



Kering – A path towards sustainable luxury

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Abstract

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Organizations are affected by exogenous shocks such as changes in consumer preferences through time, making it crucial to face these challenges in a way that will lead to a competitive advantage, as well as long-term survival. In order to overcome these situations, firms need to actively change their strategy to successfully adapt to the external environment, by altering, for instance, its technology, structure and processes.

Scholars have studied the importance of strategic change, as well as dynamic capabilities, in firm's success, highlighting the impact of an active process of change and its positive effect on performance.

This dissertation focuses on showing a real-life example of a company that changed its processes in order to increase its fit with the external environment. The teaching case focuses on Kering's path towards becoming a luxury leader in environmental sustainability, transforming its governance structure as well as operational practices. The luxury conglomerate used dynamic capabilities successfully in order to adapt, not to a crisis, but to a gradual change in consumer preferences.

This case is a clear example of how important it is for companies to sense potential changes in the external environment, and to take action in order to address those situations in a way that will improve performance in the long-run.

Resumo

Título da dissertação: Kering - A path towards sustainable luxury

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Palavras-chave: mudança estratégica, *dynamic capabilities*, desempenho da empresa, sustentabilidade, produtos de luxo

As organizações são afetadas por choques exógenos, tais como alterações nas preferências dos consumidores ao longo do tempo, tornando-se crucial enfrentar esses desafios de uma maneira que leve a uma vantagem competitiva, bem como à sobrevivência a longo prazo. Para superar essas situações, as empresas devem mudar ativamente a sua estratégia de modo a se adaptarem com sucesso ao ambiente externo, alterando, por exemplo, aspetos tecnológicos, estruturais e os processos.

Académicos estudaram a importância da mudança estratégica, bem como das *dynamic capabilities* no êxito das empresas, destacando o impacto de um processo ativo de mudança e o seu efeito positivo na performance.

Esta dissertação tem como propósito apresentar um exemplo real de uma empresa que alterou os seus processos com vista a melhor se adaptar ao ambiente externo. O *teaching case* foca-se no percurso do grupo Kering percorreu até se tornar um líder da indústria do luxo em sustentabilidade ambiental, transformando a sua estrutura de governação, bem como as suas práticas operacionais. O conglomerado de luxo utilizou com sucesso as *dynamic capabilities* para se adaptar, não a uma crise, mas a uma mudança gradual nas preferências do consumidor. Este caso é um exemplo claro de como é importante para as empresas detetar possíveis mudanças no ambiente externo e tomar medidas para lidar com essas situações de modo a melhorar o seu desempenho a longo prazo.

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1 Introduction

The objective of this thesis is to understand the implications of changing environments on the luxury industry. More specifically, I will focus on the implications coming from the rising concern for environmentally sustainable practices, on how that will affect luxury brands and on how firms can cope with these changes, adapting to them and making them, in some cases, a source of differentiation and competitive advantage.

For years, scholars have studied the reasons behind strategic change and the consequences of it. Van der Ven and Poole (1995) defined strategic change as a firm's difference in quality, state and form over a period of time. Tsoukas and Chia (2002) added that strategic change arises from both exogenous and endogenous sources, highlighting the importance of managing the process. The role of management was also reinforced by Adner and Helfat (2003), stating that outcomes will vary according to each company's resources and capabilities, as well as its top management decisions. Research conducted by Gioia and Chittipeddi (1991) concluded that change is not only needed at the time of a crisis, being an important part of a strategic reorientation process that guarantees firm's survival in the long-run.

Authors such as Teece (2007) and Zollo and Winter (2002) agreed that a firm's dynamic capabilities have a direct connection to its success. Zollo and Winter (2002) further described the structured, stable and persistent aspect of dynamic capabilities. Barreto (2010) defined them as "the firm's potential to systematically solve problems, formed by its propensity to sense opportunities and threats, to make timely and market-oriented decisions, and to change its resource base".

According to Kapferer (1997), the definition of luxury products can be described as "those that provide extra pleasure and flatter all senses at once and expand on this description to argue that psychological benefits, rather than functional benefits, provided by luxury products are the key distinguishing factors that set luxury products apart from non-luxury products". Due to the specificity of the luxury consumer and the important hedonic side of the purchase, luxury brands should have into careful consideration their brand image as a whole. It is brand reputation and image that leads to desirability and thus, purchases from customers. These consumers want to buy the brand, not the utilitarian product, as it is their essence of quality, craftsmanship and beauty that defines the desire to possess that specific good and not a cheaper one.

The managerial relevance of my thesis lies in identifying these existing threats (awareness gain) and providing recommendations on how luxury managers can cope with these problems. Moreover, it showcases the importance of strategic change within the company in order to adapt to potential changes in the environment, even when these changes are not sudden but subtle.

Kering is a pure luxury group, with 13 distinct brands and over 15 million euros in profit. When its CEO, François-Henri Pinault, took over its position he decided to transform the group into an environmental sustainability leader. In order to lead the group towards success, several actions needed to be made so that the company could change its strategy and opt for new processes. The main objective of the teaching case is to use Kering's real-life example to illustrate the importance of strategic change within a company as well as the relevance of having dynamic capabilities in order to succeed. Kering went through several measures and implemented a clear change, not only within its organizational structure but also in its core business, mission and processes, being able to ultimately align with the environment and respond to changing consumer preferences. Without having a high level of dynamic capabilities, the group would, most likely, not have been capable of responding to changes in the environment. Even less, to become a pioneer in its industry.

The structure of this dissertation will be composed of the introduction and literature review, followed by a teaching case that addresses the topic in question while linking theoretical strategy principles of Strategic Change and Dynamic Capabilities to a real-life scenario, that will best exemplify the concepts within the luxury industry. Furthermore, teaching notes will be included in order to guide instructors on how to plan class in terms of time, questions asked and respective suggested answers. These instructions will allow the instructor to analyze the teaching case in a clear and organized manner. Lastly, a final discussion drawn from the case and literature analysis, including a discussion on how the proposed strategy theories can apply to the Kering case, and a conclusion, will be presented.

2 Literature Review

The main topic and specific issue of research for this thesis is learning how firms in the luxury industry adapt to changing environments, specifically the rise of consumer concerns for sustainable practices. The main theoretical perspectives covered in order to explain and further analyze the case will be, from a strategy point of view “Strategic Change” and “Dynamic Capabilities” and from a problem-specific point of view “Luxury Goods Consumption”. In this chapter I will explain and analyze several theoretical perspectives from published authors, concerning the previously mentioned topics, in order to obtain the academic frameworks and theories that will later be applied to the specific case-study.

Strategic Change

How can firms adapt and succeed when environments are constantly changing? There is an obvious need to change the firm’s strategic plan in order to be sustainable and profitable in the long-run, commonly known as having a sustained competitive advantage. A definition for sustained competitive advantage was presented by Barney (1991), describing that it happens when a firm “is implementing a value creating strategy not simultaneously being implemented by any current or potential competitors and when these other firms are unable to duplicate the benefits of this strategy” (Barney, 1991).

However, a firm’s competitive advantage does not last forever and sometimes, firms are required to change their strategies in order to maintain a superior performance. External environment changes will require a strategic adaptation from the firms, in order to keep their performance levels.

The existing literature regarding this matter has some divergent opinions as some scholars have found that strategic change increases performance while others defend the opposite, which might indicate a non-linear relationship between the two (Zhang & Rajagopalan, 2009). Moreover, there are also dissimilar opinions on what causes the necessity for a change in the company’s strategy.

Companies that are applying an effective and successful strategy, sometimes are not able to see the need for changing and adapting it. Researchers found that commonly, past organizational success leads to firms maintaining the same strategies that have previously worked, which is called strategic persistence (Audia, Locke, & Smith, 2000). Moreover, firms

are also discouraged to modify their strategies due to high levels of managerial stress occurring from the planning and execution efforts required to implement these changes (Snow & Hambrick, 1980). However, according to this view, this behavior only works when there are no external changes, such as switches in competitive or technological conditions, or consumer preferences may turn previous strategies inadequate. Maintaining the same, successful strategy is only positive for a firm's performance when both the underlying industry and economic environments are stable (Haynes & Hillman, 2010).

Strategic change can be defined as a firm's difference in form, quality or state over a period of time (Van de Ven & Poole, 1995). It is this action of change that will enable companies to succeed in adapting to potential external changes and thus, continue to present a positive and superior performance. Snow and Hambrick (1980) explained strategic change as occurring "only when the organization (1) modifies in a major way its alignment with the environment and (2) substantially alters technology, structure, and process to fit the new alignment". In other authors perspective, in order to survive potential new environments, firms must "anticipate or detect such changes and initiate strategic transformations" (Audia, Locke, & Smith, 2000). Gioia & Chittipeddi (1991), say that "change at a firm is a process of altering an organization's current way of acting and thinking, to adapt to a new environment" .

Change is generally seen as an exception, instead of a natural ongoing process (Tsoukas & Chia, 2002) and it is inherent in organizations. Many authors consider a change in strategy when an exceptional event or shock occurs.

However, Gioia and Chittipeddi (1991) added a new view that tells us that there is no need for a "shock" or crisis for a company to adapt. Not always a crisis is necessary to implement strategic change, but rather more often a strategic reorientation aims for guaranteeing a company's viability in the long-term in a changing, dynamic environment.

Zhang and Rajogopalan (2009) explained that there are two effects that arise from a firm's strategic change (in the pattern of resources), an adaptive effect that helps the alignment with the new environment and a disruptive effect that leads to inappropriate changes or its poor implementation. While in the adaptive way, the amount of change has a positive impact on performance, in the disruptive scenario there might be negative impacts due to the fact that greater levels of change lead to higher costs and difficulty of implementation. The same authors then proposed that strategic change has an "inverted-U shaped effect on performance", suggesting that slight to moderate amounts of change have a positive effect, while moderate to

high levels might worsen the firm's performance. This research highlights the need for firms to find and manage the right amount of change in order to succeed.

Strategic change comes from both exogenous and endogenous sources. In the words of Tsoukas and Chia (2002), "changes in the environment put pressure on management to improve the customer service, but it was also management's receptivity to, and appreciation of, those changes that ultimately determined the precise organizational response."

Regarding the role of management officers in the process and consequent success of the firm, Adner and Helfat (2003) found that "within a single industry, where managers face the same external environment, time-varying corporate effects associated with corporate level managerial decisions are statistically significant". This means that to understand a firm's activities, the management teams and organizational structure play an important role. In order to build, integrate or restructure a firm's strategy, top management is responsible for the decision-making that determines the future path. Managerial decisions vary according to each company's resource-base and capabilities, thus leading to distinct outcomes for distinct firms, even if facing the same scenario (Adner & Helfat, 2003). Moreover, managers should refine their sensitivity to sense potential differences (Tsoukas & Chia, 2002).

Dynamic Capabilities

The Dynamic Capabilities View is a fairly recent strategy concept that was first introduced by Teece, Pisano and Shuen in 1997, mainly as a way to complement the Resource-Based View of the firm (RBV) theory in a scenario of changing environments. From that point onwards, several authors have decided to further analyze the framework, coming up with additions to the theory.

