McKinsey & Company

Digital transformation: Now or never

Presentation for Círculo Fortuny

February 2021

COVID-19 has led to a true disruption of the global high end market...

The luxury industry is facing its worst year in modern history

March 19, 2020

The luxury sector is bracing itself for its worst year in modern history, analysts warn

Global Luxury Brands Are Hard Hit By Coronavirus Fallout

"Virus impact on fashion and luxury to be 'worse than recession'"

More than 40 percent of global luxury-goods production happens in Italy—and all the Italian factories, including small, family-based *façonniers*, have temporarily shut down.

Covid: Museums and galleries 'fighting for survival', Art Fund says

Restaurants are converting their spaces into retail stores to ride out the coronavirus pandemic

For Luxury, an Acceleration of the Inevitable

Luxury brands gear up to deal with massive inventory problem

Coronavirus Threatens To Wipe Out 5 Years Of Gains In The Global Luxury Market

The coronavirus epidemic could wipe out $43 billion of luxury sales in 2020

Shuttered Stores, Fewer Tourists: Luxury Feels Coronavirus Effects

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... accelerating the three big shifts that had emerged to disrupt the market prior to COVID-19

Consumers

- Digital has redefined customer expectations
- Consumer behavior is changing
- New consumer touchpoints

Market

- Network effect of platforms
- Increasing importance of ecosystems and platforms
- New competitors are capturing share
- Asymmetric investor expectations
- Accelerating pace of digital innovations

Technology

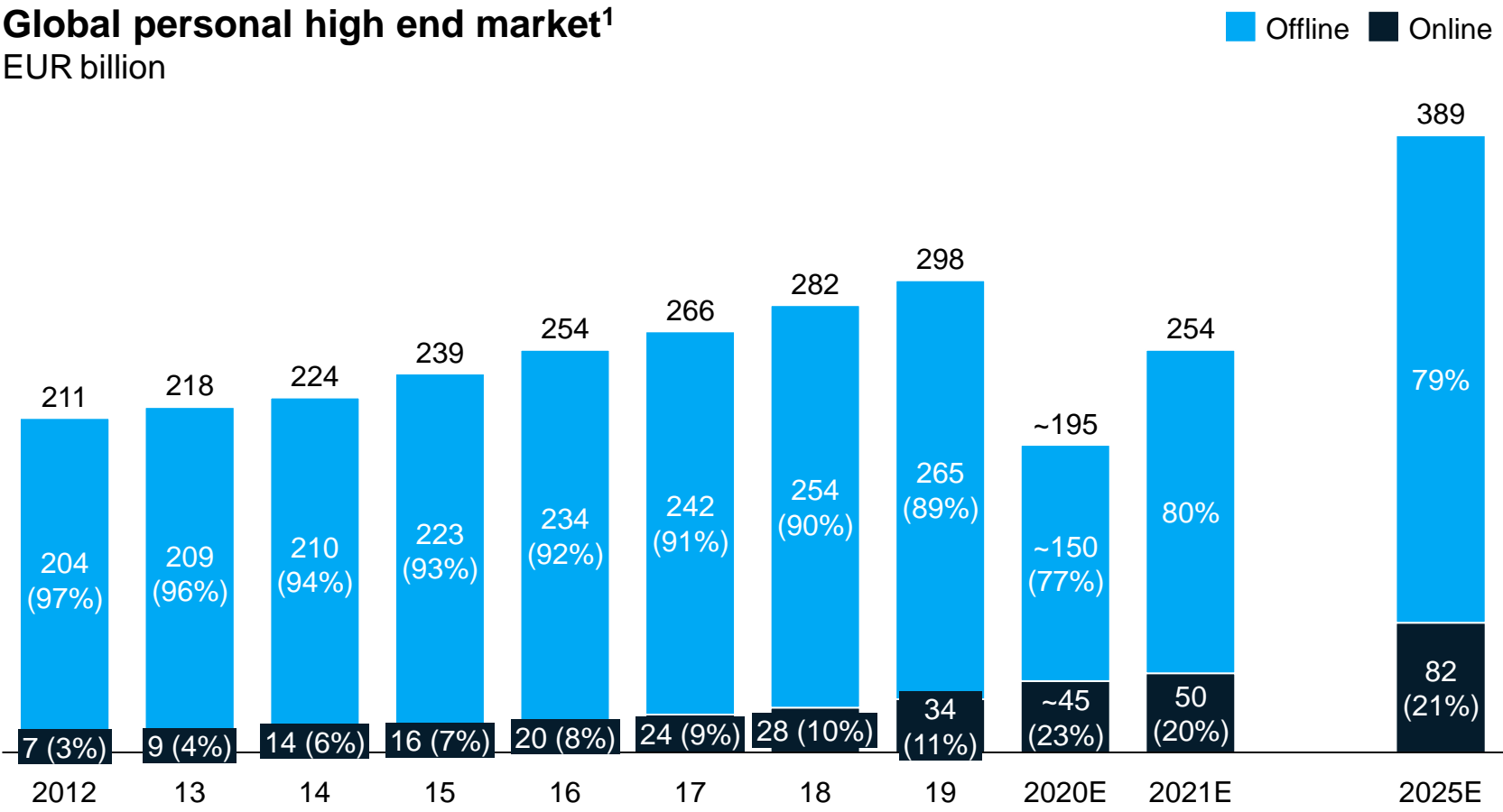- Unprecedented availability of data
- Tumbling costs of computing power
- Powerful new algorithms

