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# Hermes International

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# Hermes International

Phuong Tran

## Why Hermes International?

“Why do luxury brands still develop and expand even the economy goes down?” “How can a person spend thousands of dollars to buy a handbag or a scarf?” These questions always are secrets of Hermes International. Hermès International S.A. was founded by Thierry Hermes in Paris in 1837. It is a French company which designs and manufactures luxury products such as leather goods, silk goods, perfumes, clothing, etc. They have 304 exclusive stores which include 180 branches, 124 concessionaries and 21 retail outlets. The headquarter of Hermes is in Paris, France. Hermes only has 9081 employees working for them but their revenues keep increasing rapidly in many year. Its revenue in 2011 was 2,841 million euros which was about 3,720 million US Dollars (Global Data, 2011).

Hermes International Company knows how to deal with bad economy and attract more and more costumers by meeting and exceeding their expectations. Even though Hermes prices their products sky high, their sales still grow up every year. On average, a Hermes handbag can cost from \$3000-\$50,000, but it is still a desire of many people. Luxury industry is not a normal field; it is a place when people spend money not only to satisfy their needs but also to enjoy best quality of products and service. Luxury goods differs extremely rich people from others. Price seems to not affect much on customer’s behavior in this type of industry. Hermes has a lot of strong competitors, and Louis Vuitton is one of them. Louis Vuitton was known as the biggest company in luxury industry, but instead of competing with Hermes, they want to “swallow” this company and make it become a part of them. This plan has not became true but it proved that Hermes is such an attractive and valuable brand that even a big company like Louis Vuitton wants to have it. During 2012, Hermes also lost an important lawsuit in China and they no longer can use Hermes name in Chinese language. While Hermes is working on expanding more in China, this lost became one of their disadvantages and create a distance from them to Chinese consumers.

## Hermes’s History

“Hermes international was founded in 1837 by Thierry Hermès. He is a maker of saddles for horses. 1920, the company launched a line of clothing, watches and gloves. In 1978, Jean-Louis Dumas took over the leadership of this company. Hermes reached its 225<sup>th</sup> store in 1990 and went public from 1993. By 1999, its sale was US\$ 1 billion” (Funding Universe, 2000).

Hermes Company had to experience a lot of rise-and-fall time during its development. In 1922, Thierry Hermes’s son decided to sell his stake to Emile Maurice. Emile figured out the increase of automobiles and obsolescence of carriages, he decided to focus production on travel and sport leather goods. In 1950, Hermes launched a hand bag which was named after Princess Kelly. The name was an excellent decision of the company, because the princess was a famous and fashionable person who attracted a lot of customers’ attentions. That’s why this type of handbag was famous and remained in consistent demand for a long time.

“Emile-Maurice Hermes passed the family business on to his son-in-law, Robert Dumas, who would direct the design and production of the first Hermes *carré*, or scarf, in 1937...By the mid-1990s one Hermes scarf commanded US\$245, a tie cost US\$115, and a Kelly purse set its owner back about US\$3,500. High demand added another element to the cost: customers were known to wait more than a year for orders to be filled” (Funding Universe, 2000)

Despite the success of other competitors in 1970, Hermes started to have some issues. Their growth rate was only 5%, while the inflation in France at that time was 15%. They used natural

materials instead of man-made materials, so the cost of raw materials became one of the disadvantages for them. The younger Dumas (Jean-Louis Dumas) took charge and helped Hermes gain their strength back. He targeted the United States and Asia to expand the company. Dumas hired two new designers who came up with a lot of wonderful designs and helped Hermes to produce 30,000 different items on its array.

After 1990, Hermes focused on expanding over the world. Their stores grew from 15 in 1978 to more than 225 after 1990. In February 2012, Hermes “lost its trademark lawsuit over its appeal to China's Trademark Appeal Board to cancel a trademark similar to its Chinese name. Hermes has registered its English name and pattern in China in 1977. However, it never registered its Chinese name as a trademark.” (china.org.cn, 2012)

This fact negatively affected Hermes because China is a strong and potential market of luxury brands. China is a place where “[w]ealthy consumers looking to differentiate from the masses provide an opportunity for luxury brands such as Hermes that target the ultra-rich” (Shaun Rein, 2011). Every customer knows Hermes International under Hermes name and “its Duc carriage with horse logo”; if they cannot use this name in China, it will take away one of the biggest advantages of Hermes. They spent hundreds of years to build this name and make it popular like today.

