The Chinese Luxury Fashion Market: Strategy Implications and Recommendations for the YOOX Group

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SCHOOL OF ECONOMICS AND BUSINESS ADMINISTRATION
A thesis submitted for the degree of

Master of Science (MSc) in Management

SEPTEMBER 2011
THESSALONIKI – GREECE
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DISCLAIMER

This dissertation is submitted in part candidacy for the degree of Master of Science in Management, from the School of Economics and Business Administration of the International Hellenic University, Thessaloniki, Greece. The views expressed in the dissertation are those of the author entirely and no endorsement of these views is implied by the said University or its staff.

This work has not been submitted either in whole or in part, for any other degree at this or any other University.

Signed: [Signature]

Name: Eleftheria Votsari
Date: 30th September 2011
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I also gratefully acknowledge my supervisor, Dr. Lida Kyrgidou, whose great knowledge, insightful comments, experience and support helped me complete my thesis.
ABSTRACT

Nowadays, many luxury fashion companies are looking for growth in the promising Chinese market for luxury consumption. China represents the world’s second largest luxury market and possesses the world’s biggest online population. Hence, a great opportunity for growth in China lies ahead and there is strong international academic and business interest in the Chinese market.

This dissertation examines the internationalization process of YOOX Group (an Italy-based luxury fashion e-tailer) in the Chinese luxury fashion market and particularly sheds light on its strategic choices and implications. As such, the dissertation is guided by and aims at answering a key research question: “What would be a viable expansion strategy for YOOX in China?”

The overall contribution of this dissertation is to increase the understanding of entry mode strategies in the retailing industry with a special focus on the internationalization strategy of luxury fashion e-tailers in China. More precisely, this paper defines the factors that influence the entry mode strategy of YOOX Group and examines its viability in the demanding Chinese e-context. Therefore, an exploratory qualitative research design in the style of a case study analysis is adopted. The primary data collection is conducted through a structured Skype interview of YOOX Group’s China Country Manager. Secondary data are obtained from broader theoretical themes and empirical concerns of the existing literature. To make the data analysis even sounder, certain tools of Strategic Management are used.

The dissertation provides important managerial implications and insightful practical guidance for luxury retailers who want to penetrate the promising, yet diverse and complicated market of the Luxury Dragon.

Keywords: Internationalization strategies, Luxury fashion retailing; China market entry; Chinese luxury fashion market; YOOX Group; pure play e-tailers

Eleftheria Votsari
30th September 2011
“Delivering to China is different from having operations in China...
The only way to do serious business with China is from China”.
Federico Marchetti, Founder and CEO of YOOX
February 2011
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1 Introduction

As markets are becoming increasingly competitive, growth can be regarded as a main objective for companies operating globally. Growth can be achieved through internationalization, or more specifically through the development of new markets. Retailers are no exception in the quest for growth and currently, several luxury retail companies are looking for growth opportunities in the promising Chinese luxury market. This dissertation examines the internationalization of YOOX Group (a luxury fashion e-tailer) in the Chinese luxury fashion market and particularly sheds light on its strategy choices and implications. As such, the dissertation is guided by and aims at answering a key research question: “What would be a viable expansion strategy for YOOX in China?”

The particular dissertation focuses on luxury fashion retailers, and specifically a pure play e-tailer’s\(^1\) expansion strategy in China, as the subject of examination and analysis for three main reasons. The first reason for which a luxury fashion pure play e-tailer is chosen as the unit of analysis is due to two megatrends that pose a challenge for growth. First, China represents the world’s second largest luxury market and possesses the world’s biggest online population. China’s vast consumer base coupled with its robust economic growth makes it an increasingly attractive country for international expansion (KPMG, 2007). Thus, there is an international academic and business interest in the Chinese market, which constitutes one of the largest commerce providers. In addition, China has demonstrated increasing demand for online purchases of luxury products. These facts make the internationalization of a luxury fashion e-tailer in China a very interesting field of study, as it can be expected that its internationalization will differ from other retailers, especially in the light of the challenging country conditions in China. Second, entry mode strategies of luxury fashion retailers have never been studied from an international business strategy perspective. Entering new markets is associated with many challenges,

\(^{1}\) Pure play e-tailers have no physical stores and all their business transactions are completed online. They usually form strategic alliances or partnerships with other companies (e.g. carriers) to provide better customer services. Pure play e-tailers are Amazon.com and e-bay.com (Chen, 2010).
the most significant being the choice of entry mode. Entry mode choice can have significant and far reaching effects on the retailer's performance in a new market (Doherty, 2000). Existing literature on entry mode choice addresses mostly multinational companies (MNCs), especially from the manufacturing and service sectors. Although some studies discuss the entry mode choice of international retailers in general, they do not focus on fashion retailing, not to mention luxury fashion retailing. Moreover, most studies focus only on market entry decisions and there is an important lack of literature addressing evolution aspects over time. Also, there is scarcity of studies that have focused on pure play e-tailers. Last but not least, this dissertation is also a result of strong personal interest in fashion and attraction to branded and unique apparel, footwear and accessories.

This dissertation makes an initial attempt to study the entry strategy of a pure play e-tailer in China, an understudied phenomenon that is of considerable interest to academics and practicing managers. The overall contribution of this dissertation is to increase the understanding of entry mode strategies in the retailing industry with a special focus on the internationalization strategy of luxury fashion e-tailers in China. More precisely, this paper will define the factors that influence the entry mode strategy and examine its viability in the demanding Chinese e-context. Therefore, a qualitative case study approach is adopted and a case study of a global Internet retailer, YOOX Group's entry into the Chinese market is conducted.

This dissertation has adopted an exploratory qualitative research design in the style of a case study analysis. The primary data collection was conducted through a structured Skype interview of YOOX Group's China Country Manager. Secondary data were obtained from academic journals' databases, complemented with other Internet sources, including YOOX Group's corporate website. The data analysis was predominantly derived from the interview information. Where applicable, secondary data was grouped and filtered to focus on specific aspects related to the present dissertation.

The basic findings of the research suggest that in order to sustain its first-mover advantage in China, YOOX has to continue to invest in R&D to retain its technical edge and customer service profile, besides the necessity to move quickly and capture a substantial market share in China until the end of 2011, when the flagship theyoox.com.cn will launch. YOOX Group should also cement existing relationships with Commercial and
Strategic Partners and develop new relationships with Chinese partners. It is also recommended that the online retailer does not enter India and Brazil for the time being, as it already has enough opportunity to grow in China and Russia.

At theoretical level, this research contributes to enrich related literature and knowledge with regard to internationalization expansion strategies. To this end, the current study is in agreement with Evans’ et. al theory (2008), which states that almost every retail format requires at least some adaptation to tailor the specific needs of the foreign market. It also verifies the studies of Hollander (1970) and Lualajainen (1992), which claim that “pull” (proactive) factors are the main reason for luxury fashion retailers to enter new markets. At the managerial level, the case study of YOOX Group provides important lessons and insightful practical guidance. Managers can gain information on how they can allocate their available resources and plan an entry into the Chinese online luxury fashion market. Moreover, they are also informed about potential challenges and critical success factors in conducting Chinese e-commerce.

The structure of the dissertation is as follows. The second Chapter provides a literature review of the fundamentals of internationalization. It gives an insight into the motives for internationalization, the choice between adaptation and standardization strategies and the specific characteristics of retailing internationalization. It further clarifies the different entry modes – with particular reference to China- and their impact on the risk, control and resource structure of international operations. It also alanyzes the characteristics of luxury consumption in China. Chapter 3 elaborates on the research design and methodology applied in this dissertation. Then, in Chapter 4, the results of the case study are presented. Subsequently, discussion and recommendations about YOOX Group’s strategy in China are included in Chapter 5. Theoretical and managerial implications, as well as limitations and future research will be derived in Chapters 6 and 7 respectively. Finally, the dissertation will end up in a conclusion in Chapter 8, thereby answering the research question and sub-questions. Appendix I contains the interview protocol used to facilitate the interview. Appendix II shows the business model employed by the Group and Appendix III provides an exhibit showing the strategic coverage of the online fashion market. Appendix IV includes a PESTEL analysis.
2 Literature Review

2.1 Internationalization Processes

Recent decades have witnessed a dramatic globalization of business due to increasing trade policy liberalization, stability in monetary transactions, regional economic integration, convergence of customer preferences, and technological advances (Katsikeas, Samiee, and Theodosiou 2006). This global trend has imposed a new way of conducting business, urging firms to reconsider their business models and adjust their strategic orientations. In this context, internationalization appears a key strategy for firms’ global presence, expansion or even survival and firms have increasingly adapted internationalization strategies in order to be able to successfully compete in the new business environment. The current section is devoted to a literature review in the field of internationalization, related strategies frequently adapted, motives and factors affecting firms’ entry decisions, considering the examples of other companies that have expanded internationally, referring also to the particular industry of fashion retailing and the Chinese context, so that a general overview is provided to the reader. Building on the existing literature, the study’s primary research questions and objectives are stated next.

2.1.1 Motives for Internationalization

Firms engage in international business due to marketing objectives, strategic reasons, behaviour motives or economic rationales (Peng, 2006), but most importantly, to expand sales, to acquire resources and to minimize risk (Daniels, et al. 2003).

Wrigley and Lowe (2002) have classified “push” (or reactive) and “pull” (or proactive) factors that traditionally are cited as influencing retail internationalisation. These factors are listed in Table 1. The reactive approach claims that domestic market conditions influence retail internationalization; the so-called push factors that are external to the firm.

The proactive approach defines external as well as internal factors that motivate retailer internationalization (Evans et al., 2008). Basic external factors driving internationalization are untapped markets and niche opportunities. Furthermore,
comparative advantages, such as unique retail concepts, superior logistics, and international knowledge are proactive drivers of internationalization. Another proactive factor driving retailing internationalization can be the retail brand itself, especially in the case of fashion retailers. Thus, the uniqueness and desirability of the brand can push a retailer into new markets as well (Evans et al., 2008).

