the sky is rising

SPECIAL REPORT

LUXURY GOODS

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Michael Masnick, Michael Ho, Joyce Hung

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OVERVIEW

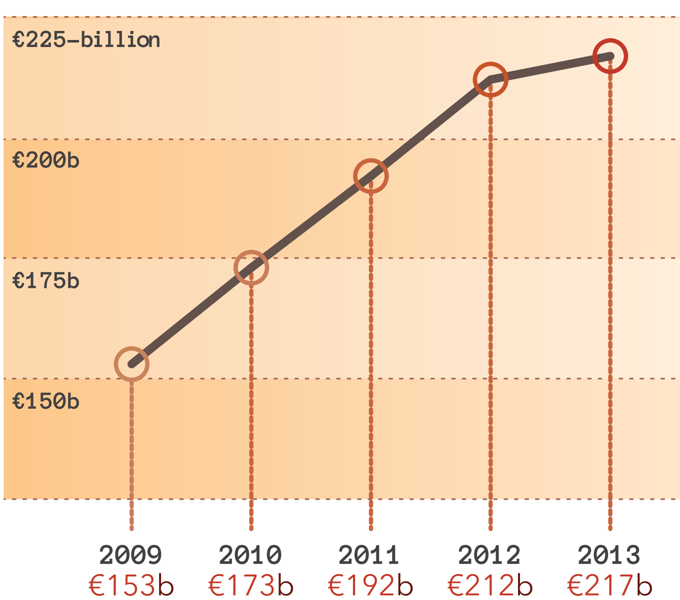
This is the third in our *Sky is Rising* series of papers, looking at data on specific industries that are being impacted by the internet. As with the previous two papers, which focused on various creative industries, this third paper looks at some industries where the stories being told about the economic impact of the internet have been quite mixed. Specifically, this paper looks at the impact on the luxury goods market. While, at first glance, this may seem like a shift from the previous papers, it fits in with the basic theme that a variety of industries are being impacted by the internet, and the full story about the impact is often not being told.

When it comes to the luxury goods market, we've certainly seen a fair amount of disruption in the market. The luxury goods market was traditionally defined by a small number of very high end players, who had tremendous control over their supply chains all the way down to the retail level. The internet has definitely shaken up that space and created new challenges for the luxury goods market, whether it was in allowing new entrants into the space, or breaking down some of the control over the supply chain and building up viable secondary markets.

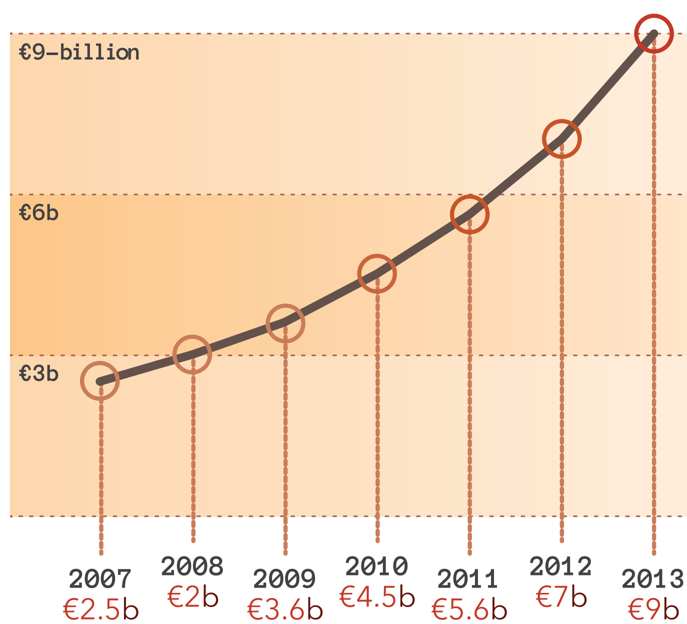
The main goal of this paper is to look at the internet's impact on the luxury goods market, and whether or not it's been beneficial or harmful. What we found is that, even with the global economic problems of the past few years, the luxury goods market is thriving — especially for brands who embraced the internet, digital marketing and innovation. Traditional players in the space who have adapted have seen tremendous success, and the opening of new opportunities and markets. Many new entrants have been able to jump-start their own offerings as well, and build up markets that were previously nearly impossible to enter.

On the whole, the luxury goods market has been growing worldwide. Even during the worst global recession in decades, the market grew from €153 billion (about $201 billion) in 2009 to almost €217 billion (about $285 billion) in 2013, a 42% increase, at a CAGR of 9%. While it's still a small portion of the total, direct online sales of luxury goods more than doubled from €2.5 billion (about $3.3 billion) in 2007 to €9 billion (about $11.8 billion) in 2013 at a CAGR of 24%.

LUXURY GOODS MARKET
» GLOBAL TOTAL



ONLINE LUXURY GOODS SALES
» GLOBAL TOTAL



Meanwhile there has been tremendous growth and opportunity in new markets. For example, the rise of China as a consumer of luxury goods has grown tremendously, nearly tripling from 2006 through 2010 — and online sales of luxury goods in China are a large and growing part of that market.

In nearly every part of the market we looked at, we found growth. The luxury fashion and accessories markets showed rapid growth over the past few years — with online sales a large and growing segment of the market. The jewelry market has practically doubled in just the past few years, and despite the depressed sales of cars during the recent recession, the luxury car market has seen solid growth as well.

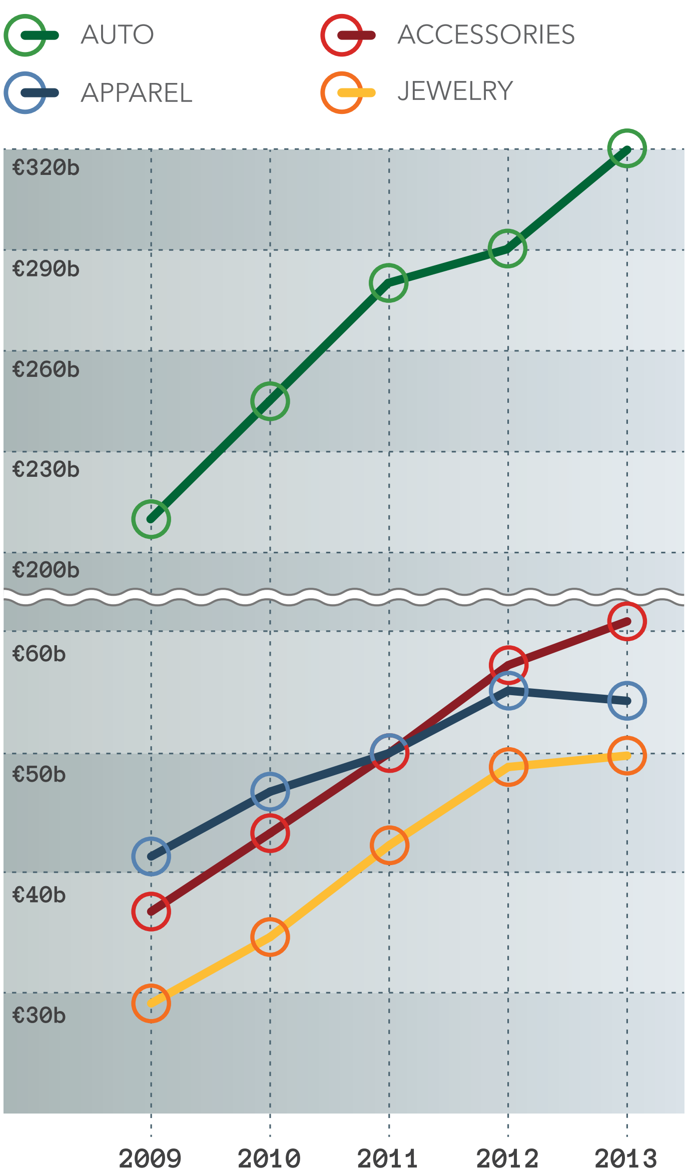
Much of this growth can be attributable to the internet. Internet companies that focus on luxury goods have seen rapid growth over the past few years. The amount of money spent online for luxury goods continues to grow at a rapid pace — and the majority of "newcomers" to the market now buy online.

The role of the internet in the buying of luxury goods is also complex, showing that the internet is a key part of the ecosystem. Even when buyers purchase luxury goods offline, the vast majority use the internet to get information about their purchase or to do comparison shopping.

Innovative e-commerce platforms like Kickstarter, Etsy, IndieGoGo, Amazon, and eBay — while not considered "luxury" platforms themselves — have also introduced some interesting online retail strategies that traditional luxury players could mimic, as they have enabled a growing number of upstarts to compete directly with traditional retailers without having to go through the long and involved process of setting up detailed retail networks and distribution partnerships.

Overall, the report will show how successful the luxury goods market has been over the past few years, and how the internet has been a key component to that success — creating greater awareness, greater opportunities to buy, more competition, valued innovations and much, much more.

LUXURY GOODS MARKET
» GLOBAL, BY SECTOR



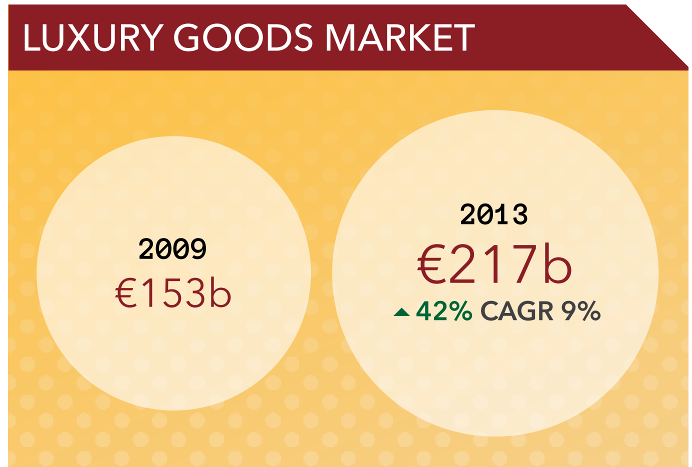
For the luxury goods market, **the sky truly is rising.**

MARKET TRENDS

Luxury is a relative term whose definition depends on what the user considers to be luxury. For example, a Rolex watch might be considered a high-end luxury item for the average consumer, while a wealthy consumer might consider it to be a normal everyday watch. However, most consumers typically perceive luxury products as being expensive, desirable, and non-essential items that possess attributes such as rarity, exceptional quality and craftsmanship, and exclusivity to the individual.

