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International Development Strategies of Luxury-goods Players in China

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The aim of this paper is to study and analyse the internationalisation strategies chosen by the main luxury-goods players in the Chinese market, demonstrating the business internationalisation processes. The research questions are: How luxury companies have developed distribution strategies in the Chinese markets? What are the main formats of distribution for the Chinese markets? Are there any differences in the internationalization process between the main players of the luxury markets and the smaller ones? The methodology is based on the analysis on multiple-case analysis on a sample of luxury-goods companies and identifies and compares the different strategies used by the players analysed. The research process starts from identifying and selecting the most well-known companies operating in the luxury branded sector, which have established a presence in the Chinese market with their own brand, collecting secondary data for the selected companies (website, corporate profile, articles on websites and in trade magazines and interviews with the management), analysing the data collected and interpreting the main results to have emerged from the research. The main findings and conclusions are that the route to development in the Chinese market taken by the players in the luxury-goods sector, historically undertaken by delocalising production operations, has in recent years begun to accelerate with new forms in play, principally linked to distribution. The Chinese market for luxury brands is ever more an outlet market rather than a production hub. The ability to create brand awareness will become a key factor for successful consolidation of the competitive position in this market, an operation that can only be performed through distribution. Moreover, Chinese high-end consumers are becoming ever more demanding, seeking out an ever more sophisticated shopping experience. Just as happening in other markets, opening directly operated stores is a strategic choice for reaching and convincing end-consumers, since these stores become their point of contact with the brand. Creating a shopping experience plays a central role in communicating the values, heritage and spirit of the brand to consumers. Global luxury-goods enterprises are multiplying their investment in opening new sales outlets, using different formats to create distribution system that is predominantly selective but that ensures adequate distribution coverage. The development of direct distribution channels, alongside the more traditional forms of indirect presence, is accompanied by the more innovative players developing the digital channel to accompany and support their retailing activities.

Keywords: marketing luxury goods, internationalization process, Chinese market, global distribution strategies

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* This paper is the joint work of two authors, however, the introduction, the paragraph on research methods and the conclusions are attributed to Piergiorgio Re while the other paragraphs are the work of Fabrizio Mosca.

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Introduction

International development strategies are created by taking action in the field of distribution. Gone are the days of production delocalisation, now this happens through direct and indirect distribution agreements.

An analysis of this phenomenon is useful for gaining an understanding of the factors that have played a role of both cause and effect in the internationalisation of markets and that have given rise to this and favoured its development (Caroli, 2008; Kapferer & Bastien, 2012).

- Scientific and economic development: Investment in creating ever more innovative products has grown exponentially, accompanied by the shortening of the life-cycle of some products, leading to their rapid obsolescence. Given this situation, expansion into new markets becomes an imperative issue.
- Development of transport and logistics systems: The steady improvement in transport systems has led to more rapid transfer times and the evolution of much quicker and more effective logistics, including in non-local markets.
- Innovation in communications: The internet has become the essential vehicle for the transfer of data, revolutionizing communications everywhere and with anyone in the world, saving vast amounts of time and money.
- Market liberalization: International agreements have led to the signing of the GATT (General Agreement on Tariffs and Trade) in 1947 laying the foundations for multilateral systems of trading relations with the aim of encouraging the worldwide liberalization of commerce. This subsequently led to the creation of the WTO (World Trade Organization) in 1995, charged with liberalizing the exchange of trade, standardizing the treatment of imported products, and eliminating the differences between economic operators.
- The international development of businesses: In addition to the transfer of goods, capital, human resources, and knowledge, it has become possible to scale up production, thus reducing the average unit cost of products.
- Homogenization of lifestyles and consumption: This affects more advanced populations. The reduction in cultural differences has facilitated contact between diverse socio-economic entities, leading to the emergence of groups with ever more purchasing power and a steady increase in per capita income. This has encouraged companies to broaden the spectrum of their potential customer base to the extent that it is now these companies that are disseminating culture.
- Opening-up of financial markets: Following a series of international agreements, the circulation of capital has become progressively freer, supported by ever more effective and efficient information technology, guaranteeing the transfer of data between the traditional bourses and those of emerging markets.

Until a few decades, China was seen as a far distant land, from both the cultural and economic point of view, but today it is a powerhouse of development that is intensive as well as rapid. China is now one of the strongest competitors both in its own internal market and in overseas markets, achieving this without losing any of those characteristics that render entry into this important market particularly difficult and contradictory.