The field of strategic management and strategy has always looked at understanding the true sources of sustainable competitive advantage (Barney, 1991) (Teece, Pisano, & Shuen, 1997). Previous frameworks such as the RBV stated the importance of the internal organization of firms (Eisenhardt & Martin, 2000; Barney, 1991), assuming that their resources and capabilities "which are scarce, durable, not easily traded, and difficult to imitate" (Amit & Schoemaker, 1993) are the focal source of economic rents and thus, value-creating strategies (Eisenhardt & Martin, 2000). Authors defended that these resources and capabilities are particular to each firm, making it unlikely to be applied to different firms, even if operating in the same industries - resource homogeneity and mobility (Barney, 1991).

However, the RBV was unable to explain how firms cope with dynamic markets, creating the need to further spread the framework to address that limitation (Teece, Pisano, & Shuen, 1997) as it was clear that it could not explain how certain firms are able to achieve competitive advantage in situations of rapid and unpredictable change (Eisenhardt & Martin, 2000).

The dynamic capabilities' framework was then created in order to address this limitation in the RBV theory. Teece et al (1997) first defined dynamic capabilities as “the firm’s ability to integrate, build, and reconfigure internal and external competences to address rapidly changing environments”. Zollo and Winter (2002), defined it as “routinized activities directed to the development and adaptation of operating routines, and reflects upon the role of (1) experience accumulation, (2) knowledge articulation and (3) knowledge codification processes in the evolution of dynamic, as well as operational, routines”. Focusing on the specific role of dynamic capabilities, literature has most commonly considered it as the change of essential internal elements of the firm (Barreto, 2010). Resources and capabilities are not disregarded as fundamental aspects of performance, but the concepts of path dependencies, routines and learning were added factors affecting the firm’s success (Teece, Pisano, & Shuen, 1997).

Zollo and Winter (2002) further described a dynamic capability as a “learned and stable pattern of collective activity”, highlighting its structured, stable and persistent aspect. Dynamic capabilities are not disjointed means to face crisis but capabilities that allow stable and efficient improvements.

One of the main discussions regards different external environments. Authors such as Teece et al (1997) defend that this view is only relevant when highly dynamic environments are in place while others, such as Eisenhardt and Martin (2000), accept environments with smaller degrees of change as relevant, defending that dynamic capabilities are relevant not only in highly dynamic markets but also in “moderately dynamic” ones.

Nonetheless, the main question in the strategy field remains unanswered: can dynamic capabilities explain a firm’s sustainable competitive advantage? Regarding the actual outcomes, that is, the relationship between dynamic capabilities and the firm’s performance, authors’ opinions have been divergent. The first point of view considers that success “lies in using dynamic capabilities sooner, more astutely, or more fortuitously than the competition to create resource configurations that have that advantage” (Eisenhardt & Martin, 2000). The same authors claim that dynamic capabilities are “necessary, but not sufficient, conditions for competitive advantage”. Anyhow, other research authors such as Teece (2007) or Zollo and

Winter (2002) have assumed a direct connection stating that “dynamic capabilities lie at the core of enterprise success (and failure)”.

However, as the definition and theory behind dynamic capabilities was not clear, Barreto (2010) formulated a concept that “avoids specification of a purpose” while keeping away previous disapproval regarding it being ambiguous or difficult to understand and apply. He defined a dynamic capability as “the firm’s potential to systematically solve problems, formed by its propensity to sense opportunities and threats, to make timely and market-oriented decisions, and to change its resource base”, adding four dimensions to the framework. These four dimensions - propensity to sense opportunities and threats, propensity to make timely decisions, propensity to make market-oriented decisions and propensity to change its resource-base – are independent, meaning that a firm can have high or low levels of each capability.

Luxury Goods Consumption - Consumer preferences

The luxury brands market has its specificities thus being important to mention some research that can explain them.

The appearance and definition of luxury product has evolved throughout time, originally being the seeable consequence of hereditary social stratification – kings and aristocracy. However, nowadays, the need of social stratification has not changed, making the use and purchase of luxury a social marker (Kapferer & Bastien, 2009).

Kapferer (1997) first described luxury products as “those that provide extra pleasure and flatter all senses at once, and expand on this description to argue that psychological benefits, rather than functional benefits, provided by luxury products are the key distinguishing factors that set luxury products apart from non-luxury products” .

Nonetheless, considering the most recent literature, a luxury brand is considered one that has premium goods, provides pleasure as a main benefit and connects with consumers on an emotional level (Hagtvedt & Patrick, 2009), showing the need to have exceptional products that fulfill the emotional need a consumer seeks when consuming a luxury product or service.

Previous research has showed that the average consumers do prefer higher-quality products when compared to a lower segment of the same product, even when it means paying a price premium for the superior product (Randall, Ulrich, & Reibstein, 1998). Although these findings were not specific towards the luxury products we may assume that the average

consumer does value the difference in quality, preferring to pay a higher price for higher-quality products. However, it is known that luxury goods are not perceived by the consumers as regular utilitarian goods, due to its hedonistic potential.

Hedonic consumption refers to the features of consumer behavior that “relate to the multi-sensory, fantasy and emotive aspects of one's experience with products” (Hirschman & Holbrook, 1982). According to Kapferer (2009) “luxury should have a very strong personal and hedonistic component, otherwise it is no longer luxury but simple snobbery”. This translates into luxury being “qualitative and not quantitative”, “hedonic over functional”, “multisensory and experiential” and “in need of a strong human component (Kapferer & Bastien, 2009).

Hagtvedt and Patrick (2009) investigated the promise of happiness coming from luxury brands, concluding that its hedonic potential is applicable and adaptable to several levels of goods. Moreover, their research has showed that inefficient management of a brand in this industry will result in a loss of its hedonic potential and thus, reduced brand equity and evaluation.

Due to its hedonic component - “the dream” behind luxury brands -, it is crucial that firms proceed carefully when managing its image, in order to maintain consistent brand cues and not to dilute the heart of the brand. Consequently, luxury products differentiate themselves by being, for instance, handmade, high-quality, aesthetically pleasing and sold in an exquisite environment – i.e. personalized services, store design and locations, strong customer relationship management (CRM) – amongst other additional characteristics.

These aspects make us realize that luxury products or services do, sometimes, address the functional need related to the product, but that is not the main need being pleased. Instead, the personal needs of self-fulfillment and social stratification are the ones being mainly satisfied.

Thus, we can see that these brands are very distinct and need specific marketing in order to reach its customers and competitive advantage. Luxury brands need to build on their own uniqueness and identity. In contrast to what happens in other industries, luxury brands do not need to compare themselves from competitors, they need to be unique and to tell its (real) story based on history, creating emotional involvement and its own identity. Always being superlative (Kapferer & Bastien, 2009).

Another main aspect regarding luxury is the importance of scarcity. Desirability towards a luxury product increases with the inaccessibility. A commonly-used technique is creating

obstacles not only financial but also cultural, logistical and time obstacles, such as long waiting-lists for purchasing a product (Kapferer & Bastien, 2009).

After all these considerations, classic marketing techniques – focusing on value strategy but seeking volume - are not the best fit in this case, but rather the opposite. Nonetheless, luxury should not be a niche. Valuable brands should have several ranges of products, including more affordable products such as perfumes or pens (Kapferer & Bastien, *The specificity of luxury management: Turning marketing upside down*, 2009).

3 Case Study: Kering – A path towards sustainable luxury

3.1 Introduction

It's October 2018, François-Henri Pinault, son of the founder, is Kering's current CEO and Chairman. Pinault smiles as he sits in his office at *40, rue de Sèvres*, in the center of Paris, waiting for Marie-Claire Daveu, Chief Sustainability Officer of the conglomerate.

His thoughts wander through the fact that Kering was considered the most sustainable luxury conglomerate¹ as well as one of the most publicly concerned with environmental issues. How did they achieve this, while being a major player in an industry known for mistreating animals, polluting and manufacturing with non-sustainable materials? And what are the next steps toward their objectives?

3.2 Kering group

It all started in 1963 when Kering was founded by François Pinault, in the French city of Rennes. By that time, it had the name of Pinault Establishments, operating in the wood and building materials sector. It was only in the 1990's that the company entered in the distribution and retail businesses with the acquisition of CFAO², the takeover of Conforama, the Au Printemps department store group, majority owner of La Redoute, and Fnac. It clearly became one of the biggest European players in that field.

However, the company had nothing to do with the luxury sector, until Pinault decided to do the bold move of changing the focus of the business by acquiring a controlling stake of 42% of the Gucci Group in 1999. From that point onwards, François Pinault was far from finished investing in the luxury sector. In the following years and until 2014, Yves Saint Laurent, Boucheron, Bottega Veneta, Balenciaga, PUMA, Girard-Perregaux, Brioni, Qeelin, Christopher Kane, Pomellato and Dodo joined the group. Alongside those brand acquisitions³, the company also bought a tannery specialized in precious skins, a watch manufacturer and signed partnership agreements with Alexander McQueen and Stella McCartney.

¹ According to the Corporate Knights' Global 100 index, 2018

² Company specialized in the distribution of electrical tools

³ Total or majority stakes

It was only in 2018, that the group finally became a pure luxury player, after having sold PUMA, and thus having no participations left in the wood and distribution industry as well as in other non-luxury brands.

To be specific, the group only became Kering in 2013. From Pinault *Etablissements* to Kering, the group had distinct corporate names such as the well-known Pinault-Printemps-Redoute (PPR). The change to its new identity was announced by CEO François-Henri Pinault alongside a new motto – “Empowering Imagination”. He explained that the name comes from France’s region of Brittany where “ker” means home. Pinault states that Kering is “a family home where our brands and employees inhabit”. Doesn’t it sound like the English word “caring”? Yes, it does. “I wanted a name that describes the attitude we have towards brands, our people and our customers and stakeholders, as well as the environment”, Pinault said.⁴

3.3 The overall luxury market

When we think of luxury, the first thought we normally get are princes and princesses, kings and queens, living in their huge palaces and wearing exquisite clothing as well as beautiful jewelry filled with gold and precious stones. The truth is that indeed, several centuries ago, owning a luxury product was strictly reserved for the few high-society individuals such as royals or aristocrats, showing a clear social stratification of society.⁵ The social ladder was very strict and included royal commands for ways people were allowed, or not, to dress, according to their placement in society.

Today, these rigid norms have luckily been cut short, and each person is allowed to dress and own everything they please. Luxury is seen everywhere, and everyone wishes to indulge in luxury products or services in order to feel emotionally satisfied and to differentiate themselves from what they perceive as ordinary.

However, the basic needs fulfilled when purchasing a luxury product remain the same. Luxury focuses on the notion of “the dream”. Basic luxury attributes include rarity, craftsmanship, sophistication, quality, beauty and exclusivity. Managing a luxury brand can be described as managing desirability, due to the highly hedonic and emotional side of a luxury

⁴ Hérisson, Clarisson le. “Interview De François-Henri Pinault, PDG Du Groupe Kering [Vostfr HD].” *YouTube*, YouTube, 22 Mar. 2013, www.youtube.com/watch?v=WXwJ3Z2HKTo.

⁵ Kapferer, J.-N., & Bastien, V. (2009). The specificity of luxury management: Turning marketing upside down. *Journal of Brand Management*, 311-322.

purchase. Inaccessibility drives the need of the luxury consumer, the more out of reach, the greatest the desire to own it. The human need for social stratification still persists nowadays, in a smaller extent.

