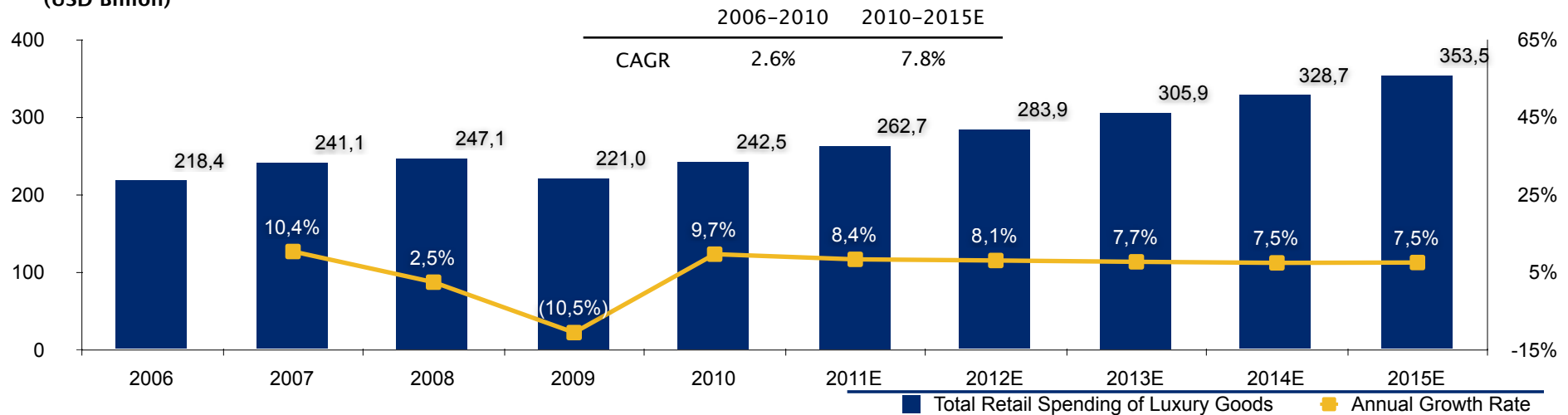
Others



Global Luxury Market Market Size

Total Retail Spending of Luxury Goods Retail Market (Global), 2006 – 2015E

Total Retail Spending
of Luxury Goods
(USD Billion)

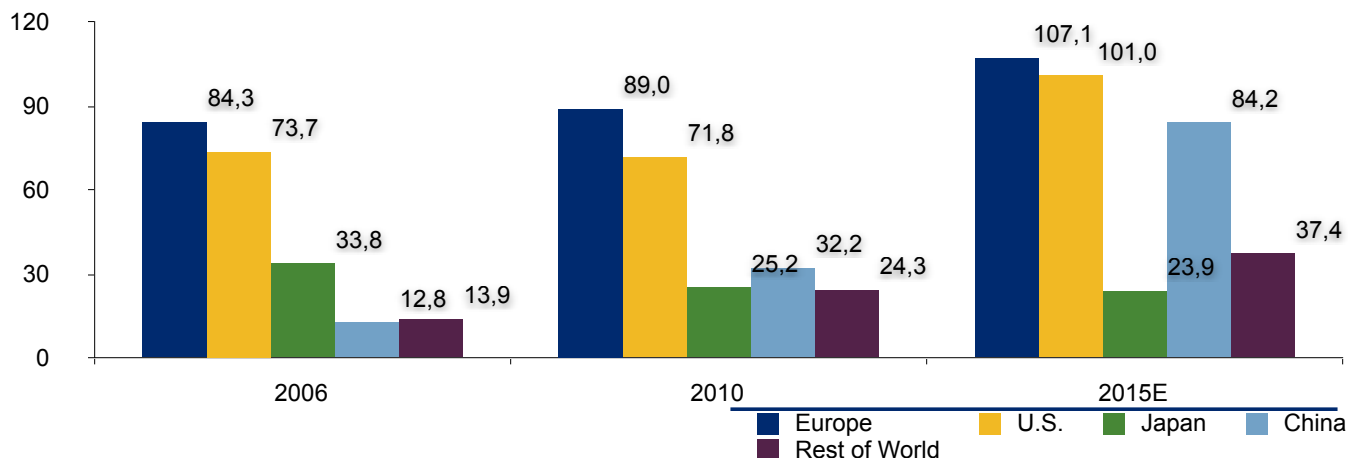


- Total luxury goods market size of US\$242.5bn in 2010A
- Market size expected to be increased to US\$353.5bn in 2015E
- Growth CAGR between 2010A to 2015E is 7.8%