In high end retail, online has not compensated for COVID-19 impact – and it will continue to roar

Global personal high end market[1]
EUR billion

■ Offline ■ Online

Year	Total	Offline	Online
2012	211	204 (97%)	7 (3%)
13	218	209 (96%)	9 (4%)
14	224	210 (94%)	14 (6%)
15	239	223 (93%)	16 (7%)
16	254	234 (92%)	20 (8%)
17	266	242 (91%)	24 (9%)
18	282	254 (90%)	28 (10%)
19	298	265 (89%)	34 (11%)
2020E	~195	~150 (77%)	~45 (23%)
2021E	254	80%	50 (20%)
2025E	389	79%	82 (21%)

1. Apparel, Footwear, Accessories, Jewelry & Watches, Leather Goods, Beauty & Perfumes

Source: Forrester; McKinsey

High end/ luxury had been the engine of the apparel industry in recent years

COVID-19 has impacted sales – mostly physical due to **store closures, lockdowns** and **socio-economic impact** of the pandemic

Digital sales have continued to grow to represent **~23%** of sales – however, **their growth has not compensate** for the physical sales steer decline

Online sales are expected to continue growing in absolute terms to represent **20-22% in 2025**

Four key shifts in the "new Digital normal"

1 **Stores and physical experiences** will have a **second life** as enablers of **omnichannel digital engagement**