Furthermore, luxury itself can be divided into three hierarchies: Absolute, Aspirational and Accessible. Accessible luxury includes products based on industrialized processes using famous brand names, such as perfumes and accessories. The prices are relatively affordable, so it makes it possible for the majority of the public to own a piece of luxury. Aspirational luxury includes the strong brand symbols, but in limited series and selective retailers. A good example is ready-to-wear collections of big designers. Absolute luxury is the most elitist and exclusive of all. The brand's best-of-the-best articles fit into this category as the customer here wants to be surprised. Some examples are haute-couture clothing, yachts or luxury cars. It is this last category that drives the "dream" that sustains the other two. When a customer is buying a Chanel perfume, he is thinking about the brand and défilés⁶.

In 2017, the global economy was in a positive period of growth. The harsh times of financial crisis seemed to be far behind, yet there were still economic and political risks to take into account, such as potential asset price bubbles, tightening monetary policies, political instability, rise in protectionism and geopolitical tensions.⁷ Despite the threats of volatility that might harm future expansion, the prospects for the luxury market remained very positive.

The global luxury market was composed of nine different segments: personal luxury goods, luxury cars, luxury hospitality, luxury cruises, designer furniture, fine food, fine wines and spirits, private jets and yachts, and fine art. In 2017, the overall luxury market grew at a 5% rate, reaching a value of 1.2 trillion €. Although 80% of the global market was comprised of personal luxury goods, luxury cars and luxury hospitality, most segments grew.⁸ Expectations were that the growth would continue, for the following three years, at a 4% to 5%

⁶ Haute couture or ready-to wear runway shows

⁷ Deloitte (2018). *Global Power of Luxury Goods 2018, Shaping the future of the luxury industry*. Retrieved October 2018, from <https://www2.deloitte.com/content/dam/Deloitte/at/Documents/consumer-business/deloitte-global-powers-of-luxury-goods-2018.pdf>

⁸ Bain & Company, Inc. (2017). *Luxury Goods Worldwide Market Study, Fall-Winter 2017*. Retrieved October 2018, from <https://www.bain.com/insights/luxury-goods-worldwide-market-study-fall-winter-2017/>

compound annual rate, reaching a total market of 295€ to 305€ billion by 2020.

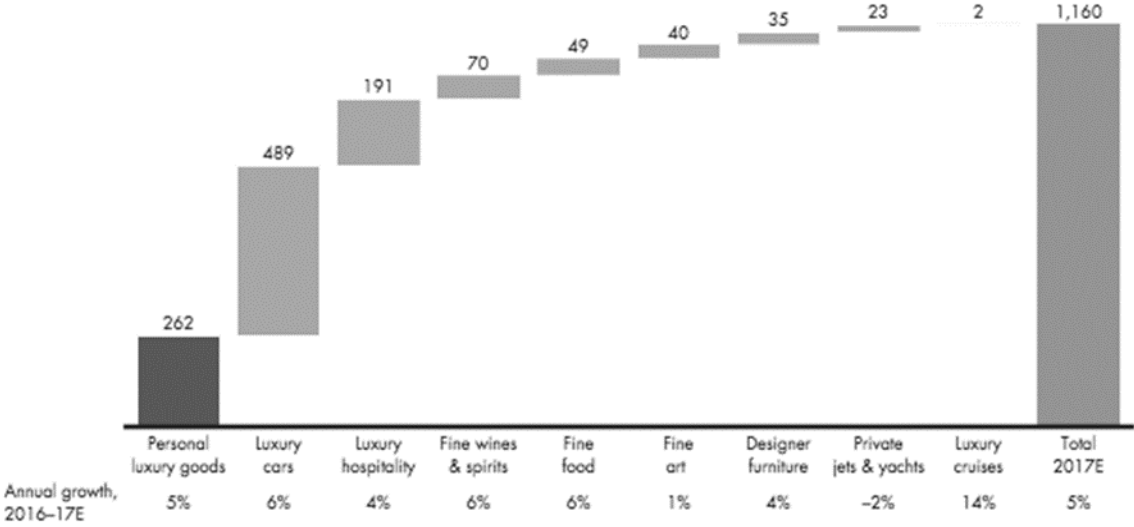


FIGURE 1- WORLDWIDE LUXURY MARKET (€ MILLIONS), EXPECTED VALUES FOR 2017

SOURCE: BAIN & COMPANY, 2018⁸

Regarding geographical factors, in 2017, stronger growth was expected in Japan and Europe, while China and the US stabilized. Europe, especially western countries, were famous for their luxury heritage. Countries such as France or Italy were home for several of the most prestigious luxury brands in the market. These areas performed well in terms of generating revenue from luxury brands, also due to tourist purchases. The euro-zone had finally recovered from the financial crisis, presenting a rapid GDP growth – higher than the US -, low interest rates that favored exports and a low inflation rate. Switzerland, known for the watchmaker industry, showed signs of recovery as the number of exports increased. Europe’s main downside was its political situation, as extremist parties were gaining popularity and votes in several countries, increasing the risks for political instability. In addition, terrorism had been a major concern in the latest years. Nonetheless, expectations were positive for Europe, as it was expected to become a fast-growing market for luxury goods. For the United Kingdom, the uncertainty arising from Brexit also affected its luxury market. Accompanied by restricted economic growth, the unstable political situation meant a decrease in consumer purchasing power. However, due to a decreasing value of the pound, it was more convenient for domestic consumers to shop in the UK rather than abroad. The currency devaluation was also turning the UK into one of the most affordable western countries, thus attracting tourism shoppers.

The United States showed a competitive luxury market, with significant growth of online sales, but smaller growth. However, consumer spending was growing at a faster rate than household income, which would not be sustainable in the future and lead to a decrease in wealth.

In addition, the US administration was planning to introduce protectionism measures, potentially harming Chinese trade relations. This meant that luxury consumption might suffer from both factors.

China was considered one of the biggest consumers of luxury goods in 2017 and was expected to maintain that title in 2018 due to the rising of the millennials and generation Z's purchasing power and the huge increase of the fashion-lover middle-class population. Chinese enjoyed the luxury experience and thus, valued the in-store purchase and luxury tourism shopping. Europe was their favorite destination, followed by the United States. China was also the number one exporter of Swiss luxury watches.

The Middle East presented close to no growth due to economic uncertainty, mainly as a result of geopolitical instability, conflicts, terrorism and shrinking oil prices, but was expected to rise to 3% in 2018. Luxury consumption was strongly linked to oil prices in this region. With one of the youngest and richest populations, this region presented a very attractive market for luxury brands. Despite the very positive luxury atmosphere, the competition between brands was also more intense and there were concerns regarding locals purchasing luxury goods abroad. Dubai was the main destination for luxury shoppers in the region.

3.4 Luxury Goods Market

The Kering group was in the personal luxury goods market. The top 5 companies in this segment, based on sales, were respectively LVMH, followed by The Estée Lauder Companies, Richemont, Luxottica Group and Kering.

The personal luxury goods sector, could further be divided into five distinct sectors: clothing and footwear, bags and accessories, cosmetics and fragrances, jewelry and watches and multiple luxury goods. The top 10 luxury brands included three conglomerates, which owned brands in multiple sectors, two jewelry and watch companies, two fashion companies, two cosmetics groups and one eyewear and accessories firm.

The biggest performer in terms of sales was the cosmetics and fragrances sector (Figure 13), perhaps due to the greater accessibility of the products to the main public – accessible

luxury. While the average consumer was not able to afford, for instance, a 4 000€ dress, he or she could pay around 90€ and have a luxury perfume.⁹

Overall, the growth experienced in the personal luxury goods sector was driven by an increase of 4% in local consumption and of 6% in tourist purchases.¹⁰

What was the future of luxury consumption? Luxury executives, including Pinault realized that the luxury consumer and purchaser was changing, as 85% of growth was sustained by Generation Y and Z. This switch to the “millennial mindset” was deeply changing consumer preferences and habits. Comfortable streetwear clothing such as T-shirts and sneakers were mere examples of categories that grew at a 25% and 10% rate, respectively.¹¹

Additionally, the dynamics of luxury purchases were changing due to digital platforms, as online sales of personal luxury goods represented 8% of the overall luxury market and were expected to reach 19% until 2025.¹² Nearly 80% of luxury sales were influenced by digital means such as social media or online websites. This happened, for instance, when consumer’s look for suggestions of products by browsing social networks and influencers’ blogs, or when they post about their purchases, displaying their style and status (Figure 14). Mobile usage was preferred to desktop, as it became the main source of information as well as favorite shopping platform, highlighting the need for brands to make their webpages “mobile-friendly”. Consumers looking for purchasing affordable luxury items, were more likely to shop online as most online purchases were cosmetics and fragrances followed by ready-to-wear clothing.¹³

⁹ Corzine, M. (2018, June 28). How Perfume Is Helping Luxury Brands Infiltrate The Beauty Industry. Retrieved October, 2018, from <https://www.luxurysociety.com/en/articles/2018/06/how-perfume-helping-luxury-brands-infiltrate-beauty-industry/>

¹⁰ Bain & Company, Inc. (2017). *Luxury Goods Worldwide Market Study*, Fall-Winter 2017. Retrieved October 2018, from <https://www.bain.com/insights/luxury-goods-worldwide-market-study-fall-winter-2017/>

¹¹ Bain & Company, Inc. (2017). *Luxury Goods Worldwide Market Study*, Fall-Winter 2017. Retrieved October 2018, from <https://www.bain.com/insights/luxury-goods-worldwide-market-study-fall-winter-2017/>

¹² McKinsey & Company (2018). Apparel, Fashion & Luxury Group. The age of digital Darwinism, enhance the customer experience and transform your business to survive and prosper in the luxury digital era. Retrieved October 2018, from <https://www.mckinsey.com/industries/retail/our-insights/luxury-in-the-age-of-digital-darwinism>

¹³ McKinsey & Company (2018). Apparel, Fashion & Luxury Group. The age of digital Darwinism, enhance the customer experience and transform your business to survive and prosper in the luxury digital era. Retrieved October 2018, from <https://www.mckinsey.com/industries/retail/our-insights/luxury-in-the-age-of-digital-darwinism>

PERSONAL LUXURY GOODS SECTOR ANALYSIS






		Number of companies	Average size of companies by luxury goods sales (US\$m)	FY2016 Luxury goods sales	Share of top 100 luxury goods sales
	Clothing and footwear	38	\$1,114	0,2%	19.5%
	Bags and accessories	9	\$1,114	3,4%	7.2%
	Cosmetics and fragrances	11	\$1,728	7,6%	15.8%
	Jewellery and watches	31	\$3,103	-4,0%	25.3%
	Multiple luxury goods	11	\$6,334	2,1%	32.2%
	Top 100	100	\$2,166	1,0%	100%

Figure 2 - Sector Analysis
 Source: Global Powers of Luxury Goods (2018), Deloitte¹⁴.

¹⁴ Deloitte (2018). *Global Power of Luxury Goods 2018, Shaping the future of the luxury industry*. Retrieved October 2018, from <https://www2.deloitte.com/content/dam/Deloitte/at/Documents/consumer-business/deloitte-global-powers-of-luxury-goods-2018.pdf>

3.5 Sustainability concerns

Millennials customers were also concerned with making eco-friendly choices, not only in luxury but also in their daily utilitarian purchases.¹⁵ Not only had consumer preferences changed over the years regarding the concerns for sustainability, but also laws and regulations. In October 2018, the European Parliament voted in favor of the ban of single-use plastics, such as straws or plates, in order to avoid pollution. This and other moves showed the major environmental changes happening in the world – firms needed to adapt to an eco-friendly world, otherwise they wouldn't survive.¹⁶

Consumers had the habit of differentiating luxury and fast-fashion brands, sometimes thinking that, as luxury was commonly higher-quality, it did not pollute or damage the environment. This idea was wrong. Luxury brands were indeed focused on producing state of the art goods, but for years their environmental concerns were close to zero. Famous cases of the luxury industry bad behavior are blood diamonds, endangered animals killed for fur and leather or soil pollution.