Global Luxury Market Breakdown by Region

Comparison of Total Retail Spending of Luxury Goods by Region, 2006 – 2015E

Total Retail Spending
of Luxury Goods
(USD Billion)



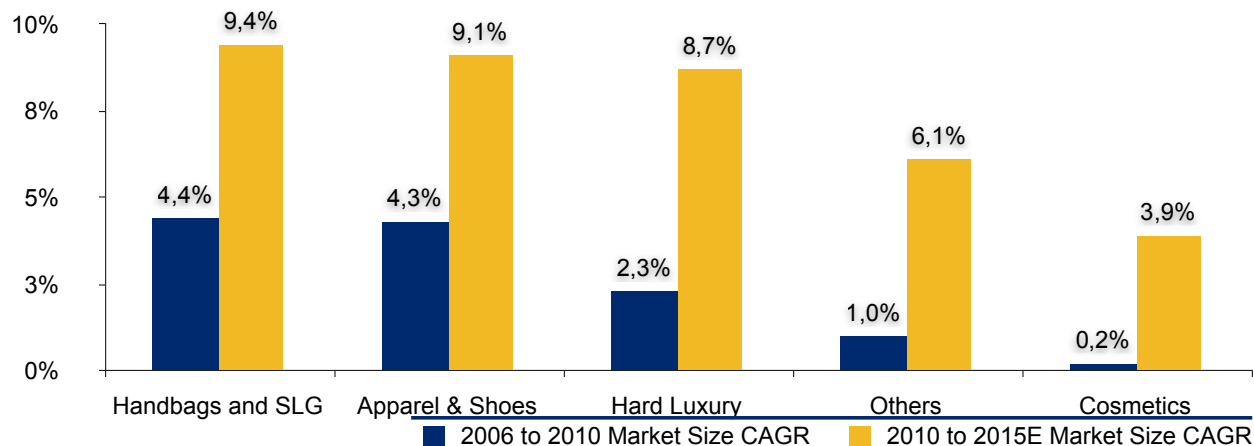
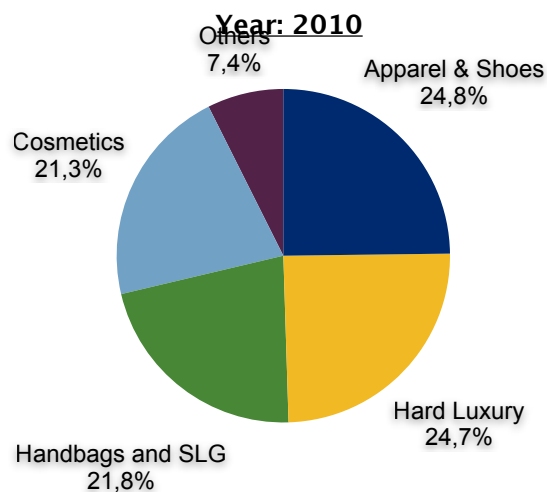
	CAGR	2006-2010	2010-2015E
Europe		1.4%	3.8%
U.S.		(0.6%)	7.1%
Japan		(7.1%)	(1.1%)
China		26.0%	21.2%
Rest of World		15.0%	9.0%

- Europe remains the largest luxury market in 2010A with US\$84.3bn of market revenue (or 37% market share)
 - Followed by US (US\$71.8bn in size or 29.6% of market share) and China (US\$32.2bn in size or 13.3% in market share)
- China market will grow rapidly from US\$32.2bn in 2010A to US\$84.2bn in 2015E (or 23.8% of market share), representing a 21.1% CAGR
- China will also account for US\$52.2bn out of the US\$111.0bn (or 47.8%) of global luxury market growth from 2010A to 2015E

Global Luxury Market

Breakdown by Product Category

Growth of Major Segments of Global Luxury Goods Retail Market (Global), 2006 – 2015E



- Apparel and shoes as well as hard luxury are the two largest luxury goods sub-segment each accounting for around 25% of market
- Handbags & small leather goods and cosmetics are the third and fourth largest luxury goods sub-segments each accounting for around 21% to 22% of the total market
- Handbags and small leather goods is the faster growing luxury goods sub-segment with an expected CAGR or 9.4% from 2010A to 2015E
 - Apparel & shoes and hard luxury have 2010A to 2015E CAGR of 9.1% and 8.7%, respectively