2 Relevance of **digital brand storytelling** will soar – key to orchestrate **digital-only narrative**

3 **Growth opportunities** will be driven by **ecosystems**

4 Companies will need to **transform "inside"** with **digital and analytics** to drive **speed and efficiency**

1: Physical experiences to influence purchase are not dead – China shows the future
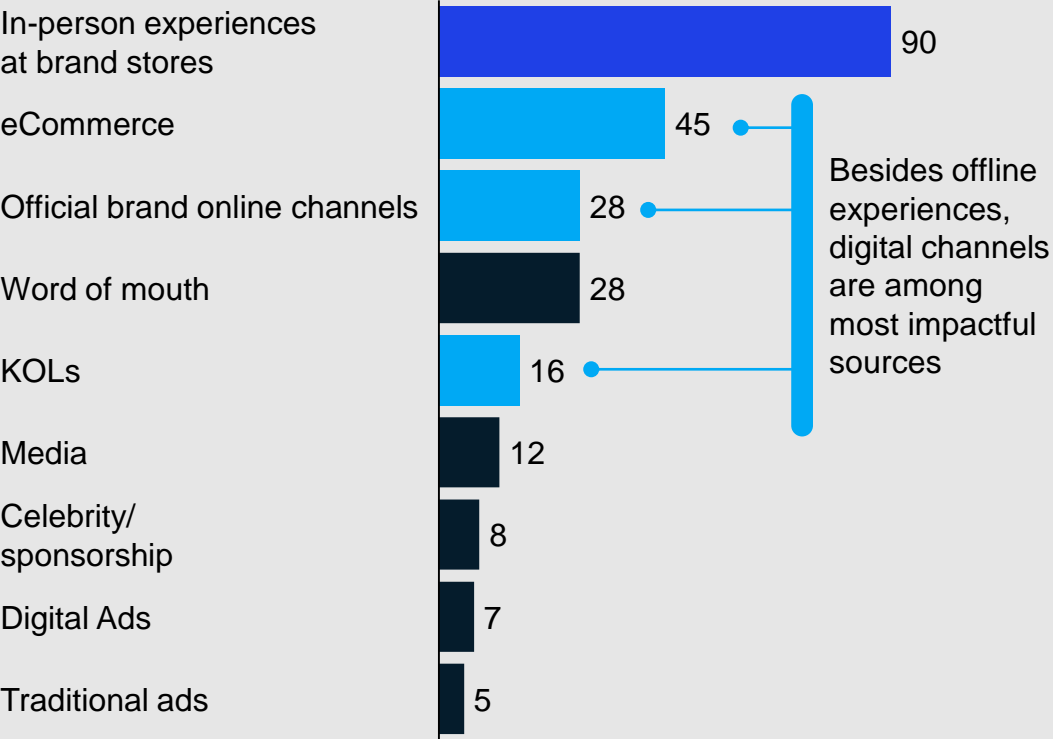
Share of omni-channel shoppers[1]
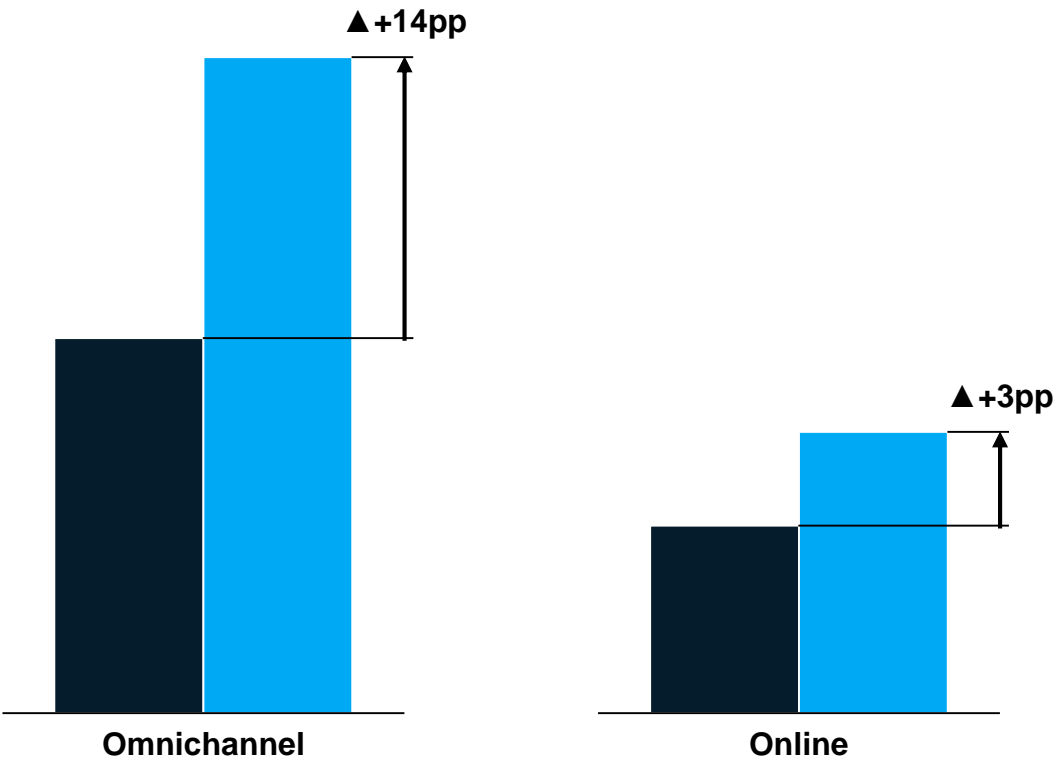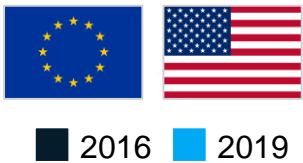
■ 2016 ■ 2019

▲ +14pp

▲ +3pp

Omnichannel

Online

What are the most impactful sources of information that influence your purchase?

% of survey respondents

Source	Value
In-person experiences at brand stores	90
eCommerce	45
Official brand online channels	28
Word of mouth	28
KOLs	16
Media	12
Celebrity/ sponsorship	8
Digital Ads	7
Traditional ads	5

Besides offline experiences, digital channels are among most impactful sources

1: What could be a target omnichannel experience merging digital and physical experience in a high end environment?

