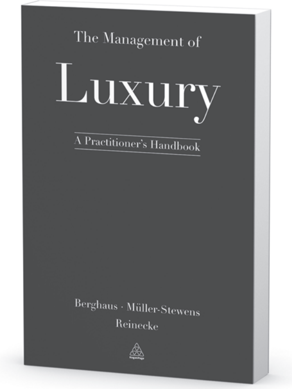
The Management of Luxury



The Management of Luxury

A practitioner's handbook

Benjamin Berghaus,
Günter Müller-Stewens
and Sven Reinecke

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CONTENTS

THE CONTRIBUTORS

Professor (FH) Emil Annen, Institute of Marketing, University of St Gallen (HSG), Switzerland (**emil.annen@unisg.ch**)
Professor Annen started his career in interior design, working for several years in numerous companies. After completing a further education programme, Professor Annen received his Master's of Business Administration from the University of St Gallen. He has worked at the Institute of Marketing (IfM-HSG) for over 30 years and in this time has held the positions of lecturer, executive consultant and tutor. In addition, Professor Annen is a speaker at various executive education seminars at the University of St Gallen. He also teaches in different training organizations such as the Höhere Fachschule für Gestaltung in St Gallen and the University of Applied Sciences and Arts Northwestern Switzerland School of Business in Basel where he has been professor of marketing for nearly 20 years.

Dr Eric Arnould, Marketing and Management Department, University of Southern Denmark (**eric@sam.sdu.dk**)
Dr Arnould is professor of marketing at the University of Southern Denmark. He has been passionate about applied social science since 1973. He has benefited from teaching students at universities on four continents and has consulted for a number of public and private organizations. Before entering academia in 1990, Dr Arnould spent 15 years working on problems of economic development, especially in agriculture and natural resource management, primarily in francophone West Africa. His research on sustainability, economic development, services marketing, consumer culture theory, cultural marketing strategies and marketing channels in developing countries has appeared in over 90 articles and chapters in major social science and managerial journals and books, including *Journal of Consumer Research*, *Journal of Marketing*, *Journal of Public Policy and Marketing*, *Human Organization* and *Journal of Marketing Research*.

Dr Elisa Arrigo, Assistant Professor of Management, Department of Economics, Management and Statistics (DEMS), University of Milan-Bicocca, Italy (**elisa.arrigo@unimib.it**)
Dr Elisa Arrigo teaches undergraduate and graduate courses in Marketing Management and Marketing Communication. She holds a PhD in Marketing and Management from Milano-Bicocca University; during her PhD studies she was visiting scholar at the Stockholm School of Business. Her research interests lie primarily in market-driven management and corporate social responsibility. She is currently involved in research projects related to the management of fashion and luxury firms, with particular reference to global retailing strategies. She has published a book and a number of book chapters and papers in referred journals on various aspects of her research topics.

Dr Verena Batt, research and teaching assistant, Marketing and Management Department, University of Basel, Switzerland (**verena.batt@unibas.ch**)
Since 2006 Dr Batt has been research and teaching assistant in the Marketing and Management Department at the University in Basel, gaining her PhD in 2012. Primary areas of research encompass luxury branding, internal branding, employer branding and marketing communications.

Professor Dr Carsten Baumgarth, School of Economics and Law, Marketing, HWR Berlin, Germany (**cb@cbaumgarth.net**)
Since 2009 Carsten Baumgarth has been professor of marketing and Brand Management at the Berlin School of Economics and Law. He has published around 250 papers and books with a focus on brand management, B2B marketing, arts marketing and empirical methods. His work has been published in *Industrial Marketing Management*, *Journal of Business Research*, *European Journal of Marketing* and *International Journal of Arts Management* among others. He has won a number of best paper awards (eg, Best marketing and Best overall paper of AIMAC 2009). Together with Daragh O'Reilly, he is acting as a guest editor of the special issue 'Brands in the arts and culture sector', *Arts Marketing,* due in 2014.

Stefan Behrens, Dipl-Oec, scientific research assistant, Leibniz University of Hannover, Germany (**behrens@m2.uni-hannover.de**)
Stefan Behrens is scientific research assistant in the Institute of Marketing and Management at the Leibniz University of Hannover, Germany.

Philip Beil, Partner, Roland Berger Strategy Consultants, Berlin, Germany (**Philip.Beil@rolandberger.com**)
A graduate of Ludwig-Maximilian-Universität in Munich, Philip Beil joined Roland Berger in 2003. Prior to that he was Director of Business Development for an international start-up company that he co-founded. As a partner in the Consumer Goods & Retail Competence Centre, Philip Beil heads the Fashion and Luxury Goods Practice, supporting manufacturers and retailers in growth and brand strategies, efficiency and M&A. He's the author of numerous studies on the luxury market and industry and a frequent speaker at important industry events. He regularly gives lectures on luxury marketing at the University of St Gallen.

Benjamin Berghaus, research assistant and project manager, Competence Centre for Luxury Management, Institute of Marketing, University of St Gallen, Switzerland (**benjamin.berghaus@unisg.ch**)
Benjamin Berghaus joined the University of St Gallen, Switzerland in 2010, first as manager of the Research Program for Luxury Brands, and since 2014 as manager of the Competence Center of Luxury Management. Previous to this he worked as a marketing manager in the luxury market. His fields of interest are the particularities of the luxury market in all management disciplines as they are resulting from the marketing strategy of luxury positioning.