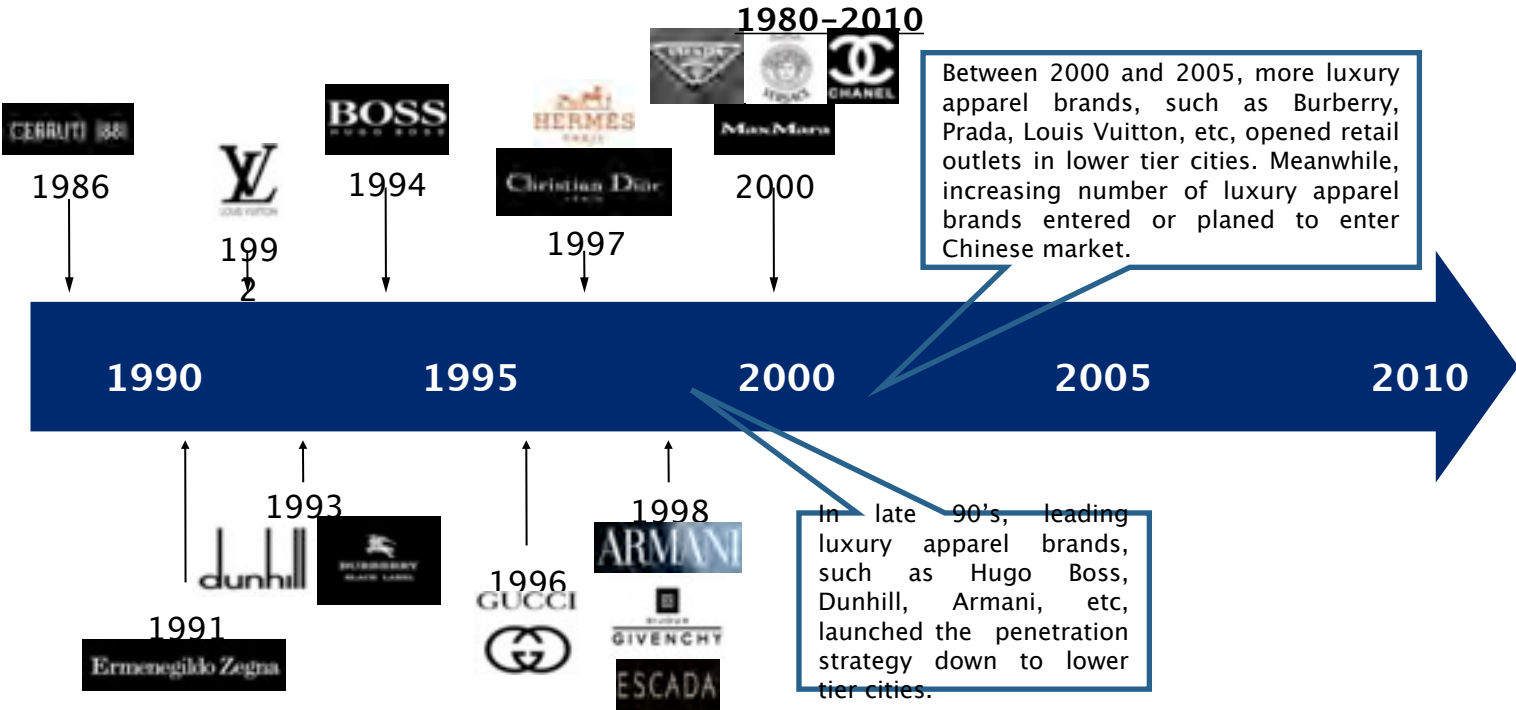
2. China Luxury Market

China Luxury Market

Market Overview – Introduction

- ✓ The first group refers to brands entered China in 90's, such as Ermenegildo Zegna, Dunhill, Hugo Boss, Armani, etc.
- ✓ The second group refers to brands entered China around 2000, such as Prada, Chanel, Versace, etc.
- ✓ Most of the first group brands launched the penetration strategy in late 90's.
- ✓ Driven by the rapid development of the Chinese luxury apparel market, the second group brands typically started penetrating down to lower tier cities as soon as they entered the Chinese market.

Timeline of the Entrance of the Leading Luxury Apparel Brands in the Chinese Apparel Market (China),



China Luxury Market

Historical Progression of Global Luxury Goods Market

Historical Progression of Chinese Luxury Goods Market

Before
1990

- During the 1980s, entry into the Chinese market by international luxury brands was restricted by the Chinese government despite the implementation of open door policy and economic reform and there was limited luxury goods consumption in China.

1990 –
1999

- The luxury goods market in China started to develop in the early 1990s when a few international luxury brands such as Armani and Hugo Boss entered into China's tier 1 cities.
- The development of the Chinese luxury goods market was relatively slow throughout the 1990s, owing to the lower purchasing power of the Chinese households as compared to many other more-established luxury market, such as U.S., EU, and Japan.