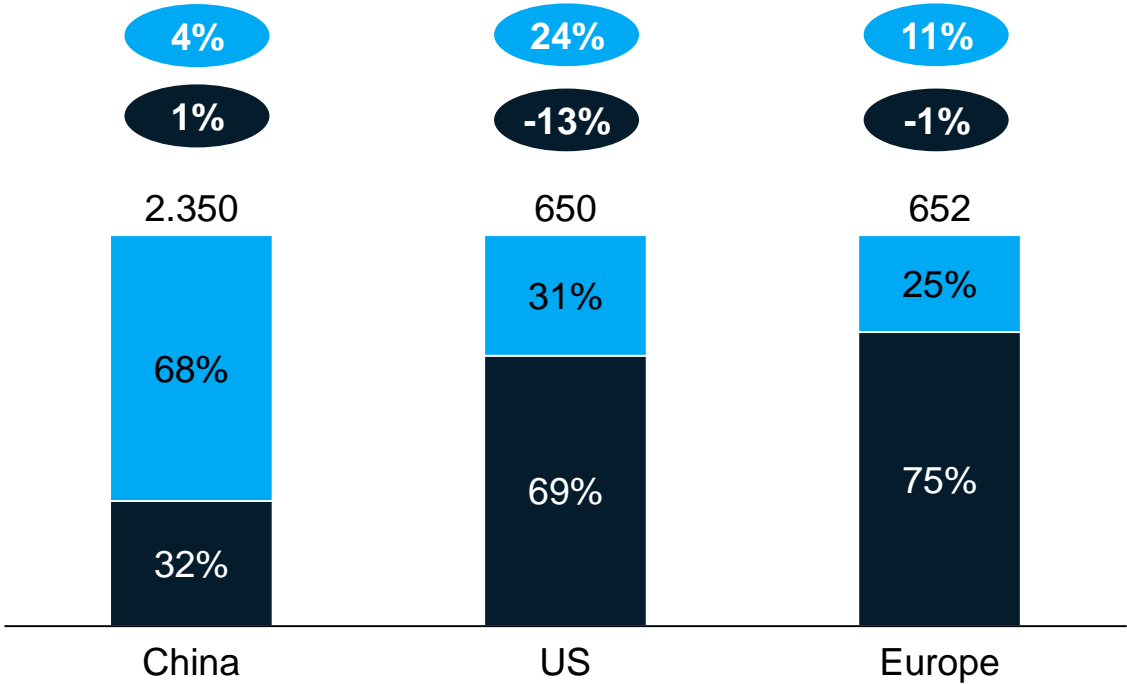Applicable to high end apparel and food retail as well as cultural institutions

Digital experience

After visit
Curated 1-1 campaigns to re-engage customers

Capture of all online and offline follow-up data

Before visit
"Capture" of customers in research stage

Pairing of customer with online advisor ("digital hunter")

Omnichannel Customer journey

Walk-in visit
Tailored store visit

New customer data captured in CRM

Out-of-stock captured for online follow-up later

Visit curation
Visit preparation based on online and CRM data

Stock reinforced to maximize chances of success of visits scheduled

Physical experience

Enablers required to make this happen

New salespeople profiles:

Omnichannel advisors

Digital curators

Digital hunters

In-store tech enabled associates

Technology and data enablers:

In-store tools for associates

CRM

Digital marketing stack

Data architecture and governance for customer data

2: Marketing spend of high end brands is shifting to digital, with China on the forefront

X̃ CAGR, 2014-19   ⬛ Digital[1]   ⬛ Non-digital[2]

High end retail players' marketing spend per channel, US$M, 2019
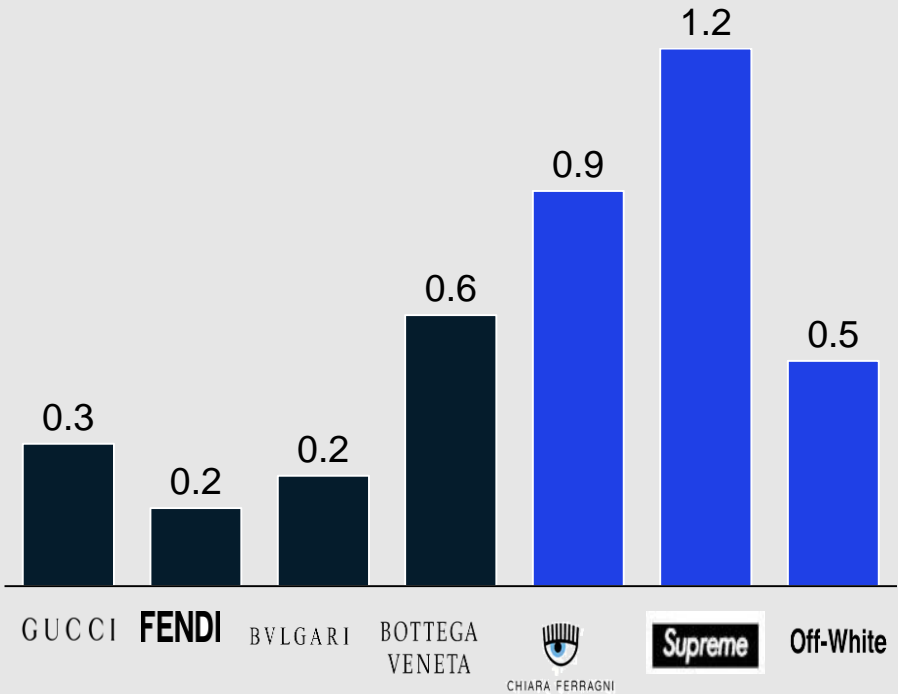
	China	US	Europe
Digital CAGR	4%	24%	11%
Non-digital CAGR	1%	-13%	-1%
Total	2.350	650	652
Digital	68%	31%	25%
Non-digital	32%	69%	75%