Dr Michael Breazeale, Assistant Professor of Marketing, College of Business, Mississippi State University, USA (**mbreazeale@business.msstate.edu**)
Michael Breazeale is an Assistant Professor of Marketing at Mississippi State University. He received his PhD from Mississippi State University in 2010. His primary areas of research encompass consumer-brand

connections, retail atmospherics and branding implications for violent extremist organizations. Dr Breazeale has published several articles in publications that include *Journal of Retailing*, *International Journal of Market Research* and *Journal of Business Research*. He has won multiple awards for both teaching and research and has performed consulting duties with clients as diverse as Millward Brown Optimor and the US Military. He is founder and co-organizer of the Brands and Brand Relationships Conference. Michael Breazeale is also one of Social Media Marketing Magazine's Top 100 Marketing Professors on Twitter and Best Online Universities' Top Web Savvy Professors.

Ludovica Cesareo, Faculty of Economics, Management Department, Sapienza, University of Rome, Italy (**ludovica.cesareo@uniroma1.it**)
Ludovica Cesareo is a PhD candidate in Business Management at the Management Department of the Faculty of Economics at Sapienza, University of Rome. During the final year of her PhD, she was a visiting scholar at Villanova School of Business, Villanova University, Pennsylvania, USA. Her main fields of research are marketing and counterfeiting. She has published on the phenomenon from both the consumers' viewpoint (analysing the antecedents of and the cultural influences on attitudes and behaviours towards counterfeit products) and legitimate firms' viewpoint (studying strategies, actions and organizational solutions undertaken by firms to tackle counterfeiting). She is also researching sustainable marketing, e-word of mouth/digital marketing and tourism marketing.

Professor Dr Claude Chailan, Director of the Executive MBA Program, Marketing and Strategy, EM Strasbourg Business School, France (**claude.chailan@em-strasbourg.eu**)
Prior to joining academia, Dr Chailan held high-level positions in international management from 1985 to 2000, including senior positions at Danone, Sara Lee and L'Oréal. He was actively involved in the development of these brands in France, Mexico and Venezuela, as COO or CEO of their local subsidiaries. Dr Chailan is currently Professor and Programme Director at EM Strasbourg Business

School. His research interests include the links between marketing and strategy, and his work has been widely published in leading academic journals including: *The Journal of Marketing Management, The Journal of Product and Brand Management*, *Euromed Journal of Business*, *The International Journal of Trade and Global Markets*, *The Journal of Competetiveness and Strategy*, *Critical Perspectives on International Business*.

Camille Depigny, project manager (**camille.depigny@essec.edu**)
Working for a famous luxury brand, Camille Depigny is an engineer and has focused her professional thesis on the jewellery market and its actual mutations.

Dr Delphine Dion, Associate Professor, Sorbonne University, Paris, France (**dion.iae@univ-paris1.fr**)
Delphine Dion is Associate Professor at Sorbonne Graduate Business School in Paris. Her current research projects explore luxury branding, material culture and ethnicity. Her research has been published in various French and international journals, including *Journal of Retailing*, *International Journal of Service Industry Management*, *Recherche et Applications Marketing*, *Decisions Marketing*, *Revue Française de Gestion* and *Revue Française de Marketing*. She has received many awards for her PhD dissertation, her research papers and books.

Alexander Gaus, Senior Consultant, Roland Berger Strategy Consultants, Berlin, Germany (**alexander.gaus@rolandberger.com**)
Alexander Gaus is a Senior Consultant at Roland Berger Strategy Consultants in the Consumer Goods & Retail Competence Centre. He joined Roland Berger in 2009 and has focused on marketing and sales topics with an emphasis on the luxury industry. He studied management at ESCP Europe in London, Paris and Berlin. He holds MBAs from each of these countries.

Kaibin He, Beijing University, Guanghua School of Management, Beijing, China (**aibinhe@pku.edu.cn**)
Kaibin He is a PhD student at the Guanghua School of Management at Beijing University. His research interest focuses on advertising,

branding, PR and product innovation. He received a Master's degree in communication at Xiamen University, and has been engaged in several consulting projects for CCTV and State Grid Corporation of China.

Professor Dr Klaus Heine, Assistant Professor, EMLYON Business School, Markets and Innovation, Shanghai, China (**heine@em-lyon.com**)
Klaus Heine taught the first luxury marketing course at TU Berlin and specialized in 'The Identity of Luxury Brands' with his doctoral dissertation. He conducted the first survey of millionaires in Germany regarding their luxury preferences and various other qualitative and quantitative luxury consumer surveys in Europe and China. Klaus Heine works as assistant professor of luxury marketing at EMLYON business school in Lyon and Shanghai, where he combines teaching about luxury brand management with applied research and practical projects.

Dr Sabrina Helm, Associate Professor, Retailing & Consumer Sciences, University of Arizona, USA (**helm@email.arizona.edu**)
Sabrina Helm is Associate Professor of Retailing at the University of Arizona. She received her PhD in business administration from the University of Dusseldorf, Germany. Prior to relocating to Tucson, she was Chaired Professor of Strategic Marketing at Witten/Herdecke University, Germany. In her research, she focuses on customer management and, specifically, the profitability of customer relationships and customer referral behaviour. She is also interested in corporate reputation and issues of sustainable consumption. She has published in *Journal of Marketing*, *Journal of Service Research*, *British Journal of Management*, *Journal of Business Research* and *European Journal of Marketing*, among others.

Dr Nadine Hennigs, Assistant Professor, Leibniz University of Hannover, Germany (**hennigs@m2.uni-hannover.de**)
Nadine Hennigs is Assistant Professor at the Leibniz University of Hannover, Germany, Institute of Marketing and Management.

Dr Anurag G Hingorani, Marketing Discipline Group, University of Technology, Sydney, Australia (**anurag.hingorani@uts.edu.au**)
Anurag G Hingorani is Deputy Head and Senior Lecturer in the Marketing Discipline Group at University of Technology, Sydney, and teaches marketing communication and related subjects at postgraduate and undergraduate levels. He has also been a Visiting Assistant Professor and Scholar-in-Residence in the School of Communication at Emerson College, in Boston. Dr Hingorani's research interests include body, advertising and corporate image as well as healthcare marketing and marketing education. He has published several papers and presented his research at local and international conferences. He has also undertaken consulting work involving marketing research, marketing strategy and marketing communications for both government and corporate clients.