Research had showed that climate change impacts water availability and crop production, meaning that crops that need water, such as cashmere, angora or cotton, have become harder to produce in a sustainable way.¹⁷

However, without scarcity and desirability luxury lost its core value. So how could firms maintain the level of scarcity while being environmentally sustainable?

3.6 Kering in 2017

In October 2018, the Kering group, had a share price of 379.7€ and revenues of 15 478 million euros (Figure 15), 34% and 31% of which coming from the European and Asia-Pacific region, respectively (Figure 16). It was one of the biggest luxury conglomerates in the market, famously known for being the owner of Gucci, amongst other big luxury brands, such as Saint

¹⁵ Flaherty. (2017, March 10). *The eco has landed: Sustainability gets stylish*. Retrieved November, 2018, from <https://www.ft.com/content/cabf4d6a-0359-11e7-aa5b-6bb07f5c8e12>

¹⁶ Reuters (2018, May 28). *EU moves to ban single-use plastics*. Retrieved November, 2018, from <https://www.reuters.com/article/us-europe-environment-plastics/eu-moves-to-ban-single-use-plastics-idUSKCN1IT160>

¹⁷ Corzine, M. (2018, July 11). *Sustainability Has Become A Business Strategy Of Its Own For Luxury Brands*. Retrieved November, 2018, from <https://www.luxurysociety.com/en/articles/2018/07/world-luxury-brands-sustainability-has-become-business-strategy-its-own/>

Laurent, Bottega Veneta, Balenciaga, Alexander McQueen, MCQ, Brioni, Boucheron, Pomellato, Dodo, Qeelin, Ulysse Nardin and Girard-Perregaux.



FIGURE 3- KERING GROUP'S BRANDS IN OCTOBER 2018

After François-Henri Pinault’s took over as CEO and chairman in 2005, Kering was metamorphosed into a global luxury group and leader. He always had a passion for sustainability. During the last 10 years, he had switched the corporate strategy in order to become a luxury leader, with Houses specialized in leather goods, fashion, jewelry, and watchmaking.¹⁸¹⁹ In the fall of 2018, Kering stood for modernity, responsibility and engagement, while having a desire to become the best luxury group when it comes to creativity, sustainability and economic performance.²⁰

In 2017, the group’s largest three brands had revenues of more than 1 billion euros. Their goal was to sustain and increase its growth in the years to come. In order to achieve that goal, the company had developed an integrated business model that combined “agility, balance and responsibility”.²¹

The corporate board decided to focus its core business model into eight pillars:

¹⁸ Kering Group. (n.d.). Retrieved October, 2018, from http://www.kering.com/en/group/biography/francois-henri_pinault

¹⁹ Kering (2018). *Activity Report 2017*. Retrieved October 2018, from <http://www.kering.com/en/group/activity-report>

²⁰ Kering (2018). *Activity Report 2017*. Retrieved October 2018, from <http://www.kering.com/en/group/activity-report>

²¹ Kering (2018). *Activity Report 2017*. Retrieved October 2018, from <http://www.kering.com/en/group/activity-report>



FIGURE 4 - CORE BUSINESS MODEL: PILLARS

SOURCE: KERING, 2018²²

²² Kering (2018). *Activity Report 2017*. Retrieved October 2018, from <http://www.kering.com/en/group/activity-report>

3.7 Kering fighting for sustainability

“We are guided by a sense of ethics and a commitment to controlling our social and environmental impact. In viewing sustainability as a source of innovation and inspiration, Kering has reconsidered its relationship with its stakeholders.”²³

As consumers from around the globe were embracing the benefits of living an eco-friendly life, Kering decided to make sustainability one of its main concerns. The group saw sustainability as a necessity and had the desire to push the brand towards “higher levels of economic, environmental, ethical and social performance”²⁴ Their goal was to be the ones who truly set the standards for sustainable luxury by reducing their environmental impact, preserving raw materials, ensuring animal welfare and supporting their suppliers, all while preserving true craftsmanship.²⁵

It all started from the inside of the organization in the firm’s governance structure. The company’s structure was crucial, as it allowed sustainability to be a part of the whole group, not only through a sustainable development committee but also within each individual brand. Marie-Claire Daveu, Kering’s Chief Sustainability Officer was part of the executive committee and reported directly to François Henri Pinault. Her job was to lead the department that created environmental policies targeted to all brands in the group. Around 50 individuals were focused on sustainability issues within the group, 15 of which were part of the Sustainability Department, and 35 of which were working for Sustainability Leads within each individual brand, focusing not only on following the group’s guidelines and reaching the overall targets, but also on keeping the brand identity along the process.²⁶

Alongside the sustainability positions, the group had three distinct ethics committees, one for the whole Kering group and two regional committees, for the Asia-Pacific and America

²³ Kering (2018). *Activity Report 2017*. Retrieved October 2018, from <http://www.kering.com/en/group/activity-report>

²⁴ Kering (n.d.) *Sustainability*. Retrieved November, 2018, from <http://www.kering.com/en/sustainability/2025-strategy>

²⁵ Kering Group. (2017, January 24). *Kering 2025 : Crafting Tomorrow's Luxury*. Retrieved November, 2018, from https://www.youtube.com/watch?v=_T8HeXezZ6c

²⁶ Kering (n.d.) *Sustainability*. Retrieved November, 2018, from <http://www.kering.com/en/sustainability/governance>

regions, respectively. These committees made sure the group’s code of ethics and principles were being implemented and responded to possible complaints from employees.

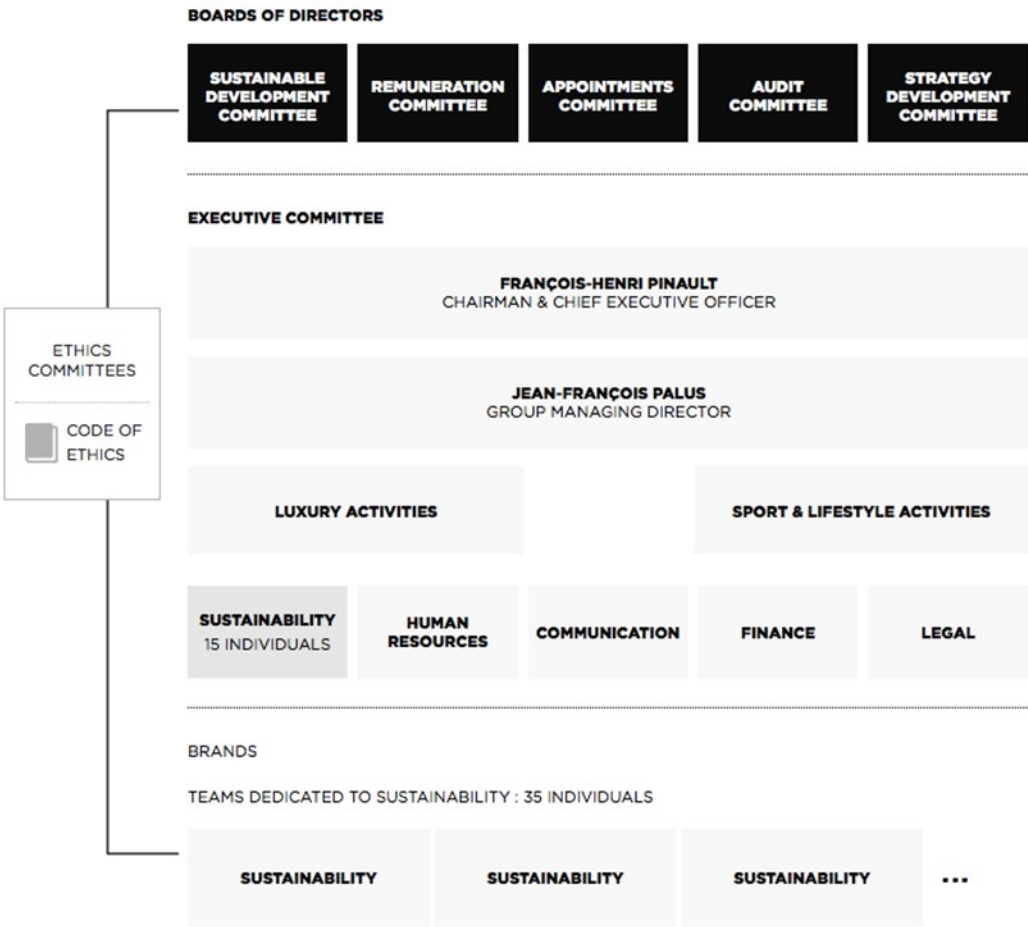


FIGURE 5 - KERING'S GOVERNANCE STRUCTURE
 SOURCE: KERING, 2018²⁶

3.7.1 Environmental P&L

One of the most important moves Kering had done in the past was to create a new tool, the Environmental Profit and Loss (EP&L). The EP&L was first introduced in 2011 with environmental results for the brand PUMA.

This tool was then further developed, in order to help firms measure and understand the real impact of natural resources across the supply chain, and consequently reorganize its resources accordingly. In response, Kering developed the Environmental Profit and Loss Account (EP&L) – an innovative tool to help identify and account for the value of natural

capital to its business. “We have implemented an EP&L analysis across all our brands’ supply chains to measure our environmental footprint and highlight environmental risks and business opportunities across our supply chains to support a more resilient business model.”²⁷ But what is really the EP&L system and what are its underlying benefits?

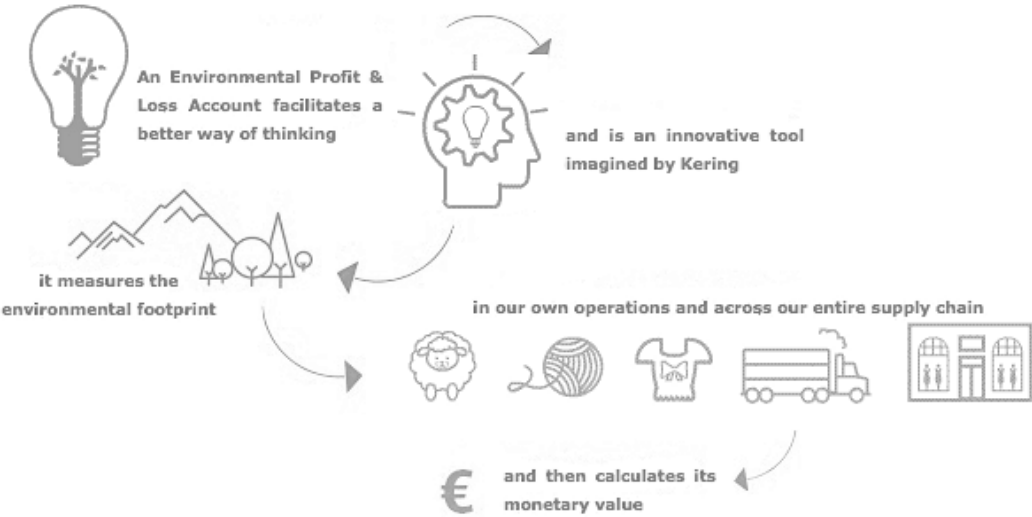


FIGURE 6 – WHAT IS AN EP&L

SOURCE: KERING, 2018

The EP&L was given in monetary values mainly due to three reasons: environmental effects are translated into a “business language” (more easily understandable), it allowed for comparisons between distinct impacts and distinct geographies and it also helped the comparison amongst brands and departments. Despite being presented in monetary units, those numbers were not related in any sense to the group’s financial results. In fact, they were the representation of an “estimate cost to society of the changes in the environment as a result of business activities and of the supply chain”. The EP&L was a tool designed to measure and monitor the costs of environmental changes associated with business. It was based on economic analysis that estimates societal costs of environmental impacts.²⁸ It was then functioning as an

²⁷ François-Henri Pinault

²⁸ Kering (2015), *Environmental Profit & Loss: Methodology and 2013 results*, Retrieved November, 2018, from http://www.kering.com/sites/default/files/document/kering_epl_methodology_and_2013_group_results_0.pdf#page=24

open-source methodology, meaning that other companies could use this tool to analyze and manage their usage of natural resources.