The total global luxury goods market has grown from €153 billion (about $201 billion) in 2009 to €217 billion (about $285 billion) in 2013 — a 42% increase at a CAGR of 9% — experiencing double-digit growth three years in a row, despite the economic recession. According to Bain & Co., the luxury goods market outlook in 2014 remains positive, despite the economic uncertainty, with expected growth rates of 4-6% in the Americas, 2-4% in Europe, 9-11% in Japan, 3-5% in the Asia Pacific region, and 2-4% in Mainland China. Driving the growth of the luxury goods market are the emerging middle class in developing markets and the growing number of millionaires. The aspirational masses in mature markets and the rising middle class in emerging markets account for more than half of the luxury market. Millionaires include "new money" and "old money" households, which make up 30-35% and 10-15% of the luxury market, respectively.

However, the recession has created a new kind of luxury consumer – younger, web-savvy consumers who know their way around the internet and are looking for good deals online. These newcomers make up 61% of luxury consumers and 36% of luxury spending, which is about the same amount of spending by traditional luxury consumers before the recession. Many luxury brands have yet to fully embrace an online sales strategy, and some have only been cautiously testing online sales, presumably to protect their brand prestige and historical sales, and because it would be difficult to adequately market the sensory aspects of their products online. However, as it turns out, the ones that have embraced the internet have been thriving.

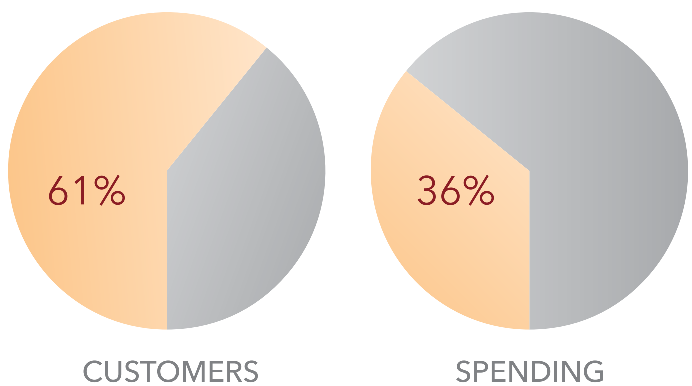


LUXURY NEWCOMERS

» AN EMERGING CONSUMER TREND

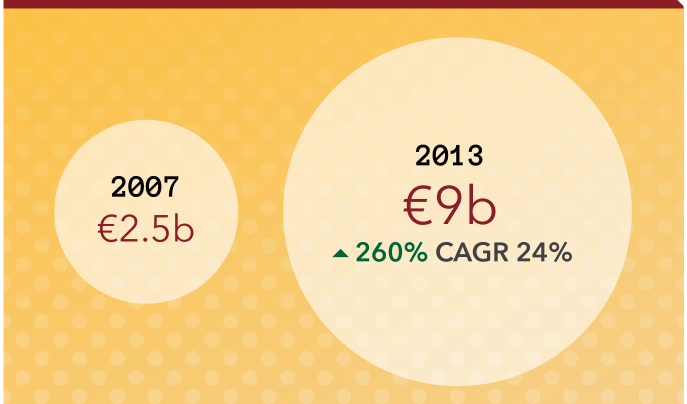
LUXURY NEWCOMERS

TRADITIONAL LUXURY CUSTOMERS



The luxury buying experience is changing — luxury consumers now care more about the product than the actual in-store buying experience, which in the past, was often considered more important than the product itself or the brand name. Today's luxury consumers want convenient shopping options and a product experience that feels upscale and exclusive. Luxury brands are finding that they need to adapt to consumers' changing shopping habits and expectations in order to stay competitive. According to a 2012 McKinsey survey, there are five strong trends in how luxury consumers shop online: they want personalized offers; they expect exceptional service, such as fast and easy checkout and same-day delivery; they look for trustworthy product information; they want instant gratification; and they want an online shopping experience that compensates for the lack of human interaction and being able to touch and feel the products. It used to be that luxury consumers would dress up, walk into a store and buy things based on the trusted expertise and advice of the sophisticated retail salespeople, but now consumers are turning to product reviews from unbiased experts online to help them decide what to buy – in the comfort of their own home.

ONLINE LUXURY SALES



FAST FACTS & FIGURES

87% year-over-year growth experienced by luxury pure-play online retailers in 2010

50% of online luxury goods sales are for full-price products

69% of luxury consumers find online shopping more convenient

91% of millionaires would prefer their favorite brands be online

78% of wealthy consumers participate in social networking websites

50% of wealthy consumers use social networking to connect with a brand

65% of wealthy consumers believe brands with no social networking presence are out of touch.

92% of luxury consumers use the internet to search for information about a product before buying

A 2013 Google/Ipsos study found that luxury buyers find shopping online more convenient (69%), and they like that it can be anywhere, anytime (60%). Other reasons for why consumers are increasingly turning to online shopping include web exclusives, online-only deals, more inventory, more product options, and no sales taxes. Furthermore, since shoppers can often return online purchases to physical retail locations, or return them for free by mail, there is less of a barrier to buying online. In fact, many online retailers, such as Nordstrom, Zappos, and Amazon, typically have very liberal return policies to encourage otherwise hesitant shoppers to buy online. However, brick-and-mortar stores are still relevant, since they provide immediate delivery and account for a significant portion of luxury sales, and because many shoppers still want to touch and feel the products before buying. While shoppers are increasingly choosing to buy online instead of in-store, luxury brands now have the opportunity to engage consumers through digital channels to inform them about their brand and products, offer personalized services, and provide a convenient way for consumers to buy exactly what they want without the hassle of the traditional luxury buying experience.

U.S. retail online sales increased at a CAGR of 30%, from $5 billion in 1998, to $135 billion in 2007, to $256 billion in 2013. Global online sales of luxury goods almost tripled from €2.5 billion (about $3.3 billion) in 2007 to €9 billion (about $11.8 billion) in 2013 at a CAGR of 24%, with luxury pure-play online retailers experiencing 87% year-over-year growth in 2010. In fact, more than 50% of online luxury goods sales were for full-price products, refuting the long-held belief that most online sales would be for discounted goods. Contrary to some expectations, 94% of millionaires say that selling luxury goods online wouldn't affect their opinion of the product or brand, and 91% say that they would like to have their preferred luxury brands available online.

It's becoming increasingly important, if not essential, for luxury brands to establish a powerful online presence in order to remain competitive. About 70% of households in the U.S. have broadband access, with more possibly using internet at work, and others using their mobile phones instead to access the internet. The global online population, which was 1.6 billion in 2009, will be 2.3 billion by 2014. Luxury shoppers spend a lot of time online. According to L2 Think Tank, 78% of wealthy consumers (those with an annual household income of at least $150,000) participate in social networking sites, with more than 50% using social media to connect with a brand, and 65% believing that brands that have no presence on social networking sites are out of touch. A 2013 Google/Ipsos study found that more than 90% of luxury buyers research products both online and offline before making a purchase. In particular, in the new markets, 92% of luxury consumers used the internet to search for information about a product before buying. The study also found that 98% of affluent consumers use the internet every day, and that they use an average of three connected devices (e.g., laptop, smartphone, tablet) to do online research. They even multitask, researching products using their connected devices while watching TV or reading a magazine. While 82% of luxury purchases still happen in-store — 69% of shoppers want to touch and feel products before buying — 78% of affluent consumers research products online before going to a physical store to make a purchase. These Research Online Research Offline (ROPO) sales are often overlooked. In fact, U.S. online retail sales totaled $252 billion in 2010, while ROPO sales totaled $482 billion. Online luxury goods sales through Rakuten LinkShare UK increased 96% from 2011 to 2012, and clicks across the network were also up 37%, suggesting that consumers are spending more time researching products online before buying.

» CONSUMER TRENDS

WHY PEOPLE BUY ONLINE

A study from the first quarter of 2013 by Martini Media showed that affluent consumers were 47% more likely to buy online, compared to consumers with a household income of less than $100,000 a year, and they were 74% more likely to buy products from a luxury retailer's website. The findings further reinforce previous data showing that being digitally connected is important to affluent consumers. In fact, affluent consumers like to buy all sorts of goods online – even ordinary things, such as event and movie tickets.

So, why do people choose to buy online instead of at brick-and-mortar stores? A recent survey of more than 25,000 consumers by Shopper Approved, conducted right after they made a purchase online, asked them "What key factor influenced you to buy online instead of locally?" The top three reasons why people preferred to buy online: larger selection (25.4%), better pricing (25.0%), and more convenient (24.7%). Similar results were also found in a recent study by Shullman Research Center, which reported that affluent consumers cited better prices (30%) and convenience (27%) as their top reasons for shopping online. Another recent study by Simon-Kucher & Partners also found that lower prices, better selection, and fast shipping were the primary motivators for buying online.

Consumers in the Shopper Approved survey also chose the following reasons for buying online: other (10.7%), time savings (7.2%), easy to compare (3.6%), and no sales tax (3.3%). Surprisingly, "no sales tax" was the least important reason for people's decision to buy online, debunking the claims — by proponents of legislation that would require internet retailers in the U.S. to collect sales taxes on online purchases — that shoppers buy online mainly to avoid sales tax. It turns out that 83% of online purchases are made from Big Box stores, which already collect sales tax on online purchases because they have a physical presence in many, if not all, U.S. states. Considering online sales make up less than 6% of all U.S. retail purchases, that means only about 1% of all retail sales are made without collecting tax online.