Professor Dr Michael Jäckel, President, University of Trier, Germany (**jaeckel@uni-trier.de**)
Michael Jäckel is Professor of Sociology at Trier University and, since 2011, President of the university. He teaches sociology, especially media sociology and sociology of consumption. His research is focused on the study of media effects and audience behaviour as well as the diffusion of new communication technologies in modern societies.

Olga Louisa Kastner, MA, project manager, Kommunikationnsagentur Liganova, Stuttgart, Germany (**louisa.kastner@gmx.de**)
Between 2012 and 2013, Olga Louisa Kastner studied the Master's programme International Business & Consulting with a focus on international marketing strategy at both the Berlin School of Economics and Law and the Parisian Business School École Supérieure du Commerce Extérieur. She wrote her thesis on forms of collaboration between luxury brands and the arts. Mrs Kastner currently works as a project manager at the Stuttgart-based communications agency Liganova and is responsible for developing the agency's luxury, watches and jewellery accounts.

Dr Christiane Klarmann, Dipl-Oec, scientific research assistant, Leibniz University of Hannover, Germany
(**klarmann@m2.uni-hannover.de**)
Christiane Klarmann is scientific research assistant at the Leibniz University of Hannover, Germany, Institute of Marketing and Management.

Eirini Koronaki, Business Administration Department, Athens University of Economics and Business, Greece
(**eirinikor@aueb.gr**)
Eirini Koronaki is a PhD candidate at the Department of Business Administration of the Athens University of Economics and Business Her dissertation deals with the role of culture in luxury brand consumption. She studied Business Administration at the Athens University of Economics and Business and received her Master of Science in Marketing and Strategy from Warwick Business School. Her research interest lies in the field of luxury branding and management, cross-cultural marketing and communications. She has presented papers at the International Conference on Corporate and Marketing Communications (CMC). She works as a professor's assistant and has participated in training teams of development programmes for marketing executives.

Dr Charles Aaron Lawry, Assistant Professor, Marketing, Lubin School of Business, Pace University, New York, USA
(**cal2135@columbia.edu**)
Charles Aaron Lawry is Assistant Professor of Marketing at Pace University. He received his PhD in Retailing and Consumer Sciences from the University of Arizona. Dr Lawry examines strategies for inspiring and incentivizing user-generated content via social media and mobile technology platforms. He is especially interested in how celebrity culture and luxury consumption fit into this research arena. He has published in *Marketing ZFP* and the *International Journal of Technology and Human Interaction.*

Nicole Lohrisch, MA, HWR Berlin, School of Economics and Law, Marketing, Berlin, Germany (**nicole.lohrisch@hwr-berlin.de**)
Since 2012, research assistant at the Berlin School of Economics and Law. She has an MA in Cultural Administration. She studied at University of Leipzig, University of Lund/Sweden and Technical University of Dresden. She worked for several years for opera and theatre, including the Deutsche Schauspielhaus Hamburg. She is also working on a PhD project in connection with the University of Hildesheim about visitor relationship management systems in theatres.

Dr Christopher R Long, Senior Data Analyst, Quantiful, LLC (**longcr@quantiful.com**)
Christopher Long is Senior Data Analyst at Quantiful consulting. He received his PhD from the University of Massachusetts in 2003 and then worked as a post-doctoral research associate at Université Catholique de Louvain, Belgium. From 2004 to 2014, he was an Associate Professor of Psychology at Ouachita Baptist University. In 2009, Chris worked as a visiting professor at New York advertising agency DraftFCB. His primary research areas include exploring similarities between consumers' brand relationships and interpersonal relationships. In collaboration with researchers in marketing, psychology, and information science, Chris also studies the effects of brand deprivation, the role of social networking (on and offline) in consumer-brand relationships, and consumer-celebrity relationships.

Anne-Flore Maman Larraufie, PhD, Professor (ESSEC), Founder & Owner of SémioConsult (Paris, France and Venice, Italy) (**anne-flore.maman@semioconsult.com**)
A Military Academy Engineer and PhD, Anne-Flore Maman Larraufie founded her own consulting business SémioConsult in 2010, whilst also pursuing academic research and teaching. SémioConsult is focused on managing brand image and identity, thanks to semiotics, along with getting consumer insights. She is a member of the editorial boards of *The Luxury Research Journal*, *The Journal of Consumer Marketing*, and of *The International Journal of Marketing Research*. She is currently a French government expert on luxury and Country-of-Origin (Made In) issues, a visiting professor in various business schools and universities (INSEEC, HEC, Ca'Foscari, …), and a trainer in brand management when facing counterfeiting issues (France, Morocco...)

Farah Montesa, MSc, Department of Business Administration, Aarhus University, Denmark (**fmontesa@yahoo.com**)
Farah Montesa has a Master's degree in Strategy, Organization and Leadership from Aarhus University, and a Bachelor's degree in Economics from New York University, United State's. She has six years' work experience in the New York fashion industry in management, marketing, sales, planning, and analysis in mass and luxury markets.

Professor Dr Günter Müller-Stewens, Institute of Management, University of St Gallen, Switzerland (**guenter.mueller-stewens@unisg.ch**)
Günter Müller-Stewens has been Professor of Management and Organization at the University of St Gallen (HSG), Switzerland, since 1991, as well as Director of its Institute of Management. Between 2005 and 2007 he was Dean of the business school, and from 2003 Academic Director of the Master of Strategy and International Management. Since 2012 he has been Academic Director of the Master of Business Management. The author of a large number of books and publications mainly in the field of strategic management, his fields of interest are corporate-level strategy, mergers & acquisitions and strategy process. He is an executive education trainer, consultant and member of the advisory board of several international companies.