2000 –
2004

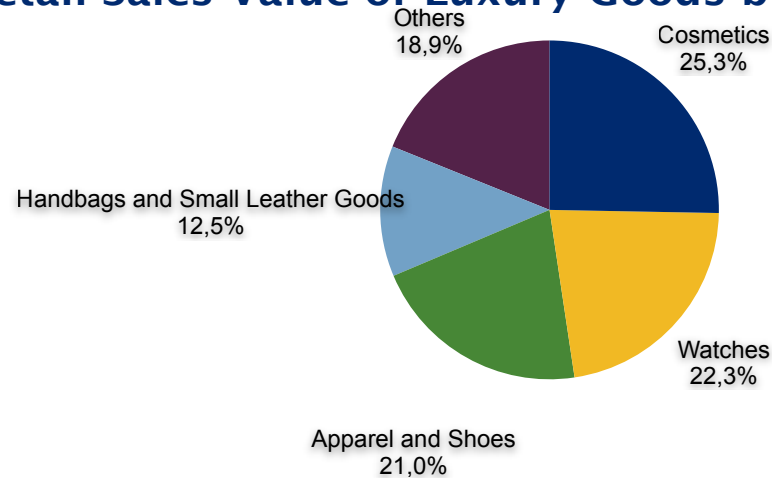
- the rapid economic and social development in China further accelerated the growth of Chinese luxury goods market around the early twentieth century. As a result, a group of luxury brands, such as Chanel, Prada, Loewe and Dolce & Gabbana, entered this market since then.
- In the early 2000s, several international luxury brands launched their expansionary strategies in China and began to open retail outlets into tier 2 and tier 3 cities in China.

2005 –
2010

- The financial crisis in 2008 made Chinese luxury goods market as one of the key markets just behind U.S. and Japan. From 2007 to 2010, Chinese luxury goods market was one of the key growth drivers to the global luxury goods market.
- The competition of luxury brands gradually moved from tier 1 cities to tier 2 and tier 3 cities in China.

China Luxury Market Major Product Category

Domestic Total Retail Sales Value of Luxury Goods by Product Category (China)

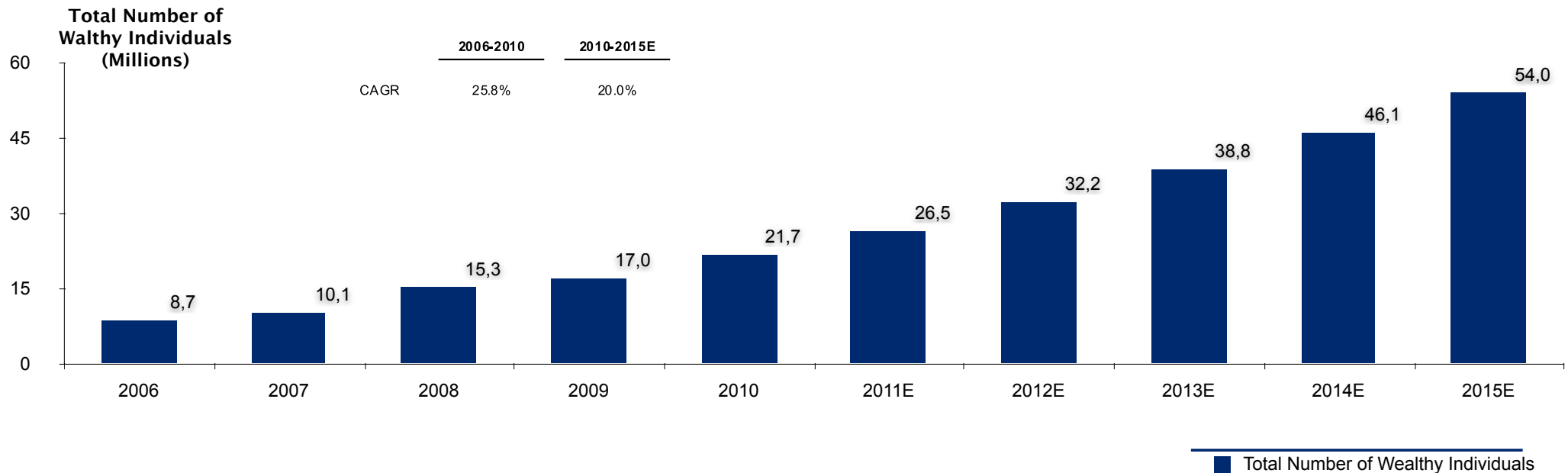


- Largest luxury goods market in China is cosmetics products, accounting for 25.3% of the market
- Followed by watches with 22.3% market share
- Apparel & shoes have 21.0% market share
- Handbag and small leather goods account for around 12.5%

