The incredible resilience of the luxury sector

Image source: fr.louisvuitton.com

Despite financial crises, pandemics and geopolitical tensions, the luxury goods market has performed remarkably well over the last 15 years.

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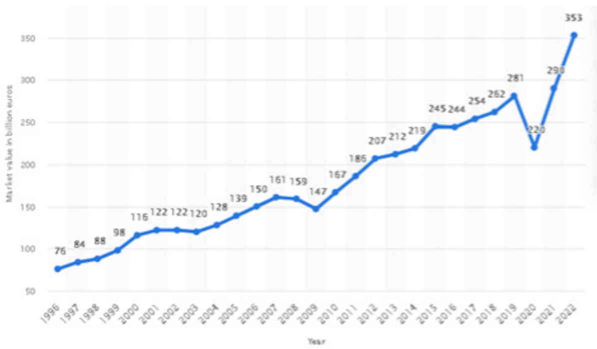
The global luxury goods industry, which includes wines and spirits, fashion, cosmetics, perfumes, watches, jewellery and leather goods, has been on an upward trend for many years. According to Statista, the value of the global personal luxury goods market has been estimated at €353 billion by the end of 2022, an increase of 26% since the end of 2019.

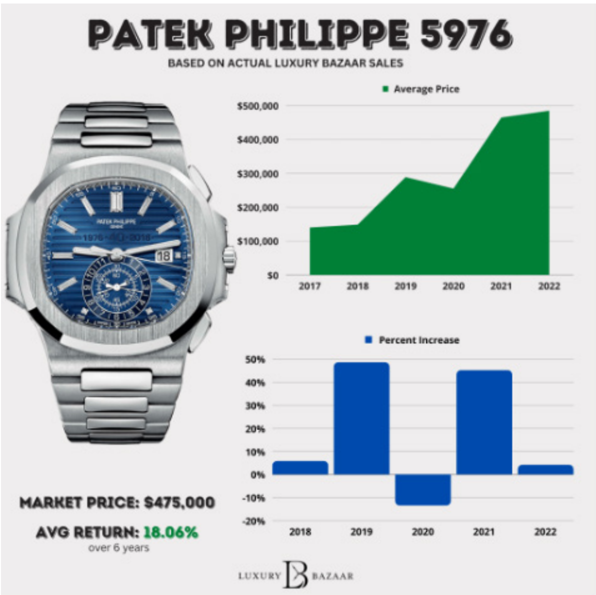
Value of the global luxury goods market for consumers from 1996 to 2022 (in billions of euros)



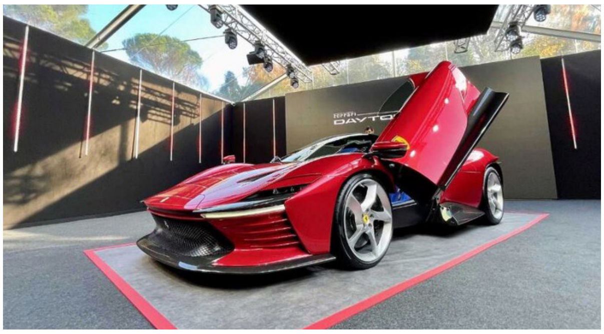
Source: Statista

An emblem of the sector, LVMH has become the 1st European company with a market capitalisation in excess of 500 billion dollars. The share value has doubled since the end of 2019.

The luxury watch sector has also eperienced an unprecedented boom. Between August 2018 and January 2023, average prices on the second-hand market for top-of-the-range watch models from the three biggest luxury brands - Rolex, Patek Philippe and Audemars Piguet - rose at an annual rate of 2.



In the automotive industry, it is Ferrari that is breaking all records: the best operating margin in the sector (over 23% by the end of 2022) and a market capitalisation of over 57 billion euros, making Ferrari the share with the highest P/E in Europe (55x). It has to be said that models from the prancing-horse maker are selling like hotcakes. The Daytona SP3, of which Ferrari plans to produce just 599 units at a list price of $2.25 million, was sold out even before the brand unveiled its outline.



Despite facing significant economic challenges, the luxury goods market has adapted and thrived in a constantly changing environment.

Before looking at the possible factors behind this resilience, let's take a look back at how the sector has behaved during the crises of the last 15 years.

The Luxury sector during the Great Financial Crisis

The crash of 2008 dragged down the consumer sector, particularly in the United States. Paradoxically, however, sales of luxury goods fell only slightly (by around 5% in 2009) and then recovered rapidly. Some luxury brands (LVMH, Hermès, Ralph Lauren, etc.) managed not only to survive, but also to strengthen their dominant position. This paradox can be explained by the unique characteristics and strategies employed by these brands during the recession. Marketers worked hard to understand their customers' preferences and buying motivations, particularly in difficult economic conditions. Instead of cutting prices, they focused on their strengths and heritage.

Here are a few examples. Hermès, known for its timeless classics and impeccable product quality, opened its first men's shop in New York at the height of the recession (2010). In the same year, Ralph Lauren opened a 2,000 square metre shop on the corner of Madison Avenue and 72nd Street in Manhattan.

The luxury sector and the pandemic

The Covid-19 crisis could have brought the sector to its knees, but it did not. Luxury brands showed their adaptability by reacting quickly at the start of the crisis. Many companies redirected their production to meet urgent health needs, making protective masks and hand sanitisers, for example. Examples include LVMH, which produced hand sanitiser rather than perfume at the height of the crisis, and Armani, Bulgari and Dior, which turned to the production of personal protective equipment.