<table>
<thead>
<tr>
<th>“Push” factors</th>
<th>“Pull” factors</th>
</tr>
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<tbody>
<tr>
<td>• Perceived/imminent saturation in</td>
<td>• Unexploited markets</td>
</tr>
<tr>
<td>domestic markets</td>
<td>• Niche opportunities</td>
</tr>
<tr>
<td>• Spreading of risk</td>
<td>• Pre-emption of rivals</td>
</tr>
<tr>
<td>• Consolidation of buying power</td>
<td>• Higher profit potential</td>
</tr>
<tr>
<td>• Public policy constraints</td>
<td>• Access to new management</td>
</tr>
<tr>
<td>• Economic conditions</td>
<td>• Following existing customers abroad</td>
</tr>
<tr>
<td>• Maturity of format</td>
<td>• Comparative advantages (unique retail concept, superior</td>
</tr>
<tr>
<td></td>
<td>logistics, international knowledge)</td>
</tr>
<tr>
<td></td>
<td>• Uniqueness and desirability of the brand</td>
</tr>
</tbody>
</table>

Table 1: Factors traditionally cited as influencing retail internationalization (Wrigley and Lowe, 2002)

Research found the motivations of luxury retailers internationalisation are mainly proactive, for example, Lualajainen (1992) argues that luxury fashion retailers, such as Louis Vuitton, entered foreign markets because of the demand for the elite brand and distinctive product offer. Hollander (1970) observed that luxury fashion houses enter international markets mainly for the prestige, whereas department stores enter new markets due to saturation. Limited number of studies which considered luxury fashion retailers, found that the major motive behind luxury retailers internationalisation is encouragement, namely, the new markets with potential benefits that pulled retailers into them. However, since they were conducted in the European and the American markets (except Lualajainens (1992) study on Louis Vuitton which covered the Asian market but not China), it is questionable if the motives behind retailers expansion into China are the same.
Furthermore, it is clear that the reasons for international expansion may differ for each company, as well as their optimal entry modes.

2.1.2 Adaptation versus Standardization strategies

For international retailers the degree of standardization or adaptation refers to the elements of the retail format (Evans et al., 2008). In this framework, a standardization strategy or a global strategy is followed when the retail format is exactly reproduced in the foreign market. On the other hand, an adaptation strategy includes variations in product, pricing and promotion to suit the specific conditions of the foreign market. However, almost every retail format requires at least some adaptation to tailor the specific needs of the foreign market (Evans et al., 2008). Sternquist (1997) makes a distinction between global and multinational retailers. Global retailers follow a standardized format in various countries while multinational retailers adapt their formats according to the socio-economic factors of the country they are moving to.

2.1.3 Market Entry Modes

Existing theories on entry mode decisions focus on development of country-specific knowledge, global strategies, and competition strategies (Johansson, 2000). Country-specific knowledge models indicate that firms usually start with low-control and low-risk entry modes and then shift to high-control and high-risk entry modes when they accumulate country-specific knowledge (Eriksson, et al., 1997). In other words, the selection of entry modes is a step-wise process. Global strategy models and competition models argue that the process may not necessarily be step-wise. Intense competition and global strategies may force firms to take high-control and high-risk entry modes before they accumulate country-specific knowledge (Kim and Hwang, 1992; Madhok, 1996). The main entry mode strategies available to retailers are contractual agreements, by licensing or franchising, and direct investments, by means of wholly owned subsidiaries (WOS), mergers and acquisitions, or joint ventures. Each of these entry modes involves another risk, cost and control structure (Moore & Doyle, 2010).
Due to their specific characteristics, luxury fashion retailers differ from other retail sectors. Moore et al. in 2010 investigated the role of flagship stores and why they are crucial to the international development of luxury retailers despite their prohibitively high cost. The researchers found that luxury flagship stores represent a strategic approach to market entry in a foreign market. Entering a foreign market with a flagship store, allows the luxury fashion retailer to benefit from strategic brand building and market development advantages (Moore et al., 2010).

### 2.1.4 Factors influencing market entry modes

Literature defines several factors that have an impact on entry mode selection. A recent study published in the *Journal of Fashion Marketing and Management* by Lu et al. (2011) identifies nine factors that influence fashion retailers’ entry mode choice. These factors were classified in three groups: firm-specific factors; country-specific factors; and market-specific factors. Table 2 below summarizes these factors. It is important to highlight that the combination of factors may suggest different entry mode choices and trade-offs may be necessary (Lu, 2011).

<table>
<thead>
<tr>
<th>Group</th>
<th>Determinant factor and retailer’s characteristic</th>
<th>Entry mode choice</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Higher control</td>
</tr>
<tr>
<td>Firm-specific factors</td>
<td>Asset specificity</td>
<td>High</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Low</td>
</tr>
<tr>
<td></td>
<td>Brand equity</td>
<td>High</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Low</td>
</tr>
<tr>
<td></td>
<td>Financial capability</td>
<td>High</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Low</td>
</tr>
<tr>
<td></td>
<td>International experience</td>
<td>High</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Low</td>
</tr>
<tr>
<td>Country-specific</td>
<td>Country risk</td>
<td>High</td>
</tr>
</tbody>
</table>
Pan & Tse (2001) further noted that industries with high advertising intensity tend to exclusively enter foreign markets by means of WOS, a fact that also applies for luxury fashion retailers. Luxury fashion retailers rely heavily on the reputation of their brands, which depends on their investments in brand building via advertising.

### 2.1.5 Entry Modes in China

Selection of entry modes in China has been a topic of strong interest to international marketing and strategic management researchers. This is not surprising, as China has grown into a magnet for foreign investments. Several firm-level studies have tested the applicability of the internationalization theory to explain the entry mode of MNCs in developing countries. For instance, Mok et al. (2002) have examined the entry mode of Coca-Cola in China since 1979. Coca-Cola employed different modes of market entry over three different stages of operation; a) The franchise mode of entry (1979-1984): at this stage Coca-Cola sold syrup to its franchised Chinese-owned bottlers and employed local market agents for production and distribution b) The joint venture Mode of entry (1985-1992): Coca-Cola penetrated China by acquiring the management rights to the bottling plants through joint ventures. Also, it built concentrate plants in Shanghai in the form of WOS c) A hybrid mode of entry (1993-present): Coca-Cola’s franchising arrangements with foreign bottlers and its JVs with Chinese suppliers constitute the main elements of the company’s internationalization strategy.

<table>
<thead>
<tr>
<th>specific factors</th>
<th>Low</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cultural distance</td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Government restrictions</td>
<td>High</td>
<td>x</td>
</tr>
<tr>
<td>Market potential</td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Market competition</td>
<td>High</td>
<td>x</td>
</tr>
<tr>
<td></td>
<td>Low</td>
<td>x</td>
</tr>
</tbody>
</table>

Table 2: Decision making factors for the entry mode choice of fashion retailers (Lu, 2011)
In another interesting article, a Euromonitor International analyst compares the expansion strategies of Carrefour and Wal-Mart in China (Moreau, 2008). Wang (2009) offers a comprehensive analysis of success stories and setbacks of foreign retailers’ penetration in post-WTO China. As expected, the study concludes that the Western retailers (eg. Wal-Mart, Carrefour, Auchan, B&Q, Metro, Ikea, Makro), which possess the most resources and advanced information technologies, are taking the lead in penetrating the Chinese market. The Southeast Asian retailers (Lotus, Trust-Mart, E-Mart) have also expanded with impressive results, but their staying power is unclear. Although the Japanese (eg. Isetan, Jusco) retailers received the least negative publicity, they have made the least inroad in penetrating the Chinese market.

Other studies offer insight on an industry-level basis. For example, Ling et.al (2005) determined the important strategies that foreign architectural, engineering and construction firms adopt when they undertake projects in China. The specific objectives of this study were to investigate the effective market entry modes for penetrating China and the effective business strategies for managing projects in China. Another important article analyzed combinations of internationalization strategies and modes that automotive suppliers expanding into China have chosen (Kaufmann and Jentzch, 2006).

A study by Li (2002) departs from existing studies, by exploring the ways that online trading and online information exchanges influences entry mode selection of Western manufacturers in China. The study detects that with online trading and information exchanges, country-specific knowledge, market contacts and language barriers have less impact, when at the same time competition intensifies. Consequently, “...manufacturers now tend to enter China with traditionally high-risk and high-return entry modes and they do not have to do it in a step-wise way” (Li, 2002).

2.2 The Chinese Context

According to “China luxury market study 2010” by Bain & Company, China recently became the world’s second largest market for luxury goods, even surpassing Japan. Estimates for the years to follow indicate that China will become the largest luxury market in the world.
Six key trends have been identified in the luxury goods market in China:

- Continued trend of increased domestic shopping (vs. overseas)
- Tier 2 (fastest growing cities) and Tier 3 (regionally important) cities are the new battleground
- People consider themselves fashionable in most parts of the country, regardless of city Tier
- Consumers expect comprehensive and differentiated service experience
- Continued importance of online platforms
- Brand building efforts are more localized and are increasing
- Gifting is increasing and is more diversified

Based on market overview and key trends, the main challenges for luxury brands in China is to consistently deliver great consumer experience. It is notable that there is no backoff in pursuing luxury, as demand for counterfeit products decreases. Luxury shoppers are much too sophisticated and do not risk the embarrassment of owning a fake product. (Bain & Company, 2010).

According to a McKinsey survey, Chinese are becoming more attached to Western brands and brand loyalty increases. Additionally, 36% of China's young adults prefer to try out foreign brands frequently. They also spend large amounts for apparel and accessories and tend to spend even more as their income rises. As far as online sales are concerned, it is estimated that about 450 million Chinese are connected to the Internet, making the country the world’s most-populated online market. Finally, a great challenge for luxury brands is the unusual high taxes. (The McKinsey Quarterly, 2007).