To measure the environmental footprint, the EP&L focused on analyzing elements such as carbon emissions, water usage and pollution, land use, air pollution and waste. In addition, value chain elements such as raw materials, processing, manufacturing, assembly, operations and retail were also taken into account.²⁹ The methodology had developed since the first 2011 version and was then divided into seven steps:



FIGURE 7 - EP&L STEPS

²⁹ Kering (n.d.), *Sustainability*. Retrieved from <http://www.kering.com/en/sustainability/whatisep&l>

SOURCE: KERING, 2018²⁹

This tool brought many benefits for the quantitative analysis of a brand’s sustainability, as it helped to achieve a greater understanding of the drivers and consequent impacts, along with providing better relationships with suppliers and ultimately, more transparency for stakeholders and better performance.

The EP&L results for 2017 (Figures 8 & 17) showed that, for Kering, the most significant impacts were happening in the supply chain, mostly in the raw material production and processing areas, both making up 76% of total. Within these materials, the major drivers were leather and animal fibers (i.e. wool or cashmere). Comparing with the previous year, the EP&L value had increased, mainly due to business growth and consequent higher raw material usage, according to Kering’s EP&L report. Manufacturing showed an increase of 18.2 million euros and raw materials production and processing’ values increased 51 million euros. Nonetheless, the group was able to reduce 0.3 million euros regarding operations as a result of renewable

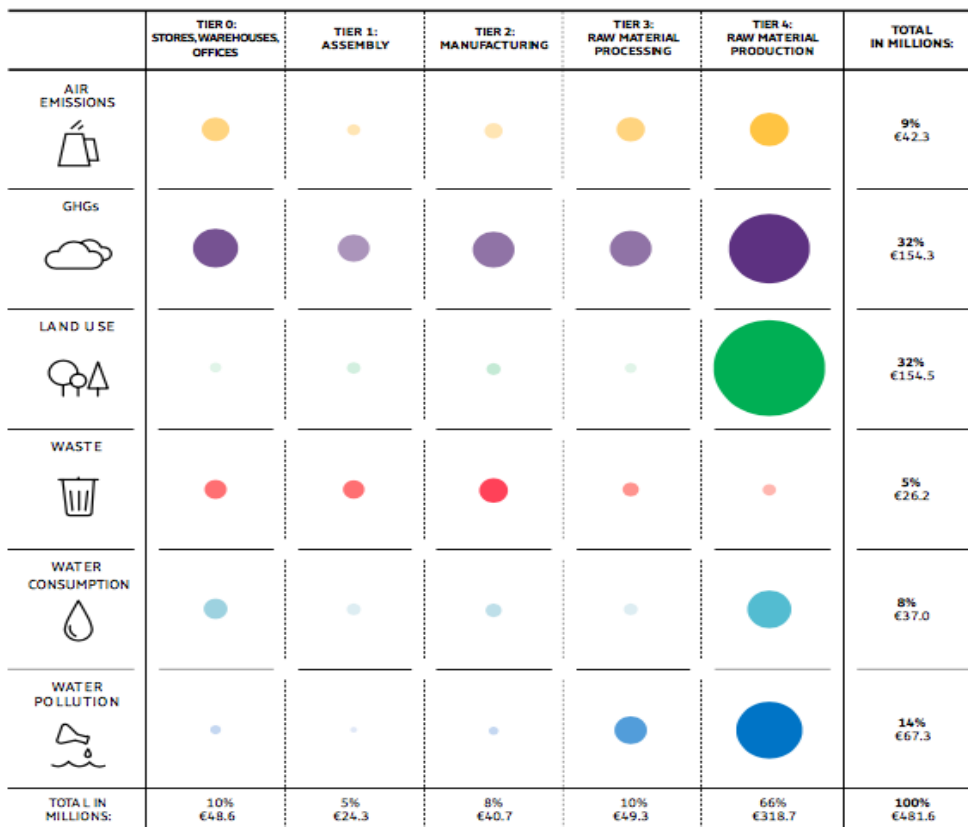


FIGURE 8– KERING’S EP&L IMPACTS ACROSS SUPPLY CHAIN TIERS SPLIT BY IMPACT AREA

SOURCE: KERING, 2018³¹

energy use and energy efficiency programs across warehouses, offices and stores.³⁰ Regarding these results, Kering decided that a good strategy to overcome this was to make small-scale changes in sourcing alternatives as, for instance, using recycled materials.³¹

3.7.2 The 2025 Strategy - Crafting Tomorrow's Luxury

“More than ever I am convinced that sustainability can redefine business value and drive future growth. As business leaders we all have a crucial role to play and I worked with the CEOs of our luxury Maisons to embed sustainability across our activities while developing this next important phase of our sustainability strategy.” François-Henri Pinault, 2017

In order to attain the goal of being the one who sets the standards for luxury sustainability, Kering came up with the 2025 strategy with the motto of “Crafting Tomorrow's Luxury”. The whole premise focused on one thing only – creating a new and more sustainable luxury by 2025. By using the 2025 strategy, the group wanted to set up a clear path in order to explore disruptive innovations and invest in new platforms or business models that would allow for positive impacts and, in the future, a transformation within the luxury industry.

The 2025 Strategy focused on three themes: Care, Collaborate and Create and inside each one there were concrete objectives to be accomplished by 2025.³²

³⁰ Kering (2018). *Environmental Profit & Loss (EP&L) 2017 Group Results*. Retrieved November, 2018, from http://www.kering.com/sites/default/files/kering_2017_epl_report.pdf

³¹ Kering (2018). *Environmental Profit & Loss (EP&L) 2017 Group Results*. Retrieved November, 2018, from http://www.kering.com/sites/default/files/kering_2017_epl_report.pdf

³² Kering (n.d.). 2025 Strategy: Crafting Tomorrow's Luxury. Retrieved November, 2018, from <http://www.kering.com/en/sustainability/2025-strategy>

CARE - The group desired to find new solutions for restoring and protecting biodiversity and eliminating chemicals.³³ Within this pillar, Kering promised to:

CARE

“We CARE for our impact on the planet, on climate change and on natural resources by reducing our environmental footprint and preserving our raw materials”



Extend their EP&L (Environmental Profit and Loss account) methodology to cover a product’s use and end-of-life phases, to better understand and reduce impacts.

Reduce their EP&L across the supply chain by 40% by 2025, via actions that tackle the impact of their sourcing, manufacturing and operations.

Implementing science-based targets to reduce carbon emissions by 50% in selected scopes by 2025.

Tracing 95% of raw materials (for example cotton, leather, precious skins, wool) by 2018, to ensure a transparent and responsible supply chain.

Deploying Kering social, environmental and animal welfare standards across 100% of their supply chains, to safeguard the sourcing of raw materials for the long-run.

FIGURE 9 - 2025 STRATEGY: CARE

SOURCE: KERING, 2018³³

³³ Kering (n.d.). 2025 Strategy: Crafting Tomorrow’s Luxury. Retrieved November, 2018, from <http://www.kering.com/en/sustainability/2025-strategy/care>

COLLABORATE – The group was keen on supporting and empowering their employees by creating new opportunities and promoting social welfare and equity.³⁴ Regarding this premise, Kering promised to:

COLLABORATE

"We COLLABORATE with people across our business ecosystem including suppliers, and engage with our employees and clients to preserve our industry's heritage, instill gender parity and diversity and be an employer of choice"



Create a suppliers' platform, which offers training on Kering standards and enables the sharing of best practices.

Provide craftsmanship and artisanal training programs to those in operating regions, so as to safeguard the rich heritage of their communities and the future of luxury.

Reach gender parity and ensure salary equality in all functions, across all levels.

Implement a sponsorship programme for training and coaching key women managers, and roll out mentoring programmes in all regions.

Promote the development of innovative career paths, irrespective of gender.

Offer teams a more sustainable and caring working environment: a well-being policy, a benefits policy and, from January 2017 a global parental policy which means parents receive standardized benefits irrespective of their personal circumstances.

Ensure exemplary working conditions for all those people working in their supply chains, going beyond social compliance and enabling their capacity building

FIGURE 10 - 2025 STRATEGY: COLLABORATE

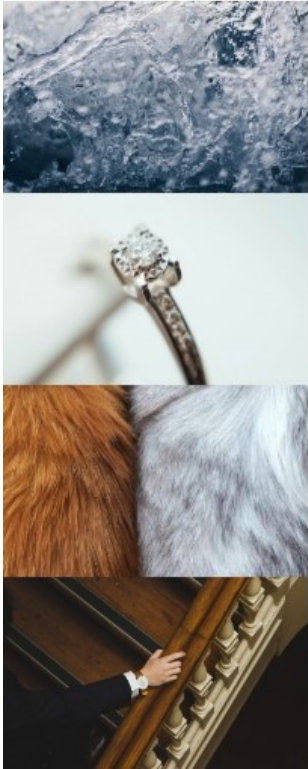
SOURCE: KERING, 2018³⁴

³⁴ Kering (n.d.). 2025 Strategy: Crafting Tomorrow's Luxury. Retrieved November, 2018, from <http://www.kering.com/en/sustainability/2025-strategy/collaborate>

CREATE - In order to implement new efficient and sustainable business models, Kering invested on knowledge and innovation by seeking and promoting creativity.³⁵ Here it was expected to:

CREATE

"We CREATE innovations to ensure our planet, our industry and our brands thrive for the long-run by launching disruptive innovations and empowering the future generations"



Develop new sourcing solutions, raw materials and processes by applying innovations such as biotech and the circular economy to luxury's current practices and collaborating with start-ups and academia.

Establish a Watches & Jewelry Innovation Lab, following the success of Kering's Materials Innovation Lab for textiles and fabrics.

Reinforce the education of next generation of designers via co-developed sustainability curriculums at universities and educational institutes around the world.

Launch a Young Leaders Advisory Group to enable future business leaders to reimagine and inspire the group's decision-making.

FIGURE 11 - 2025 STRATEGY: CREATE

SOURCE: KERING, 2018³⁵

³⁵ Kering (n.d.). 2025 Strategy: Crafting Tomorrow's Luxury. Retrieved November, 2018, from <http://www.kering.com/en/sustainability/2025-strategy/create>

3.7.3 In Action – Examples of Brands

What were the main initiatives, within each brand, to reduce the conglomerate's EP&L?