Daniela Ott, COO, Luxury Division, Kering, France (**Daniela.Ott@kering.com**)
Daniela Ott is Chief Operating Officer, Kering Luxury (former PPR). Over the past 15 years, she has built a dual competency in brand management, strategy and finance, on the one hand, and in merchandising and product knowledge on the other. Daniela Ott was a Director of PPR Luxury, advising its Deputy CEO and CEO, Strategy Director of Gucci Group, and Strategy and Marketing Director at Balenciaga. She graduated *summa cum laude* with a Bachelor's and Master's from the London School of Economics, received the LSE Research Award and Economic & Research Council Award. She also studied at Central St Martins & Bocconi, and was elected a member of the Rising Talents at the Women's Forum for Economy and Society. She is passionate about consumers and brands, researching and lecturing on this topic.

Professor Dr George Panigyrakis, Professor of Marketing, Department of Business Administration, Athens University of Economics and Business, Greece (**pgg@aueb.gr**)
George Panigyrakis is Professor of Marketing at Athens University of Economics and Business. He received his PhD in Marketing Management from University College of Wales. He has worked in industry and taught in several management development programmes for marketing executives and is a founding member of the Greek Institute of Customer Service. He has served on the faculties of Groupe ESSEC and the University of Stirling and has held visiting appointments at Audencia Business School, Rennes Business School, Lille Business School and at the International Institute for Management Development. His research interests lie in the areas of brand management, international marketing and marketing communications. He has published in such journals as *Journal of Financial Services Marketing*, *Journal of Promotion Management*, *Corporate Communications* and *Review of Business Information Systems*.

Professor Alberto Pastore, Professor of Management, Sapienza University of Rome, Italy (**alberto.pastore@uniroma1.it**)
Alberto Pastore is Full Professor of Business Management at Sapienza University of Rome, where he teaches Strategic Management and Marketing. He is the Director of the Master in Marketing Management at the Management Department. He is President of the Italian Management Society (SIMA), the scientific society of all Italian professors of management. He is also on the scientific board of several national and international academic journals. He has published numerous books and articles on business management, marketing strategies, marketing communication, retailing, sustainable marketing, digital marketing and counterfeiting. He is management and marketing consultant for national and international companies and institutions.

Professor Dr Michel Phan, EMLYON Business School, Markets & Innovation, Shanghai, China (**phan@em-lyon.com**)
Michel is Associate Professor of Luxury Marketing at EMLYON Business School, Director of MSc in Luxury Management and Marketing Programme and Editor-in-Chief of *Luxury Research Journal*.

Professor Dr Sven Reinecke, Institute of Marketing, University of St Gallen, Switzerland (**sven.reinecke@unisg.ch**)
Since 2004 Sven has been Professor of Management, specializing in marketing, at the University of St Gallen and since 2009 Director of the Institute of Marketing. He is Director of the Competence Centre, Marketing Performance Management, and the established research programme, Best Practice in Marketing (in close cooperation with Continental AG, Loewe AG, Miele & Cie KG, Deutsche Telekom AG, Galenica AG and Swiss Life AG).

Dr Michael Reinhold, Head, Centre of Competence, University of St Gallen, Switzerland (**michael.reinhold@unisg.ch**)
Michael Reinhold received his Diploma in Physics and his PhD from the University of Basel. After a three-year postdoctoral phase at the ETH in Zürich, he continued his professional career in various high-tech companies in managerial positions. Returning to academia after 20 years, he took a position of lecturer and project manager at the Institute of Marketing at the University of St Gallen. He taught marketing at the ETH in Zürich for 10 years and is currently teaching B2B-Marketing at the University of Berne as well as in programmes for executive education. Furthermore, he is engaged in several marketing projects in different industries. Over the years, he has published papers and book articles about industrial marketing and sales.

France Riguelle, teaching and research assistant, University of Liege, Belgium (**france.riguelle@ulg.ac.be**)
France Riguelle holds a Master's Degree in Business Engineering (2011, University of Liege). She is a teaching and research assistant at HEC School of Management (University of Liege), where she will present a PhD thesis focused on reputation risk management of luxury firms especially in Belgian luxury firms. As a member of the Research Centre on Corporate Performance (CEPE), she has participated in several international conferences and has conducted various researches about the management of luxury firms. She is also involved as an expert in several research projects or consultancies for public and private organizations.

Professor Dr René Rohrbeck, Associate Professor of Strategy, Aarhus University, Denmark (**rrohr@asb.dk**)

René Rohrbeck's research interests are corporate foresight, innovation management and organizational future orientation. His research has been published in *R&D Management, Technology Analysis & Strategic Management, Futures, Technological Forecasting and Social Change* and in several books, including *Corporate Foresight: Toward a maturity model for the future orientation of a firm*. René Rohrbeck has six years' practical experience in the ICT and automotive industry, working at Deutsche Telekom and Volkswagen on strategic management, innovation management and corporate foresight. In addition he has served as consultant for various companies in the ICT, automobile, luxury goods and energy industry.

Professor Dr Marcus Schögel, Associate Professor, Institute of Marketing, University of St Gallen, Switzerland (**marcus.schoegel@unisg.ch**)

Professor Dr Marcus Schögel is the director of the Institute of Marketing at University of St Gallen (IfM-HSG). For over 20 years he has been working in education, research and consulting on innovative and successful approaches to sales. He is the author of the renowned textbook *Distributionsmanagement – das Management der Absatzkanäle*.

