ADWEEK

Luxe Market Faces Wealth of Challenges

The current downturn has not spared the wealthy or their taste for luxury

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- Mark Dolliver

Look up "luxury" in the dictionary and you'll find a passage defining it as "something adding to pleasure or comfort but not absolutely necessary." With economic conditions compelling even affluent consumers to pay more heed to what's "absolutely necessary," how is the appetite for luxurious "pleasure or comfort" holding up? Survey data on the attitudes of affluent consumers, plus the observations of people in the business of tracking their thinking, point to a market that faces a wealth of challenges.

Before the current recession, popular wisdom said wealthy people tended to be relatively untouched by the ups and downs of the economy and would keep buying high-end products and services no matter what. However true that might have been in the past, the current downturn -- with its sharp decline in stock prices and real estate values -- has not spared the wealthy or their taste for luxury.

AFFLUENT BUT PRACTICAL

One gets a taste of this from the Luxury Institute's State of the Luxury Industry 2009 Survey, developed in conjunction with Evins Communications and released last month, based on August fieldwork. Seventy-seven percent of the respondents (a cohort whose yearly household income averages $415,000 and whose household net worth averages $4.9 million) agreed that luxury is less important in today's economy. Fifty-eight percent said they are "spending more on essentials rather than on what they want"; 56 percent said they are "being more practical about spending."

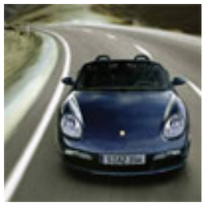
This fall's tracking study of high-net-worth/high-income consumers by the American Affluence Research Center gives another telling sign of their current mind-set: 9 percent said they would spend "nothing" this December on holiday gifts, and those who do plan to spend anticipate laying out 5 percent less on average than they did last year.

It's not just a matter of feeling chastened by the economy's travails. "Even wealthy people were living beyond their means," says Milton Pedraza, chief executive officer of the Luxury Institute, a rating and research organization that tracks the luxury field. "Now, whether they want to or not, they're being forced to live within their means," Pedraza says. And when they do spend, this means bringing a more critical kind of thinking to the process. "They're more value-driven," says Greg Furman, chairman of the Luxury Marketing Council, whose membership includes top executives of luxury brands. "They want to understand the price/value equation."

Opinions do differ, though, about the depth of the change in wealthy consumers' behavior. "We do not believe that there has been a paradigm shift in affluent consumer behavior as a result of the financial downturn," says David Thompson, managing director, affluent market at Phoenix Marketing International. "Unlike the Great Depression, this one was far too short and the markets have partially recovered too quickly to cause a seismic change in behavior. Most mainstream investors have weathered the storm quite well, overall."

RISE AND FALL OF THE 'ASPIRATIONAL'

One problem for the luxury market, though, is that it



came to rely partly on customers who weren't really wealthy enough to be buying such goods in the first place -- the "aspirational" consumers who relied on credit to indulge in the luxe life. And rising equity and real estate prices made sizable numbers of people feel as though they'd joined the ranks of the truly wealthy, even if they really hadn't. Furman says the growing number of such people prompted many luxury marketers to chase after them. But these overextended consumers have been conspicuous casualties of the economic downturn. "They're gone," agrees Pedraza. Instead of shopping for luxuries, he says, the aspirational consumers are now just trying to cover their basic expenses.

The departure of these people from the scene would matter less if luxury marketers could count on everyone who remains affluent to shop for fancy, high-end goods. But studies by the American Affluence Research Center suggest a majority of affluent consumers are largely indifferent to luxury goods of the conspicuous-consumption ilk. In a report issued this past spring, it noted that "the affluent market is composed primarily of people with middle-class backgrounds who continue to pursue a somewhat middle-class lifestyle with middle-class values." Far from being avid customers of luxury brands, most of the affluent were said to be "not familiar" with them. The report went on to say that just 1 million households "might be considered conspicuous consumers."

