

Luxury Takes Centre Stage



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A re-shoring of overseas luxury expenditure is contributing to the strong rebound in China's luxury market post COVID-19, attracting luxury brands to expand store networks once again.

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Average footfall of luxury projects in six cities are 1% higher than 24-month average

Back on track

The global luxury market is pinning its hope on a swift recovery of the China retail market, a key driver of growth and one of, if not the, biggest market in the world. As life starts to get back to normal, albeit with some virus prevention measures remaining in place, shopping malls around the country reopened and resumed close to full operations starting in April. Over the five-day May holiday period, landlords and retailers implemented extensive promotional campaigns to stimulate sales. LVMH and L'Oréal have already reported positive year-on-year (YOY) sales growth in China.

Food consumption gradually recovered to pre-COVID levels in May while non-discretionary items continue to improve, in particular cosmetics sales accelerated to growth of 17% YoY and automobile sales rebounded and recorded a YoY increase of 6%.

The luxury market also witnessed improving sales, supported by revival in footfall levels. Benchmark luxury projects in six cities showed average footfall levels returning to 24-month

averages in June. Considering luxury project footfall levels typically show a stronger correlation to sales than mass market projects, luxury brands are expected to see sales benefit from this pick-up in shopper presence.

Luxury projects saw average footfall drop by roughly 80% in February, but quickly rebounded to an average of 54% of normal levels by March. In June, footfall levels reached the average of the past 24 months for the first time since the beginning of 2020.

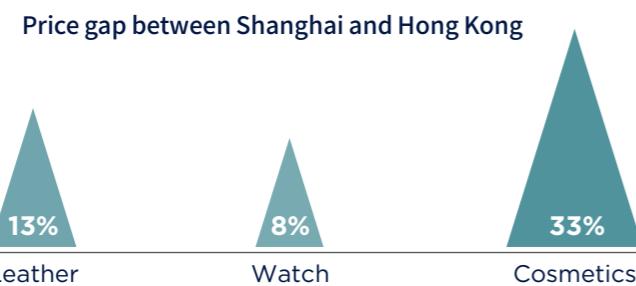
Footfall levels varied across different cities with Chengdu witnessing the strongest and swiftest rebound with footfall exceeding historical averages as early as April. In June Guangzhou footfall levels outperformed historical levels while Shanghai remained just off the pace. Meanwhile Wuhan, the epicentre of China's viral outbreak, showed a stronger than expected recovery, with footfall levels reaching 89% of historical levels in June, even higher than Beijing where lockdown measures remain some of the strictest in China.

Footfall index of benchmark luxury project in six cities Footfall levels returned to 24-month average by Jun 2020



Source Savills Research, MobTech

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Reshoring of luxury spending

A full resumption of international flights is unlikely in the foreseeable future, though there may be selective reopening with specific countries. In fact, the World Tourism Organization estimates that international tourist numbers will fall by 60% to 80% in 2020 due to the global spread of COVID-19.

Chinese overseas travel growth rates had already started to slow in 2H/2019, increasing just 3.5% YoY compared to 14.0% in 1H/2019 and 4.9 ppts slower than the growth in domestic travel. As China's tourism market continues to mature, the quality of domestic tourism has been significantly improving in terms of facilities, product/service offerings and overall experience. Tourism revenue accounted for 12.4% of China's tertiary industry in 2019, the highest level on record.

