# Business Model Makes a Difference? Impacts of the Financial Crisis on Luxury and Mass Apparel Companies from 2008-2011

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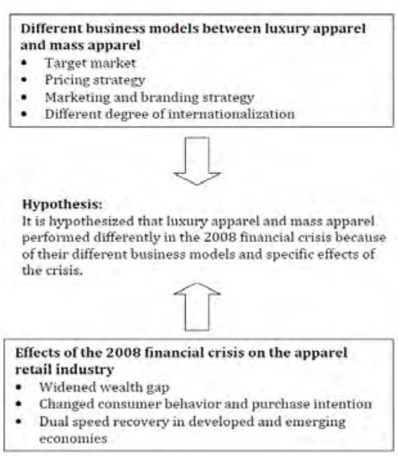
Background: The world financial crisis that started in 2008 had a profound impact on the global apparel industry (Newbury, 2010). However, at the firm level, impact of the financial crisis seemed to be unevenly distributed, with several luxury apparel companies (LA) such as Louis Vuitton achieving stable net sales and quite a few mass apparel companies (MA) such as GAP experiencing significant drop of sales and profits (Hoover's, 2012). But it remains a question whether such apparent different financial performances is a random phenomenon among several companies or reflects a more general pattern between LA and MA because of their respective business models and specific effect of the financial crisis since 2008.

This study intends to evaluate whether the financial performances of LA and MA significantly differed from 2008-2011 as a result of the financial crisis. Findings of this study will make important contribution to the understanding of the apparel-specific sectoral impact of the 2008 financial crisis, which has seldom been discussed. By comparing the business models of LA and MA, findings of the study may also suggest best business practices for apparel companies in response to the new market situation since the financial crisis.

Theoretical framework: This study hypothesized that LA and MA performed differently in the financial crisis since 2008 because of their different business models and specific effects of the crisis. The business models of LA and MA are different because: first, while LA targets most wealthy members of society, MA targets middle-class or low-income groups (Keller, 2009);




Second, while LA companies focus on a premium pricing strategy to shape their premium brand image, MA companies commonly offer discounts and markdowns to attract their more price sensitive consumers. Third, LA usually appeal to target markets through communicating its aspirational product quality. This is in contrast to MA which often stresses the good value and low price of its product (Okonkwo, 2007). Fourth, LA typically has a high level of global brand awareness and MA companies are less prevalent in internationalization efforts, especially in emerging markets such as China and India.

On the other hand, the specific effects of the financial crisis since 2008 seem to favor LA more than MA, because: 1) widened wealth gap created more top rich, the leading consumer bases of LA and less middle class, the target market of MA; 2) tightened budget made middle class, the consumers of MA become even more price sensitive; Price is not a major concern behind LA consumers, however; 3) Dual speed recovery in developed and emerging economies created new customers for LA, but not for MA (Curran & Zignago, 2010).

Method and Data: To test the hypothesis, financial performances of LA and MA were compared by using the MANOVA technique based on six indices developed under the Dupont Strategic Profit Model (including annual growth of net sales; annual growth of cost of goods sold; gross margin percentage; net profit margin; asset turnover and return on assets). Because no official list of either LA or MA are available, a pool of 22 LA companies and 50 MA companies were first created based on World Luxury Association (2012), Interbrand (2008), and Okonkwo (2007) and Speer (2012) respectively. The lists were further filtered based on: 1) availability of company's financial data; 2) whether the company is counted as an apparel company according to the Hoover's database. Eventually eight LA (PPR, LVMH, Hermès, Prada, Burberry, Christian Dior, Hugo Boss, and Mulberry) and eight MA (Limited Brands, Ralph Lauren, Urban Outfitters, Chico's, GAP, Ann Inc., Guess, and Perry Ellis), which met both criteria, were selected. To illustrate the pattern over the years, MANOVA was conducted both on selected companies' financial performance from 2008-2011 annually and on their average performance over that period. MANOVA was conducted by using the SAS9.2 statistical package.

Results and Discussions: Results show that: first, the overall financial performance between LA and MA was suggested statistically different from 2008-2011 ($p<0.01$), i.e., hypothesis was supported; Second, LA and MA were suggested having different gross margin and asset turnover from 2008-2011; Third, there was no evidence showing that LA and MA achieved different annual growth of net sales, annual growth of cost of goods sold and return on assets (ROA) from 2008-2011; Fourth, LA outperformed MA starting in 2010 in terms of net profit margin statistically, indicating more robust recovery in the post-crisis recovery.

Implications and Future Research: The research findings have several important implications. First, the results confirmed the different business models between LA and MA reflected by their performances in gross margin percentage and assets turnover; Second, the findings suggested that LA achieved a more robust post-crisis recovery than MA; Third, results of the study suggest that MA should not rush entering into the luxury apparel market because ROA of LA turned out to be no better than MA from 2008-2011, even in those years that LA achieved higher net profit margin. Case studies can be conducted in the future to further explore the success stories of LA in the financial crisis. With the availability of data, future studies can further evaluate LA and MA's performance on a country-by-country basis. Additionally, financial performance of LA can be compared to other retail formats such as department stores and discount stores.

Table 1 MANOVA Results

| | Sales Growth% | Cost of Goods Sold Growth% | Gross Margin% | Net Profit% | Assets Turnover | ROA |
|---|---|---|---|---|---|---|
| 2008 | 0.60 | 0.87 | 15.67 | 1.96 | 7.57 | 0.13 |
| | (0.45) | (0.37) | (0.002)** | (0.19) | (0.017)* | (0.73) |
| 2009 | 0.57 | 0.98 | 13.82 | 1.35 | 6.27 | 0.73 |
| | (0.46) | (0.34) | (0.002)** | (0.26) | (0.025)* | (0.41) |
| 2010 | 1.16 | 0.01 | 19.76 | 10.54 | 9.51 | 0.01 |
| | (0.30) | (0.93) | (0.001)** | (0.006)** | (0.008)** | (0.93) |
| 2011 | 0.48 | 1.00 | 22.82 | 13.00 | 12.91 | 0.55 |
| | (0.50) | (0.33) | (0.000)** | (0.003)** | (0.003)** | (0.47) |
| 2008-2011 | 0.44 | 0.02 | 19.96 | 6.54 | 11.33 | 0.02 |
| | (0.52) | (0.89) | (0.001)** | (0.023)* | (0.005)** | (0.88) |

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