### 2.2.1 Motivation for luxury consumption

Luxury consumption is undoubtedly an important component of the global economy. Despite a serious amount of research on luxury consumption, to date, most studies have been conducted in Western developed countries. Nevertheless, Wong and Ahuvia (1998) compared Singaporean women’s consumption of brand name luxury goods with those of the West. The researchers argued that Asians’ luxury consumption was mainly influenced
by Confucian collectivism, individual or group needs and values of being modest. Moreover, Asian consumers are more likely to purchase luxury brands for gifting, conforming to social pressure and status differentiation. Other studies (Zhou & Belk, 2004; Zhou and Nakamoto, 2000) have concluded that a major collectivistic value—“face”—which denotes the importance of the regard of others—may be the reason for Asians’ consumption of luxuries. Ying Wang et al. (2010) conducted a study in a metropolitan city of China and found that eight motives drove luxury consumption for Chinese consumers; these were self-actualization, product quality, social comparison, others’ influence, investment for future, gifting, special occasions, and emotional purchasing. Results showed that personal income, age, the motives of gifting, others’ influence, and product quality were significant predictors of luxury spending. Younger consumers, who did not typically make plans before buying, were more likely to buy luxury products out of emotion and less likely to do so for self-actualization or future investment.

2.2.2 Chinese Consumers’ Profiling

Numerous studies (e.g. Cui and Liu, 2001; Zhang et al., 2008) have shown the presence of diversity among Chinese consumers, implying that retailers operating in China must understand this diversity and market products accordingly. However, only one recent study focuses on segmentation of affluent Chinese consumers, who form the most promising target groups for luxury fashion goods. The authors of this study identified and profiled (according to psychographic criteria) five distinct submarkets of affluent consumers in 12 large cities, namely; achievers, conservatives, experiencers, followers and idealists. Of these segments, three seem the most suitable for potential niche markets for luxury fashion goods in China.

- Experiencers (early adopters, trendsetters), the largest segment identified, were found to be the best prospect of the five for developing a luxury fashion market.
- Achievers was the next best candidate group for luxury market, who have a strong awareness of brands and buy luxury products to show their status and wealth.
Idealists were found to be active purchasers of luxury products, but were the least conscious of well-known brands and engaged in individually oriented activities (Gao et al., 2009).

Chinese luxury consumption has been predominantly male-driven, a unique situation in the industry of high-end products. But as women are becoming more economically independent, they begin to account for a larger share of the luxury market and they are believed to have great potential in dominating an even larger share in the future (Rahda and Husband, 2006).

2.3 Research Gap and Research Questions

Although the aforementioned existing body of literature offers multiple insights and has unique strengths, it has also certain limitations that should be addressed. The most important of them are noted below;

1. Research addresses mostly MNCs, especially from manufacturing and service sectors. Although some studies discuss the entry mode choice of international retailers in general, they do not focus on fashion retailing, not to mention luxury fashion retailing.

2. Most studies focus only on market entry decisions and there is an important lack of literature addressing evolution aspects over time.

3. There is scarcity of studies that have focused on pure play e-tailers

To this end, the purpose of this thesis is to broaden the scope for potential theoretical development of e-tailer market entry mode strategy, a facet of international retailing which has remained relatively underdeveloped. The dissertation is guided by a core research question; “What would be a viable expansion strategy for YOOX in China?”. In order to answer the research question, the following sub-questions shall be answered:

- How attractive is the Chinese market for luxury companies and especially for YOOX?
- What characterizes the Chinese consumers and what are their expectations to and motivations for purchasing luxury fashion brands?
• How should YOOX sustain its first-mover advantage in China and what pricing strategy and positioning should develop?
• Which operations should be localized?
• What are the challenges ahead?
• What is the role of strengthening current partnerships and/or developing new ones?
• Is it crucial (and to what extent) for YOOX to develop its technology and logistics platforms?
3 Research design and methodology

So far this dissertation has discussed the factors and motives of retailers’ internationalization and entry mode strategies with a special reference to China. It also shed light on the characteristics of Chinese consumers’ consumption profile and China’s luxury fashion market. These fundamentals and the derived propositions about luxury fashion retailer internationalization have to be linked to empirical research in order to answer the research question of this paper, namely the viable strategy that a luxury fashion pure play e-tailer like YOOX should follow in China. In this vein, the following section is devoted to the empirical part of the study.

3.1 Research design

In order to gain insight into the motives, entry mode and strategies behind luxury fashion retailers’ entry into China, an exploratory qualitative case study research methodology was adopted, because an in-depth and open-ended research design which is qualitative in nature, is suggested for acquiring deeper comprehension of the complicated processes related to retailers’ internationalisation processes (Simpson and Thorpe, 1996; Doherty, 2000). Additionally, it is proved to be the most suitable for this sort of research, as it has been extensively used in previous studies conducted within luxury fashion retailers’ internationalisation context (Lualajainen, 1992; Fernie et al., 1997; Moore and Doyle, 2010). Given the exploratory nature of the research questions, a qualitative research method was employed for two reasons. First, a quantitative research approach could not capture the full diversity of non-standardized information that was needed for the purposes of the current study. Second, most of the required information was not quantifiable.

Researcher Robert K. Yin defines the case study research method as an empirical inquiry that investigates a contemporary phenomenon within its real-life context, when the boundaries between phenomenon and context are not clearly evident and in which, multiple sources of evidence are used. Case study research is a very useful method since it allows expansion and generalisation of theories through the combination of existing theoretical knowledge with new empirical insights (Yin, 1984). Moreover, a single case
can provide a holistic perspective on real-life events and processes leading to certain results.

On the contrary, a major point of critique is that it is difficult to access confidential data; moreover, the interviewee may not be totally honest. Also, it is hard to find a balance between depth and breadth: a single case increases the former but decreases the latter, while a multiple case study increases the latter but decreases the former.

This dissertation has adopted a qualitative research design in the style of a case study analysis, which was achieved by using in-depth interviews to gather meaningful and thorough data. This holistic way of data gathering, analysis, interpretation and understanding is appropriate for the study of management decision making and business activities as it examines the reasons of such actions within organisations (Silverman, 2000). In this respect, using an in-depth and open-ended qualitative approach is highly suitable for the purposes of the particular study because its aim is to examine the strategic decisions luxury fashion retailers make when entering China.

There are mainly two sorts of data, primary and secondary, that a researcher uses as a basis for a study. Primary data is collected by the researcher in order to provide answers to the study questions, whereas secondary data is collected by other researchers.

### 3.2 Collection of primary data

The chosen tool for the dissertation’s primary data collection was an interview through the use of a structured questionnaire, addressed to an executive believed to possess key insights primarily within the luxury fashion business, strategy formulation and execution, and emerging market challenges. In this framework, questions in a structured questionnaire were answered by a female top executive from YOOX’s office in Shanghai via an interview. Skype is nowadays a preferred method to conduct long-distance interviews. Due to the geographic distance the interview for this dissertation was carried out on Skype. The interviewee was the China Country Manager at YOOX Group, whose name is not disclosed for anonymity and confidentiality reasons. The executive was traced and initially contacted by the writer via the professional network Linkedin, was
informed about the study’s purpose and was ensured confidentiality and anonymity with regard to all information provided.

To ensure the coverage of all relevant topics, an interview guide was prepared, which is presented in Appendix 1 (Blumberg et al., 2008). Interview questions were tailored specifically in order to answer research questions, as it is well known that the quality of questions asked determines how good the answers will be (Merriam, 1998).

When the executive agreed to participate in this research, an informative electronic package was e-mailed to her several days before the interview appointment. This digital package included a brief overview of the research objectives and the standardized interview protocol, so that she could be better prepared.

The interview protocol was used to keep the interview focused, but dialogue during the interview allowed for flexibility in the pursuit of greater insight into important and interesting practices (Yin, 2003). The interview protocol was pretested with three experts in the field of strategy and international business and marketing, both academics and practitioners. The protocol contained fifteen open-ended questions and considered parameters related to internationalization strategy and mode of YOOX in China, including the time of market entry, its present position, its strategic alliances and its expected position in the years to come.

The protocol was composed in English and the Skype interview was also conducted in English, so no translation was required. The Skype interview lasted twenty minutes and took place on 05/09/2011 from 10.00-10.20 a.m. local time (15.00-15.20 p.m. in Shanghai). No major technical problems occurred during the interview procedure.

### 3.3 Collection of secondary data

Secondary data were obtained mainly from databases such as EBSCO Host, Science Direct, and Emerald Online Journals, complemented with other publicly available Internet sources. Specific information about YOOX Group operations, financials, strategy and entry into China was gathered from the company’s website, annual reports, roadshow
presentations, newspaper articles, and cited interviews of its founder and CEO, Federico Marchetti.

By combining primary and secondary data, the writer of this dissertation was able to identify many issues relevant to the internationalization strategy of YOOX’s entry strategy in China and answer the research questions of this paper.