Does this reflect a marketing failure on the part of luxury brands, or is it more a matter of an innate disinclination by affluent-but-unshowy consumers to engage with such luxuries? "I think it is probably a bit of both," says Ron Kurtz, president of the research center. "On the one hand, the luxury brands seem to have gone after the low-hanging fruit, i.e., the consumers most interested in making a statement about themselves and/or those who are self-indulgent. The affluent consumers still pursuing a somewhat middle-class lifestyle and values need to be 'educated' about the luxury products and brands. This requires a different marketing approach than one that is in one way or another based on the premise of 'if you've got it, flaunt it,' which seems to be what the luxury products were following as a strategy."

NAME YOUR TOP PRICE

The center's spring report included survey data on how much affluent consumers would be willing to shell out for various items, and it certainly belied the anecdotes one heard in pre-recession days of wealthy people tossing around vast amounts of money for flashy goods. Respondents' household income averaged $304,000, net worth averaged $3.1 million and primary home was worth $1.2 million. Notwithstanding those gaudy figures, the most they'd be willing to spend on a new car for personal use averaged out to a non-stratospheric $40,000 by the men and $35,000 by the women. Women and men alike said $1,500 was the most they'd spend on a washer/dryer combination, and they also agreed on a figure of $300 as their upper limit for a hotel room in New York. (Lots of luck!) As for the image of rich folks ordering thousand-dollar bottles of wine, $40 was the most the survey's men could imagine spending for one "for a special dinner at home," and $30 was the female respondents' upper limit.

In theory, such non-flaunting affluent consumers could be an especially attractive potential market these days for brands that are expensive but unostentatious. After all, these are the sorts of prosperous-but-frugal souls who didn't overextend themselves financially in the pre-recession days. "But they are still being very cautious in their spending and their saving, according to our recent surveys," says Kurtz. "As a result, they will not necessarily be an easy sale."

For that matter, affluent consumers who are in the habit of buying luxury goods are not an easy sale, either, and not simply because the economy is constraining their spending. There's also an element of dissatisfaction with what the luxury market is offering. In the Luxury Institute's recent poll, 83 percent of respondents included "superior quality" among the essential characteristics of a luxury brand. Also high on the list were "superior craftsmanship" (78 percent), "superior design" (69 percent), "exclusive products" (58 percent), "brand heritage and history" (54 percent) and "superior service" (53 percent). "Yet, quality, craftsmanship and service are the top three benefits that the luxury industry is still failing to deliver," says the institute's analysis of the findings.

It doesn't help matters that potential customers feel the luxury market has become oversaturated with offerings: 53 percent of the Luxury Institute poll's wealthy respondents said they believe "there are too many brands in most luxury categories today." Similar polling at the beginning of this year found 44 percent of respondents saying luxury brands were becoming "commodities," a dirty word if ever there was one in this sector.

THE IMPORTANCE OF PEDIGREE

In other markets, the struggles of long-established brands would indicate an opening for newcomers to exploit. But, just as the rich are different from the rest of us, the luxury sector is different from others as well. A luxury brand's long-standing heritage is often an important part of its value to wealthy shoppers, and this fact presents a steep barrier to entry for marketers hoping to get into the luxury market. "There are very few new luxury brands," notes Pedraza. "It's extremely hard to be a luxury brand without the pedigree and longevity." He adds that the heritage of a brand serves as an indicator of its value. "In this market, people are gravitating toward quality and history," he says. In this context, he mentions a story he recently heard of a woman at a party showing off the Hermes bag her grandmother gave her -- a kind of longevity twofer.

Of course, one advantage of a luxury item that was bought generations ago is that the purchase doesn't come across as an affront to everyone who's suffering through the current recession. Earlier this year, one heard tales of wealthy people buying expensive luxuries but then sneaking them home in plain brown paper bags so as not to flaunt the purchases at a time of general austerity. For better or worse, that phenomenon of luxury stealth seems to have passed. "It was a flash in the pan," says Furman. "It came and went."

(Coming next Monday in Part 2 of this article: Forecasting wealthy consumers' post-recession behavior, the role of online marketing, the perils of luxury-brand discounting and more.)