Alexander McQueen – Organic Cotton³⁰

In order to reduce raw material related impacts, the brand tried to find alternative ways of sourcing its resources. Considering one of its main resources as cotton, and that its production requires great levels of water consumption, Alexander McQueen decided to replace common cotton for an organic alternative. By doing this, all while assuring a sustainable production, the brand's products used only one third of the water, half of the fossil fuel energy and avoid chemical fertilizers. Overall, 80% less of negative environmental impacts.³⁶

Bottega Veneta – Chrome-free Leather Tanning³⁰

Leather usage was a massive part of Bottega Veneta, as the brand is famous for their bags and shoes. However, according to Kering's EP&L results, this raw material was one of the biggest contributors to greenhouse gas emissions due to its processing and tanning methods. Bottega Veneta purchased over 54000 square meters of chrome and metal-free leather, reducing water and energy waste.

Gucci – Regenerated Cashmere and Fur-Free³⁰

Around 2% of Kering's impact was due to waste such as fabric cuttings. By re-using cashmere fibers from offcuts and transforming them into new fibers, the production process required zero water and chemicals. Moreover, the impact of the animal wearing phases was reduced, along with the waste and water.

Gucci's fur-free statement was made in October 2017 by its CEO Marco Bizzari. He said that "being socially responsible is one of Gucci's core values, and we will continue to strive to

³⁶ Kering (n.d.), *Sustainability, EP&L Results*. Retrieved November, 2018, from <http://www.kering.com/en/sustainability/results>

do better for the environment and animals.” The brand promised to remove fur from all their future collections, starting as off Spring/Summer of 2018.³⁷ Moreover, Bizzari stated that “Technology is now available that means you don't need to use fur. The alternatives are luxurious. There is just no need”, while explaining that the inspiration for this measure had come from Gucci’s younger employees.³⁸

The group’s sustainability strategy was awarded with several recognitions by NGO’s and rating agencies. Some examples include the Dow Jones Sustainability Index (DJSI), that listed the best sustainable performers among the 2500 biggest firms in the S&P Global Market Index. Kering was the only luxury group to be featured in the list in 2017. Alongside, Kering was also considered one of the world’s most sustainable corporations by the Corporate Knight’s Global 100 index, again being the only luxury group featured. Finally, the group was also present as a top leader in the Carbon Disclosure Project Climate Performance Leadership Index, within its industry. This list rated companies according to the climate change risks linked to the companies’ policies.³⁹

3.8 The Kering Foundation

The Kering foundation was created in 2008 by François-Henri Pinault with the goal of fighting the violence against women.

The basis of the foundation was divided into three main geographical areas, each focusing on a specific issue. In America, the focus was on fighting sexual violence against women, in western Europe the main actions were targeting hurtful traditional practices and in Asia, the focal point was domestic violence.⁴⁰

³⁷ *Fur-get it: Gucci goes fur-free. (2017, October 12).* Retrieved November, 2018, from <https://www.ft.com/content/cb6ee2a3-9d05-37ba-9f33-75ff83549fc9>

³⁸ Pithers, E. (2017, October 12). Gucci Announces It Will Be Going Fur-Free. Retrieved November, 2018, from <https://www.vogue.co.uk/gallery/gucci-announces-it-is-going-fur-free>

³⁹ Kering (n.d.). Sustainability, Recognition from Stakeholders. Retrieved November, 2018, from <http://www.kering.com/en/sustainability/recognition>

⁴⁰ Kering (n.d.). Sustainability: Kering Foundation. Retrieved November, 2018, from <http://www.kering.com/en/sustainability/corporate-foundation>



FIGURE 12 - KERING FOUNDATION' REGIONS OF ACTION

SOURCE: KERING, 2018⁴⁰

The action structure of the foundation was very simple and also followed a three-headed focus, where its operations were based. Firstly, by supporting local and international NGOs fighting for women welfare. Secondly, by awarding social entrepreneurs and finally, through the organization of awareness campaigns.⁴⁰

“1 in 3 women in the world are victims of violence. Women make up 41% of the world’s workforce. Whether we talk about it or not, Violence against Women is an issue that touches all of us, be it as an individual, a corporation or a society. Through the Kering Foundation, my wish is to break the silence and stop the violence” François-Henri Pinault

3.9 Outlook for the future

Kering’s pioneer vision to preserve the environment made them a sustainability leader in the luxury industry. More than just coping with a consumer preference change, the company decided to go further and make sustainability a part of the group’s core business. Caring for the environment had become an identity for Kering. As a luxury conglomerate, some challenges may arise as the ancient luxury consumer’s perceived notion of high quality and preciousness may be lost due to environmentally-friendly practices.

Nevertheless, the growing percentage of millennials taking over the luxury's client base will most likely value the new efforts and thus positively affect the group's sales performance and customer base.

Looking ahead into the future, some questions naturally came up regarding not only the success of Kering's new strategies but also regarding the industry itself.

Would Kering achieve its 2025 goals? Would the environmentally-friendly approach be approved by the majority of luxury consumers? And would the industry follow Kering's steps and focus on improving their activities in order not to damage the environment?

Nonetheless, the group was able to efficiently tackle a preference change that was gradually arising within millennial consumers and became a pioneer and example in an industry formerly known for environmental malpractices.

Additional case figures:

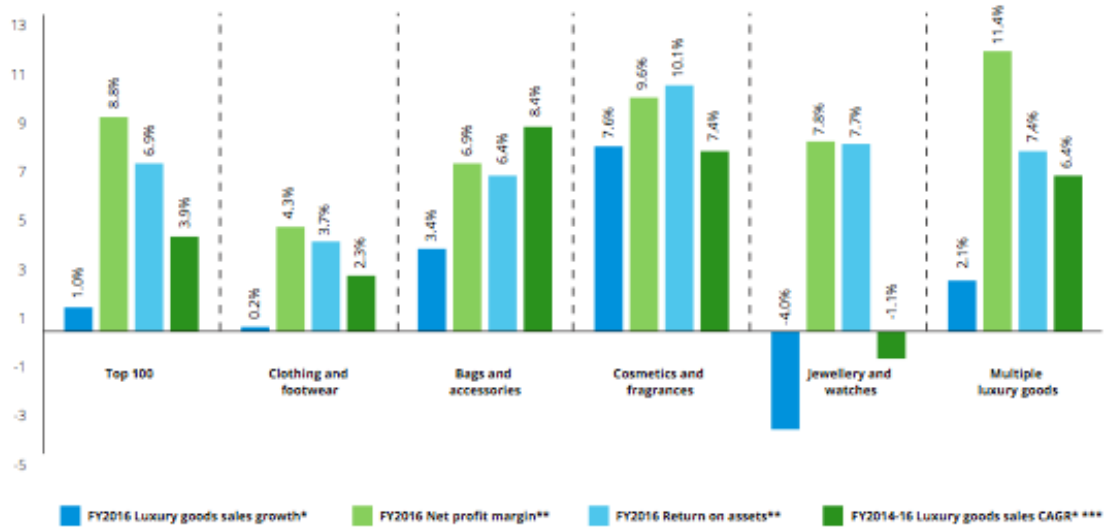
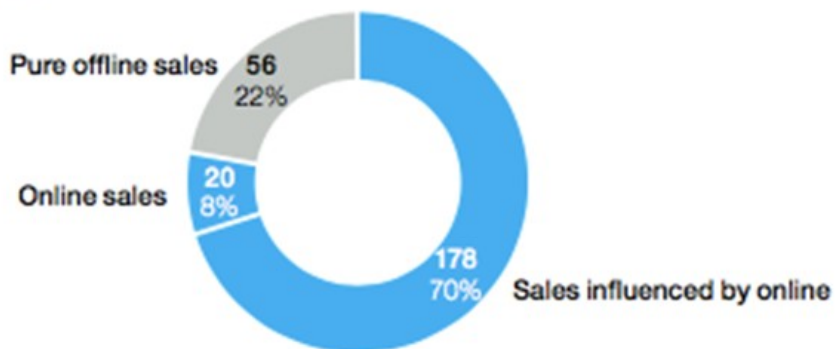


FIGURE 13 - PERFORMANCE BY PRODUCT SECTOR

*SALES-WEIGHTED, CURRENCY-ADJUSTED COMPOSITES ** SALES-WEIGHTED COMPOSITES *** COMPOUND ANNUAL GROWTH RATE

SOURCE: DELOITTE (2018). GLOBAL POWER OF LUXURY GOODS 2018, SHAPING THE FUTURE OF THE LUXURY INDUSTRY. RETRIEVED OCTOBER 2018, FROM [HTTPS://WWW2.DELOITTE.COM/CONTENT/DAM/DELOITTE/AT/DOCUMENTS/CONSUMER-BUSINESS/DELOITTE-GLOBAL-POWERS-OF-LUXURY-GOODS-2018.PDF](https://www2.deloitte.com/content/dam/deloitte/at/documents/consumer-business/deloitte-global-powers-of-luxury-goods-2018.pdf)

80% of sales are influenced by online
Sales of personal luxury goods¹, € billions



SOURCE: Euromonitor; Forrester; companies' Annual Reports; McKinsey

FIGURE 14 - PERSONAL LUXURY GOODS' SALES BREAKDOWN

Source: McKinsey & Company (2018). Apparel, Fashion & Luxury Group. The age of digital Darwinism, enhance the customer experience and transform your business to survive and prosper in the luxury digital era. Retrieved October 2018, from <https://www.mckinsey.com/industries/retail/our-insights/luxury-in-the-age-of-digital-darwinism>

<i>(In € millions)</i>	2017	2016	Change
Revenue	15,478	12,385	+25.0%
EBITDA	3,464	2,318	+49.4%
<i>EBITDA margin (as a % of revenue)</i>	<i>22.4%</i>	<i>18.7%</i>	<i>+3.7pts</i>
Recurring operating income	2,948	1,886	+56.3%
<i>Recurring operating margin (as a % of revenue)</i>	<i>19.0%</i>	<i>15.2%</i>	<i>+3.8pts</i>
Net income attributable to owners of the parent	1,786	814	+119.5%
o/w net income from continuing operations excluding non-recurring items	2,002	1,282	+56.2%
Gross operating investments⁽¹⁾	752	611	+23.1%
Free cash flow from operations⁽²⁾	2,318	1,189	+94.9%
Net debt⁽³⁾	3,049	4,371	-30.2%
Average number of employees (full time equivalent)	38,596	35,877	+7.6%

⁽¹⁾ Purchases of property, plant and equipment and intangible assets.

⁽²⁾ Net cash flow from operating activities less net acquisitions of property, plant and equipment and intangible assets.