3.4 Research credibility

During the research design phase, researchers must ensure that the study is well structured to guarantee construct validity, internal validity, external validity and reliability. Construct validity refers to the usage of the correct measures for the concepts being studied. Internal validity (of significant importance in explanatory or causal studies) demonstrates that certain conditions lead to other conditions and requires the use of multiple pieces of evidence from various sources. External validity reflects whether or not findings are generalisable beyond the immediate case or cases; the more variations in places, people, and procedures a case study can withstand and still yield the same findings, the greater external validity it possesses (Lewis, 2009). In a qualitative study like the one employed for the purposes of the current dissertation, the result is based on the way the interviewee (YOOX China Country Manager) perceives the reality - the researcher is responsible of portraying the reality as correctly and precisely as possible. If this is the case, then the study possesses internal validity. As a way to control for internal validity in this dissertation, the interview guide (protocol) was pilot tested sent to three academics and practitioners related to the field of Strategic Management beforehand to read it through and receive feedback. Reliability refers to the stability, accuracy, and precision of measurement. Exemplary case study design ensures that the procedures used are well-documented and can be repeated with the same results over and over again. In the case of the present dissertation, it is crucial that internal validity is high; “…instead of creating high reliability a qualitative study should strive to reach a result with meaning.” (Merriam, 1998).
4 Data analysis

One of the most critical – and undoubtedly one of the most difficult – aspects of a qualitative methodology is to write an interpretive analysis and to assemble and interpret the information that was collected. The present analysis is a synthesis of primary data collected during the interview as well as secondary data collected via academic and business articles and other Internet sources. To make the analysis even sounder, certain strategic tools (Pestel, SWOT, Porter’s five forces) were used.

In the present case, at the end of the interview, it was essential to review the notes. The informational base was extremely fragile because, as time passes, it becomes increasingly difficult to reconstruct information derived from an interview conducted via Skype. This is especially true in regard to the insights or preliminary conclusions that the writer might have drawn while listening to the respondent. For this reason, immediately after the interview had taken place, the writer organized, and interpreted the information provided and searched its association to the main objectives of the dissertation. In some cases, direct quotes were used. Similarly, secondary data was grouped and filtered to focus on specific aspects considered.

This chapter will discuss the motivation of YOOX Group to enter the Chinese market and the factors that enabled the company to enter the specific market with a wholly-owned subsidiary. Therefore, the profile and current positioning of the Group is presented first. Afterwards, a thorough environmental analysis is provided, as well as an evaluation of the Group’s strengths and weaknesses with the aim to identify what the company can leverage and what it needs to be aware of in terms of threats to achieving organisational success within the Chinese market. Certain strategic tools and models that were taught to us during Business Strategy course were employed in order to conduct the particular analysis. The Chapter continues with an examination of the industrial context in the form of suppliers, consumers, competitors, new entrants and substitutes. Next, the competitive landscape is presented. Finally, the expansion strategy in China is examined.
4.1 The YOOX Group’s Profile

The Italy-based YOOX Group is a global Internet retailer (pure play e-tailer) for leading fashion and design brands. Therefore, the reference market is the online retail market. Within this market, the Group operates in the clothing, footwear and fashion accessories segments. The YOOX Group (hereinafter “the Group”) includes, as well as the Parent YOOX S.p.A. (the “Parent”), the companies YOOX Corporation and Y Services, which are subject to US law and which manage sales activities in the US, YOOX Japan, which is subject to Japanese law and which manages sales activities in Japan, and the newly established Mishang Trading (Shanghai) Co. Ltd, which manages sales activities in China.

The Group operates with a unique business model, with two differentiated but synergic business lines, through its two multi-brand virtual boutiques (yoox.com and thecorner.com) and 23 mono-brand online stores for major fashion brands (Appendix 2).

YOOX brand is well-known both in Italy and globally. The awareness of YOOX brand is strategic in attracting, establishing, developing and maintaining long term brand relationships.

A description of its two business lines is provided below (Yoox Annual Report, 2010).

4.1.1 The multi-brand business line

The multi-brand business line (76.4% of consolidated net revenues in 2010) is carried out mostly through yoox.com, a virtual boutique established in 2000. Thanks to direct, well-established relations with designers, producers and authorised dealers (referred as Commercial Partners), yoox.com offers a selection of products at attractive prices, that are hard to find elsewhere such as: an extensive selection of end-of-season clothing and accessories from the world’s most important fashion designers, exclusive capsule collections, eco-friendly fashion, unique design objects, rare vintage collectibles and original art books.
YOOX also launched thecorner.com in 2008, a virtual department store with dedicated “corners” for each brand, providing a collection of in-season men’s and women’s clothing and accessories of niche premium brands with limited distribution. The products sold on thecorner.com carry prices in line with those found in the traditional channel (Yoox Annual Report, 2010).

The merchandise for the multi-brand channel is rather complex, due to the wide range of brands and products. Purchases are negotiated each season and binding minimum volumes or other commitments do not exist. YOOX's suppliers are fashion houses (and their licensors), retailers, producers and design companies. There are around 1,000 suppliers, with very limited concentration. Selling prices can be easily modified through gradual promotions and discounts that enable the Group to optimize sales, margins and therefore inventories. This is a key competitive strength for YOOX, because it can react quickly to demand changes (Cheuvreux, 2011).

4.1.2 The mono-brand business line

The mono-brand business line (launched in 2006) includes the interface design, set-up and management of mono-brand Online Stores for leading fashion brands on an exclusive basis, which offers customers the opportunity for shopping on the web for their in-season collections. The YOOX Group offers its so-called Strategic Partners a total solution, including a global technological and logistics platform, innovative interface design, excellent customer care and international web marketing. The partnership model is mostly of 5-year contracts with Strategic Partners. All Online Stores display the wording “Powered by YOOX Group”, which is considered a guarantee of service quality offered by YOOX.

Pricing policies are determined by the brands themselves and are aligned with the retail price of off-line stores, so they have less flexibility in adjustments. Each brand chooses the range of products offered, prices, marketing and communication strategies and YOOX assists brands with consultancy and web marketing services.

The merchandise for the Monobrand Stores is 100% available on consignment (no risk for the YOOX Group) and unsold items may be returned to each brand at the end of
every season. However, brands have the option to sell to yoox.com the unsold items from their Mono-brand Stores at the end of each season. This aspect of the Mono-brand business allows YOOX to take advantage of a privileged sourcing channel for yoox.com, while avoiding any inventory risk, “which clearly has a positive effect on working capital management, debt and interest expenses”

Mono-brand online clients differ from the Multi-brand clients, as they are typically "brand lovers" who seek the newest collections. Thus, no major cannibalisation risk with the price-product positioning of the Multi-brand channel is observed (Cheuvreux, 2011).

The two business lines share the same technological platform, tools and know-how, thus offering very significant potential for cost synergies across the value chain, especially in marketing, retail and business development. Through the two different channels, YOOX covers a wide range of potential online shoppers, having a different attitude towards products, brand and price, with no risk of cannibalization (Appendix 3). (Yoox Group’s Roadshow presentation, 2011).

4.1.3 Operational Structure

The Group’s operational structure includes its headquarters in Bologna, seven local offices (located in US, Italy, Japan, France, Spain, China, Hong Kong), five logistic hubs (located in Italy, US, Japan, China, Hong Kong), four digital production facilities (in Italy, US, Japan and China); and eight customer care centres. YOOX delivers to over 100 countries worldwide and almost 99% of deliveries are on time (YOOX Group’s Annual Report, 2010).

4.1.4 Financial information

As shown in Picture 1, the Group reported a sales increase of 40.8 percent to 214.3 million euros in 2010. Net profit in 2010 was 9.1 million euros against 4.1 million euros in 2009. YOOX S.p.A. was listed on the stock market in December 2009.
The European market represents 71.1% of the Group’s revenue in 2010 with Euro 152,229 thousand. The first country in terms of revenue is Italy, followed by France, Germany and United Kingdom. Penetration in other European countries is continuing, with excellent prospects, including Russia thanks to the localization strategy implemented in this market in late 2010. The Chinese market has been added at the end of November 2010 through the Mono-brand business line. “Not country related” category includes payments for setting up and maintaining the Online Stores, revenue generated from the sale of media partnership projects, and revenue from web marketing and web design services offered to Strategic Partners (YOOX Group’s Annual Report, 2010).

### 4.1.5 Human Resources

There are 372 people employed in YOOX Group, including 16 managers. Around 93% of YOOX employees are based in the three Italian offices, with 7% based at offices abroad. The working environment is dynamic and competitive, with an average age of only 32. YOOX’s workforce is also characterized by a high percentage of women (56%). In 2009, the turnover rate was 12.8% (YOOX Group’s Annual Report, 2010).
4.2 Motivation to Internationalize

The Group has developed a sound internationalization process over time, expanding its business worldwide. YOOX Group claims that mostly "pull" factors determine the direction of its international growth.

The economic attractiveness of China is the main reason that YOOX Group decided to enter the Chinese market. China represents the world’s second largest luxury market and the world’s youngest market with 80% of consumers under 45 years old (who are also less inclined to save). On the other hand, China possesses the world’s biggest online population (ca. 295M Internet users in 2010) and according to online retail forecasts, the number of online buyers in China is expected to grow substantially by 2015 and almost reach total current US population (McKinsey & Company, 2009). YOOX Group, positioned at the convergence of the aforementioned megatrends, decided to tap into China and be the first mover in the world’s fastest growing market. In addition, comparative advantages of YOOX acted also as "pull" factors. For instance, both e-shops of YOOX Group (yoox.com and thecorner.com) ship to China for many years now, making it easier for YOOX to estimate the potential demand from a localized website.

YOOX does not deny “push” factors, for example spreading of risk and minimization of exposure, as the driving forces behind its internationalization. For example, another motive and a classic “push” factor for entering China was the decision to reduce its dependence on Europe.