1. Digital: Display, search, video, social, and all other digital
2. Non-digital: TV, Magazines, Out-of-home, Newspapers, Radio and Cinema

Followers of challenger brands are more active and engaged than those of legacy brands

Instagram like – follower ratio (LFR)

| GUCCI	FENDI	BVLGARI	BOTTEGA VENETA	CHIARA FERRAGNI	Supreme	Off-White
0.3	0.2	0.2	0.6	0.9	1.2	0.5

3: In the new digital world, traditional supply-chain demand may be disrupted by ecosystems

Traditionally, customer needs have been served by dozens of parallel value chains…

Producer/manufacturer

Intermediary
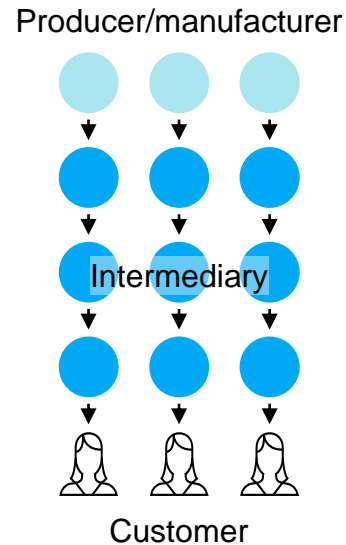
Customer

… recent technology and customer trends create a shift in these chains…
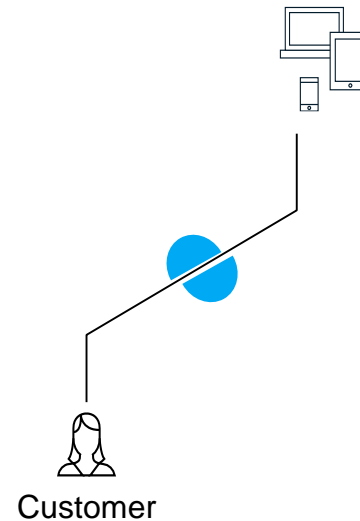
Customer

…and increasingly, value chains are collapsing into one chain around each key customer need