Numerous Western players in the luxury-goods sector, after working out suitable strategies and making sufficient investments, have embarked on a practical path to the long-lasting development in this market.

At least 80% of the major luxury brands with a high global profile are now in direct competition with each other, although their approach differs in terms of their timing for entry into the Chinese market. There could be said to be three waves of entry, corresponding to similar phases in the economic and political situation in China at the time of entry.

The first entry wave took place between 1990 and 1995, a period during which the Chinese luxury-goods market was penetrated by a limited band of players who could be thought of as pioneers. In our sample there are Zegna, Louis Vuitton, Burberry, Dunhill, Ferragamo, and Hugo Boss. It was only from the beginning of the 1990s that the nation began opening up economically and in terms of trade, following an era when the authoritarian government had imposed limits on the consumption of high symbolic value goods.

The second wave happened between 1995 and 2000, with the entry of an increasing number of Western luxury-goods companies, among which were Gucci, Hermès, Lancôme, Armani, and Max Mara, attracted by the growing income and purchasing power of Chinese citizens, that gave rise to a broadening of the potential market of consumers of luxury goods.

The third wave, starting from 2000, saw the entry of the late-comers, possibly simply more prudent enterprises. Faced with the unstoppable growth of the Chinese economy, even these more cautious players could no longer pass up the huge opportunities offered by the Chinese luxury-goods market and be left out in the cold. This wave saw the entry of Chanel, Prada, Dolce & Gabbana, and other major brands analysed in our multiple-case study, for example, Porsche and Coach.

The information relating to entry timing is particularly significant because trade liberalisation both internationally and within China has been a gradual process, imposing some severe limitations on the strategic options for entry, and the earlier luxury goods companies took that first step into the Chinese market, the greater were those limitations.

One of the most important moves in China's economic and commercial opening-up process was its entry into the WTO in 2001 that led to a steady reduction in customs duties on all products.

Entry into the WTO also had an effect on domestic trade in that it became possible for international companies to operate in retail sales by setting up joint ventures with a Chinese partner.

In the light of the above analysis, it follows that the first-movers had considerably fewer strategic options available for entry to the Chinese market due to the regulatory constraints, while second-wave and late-comers benefitted from a much broader spectrum of business opportunities.

Literature Review

Ever since the early 1990s, theories surrounding the processes of internationalisation have demonstrated the surprising growth in interdependence among the markets of the main geopolitical areas. In the past, the competitive environment was, for most companies, their home nation whereas today, borders have faded away, leaving with ample space for manoeuvre. This phenomenon is known as globalisation, in which single markets are formed on a worldwide scale with the consequent integration of different parts of the world. Subsequently, a number of studies have focused mainly on the content of international management (Doz, 1980; Doz, Bartlett, & Prahalad, 1981; Hamel & Prahalad, 1983; Prahalad & Doz, 1987; Bartlett & Ghoshal, 1987, 1988, 1989, 1992). Any business wishing to expand into new international markets needs to be well equipped with management and organisational skills (Zaheer, 1995; Zaheer & Mosakowski, 1997).

Finally, some authors (Stopford & Wells, 1972; Johanson & Vahlne, 1977; Boone & Kurtz, 2012) maintained, also on the basis of empirical evidence, that selection of entry methods is conditioned by the company's international experience and its product diversification strategies, as well as by the cultural and national differences between the country of origin and the target nation. During the 1970s, theoretical research into internationalisation processes focused on the attempt to explain the international expansion process as slow and incremental, typical of the large-scale manufacturing enterprises (Johanson & Wiedersheim, 1975; Buckley & Casson, 1976; Rugman, 1981; Dunning, 1988; Johanson & Vahlne, 1990; Andersen, 1993).

During the next decade, the research gradually extended to small and medium-sized enterprises that were beginning to operate on the international scene in a wide range of industries, despite their limited resources and capacities (Sharma & Johanson, 1987; Welch & Luostarinen, 1988; McDougall & Oviatt, 1994; Bell, 1995; Coviello & Muno, 1997; Madsen & Servasi, 1997; Cafferata & Genco, 1997; Coviello & McAuley, 1999; Aprea & Di Napoli, 2002; Hines, 2004).