China Luxury Market

Luxury Market Driven by Increasing Wealthy Individuals in China

Total Number of Wealthy Individuals (China), 2006 - 2015E



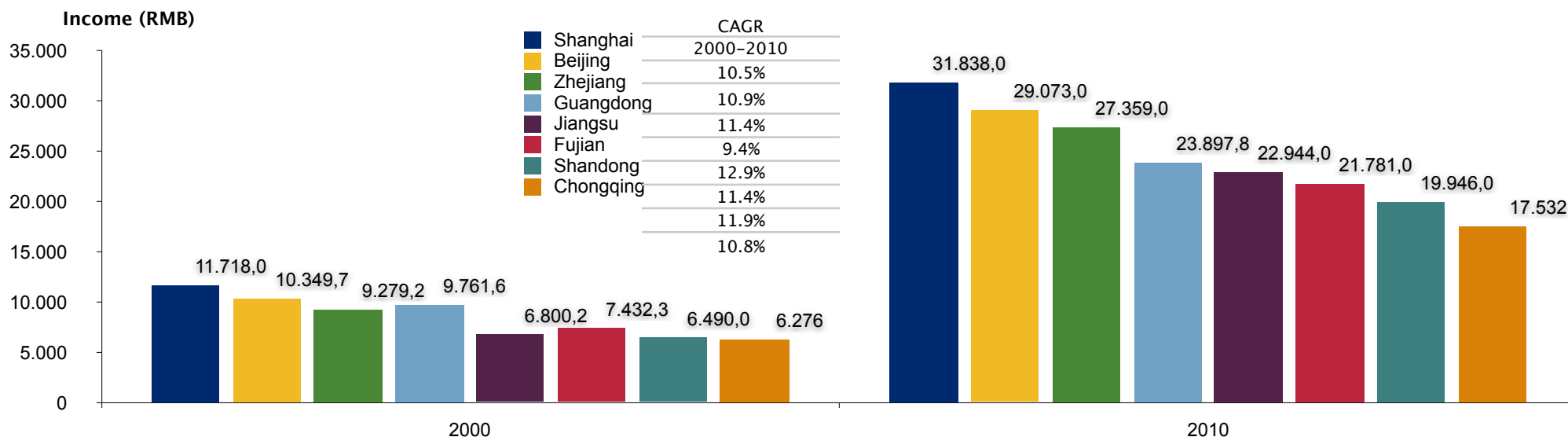
- The total number of wealthy individual (people with annual disposable income greater than RMB100,000) in China reached 21.7 million in 2010 up from 8.7 million in 2006, represented a CAGR of 25.8% from 2006 to 2010.
- This number is like to reach 54.0 million in 2015 with a CAGR of 20.0% from 2010 to 2015
- The wealthy individual group is the main targeted customers of the luxury goods.
- The rapid expansion of the wealthy individual group is likely to increase the purchasing power of luxury goods consumers in China

China Luxury Market

Coastal Cities With Higher Income Been Key Driver of Luxury

Market

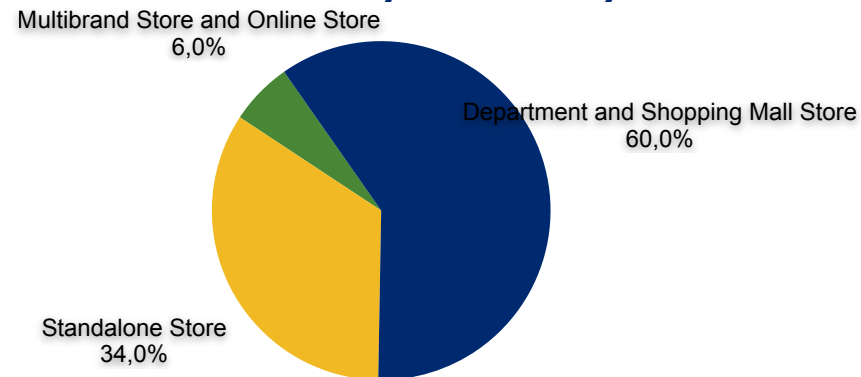
Per Capita Annual Disposable Income of Urban Households by Province and Municipality (China), 2000 - 2010



- As tier 1 cities, Shanghai and Beijing achieved higher per capita annual disposable income of urban households than most of other cities in China by the end of 2010.
- At the same year, Zhejiang province ranked the first in terms of per capita annual disposable income of urban households among all provinces in China
 - Followed by Guangdong province, Jiangsu province, Fujian province, and Shandong province. Jiangsu province achieved the greatest growth rate from 2000 to 2010, represented a CAGR of 12.9%
- As a result, leading luxury brands have already taken these rich coastal regions as their key markets in China

China Luxury Market Main Distribution Channel

Domestic Total Retail Sales Value of Luxury Goods by Distribution Channel (China), 2010