### **Current and Future CEO**

Patrick Thomas is the first non-family member of Hermes International Company. “Thomas began his career as a financial analyst, after studying at the ESCP business school. He then held an executive position at the drinks company Pampryl, which was founded by his family and later sold to Pernod Ricard. At Pernod Ricard he was first finance director, then managing director of the group’s UK subsidiary” (Daniel Tournier, Jean-Louis Petibon, 2011). “Mr. Patrick Thomas has been the Chief Executive Officer of Hermes International SA since January 2006. Mr. Thomas served as Joint Chief Executive Officer of Hermes International S.A. since September 16, 2004. He served as the Chief Executive Officer of Hermes International S.A. from July 15, 2003 to September 16, 2004 and previously served the same position from 1989 to 1997” (Bloomberg Business week, 2011).

Patrick Thomas not only works with recent strategies, but also has strategic plans ready for long term future. When the board asks him about Hermes International’s performance, they mean it in 10 years from now. That is the reason why Patrick Thomas always works hard to be ready for the far future. In the recent interview, he mentioned about the new tax rate in France. He thinks “the combination of these new taxes will cost one percentage point in terms of profitability by the end of the year” (Business of Luxury, 2012). As a person who is always well prepared for anything bad that can happen, Patrick believes that their products still remain attracting customers due to high quality merchandise and service. Knowing this new tax’s negative affect, he decided to change the manufacturing location beforehand. It will increase capacity and reduce production cost. Therefore sale revenue will be increased. This early action will help Hermes cover its losses from higher tax rate.

Patrick Thomas is the person who successfully leads Hermes in the right direction to grow rapidly from 2006 until now. Rather than stay in the familiar market like France, Japan or the United States, he decided to open more stores in Asia because he thought it would be a potential market. He said "Hermes is going to be more and more Asian. When I joined in 1989, a third of our business was in Asia; now it's 50% and in 20 years, it will be 66%" (Heidi Ueberroth, 2005). And he was right; Asia is a place that contains a lot of wealthy customers who voluntarily spend hundreds of thousands of dollar for luxury items. In September 2012, Patrick stated that “their sales in Mainland China rise 28 percent during the first six months of this year” (Victoria Delevigne, 2012).

Patrick Thomas also is a great leader of Hermes. He knows how to use their healthy financial situation to motivate his employees and increase their loyalty. He decided to give out high salary

levels to his employees in order to make them satisfied with their jobs and work harder. He knows what makes Hermes successful like today is because of the important contributions from his employees and craftsmen. Even Patrick Thomas is a successful manager who has led Hermes for more than 5 years; he never stops studying from people to make things better. He studied a lot of experiences from Jean Louis Dumas who spent an hour every day to shake hands with every single employee who worked there. This is not a wasting time habit; it helped Jean to get to know his people more and it helped create sense of team spirit.

Patrick Thomas's favorite sentence about leadership is "If you want to lead people, you must get behind them" (Egon Zehnder International, 2011). He always cares about the long term future. He expects to own a great quality team rather than individuals. He even prepares for his own retirement plan. He wants to hand over successful teams with excellent skills to the next CEO. In 2012, Hermes already announced the new CEO, Axel Dumas will replace Patrick Thomas's position in a couple of years. Instead of waiting for that moment to come, Patrick Thomas decided to ask Axel to work alongside him to study experiences from him and get ready for his new responsibilities. He works hard to make sure Hermes International grows even without his leadership.

Axel Dumas is 41 years old, and a member of the 6th generation of the Hermes family. Axel got his master degree in Law and bachelor in Philosophy. He studied in both Sciences Po University and Harvard University. He started working for Hermes after his banking career in 1993. Before working in the leather department, he used to join in the jewelry division. In 2011, Axel became chief operating officer of Hermes International. In May 2012, "Axel Dumas is named as Hermes chief" (Scheherazade Daneshkhu, 2012). He has already worked alongside Patrick Thomas for a couple of years, so he will be ready to become the new CEO of company in the near future.