More recently, the internationalization process has been analysed as a delocalization of production process (Dematté & Perretti, 2003; Pellicelli, 2007; Valdani & Ancarani, 1995; Galdini, 2009; Bertoli, 2010; Atwal & Bryson, 2014). According to the literary review, there it seems necessary to develop studies regarding the internationalization of distribution activities. Some authors have developed studies about the internationalization process (Corbellini & Saviolo, 2007; Hoffman & Coste-Manière, 2013; Chrysostome & Molz, 2014) and more specifically about the internationalization of Made in Italy companies in global markets (Aiello, 2005; Cedrola & Battaglia, 2012). This study investigates and focuses its attention on the internationalization process with the distribution variable in the Chinese market for luxury goods.

Research Methods

The methodology for this study involved conducting a multiple-case analysis on a sample of luxury-goods companies. The research process took place over the following phases:

- identifying and selecting the most well-known companies operating in the luxury branded sector which have established a presence in the Chinese market with their own brand;
- collecting secondary data for the selected companies (website, corporate profile, articles on websites and in trade magazines and interviews with the management);
- analysing the data collected and interpreting the main results to have emerged from the research.

The companies analysed can be divided into two broad categories:

- the first-movers, pioneers who are notable for being the first entrants into the People's Republic of China, already there by the 1990s;
- the late-comers, businesses only embarking on international development with their own brand in the last decade.

Multiple-case Analysis and Research Results

Adopting the multiple-case analysis method has made it possible to identify the principal strategies selected by businesses for internationalisation in the Chinese market.

The prime objective is to provide an accurate representation of the most innovative and dynamic aspects of the processes underway and secondly, to identify the alliances forged between the businesses studied and local importer-distributors.

The analysis was performed according to the following system and logic.

- Each case-study was analysed in depth, starting from the entry period and the entry strategies adopted, and then proceeding to an examination of the development strategies, the distribution formats, penetration strategies, and the strategies for branding and communications;
- A further variable is the period chosen for the sample, taking into consideration both major players and

small and medium-size enterprises in the luxury-goods sector which appeared in the Chinese market at different times;

- Finally, corporate documents and such official documents as investor information sheets and financial reports were analysed.

The initial results are summarised in the table below.

Table 1
Chinese Market Entry Strategy

Players	Periods	Company	Entry Year	Entry Method	Evolution	Current Situation (2014)
Major players	Initial entry wave (early 1980s-1995)	Ermenegildo Zegna	Early 1980s	Opening of a subsidiary	2003: acquisition of 50% of the local company sharemoon as an E-commerce platform	80 boutiques in 35 cities in mainland China
		Burberry	1993	Creation of a WFOE and investment in the web		71 boutiques in 36 cities in mainland China
		Alfred Dunhill	1994	First sales outlet, a franchise, opened in Beijing (importer-distributor strategy)	2006: joint-venture with China Resource Holdings Co. Ltd	58 boutiques in 18 cities in mainland China
		Salvatore Ferragamo	1994	First sales outlet opened in Shanghai. (Importer-distributor strategy)	Creation of subsidiary. January 2013: achieved 75% of the share held by Imaginex Group with which it had set up a joint venture agreement	67 boutiques in 37 cities in mainland China
	Second entry wave (1995-2000)	Hermès	1996	Retail presence estabilished using franchised outlets and a local importer-distributor	2008: creation of a branch which became a WFOE	21 boutiques in 16 cities in Mainland China.
		Gucci	1996	2 mono-brand sales outlets opened by creating a franchising network and using a local importer-distributor	Increase in directly operated stores	66 boutiques in 35 cities in mainland China
		Armani	1998	Reliance on Hong Kong based importer-distributor and a joint venture set up with local partners	2010: creation of an online platform for sales of its own products	Over 100 boutiques in 40 cities in mainland China
	Third entry wave (from 2000 onward)	Porsche	2001	Indirect export through an importer-distributor intermediary	2008/2009: creation of Porsche China Motors Ltd	44 sales outlets in 36 cities in mainland China
		Coach	2003	An importer-distributor intermediary	2008: riacquisition of its own retail network	73 boutique in 36 cities in mainland China
SMEs		Richard Mille	2009	Indirect export through an importer-distributor intermediary		