Producer/manufacturer

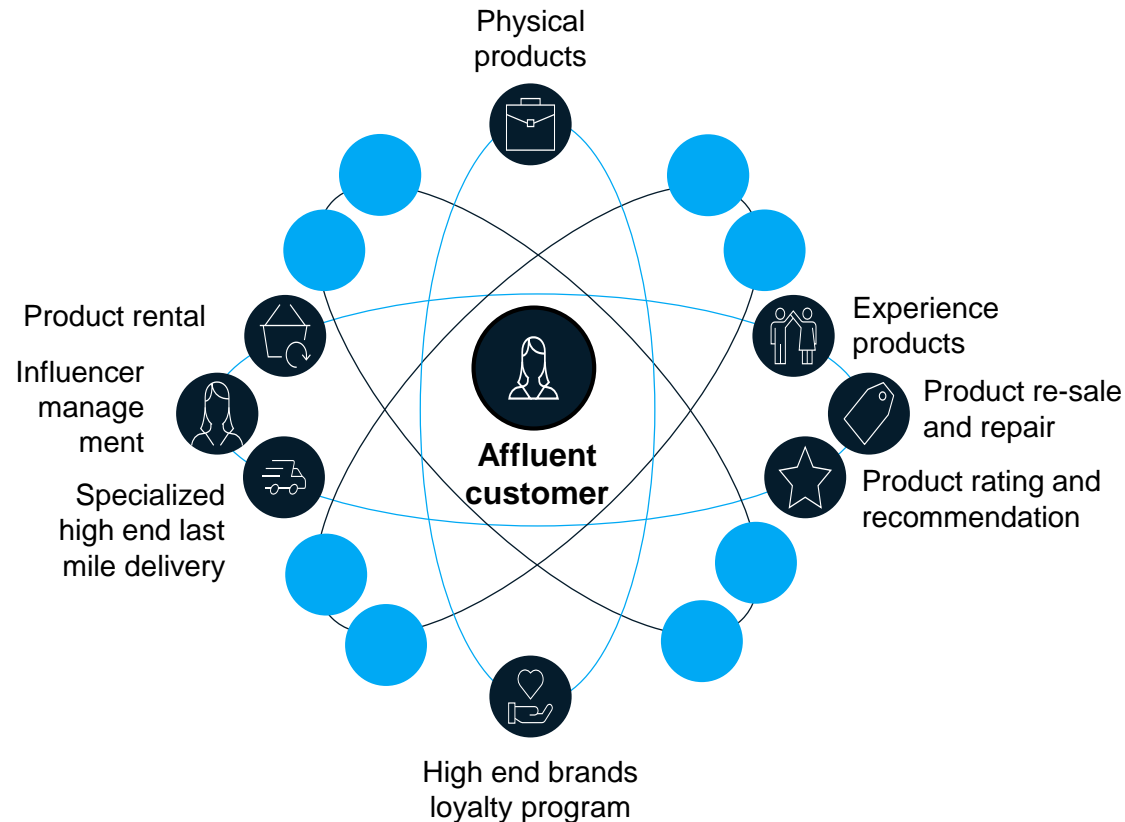Intermediary

Ecosystem orchestrator
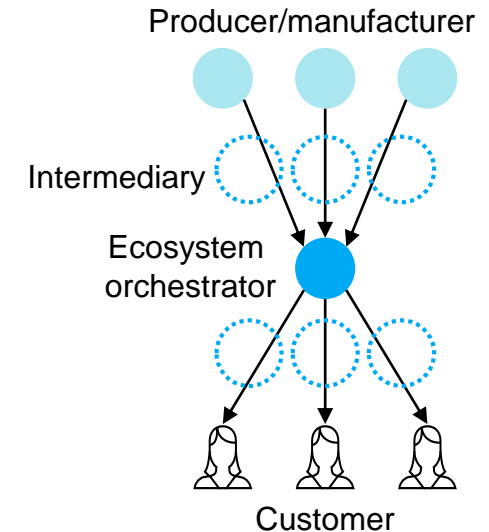
Customer

Risks from ecosystems are high for high end players

Loss of customer ownership

Disintermediation

Commoditization (less in high end products and services, but still relevant)

To succeed, a compelling end-to-end digital relation is needed

Cross-sectoral in nature

Delivered in a differentiated way

Holistically address customer needs

3: To win in ecosystems, players will need to win the battle for customer's attention

Physical products

Experience products

Product re-sale and repair

Product rating and recommendation

High end brands loyalty program

Specialized high end last mile delivery

Influencer management

Product rental

Affluent customer

NIKE

What?
Everything sports amateurs

How?
Digital tools to support you end-to-end in your amateur sporting journey (improving, challenging others, etc)

NESPRESSO.

What?
Everything coffee

How?
Hardware (coffee makers at all price points), product (coffee and adjacent products) and best-in-class customer service

Google Arts & Culture

What?
Everything arts and culture (within the broader Google ecosystem)

How?
Access to a global museums collection online, tickets and experience related to arts and culture

3: Three Squirrel is an example of building direct customer relationships through DtC channels

Who is Three Squirrels

Leading Chinese premium snack player founded in 2012 and IPOed in 2019

## What is their business model and how they fought back the B2C ecosystems in China?

Leveraged digital and innovative marketing to build strong brand to avoid "losing the customer"

Built a balanced mix of channels: Physical channels to foster visibility, platforms (T-mall) and owned channels (owned D2C online and offline with 150+ physical stores)

Diversified product offerings to expand addressable markets and margins

Expanded across the value chain to build its own ecosystem around premium food items and related services