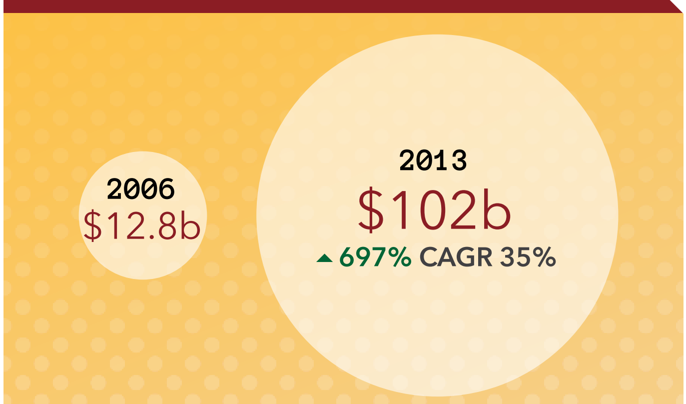
It's clear that most consumers are comfortable researching and purchasing products online, so luxury brands should continue to increase their digital presence and marketing efforts, focusing on improving in the areas of selection, pricing, and convenience to attract more customers and encourage more online purchases.

Mobile commerce is also becoming more popular. According to ABI Research, more than a third (35.4%) of the consumers it surveyed in 2011 owned three or more mobile devices, including smartphones, tablets, and portable media players. In 2012, 15 million consumers made purchases on their mobile phones each week. According to Branding Brand, 39% of traffic to the Top 500 e-retailers came from smartphones in 2013, and smartphone use is growing so rapidly that by 2014, more than half of traffic to these online stores will be coming from mobile phones. According to Forrester Research, retail sales in the U.S. made from smartphones reached $8 billion in 2012 (3% of total e-commerce sales), and they're expected to continue increasing in the next five years. eMarketer reports that mobile commerce sales (smartphone and tablet) were up 82% in 2012 to $24.8 billion (11% of total e-commerce) and continued to increase in 2013. Rakuten was already reporting that 19% of its sales were coming from mobile devices in late 2009. According to comScore, some of the major reasons consumers buy via mobile commerce include: on-the-go convenience (63%); special offers/coupons (52%); easy to compare prices, find the best deal (48%); and they're in the store and the product isn't available (41%). PayPal reports that consumers aren't just buying ordinary things like books and CDs from their smartphones, they're also buying more expensive items like diamond jewelry.

According to a study by the Luxury Institute, 76% of wealthy consumers compare prices using mobile devices, and 27% have actually made purchases using a mobile device. Additionally, 21% will look up product information while shopping in stores. Mobile can enhance the traditional shopping experience. For example, department store chain Bloomingdale's created a mobile application that allows consumers to view additional product information and read reviews with an in-store bar code scanner. According to Jordan Phillips, the founder of Lure of Luxe, consumers don't think of mobile shopping as a different experience from e-commerce – it's just a different way of buying. In the future, "mobile" won't be just a buzzword, it's just going to be another important way for people to buy things. This is especially relevant in emerging markets where mobile phones are bridging the digital divide, providing internet connectivity to people who otherwise wouldn't have access, and giving them the ability to conduct financial transactions using their mobile phones.

China is set to become the world's largest consumer market for luxury goods. The Chinese gross domestic product is growing at a rate of almost 10% per year, and the number of billionaires in China doubled from 2009 to 2010. According to Boston Consulting Group, there are 700,000 households in China with assets worth more than $1 million, and they control 48% of the country's wealth. As incomes continue to rise in China, the demand for luxury goods in the country will also increase. Total retail spending on luxury goods in China has increased almost eightfold from $12.8 billion in 2006 to $102 billion in 2013, at a CAGR of 35%. In 2010, 49% of Chinese consumers spent more than 11% of their salary on online purchases. In response to a survey question about why they shop online, 78% of Chinese luxury consumers said they shop online to avoid salespeople, compared to 46% of Americans and 56% of Europeans. A majority of Chinese luxury buyers (78%) like to research online – particularly through blogs and social media — before making a purchase in-store, as evidenced by ROPO sales which totaled $96 billion in 2010, compared to online sales which totaled only $10 billion. China's online luxury sales are estimated to be worth $27 billion

CHINESE LUXURY SPENDING



FAST FACTS & FIGURES

49% of Chinese consumers spent more than 11% of their salary online in 2010

78% of Chinese luxury consumers said they shop online to avoid salespeople, compared to 46% of Americans and 56% of Europeans in 2013, which is still only a fraction of the total e-commerce market in China ($296 billion in 2013). As a consequence, new companies are emerging to cater to Chinese luxury consumers. For example, New York-based Bomoda curates content about luxury goods and lifestyle in Mandarin Chinese.

Curated shopping sites are growing in popularity as luxury consumers seek personalized product recommendations from expert stylists, trendsetting celebrities, and the social web community, instead of spending hours searching through an endless selection of products. As Fashionising.com puts it, in a world where the average consumer can afford a massive yet fashionable wardrobe, curated products are the new luxury. Luxury brands can benefit greatly from social sites that curate luxury goods to make meaningful connections with consumers that will ultimately lead to a greater consumption of luxury goods.

» CONSUMER TRENDS

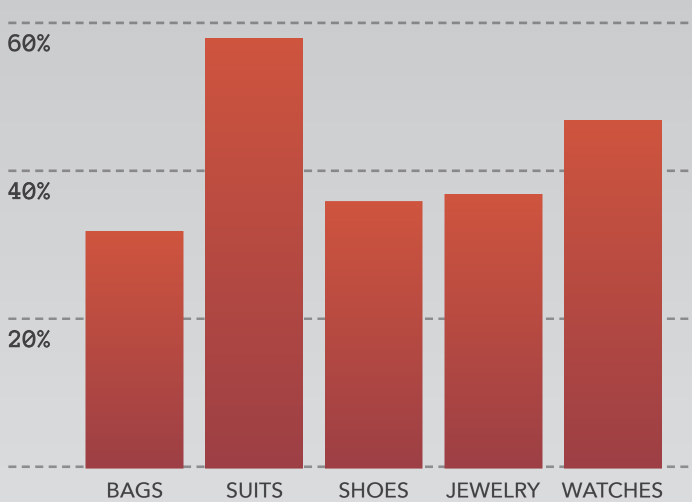
CHINESE LUXURY CUSTOMERS WANT THE REAL THING

Since luxury goods can be up to 40% more expensive in China, many Chinese luxury consumers are buying from their favorite brands abroad, according to McKinsey's 2012 Chinese Luxury Consumer Survey. In fact, more than 50% of Chinese luxury spending takes place outside of China. Even though every major luxury brand has a brick-and-mortar store in China, it appears that the convenience of having a physical store near to where they live and work just isn't as much of a draw as it used to be.

Meanwhile, online sales of luxury goods in China increased by 71% from 2011 to 2012. Bain & Company reports that China's e-commerce market has grown at an average rate of 71% from 2009 to 2012 (compared to 13% for the U.S.), and is expected to exceed $500 billion by 2015. However, considering China is well-known for counterfeiting luxury goods, it's not surprising that Chinese consumers themselves are wary of buying luxury goods when they can't be sure of their authenticity. A 2011 survey by China Market Research found that 95% of young Chinese women would be embarrassed to own a counterfeit handbag. While the counterfeit market still exists – Chinese authorities seized over $800 million in counterfeit goods in 2011 – Chinese consumers are increasingly unwilling to buy fake products. Women's luxury fashion group Escada found a significant decrease in Chinese consumer willingness to buy fake goods, from 31% in 2008 to 12% in 2010.

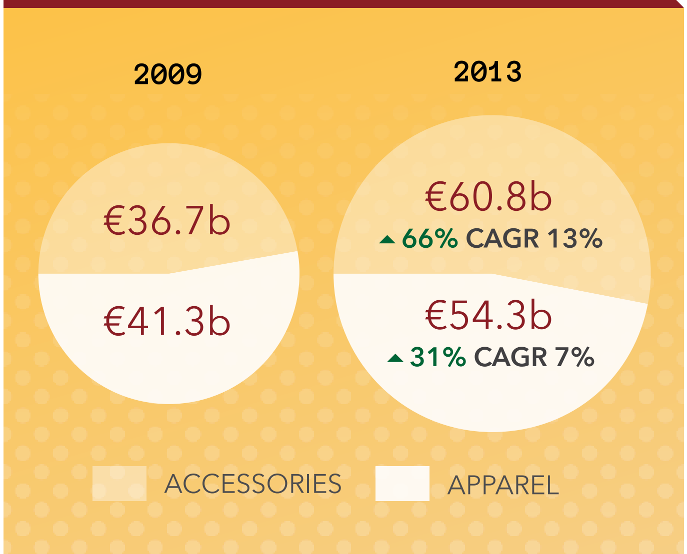
Chinese consumers do a lot of research on luxury goods online, and those who do shop online (70% of them) are looking to find better prices on luxury items — closer to what they would pay overseas — reporting average savings of 32% on bags, 58% on suits, 36% on shoes, 37% on jewelry, and 47% on watches. It's also clear that Chinese consumers are willing to make big-ticket purchases online. For example, in 2012, Chinese consumers snapped up 300 limited edition Smart cars (priced at around $24,000) in just 1.5 hours, as part of an exclusive online flash sale. Simply building brick-and-mortar stores just isn't cost effective and doesn't take into account China's changing commercial landscape. According to iResearch and Bain & Company, China became the largest e-commerce market in the world in 2013, with a market size of $215 billion. In order to continue to grow and reach all Chinese consumers (not just those in big cities like Beijing and Shanghai), luxury brands need to embrace the online sales channel and deliver exceptional and meaningful customer experiences to further distinguish their products.

ONLINE SAVINGS IN CHINA



LUXURY FASHION

LUXURY FASHION MARKETS



The global luxury apparel market grew from €41.3 billion (about $54.3 billion) in 2009 to €54.3 billion (about $71.4 billion) in 2013, a 31% increase at a CAGR of 7%, while the global luxury accessories market grew from €36.7 billion (about $48.3 billion) in 2009 to €60.8 billion (about $80 billion) in 2013, a nearly 66% increase at a CAGR of 13%. Consumers are not only researching luxury fashion online, they're also buying more online. U.S. retail online sales of all apparel and accessories have grown from $28 billion in 2010 to $44.7 billion in 2013, a 60% increase at a CAGR of 17%.