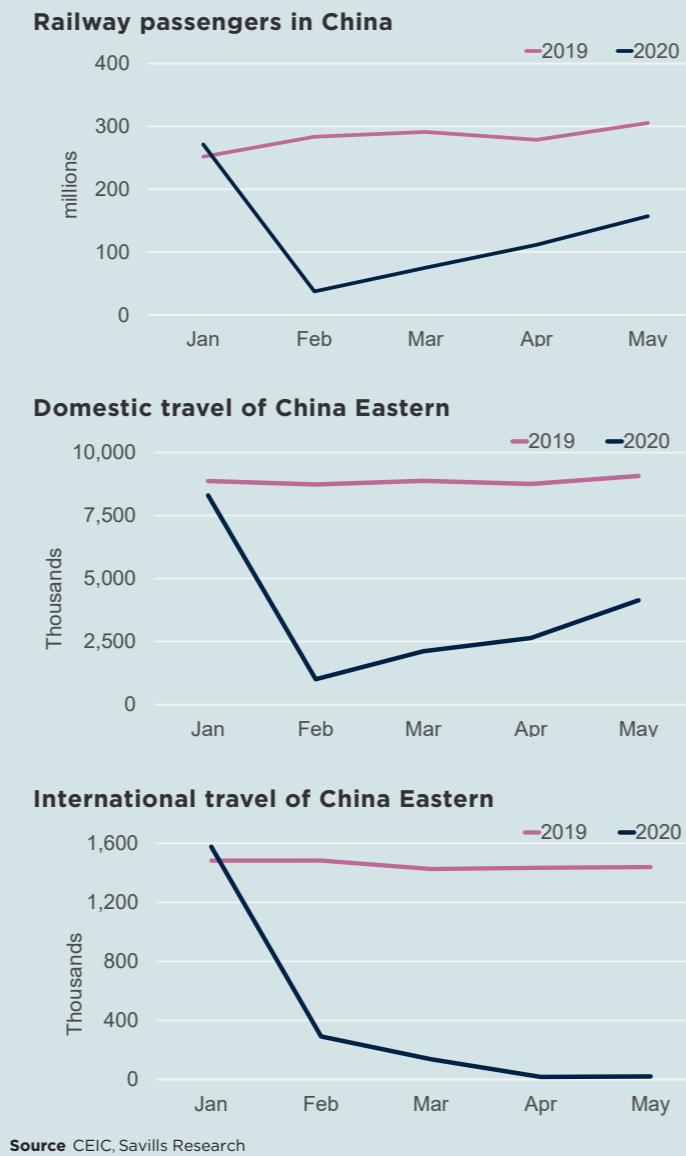
Overseas luxury spending used to account for over 70% of total luxury consumption by Chinese consumers according to Bain & Co. However, with the continued development of ecommerce platforms, improved after sales service and narrowing of price gaps with overseas markets, more consumers have chosen to purchase within China since 2018. The COVID-19 pandemic is expected to accelerate the trend as both overseas travel and dai-gou activities are greatly restricted.

The price gap between domestic and overseas markets continued to shrink as luxury brands normalize their pricing structures. The average price disparity between Shanghai and Hong Kong fell from 30% to 15% from 2013 to 2019, though, given online sales penetration rates, the actual price gap could narrow further.

The central government has also recently released a series of policies to encourage luxury consumption to take place within China's borders, such as promotion of duty-free stores. The growth of duty-free networks as well as smaller outlets will likely continue though not too rapidly so as not to detract significantly from the numerous city centre locations.

Domestic travel bottomed out in February. Railway passenger volumes reached 50% of pre-COVID levels in April. China Eastern saw domestic travel fall to 11% of pre-COVID levels in February, but have since recovered to 47% in May with seat occupancy rising from 45% to 66%.

Overseas traveler volume, given the stringent travel restrictions, still remain weak, with April figures only at 1% of that before the pandemic.



