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RETAIL

What will a second wave of COVID-19 mean for the luxury world?

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After becoming the poster child of COVID-19 success, Europe has become careless and triggered a second wave of infections. How will it impact luxury? Image credit: Shutterstock

By Adina-Laura Achim

CNN reports that Madrid is returning to lockdown measures in a push to curb a dramatic resurgence of COVID-19 cases.

The Spanish capital's corona-related measures include restrictions on hosting large gatherings only six people per meeting and new limits imposed on indoor establishments, which are now forced to reduce their capacity by 50 percent and close their doors by 10 p.m.

Moreover, individuals are not allowed to "leave or enter their area except for work, education or health reasons," according to CNN.

After reporting 12,565 cases of COVID-19 on Oct. 11, France is raising its alert to the maximum. The BBC states that there are currently 203 active COVID-19 "clusters" in the wider Paris region, so authorities have announced the closure of bars, gyms and swimming pools.

This week, the Italian government will release a new emergency decree with strict measures intended to curb the number of COVID-19 infections, and the United Kingdom put the breaks on the country's reopening as the number of cases surged again.

After initially becoming the poster child of COVID-19 success, Europe became careless and triggered a second, much-feared wave of infections. So, how will a second wave of COVID-19 impact luxury?

At the current level of infections, we foresee that manufacturers, ateliers and retailers will not shut off production lines. But they will have to implement precautionary measures and provide protective gear to their employees. These new workplace safety measures will be costly.

"Businesses will need to put in place new safety measures to combat the spread of the coronavirus pandemic," said CNN Business. "That will change how companies, employees, customers, and the government interact with one another. And it will cost the private sector and the customers they serve a pretty penny."

According to a report from the ratings agency Moody's, companies that invest in prevention practices and safety measures are left with fewer funds for paying off debts and stock investments.

Also, spending data shows that post-COVID-19, affluent European consumers kept their wallets closed and stayed away from irrational purchases.

Reuters highlighted a study done by the London Business School of card transaction data, which showed how British consumers with an after-tax income of at least 40,000 pounds ($51,250) accounted for around 35 percent of spending in 2019. Yet this same group was responsible for 45 percent during the second-quarter decline of 2020.

In a bid to maintain their margins, the world's most famous luxury brands hiked prices for their top-performing products, such as leather bags and accessories, during the first wave of COVID-19.

Take, for example, Louis Vuitton Moet Hennessy. Despite a strong rebound in mainland China, Business Insider reports that LVMH recorded a sales drop of 27 percent in the first half, and profits from recurring operations declined 68 percent, from 5.30 billion euros in 2019 to 1.67 billion euros.

Then the group tried to redress its profit margins by employing exploitative price strategies in Asia.

Instead of lowering prices and using discounts to liquidate any surplus inventory and generate cash, luxury brands hiked prices or redistributed their products to different markets.

Premium brands also engaged in inventory swaps. But price hikes punish loyal customers instead of compensating them for their devotion, and even exploitative pricing strategies will not save distressed luxury companies that could be targeted by overseas investors.

Since the 2008 recession, various European heritage brands have been acquired by overseas investors and private-equity firms or became subsidiaries of foreign companies. And despite best efforts from European Union officials, it is expected that this crisis will open up some companies to hostile takeovers and investments.

Foreign Policy highlights that Beijing could use the post-pandemic crisis "to go on a buying spree."

Lastly, Western consumers should expect big changes for the upcoming holiday season.

Those formidable sales that were a reminder of the 2008 recession are unrealistic. Nowadays, retailers are far better prepared to deal with a crisis than they were in 2008 or at the beginning of the pandemic.

Simeon Siegel, a retail analyst at BMO Capital Markets, told the New York Times that retailers had time to reduce their inventories to avoid the drastic price markdowns that decimate margins.

"People hear pandemic' and think of mass discounts," Mr. Siegel said. "The reality is, unlike 2008, retailers and brands clamped down, stopped ordering, and, therefore, the surprising truth is that inventory seems fairly under control.

"So come the holidays," he said, "depending on what the demand looks like, I don't know that everyone should be expecting fire-sale prices."

As such, privileged markets that have won the fight against COVID-19 and have a high concentration of cash-rich consumers China, South Korea, Singapore and Japan should expect another wave of price hikes.

At the same time, wealthy consumers in traditional luxury markets such as the E.U. or the United States will pause their discretionary spending, focusing on essentials.

There is also strong evidence that the European and North American holiday season will move online.

Because of fear of raising COVID-19 infection rates and chaos at stores, consumers will buy their holiday gifts from ecommerce platforms instead of bricks-and-mortar stores.

It is safe to say that this holiday season will be unprecedented, and crucial changes should alter the retail ecosystem for good.

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