Dr Fabian Sommerrock, Principal and member of the management team, Roland Berger Strategy Consultants, Zurich, Switzerland (**fabian.sommerrock@rolandberger.com**)

Dr Fabian Sommerrock joined Roland Berger in 2005 and focuses on the financial industry and public services. He is an expert in strategy development, transformation, post-merger integration and reorganization as well as efficiency improvements and change management. He studied Business Administration at the University of Mannheim (Dipl.-Kaufmann) and Economic Policy at American University, Washington DC, completing his degree in 2004. Fabian Sommerrock did a PhD (Dr rer. pol.) with *magna cum laude* in economics and social science at the Kassel University (thesis: Successful post-merger integration in public institutions). He is a visiting lecture at the University of St Gallen (HSG) has been giving lectures on luxury in the master class since 2012.

Alexander Stigelski, BSc, research fellow, Leibniz University of Hannover, Germany (**astigelski@yahoo.com**)
Alexander Stigelski is a Research Fellow at the Leibniz University of Hannover, Germany, Institute of Marketing and Management.

Dr Prokopis Theodoridis, Department of Business Administration of Food and Agricultural Enterprises, University of Patras, Greece (**proth@upatras.gr**)
Prokopis K Theodoridis is an Assistant Professor of Marketing at the department of Business Administration of Food and Agricultural Enterprises of the University of Patras. He holds an MSc in Marketing (University of Stirling, UK) and was awarded a PhD from the Athens University of Economics and Business. His primary research interests include food and beverage marketing, retail and services marketing, marketing communications, internal marketing and consumer behaviour.

Timo Tischer, MA, Institute of Marketing, University of St Gallen, Switzerland (**timo.tischer@student.unisg.ch**)
Timo Tischer is doctoral candidate at the Institute of Marketing, University of St Gallen, from where he graduated with an MA in Strategy and International Management (SIM) in 2008. Prior to resuming his academic career, Timo worked as a strategy consultant at the Zurich office of The Boston Consulting Group focusing on consumer goods and financial institutions.

Ivan Valek, MSc, International University of Monaco (**ivalek@monaco.edu**)
Ivan Valek is a Croatian writer. He holds an MSc degree in Luxury Management from the International University of Monaco. His fields of interest relate to arts, culture, luxury and management, as well as finding correlation and linkage between those sectors and fields of human activities. He wrote a thesis entitled ‘Corporate art collections in EU: corporate art collecting phenomenon among leading companies on European Union territory’ and is planning to pursue a career in the artistic, cultural, scientific and educational fields.

Professor Didier Van Caillie, Director of the CEPE, University of Liege, Belgium (**d.vancaillie@ulg.ac.be**)
Didier Van Caillie is Full Professor at HEC School of Management (University of Liege) and Director of the Research Centre on Corporate Performance (CEPE, University of Liege). His teaching, research and expertise activities are focused on management control systems, performance management and enterprise risk management, especially in SMEs and hybrid organizations (universities, agencies, health care organizations). He is involved in numerous research projects intending to develop original business models and performance management systems in high-tech firms serving the luxury industry. He has published more than 100 contributions about his research interests that are available via open access databases.

Sofia Vassou, Business Administration of Food and Agricultural Enterprises Department, University of Patras, Greece (**vassousonja@yahoo.gr**)
Sofia Vassou is a PhD student in the department of Business Administration of Food and Agricultural Enterprises of the University of Patras. Her PhD thesis concentrates on consumer behaviour and luxury food. She studied Business Administration at University of Macedonia, Greece and holds an MBA-Food Business Management from the University of Western Greece. Her research interests focus on consumer behaviour and the luxury business.

Dr Vera Waldschmidt, Institut für Marketing und Dienstleistungsforschung Wirtschafts- und Sozialwissenschaftliche Fakultät, University of Rostock, Germany (**vera.waldschmidt@uni-rostock.de**)
Dr Waldschmidt is a post-doctoral researcher in high-end consumer behaviour.

Dr David S Waller, UTS Business School, University of Technology, Sydney, Australia (**David.Waller@uts.edu.au**)
David Waller has over 20 years' experience teaching marketing subjects at several universities, as well as offshore programmes in Malaysia and China. Prior to his academic career, Dr Waller worked in the film and banking industries. His research has included projects

on marketing communications; advertising agency-client relationships; controversial advertising; international advertising; marketing ethics; and marketing education. He has published over 60 refereed journal articles, authored/co-authored several textbooks and workbooks, and is a regular presenter at local and international conferences.

Dr Rui Wang, Associate Professor of Marketing, Peking University, China (**rwang@gsm.pku.edu.cn**)
Wang Rui currently serves as Associate Editor of *Journal of Business to Business Marketing*. Dr Wang gained her PhD in Marketing from Pennsylvania State University. Dr Wang's current research interests are mainly in areas such as B2B marketing, marketing leadership and marketing strategies. Her research has been accepted for publication in journals such as *Strategic Management Journal*. Her work is funded partly by the National Natural Science foundation China.

Wen Yue, Guanghua School of Management, Beijing University, China (**wen.yue@hotmail.com**)
Yue Wen is a master student from the Marketing Department of Guanghua School of Management.

Professor Dr Klaus-Peter Wiedmann, Leibniz University of Hannover, Germany (**wiedmann@m2.uni-hannover.de**)
Klaus-Peter Wiedmann is Chair and Director of the Institute of Marketing and Management, Leibniz University Hannover.

Professor Duane Windsor, Jones Graduate School of Business, Rice University, Houston, Texas, USA (**odw@rice.edu**)
Duane Windsor, PhD (Harvard University) is Lynette S. Autrey Professor of Management in the Jesse H. Jones Graduate School of Business at Rice University. His work focuses on corporate social responsibility and stakeholder theory. His articles have appeared in *Business & Society*, *Business Ethics Quarterly*, *Cornell International Law Journal*, *Journal of Business Ethics*, *Journal of Business Research*, *Journal of Corporate Citizenship*, *Journal of International Management*, *Journal of Management Studies*, *Journal of Public Affairs* and *Public Administration Review.*

PREFACE

There are no simple answers

A luxury good must be rare and desirable. Ideally, it should be close to unobtainable. And yet, the luxury market grows faster than most others, suggesting an ever increasing accessibility to an ever growing populace. A luxury good must be extreme compared to the other offerings in its category but there is something inherently relative about luxury goods, driving the definition of luxury away from the offering itself and toward a consumer's perspective. Although a luxury good is meant to be uncompromisingly extravagant in terms of effort and materials invested, luxury and responsible managerial and consumer behaviour are becoming a more viable combination, creating eco-conscious fashion and hybrid high-performance cars.