Enduring luxury

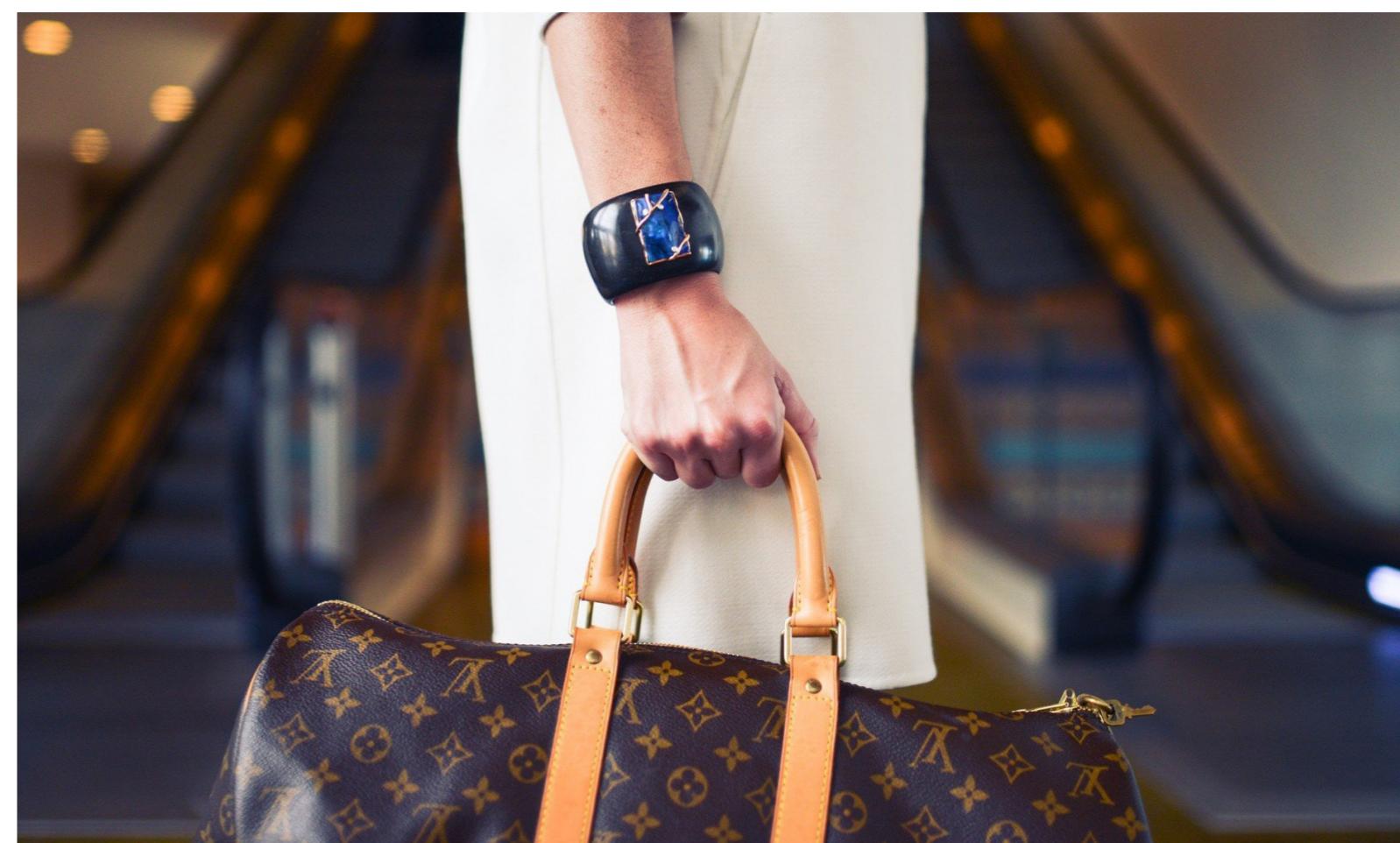
Top-tier luxury retail brands showed their resilience and commitment to the China market despite rising economic uncertainties. Top-tier brands grew their average store count in key cities by 4% over the last 12 months, while affordable luxury brands saw their average store count fall by 3% over the same period.

Retail brands did not merely see their sales impacted by COVID-19, but also their production capacity, as factories were closed or repurposed facilities to produce PPEs and domestic and international supply chains were heavily disrupted. A number of brands,

including Louis Vuitton and Chanel, chose to raise their prices in order to offset the slower sales and ration existing stocks.

China is home to a significant and rising share of the world's high-net-worth-individuals (HNWIs) and they seem to be relatively unfazed by the pandemic. Although luxury brands

may see pressure on global revenues, in China the price increases seem to have had only a minimal impact on short-term sales with the brand premium and status symbol of top-tier brands still highly attractive to Chinese consumers.