From the multiple-case analysis and examination of the documentation, it is possible to arrive at the following conclusions with regard to the current and future internationalisation strategies by way of distribution in the Chinese market:

- Market presence is with both direct and indirect distribution options;
- The choices range over the options described in the previous pages. The first market entry phase involves an indirect distribution strategy. However, in the second phase, the entry method is direct; in the third and most recent phase, there is a mixture of both direct and indirect entry methods;
- Once the brand presence is consolidated, the share of investment in direct distribution grows by means of ample use of directly operated stores;
- Flagship stores are a distribution format used during the second and third phases of Chinese market penetration. They are integrated with other direct and indirect formats, with the aim to support the growth of brand awareness (Capellari, 2008);
- There are clear differences in the routes taken by small and medium-size enterprises for which an indirect strategy is more advantageous compared to the major players who have opted for direct distribution for some time;
- The digital channel, whether directly or indirectly managed, is confirmed as an additional support to the physical channel helping to support development in the Chinese market, above all in second-level cities in which physical sales outlets have not yet been opened.

Indeed, it can be seen that the first major players to arrive in China used predominantly the direct strategic model, while for the second phase, the luxury brands opted for an indirect entry strategy, to be followed in the last decade by small and medium-size enterprises.

From the 1990s and on, the major players made use of a local importer-distributor as an intermediary (Chevalier & Mazzalovo, 2012).

Small and medium-size enterprises attempting to launch themselves on new international markets embark on ever more complex and intensive routes. These are complex because they involve different areas of business activities and are more intensive because they tend to favour putting down roots to mobility.

As ever, it is the prerogative of the internet and e-commerce that supports the brand and communicates its identity.

Discussion

Currently the major players push harder for development in the form of a direct presence in distribution, in line with strategies they have already adopted in other international markets.

The term "indirect export" is used for the transfer of goods and services across national boundaries by indirect methods (Young, Hamil, Wheeler, & Richard, 1989), by calling on third parties with a great deal of knowledge of the local market to act as intermediaries.

This entry strategy enables the company to build its presence in the new market without transferring any of its own know-how and without having to set up a specific operation for sales on the overseas market, entrusting this to existing local organisations.

The advantage of this strategic approach is that the entire burden of risks and costs associated with internationalisation is transferred to and born by the intermediary. The disadvantage is that it allows the company to exercise only limited control over the overseas market (Mosca, 2010).

This approach is particularly useful when the company has relatively little knowledge of the outlet market since appointing an intermediary to handle sales makes it possible to check the absorption potential of a given market and to acquire useful information about the needs and characteristics of potential purchasers without assuming any direct risks (Pellicelli, 2007).

This indirect method of building a presence in the target market is also more widely used by small and medium-sized enterprises because of its risk limitation, lower use of resources, and greater flexibility of action in that it appoints an intermediary whose organisation is independent of the exporting company. This intermediary undertakes to purchase the goods on its own account and to import them into the domestic market, in addition to managing their subsequent distribution.

The local distributor has to penetrate the overseas market on behalf of the entrant company, managing such operations as product purchase and import, setting up warehousing facilities in the outlet market, promoting the brand, and selling the products, usually on a sole agency basis, and selection of the distribution channels. The local distributor has to manage both wholesale and retail channels, performing such tasks as selecting locations, managing sales personnel, and bearing the operating costs, while the brand is required, where applicable, to provide the layout of the retail outlet and its design, handle merchandising, and set general marketing guidelines.

Finally, the local distributor also often has to shoulder responsibility for communications, setting a budget amounting to a percentage of the sales achieved.

Distributors-importers usually handle a number of brands since, with a number of customers in their portfolio, they are able to spread the fixed costs of their operations over a larger number of entities. This solution represents an advantage for the exporting company in that it allows the distributor to wield greater power in negotiations with department stores or independent retailers and therefore to get the best prices.

A second advantage provided by this model is that the distributor is saddled with all the risks associated with distribution activities.

There are however, some disadvantages. The brand lacks control over the distributor, running the risk that their interests fail to coincide, above all in matters of promotion and communications between the brand in question and the distributor.

This can lead to a situation in which the distributor tends, when allocating the advertising budget, to favour promoting the retail outlet whereas the brand is more interested in building brand awareness and obtaining a more psychological response with wider-ranging campaigns involving ample use of the media.