Euromonitor predicts that 40% of the world's population will be online in 2020 – that includes 281 million internet users in the United States and 711 million internet users in China. Today, luxury goods companies that are embracing the internet, digital marketing, and innovation are thriving despite the recession. As consumers are increasingly willing to buy even the most expensive products online, from the convenience of their homes, traditional luxury brands are beginning to change their attitudes, and those that have adapted are doing better than they could have imagined.

Oscar de la Renta CEO Alexander Bolen has expressed surprise at the success of their online experiments. In one instance, a new customer bought an $80,000 sable coat online, and customers are regularly buying the brand's core product online – $4,000 cocktail dresses. Bolen says the company sees creativity as a competitive tool and isn't afraid to innovate or experiment or fail. It was one of the first brands to use Facebook commerce with its exclusive product-of-the-month offers. In one experiment, Oscar de la Renta had an exclusive deal with social photo sharing webstore TheFancy.com (sometimes referred to as "Pinterest for shopping"), where Fancy took advance orders for a $2,490 sweater that would be showcased at an upcoming fashion show. Within 24 hours of the show, more than 500 people had clicked on a photo of the sweater on Fancy, and five of the sweaters had been sold. Oscar de la Renta now has its own dedicated team to handle all things digital, and has big plans for future online sales.

Gucci saw a 30% increase in online sales from 2011 to 2012 despite the economic uncertainty, and its Interbrand Brand Value has more than doubled from $4.7 billion in 2004 to $10.1 billion in 2013. The Interbrand Brand Value is the estimated value of a brand based on the financial performance of the brand, the role of brand in the purchase decision process, and the strength of the brand, as determined by Interbrand, the world's largest brand consultancy. In 2011, Gucci launched its first click-to-buy video where viewers could scroll over products in the video and click to buy them, satisfying the luxury consumer's desire for instant gratification through digital sales channels. The brand operates its e-commerce site in 27 countries, and in early 2013, it launched its first mobile site. Half of Gucci.com's traffic comes from people on mobile devices. Twice as many luxury consumers are using their smartphones to shop, compared to regular consumers, and they're using the mobile sites to enhance their in-store shopping experience. Since the launch of the new mobile site, Gucci's revenue has grown by almost a factor of four. The mobile site, which already accounts for 13% of total online revenue, was created to meet the growing demand for customers being able to browse and purchase the brand's products anytime, anywhere on their mobile devices.

Louis Vuitton has been doing exceptionally well. It's one of the few luxury brands that offers nearly all of its products online, and it has created a successful luxury shopping experience through Facebook with its Mon Monogram app, demonstrating that luxury brands can indeed preserve the feel of an exclusive shopping experience and their aspirational brand image online. The Mon Monogram app allows users to fully customize a bag with hand-painted personal initials and stripes in various colors and directions, then it prompts them to visit the Louis Vuitton online store to buy their customized bag. According to the brand's communications director Antoine Arnault, online sales bring in as much money as one of its largest physical stores. Its Interbrand Brand Value has more than tripled from $6.6 billion in 2004 to $24.9 billion in 2013.

» CHANGING MARKETS

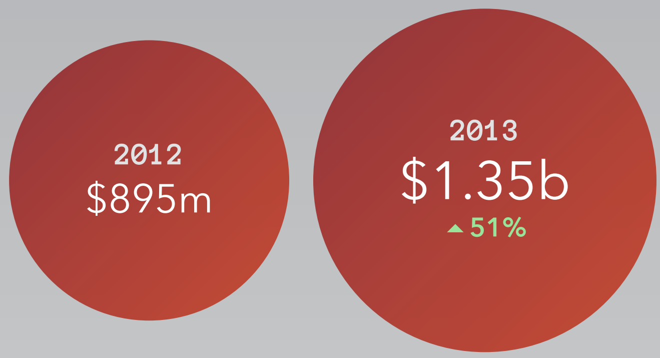
THE ETSY ECONOMY

Etsy, the online marketplace for unique handmade and vintage goods, has been growing at an impressive rate since it launched in 2005 as a small, niche startup. While Etsy isn't considered a luxury platform, it has the potential to change the way consumers think about luxury and exclusivity. It has already helped generate many opportunities for new online businesses, some of which do specialize in selling luxury items, such as handcrafted leather handbags, as well as others that sell high-quality, exclusive, and custom-designed products that consumers won't find at a store.

Founder Rob Kalin was an artist who was looking for a place to sell his own works, after he tried eBay and realized his art wasn't a good fit there. So he created Etsy as an online place for others like himself to sell their own creative works. It has since turned into a leading social commerce company, with its 22 million members selling $1.35 billion in merchandise in 2013, up from $895 million in 2012 (a 51% increase). Jewelry remained the top selling category in 2012, but other products like clothing, wedding goods, and home decor are also growing strongly, with furniture being the fastest-growing category.

Part of Etsy's growth can be attributed to sellers promoting their shops on social media -- Etsy is now the top pinned site on Pinterest -- but also, consumers are looking for more personal shopping experiences, which giant e-commerce sites like Amazon.com just can't provide. Etsy has also benefited from eBay's loss of focus on smaller sellers, as it operates as kind of a "niche eBay" for arts, crafts, furniture, and

ETSY MERCHANDISE SALES

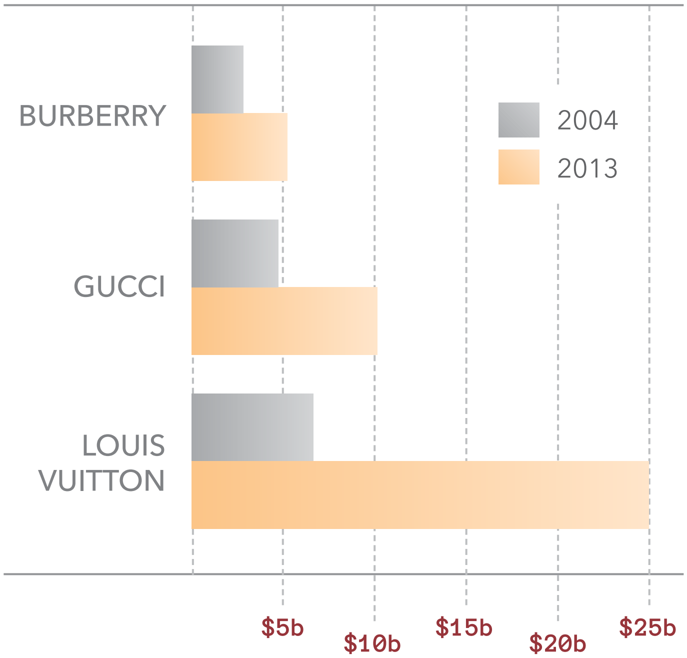


design. Etsy makes it easy for entrepreneurs to start a small business. Compared to eBay, there's a much lower cost of entry – sellers pay $0.20 to list an item in their shop, and if it sells, Etsy takes a 3.5% cut. However, eBay recently rolled out a new fee plan, giving sellers 50 free item listing per month, but taking a 10% cut on the sale price if an item sells.

According to CEO Chad Dickerson, the company wants to create an "Etsy economy" – a people-powered economy with person-to-person commerce -- where online shopping feels more like a farmer's market than a supermarket. Going forward, Etsy is increasing its efforts to support new business owners, such as teaching entrepreneurship skills to residents of local communities, and connecting its members with buyers from brick-and-mortar retailers, such as Nordstrom, to help them sell wholesale. By focusing on helping small, niche sellers succeed, Etsy is quickly growing to become the marketplace for selling exclusive goods.

LUXURY BRAND VALUE

» AS DETERMINED BY INTERBRAND



British fashion house Burberry has been ranked at the top of L2 Think Tank's Digital IQ Index, which ranks fashion brands based on their online competence. Burberry's online sales increased by 30% from 2010 to 2011. In 2012, it opened a technologically-advanced store in London that was designed to be a physical expression of its website, Burberry.com, combining bricks-and-mortar retailing with digital technology. In an effort to create a more customer friendly shopping experience, Burberry's new store promotes a less intimidating retail environment than is typical for luxury goods stores. Its Interbrand Brand Value has almost doubled from $2.8 billion in 2006 to $5.2 billion in 2013.

There have also been many innovative luxury fashion startups that have emerged to take advantage of the online sales channel. NET-A-PORTER, an online luxury retailer owned by Swiss luxury conglomerate Richemont, has seen its annual sales grow from £11.8 million (about $18.4 million) in 2005 to £368 million (about $575 million) in 2012, a 20-fold increase at a CAGR of 53%. In 2011, it acquired the Chinese discount online retailer Shouke, and relaunched it in 2012 as the Chinese version of designer discount store the Outnet, marking its first entry into China's luxury market. Most recently, it set up new automated distribution centers in Britain, the U.S., and Hong Kong, and launched French, German, and Mandarin Chinese versions of its website. Asian online shoppers make up one third of NET-A-PORTER's customers.

Yoox, an Italian online luxury fashion retailer, has seen its revenues grow from €291 million (about $383 million) in 2009 to €456 million (about $600 million) in 2013, a 57% increase at a CAGR of 12%, with growth strongest in Asia and North America, its top market. Yoox designs and manages online stores for more than 30 fashion and luxury goods brands. In 2013, the average number of unique monthly visitors to the company's websites increased more than 25% to 13.2 million, the number of orders increased more than 13% to 2.8 million, and the average order value increased more than 15% to €215 ($283). It also reported that 25% of holiday traffic to its website came from mobile devices. The Chinese version of Yoox.com was also launched in 2012.

