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HEALTHCARE

What the coronavirus outbreak means for the luxury business

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Burberry is among the luxury companies whose stocks fell amid coronavirus scares. Image courtesy of Burberry

By SARAH JONES

As the outbreak of the coronavirus in China worsens, there could be significant ramifications for the luxury business that has grown dependent on Chinese consumers for growth.

Looking to contain the spread of the coronavirus, the Chinese government has banned travel to and from a number of cities and it has canceled all group trips from China. From Europe to Japan, stock markets have taken a dive amid worries of the financial implications of the outbreak, but what are the long-term implications for the luxury market?

"We are closely monitoring the situation with a local team in China," said Marie Driscoll, managing director luxury and fashion at Coresight Research, New York. "Lots of unknowns, but near term, buying luxury won't be top of mind for people in the region.

"Travel plans are being canceled," she said. "Luxury sales will be impacted, however many will find luxury products online, mitigating the drop in sales at brick-and-mortar flagships."

Outbreak outlook

The coronavirus is thought to have originated in Wuhan, a city of 11 million people within the centrally located Hubei province.

More than 100 individuals in China have now died from the disease, and more than 4,000 people in China have been diagnosed with the virus. Cases have also popped up in the United States, France and Japan.

Many are making comparisons between this virus and severe acute respiratory syndrome (SARS), which originated in Guangdong in 2002. SARS resulted in more than 8,000 cases of the disease and 774 deaths, according to the Centers for Disease Control and Prevention.

Unlike SARS, the coronavirus is said to be contagious even before individuals are showing symptoms, making it potentially more easily spread as travelers who do not realize they are carriers infect others. According to a report from the *South China Morning Post*, China's National Health Commission minister Ma Xiaowei said, "The outbreak is expected to continue for some time."

Back in 2003, Asia excluding Japan accounted for about 14 percent of total luxury sales, according to a report from CNN. Comparatively, Chinese consumers alone accounted for 35 percent of the luxury market in 2019 and 90 percent of total luxury growth during the year, according to Bain.

Last year, Mainland China saw the strongest growth of any region, with sales rising 26 percent. Part of what drove growth in China was Chinese consumers spending at home, as they shied away from traveling to Hong Kong and international destinations (see story).

Some luxury companies' exposure to China is even greater than 35 percent.

Per UBS, an estimated 50 percent of Swatch Group sales are to Chinese consumers, with around 45 percent for Richemont and roughly 40 percent for Burberry.

Similarly, Chinese consumers account for an estimated 35 percent of sales at Kering, Moncler and Prada, and around 30 percent at LVMH, Salvatore Ferragamo, Herms and Tod's (see story).

With travel bans in place in Wuhan and other parts of the Hubei province, destinations in Europe and elsewhere may see an even further slowing of tourist traffic from China. Chinese New Year, usually a popular travel time, has been extended in an effort to reduce travel within China.

The quarantine is also dealing a blow to industries that operate in the Wuhan area, including automakers such as Cadillac that have production facilities there.

General Motors' Wuhan plant. Image courtesy of GM

"With China authorities restricting travel for 35 million people in more than 10 cities including Wuhan, retailers across auto industry, non-luxury and luxury retail, restaurants and furniture industries have either temporarily shut down or decreased operations to minimal manning," Ms. Driscoll said. "The labor workforce is limited and all industries are awaiting word to fully open their operations."

Along with travel bans in China, both the United States and Canada have issued travel warnings to their citizens about visiting China and Hubei, respectively.

Luxury stocks for companies including LVMH, Kering, Richemont, Burberry and Herms were all down between 2 and 4 percent on Jan. 17 as investors showed concern for the outlook amid the viral outbreak.

Meanwhile, airline firms including Deutsche Lufthansa and Air France were also down.

According to UBS, share prices of share prices of luxury goods stocks fell 20 percent between November 2002 and April 2003 during the SARS epidemic.

Projections from Bernstein estimate that China's real GDP growth will lose between 0.8 percent and 1.9 percent points, depending on whether the epidemic lasts three months or nine months. Comparatively, SARS lowered the nation's GDP growth by two percentage points.

"If the virus spreads, stock prices will likely remain under pressure, reflecting reduced demand and lack of visibility," Ms. Driscoll said. "The travel ban has affected tourism and retail, and restrictions are impacting the regional economy and most parts of China.

"It is anticipated that GDP in Wuhan may decrease 0.5 to 1 percent in 2020 against the forecasted 5.9 percent, compared to 7.8 percent in 2019," she said. "However, some economists anticipate that the coronavirus will have only short-term economic impacts, similar to past similar natural disasters and epidemics including SARS in 2003 to 2004.

"During the SARS crisis, retail growth rebounded in 2003 from 4.3 percent to 8.3 percent during the second and third quarters, and economic impact was $40 billion to the world economy. However during the SARS crisis, Chinese spending was less than 10 percent of the luxury market, compared to today at about a third of global spending, so the impact to the luxury market is likely to be more extreme if this is prolonged."

China concerns

The coronavirus outbreak comes during an already turbulent time for the luxury business in China.

Amid political unrest in Hong Kong, personal luxury good sales are down 20 percent from 2018, per Bain. Despite an estimated 40 percent decline in tourist visits and a decrease in foot traffic between 30 and 40 percent, the consultancy notes that luxury store counts are remaining stable, with approximately 1,000 monobrand boutiques (see story).

This commitment to bricks-and-mortar retail in Hong Kong may change as the demonstrations drag on.

French fashion label Louis Vuitton is shuttering one of its Hong Kong outposts, making it the first luxury retail casualty of prolonged protests in the region.

Louis Vuitton will close its store in the Times Square mall, located within the Causeway Bay shopping district, as first reported by the *South China Morning Post*. Since early June, protests in Hong Kong have impacted the local economy, from retail to tourism, leading to a fall in luxury spending (see story).

In the midst of the coronavirus, digital engagement is one way for luxury brands to maintain relationships and business.

"[Brands] can communicate via social and WeChat with their consumers," Ms. Driscoll said. "Keep them engaged and drive demand. Increase gamification to help change the focal point."