What is certain is the fact that almost all the main Western players in the luxury-goods sector choose to enter and operate in the Chinese market with the support of a local importer-distributor because this can be a winning strategy(Chevalier & Lu, 2009), also above all for small or medium-sized entrants. Indeed, for brands with limited resources and low levels of awareness recorded in Europe and the US, the support of an importer-distributor can be a key factor in developing their business and creating interest in their brand on Chinese soil. In other words, what the brand loses in terms of control gains in terms of market presence (Lu, 2008).

Direct Entry

Using this method, the business does not entrust its affairs to intermediaries but it directs the entry channel and the local distribution system, using its own commercial organisation, which may vary in scale, to operate in the target market.

Compared to the previous strategic approach, direct entry means that the company takes all the business initiatives for penetrating the outlet market. It identifies potential purchasers, establishes and maintains direct contact with its client-base and intermediaries; it carries out market research and analysis and makes independent decisions about its marketing strategies.

This policy involves greater use of human resources, in addition to increased costs and risks, but it also guarantees a whole series of advantages: the ability to direct more stable penetration of overseas markets, to glean more information about the market, to make a higher profit on sales, and to retain greater control over distribution methods.

The direct entry methods employed by Western luxury-goods firms in the Chinese market can be summed up as follows: sales agents, overseas operating units, and e-commerce.

By creating a network of sales agents, the assumption is that the company will launch its campaign to penetrate the market through contracts with local agents who take on the role of intermediary between the exporter and the buyer. The local agents act as representatives of the company that appointed them, handling sales promotion, contacting potential customers, taking orders, and keeping the exporting company informed about market trends.

The main difference between a sales agent and a local distributor is that the former is an independent entity operating on behalf of the company wishing to penetrate the market in the target country. The latter entity purchases the goods from the producer company in order to resell them to intermediary or end-customers, taking on the risk of lack of sales. In terms of the services provided, the distributor also takes on the jobs of entry logistics, storage, delivery and after-sales service, while the agent may only handle these in some circumstances. As a result of this difference, agents are paid a commission based on sales volumes while distributors' revenue is based on profit margin (Dematte, Perretti, & Marafioti, 2008).

This method is not particularly common among the major luxury-goods players, but it is sometimes used by small and medium-size enterprises.

Opening an overseas operating unit is a strategy more focused on controlling the marketing mix factors.

The company sets up its own operating unit in the overseas market in question in order to distribute products directly and to coordinate its own operations with those of agents and local distributors. Such operating units may be set up as one of two different juridical entities: a branch which is not a juridical person in its own right or a subsidiary which is a juridical person. Subsidiaries, in which the parent company has either a total control or a majority shareholding, offer the maximum degree of control.

The advantage to be gained is that the direct presence makes it possible for the company to distribute its products more rapidly in the overseas market.

While a subsidiary that is a juridical person is a more fleet-footed operating unit than a branch, it is subject to all the local tax and corporate legislation, but it does offer the advantage of being able to hold its profits on the sales market in the foreign currency. The subsidiary may take the form of an agency office, an affiliated company in which the parent company owns less than 50% of the share capital, a subsidiary in which the parent company owns over 50% but not all of the share capital or finally, it may be a wholly foreign-owned enterprise (WFOE).

Given that setting up an agency office in the People's Republic of China is a relatively simple procedure, this is more commonly done by small and medium-size enterprises than by the major luxury-goods players who, being able to call greater managerial and financial resources tend to operate more directly in the market with higher levels of control and more freedom of action.

For both new entrants and companies already operating in the Chinese market, a strategic approach based on operations managed by subsidiaries can be more effective in major, first level cities in which the entrant business can count on support services provided by local operators. However, currently this approach is less suited to penetrating and establishing the business in the more internal regions in which the support of a local distributor capable of dealing with the local authorities and more familiar with the specific nature of the particular region is still advisable.

The third method of direct entry is through e-commerce. Online sales and marketing are the most recent development in direct contact with the end-users, and it has a number of advantages, among them a rapid response to consumer requests, greater personalization and economies provided by the reduced communications and advertising costs incurred by using the digital channel. This therefore can also be a potentially winning entry method for small businesses with limited resources. However, given that the Chinese luxury-goods market is becoming increasingly crowded and the fact that consumers, particularly in the smaller and less advanced second and third level cities, are still showing considerable confusion over and lack of familiarity with the purchase and consumption of high symbolic value goods, in addition to being less accustomed to using digital technology, if there is not yet a certain level of brand-awareness, direct entry through e-commerce alone may not be particularly effective.