- In 2010, department and shopping mall store has been the largest distribution channel in Chinese luxury goods retail market.
 - Compared with tier 1 cities, department and shopping mall stores are adopted more regularly in lower tier cities.
 - Along with penetrating strategy by most of the luxury brands, the retail sales value through this distribution channel is likely to increase
- Standalone store represented around 34.0% of the total retail sales value in China in 2010. This distribution appears more frequently in tier 1 cities
- Online store and multibrand store are in an early stage now with limited retail sales value.
 - As the fast development of electronic commerce in China, more and more luxury brands are expected to focus on the online store channel in the future.
 - However, considering the price and safety issue, only a few people purchase luxury apparel through internet at this moment

China Luxury Market

Macro Market Drivers

Luxury Goods Retail Market: Market Drivers Ranked in Order of Impact (China), 2011E - 2015E

Rank	Drivers	Description	1-2 Years	3-5 Years
1	The Strong Growth in Nominal GDP and Disposable Income	<ul style="list-style-type: none"> China maintained strong growth in both nominal GDP and disposable income even under the financial crisis and the rapid growth is expected to continue in the future. The increasing in GDP and disposable income to boost the purchasing power of luxury goods 	High	Medium
2	The Rapid Expansion of the Wealthy Individual Group	<ul style="list-style-type: none"> The total number of wealthy individual (people with annual disposable income greater than RMB100,000) in China reached 21.7 million in 2010 This number is like to reach 54.0 million in 2015 with a CAGR of 20.0% from 2010 to 2015. The increasing number of wealthy individual enlarges the consumer group of luxury goods. 	High	Medium
3	The Rising Urban Population and Urbanization	<ul style="list-style-type: none"> With the continuous development of urban facilities, the urban population is expected to maintain a CAGR of 2.8% from 2009 to 2014 and reach 732.3 million urban population by 2014, with urbanization rate of 53.5%. This is likely to accelerate the steps of penetration of luxury brands in China. 	High	Medium
4	The Law and Regulation for Anti-piracy	<ul style="list-style-type: none"> Pertinent laws and regulations are raised for anti-piracy and blocking all kind of activities of selling fake products. Brand's reputation and image are expected to be protected from those laws and regulations. Other laws, such as PRC Anti-unfair Competition Law, are designed to standardize norms for the luxury goods retail market. 	High	Medium
5	The Tax-Free Policy in Hainan	<ul style="list-style-type: none"> Chinese consumers have another option to purchase cheaper luxury goods instead of Hong Kong. Following Hainan, Chinese government is considering to launch more duty-free area in mainland China in the future to drive the development of luxury goods retail market. 	Medium	Medium

China Luxury Market

Micro Market Drivers

Luxury Goods Retail Market: Market Drivers Ranked in Order of Impact (China), 2011E – 2015E

Rank	Drivers	Description	1–2 Years	3–5 Years
1	The Raising International Status of Well Developed Cities in China	<ul style="list-style-type: none"> Shanghai, Beijing, and other well developed cities in China have achieved great international status worldwide. A large amount of foreign tourists and businessmen are attracted to visit or live in those cities. Foreigners are expected to have greater contribution to Chinese luxury goods retail market. 	High	Medium
2	The Diversification of Distribution Channels	<ul style="list-style-type: none"> The establishment of online distribution channel has a positive impact to the Chinese luxury goods retail market. Though the retail sales value generated by the online stores is limited at the present, the online stores have a great contribution in advertising and promoting. More consumers are likely to treat the luxury online stores as the major source to obtain the information of products. 	Medium	Medium
3	The Appearance of Experienced Distributors	<ul style="list-style-type: none"> In Chinese luxury goods retail market, there are many experienced distributors. New entrants are likely to enter this market more easily with the help of those well qualified distributors. 	Medium	Low
4	The Raising Popularity of Western Culture	<ul style="list-style-type: none"> Chinese people are strongly influenced by western culture through movie, music, fashion show, magazine, and other media, especially in fashion area. Thus, more western luxury brands are likely to be known and welcomed by Chinese people in future five years. 	Medium	Low

China Luxury Market

Consumer Behavior Analysis

Increasing Brand Awareness

- Chinese consumers are now strengthening their ability to recognize the luxury brand through its logo and other links, and also the ability to distinguish one brand from another in terms of brand's culture and background.
- The increase in brand awareness is directly leads to the increase in the consumer's willingness to pay the higher price for those luxury goods.

Increasing Brand Loyalty

- China consumers become more sophisticated and experienced. Consumers consider more about perceived value, satisfaction and brand trust on brand selection.
- Brand loyalty is generated and accumulated through their consumption experiences and consumers with higher degree of brand loyalty is likely to have lower sensitivity to price.