YOOX Group uses foreign operations as an integrated marketing tool to increase brand awareness in new markets. YOOX’s marketing budget in China is proportionally high compared to the current operation in the country (Interview with YOOX China Country Manager, 5/09/2011).
4.3 PESTEL Analysis

The PESTEL analysis tool is used to determine how the macro-economic environment might influence the Group’s strategy in China. As YOOX is already operating in the Chinese market— with three Online Flagship Stores at the time being - the writer decided that a detailed PESTEL analysis would be of less relevance here. However, for the interested reader, the analysis is included in Appendix IV. Table 3 shows the main findings of the PESTEL analysis.

| Political factors                  | • Domestic retailers enjoy government support  |
|                                  | • Bureaucracy                                   |
|                                  | • Excess government control                     |
| Economic factors                 | • China: 2nd largest luxury market             |
|                                  | • Rising wages                                  |
|                                  | • High tax rates                                |
| Socio-cultural factors           | • Sophisticated consumers who buy to show       |
|                                  | status or to give gifts                         |
|                                  | • Awareness of mega-brands                      |
|                                  | • Importance of interpersonal relationships     |
|                                  | (guanxi)                                        |
|                                  | • Talent shortage in human resources            |
| Technological factors            | • Undeveloped logistics infrastructure          |
|                                  | • Increasing Internet penetration              |
| Environmental factors            | • Environmentally conscious consumers          |
| Legal factors                    | • Counterfeiting                                |
|                                  | • Inadequate regulations for e-commerce         |

Table 3: PESTEL analysis
4.4 Porter’s five forces of online fashion luxury industry

According to Michael Porter, some industries are more lucrative than others, because an industry’s attractiveness is determined by the dynamics of the competitive structure. To assess the nature of competition in the luxury fashion industry in China, the Five Forces Model by M. Porter is used. Porter explains that there are five forces that determine the industries’ attractiveness and long-run industry profitability, which are: rivalry, entry barriers, threat of substitutes, supplier power, and buyer power.

<table>
<thead>
<tr>
<th>Force</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bargaining power of suppliers</td>
<td>The suppliers (fashion houses and their licensors, retailers, producers, and design companies) are fragmented, a fact that weakens their bargaining power. However, in limited cases, certain specialised products and brands increase switching costs for buyers, so the suppliers have higher power.</td>
</tr>
<tr>
<td>Bargaining power of buyers</td>
<td>All the buyers are individual consumers which significantly weakens buyer power. Furthermore, YOOX offers exclusive collections, which are not easily found at other online boutiques.</td>
</tr>
<tr>
<td>Threat of new entrants</td>
<td>For an online established retailer (like YOOX), a strong brand image generates consumer trust. Moreover, long-term relationships with suppliers and partners build a barrier to new entrants. All these are retaliating factors for newcomers. However, capital requirements are low for potential online business entrants.</td>
</tr>
<tr>
<td>Threat of substitutes</td>
<td>Substitutes for luxury fashion apparel and footwear include buying direct from physical stores, where products can be felt, touched, and seen. Renting luxury products instead of</td>
</tr>
<tr>
<td>High</td>
<td>buying them is also increasing in popularity. Other substitutes include custom-made couture clothing.</td>
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<td>------</td>
<td>--------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Competitive rivalry</td>
<td>The competition in the current apparel market is becoming fierce among both domestic e-retailers and foreign e-retailers.</td>
</tr>
<tr>
<td>High</td>
<td>From the Five Forces analysis, the online fashion luxury industry in China is an attractive industry to invest in with low bargaining powers for both suppliers and buyers. However, attention must be paid especially to differentiation from competitors.</td>
</tr>
</tbody>
</table>

### 4.5 SWOT Analysis

#### Strengths
- Global reach combined with strong local presence (over 100 countries served)
- Flexible business model, based on an advanced technological and logistics platform, capable of managing high volumes across both business lines
- Customized offering for different geographical areas (currencies, languages, customer care centres)
- Differentiated but synergic offering through two complementary business lines (multi-brand and mono-brand channels)
- Important recognition and awareness of the YOOX brand as a leading retail e-player
- Young and well-motivated management team and staff, implementation of excellent HR practices
- Advanced mobile commerce techniques
- Fully automated distribution platform (state-of-the-art automation systems)

#### Weaknesses
- Small size compared to established players in China
- High tax rate
- High level of inventories for the multi-brand channel due to increased expected growth in volumes
Opportunities

- Increased consumer spending in China
- Additional opportunities for synergies between the multi-brand and the mono-brand channels
- Increasing internet penetration, broadband connections’ growth, increasing number of online shopping in China
- Diffusion of web-friendly online payment methods and online security concerns
- Wide number of fashion houses that have not yet launched online stores, can become YOOX’s Strategic Partners in China.

Threats

- Risk of failure to successfully exploit synergies between the two business lines
- Risk of non-renewal of contracts with strategic partners
- Risk of weakening of the relationships with existing partners
- Complexity related to managing international growth and expansion process
- Difficulty in finding, training and retaining professionals with necessary skills in China
- China has no nationwide credit database, so it is difficult to assess consumers’ credit-worthiness
- Underdeveloped infrastructure
- Risks related to intellectual property infringement

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### 4.6 Competitive Landscape

YOOX’s market positioning at the crossroads of e-commerce and fashion, its product range (off-season and in-season branded products) and unique business model (with the Multi-brand and Mono-brand business lines) make it very difficult to recognise the core competitors of YOOX.

For this reason, three categories of possible competitors have been identified:
### a) E-commerce companies

<table>
<thead>
<tr>
<th>Company</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>ASOS (<a href="http://www.asos.com">www.asos.com</a>)</strong> is an online fashion and beauty store operating mainly in UK. Unlike YOOX, it does not operate online mono-brand stores and it does not have close relationships with brand owners. Half of its sales are generated by its own ASOS brand. Regarding revenues and profitability, it is rather similar to YOOX. According to their recent annual report, China is on the company’s radar and it plans to “invade” China with the help of a Chinese business partner. (ASOS plc. Annual Report 2011)</td>
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<tr>
<td><strong>Within the fashion sector, Amazon “operates owned fashion online stores as YOOX does in its multi-brand business line, and online stores on behalf of third parties as YOOX does in its mono-brand business line” (Mediobanca Securities, 2009). The Amazon Group has highest revenues but lower profitability than YOOX.</strong></td>
<td></td>
</tr>
<tr>
<td>Taobao, which is operated by Alibaba Group, has a phenomenal reach throughout China and is a key player in the Chinese e-commerce industry. Its B2C platform, <strong>Taobao Mall (<a href="http://www.tmall.com">www.tmall.com</a>)</strong>, offers branded goods. Taobao also launched a “designer-to-consumer” (D2C) site for limited-edition or custom-made designer clothes — a sign that Taobao may move its TMall more upmarket.</td>
<td></td>
</tr>
<tr>
<td>Wooha (<a href="http://www.wooha.com">www.wooha.com</a>) was founded in 2006 and by 2010 it had 2.3 million registered users. The Beijing-based e-tailer targets exclusively high-end female consumers over the age of 26 and has set the objective of focusing more on premium brands. Wooha gives prominence to brand awareness and education through its “Trends” section. It provides history in both the house and designer, which accounts for a lot of value to...</td>
<td></td>
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<tr>
<td><strong>Chinese customers. Nowadays, LVMH Group holds conversations with WOOHA about the possibility of future cooperation.</strong></td>
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</tr>
<tr>
<td><strong>At the beginning of 2011, the leading China-based Internet technology company, NetEase, launched its own luxury e-commerce site, NetEase Premier. The business model is similar to the so-called flash sale websites (members of the site are offered luxury goods at a high discount during a short time — usually 24 to 72 hours). Premier also provides certificates of authenticity, and is “heavily promoting its comprehensive customer service” (China Fashion Trends, 2011).</strong></td>
<td></td>
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<tr>
<td><strong>Just in August 2011, Sina, the largest Chinese-language news portal, launched its own e-commerce luxury platform, Sina Luxury. Sina is one of the country’s most popular news portals. Despite its reputation, the website still does not have menswear.</strong></td>
<td></td>
</tr>
<tr>
<td><strong>The VIP Store is a flash-sale site. Its future objective is to add more second-tier brands to its portfolio and broaden its brand portfolio.</strong></td>
<td></td>
</tr>
<tr>
<td><strong>My Mingpai is a dual online fashion/luxury magazine and shopping mall. The site features daily Shanghai street style looks. MyMingpai also offers advice on what to wear on occasions (China Fashion Trends, 2011).</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Secoo was founded in 2009 and sells second-hand luxury goods through its website, offline “clubs”, and in its 10 physical partner stores. Secoo has partnered with “Wardrobe of Love” to form a new philanthropic program to help underprivileged children (China Fashion Trends, 2011).</strong></td>
<td></td>
</tr>
</tbody>
</table>
b) E-commerce service providers

| GSI Commerce, an eBay Inc. company, provides e-commerce, multi-channel retailing and interactive marketing services to large businesses. Its clientele in Apparel, Accessories and Footwear includes companies like Nautica, DKNY, Timberland and others. |

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c) Luxury goods companies

| PPR² holds many Groups that have developed retail operations in the traditional channels and have the same offering as YOOX in terms of products and same price positioning (in the mono-brand channels and thecorner.com for the multi-brand business unit). In some cases, they are either Strategic Partners or Commercial Partners of YOOX Group itself. Tod’s presence in China is quite important but their strategy is to keep their distribution small and exclusive. Their website is also available in Chinese language. |

| Luis Vuitton opened in China in 1992 and has long moved operations there. Its website is available in Chinese language. According to Bain & Company (2010), Chinese consumers’ taste for luxury brands have made Louis Vuitton and Gucci, the most popular brands in China, ranking in first and third position respectively. |

| Burberry, having a strong presence in China, buyed out last year its franchisees in mainland China, to have more control over the |

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² PPR is a French multinational holding company specializing in retail shops and luxury brands. As of 2011 PPR’s main subsidiary is the Gucci Group (Gucci, Bottega Veneta, Yves Saint Laurent, Alexander McQueen, Balenciaga, Boucheron, Girard-Perregaux, Sergio Rossi, Stella McCartney) (http://en.wikipedia.org/wiki/PPR_(company)
merchandise and how it is marketed. Burberry and some brands within LVMH Group have also started online retail operations, although this does not represent a significant part of turnover for all of them (Mediobanca Securities, 2009).