On the other hand, the potential of the web, as a platform both for communications and for direct sales, has become a market entry strategy adopted by all the main players. Moreover, subsequent expansion in the Chinese market often involves the adoption the digital channel with the aim of becoming more rapidly rooted in the territory.

Strategic Agreements

Strategic agreements take the form of medium to long-term arrangements that enable the new entrant to reap benefits that would not normally be available to a company operating on its own. These advantages of this approach are that it spreads the investment necessary for setting up overseas, it grants immediate access to specific complementary resources and skills, it leads to more rapid achievement of adequate efficiency levels, and finally it produces cost savings. Moreover as technology becomes ever more complex and the cost of research increases, enormous pressure is exerted on corporate behaviour. This pressure means that such activities as monitoring new technological developments and the ability to respond to the findings of overseas research by generating new products more rapidly than their competitors become crucial factors for the international success of companies.

Among the various different types of strategic agreement, the most relevant for our research is licensing, franchising, and the joint venture.

Licensing

Licensing is a contractual agreement in which the licensor grants the licensee the right to produce and distribute a product or service on a particular territory, subject to payment of royalties. The licensee has full discretion in managing the target market as his contribution is guaranteed by such clauses as minimum guaranteed return, royalties by volume and the ability to terminate the contract for any violation of its terms and conditions (Hill, Hwang, & Kim, 1990).

The advantages include being able to enter an overseas market and discover its potential with the minimum investment and risk, also overcoming any possible entry barriers. The main disadvantages are the risk of having the company’s intellectual property rights violated, the need to share profits with the licensee business, the risk of losing control over the quality of distribution and the management of the distribution channels, and the possible outcome damaging the licensor’s reputation through improper use of the licence.

In the luxury-goods market in China, use of the licensing system is not particularly widespread as a result of the risks inherent in entrusting the brand to third parties without retaining control over it and also because of the difficulty, particular for Western pioneer entrants and second-wave players, of selecting a reliable local partner capable of competent management of both production and marketing.

Another type of local business that may be selected as licensee is the private export-oriented firm. While such businesses are able to handle export activities successfully and then move on to production and distribution for the local market, they still manifest a manufacturing rather than a marketing culture.

Finally, potential licensees can be found among local firms that, having developed their own brand, could be interested in launching a foreign luxury brand in the domestic market, thus being able to infiltrate the high-end bands of the market and gain access to space in the shopping malls and department stores that would otherwise be closed to them. However, such businesses may have goals that are in conflict with those of the foreign company, leading to decision-making problems when it comes to allocating resources, balancing the need to promote their own brand with the need to make the appropriate investment to launch the foreign band on the local market. Moreover, as a result of repeated negative experiences in the past, many local firms are wary of making all their knowledge and business skills available to the licensor company, only to be dropped as soon as that company acquires the competitive edge it has been seeking. In this situation however, ways out of these dilemmas can be found in incentivising and motivating techniques put in place by the foreign company seeking to operate in the Chinese market through a licensing agreement. One of these techniques is to insert, at the negotiating stage, a clause in the contract setting up an open-ended relationship with, for example, automatic contract renewal provided that all the provisions for royalties have been met.

Franchising

Franchising is a contractual arrangement that sets up a partnership agreement with a producer company, known as the franchisor and one or more distribution companies, known as franchisees. The two parties are legally and economically independent of each other, the purpose of the contract being the distribution of goods and services in the overseas market in question. In this type of agreement, the franchisor grants the franchisee the right to use its business model within a defined territory, according to set rules and under a given name and trademark. The franchisor company offers the franchisee ongoing assistance while allowing it to perform its own business function within its own area of competence under the best possible conditions. The franchisee undertakes, under the terms of the contract, to pay the franchisor compensation for the use of the trademark and for the benefits gained from the know-how provided by that company. In the luxury-goods market, distribution through franchising contracts takes the form of building a network of sales outlets, generally in the form of mono-brand boutiques, in the overseas market in question.

A particular form of franchising often used by Western companies operating in the Chinese luxury-goods market is the master franchisee contract in which franchisors grant the franchisees the power to set up sub-franchises with other operators in the geographic area for which they have sole agency.