Aided by the recession, flash sales sites have grown significantly in the past few years, helping luxury brands move excess inventory at discounted prices, and catering to web-savvy luxury newcomers. There's an addictive quality to these sites that makes shopping more exciting, as they offer deals on high-end or rare items for only a limited time — shoppers feel the need to act on the purchase right away and then enjoy a feeling of euphoria when they snap up a great deal. Founded in 2001, Vente Privee was one of the very first members-only luxury flash sales sites on the web, inspiring a whole generation of similar exclusive luxury flash sales sites like Gilt Groupe, One Kings Lane, and Rue La La. Gilt Groupe has seen its revenues grow from $25 million in 2008 to $580 million in 2012, a 23-fold increase at a CAGR of almost 120%. Five years ago, the New York startup transformed the online retail market for fashion by offering limited-time, members-only "private sales" for designer fashion at significantly discounted prices. It rose to dominate the American private sales landscape, capitalizing on the huge inventory surplus of designer goods following the onset of the recession. However, these days luxury flash sales sites aren't doing quite as well as they used to due to an over-saturation of players in this market. Nevertheless, companies like Gilt are continuing to innovate, experimenting with technology to make their limited-time-only offers more effective. For example, Gilt has started offering exclusive mobile-only sales, which create an extra level of excitement that gets customers returning at a very high rate. Now 40%

of Gilt's total revenue comes from mobile commerce. It has also launched a personalization feature called Your Personal Sale, where members are offered a unique new sale every day that's curated with their favorite brands and styles, based on their shopping behavior, personal preferences, and browsing history. Both the Gilt website and the mobile app feature "Your Personal Sale" badges to highlight the special offering among the other sales.

Going forward, luxury fashion brands are not only improving their online presence and digital marketing efforts, they are also increasingly diversifying into hard luxury (jewelry, watches) to capitalize on untapped opportunities, with the goal of penetrating all luxury goods categories at all price points.

» CHANGING MARKETS

THE DISRUPTION THAT IS CROWDFUNDING

It would be difficult to write a report about the impact of the internet on luxury goods without looking more closely at the meteoric rise of crowdfunding as a means for raising money, verifying demand and drawing marketing attention to new products. While there were a few earlier attempts at crowdfunding and even some very similar platforms, most people recognize that crowdfunding really began to "catch on" with the rise of Kickstarter, which launched in the spring of 2009. While Kickstarter is the most recognized crowdfunding platform in the market, there are many other players, with IndieGoGo often being discussed as a popular alternative. There are also numerous smaller players, some of whom are targeted towards specific verticals or styles.

The basics of crowdfunding are well-known at this point. Someone with a project they're working on launches a campaign, in which they describe what they're working on and then offers various "tiers" at which supporters can provide money to the project creator, in exchange for something of value. With many (though not all) crowdfunding projects, a "target" total is set, and if the project fails to reach that amount of pledged money, no funds are given, so the risk for supporters is lower. Some platforms, like IndieGoGo also do allow campaigns that will collect all money pledged, whether or not it reaches the goal.

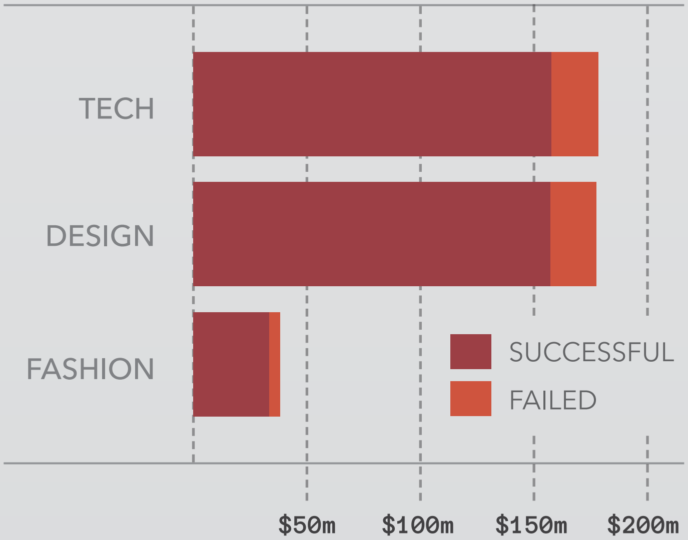
The different rewards can vary greatly depending on the type of project, but when it comes to hard goods, most of the rewards tend to focus on getting the actual good. Usually, the funds are used to cover the costs of supplies and manufacturing, so there is frequently a time lag (sometimes a significant one) between people paying and the product actually being delivered. In many ways, people are signing up to pre-purchase the goods being offered. There is, of course, some risk associated with this (the product might never be delivered, for example), and Kickstarter has tried to be increasingly explicit that it is "not a store," but rather a way to support a project.

While neither Kickstarter nor IndieGoGo directly break out "luxury" goods, it's quite clear that luxury goods have found a home on these platforms, often allowing new entrants and upstarts to get word out about their product -- and also to conduct a form of real-time market research prior to actually spending on supplies and production. In fact, it's been reasonably argued that projects that don't reach their targeted pledges should not be seen as "failed campaigns," since it would be a much larger failure if the creators had spent money on supplies, production, and distribution only to find out later that there was insufficient demand.

Both Kickstarter and IndieGoGo have extremely busy and successful "design" categories, in which many luxury goods are offered. Kickstarter's statistics show that design projects have successfully raised nearly $100 million dollars across 5,000 projects, with nearly 40% meeting their goals. About 200 projects have raised over $100,000 (and six have raised over $1 million). In the technology category, approximately 3,000 projects have been launched, with about 35% reaching their goal, bringing in over $80 million. Nearly 200 projects have raised over $100,000, and around 10 have broken $1 million. The fashion category has also seen over 4,000 projects, with about 30% reaching the target amount, bringing in a bit over $20 million. About 25 have raised over $100,000, and just one (so far) has broken $1 million.

IndieGoGo doesn't break out its stats, though some re-

KICKSTARTER SUCCESS
» LIFETIME FUNDING TOTALS AS OF Q3 2014



ports suggest much lower rates of projects meeting their goals. As IndieGoGo notes, such comparisons are not quite fair, given the very different nature of the platforms, the fact that some IndieGoGo users run plenty of "test campaigns" to see what resonates, and, importantly, the fact that IndieGoGo allows campaigns that don't reach the target amount to still get the money.

While the numbers may look small compared to some traditional luxury brands that will blow millions of dollars on a marketing campaign for a new product, it's important to recognize that all of this has sprung up in just a few years, and the rate of growth has been incredible. Kickstarter went from $27 million raised in 2010 to $283 million in 2012, and $480 million in 2013.

Among other things, what Kickstarter has demonstrated is that it's possible to launch a new product with much less funding than was traditionally necessary. This is, in part, because crowdfunding removes a large element of risk. You don't necessarily need to spend the resources if the demand isn't there. That allows companies to more accurately project necessary resources and expenses, and allows for many more niche products to exist and thrive within the right context.

One example is the Pebble smartwatch. While some might not consider the Pebble smartwatch to be a true "luxury" good, the success of its crowdfunding campaign on Kickstarter is instructive in how a previously unknown upstart can catapult into being a leader in the field. For years, the smartwatch market had been predicted with frequent regularity, only to flop when products were actually introduced. Microsoft, famously, had entered the market in a big way in 2004 with SPOT (Smart Personal Object Technology) smartwatches only to find that the demand for their offerings was minimal. That effort was shuttered in 2008, having failed to catch on.

Given that, it's quite impressive that when the Pebble launched on Kickstarter, it wasn't even clear that there was a significant market for such a product. In fact, Pebble's founder admitted that venture capitalists had refused to fund the company. However, support on Kickstarter poured in at a record rate, as something about the basic simplicity of the watch, combined with the somewhat viral nature of Kickstarter itself, quickly turned the Pebble into Kickstarter's most funded project ever -- a title it still holds today, nearly two years after the campaign. The campaign reached $100,000 in 2 hours, $1 million in 28 hours, and stopped taking new orders when there was still a week left in the campaign period. They had so many orders that they worried about meeting the demand (and, in fact, production and shipping of Pebbles ended up being delayed several times, much to the chagrin of some buyers).

Overall, though, the story of the Pebble showed how a previously unknown upstart, which couldn't secure traditional funding, was able to jump into a market and raise $10,266,844 from 68,928 supporters, thereby guaranteeing demand for the product, as well as creating a form of a marketing "event" that got people excited to contribute money, even though the product wasn't ready yet. It's become clear that new crowdfunding platforms have helped to open up opportunities for upstarts to create a strong focus that can allow them to leapfrog into the public consciousness with premium products, even ahead of giant traditional companies.

However, crowdfunding isn't the only new business model that has appeared online -- the rise of person-to-person sales, flash sales, group buying, 3D printing, and a variety of other new ways of hard goods sales and production are reinventing what it means to be a producer and seller of hard goods today, and it seems likely that we'll see many other models and concepts in the years and decades to come. Nevertheless, the rapid success of crowdfunding is an important trend to watch, in seeing how new concepts can become reality where they almost certainly would never have gone beyond the mental drawing board in the past.

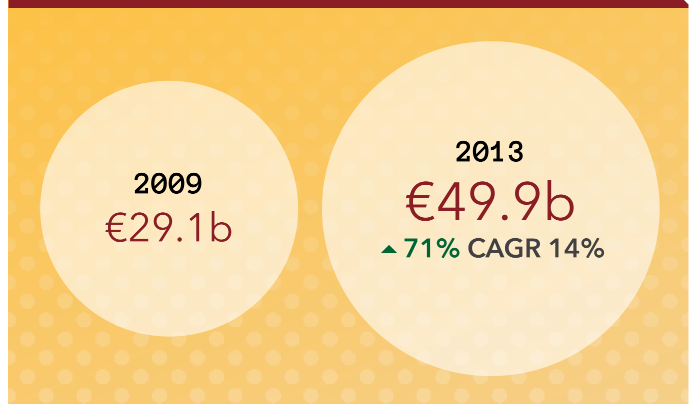
HARD LUXURIES

The global market for luxury watches and jewelry grew from €29.1 billion (about $38.3 billion) in 2009 to €49.9 billion (about $65.6 billion) in 2013, a 71% increase at a CAGR of 14%. In particular, the global diamond jewelry market has grown from $56 billion in 2000 to $72 billion in 2012, a 28% increase at a CAGR of 2%. According to data from the Antwerp World Diamond Center, the average price for a 1 Carat D Loupe Clean wholesale diamond has increased 10-fold from $2,700 in 1960 to $28,400 in 2013. Despite the recession, the diamond industry has been doing very well, and overall demand for diamond jewelry has been growing.

