



Fine Wine 2010

III Congreso Internacional de la Ribera del Duero

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Overview

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1. China's luxury market

- China's total consumption of luxury goods reached US\$8.6 billion by January 2009 and is expected to reach US\$12billion by end of 2010 and US\$17billion by 2015
- China accounts for 25% of the total luxury market in the world, recently surpassing US and just behind Japan; By 2015, China is expected to be the top country for luxury goods
- Luxury market is growing in the largest adult segment of the population – between 25-40 yrs of age & in China's coastal cities as well as in secondary cities
- Growth has been 20-25% per annum for the past 3 years & expected to continue at same rate
- Louis Vuitton, Gucci and Chanel are China's top luxury brands

Figures from World Luxury Association's report on China 2009
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2. The challenges

- Fragmented market
- Legal issues with establishing a joint-venture or wholly owned foreign enterprise
- Logistics challenges in shipment, delivery, customs
- Lack of nation-wide distribution network within China
- Quality issues with service and point of sales
- Issues with authenticity, imitations and label integrity



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3. The cultural dimension

■ Hierarchical society



- Confucius values still form the core of Northeast Asian cultures.
- Confucius emphasized a set of hierarchical rules to guide society – e.g. loyalty to superiors, social obligations towards others, respect for elders, attendance to ceremonies



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3. The cultural dimension

■ Social values



- Individual's identities intertwined with others
- Obligation towards giving 'face', respect, honouring special guests, VIPs
- Luxury items are as often for others as for self
- Meals in a business context function to 'give face' and 'honour' guests



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3. The cultural dimension

■ Lifestyle



- City living means tiny living spaces across all the major cities in Asia
- Eating out is just as common as eating at home
- Luxury items play an even more important role with a 'going out' vs staying home lifestyle

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4. Success of LVMH

- LVMH, the largest luxury goods group in the world, reported more than 30% growth of profits in China's mainland. It has opened **27 Louis Vuitton outlets in 22 Chinese cities**, for sales of only LV
- The Shangjia Center in Shanghai, known as the “LV mansion” will turn into an international luxury base with **joint investment** from LVMH Group and gaming magnate Stanley Ho in Macau.
- LVMH has done an excellent job of brand positioning and has succeeded in gaining **a following among the top percentage of wealthy Chinese**
- LVMH's brand imaging relies heavily on pushing its **European heritage**, especially in its advertising
- Despite moving production to China, LVMH has managed to **keep retail prices high** due to its strong brand image and following among wealthy Chinese

*Source: BrandChannel, *By Design: Luxury Brands in China*, 18 May 2009

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5. Decline of Audi

- Audi's **share of the Chinese luxury car market dwindled to 42 percent** from 66% over a period of six years
- After a 20 year dominance in China as the Chairman's car of choice, Daimler AG (Mercedes) and BMW are gaining market share as they **target governments for bulk purchases**
- The shift to new market entrants indicates a **lack of brand loyalty** among Chinese consumers who are only now being exposed to a wide variety of luxury brands for the first time
- The drop in Audi's market share came after Daimler and BMW **established joint ventures** over the last seven years **to build cars locally**
- Mercedes debuted a longer E-Class in Beijing in April 2010, while BMW showed an extended 5-Series, both cars **developed specifically for the Chinese market**. The longer vehicles are meant to appeal to wealthy Chinese buyers, who are **typically chauffeured**.

*Source: Bloomberg BusinessWeek, *Audi's Two-Decade China Dominance Threatened by BMW, Mercedes*, 21 April 2010

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6. Takeaways

- **LVMH understood the influence and power of opinion leaders, image makers and the elite** while selling products that were accessible for upper middle class.
- **LVMH formed important social bonds** with the local market by **forming joint ventures** and creating local products such as LV Chinese Lantern Charm accessories
- **LVMH catered to the 'going out' lifestyle** by creating mega-lifestyle stores that goes beyond just handbags
- Audi became complacent and **did not understand nor integrate with the local market** – e.g. did not create larger cars for chauffeur driven lifestyle; did not form joint ventures to form close social bonds; did not target their marketing efforts to the opinion leaders such as government officials.
- Establishing local presence may entail **shifting part of the manufacturing** to China (e.g. Coach, Paul Smith, Armani) or finding locals to help navigate the market -- Hong Kong's Dickson Concepts with Polo Ralph Lauren, Brooks Brothers and ST DuPont



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7. The Lafite phenomena

- One market effectively pushed up the price of one brand
- Combination of factors behind Lafite's success:
 1. **Bordeaux' 1855 classification** is easily understandable to a society based on a pyramid/hierarchical social structure. Lafite is clearly at the top of this pyramid.
 2. **Opinion leader** endorsements by senior government officials and top business leaders who served Lafite at prestigious formal dining occasions, this then led to a cascading effect
 3. **Lafite caters to the dining-out culture** of urban Chinese who has increased spending on food by 17% per year on average between 2004-2009 (USDA FAS report 2010).
 4. **Lafite has luxury brand** appeal with an easy to pronounce Chinese name and enjoys a perceived scarcity factor and high price. Lafite's classic label has marketing appeal & represents both heritage & prestige.
 5. **Lafite's joint venture with CITIC** (China's largest state-owned investment company) to establish a winery in Penglai lays the foundation for creating strong social bonds within the industry.



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