Considering the competitors mentioned above the following conclusions emerge:

a. Within the e-commerce retailers, ASOS is considered as the most comparable company in terms of size and earnings, but its growth prospects are more limited than YOOX's, given that it is local rather than global as YOOX is, and it generates a substantial part of its business under its own label. Furthermore, YOOX possesses specific expertise in online retail and, particularly, in marketing and logistics. Regarding the local e-tailers in China, it is evident that these players are numerous and may have a deeper understanding of the local business environment. According to the opinion of YOOX's China Country Manager, it is believed that “Taobao Mall is the stronger local competitor, followed by Wooha which shows dynamism and Netease Premier which enjoys large awareness”.

b. GSI’s operations are similar to those that YOOX carries out for its Strategic Partners in the mono-brand business, which, in the case of the Italian Group, benefits from synergies resulting from its common platform with the multi-brand businesses. The mono-brand business is synergetic with the multi-brand business and is positively affected by the strong relationship that YOOX has built with its partners for the off-season items via yoox.com. Within the YOOX Group, the mono-brand and multi-brand businesses are two sides of the same coin, which feed each other. This is unique in the e-tail industry, as the Group combines expertise in managing a forefront platform of ecommerce services, deep knowledge of the fashion industry and retail dynamics.

c. YOOX and the aforementioned luxury goods companies have a common consumer base and common macro factors driving the demand for fashion luxury goods. However, these luxury companies have substantially lower growth prospects in terms of both revenues and earnings, which have been affected by
weak demand over recent years. They also still lack innovation in terms of distribution channels, unlike YOOX. Finally, YOOX benefits from a shift from the traditional to the online channel.

To highlight the results of the competitors’ analysis, it is obvious that China already has several established e-retailers. Even though YOOX is a well-funded and experienced international retailer, it still needs a fast, competitive approach to succeed in China.

4.7 YOOX Group’s strategic expansion in China

China represented for YOOX Group one of the most important pillars for completing its offering to the fashion industry. The Group wanted to seize the opportunity to expand its geographical reach, by entering the emerging market of China. Management of the Group expects China to be the third country in terms of revenues for the Group in 2015. YOOX Group entered the Chinese market in 2010. On November 2010, the Emporio Armani Online Flagship Store, emporioarmani.cn was launched, the first to be “Powered by YOOX Group” in China (which was followed, on March 2011, by the launch of the Marni Online Flagship Store and the launch of the Bally Online Store on May 2011).

Although mass-market and fast-fashion brands like the Gap and Wal-Mart have recently created e-commerce sites for China, Armani’s online venture is the first developed by such a high-profile fashion brand, so as to provide the Group with an important first-mover advantage. Other domains will follow in the near future to enrich the Mono-brand line. The Group has landed in China as a first mover with its own Mono-brand business line, consolidating its position as a retail Internet global partner for the major fashion brands. The Mono-brand business line will subsequently be joined by the Multi-brand line, initially through the launch of thecorner.com by the end of September 2011, and later, to complete the offering, with the launch of yoox.com in 2012.

According to the interviewee, the Group’s mission for the strategic expansion plan in China is “to be the official Internet retailing partner in China for leading fashion brands”, which is accompanied by the objective of “supporting the Group’s long-term growth”. As
far as positioning is concerned the Group “will start with in-season offerings, excellent customer service and superior shopping experience”.

The Group plans to start initially with a full price strategy (Mono-brand Stores), thanks to the extension of some of its existing partnerships, and then introduce the Multi-brand web-site thecorner.com in late September 2011 (starting from the Fall/Winter collection) and yoox.com in 2012. It is observed that the Group will follow a gradual and cautious approach and will implement a three-phased plan in a timeline of three years;

1. The first phase includes extension of existing partnerships and development of new agreements with leading fashion houses by powering their Online Flagship Stores in China. The Armani, Marni and Bally Online Flagship Stores, fully operational in Chinese language are included in this phase.

2. The second phase includes the launch of the online multi-brand boutique thecorner.com. This will also provide mono-brand partners (Strategic Partners) with an additional shop-window to showcase and sell the same products available in their Online Flagship Stores. In addition, it will host selections of well-known designers appealing to Chinese customers.

3. The third phase includes the launch of the megalith flagship yoox.com in China in 2012. This will help Strategic Partners minimize risk of local end-of-season inventory through a reliable channel that does not dilute their brands’ image.

The YOOX Group strategy in China consists of extending some of the current partnerships with prestigious fashion and luxury brands, adopting a full price strategy and positioning itself at the top end of the market.

Having set the goal of providing its customers with the highest possible level of service, comparable with what is on offer in all countries in which they operate, YOOX will be adopting the same winning model in China that is already established in other markets; all strategic activities will be carried out directly; for remaining activities YOOX will rely on the support of prestigious partners who already have a presence in China. A Chinese subsidiary (Mishang Trading Co. Ltd) wholly owned by YOOX S.p.A. has therefore been set up. It operates through a local office in Shanghai where a team is involved in buying and merchandising, content management, communication and retail marketing, customer service, web graphics and technology and there is a logistics centre with digital production studios for cataloguing and photographic services. This independent subsidiary in China
has the necessary structure to exploit opportunities in this country. This market must be approached with a good understanding of its unique characteristics. A local subsidiary is the best way to approach this market, to meet the specific needs of Chinese clients.

The opening of the Shanghai Company required special attention in the creation and search for new employees and for this reason a Human Resources Manager was installed on the spot in order to deal more appropriately with the requirements and specific needs of the local market.

The online retailer, does not plan to enter the emerging markets of India and Brazil in the near future, as it already has enough opportunity to grow in China. As the China Country Manager said during the interview: "Everybody claims to be global, but we claim to be local. If you want to compete on the Chinese market you need to compete with the local players and you need to be local and that's our strategy."

The Group has strategically integrated recently e-commerce solutions in the Chinese market, adapting the technical features of the localised e-commerce to meet the requirements of the country. The solution put in place makes it possible to integrate the local warehouse, provide web services directly from servers located in China and adapt the payment processes and payment services to meet local requirements.

According to the Group's website information, to guarantee the best buying experience and satisfy the sophisticated Chinese customers, the best "sur mesure" e-commerce solutions will be implemented first by thecorner.com.cn and then by yoox.com.cn;

- localised Chinese websites,
- a size conversion system,
- currency in Yuan,
- the possibility of secure paying in Yuan by C.O.D. or other local payment systems,
- customer service in Chinese by email and by phone,
- fast and reliable delivery in 400 towns courtesy of FedEx and in the rest of China through Express Mail Service,
- luxury packaging,
- a 24-hour call centre and instant-messaging fashion advisers who can answer questions about fabric, quality, style and sizing,
• free returns (with an exclusive additional service: the courier waits whilst the
customer can try on the product),

• anti-fraud microchip seal, created using the most recent RFID monitoring
technology to guarantee the authenticity of every product,

The latter two points deserve further analysis and attention. First, concerning the
exclusive additional service, China Country Manager explained that “the YOOX Group
has partnered with FedEx to offer Chinese shoppers a customised service which will see
delivery staff waiting by the door while customers inspect their purchase, try on for size
and decide whether the item deserves to be kept or sent back”. The Parent company
designed this service to engage with China’s top-tier shoppers. The service will be offered
from late September 2011, to coincide with the launch of thecorner.com.cn. If the service
proves successful in China, the Company plans to introduce it to other markets. This
customised delivery option offers customers a sense of exclusivity and a highly
personalised approach, powerful e-commerce trends, that is sure to pay off for the YOOX
Group.

Secondly, to ease concerns about counterfeit products - a big issue in China – YOOX
will attach a radio-frequency-identification (RFID) tag to to each product in order to track
products from warehouse to doorstep, thus making sure nothing that nothing is replaced
with fake products. Chinese consumers will know that if a product doesn't come with the
RFID tag, which looks like an extra price tag, then it will not be an original.

Products ordered on thecorner.com.cn in China will also come with the shopping bag
of the brand and in a reusable, extra-durable gift box made of hard cardboard with a
magnetic clasp, as “Chinese buyers like to show off their purchases”, according to China
Country Manager.

Summarizing, the YOOX Group has started to implement a gradual, three-step
approach to enter China. This will be supported and accompanied by a wholly-owned
subsidiary which has been established for this purpose. The entry strategy is characterized
by certain adaptation elements to tailor the specific needs of the foreign market.

The obstacles for establishing direct operations in China were diverse for the YOOX
Group. First, there is the vast administrative environment shaped by bureaucracy.
Bureaucracy may be tackled at first hand by relationship building, which is central in the
Chinese culture. However, this should not exceed reasonable and moderate limits, so as
not to be considered unethical and illegal. Second, counterfeit products is still a big problem in the country, leading the Group to consider offering RFID solutions to overcome this. Third, the logistics infrastructure is underdeveloped, which necessitated the investment for a fully localized state-of-the-art platform and distribution center. Finally, the Group faced the problem of recruiting educated staff, suitable for its quality standards. Therefore, the Group spends a lot of time and money on training and bringing staff up to desired levels.

If successful, YOOX's move into China will raise revenues and minimize its risk exposure to Europe. The launch of thecorner.com.cn, which hosts fewer brands, will allow YOOX to test its local operations prior to the launch of the flagship yoox.com.cn. Nevertheless, YOOX will face intense competition in the market.
5 Discussion of Findings and Recommendations

This Chapter discusses the most basic research findings of the previous chapter and presents recommendations for the future.

YOOX cannot allow to be perceived as a discounter, so it positions itself at the top end of the market. It is the author’s belief that this strategy will be totally successful given that the Group will offer high service quality and an unforgettable shopping experience. In this way it can attract more Chinese customers and inspire brand loyalty. Therefore, YOOX should continue to invest in its technological platform, enhance e-commerce, mobile and tablet applications for both Multi-brand and Mono-brand sites, further personalize and innovate the user experience, and introduce new ways to present, pay and deliver products.