Luxury brands have also emphasised their philanthropic efforts and contributions to society, which has resonated positively with consumers and strengthened their brand image.

Finally, the fact that households were able to continue to receive their salaries while being confined to their homes created an unprecedented accumulation of savings. Some of these savings were used to purchase luxury goods during the pandemic (via e-commerce) but especially afterwards.

Why the resilience of the luxury goods market may persist

Generational trends will be a powerful growth driver for the sector over the next decade. Consumers of luxury goods are getting younger and younger, and have significant purchasing power. Millennials/Generation Y (born between 1981 and 1984) and Generation Z (1996-2010) accounted for all of the market growth in 2022. Spending by Generation Z and Generation Alpha (born after 2010) is expected to grow three times faster than other generations, accounting for a third of the market by 2030. Another point to emphasise is that generation Z starts buying luxury products at the age of 15, three to five years earlier than millennials. Generation Alpha is likely to be even earlier. The younger generations attach great importance to their image. Owning luxury goods can be a form of personal expression and a way of crafting the image they wish to project. Today, luxury is a symbol of success, taste and discernment.

Everyone wants a slice of luxury, and the brands that have understood this are thriving today. By adapting to consumer preferences and engaging with them through different channels, luxury brands can target different social and demographic strata, allowing them to expand the size of their target markets.

Technology is making luxury more accessible. The internet, social networks, social shopping and e-commerce have become essential for reaching the digital-savvy Y, Z and alpha generations. By 2021, luxury brands will have allocated around a third of their marketing budgets to digital strategies, focusing on improving websites, creating content and collaborating with influencers via social networks. Content on platforms such as Instagram, TikTok and YouTube has generated interest in luxury goods, making them more accessible and desirable to young people.

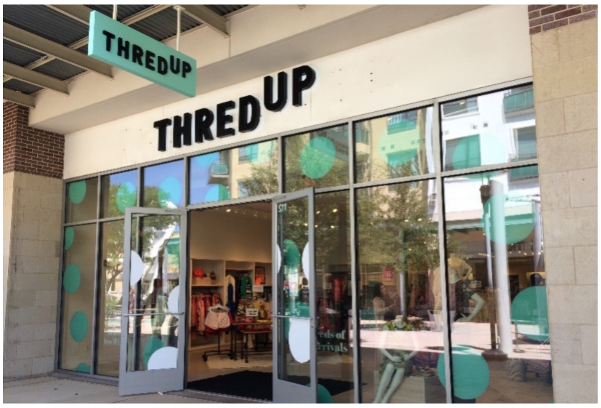
Changing consumer preferences also play a role. Coco Chanel's timeless quote, "Luxury must be comfortable, otherwise it is not luxury", resonates more strongly today. Luxury is no longer synonymous with formality. The Covid-19 pandemic has changed consumer preferences, and brands have adapted to meet changing demand. Those who have known the comfort of working from home for two years are unlikely to return to a more formal dress code. In the footwear industry, trainers from designers such as Alexander McQueen, Louboutin and Prada have become as desirable, if not more so, than high-heels. This evolution has allowed new players such as Golden Goose and Athletic Propulsion Labs to take centre stage.

Will luxury be able to keep pace with the rising cost of living?

A number of factors suggest that luxury goods could continue to prosper in an environment of high inflation.

1. “Cheap is Expensive”

A survey by Bank of America (2022) revealed that almost 40% of spending on luxury goods is by people earning $50,000 or less a year. This paradox can be explained by the younger generation's penchant for minimalism and their rejection of over-consumption, exemplified by the 'fast fashion' industry. These discerning luxury buyers place a high value on sustainability and are contributing to the growth of the sector by buying fewer items and embracing the second-hand market. The emergence of e-tailers such as ThredUp (USA) and Mercari (Japan) has increased the availability and accessibility of luxury goods.



2. The resilience of the high end

Luxury brands are mainly aimed at affluent consumers, who may be less affected by the rising cost of living than low-income consumers.

3. Exclusivity effect

Luxury brands often focus on the value for money of their products. They emphasise factors such as the use of craftsmanship, exclusivity and the overall experience associated with owning luxury products. This perception of quality can help sustain demand despite inflation. Consumers who perceive luxury goods as long-term investments may be more inclined to allocate their resources to this type of purchase. For the sector, this means maintaining a "scarcity effect" that can justify price rises.

The outlook for the luxury sector

The luxury market has seen a hyperpolarisation of its performance, with significant variations in growth rates and profit margins between different luxury brands and segments. In the future, the dominance of certain players in the sector will continue to depend on three key factors: the strength of the balance sheet, the resilience of the operating model (digital strategy, supply chain agility, distribution networks) and the ability to adapt in times of crisis.

The outlook for the luxury goods sector to 2030 is favourable. Solid fundamentals are expected to boost the value of the market from €353 billion in 2022 to €540 billion by the end of the decade, an increase of more than 50%.

Chinese and Asian consumers offer the most promising growth prospects and remain essential to the future of luxury goods. Although sales are down on 2021, the Chinese market is expected to recover by the second half of 2023. China is poised to overtake America and Europe to become the world's largest luxury market, accounting for 25-27% of global purchases. In India, the size of the luxury market is expected to increase 3.5-fold by 2030. Other countries in South-East Asia and certain African nations also have strong potential.

Web 3.0 (metavers, NFT, etc.) also offers new prospects for growth. Experiences 3.0", including virtual shops and digital shopping assistants, promise to redefine the concept of the consumer experience.

For further information

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