### **Plans and Objectives**

Talking about the vision of Hermes International, Patrick Thomas brought up the dilemma that the luxury industry has to face. He said "The luxury industry is built on a paradox: the more desirable the brand becomes, the more it sells but the more it sells, the less desirable it becomes" (Interbrand, 2011).

This fact will be one of the biggest challenges that not only Hermes but also another luxury brands have to deal with. Instead of being satisfied with high revenue and enjoying the unstoppable growth, Hermes already has a good vision about the near future when customers are going to get used to their brand, products and services. The vision of Hermes will be a solution for them to get over this problem. They always want to focus more and more on the best quality materials. Their best craftsmanship with excellent creativity will bring to customers satisfaction and remain the buyer's desire. To Hermes, raising revenue or benefit is equal weight with keeping a strong and high quality brand. They do not want to give up their brands that they built for hundreds of years just because of large volume of sale. Customers deserve the best quality products and services that they spend a lot of money for.

"Hermes objectives are achieving the sales and profit targets by providing the quality fashion brands to its' customers, mission of the company is to become a leading company of the market in quality fashion brands by meeting the new fashion trends of the market place. The company is spending a lot of funds on research and development activities, which are under taken for the purpose of not only to find out the new method for producing quality products but also to explore new fashion trends among customers. The company is creating the effective awareness of fashion brands in customers and also focusing on the creations of positive image and word of mouth in customers. Hermes is also focusing to sponsor the events like its sponsor horse competition in Paris" (Smith, 2004).

During the third quarter of 2012, Hermes experienced healthy growth while other competitors like Burberry or Gucci were starting to suffer. Patrick Thomas said “We have not seen any inflexion of any kind in our sales, Therefore our targets for the year remain unchanged” (Astrid Wendlandt, 2012). Hermes’s goal right now is launching their next spring collection successfully and maintaining their sales as last year due to economic down turn. Christophe Lemaire is an ex-Lacoste designer, who has a lot of experience in luxury industry. He is working on his fourth ready-to-wear collection for Hermes and plans to introduce it to customers in the near future. Customers now care about high quality clothes which are fashionable but not ostentatious. Understanding these tastes, Christophe presented his collection which “featured simple, minimalist ample white tunics, draped exotic printed silk suits and safari-inspired beige and ochre raincoats and jackets.” “The collection seemed this year more eclectic than in the past, critics said” (Astrid Wendlandt, 2012)

### **Environmental Problem**

Due to the fact that almost all of their raw materials are from crocodile, lizard, and ostrich skins, Hermes has to face a lot of environmental concerns from the animal protection organizations, such as “People for the Ethical Treatment of Animals, which is the largest animal rights organization in the world, with more than 3 million members and supporters.” (PETA Organization, 2012) The hot topics that people from all over the world are talking about are protecting the environment from pollution and animals from extinction. Limited and unethical supply is still a threat to Hermes until they find out another type of ethical and high quality raw material that can substitute for an animal’s skin. “Naturally this issue has aroused the interest of PETA (People for the Ethical Treatment of Animals), an organization that firmly believes that products such as fur and animal skins should have no place in modern fashion. Dan Matthews, PETA’s Senior Vice President, said: ‘If Hermes really wants to be a leader in the fashion industry, it should stop killing animals and use cruel-free mock crocodile and fake snake instead.’ Unsurprisingly Patrick Thomas of Hermes disagrees: ‘Luxury is when desire is stronger than reason’” (Reality sense, 2009)

In the beginning of 2009, PETA gave Hermes a warning about Hermes’s crocodile farms. The organization stated that “breeding crocodile is still murder – even if the crocs belong to” Hermes (Elena Gorgan, 2009).

So the question here is “Why Are Crocodile Skins So Valuable?” It is valuable enough that luxury brands cannot give up it and switch to another type of materials. First, the only two parts of the crocodile skin what can be used to make leather goods are from belly and cheeks. The skin from crocodile back is too tough to make anything. To make a single bag, belt or wallet, skin from only one crocodile is not enough. Thomas Patrick stated that they normally use three or four animals’ skins to make a Hermes handbag. This huge amount of material can lead to crocodile’s extinction and create a bad image of the Hermes brand. Second, crocodile’s skin is imported from breeding farms which are mostly in Australia. It increases the value and the price of the skin. Fashion brands are willing to pay high custom duties to import these materials. Hermes purchases their crocodiles’ skin legally from the farms, so it reduces the threat from animal protection organizations.