The advantages of this entry method include the franchisor company being able to penetrate and expand its presence in the overseas market while retaining a good level of control over critical operations, at the same time benefitting from the financial resources, the know-how and the organisational skills of the franchisee company for the management of distribution and sales. The main risk associated with this strategic approach is that it is highly dependent on the good faith and the conduct of the franchisee network whose members have, in numerous cases, demonstrated little inclination to take on the necessary expenditure for marketing and communications in order to launch and support the brand, preferring to exploit the benefits arising from supporting a brand already launched up to the point at which its potential is exhausted. This can be seen in cases in which the franchisor gradually loses control over franchisees that are focused less on building brand image than on making the maximum profit for the minimum investment. This situation can even more easily occur when the master-franchisee option is chosen, in which the sub-franchisee system causes the original brand to lose part of its powers of control over the operations of the individual members of the franchise network.

Despite the risks it carries, this method has been widely used, as it can be seen, by the major luxury-goods players on their entry to the Chinese market. Particularly in the first two waves, this is due to the impossibility or inconvenience of setting up a network of directly operated sales outlets, and for small and medium-sized enterprises lacing the necessary resources for operating independently in the market. This is also a way of managing the brand’s presence in the market and preserving its true value, both for new entrants and for brands already operating in the Chinese luxury-goods market, particularly when building a presence in second and third level cities in which a direct presence is both high-risk and costly (Ricca & Robins, 2012).

Some examples of major luxury-goods companies using this method to operate in the Chinese market are Zegna, Armani, Dunhill, Ferragamo, and Max Mara, while small and medium-sized enterprises are represented by Richard Mille and the Swiss watchmaker.

Joint Ventures

An international joint venture is an agreement between two or more partners that gives rise to a new enterprise that is legally separated from the constituent companies with the aim of pursuing common goals in research, production, or marketing. In order to take part in a joint venture, each of the partners has to contribute its own share of capital, know-how and technical and management capabilities.

The main advantage of joint ventures is that they give potential new entrants the opportunity to acquire experience and expertise in the overseas market, providing them with in-depth knowledge of the nature of that market, of consumer needs, competitors' strategies and any forms of state intervention, gaining rapid access to the distribution networks of their local partners.

For these reasons, joint ventures are seen as a particularly attractive entry method for both major luxury brands and medium-sized companies wishing to enter the Chinese luxury-goods market. Until 2004, joint ventures were the only way of operating directly in the Chinese market and it is still a preferred strategy, including those luxury-goods companies already presenting in the Chinese market which see it as an ideal way of increasing their control on that market and continuing to expand within it (Wang & Li-Hua, 2006).

Entry Strategies Employed by Small and Medium-sized Enterprises

Having analysed the entry methods available to Western companies intending to enter the Chinese luxury-goods market, it is now time to look in greater detail for what among the strategic approaches described above are most frequently used by small and medium-sized enterprises, on one hand, and the major luxury brands, on the other, the time to enter that market.

For small and medium-sized enterprises, the most widely used solution is indirect export. Because this reduces both costs and risks compared to methods involving a direct market presence, it has been found to be particularly suitable for companies with limited financial and managerial resources at their disposal.

Among the various indirect export methods available to small and medium-sized enterprises in luxury-goods markets, the most frequently employed, at least as the first step toward further development in the future, is for the brand to turn to large-scale buyers, approaching them at trade fairs and other events both in their country of origin and in China, in particular the latter, since large-scale Chinese buyers tend not to visit their supply markets very frequently. The Italian system, as an example, has over time developed initiatives to support internationalisation, providing showcases for products demonstrating the excellence of the Made-in-Italy brand. Some of the Chinese regions targeted for this business development have just been Fujian, Zhejian, Jiangsu, and Guangdong.

By its very nature, exporting can only deal with tangible products and it is also the most widely used method of establishing a presence by small and medium-sized enterprises because it dramatically cuts risks, requires far less use of resources, and allows a great deal of flexibility of action (Young et al., 1987).

A second indirect entry method to the Chinese market is to call on the services of a local importer-distributor as an intermediary. This method allows a more structured approach to establishing a presence but it also requires a greater financial commitment and more involvement on the part of smaller luxury-goods companies. It is therefore a method used mainly by more financially sound players. The final entry method by indirect export for small and medium-sized enterprises to group together to tackle the Chinese market is by forming export consortia.