Preference for Household Names

- Chinese consumers prefer household names during luxury consumption.
- Luxury product is often regarded as an emblem of wealth and status in China. Leading brands, with recognized logo are likely to get success more easily than other brands in China.
- Compared with lesser-known brands, leading brands, such as Gucci, Louis Vuitton, Prada, and etc, often achieve better performance in China.

Young Consumers

- Compared with consumers in western countries, Asian consumers in luxury goods retail market are much younger. In Japan, teenagers and people between age of 20–30 are the key consumer group. The average age of Chinese consumer kept decreasing in past few years and is expected to be lowered further in future five years.
- Young generation has stronger willingness to pursue higher level of living standard. In China, luxury goods have been regarded as high level of living standard. On the other hand, Chinese parents are more willing to spend on their children. Hence, Chinese young people's desire on luxury goods are more easily to be satisfied by their parents.

Gifts and Vanity

- Gifting is part of Chinese culture. As the increase in popularity of luxury goods in China, luxury goods become one of the key option for gifting.
- Chinese people usually purchase luxury goods to keep up with others. Comparison and vanity is one of the key factors on luxury goods consumption in China.

China Luxury Market

Competitive Landscape Overview

- In 2010, luxury apparel market generated RMB14.2 billion in terms of total retail sales value in China, with luxury menswear of RMB10.5 billion and luxury womenswear of RMB3.7 billion.
- Although the luxury apparel market in China is still in an early stage of development, Chinese consumers are not unfamiliar with various leading global luxury brands.

- Leading global apparel brands such as Armani, Gucci and Hugo Boss have been active in the Chinese luxury apparel market since the early 1990s and 2000s and, driven by the booming Chinese economy, the domestic luxury apparel market has expanded rapidly in the last decade.

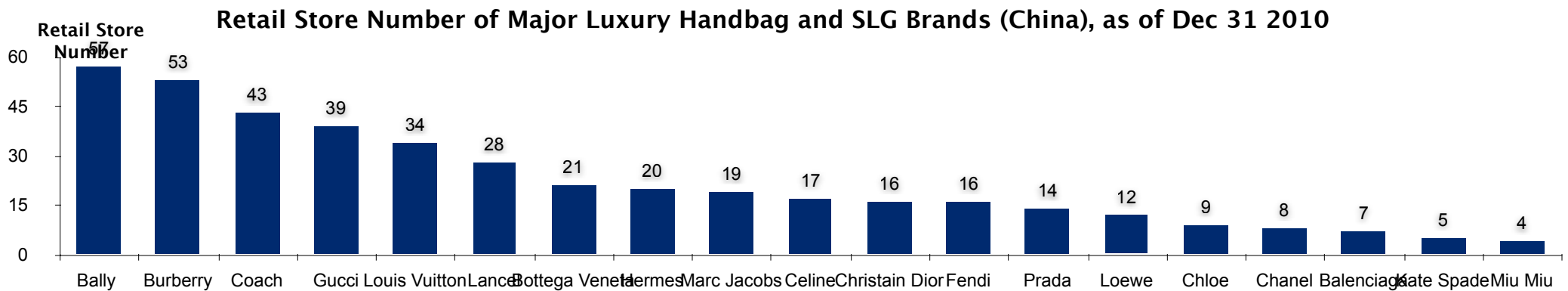


- As of 2010, over 40 luxury apparel brands have entered the PRC market, with 20 of them being leading brands. These leading brands have also launched successful market penetration strategies successively over the past few years due to the rapid development of lower tier cities.

Compared to leading peers, many young luxury brands have only entered the tier 1 cities in China recently. The entrance of these new brands will intensify the competition.