When looking to better understand the luxury phenomenon, we hear many industry and consulting voices offering ready-made directions to success in luxury management. Some can even be reduced to single-word statements: China, retail, online, and diversification. However, following these simple imperatives leads to the real challenges: how to enter a vast and foreign market and how to make an impact while not diluting the brand; how to optimize the retail experience and not sink millions in the process; how not only to sell online but also to be successful in doing so; and how to diversify without overstretching the scope of the firm. Industry's approaches to 'the how-to of luxury' vary wildly and largely depend on the individual case – as they should. There are no simple answers. And the question is not only how to ride the recent wave to its end; it is also how this cyclical business will look and have to be managed after the next downswing.

The strong upswing of the luxury business has inspired a growing interest among researchers to shed some light on the luxury phenomenon. But while there is a broad range of publications, the field still lacks common theoretical and methodological conventions.

Luxury consumption still remains cloudy even in its fundamental definitions. There are no reliable approaches to delineating luxury companies and consumers from their non-luxury counterparts. The luxury phenomenon proves, time and again, to be too complex to be framed by scientific models that consider all the interacting factors. Although academia has presented substantial work in the field of luxury, it has not provided many conclusive or simple answers.

While this may sound quite depressing, we find that the luxury market could not ask to be in a better situation. Structures are not set in concrete and there remains substantial opportunity for entrepreneurial creativity. Where there are no simple questions, there is a chance for true uniqueness. And where there are no simple answers, refocusing on asking better questions is what's called for. It is encouraging that neither professionals nor researchers can provide generalizable answers yet – if they could, the market would be past its prime.

Thus, we find that the most fruitful approach to better understanding the luxury market is to engage in a critical discussion, to go beyond easy-to-apply rules and to start reconsidering the questions. This book will give you a contemporary perspective on the luxury market, from a variety of international perspectives, considering a multitude of interesting fields. We do not offer simple answers, but we do promise food for thought on some of the pressing questions in luxury today.

Keeping with our approach of trying to develop better questions, the editors and authors will be happy to discuss your thoughts on the proposals presented in this book. This book is meant to be the beginning of a worthwhile discussion.

Complexity fuels challenges

Organizations in the luxury market offer top-of-the-range products and services in a number of sectors. This shared identity of being part of the leading suppliers in any category brings several benefits like potentially higher profitability and a greater chance of consumer awareness, but it also comes with a particular set of challenges.

A fundamental management problem of luxury is that of producing the extreme top-end offering in one or even multiple sectors at the same time. For companies engaged in luxury, this implies that they have to be able to create and deliver these extremes as a regular output. Thus, organizations in the luxury market tend to the extreme by nature: The most innovative products are being developed by the leading engineers and designers in their field using the best materials; they do not shy away from additional production effort to achieve the perfect result. The product or service is being offered to a very exclusive set of consumers at exceptional prices in environments that go far beyond simply facilitating the sale by immersing the consumer in an experience driven by the extraordinary. But dealing with the excessive can be hazardous: organizations tending to the extreme in their offerings require managers who can guarantee the profitability of the firm. These managers have to find the right balance between creative effectiveness and operational efficiency. If they focus too much on productivity and control, they may limit or even destroy creativity; if they do not steer the creatives toward what is commercially viable, the organization may face financial instability.

Another typical challenge to companies in the luxury field is achieving growth. There are several aspects in this challenge that make it particularly daunting. First, luxury offerings are often driven by craftsmanship. Manufacturing processes at the highest level do not scale well while the increased use of machinery and factory production detracts from the luxury appeal. Secondly, expanding the luxury brand beyond existing product categories can be time-consuming and costly since luxury brands are commonly trusted for their perfection in very specific product groups. Thirdly, luxury products need the cachet of rarity and exclusivity, which erodes with continuous growth. The final challenge appears once growth has happened: how do you continuously stimulate excitement with your brand when your company has grown, production is geared toward quantity and consumers find your products almost everywhere?

Another, particularly notorious challenge for the luxury market is its lack of transparency. The luxurious products market is highly fragmented and, at the same time, many significant brands are being managed under a corporate umbrella; and there are very few organizations that report business figures on a regular and transparent basis. While there are several sources for industry reports, numbers are unlikely to be much more than estimates. Some managers in the luxury field consider the lack of transparency a benefit: less transparency, less competition. However, greater market transparency will substantially increase any manager's understanding and grasp of the market and, in turn, improve strategic decision making.

With these examples of luxury-specific challenges, any market observer would expect a disorganized, unmanageable market segment. However, the success of the luxury sector as a whole as well as the stellar performance of several individual organizations suggests that managing the excessive is possible and that, indeed, it is a question of good management whether organizations in the luxury market flourish or go under.

There is no management of luxury

From a classic, scientific perspective, the management of luxury is nothing new. Research has developed substantial knowledge on managing firms over many decades. This knowledge claims to be applicable to all types of industries and so luxury should not require anything different. How can the growing field of researchers in luxury management justify doing research focused on the luxury segment in which companies commonly engage the market in a classic business-to-customer approach? Do we believe that parts of the generic management knowledge we already have can't be transferred to this segment, or has at least to be modified?