Demand for diamonds is growing fastest in China and India, as wealth increases in both countries. China, which is now the world's second largest diamond jewelry market after the United States (U.S. market was $26.9 billion in 2011), has seen it grow more than 30% per year, from about $2 billion in 2005 to $9.2 billion in 2011. Internet sales of diamonds in China are still only a small percentage (2%) of total diamond sales, but they're expected to take off in the next five years as companies like vertical B2C diamond retailer Kela.cn invest heavily in e-commerce efforts. CEO of Kela, Guo Feng, has said that he expects giant online diamond resellers to emerge in China in the next 3-5 years, with some of them possibly even surpassing traditional sales channels. Kela reported more than $96 million in sales in 2011, and the company has grown more than 220% each year since it was founded in 2007.

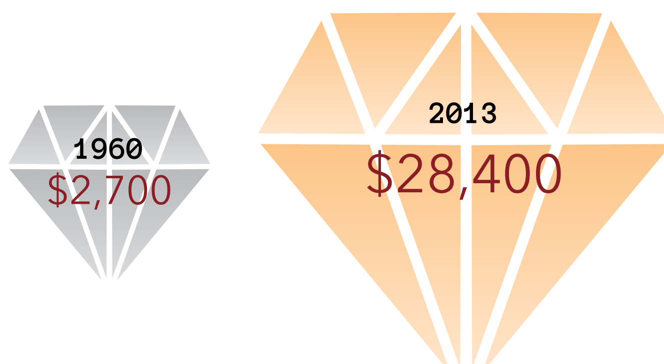
The U.S. diamond market makes up 40% of global demand, largely due to the marketing efforts of De Beers, with its unforgettable "A diamond is forever" slogan, which convinced Americans that diamonds were the ultimate symbol of love. More than 80% of American women now receive diamond rings when they get engaged. De Beers has continued to stimulate consumer demand for diamonds by coming up with innovative ring designs, such as the "Eternity Ring" in 1970, or more recently in 2012, the "Center of My Universe" ring. De Beers created De Beers Diamond Jewellers, a joint venture with Louis Vuitton Moet Hennessy (LVMH),

WATCH & JEWELRY MARKET

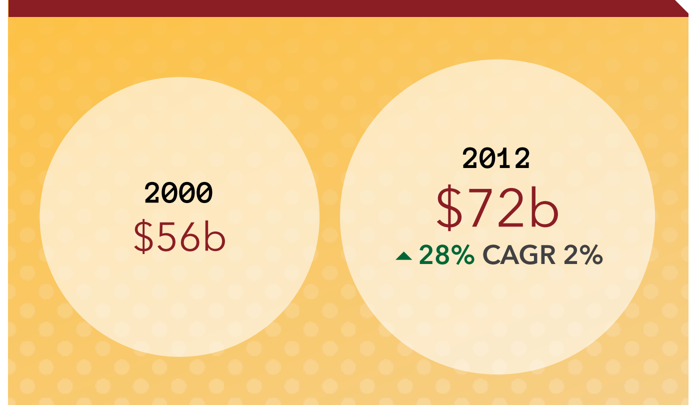


WHOLESALE COST OF A DIAMOND

» BASED ON A 1-CARAT D LOUPE CLEAN



DIAMOND JEWELRY MARKET



in 2001 to sell diamond jewelry. De Beers opened its first online store in the U.S. in 2007, offering a wide range of its product line, with the goal of generating revenue online and increasing visits to its retail locations. Diamond sales in the U.S. have slumped since the recession, but they're recovering, and diamonds still rule the U.S. jewelry market, accounting for about 50% of revenues.

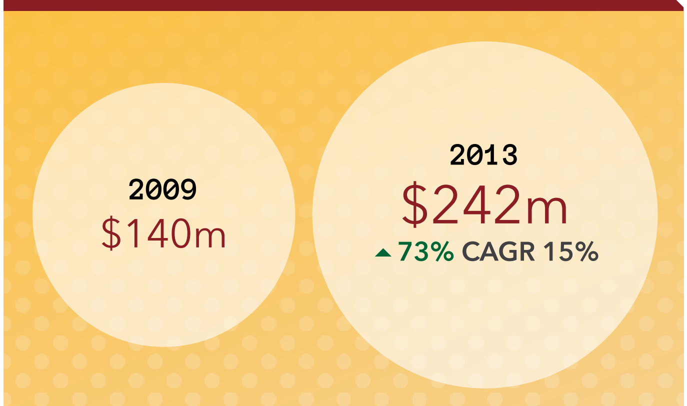
Tiffany & Co., one of the largest online jewelry retailers, has seen its online sales grow from $140 million in 2009 to $242 million in 2013, a 73% increase at a CAGR of 15%. The company has also been recognized by Internet Retailer as having one of the most innovative e-commerce sites. The internet is becoming a growing priority for the company. It already operates e-commerce sites in 13 countries, and online sales make up about 6% of its worldwide sales of $3.79 billion, growing 4% in the past year. Soon, Tiffany plans to launch a redesigned website that will take advantage of recent changes in the digital landscape, including social media and the increased use of mobile devices. Tiffany's Interbrand Brand Value has increased 50%, from $3.6 billion in 2004 to $5.4 billion in 2013.

Cartier, which has been stepping up its efforts to incorporate digital elements into its marketing strategy, has exceeded the expectations of analysts, making $2.65 billion in annual profits despite the economic downturn. Part of its success has been in creating an experience around the brand that combines both the physical and the digital. For example, it has been using videos to create unique, immersive experiences alongside displays of iconic and new jewelry designs. It has also launched a new e-catalog that engages customers with its rich storytelling in a modern form. Cartier's Interbrand Brand Value has more than doubled, from $2.7 billion in 2004 to $6.9 billion in 2013.

While Amazon.com isn't a luxury retailer, it has been successfully selling diamond jewelry online, experimenting with different ways to engage its customers. In 2006, Amazon's sales of jewelry and watches increased more than 100% year-over-year. Its "Create Your Own Ring" feature proved popular with consumers, as its custom-built engagement ring sales increased 254% year-over-year. In 2008, Amazon reported that its retail diamond sales increased more than 100% in the first quarter, noting that its customers were increasingly buying luxury goods, such as diamonds. In 2011, Amazon made an estimated $350 million in watch and jewelry sales, up from $300 million in 2010. Gucci has even made Amazon.com its official authorized online retailer.

Luxury jewelry brands and retailers that have expanded their online sales and marketing efforts, tying together the digital and physical brand experience, have weathered the recession quite well and are seeing positive effects on their revenues. Going forward, they should continue innovating, using the internet to distinguish themselves and engage their customers, as luxury fashion brands are increasingly expanding into the luxury jewelry and watch market.

TIFFANY & CO. ONLINE SALES



FAST FACTS & FIGURES

40% of global demand for diamonds comes from the U.S. market

80% of American women receive diamond rings when they get engaged

6% of Tiffany & Co.'s worldwide sales of $3.79-billion are now online

100% Y.O.Y increase of Amazon.com's jewelry and watch sales in 2006

254% Y.O.Y increase of Amazon.com's custom-built ring sales in 2006

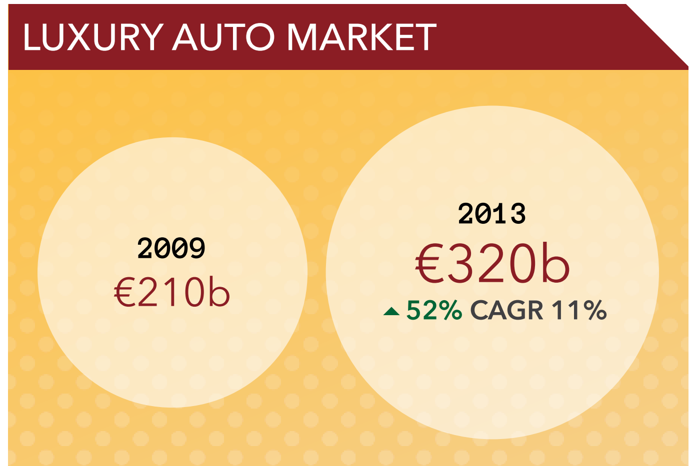
100% increase in Amazon.com retail diamond sales in Q1 2008

LUXURY CARS

The global market for luxury cars has grown from €210 billion (about $276 billion) in 2009 to €320 billion (about $421 billion) in 2013, a 52% increase at a CAGR of 11%. According to Digital Luxury Group, cars made up 48% of more than 470 million luxury brand Google searches in the U.S. in 2011, with automakers BMW and Audi being the first- and second-most searched luxury brands, respectively. These two automakers are also the top two automotive brands that dominate social media channels, such as Facebook and Twitter. Despite the recession, high unemployment, and expensive gas prices, it seems that Americans still spent many hours online researching luxury vehicles that often cost more than the median U.S. household income.

According to L2 Think Tank, 80% of Americans use the internet to research vehicles before making their purchase, and a 2012 study by mobile advertising company Briabe indicates that 87% of prospective car buyers will use mobile devices to research vehicles. A majority of automakers (86%) have already created mobile-optimized sites with advanced functionality, and they're beginning to challenge third-party reference sites, with customer service features, such as detailed FAQs, live chat, and prompt followup on dealership referrals.