Three Squirrels sales
USD Million

Year	Sales
2013	9
15	361
17	865
2019	1,695
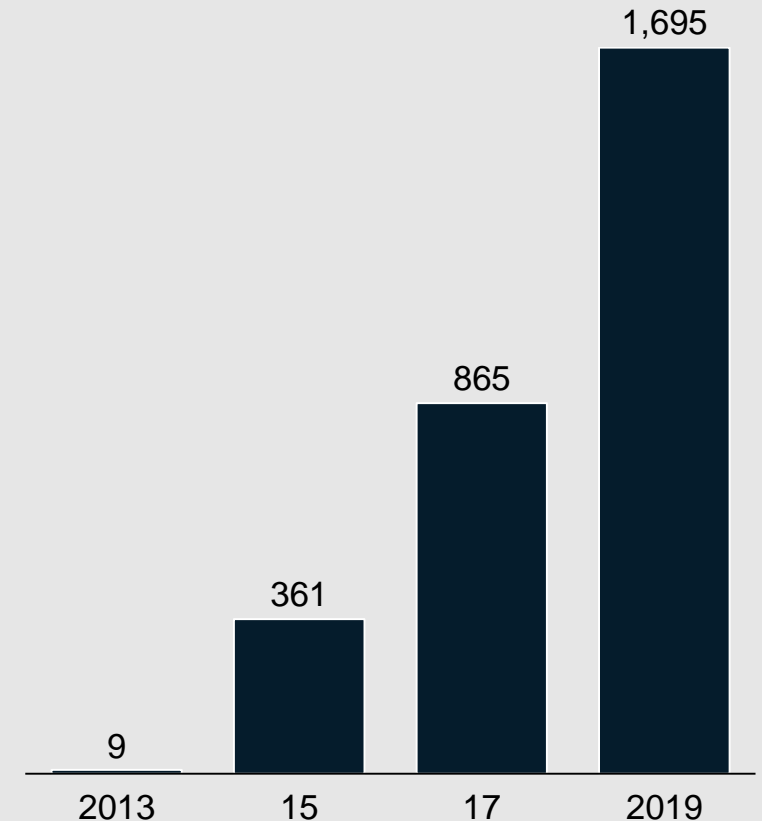
4: Beyond customer experience and brand, there are many "internal" use cases with significant experience for high end players
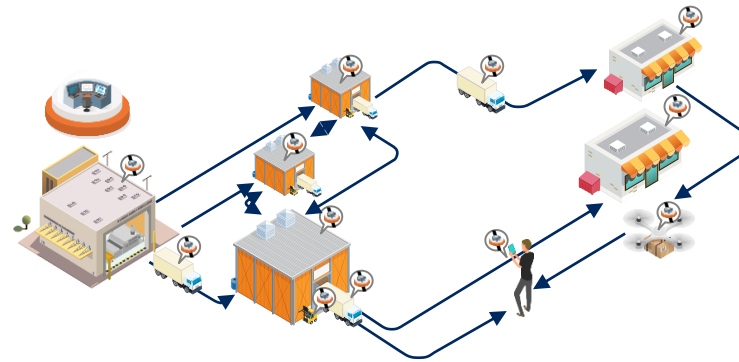
Illustration for high end fashion and food retail, applicable also to other high end industries