A central argument against a common denominator of management practice in the luxury industry is that 'the luxury industry' is no more than an idealized construct of consultants and researchers: it is an ill-defined amalgamation of companies, corporate affiliates, business units and integrated brand management teams acting in a virtual world of brands. Due to the subjectivity of the term, even experienced professional observers struggle to robustly delineate the luxury industry. Arriving at a common practice of managerial specialization would require some sort of a homogeneous setting for this specialization, but luxury is anything but homogeneous.

Furthermore, since the business of luxury is not tied to one particular industry, each of the industries represented contributes different development stages, business cycles, competitive dynamics and business models. For example, the luxury cosmetics business is already much more industrialized than that of watches. Only a few companies dominate the worldwide market for fragrances while in watchmaking, we can still find hundreds of small and medium-sized companies. Luxurious jewellery, for example, is produced to last for generations, while in the luxury fashion business, products are created to last one season and the designer has to be able to reinvent his or her offer in half-year cycles. In selling luxury experiences, success depends on personal interaction and experience during the service while selling personal luxury goods relies on the quality of the tangible product and the kudos it gives to the consumer when it is being worn or used. Thus, managers are more likely to adapt to local challenges and to seize industry-driven opportunities than to think in terms of a vague notion of a specific market segment.

Beyond the rather ambiguous definition of the industry and the introduction of multiple cultures by the industry members' original sectors, what is really there to find? Organizations offering premium products are, just like other organizations, focusing on basic economic mechanics and dealing with quite ordinary business challenges. Even if there were a coherent group of companies that could be considered a specific sector in its own right, the insights generated for management in this field would centre on the same challenges and require the same training as management in any other area. Indeed, where there is a strong artistic and craftsmanship influence, traditional managerial training may bring a necessary business discipline to otherwise rather loosely organized companies. This could help steer organizations away from overspending on product development and undervaluing the economies of scale and instead focus on the bottom line and ensure financial survival.

Taking a critical approach thus debunks luxury management as a fad of its time. Luxury management is nothing but a product of a local upswing in a market segment, driven by consumer demand and not by systematic and professional development of organizational and industrial structures, increased competition and industrialization. There is no luxury management.

Or is there?

Any scientific field specializing in a particular business segment is likely to be challenged by the more established, fundamental research community. The common question is: does management in this sector really behave differently to other industries? Do the established rules really not apply? Can a common denominator for successful luxury management really be ruled out? We feel that luxury meets the challenge.

Fundamentally, luxury is not a homogeneous industry in the classic, product-category-driven sense. Rather, it is a group of businesses with the common factors of high performance, high status and high price products aiming to satisfy homogeneous consumer needs. This notion leads us away from the impression that research in luxury aims to assume the role of an industry-specific research field and toward analysing the impact of a strategic business decision that imprints on all aspects of the organization. We are not looking at a group of companies that produce the same product; rather we are looking at companies that are being driven by the same approach to quality, performance and appeal to consumers and other stakeholders.

The business of luxury goods emerges in a very specific context, in which creative and aesthetic values are central to their process of value creation. This opens up luxury-specific management challenges. Which governance regime works best in a context of exclusively commercializing creativity? What would be the impact of losing key personnel like the art director on the organization's creative performance? Shifting the focus from the artistic toward the common aim of manufacturing perfection, another joint characteristic appears: the innovative capacity of the organization and the uniqueness of its products and services are key factors for success in the luxury goods business. But how can the development of unconventional strategies be stimulated? What, for example, is the role of cultural resources in such a process?

The core asset of a luxury goods company is its brand. In the consolidated balance sheet of LVMH, the brands (and some other intangible assets) count for 23 per cent of total assets (€49.93 billion). Therefore the focus of the top management is on branding. Considering the social mechanics of consumer behaviour in the luxury domain, the brand changes from being a marketing tool for consistency into the product itself. The handbag is the product, but the brand satisfies the central consumer need as it assures the highest quality and indulgence as well as social prestige and differentiation from the masses.

Having focused on many of the consumer-oriented aspects that characterize luxury companies, the industry is beginning to establish itself. There is continuous consolidation going on in the luxury business. Indeed, there are many developments in the luxury market that are comparable to those in other industries. The mechanisms behind these developments seem to work as follows. A small number of dominant and diversified multi-business and multi-brands companies have emerged. Together, the leading three companies (LVMH: €29.14 billion sales and more than 60 brands; Richemont: €10.15 billion sales and 19 brands; Kering: €9.75 billion sales and 20 brands) account in 2013 for almost a quarter of the €217 billion market for personal luxury goods. Since organizations in luxury are getting larger and more global, managers of these companies learn to steer complex multi-dimensional organizations and have to industrialize their manufacturing processes to realize the benefits of scale.

Companies in the luxury market manufacture products that are exceptional in terms of materials, the detail and quality of craftsmanship, experience and performance in use and design. Thus, luxury companies rely on their manufacturing capabilities to achieve their central claim to a common identity. This common identity, rooted in manufacturing excellence, leads to the need to develop innovative products of the highest quality and value. Furthermore, the majority of the brands and goods are produced in a few European countries. The European heritage and the often very long tradition of the brands is one of their major differentiating factors.

With regard to business profitability, organizations in luxury are both advantaged and challenged. On the one hand, luxury goods can be priced highly, yielding large margins. However, luxury goods are produced in much smaller quantities than mass-market products, so benefits from economies of scale in production are limited. With regard to the organizational value chain, luxury companies cannot compromise when they decide to focus on the very top end of the market, so they face the risks that come with the substantial investment needed to attract consumers willing to pay the highest prices.

Comparing both sides, arguing for and against a specific management logic for luxury, we once again conclude that there are no simple answers to be found. The management of luxury is as much a statement as it is a question. With this book, we would like to invite you to think about the management of luxury as a question, and to consider the many different perspectives, ideas and cases present in this book.

Our motivation

The strategic changes and particularities of the business motivated us to bring together academic knowledge on a broad array of luxury goods topics, to encourage a discussion on the industry dynamics. In particular, there were four thoughts that motivated us to initiate and edit this book.