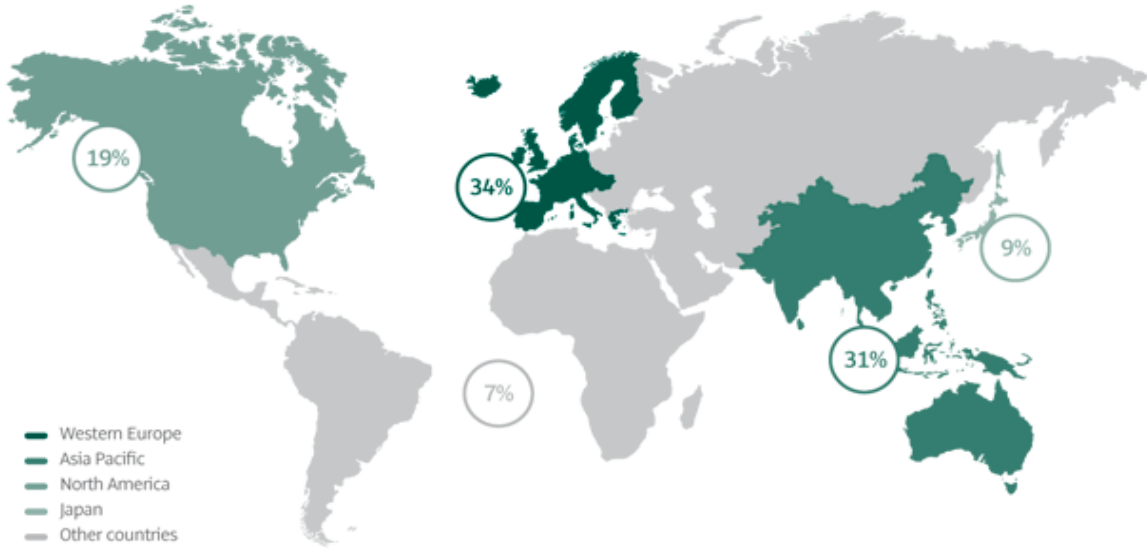
⁽³⁾ Net debt is defined on page 6 of the 2017 Reference Document.

FIGURE 15 - KERING'S KEY FINANCIALS 2017

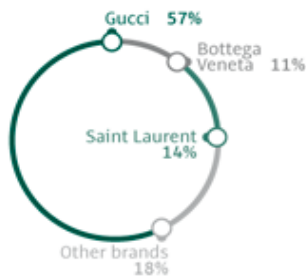
SOURCE: KERING (2018). GROUP KEY FIGURES. RETRIEVED OCTOBER, 2018, FROM [HTTP://WWW.KERING.COM/EN/FINANCE/GROUP/GROUP-KEY-FIGURES](http://www.kering.com/en/finance/group/group-key-figures)

breakdown of revenue

By region



By brand



By product category



By distribution channel



FIGURE 16 - KERING'S REVENUE BREAKDOWN

SOURCE: KERING (2018). BRANDS KEY FIGURES. RETRIEVED NOVEMBER, 2018, FROM [HTTP://WWW.KERING.COM/EN/FINANCE/GROUP/BRANDS-KEY-FIGURES](http://www.kering.com/en/finance/group/brands-key-figures)

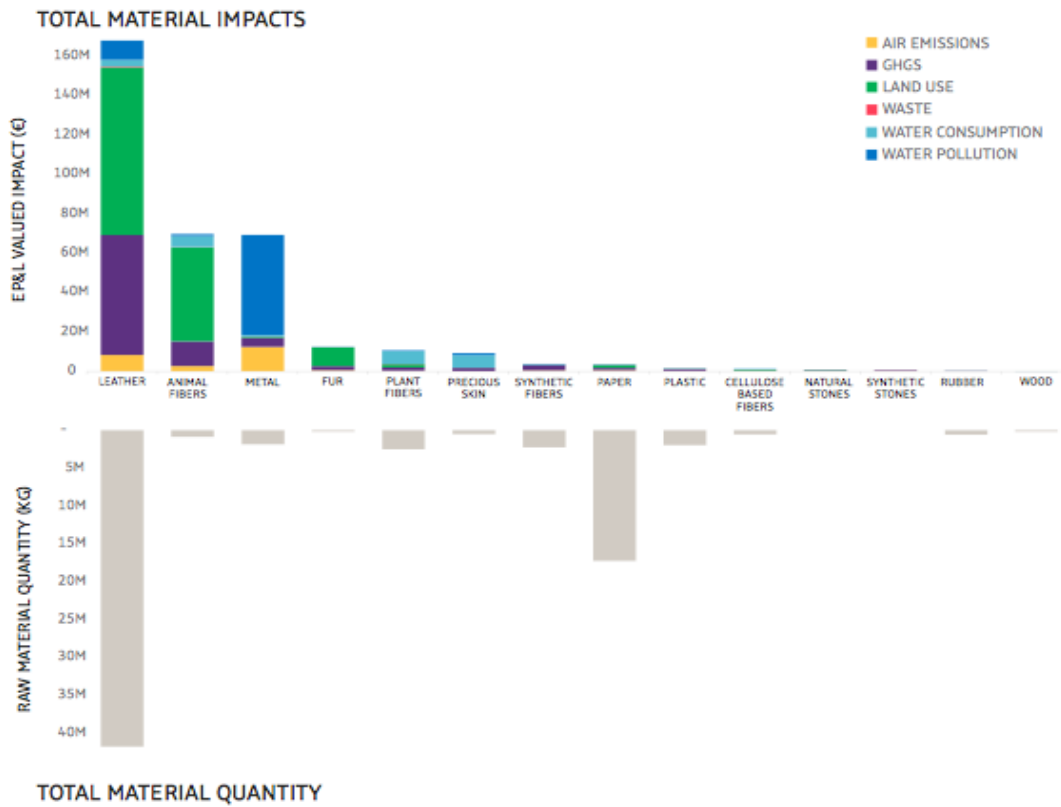


FIGURE 17- EP&L CONTRIBUTION OF MAJOR GROUPS OF RAW MATERIALS AND QUANTITY OF CONSUMPTION

SOURCE: KERING (2018). ENVIRONMENTAL PROFIT & LOSS (EP&L) 2017 GROUP RESULTS. RETRIEVED NOVEMBER, 2018, FROM [HTTP://WWW.KERING.COM/SITES/DEFAULT/FILES/KERING_2017_EPL_REPORT.PDF](http://www.kering.com/sites/default/files/kering_2017_epl_report.pdf)

3.10 Teaching Notes

3.10.1 Overview

The “Kering – A path towards sustainable luxury” case study analyses how the luxury conglomerate Kering was able to adapt to the increasing public concerns regarding environmental sustainability, given its industry and business model.

To start off, the first part focuses on a small introduction followed by a presentation of the Kering group, explaining all about its creation, the history and the conglomerate’s current and former brands.

The second part dives into the overall luxury market, presenting its major players, history and also relating its performance with the 2017 economic outlooks and geographical implications. Moreover, it explains the division of the luxury segments and goes into detail about the personal luxury goods sector. This part ends with the topic regarding sustainability concerns, in and out of the industry.

The third part goes back into Kering, now focusing on the brand in 2017. It shows its business model and explains its fight for sustainable luxury. The group’s efforts for being environmentally sustainable, from its 2025 strategy, EP&L tool and the Kering foundation. Moreover, specific examples regarding individual brands are given, in order to make the strategy clearer.

Finally, the fourth and last part, is an outlook for the future. This is a reflection on how these efforts will affect the firm’s performance and whether it is a positive path for a luxury conglomerate to follow.

3.10.2 Teaching objectives

This case study has as its main objective raise students’ awareness regarding the luxury industry and the increasingly importance of sustainability issues in the business world.

Firstly, the primary goal is to educate students regarding the importance of the external environment on corporate performance, especially on how significant changes in this environment can affect the firm and on the importance of adaptation.

Secondly, to analyze the ability of a big successful conglomerate to sense critical market changes and to adapt to them successfully, while maintaining its core values intact. Also, to

understand how a firm's dynamic capabilities impact its ability to adapt to an environmental change.

Finally, to examine the importance of corporate structure in the achievement of corporate-set goals.

3.10.3 Intended contribution

The case's focal contribution is to highlight how Kering, one of the biggest luxury conglomerates, was able to successfully adapt to the important consumer-preference shift that was the rise in concerns for environmentally-sustainable products consumption. Being a part of such a specific industry such as luxury goods, that represents significant differences in buying behaviors when compared to other industries, the firm was able to maintain its prestige and desirability level intact – or even superior – while changing towards more sustainable practices.

The Kering case's objective is to illustrate both the topic of Strategic Change and Dynamic Capabilities, more specifically the importance of using these in order to successfully adapt to an external environment change.

3.10.4 Pedagogical overview

For a better understanding as well as analysis of the case situation, the optimal audience for the “Kering – A path towards sustainable luxury” case are MSc-level students, with prior basic strategy knowledge. The case should be used either in a strategy course or, if the instructor sees fit, a luxury-focused course.

In order to efficiently study this teaching case students must have read it in advance, before class.

Moreover, students are required to have prior knowledge regarding strategic change and dynamic capabilities' frameworks. In light of that, both the instructor and students are advised to have read Barreto's paper “Dynamic Capabilities: A Review of Past Research and an Agenda for the Future” (Barreto, 2010, Journal of Management) in order to apply the author's Dynamic Capabilities' framework.

In order to present this case to students, the instructor should have an understanding of the luxury industry, as well as the luxury-consumer behavior, thus it is suggested the reading

of Jean-Noel Kapferer's paper "The specificity of luxury management: turning marketing upside down."

It is crucial that the instructor is familiar with the Kering group, its brands, core values and mission. For that, prior research is recommended, such as visiting the company's website, researching about its history and reading the latest company reports.

3.10.5 Assignment questions & Analysis

This case follows the luxury conglomerate Kering's path towards being a company that successfully adapted to more environmentally-sustainable practices, despite being in an industry known for its harmful manufacturing ways. In order to guide the student's understanding of the Kering case, I propose four distinct questions that should be asked and further analyzed in a class discussion.

Question 1: After carefully reading the case, analyze the external environment for the luxury goods industry. Explain what was the exogenous change that affected brands in this industry.

The goal of this question is for students to study the external environment affecting the luxury industry. In order to answer this question in a structured way, students may use, for instance, the PESTEL framework.

P – Political

There are several political factors affecting the luxury industry, as mentioned in the case. Apart from terrorism, other factors such as the growing popularity of extremist political parties in Europe were affecting the continent's political stability. Brexit was also a crucial factor for the UK's market, as it leads not only to political instability but also to a decrease in the level of international commercial relations. The United States' administration's potential protectionist measures could harm the country's commercial relations with China, one of the greatest consumers of luxury goods. In the Middle East, terrorism and geopolitical instability also reflected uncertainties for the luxury market.

All these factors were causing uncertainty in the luxury industry.

E – Economic

Economic factors intensely affect the luxury market. In 2017 the global economy was in a positive period of growth after having gone through a harsh financial crisis. However, tightening monetary policies could affect consumer's purchasing power. Europe presented a rapid GDP growth as well as an increase in exports. Middle Eastern countries were strongly affected by shrinking oil prices.

S – Social

Social factors represent one of the main aspects affecting the luxury industry. The consumer preferences were rapidly changing, with millennials appearing as an important part of the luxury consumers. The majority of consumers from this generation were concerned about making environmentally-friendly choices in their life, even when indulging in a luxury purchase. The so-called "millennial-mindset" also shows a switch in preference in terms of style with casual streetwear clothing and sneakers increasing at a 25% and 10% rate, respectively.

T – Technological

Consumer's way of purchasing their items was changing as digital platforms became the preferred mean of shopping and information-gathering, especially through mobile smartphones. Social media also played a significant role, as digital influencers defined new trends and consumers posted about their possessions, in order to showcase and define their social status.

E – Environmental

Climate change impacts water availability and crop production such as cashmere, angora or cotton, which are massively used in the fashion luxury industry. Animal welfare was compromised when brand's used skins and fur for the production of clothing and accessories. Many production processes, such as tanneries or crops, were polluting and damaging for soils and water. Consumer's preferences had also switched towards eco-friendly products.