Aside from the indirect export methods, it is not uncommon for small and medium-sized enterprises to enter the luxury-goods market by direct export. However, these confine themselves to setting up an overseas sales network and using agents, since it is more difficult for such businesses to commit to the larger direct investment required to set up subsidiaries or create WFOE, particularly when this is their first step into the Chinese luxury-goods market. The same is a true of e-commerce, which, while it undoubtedly has some economic and organisational advantages, is not the most suitable entry method, above all if the brand does not already boast a high profile in the Chinese market and therefore needs to opt for methods that enable it to increase band awareness.

Finally, strategic alliances can be a valid entry approach in that it allows costs and risk to be shared with the local partner. However, empirical evidence suggests that this method is not widely used by small and medium-sized enterprises dealing with goods with high symbolic value. In contrast, franchising is more often used, although limited to a small number of sales outlets, given the limited resources available to small and medium-sized enterprises, usually located in prime level cities and managed with the support and assistance of a local distributor, as in the case of Richard Mille, one of our case studies.

It should however, be mentioned that this approach is normally adopted in the subsequent phase of market development rather than on first entry.

Flagship Stores

Flagship stores set up by the top luxury goods brands often accompany both entry to and expansion in the Chinese market, alongside other formats.

Flagship stores stand out from other international sales outlets by virtue of their design, location, their fittings, and management costs, all of which perform the function of showcasing the brand and supporting and sustaining the entire sales network within the brand’s home country and in foreign markets.

This distribution format presents a display space between five and eight times larger than a directly operated store, in that its job is to demonstrate to consumers the brand values and the heritage of the product.

Flagship stores are mainly concerned with providing an intense brand experience within the display space that gets consumers totally involved.

Another strategic feature of flagship stores is their location. A high-prestige address in a major metropolis immediately becomes a powerful tool for communicating the potency of the brand. Getting a leading architect on board can also become a strategic asset for growing the brand image, but stand out from its competitors above all it makes. The design and fixtures and fittings of retail stores are usually fairly standard but flagship stores display a unique style whose design emphasises and expresses to the full the personality and positioning of the brand (Saviolo, 2010).

Flagship stores are a major marketing tool (Chadha & Husband, 2007; Sacerdote, 2011) for penetrating new markets and they often mark the transition from the first phase of an international presence to a second, more structured phase signalling a more stable position in the target market. The main advantages of opening one or more flagship stores in the overseas market penetration phase are as follows.

- It introduces, strengthens, and grows the brand image and its positioning in the luxury-goods market;
- It opens the way to developing and exploiting new business opportunities;
- It stimulates and intensifies relations between retailers, partners, the fashion media, and customers.

Future Developments

This research study is presented as an initial and exploratory survey, and there are plans to develop it in the future by broadening the sample to be analysed, increasing the number of major players and small and medium-size enterprises studied, and doing further research into second-level cities containing high-end consumers with a high disposable income who do not yet have easy access to physical sales outlets.

A further line of development for this research could be to perform an in-depth analysis of the different distribution formats.

Conclusions

Table 1 shows the different approaches to international development in the Chinese market adopted by luxury-goods companies. These diverse approaches are highly dynamic with different distribution options varying over time in line with a market in rapid and explosive growth.

The Chinese market is constantly evolving with a rapidly growing middle to high-income class so that it has the potential to become the world's leading outlet market. Faced with this scenario, the Western luxury-goods players operating in the Chinese market have enormous potential to exploit in the near future.

In particular, the ability to create brand awareness will become a key factor for successful consolidation of the competitive position in this market, an operation that can only be performed through distribution. Moreover, Chinese high-end consumers are becoming ever more demanding, seeking out an ever more sophisticated shopping experience.

Just as happening in other markets, opening directly operated stores is a strategic choice for reaching and convincing end-consumers, since these stores become their point of contact with the brand. Creating a shopping experience plays a central role in communicating the values, heritage, and spirit of the brand to consumers.

Global luxury-goods enterprises are multiplying their investment in opening new sales outlets, using different formats to create distribution system that is predominantly selective but that ensures adequate distribution coverage. The development of direct distribution channels, alongside the more traditional forms of indirect presence, is accompanied by the more innovative players developing the digital channel to accompany and support their retailing activities.

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