China Luxury Market

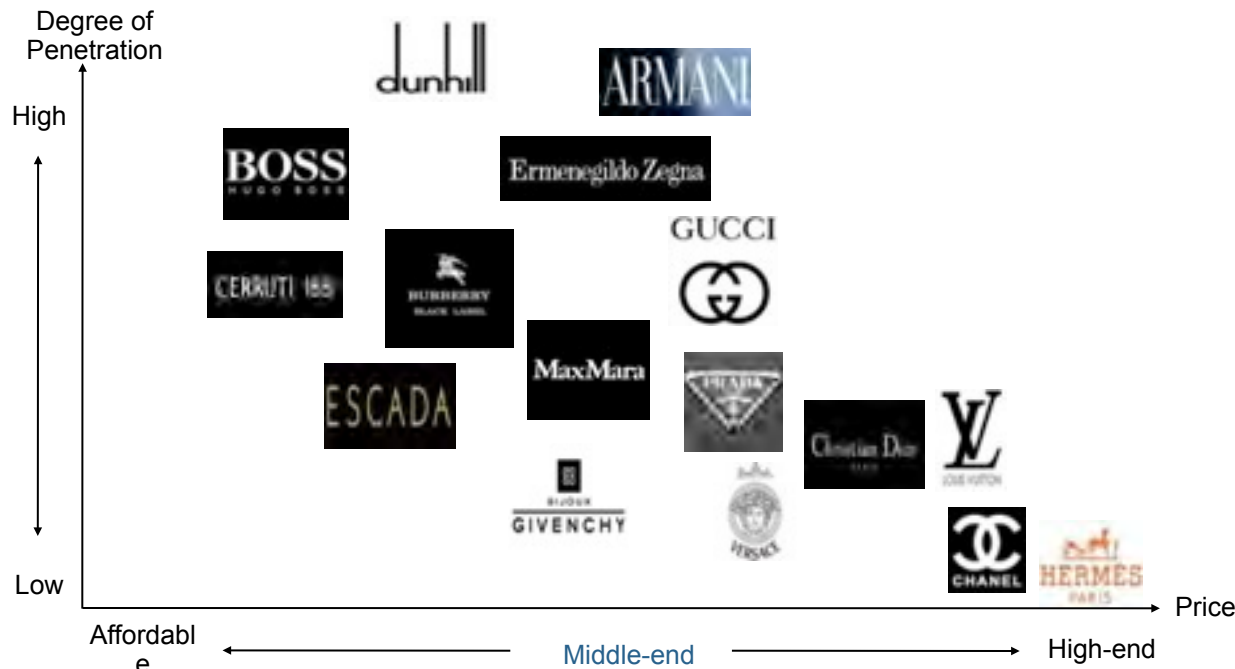
Major Luxury Handbag Brands by Retail Store Number in China



- Both Bally and Burberry have a large number of retail stores in China.
 - The total number of retail stores of those two brands reached 57 and 53, respectively by the end of 2010.
- Coach, Gucci, Louis Vuitton, and Lancel had retail store number of 43, 39, 34, 28, respectively by the same period.
- Other world famous luxury handbag and SLG brands, such as Bottega Veneta, Hermes, Marc Jacobs, Celine, Christain Dior, Fendi, Prada, Loewe, and etc applied different strategies in Chinese market.
- The strong growth on Chinese economy and fast development of lower tier cities attract more luxury brands to invest in China continuously. The total retail store number in Chinese luxury handbag market is likely to raise dramatically in the future.

China Luxury Market

Major Product Retail Price Range of the Leading Luxury Apparel Brands,



- In China, luxury apparel brands are distributed among affordable, middle-end and high-end in terms of the retail price.
- Brands with affordable retail price usually have higher penetration rate than those brands with high retail price.
 - Some middle-end brands with long history in Chinese market, such as Armani, also have relative high penetration rate compared to the rest.
- Brands within different positions have different strategies in Chinese market.
 - Affordable brands normally cooperate with local partners or distributors to launch the expansion or penetration strategy. Qualified and experienced distributors with widespread retail network often benefit the brands when they are penetrating down to lower tier cities.
 - High-end brands also collaborate with those distributors which are well qualified in brand management skill, store operation skill, and other skills, to achieve excellent brand image and improve the store management.

Risk Factors of China Luxury Goods Market

Effective brand messaging and maintenance is key to success

- Turnover heavily rely on strength of brand
- Brand maintenance depends on reputation for superior craftsmanship and quality products, complemented by consistent customer services

Sales is strongly sensitive to macroeconomic changes

- Changes in business conditions, real estate market outlook, stock market movements etc. all affect consumer confidence

Business operations rely on certain key personnel

- Business success heavily rely on industry expertise of key personnel such as design and production team
- Loss of such personnel is costly to replace and takes long time to train and develop

Dependent on strength of trademarks and intellectual property rights

- Business is highly dependent on brands' ability to protect and promote trademarks and intellectual property rights

Increasing difficulty in finding suitable locations for new stores

- Supply of prime locations is scarce and competition to secure these locations is intense
- High cost associated with expansion either through purchasing or leasing suitable properties

Intense competition in all luxury goods categories

- Intense international luxury goods competition
- Success depends on financial resources and negotiation power with suppliers, wholesale accounts, landlords etc.

Success depends on ability to identify market trends and customer preferences

- Brands have to identify market trends and tailor products according to different customer preferences in respective regions
- Results will be negatively affected if new design cannot be delivered in a timely manner

Decrease in number of tourists could negatively affect sales

- PRC tourists constitute a major group of customers in luxury goods market especially in Hong Kong and Macau
- Tourism industry is highly susceptible to certain events such as government policies