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As Q1 results disappoint, should brands look beyond China?

May 18, 2022

From Tod's to Tesla, many brands reported plummeting sales in the first quarter due to China's lockdowns. Is this a lesson on overexposure? Image credit: Roger Vivier

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Tapestry, Tod's and Tesla: these are just a few names in the long list of brands that reported less-than-stellar results in the first quarter.

While China was the saving grace for global companies when the rest of the world was shuttered, roles have been reversed.

With the government relentlessly sticking to its zero-COVID policy, Shanghai has remained in lockdown for almost two months, trapping residents indoors and leaving retail outlets deserted.

In fact, the financial hub moved to impose its tightest restrictions yet last weekend, barring commercial food deliveries and forcing those who live near positive cases to move into quarantine facilities.

Naturally, brands with wider exposure to the market were dealt bigger blows.

Roger Vivier, for example, was the only label in the Tod's Group portfolio to report single-digit growth rather than double-digit growth due to its larger footprint in China: 22 stores in the mainland, four of which are in Shanghai.

The owner of Tod's and Hogan also reported that 30 percent of the company's stores remain shut, while goods are stuck at its distribution center in Shanghai, making it impossible to fulfill ecommerce orders.

Luxury fashion was not the only category impacted.

Tesla, which saw its Gigafactory in Shanghai closed for weeks, was the automaker that suffered most in the world's largest EV market, with sales in April plunging 98 percent from March.

Although Tesla CEO Elon Musk downplayed concerns about the lockdowns, the company has cut its daily factory output to fewer than 200 cars because supplies of some key components had been suspended.

Even the food and beverages category was not spared from sluggish spending.

Starbucks suspended guidance after reporting same-store sales in China fell by 23 percent in the quarter a stark divergence from the 0.2 percent increase analysts expected.

"Conditions in China are such that we have virtually no ability to predict our performance in China in the back half of the year," said interim CEO Howard Schultz on an earnings call.

However, many brands were able to offset these losses thanks to the strength in North America and Europe.

Aeffe, parent company of Moschino, nearly tripled its net income in the three-month period, as Europe which represents almost one-third of its total revenue jumped 37.5 percent, thanks to Germany and the United Kingdom.

Tapestry shares even climbed on May 12 after it posted that sales in North America rose 22 percent year-on-year, fully offsetting mid-teens decline in China.

These two regions will be crucial as China slowly recovers from its worst COVID-19 wave since 2020.

Although the mainland is on track to become the world's largest luxury market by 2025, the United States is still in top spot, accounting for 31 percent of the global market, with China accounting for 21 percent.

As such, it is important for brands to continue building traction in North America and Europe to cushion against near-term losses in Asia.

Given that about 375 million people in 45 Chinese cities were in some sort of lockdown in April, regional sales will likely continue to struggle in the second quarter.

Beijing imposing stricter measures to curb the virus, although denying rumors of a Shanghai-scale lockdown, also makes it unlikely that the zero-COVID policies will lift soon, particularly as the capital gears up to host the party congress in November.

Even when Shanghai inevitably does lift its lockdown, it may take a lot more than coupons to stoke consumer spending. Luxury should brace for a bumpy ride.

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