Consumers are also buying cars from their mobile devices. While companies like eBay, Carvana, or Amazon aren't selling new luxury vehicles, their online sales experiments have demonstrated that consumers are willing to buy big ticket items such as vehicles directly from their phones. eBay, which sells more than 11,000 pre-owned vehicles through its online auctions each week, has created its own eBay Motors app to handle the high traffic from mobile shoppers. Carvana, a startup that buys cars at auctions and then sells them online, uses high-definition photo technology to give shoppers the ability to zoom in on the actual vehicle (not a stock image) to see everything in detail, including imperfections that car buyers may not notice on the lot. Carvana is using technology to change a very old and established industry, and has shown that people will buy vehicles with their phones. Amazon.com sells practically everything, but it doesn't sell cars. However, it recently partnered with Nissan to promote the 2014 Nissan Versa Note through a product page on its website. While the Versa Note product page on Amazon.com isn't as visually appealing as Nissan's official one, it does provide lots of information about the car for shoppers who are researching the vehicle. Instead of the usual Amazon "Add to cart" button, there's one that says "Visit Versa Note," which takes shoppers to the official Nissan Versa Note page. Shoppers can then enter their ZIP code to find offers from local Nissan dealers. As part of the promotion, the first 100 Versa Note buyers who initiated their purchase through Amazon



FAST FACTS & FIGURES

48% of 470-million luxury brand Google searched were for cars in 2011

80% of Americans use the internet to research vehicles before making their purchase

87% of prospective car buyers will use mobile devices to research vehicles

86% of automakers have created mobile-optimized sites with advanced functions received a $1,000 Amazon gift card, and three lucky buyers got their cars delivered to their door in a giant Amazon box. While the collaboration between Amazon and Nissan was a one-off marketing experiment, it showed that consumers are using the internet to research and initiate large purchases. Now, even Gilt Groupe is experimenting with selling luxury vehicles through its website. Working with Infiniti, Gilt is offering two all-new 2014 Q50 luxury sports sedans, one designed by Thom Browne and the other by Zac Posen.

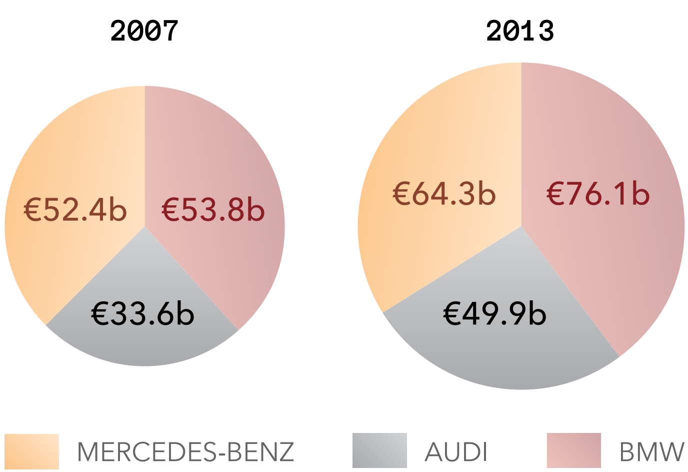
While the U.S. is currently the top market for luxury vehicles, China is expected to take over the number one spot within the next seven years, according to Digital Luxury Group. The luxury car market in China has been growing at an annual rate of 36% in the past ten years. In comparison, the overall Chinese passenger vehicle market has increased at an annual rate of 26% during the same time period. While the older generation of Chinese consumers bought luxury cars to show off their social status, the newer generation is buying them for a variety of different reasons. In a McKinsey survey of middle class Chinese consumers, some of the reasons given for buying a luxury car included: it's a reflection of social status; self-indulgence; the car is a "business card" for credibility; they're attracted to the sophisticated functions and innovative designs; the car is a source of fun in life; and because they demand excellent service. Cars are the most searched for luxury items in China, which is already the top market for some luxury auto brands, like Jaguar. The top three luxury vehicle brands in China are Audi, BMW, and Lexus, with German automakers accounting for 80% of the Chinese luxury auto market.

The top two luxury automotive brands that have invested a lot in digital marketing – BMW and Audi – have been doing very well. BMW, which overtook Lexus in 2011, has become the best-selling luxury vehicle brand in the U.S. and has remained at the top ever since. BMW Group's revenues grew from €53.8 billion (about $70.8 billion) in 2007 to €76.1 billion (about $100 billion) in 2013, a 41% increase at a CAGR of 6%. BMW's innovative approach to online marketing includes: their website; special feature web sections, such as bmwfilms.com and an online racing game; personalized e-mails; e-magazines and virtual brochures; special event webcasts; online advertising; a mobile website; Facebook apps; and a YouTube channel. One example of BMW's digital marketing efforts was the "X3 Matchup" campaign, which the automaker launched in 2011 to engage its Facebook community of 7 million fans, challenging them to customize the exact same car that appeared in a BMW X3 commercial. That year, working with 50,000feet, an independent creative agency, BMW also launched BMW Aftersales Online Marketing tools (e-commerce, search engine marketing, e-mail marketing, digital assets, and social media), which helped BMW dealers generate millions more in revenue.

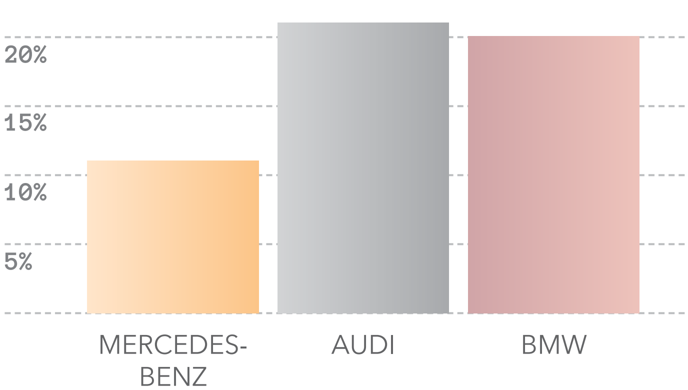
Audi's revenues increased from €33.6 billion (about $44.2 billion) in 2007 to €49.9 billion (about $65.6 billion) in 2013, a 48% increase at a CAGR of 7%. Audi has conducted several successful viral marketing campaigns to increase awareness of its brand worldwide. Campaigns like the "Stolen Audi" miniseries and "Meet the Beckers" videos became instant hits both online and offline, and have increased Audi's brand

LUXURY AUTOMAKER REVENUES

» AMONG 3 DIGITALLY ACTIVE BRANDS



2013 BRAND GROWTH IN CHINA

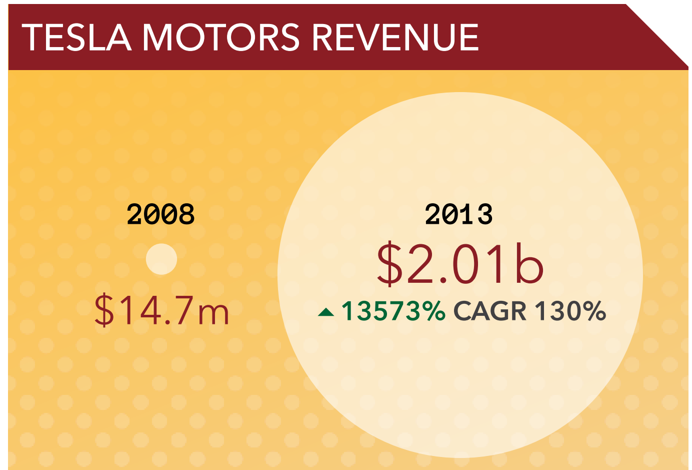


awareness over its competition. A study by marketing and consulting company Phoenix Automotive recently named Audi a top advertising performer in the luxury category because of its ability to use effective story-telling and humor to demonstrate a specific vehicle feature in its ads. Audi was also recognized as a brand that generates much more online conversations compared to its competitors. In an effort to allow tech-savvy consumers experience the brand both physically and digitally, Audi opened its first Audi City digital showroom in London in 2012, where shoppers can customize their own cars by selecting vehicle options from a digital media system, and then view it on a 1:1 scale on a large screen. There are also "Customer Relationship Managers" there to help shoppers if they decide they want to buy a car on the spot.

According to a 2011 L2 Think Tank study of the top 20 luxury brands in China, Audi and BMW ranked No. 1 and No. 3, respectively. The brands were ranked based on their website, social media efforts, digital marketing, and mobile efforts, taking into account factors like website load time, translation efforts, Chinese search engine optimization, mobile adoption, and presence on the top seven Chinese social media sites. Aside from being present on six of the top seven social media sites, and having more than 250,000 videos on YouKu (the Chinese version of YouTube), one of the main reasons for Audi's high rating is its multi-language, multi-platform mobile application, which is increasingly relevant considering many Chinese consumers are going from having no internet, to having mobile internet. In both 2012 and 2013, Audi and BMW were also the top two most-searched for luxury brands in China, based on Digital Luxury Group's analysis of more than 150 million searches on Baidu (the leading search engine in China) and Google.

While Mercedes-Benz has seen its revenues increase from €52.4 billion (about $68.9 billion) in 2007 to €64.3 billion (about $84.6 billion) in 2013, a 22% increase at a CAGR of 3%, it has been lagging behind BMW and Audi, especially in China. In 2013, Mercedes saw a 11% increase in vehicle sales in China, while Audi and BMW reported an increase of 21% and 20%, respectively. However, the automaker has a new growth strategy – "Mercedes-Benz 2020" – which aims to provide customers with a consistent luxury brand experience whenever they interact with Mercedes. The new marketing and sales strategy includes a variety of approaches, including greater use of digital presentation tools at its showrooms, increased online activities, and online stores. Recently, in an effort to get Gen Y fans excited about its new entry luxury CLA-class four-door coupe, it launched a new social media campaign where five top Instagram photographers were given a CLA for one week, during which they posted photos of their experience with the car. Instagram photos were also cross-posted on Mercedes-Benz's Facebook page for greater exposure. The photographer with the greatest number of "Likes" on their photos from that week won a three-year lease on the CLA, while fans could also try to win a lease on the car by submitting their own Instagram feed to the CLA contest website. Mercedes-Benz also launched its "Mercedes-Benz Connection Online" stores, where customers can order and finance vehicles anytime, anywhere. Mercedes hopes the experiment will provide it with some insight on how customers react to this kind of online sales channel.