The Chinese online market is currently dominated by a single player, Taobao. According to a Financial Times article by Sanderson and Hille, Taobao prepares an aggressive move. The company plans to roll out a massive logistics operation to improve services for consumers, and to reposition its B2C Taobao Mall at the top end of the market (Sanderson and Hille, 2010). For the Group, this represents a major challenge and it is the writer’s view that it must act extremely quickly and capture a substantial share of the market in the first three months of the operation of thecorner.com.cn. In other words, it is imperative to strengthen its position in China until the end of 2011, when the flagship theyoox.com.cn will also be launched.

As the interview revealed, the online retailer does not plan to enter the emerging markets of India and Brazil in the near future, as it already has enough opportunity to grow in China. This is deemed by the writer as a wise step, for one more reason. Since September 2010, the Group has started operations in Russia and adopted a localization strategy to meet the specific requirements of that market. It would be risky in terms of capital investment, as well as managerial complexity, to operate in more emerging markets at this time. However, even the expansion in China needs special caution. The YOOX Group plans to roll out three to four mono-brand stores in China annually and expand its multibrand offerings via the launch of the corner.com.cn and yoox.com.cn.
Such an aggressive roll-out hides potential execution risks, which may hinder sales and profits growth.

The YOOX Group has attained a first mover advantage in the Chinese online luxury market. There are three factors that the writer perceives as critical for sustaining this advantage:

1. Continue to *develop state-of-the-art technology platforms*, which provide a competitive advantage and significant barriers to entry.

2. *Effective order fulfillment and product distribution.* Regarding order fulfillment, it is vital to fully exploit synergies and economies of scale created by YOOX’s unique business model, so as to be able to utilise common e-commerce and fulfillment systems across the multi-brand and mono-brand businesses. By the same token, logistically it makes sense for YOOX to be based in China, so inventory management and shipping operations can be performed impeccably. To this end, it is crucial for the Group to invest on -and upgrade in the future if necessary- its network platform and logistics center in Shanghai.

3. *Cement existing relationships with Commercial and Strategic Partners and develop new ones, including Chinese partners.* In this case, the aim is to sustain the trust built in these relationships and search for strategic partnerships with non-competitive brands that target similar customers.

The interview with China Country Manager revealed that although the appeal of an online retailer might theoretically be its global nature, in fact, to succeed, online retailers need to act local. For this reason, the Group has established a Chinese-registered subsidiary in Shanghai to allow for greater autonomy and local decision-making. The YOOX Group will follow a comprehensive localized strategy in the core market of China with the following most important features:

- Chinese websites with localized payment system, Chinese tags in clothing, and Chinese sizing
- Attachment of an anti-fraud chip on every item sold, in order to avoid returns of counterfeit items
- Offering of an unforgettable shopping experience via the new VIP service designed in collaboration with FedEx. The delivery man will wait as consumers try
on their purchases and decide whether to keep them. This service clearly saves time and money for the customer in relation to return and refund processes.

Apart from the above features highlighted during the interview, the writer firmly believes that another three aspects are of great importance:

a. The YOOX Group will have to place initially a greater weight on men’s wear than women’s wear, as a larger percentage of Chinese e-luxury consumers are men. However, it is expected that young women will become the major clients of luxury goods in the future. For this reason, YOOX’s marketing executives must be ready to follow purchasing patterns when such a shift occurs.

b. It is also advisable to include more mega-brands (such as Marc Jacobs, Salvatore Ferragamo etc) rather than niche brands (such as Philip Lim, Martin Margiela etc), because Chinese consumers prefer big brands with high recognition.

c. It is recommended that the Group assembles a strategy to highlight the heritage of the brands offered in China. A brand’s rich heritage is a selling point for luxury consumers and this concept is also apparent among Chinese luxury consumers, who want to know the story and history of a brand. It goes without saying that in order to achieve this, the Group will have to work closely with Commercial and Strategic Partners in order to illustrate each brand’s company history and product craftsmanship effectively. Recognizing the need to highlight heritage, museum exhibits can be organized to showcase designs from years ago, including some timeless ones that remain ‘in-fashion” even today. A second solution may be to bring artisans to China to showcase their craftsmanship. Another possibility could also be to identify influential bloggers and educate them about the heritage of the brands.

Nevertheless, even if most Chinese consumers like brands with international heritage, all of them would appreciate products, labels or sub-brands that reflect China’s heritage. The YOOX Group can accommodate this desire by collaborating with Chinese designers to offer a series of exclusive China-tailored collections.
6 Theoretical and Managerial Implications

The discussion of the results of the present case study leads to many conclusions, both theoretical and practical in nature, which can help guide both future research and retail internationalization strategy.

6.1 Theoretical Implications

At the theoretical level, the current study adds to knowledge with regard to internationalization strategies and particularly pure play e-tailers’ entry strategy in China. Concerning the global-local dilemma and the extent to which services may be standardised across national boundaries or need to be adapted to meet the requirements of specific national markets, this study clearly highlights that YOOX Group’s strategy in China must be locally responsive. In this respect, Evans’ et. al theory (2008), that almost every retail format requires at least some adaptation to tailor the specific needs of the foreign market, is affirmed. According to Hollander (1970) and Lualajainen (1992), pull (proactive) factors were expected to be the main reason for luxury fashion retailers to enter new markets, which is verified by the case of YOOX. It was expected that luxury fashion retailers following a global strategy would tend to pursue establishing WOS to retain full control over their operations. While the YOOX Group fulfills this expectation, other retailers identified in the literature such as Coca-Cola, despite following a global strategy, chose initially low risk contractual agreements in China. A possible explanation for this inconsistency may be the different industry or the different reference time period. What is more, YOOX is an online retailer and as such it can easier enter China with a high-risk and high-return entry mode. Thus, the study by Li (2002) is verified by the present case study.
6.2 Managerial Implications

It is highly important for international businesses to recognize the importance of the compatibility of their unique value-proposition and strategic fit with the local market conditions. YOOX Group originally had a very clear definition of its strategic positioning in the Chinese market. The YOOX Group strategy in China consists of extending some of the current partnerships with prestigious fashion and luxury brands to this market, adopting a full price strategy and positioning itself at the top end of the market. Thus, its strategic positioning had a fit with the Chinese demand market conditions.

When an international business identifies a foreign market with a high potential for growth and profit, the firm must consider the scale of entry and strategic commitments. A large scale market entry involves the commitment of significant resources and enables the firm to capture first-mover advantages that are associated with demand preemption, economies of scale, and switching costs. YOOX Group initially entered the Chinese market on November 2010, with the Emporio Armani Online Flagship Store, followed, on March 2011, by the launch of the Marni Online Flagship Store and the launch of the Bally Online Store two months later. It will gradually move to the launch of thecorner.com by the end of September 2011, and later with the launch of yoox.com in 2012. As it is observed, YOOX Group obtains a rapid and large scale entry, even though this is carefully planned in different consecutive stages. YOOX will be adopting the same winning model in China that is already established in other markets; all strategic activities will be carried out directly from the Chinese subsidiary wholly owned by YOOX S.p.A. and for the remaining activities they will rely on the support of prestigious partners who already have a presence in China.

Prior to the market entry, YOOX Group had defined its “strategic commitments” for the Chinese market. The Company sees China, becoming one of its top three markets by 2015. To this end, the Group decided to focus on China with approximately 3-4 monobrand launches per year (either as extensions of existing partnerships or as new partnerships). In other words, China is a strategically important market for the Group and it is worthwhile to allocate significant capital resources to capture customers and partners
there. For this reason, YOOX Group is prepared to develop an effective localization strategy, since it has a clear projection of how much it is willing to invest and grow in this market. The online retailer does not plan to enter the emerging markets of India and Brazil in the near future, as it already has enough opportunity to grow in China.

It is evident that the case study of YOOX Group provides important managerial lessons and insightful practical guidance. Managers can gain information on how they can allocate their available resources and plan an entry into the Chinese online luxury fashion market. Moreover, they are also informed about potential challenges and critical success factors in conducting Chinese e-commerce. This knowledge has a favorable impact on both the effectiveness and efficiency of operations.
7 Limitations and future research

There are a few limitations of this study that warrant comment. Firstly, since the findings are based on a single case study, no generalizations about the internationalization of luxury fashion e-tailers can be made without further studies. Another concern relates to whether the strategy recommendations for pure-play e-tailers fit to “bricks and mortar” luxury fashion retailers. Also, any generalizability beyond the Chinese mainland should be undertaken with caution. In addition, the study considered only certain factors that influenced YOOX Group’s strategic expansion mode. There are other factors that might equally influence such decisions that should be examined in future.

The second set of limitations is associated with the research method. This study has employed the qualitative methodology approach. A multi-method approach incorporating both quantitative and qualitative perspectives could help accomplish both generalizability and rich implications of research findings. In this study, the skype interview was conducted in English. Given that the China’s Country Manager primary language is not English, some miscommunications due to language differences and interpretations of questions may have occurred. In addition, the single key informant was an executive from YOOX Group, and this can exaggerate positive perceptions and opinions towards the Group’s performance in China. Such concerns with mono-method bias could be greatly reduced if data were gathered independently from numerous different respondents/executives in the Group or even additionally from an executive of a competitor company. Lastly, as the Chinese market is a fast-changing environment, the recommendations and conclusions of this study may need to be altered or complemented in future time to fit market conditions.