L – Legal

Legislation has been increasingly protecting the environment. As stated on the case, in 2018 the European Parliament banned single-use plastics such as straws or plates. This clearly shows the change occurring in terms of laws and regulations, that focuses on reducing waste and pollution.

Students should then refer the **exogenous shock** affecting the industry:

The main exogenous shock present in the case is a change in consumer preferences. Concerns for environmentally-friendly practices and products were significantly growing, translating into consumers attributing a higher value to products and companies that did not harm the environment.

Question 2: What did the board of Kering change in order to align with the external environment?

This question aims at the analysis of the company's internal environment. Students should state and explain 3 main actions:

Change the organizational structure: Kering developed an important Sustainability Department and Committee that was embodied throughout the whole conglomerate, from the Board of Directors (with a Chief Sustainability Officer) to each individual brand. (See figure 5). Furthermore, the group included three distinct ethics committees, with the objective of maintaining the code of ethics.

Develop the Environmental Profit and Loss (EP&L): The EP&L's creation and usage was one of Kering's most relevant moves towards sustainability. The tool allowed the measurement and analysis of the group's resources and across the supply chain (See figure 7 and 8).

Propose the 2025 Strategy: Kering's strategy focused on specific goals to be achieved until the year of 2025. By having these clear targets set, based on three pillars – Care, Collaborate and Create -, the group was able to focus as well as transmit its “green” vision towards all its brands (See figures 9 to 11).

In addition to these main points, students can add specific brand's actions such as:

Alexander McQueen's replacement of cotton for its organic alternative, not only decreasing pollution but also saving water, fossil fuel and energy.

Bottega Veneta's decision to use chrome-free leather tanning, saving water and energy.

Gucci's new regenerated cashmere production, improving waste and animal welfare, and its 2017 decision of going completely fur-free.

Question 3: Analyze Kering in 2018 and apply the Barreto's dynamic capabilities framework. Quantify each capability by using "low", "medium" or "high".

Propensity to sense opportunities and threats – high

The change in consumer preferences for environmentally sustainable practices and products could be seen both as a threat and an opportunity for luxury brands. Kering sensed it and used it as an opportunity, making "green luxury" a differentiating part of its mission and business model.

To have "a responsive vision for luxury" had been in the group's core business model, showing the commitment to being sustainable (See figure 4).

When Pinault took over its position as CEO, he had a clear vision to turn Kering into a pure luxury group, all while standing for "modernity, responsibility and engagement, while having a desire to become the best luxury group when it comes to creativity, sustainability and economic performance".

Propensity to make timely decisions – high

Kering first implemented the pioneer EP&L system using it for the PUMA brand, further broadening the tool to the whole group. Kering is the only luxury player present on sustainability markers such as the Dow Jones Sustainability Index, S&P Global Market Index or Corporate Knight's Global 100 Index, showing a faster response to environmental concerns than its competitors.

Moreover, the group was not facing any crisis and was not under any attack of external agents, meaning that the decision was not forced. Kering decided to move into this direction

due to its core values and to its own belief that it was the best position to achieve a long-term success. Kering was a clear first within its industry, thus making a timely decision.

Propensity to make market-oriented decisions – high

Kering tackled the rising consumer concern for sustainable products, enabling them to become an awarded leader in the matter as the group's sustainability strategy was recognized and awarded by several NGO's and rating agencies.

Propensity to change the resource-base – medium

Kering reconfigured its resources by adopting new production processes such as regenerated cashmere production, chrome-free leather tanning or organic cotton usage. An example of this is the decision taken by Alexander McQueen brand: "In order to reduce raw material related impacts, the brand tried to find alternative ways of sourcing its resources." In its Core Business Model: Pillars (Figure 4) Kering says it wants to focus on innovation within the Houses, as a way to also reconfigure its resources.

Regarding the expansion of its resource base, the Group mentions the acquisition of tanneries.

The Group also reduced its resource base to fulfill its desire to become a pure luxury player, when it sold PUMA in 2018. This decision allowed to focus the core business on the specificity of managing luxury brands. Also, being an "all luxury" group increases the group's prestige in the mind of the consumers.

Question 4: (Reflection question) Do you think it is possible for a luxury conglomerate such as Kering to keep its notion of rarity and craftsmanship while being environmentally sustainable?

The aim of this question is to encourage divergent thinking and discussion among students.

For instance, some students might advocate that luxury is about exclusivity, rarity and precious materials, which ultimately diverges from the new "ecological" mindset and will

ultimately lead to failure. Without scarce and valuable materials, such as precious animal skins, stones or natural materials, a luxury brand's product will have the same real value than other "lower-end" brands, as it is the supreme quality that makes the luxury consumer want and buy the product. Moreover, without using scarce materials, production processes are much simpler, and it is possible to increase stocks, completely destroying the scarcity.

However, students might also defend that a luxury product's value is in the mind of the consumer, meaning that, no matter the actual materials or production method used, it is mostly the perceived brand value that will prevail. In addition, craftsmanship will not be lost as specialized artisans and designers will continue to create products, the only change will be the material. Regarding scarcity, and in order to preserve it, brands should be careful with manufacturing and inventory numbers, maintaining a very limited amount of goods at all times.

3.10.6 Board plan

This case is best used during a 90-minute lecture. A possible usage of class time is represented in the following table:

Activity	Time (minutes)
Dynamic capabilities theoretical review	15
Question 1 – external environment	15
Question 2 – internal environment	15
Question 3 – dynamic capabilities	20
Question 4 – reflection and discussion	15
Conclusion and overall review of the Kering case	10

4 Discussion

This thesis supports and exemplifies the importance of strategic change within a company in order to survive and maintain a superior performance in a changing environment. The Kering case shows how a real company reorganized its corporate strategy and organizational structure with the objective of implementing different processes that are best aligned with new consumer preferences. It also illustrates the dynamic capabilities' view, displaying evidences of Kering's individual usage and level of this concept, that can be defined as "the firm's potential to systematically solve problems, formed by its propensity to sense opportunities and threats, to make timely and market-oriented decisions, and to change its resource base" (Barreto, 2010) .

Van der Ven and Poole (1995) defined strategic change as a firms' difference in form, quality or state over a period of time. Furthermore, Snow and Hambrick (1980) explained it as occurring when "the organization (1) modifies in a major way its alignment with the environment and (2) substantially alters technology, structure, and process to fit the new alignment." Considering to these two article's statements, Kering exemplifies these theories as it has showed to have experienced strategic change. The company adjusted its core business, mission and vision in order to face important environmental changes, growing into a pioneer group in sustainable luxury. Additionally, the group reconfigured its internal corporate governance structure to include sustainability and ethics committees, as well as an executive Sustainability Officer, and developed innovative processes and tools to incorporate sustainable production processes.

According to some authors, change is seen as an exception (Tsoukas & Chia, 2002), accompanying a rapid environmental shock. However, this case does not show a sudden environmental shock, but rather an ongoing process of change in consumer preferences and behavior, as it was something that happened gradually along with the ascendance of the millennial generation to active consumers and consequent rising concern about environmental protection. Instead, the Kering group case supports the statements of Gioia and Chittipeddi (1991). These authors explained that strategic reorientations are crucial for maintaining success and growth in the long-run, meaning that a crisis is not always needed for firms to implement change.

Authors such as Adner and Helfat (2003) reinforced the importance of management in strategic change decisions. Kering's development to a sustainable pure luxury group was implemented much due to CEO François-Henri Pinault. His vision was to build a luxury group focused on sustainability and care, not only for the environment but also for their employees.

Audia, Locke and Smith (2000) stated that in order to survive, firms must “anticipate or detect changes and initiate strategic transformations”. Indeed, Pinault’s ability to sense a potential opportunity for his company, in the luxury goods sector, enabled the group to differentiate from its competitors by being actively environmental sustainable and was crucial for its path towards success.

The dynamic capabilities view, a recent concept, was also present within the Kering teaching case. Teece et al (1997) defended these capabilities as only being relevant in highly dynamic environments, which is not the case regarding Kering, as the changes in consumer preferences mentioned in the case are not sudden but on-going. Nonetheless, other authors such as Eisenhard and Martin (2000) admit as relevant more moderate environments in regard to dynamism.

Zollo and Winter (2002) mentioned these capabilities as being structured, stable and persistence. Kering showed its persistent and ongoing efforts, not in response to any scandal or rapid switch on consumer preferences, but to consistently improve the group’s processes and performance.

While Teece (2007) defended that “dynamic capabilities lie at the core of enterprise success”, Barreto (2010) added four distinct dimensions, creating a more detailed framework for the concept. Considering Kering, it is showed with evidences from the case, that these dimensions can have distinct levels and are relevant to the survival and success of the company. The group had mostly high propensities, which probably defined its success in the industry. My findings, represented by the Kering teaching case, show that companies need to have dynamic capabilities to succeed in their field.

The literature and the case show the importance for managers to look at the market in its whole and try to predict its potential opportunities and threats, in order to address them in a regular and on-going manner, instead of waiting and then trying to “fix” a firm’s strategy after a crisis.

The limitations regarding these theories exist, especially within the dynamic capabilities’ literature as it is a recent topic in strategy. The lack of quantitative frameworks for dynamic capabilities makes it difficult to analyze with precision the level for each firm. Having this into account, future research regarding this subject would be a crucial improvement for the strategy theory. Moreover, future research could also focus on how firms can change its organizational structure to new sustainability departments and officers, and whether it has a real effect not only regarding environmental results but also profitability.

5 Conclusion

Literature has shown that strategic change is crucial for a firm's survival and success, not only in cases of crisis or shocks but also in order to progressively adapt to changing environments. The main theoretical perspectives mentioned in this thesis are Strategic Change as well as Dynamic Capabilities. A company's two fundamental dimensions of success are profitability and survival. However, having a sustainable competitive advantage is what differentiates regular firms from top performers in the industry. In order to achieve top performance, it is crucial for firms to adapt and to go through internal changes.

The main theoretical perspectives mentioned in this thesis are Strategic Change and Dynamic Capabilities. Strategic change happens when a company changes its internal structure, technology, processes or resources in order to better align with the external environment. The Dynamic Capabilities view is undoubtedly important in explaining how a company can achieve a sustained competitive advantage in changing environments.

This teaching case was created in order to illustrate the literature in these fields, using a real-life example. The case, focuses on the luxury industry, in the case of Kering, a pure luxury group, that was able to successfully implement change following a shift in consumers' preferences. Change can happen not only in the organizational structure, but also in rearranging processes, defining goals or company's mission. Kering has become a pioneer in the luxury sector, by following a core business strategy focused on having positive practices, making the least damage possible to the environment.

Moreover, the fairly-new strategy concept of Dynamic Capabilities explains how some companies are able to survive and others to fail when faced even with moderately dynamic environments. Kering exemplifies how having a set of dynamic capabilities has been crucial for the company to be able to succeed in its change, as it had the means to do the right decisions, at the correct time. Also, the Kering case depicts the specificity of the luxury industry and its consumers, factors which are relevant for the analysis of the external environment.

The final conclusion of this thesis falls for the importance of having the capacity to make the correct internal changes, at the right time, in order to succeed. Dynamic capabilities are crucial not only for a firms' survival but also for its prosperity within the industry, meaning that top players are the ones who have high-leveled dynamic capabilities as well as an ease in sensing external changes, no matter how slight, and implementing new processes to respond and thus adapt to them.

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