Physical space operation

Macro space optimization

Personalized customer journeys to maximize customer value

Automated out of stock detection and minimization

Omnichannel space of the future

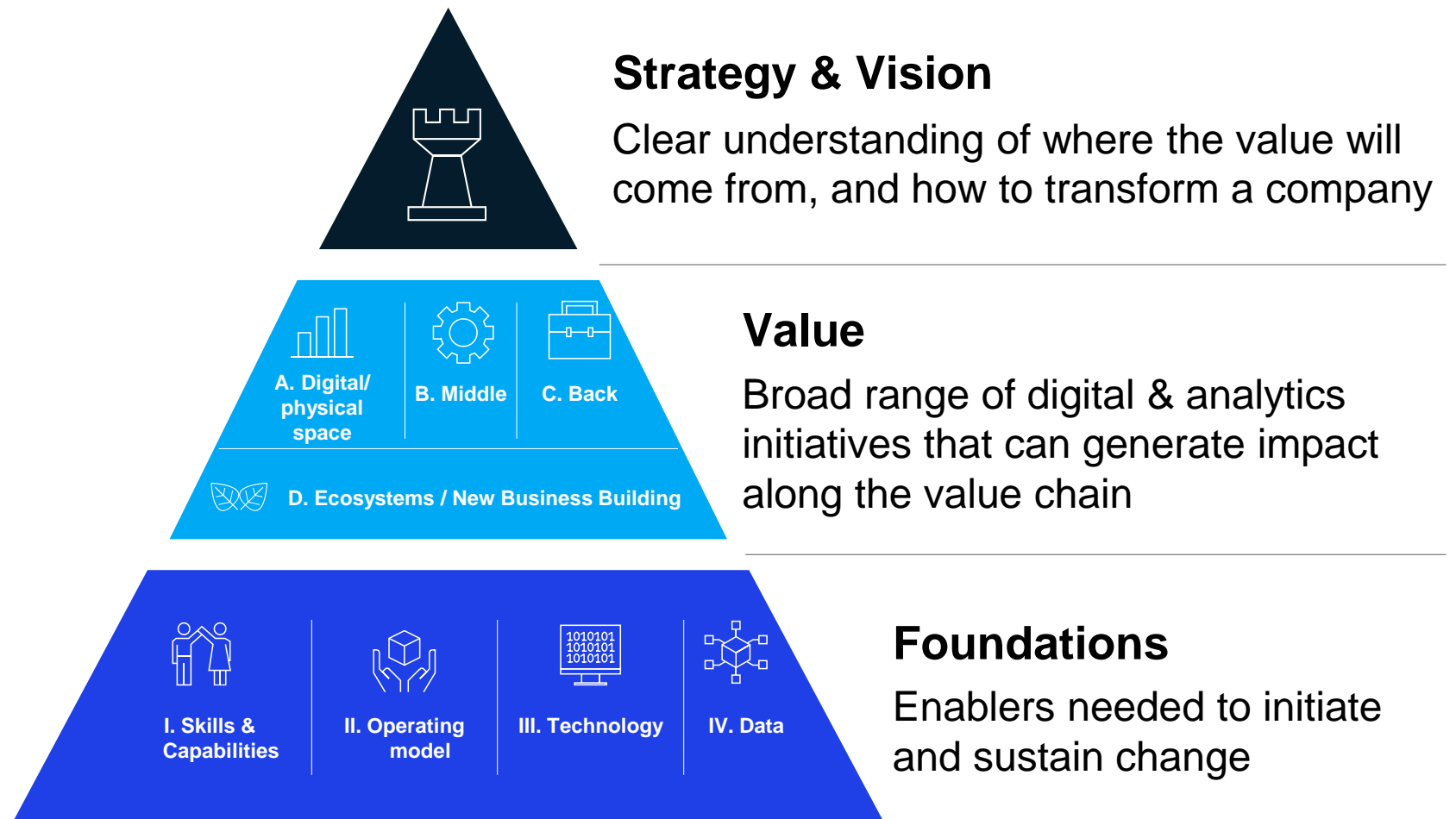Seamless omnichannel experience

Distribution and supply chain

AA-powered demand forecasting and replenishment

IOT-enabled warehouse optimization and automation

Optimal warehouse picking and slotting

E2E digitized supply chain planning

AA-powered network, transport and route optimization

Platform economy last mile delivery

Headquarters

Machine learning-based design and creative inputs

Digital product design

Digitally-enabled buying sessions

Digitized and robotized finance and back office processes

Talent and HR analytics

Three elements required to mobilize an organization for a digital transformation

Strategy & Vision

Clear understanding of where the value will come from, and how to transform a company

Value

Broad range of digital & analytics initiatives that can generate impact along the value chain

Foundations

Enablers needed to initiate and sustain change

Pyramid labels:
- A. Digital/physical space
- B. Middle
- C. Back
- D. Ecosystems / New Business Building
- I. Skills & Capabilities
- II. Operating model
- III. Technology
- IV. Data

What to do next

Strategy & Vision

- Define a **bold digital aspiration** as the key element to **rally your organization for the challenge**

Value

- Define a **broad portfolio of digital and analytics initiatives** linked to your strategy
- **Find fast (>6 months) and high impact projects** can help drive change and fund the transformation

Foundations

- **Do not invest in foundations** if **not directly linked to value** initiatives
- **Build foundations gradually**, as value initiatives deliver impact

Initial first practical ideas to get started

How could you increase traffic?

Optimize and re-deploy marketing spend to enhance brand in digital space

Personalize digital communications – e.g., email

Streamline customer registration and data gathering process

How could you enhance conversion?

Re-engage customers who abandon cart

Reduce friction in customer journey to minimize "bounce rates"

Minimize lost sales from out-of-stock with unified stock (if applicable) and intelligent options

How could you grow average order value?

Leverage chat to up-sell

Tailor web content to customers (high level, e.g. location-based)

How could you improve omni-channel experience?

Offer seamless digital customer experience and returns

Deliver more tailored physical experiences – e.g., curated visits