The writer believes that this study provides a useful start in thinking about entry modes, strategy implementation and localization of luxury fashion e-tailers in China and also provides a methodological platform for selective replication and extension in other
contexts. However, the findings stressed in this paper need to be investigated in greater depth. For further research it would be interesting to investigate the market entry of other pure play luxury fashion e-tailers. It would be very interesting to study luxury fashion retailers that choose another form of market entry than a wholly owned subsidiary. In addition, future research could focus on various factors that influence a luxury fashion retailer’s strategic expansion mode in China, other than those related to YOOX Group. Finally, investigating the successful establishment of luxury fashion online retailers in other emerging markets (mainly BRICs) would provide an insight into any national or cultural differences in the internationalization of luxury.
8 Concluding Remarks

This dissertation was based on a single case study of a luxury fashion e-tailer that entered China by means of a wholly owned subsidiary. The main objective of this paper was to examine the entry mode of the YOOX Group in China and to discuss what would be a viable expansion strategy. The adopted case study approach provided interesting insights into the internationalization strategies of luxury fashion retailers.

Summarizing the findings of the research, there is evidence and belief that China is a fantastic growth opportunity for the YOOX Group in the medium and long term: a growing luxury demand; broadband penetration in the country is increasing; luxury consumer brands are not easily displaced by domestic competition; and Chinese consumers, in particular, are very brand conscious. However, YOOX Group’s expansion in China requires understanding and respecting the cultural differences by building connections and integrating with local culture. The Chinese market is promising but also entails the necessity to manage complexity to a much greater degree than before, to respond to local social concerns, and to sell a sense of tradition.

YOOX’s smart gradual approach, to fully enter China by a three-phased plan in a timeline of three years, will in the writer’s view be successful and the Group’s target that China will become one of their top three markets within four years could be a conservative one. YOOX has set up in 2010 an independent subsidiary in China and it has the necessary structure to exploit opportunities in this country. It also seems to have found the appropriate balance between companywide consistency and local customization. In order to sustain its first-mover advantage, YOOX has to continue to invest in R&D to retain its technical edge and customer service profile, besides the necessity to move quickly and capture a substantial market share in China until the end of 2011, when the flagship theyoox.com.cn will launch.
List of references

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Appendix
Appendix I: Interview Guide – YOOX, China Country Manager

1. Briefly describe the factors that motivate YOOX to expand into international markets?
2. Do you think saturated markets in Europe are a reason for YOOX’s expansion in China?
3. How attractive is the Chinese market for luxury fashion companies and especially for YOOX?
4. At what level in the company are strategic decisions about internationalization taken?
5. What were the greatest obstacles when entering the Chinese market? Did you experience any difficulties with regard to bureaucracy, human resources, counterfeit and logistics?
6. Do you think culture was an obstacle for YOOX when the company entered China?
7. What entry mode did YOOX select to enter China? Why?
8. Please name the main competitors of YOOX in China.
9. What would be a viable expansion strategy for YOOX in China?
10. How should YOOX sustain its first-mover advantage in China and what pricing strategy and positioning should develop?
11. Which operations are localized in China?
12. What is the role of strengthening current partnerships and/or developing new ones in China? Please name a few.
13. Is it crucial (and to what extent) for YOOX to develop its technology and logistics platforms in China?
14. Do you think the entry of YOOX in China was a success?
15. What are the challenges and risks ahead in relation to YOOX’s entry and establishment in China?

Thank you very much for your time and your answers.
Appendix II: YOOX Group’s business model

Multi-Brand: building long-standing relationships with Commercial Partners

YOOX.COM
- Broad offering of off-season premium apparel and accessories at attractive prices, exclusive and special collections, vintage, home & design products
- Launched in 2000

Mono-Brand: leveraging the know-how together with Strategic Partners

OnlineSTORES
- Exclusive official flagship Online Stores of leading fashion brands
- In-season premium apparel and accessories
- Partnership model: mostly 5-year contracts

2006
- Marni (.com)
- Diesel (.com)
- Company (.com)
- Valentino (.com)
- Emilio Pucci (.com)

2007
- Emporio Armani (.com)
- Zegna (.com)
- Missoni (.com)

2008
- Napa (P) (.com)
- Alberta Ferretti (.com)
- ZEUS (com)
- Missoni Martin Margiela (.com)
- Emanuel Ungaro (.com)

2009
- Moschino (.com)
- Bally (.com)
- D&G (.com)
- Jil Sander (.com)
- Roberto Cavalli (.com)

2010
- Coccinelle (.com)
- Napa (P) (.com)
- Napa (P) (.com)
- Y3 (.com)
- Bikkembergs (.com)

2011
- Brunello Cucinelli (.com)
- Moncler (.com)

Opening soon

R. THECORNER.COM
- In-season premium apparel and accessories from selected brands
- “Shop-in-shop” model
- Launched in 2008

Appendix III: Strategic coverage of the online fashion market

Appendix IV: PESTEL Analysis

Political factors

The Chinese retail and distribution sector were the last ones to be deregulated in mid 1990s, which resulted in domination of domestic retailers in many geographical areas. Also, domestic retailers enjoyed frequently government support. Foreign investors are further discouraged by subsidised competition, restricted access, conflicting regulations, a lack of protection for intellectual property and. Although liberalisation has increased, the government retains important control over areas directly related to the retail sector (e.g. advertising rates) (The Economist, 2009).

Economic factors

The general economic environment for investment in China is positive and optimistic (Bain & Company, 2010). In the fashion retail market, the inflow of foreign capital into Mainland China is a rather recent phenomenon, but, nevertheless, a growing one. Rising wages and the growing disposable income have encouraged middle-income Chinese to purchase goods that were previously out-of-reach. According to “China luxury market study 2010” by Bain & Company, China recently became the world’s second largest market for luxury goods with an annual increase of more than 30% in 2010, even surpassing Japan. Estimates for the years to follow predict that China will become the largest luxury market in the world.

Nevertheless, the prices of luxury goods in China are typically higher than overseas, largely due to Chinese taxes. The tax on luxury goods in Mainland China is high, namely a 17.5% value-added tax, a 10% consumption tax and an average 24% luxury tax on high-end goods (KPMG, 2007).

Socio-cultural factors

The Chinese urban middle class has emerged in an increasingly sophisticated consumer base demanding higher quality, variety and innovation from retailers. Most
Chinese buy luxury products to demonstrate their status and success. In this respect, China offers a huge potential as a fashion luxury market, given its populations and the younger generation’s desire for designer goods. Chinese consumers enjoy displaying their wealth and success and are not just spending on themselves but also purchasing gifts for friends and family. However, brand awareness is evolving slowly, since most spenders are often only aware of the most popular luxury labels.

“Mall culture” is increasing rapidly in China and shopping is adopted mainly as a pleasure activity, while the acceptance of Western goods is impressive. Undoubtedly, there has been a growth in demand for foreign-branded or imported goods.

As far as cultural barriers are concerned, when Western companies enter the Chinese market, they tend to focus on the language barriers and bureaucracy. But to be successful, a foreign operator must understand China’s long history and culture. Overcoming cultural obstacles, however, can be a major challenge. For example, Western companies want to close a deal very quickly, while Chinese prefer to negotiate longer. Furthermore, the way of doing business in China is relationship-driven. As Luo explains “interpersonal relationships (guanxi) is one of the major dynamics of Chinese society”. Broadly, guanxi means “interpersonal linkages with the implication of continued exchange of favors” (Luo Yadong, 2011).

Developing human resources in China and staffing a local management team are also significant challenges. The talent shortage, especially for luxury brands, is very serious (Wild, 2005).

### Technological factors

To a degree, the development of the information industry in China appears to be on pace with the rest of the world. Electronic commerce has risen during the last decade, yet it faces a number of practical and regulatory challenges. Regarding mobile commerce, although it has been widely introduced in China, industry analysts believe its development
Appendix IV: PESTEL Analysis

may hit a bottleneck because the Web environment is not as good as in developed countries and the use of smartphones is not as widespread.

Moving on to another important component of online shopping, the logistics industry in China offers poor support for fulfilment of online shopping transactions. According to Li & Fung Research Centre (2011), the existing logistics infrastructure in China is underdeveloped and there is huge room for improvement, although China is the first manufacturing country in the world. Service failures including order fulfilment delay and product damage happen frequently. Thus, logistics remains the bottleneck of online retail development. The problem is less apparent in cities like Shanghai and Beijing, but distribution to Tier 2 and Tier 3 cities remains largely inefficient and unpredictable. Moreover, the current logistics capacity cannot handle the boom in e-commerce industry and cannot keep up with the growth that is witnessed in online shopping. To this end, global players build their own infrastructure network. For example, Joyo Amazon, the Chinese subsidiary of US-based online retailer Amazon.com Inc, has started to build its own logistics network. Another example, Taobao, the largest online retailer in China, launched its online logistics platform named Wuliubao in June 2010 to aggregate demand of logistics-related services.

Environmental factors

Chinese consumers tend to ponder on environmental issues when making a purchase. According to Li (2007), the convergence of environmental pressures and rising incomes is resulting in a rapid ascendance of LOHAS (Lifestyle of Health and Sustainability) in China. 17% of consumers in China’s top five cities - more than 60 million people - describe themselves as LOHAS-focused. China’s LOHAS consumers are not price sensitive – nine out of ten consumers would be willing to pay 20% more on average for sustainable products, and are looking for increased product choices and availability.
Appendix IV: PESTEL Analysis

Legal factors

Concerning the legal environment, regulations governing online transactions in China are still inadequate. Companies are required to get several levels of authorization and support from local government to establish and operate online ventures.

Secondly, counterfeiting is still a big problem in the fashion luxury industry. According to the U.S. Embassy in Beijing (2005), the piracy rate in China remains one of the highest in the world and, on average, 20% of consumer products are counterfeit. However, China’s entrance in the WTO has improved the protection of intellectual property rights, but counterfeit operations in China are still apparent, secretive and geographically dispersed. It is clear that counterfeit products undermine the luxury brands’ value. On the other hand, others believe that the availability of counterfeits help to make the genuine products more sought-after and desirable, as well as increasing brand awareness of luxury names (Yeh, 2006). The Chinese government has made progress in establishing an effective law system regarding IPR protection, yet there is plenty room for improvement in terms of enforcement and penalty.