While Tesla Motors – probably the most successful American startup car company in the last 50 years – doesn't like to be called a luxury car company, insisting its goal is to create an affordable mass-market electric car, it continues to be compared to luxury brands. Tesla calls its vehicles "premium" rather than "luxury," and says it's focused on delivering performance rather than trying to establish itself as a luxury automaker. Nevertheless, its vehicles are attracting luxury consumers, and it has been outselling the likes of Mercedes, BMW, and Audi – with a marketing strategy that doesn't include any advertising, ad agencies, chief marketing officer, or dealer network. Tesla has seen its revenues grow from $14.7 million in 2008 to $2.01 billion in 2013, an impressive 137-fold increase at a CAGR of 167%. Disrupting the established dealership franchise system in the U.S., Tesla



promotes its vehicles through “stores” in upscale shopping malls, where shoppers can ask questions without having to deal with high-pressure sales tactics, and then if they decide to purchase, they can order their car directly through Tesla’s website (see sidebar). Tesla already has 35 retail locations in the U.S., Europe, and Asia, and plans to expand to 50 stores over the next few years, but it’s currently in a legal fight with dealer associations in several U.S. states over the right to sell cars directly to consumers.

Whether or not buying vehicles online eventually becomes mainstream, luxury vehicle brands should continue to experiment and engage with customers online, since most car buyers these days will use the internet to conduct research or even initiate a purchase before actually stepping into a dealership.

» CONSUMER TRENDS

BUYING A PREMIUM ELECTRIC CAR FROM TESLA

Year after year, consumer surveys show that people rank buying a car as one of their least favorite experiences. This sentiment is closely associated with the typical car-buying process in the US that is deeply entrenched in a franchise system — where car manufacturers are legally prohibited from selling their own cars directly to consumers. The first car dealership was created in 1898 to sell steam-powered automobiles made by the General Motors Corporation. However, the franchise system of car dealerships was far from established at that time, and for the first two decades of the 1900s, “virtually every type of distribution was tried in the automobile industry. Manufacturers sold vehicles directly through factory stores, and by mail order and consignment arrangements, and indirectly through retail department stores, traveling salesmen, and wholesale distributors.”

Over a century later, Tesla isn’t the first company to try to sell cars through an online dealership. In the 1990s, Scott Painter wanted to launch a virtual dealership online, but he quickly discovered that none of the major car manufacturers would even consider the concept of an online dealership. Across the US, various state laws make it extremely difficult to change the traditional relationships between car makers and brick-and-mortar dealerships, effectively preventing an online marketplace that would supplant traditional dealerships. Painter still founded CarsDirect.com to facilitate the purchase of cars online, but the venture worked with dealerships instead of circumventing them.

The typical process for buying a new car online, even a luxury brand vehicle, is unlike the process for buying other expensive items on the internet. A luxury car buyer might think that he/she should be able to select any model online, customize it with any desired options, pay for the vehicle by entering in some numbers and making a few clicks, and expect to be able to pick up the car when it is ready. The actual process allows a buyer to customize a vehicle online with a multitude of factory-installed options, but when it comes to paying, the buyer is told to request a price quote from a local dealership. Requesting a quote from a dealership is not exactly a 1-click shopping experience, but it is a legal requirement of the franchise system for automakers. Perhaps surprisingly, buying a used car can be done completely online without “requesting a quote” from a dealership, so it’s a bit puzzling how the new car market tolerates a more convoluted buying experience — especially for new luxury vehicles.

For a luxury — or premium — car brand, it is essential to maintain an excellent buying experience, and Tesla has decided to keep its retail business in-house, instead of relying on franchises. The resulting retail experience has been described as Apple-like, after the strategy Apple employs to sell its electronics in its own high end stores. This retail strategy aims to enhance the feel of exclusivity for Tesla’s products, as Tesla’s dozens of physical sales locations are dwarfed by the tens of thousands of other car dealerships in North America. Tesla’s salespeople don’t work on commision, and the company boasts that its buying experience is simple, no-haggle, and reassuring. Additionally, Tesla’s website creates a virtual dealership that allows anyone to purchase directly without “requesting a quote” as other car dealers do. Tesla doesn’t have that many different models, but its website still allows buyers to customize the vehicle with a variety of options. Tesla’s prices are made clearly available, and not surprisingly, customers can conveniently pay using Paypal.

CONCLUSION

What we've seen throughout this report is that, as with many other industries, the internet has transformed the luxury goods market in all sorts of ways -- some of which can't be easily summarized as "good" or "bad." However, what has become clear is that the internet has enabled all sorts of new and useful ways for luxury markets to develop, while also enabling consumers and brands new ways to connect, build relationships and to buy and sell the luxury goods that matter to them most.

This has created new opportunities and tremendous business growth in both established and new areas, while also allowing consumers better ways to learn about and purchase luxury goods.

Furthermore, the rise of e-commerce in general, and a variety of specific innovations in and around e-commerce, has also helped luxury brands go global, finding audiences in places where it might not have seemed worth it to explore previously. As with many other industries, the luxury goods industry has discovered that the internet has created not just the ability to sell goods through the web, but more, different (and often better) ways to promote and connect with buyers and aficionados. This has opened up all sorts of new possibilities, with many brands and retailers embracing what these opportunities enable.

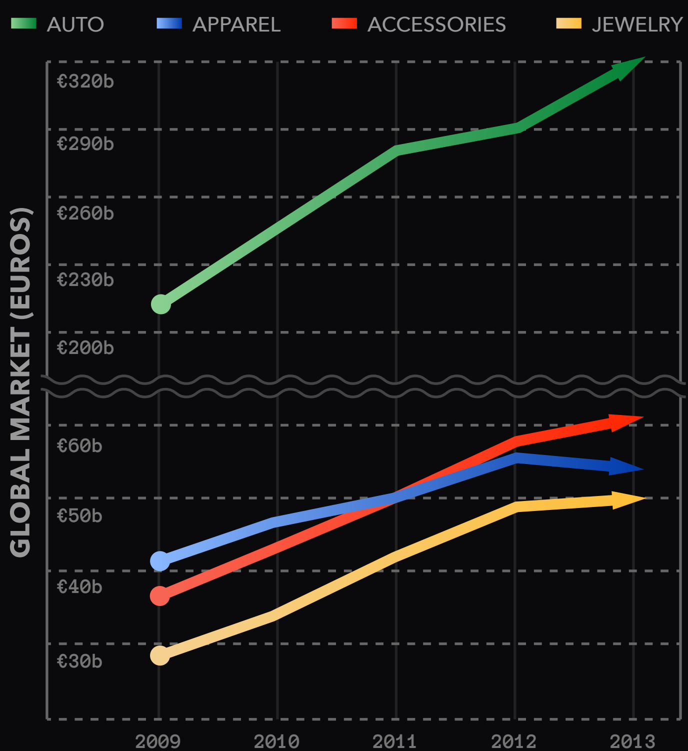
Given the pace of growth and innovation in these markets, **we expect that even greater opportunities for growth lie ahead.**

thesky is rising

LUXURY GOODS

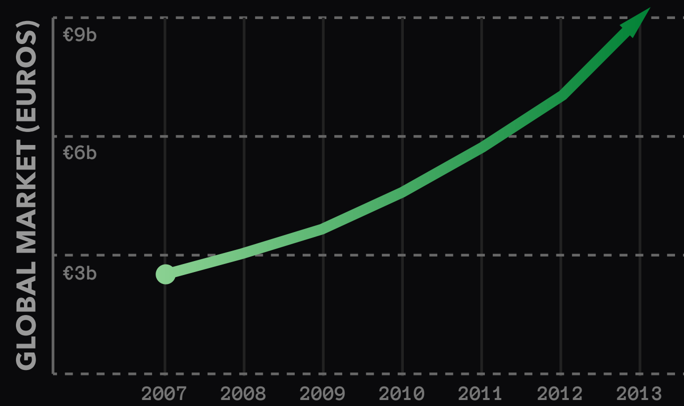
THE LUXURY MARKET

» GLOBAL, KEY SECTORS



ONLINE LUXURY

» GLOBAL MARKET SIZE



» ONLINE CONSUMER TRENDS

69% of luxury consumers find online shopping more convenient

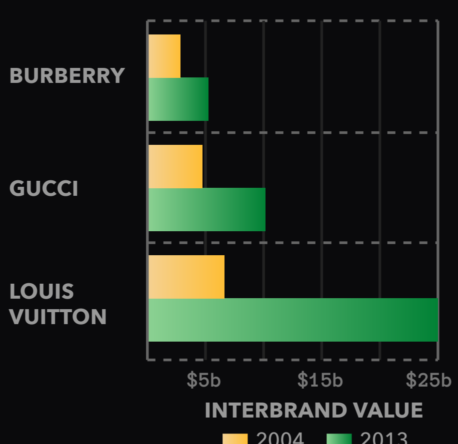
91% of millionaires would prefer their favourite brands be online

65% of wealthy consumers believe brands with no social networking presence are out of touch.

92% of luxury consumers use the internet to search for information about a product before buying

LUXURY FASHION

» BRAND VALUE IS GROWING



JEWELRY & WATCHES

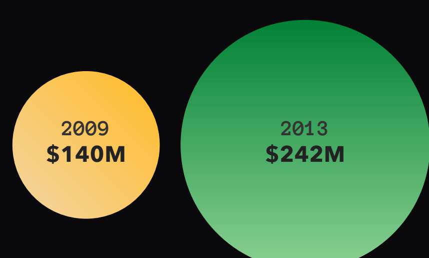
» DIAMONDS ARE BOOMING

28% growth of the international diamond market, 2000-12

325% growth of the Chinese diamond market, 2005-11

1052% increase in price of a 1K D Loupe Clean, 1960-2013

» TIFFANY & CO. ONLINE SALES



LUXURY AUTO

» ONLINE RESEARCH IS KING

80% of Americans use the internet to research vehicle purchases

87% of prospective buyers will use mobile devices to research vehicles

86% of automakers have built mobile sites with advanced functionality

» CHINA EMBRACES LUXURY

36% annual luxury auto market growth in China over the past 10 years

7 years until China replaces the U.S. as the top luxury auto market in the world.