We believe in the value of scientifically-founded insights for business students and practising managers alike. With regard to mechanisms, the luxury business is likely to be comparable to other non-commodity fields. However, on questions of how to operate the mechanisms, which levers to pull and in which order, we find many differences between the mass-market and the luxurious. Thus, the value of insight in luxury business is rather small in terms of introducing new theory, but very rich with regard to applying existing theory and dealing with effects introduced by the extremes of luxury business. Thus, we aim to provide links between the classic theory of the firm and the particularities of luxury business.

We are convinced that publicly-funded academia owes generated insight to society. While the contract between research and public funding is obvious, engagement in the luxury business requires some justification: luxury is not among those topics readily associated with societal benefit. Taking a closer look, we find that many organizations in luxury are commonly among the oldest in their field. They are the places where traditional craftsmanship was cultivated over centuries, protected against the short-term winds of change, and enhanced to amazing levels of excellence. Thus, closer inspection may lead to insights on the longevity of organizations. Businesses in luxury push forward innovation in their sectors because the prices that can be levied enable greater investment, and customers expect outstanding performance for expensive purchases. Finally, luxury seems to be one of the few types of offerings that organizations in Europe will be able to produce in the foreseeable future that are not limited to local production for logistical reasons, but because it is seen as a field where Europeans have a clear competitive advantage. Thus, aiding the professionalization of the management of luxury is intended to support this valuable part of the European industry landscape.

We believe in the value of fresh and innovative perspectives. Literature on luxury is nearly as old as the written word itself, not least because luxury has always had connotations of lust, exuberance, prodigality and sin. In more recent scientific thought, luxury has seen an increase in attention since the 1990s, with a small school of mainly French scientists investigating the nature of the term. In the 2000s, there was substantially more published, with several authors establishing themselves in the field. When developing the concept for this book, we made a conscious decision to provide a forum for new voices, especially junior academia. With this decision, we aimed to introduce new ideas to a topic that is generously endowed with previous thought but that could benefit from new perspectives and impulses.

We share the belief that the increasing complexity of the management challenges in luxury organizations needs an interdisciplinary approach. Up to now the field has been dominated by marketing research, for good reasons. But creating core competencies for the future, to compete with superior business models, and to manage manifold types of partnerships, requires the interaction and close collaboration of all management disciplines. Therefore we did not focus our call for chapters on a specific discipline, but purposefully invited authors from all fields of management science.

Perspectives on the topic

This book covers a variety of topics on the management of luxury today: introducing thoughts on the market itself, presenting perspectives on the actualization of luxury brands, particularities of strategic management, and putting a spotlight on the important topic of corporate social responsibility for luxury organizations.

In the first part, 'The luxury market', there are four contributions. First, the editors present an introduction to the business, giving not only accounts of the elements, drivers and the status quo, but also reflecting on those readings in luxury research that have had the greatest impact. In Chapter 2, Jäckel adds a socio-historical perspective on luxury and gives an overview of the origins of the field. In their contribution on luxury consumer behaviour, Theodoridis and Vassou (Chapter 3) return the reader to today's market and conceptualize the known mechanisms behind the phenomenon that is luxury consumption. In Chapter 4, Heine, Phan and Waldschmidt conclude the part with their account of the construction of luxury brands.

The second part, 'Luxury brand strategy', presents seven contributions that consecutively build on each other to span the distance from the designer and artist to the luxury retail setting. In Chapter 5, Breazeale, Long and Ott point to the role of the public face of luxury brands, and Lawry and Helm in Chapter 6 introduce the concept of curating creative genius within luxury brands. Baumgarth, Lohrisch and Kastner (Chapter 7) pick up the concept of the central figures in luxury and apply this idea to the role of art for luxury. Panigyrakis and Koronaki (Chapter 8) add a broader perspective, taking into account the role of luxury as a societal mentor. In the contribution by Chailan and Valek (Chapter 9) we look at the implementation of art in the luxury retail setting, while in Chapter 10 Dion and Arnould write about charisma and adoration. Chapter 11, by Schögel and Tischer, concludes the part by considering the digitalization of the retail space and branded behaviour.

The third part of the book, 'Luxury business strategy', opens with Chapter 12 in which Beil, Sommerrock and Gaus present a perspective on European luxury brands entering the Chinese market, while in Chapters 13 and 14 Wang, He, and Wen respond with an historical account of the diverse market entry modes commonly employed in China and a recommendation based on best practice. Wiedmann, Klarmann, Hennigs, Behrens and Stigelski (Chapter 15) present a study of vertical brand extensions while Arrigo (Chapter 16) gives an account of the role of online business for organizations in the luxury market. Dealing with aspects of competitive behaviour, the contributions by Riguelle and Van Caillie (Chapter 17), Reinhold and Annen (Chapter 18) and Maman and Depigny (Chapter 19) first present a study on competing as a small or medium-sized enterprise in luxury, then a case study on the luxury-positioned sole remaining European camera company, and finally elaborate on the role of price fluctuations in luxury organizations. Counterfeiting is discussed by first describing the problem in detail (Maman, Chapter 20) and then proposing an action framework to manage the challenge (Cesareo and Pastore, Chapter 21). This part concludes by taking a look at challenges in human resources. Here, the role of a prestigious brand image in attracting employees (Batt and Berghaus, Chapter 22) and the role of luxury image for management performance (Berghaus and Reinecke, Chapter 23) are discussed.

The final part of our book takes an in-depth look at the role of corporate social responsibility. The compatibility of luxury and social responsibility is investigated in the form of a conceptual literature review by Windsor (Chapter 24). In Chapter 25, Montesa and Rohrbeck propose a CSR toolbox for luxury organizations, and finally, Waller and Hingorani (Chapter 26) give a case analysis of the social engagement of luxury's biggest corporation.