140%

YOY increase of new account openings of luxury brands on TikTok and RED in April and May

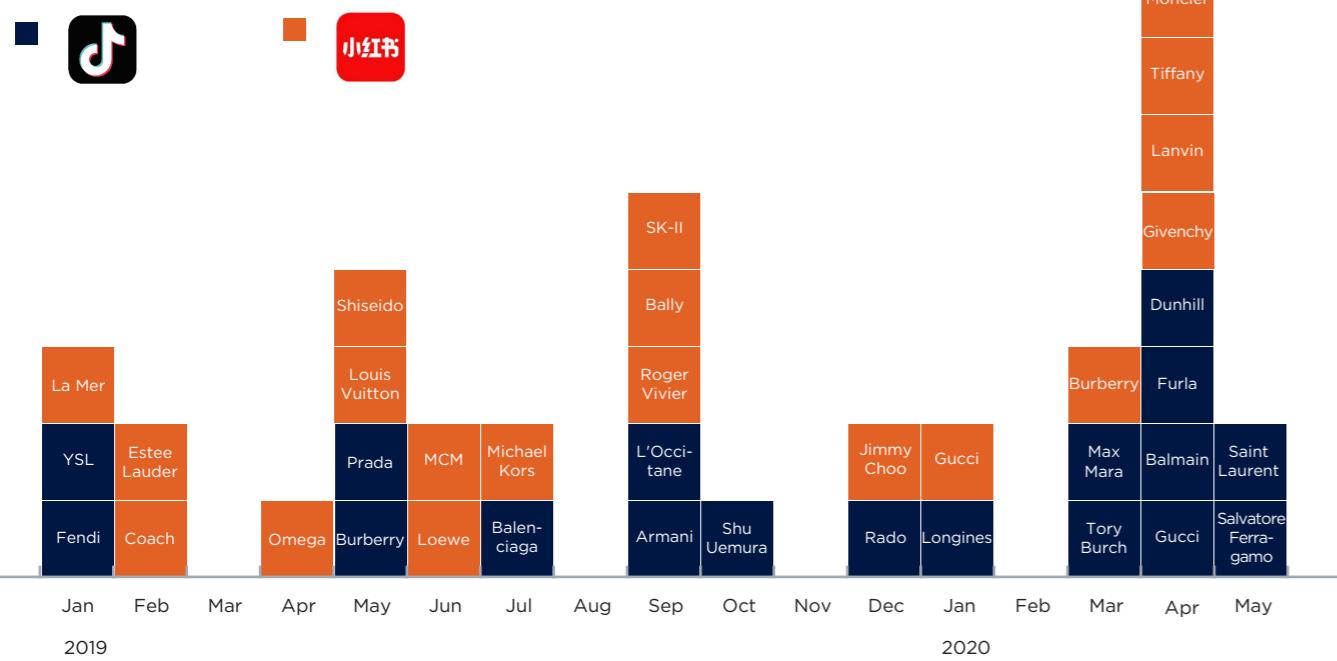
Exploring channels

The pandemic has also accelerated the trend of luxury brands moving online. China online sales and marketing ecosystem is one of most developed in the world with innovative tools, new channels and product updates that are able to capture approximately 20-25% of consumer purchases. Luxury retailers, while initially resistant to the lure of online platforms due to concerns of watering down their brand image and exclusivity, are now coming around to the idea that they need to embrace these platforms in order to reach the new wave of luxury consumers and adapt to Chinese consumer preferences.

Luxury brands are not only exploring traditional online platform icons such as Tmall or JD, but have also started to tap into some of the many different social platforms used by young consumers. TikTok and RED (also known as Xiaohongshu) recorded the opening of new accounts by several luxury brands in April. Brands also cooperated with KOLs to sell products direct to consumers, or launch vlogs or live shows to attract younger cohorts. TikTok's fashion show in March with Chanel, Dior and Burberry was viewed over 4.0 million times. Meanwhile, Givenchy saw its number of fans increase 5.5 times after it launched a live show on RED.

Online marketplaces also help luxury brands reach more consumers in low-tier cities where physical stores would not be able to cover. Stronger ties with these consumers through online channel will potentially allow brands to expand their consumer base and establish greater loyalty. Online platforms also give brands the ability to better understand their consumer profiles and preferences and adapt to nascent consumer trends more swiftly.

New Brand Accounts on TikTok and RED 2019 – May 2020



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