Third, Cost of Breeding is really high. “According to Sunday Times, crocodiles are difficult to rear, since they are extremely aggressive and enormous. They have been known to attack humans for any slight provocation, making them hard to feed and look after. Crocodiles are carnivorous and consume huge amounts of food. Although crocodile skins are valuable, the cost of breeding crocodiles is high, due partly to the cost of having professionally trained personnel and the cost of meat” (Jane Doucet, 2010)

Due to these three main reasons, even though Hermes has to face a lot of concerns about the environments when they use crocodile’s skin as their raw materials, they still use and import

them at least for now. This type of material is special, high quality, durable and valuable. These characteristics are things that Hermes always wants to focus on and use as main goals.

### **Low productivity-Long waiting Time**

Hermes's products are handmade by craftsmen who have excellent experiences and skills in this industry. They do not let machines or technology be involved much in their production. That is the reason why technology changes over time but has not affected their company much. Compared to other companies, Hermes has really low productivity. For example, Ille Toyota spends about 30 hours making a car, while Hermes's craftsmen normally spend 48 hours finishing a handbag (Jeffrey Hays, 2009). Even though their productivity is low, it doesn't mean they need to change it. Consumers who purchase luxury products expect to have excellent and high quality goods, and they are willing to pay extra money to own a limited edition, lifetime guaranteed handbags, purses, etc. For now, technology is something that is not a threat to Hermes, and they do not need to change to catch up with other companies.

The most important thing that they need to do right now is increase the number of their craftsmen, due to massive demand. Hermes is known as a fashion brand which has the longest waiting time. For example, "[a]s one of the most sought-after and precious handbag in the world, an authentic Birkin bag from Hermes shops has price tag of \$7000 to \$140,000 on average, and selling price is much higher in reselling market. It is highly coveted and, for many years, was reputed for having a waiting list of up to 6 years – the longest wait for any bag in history" (Know Hermes Birkin Bag Waiting List, 2011). This waiting list can impress people, but it is not good news to them. None of the sellers want to make their customers wait for that long. The longer they wait, the more customers Hermes is going to lose.

### **Change in Target Customers and Luxury Industry**

About 50% of Hermes's products are leather goods which include handbags, wallets, and purses. Birkin Bag is one product that belongs to Hermes which has massive demand from customers. This handbag is a 100% handmade in leather and named after famous singer and actress Jane Birkin (Robin Givhan, 2004). Hermes sells this handbag from \$9000 to \$150,000. Birkin bag are made by calf, ostrich, crocodile and lizard's skins. Both interior and exterior of this bag have the same color, and it comes with a variety of sizes. Hermes stamps number-codes in both the lock and key of this handbag to differ their handbag to the ungentine one. A special thing about all metallic hardware they use on their products is they are plated with gold or palladium. These high quality and expensive covers will prevent the tarnishing process and make the handbag last longer. Customers also receive a wonderful after sale service from Hermes. They offer a service called "spa treatment" which reconditions the used handbags and makes it look like new.

"In 2011 the luxury industry experienced an unprecedented level of change. LVMH had snapped up controlling share in Singapore's Heng Long, through a jointly created holding company" (Sophie Doran, 2011). This fact has really big effect to Hermes, because Heng Long is their biggest supplier. Two-thirds of their crocodile skins are supplied from them. LVMH is known as the world's largest company in luxury industry. From now on, they have a control power of an important supplier; they will have strong influence to the rest of the luxury brands.

On the other hand, luxury industry also started suffering due to economic issues in 2011. While the United States experienced high unemployment rates, and European increases in debt, China went through a hot economic growth. Depending on these facts, Hermes and other luxury brands wanted to change direction and focused more on Asian areas especially in Mainland China.

"Yet 2011 was a year of stellar performance for the industry, in most cases brands and conglomerates enjoyed overall double-digit growth. Global luxury goods sales have continued 2010's

double-digit growth trajectory and will see an increase of 10 percent, to €191 billion in 2011” (Sophie Doran, 2011).

According to the luxury market study, Bain predicted the luxury industry will grow six to seven percent in 2012. Bain also “has identified the top nine market-defining factors for luxury in the next three to five years”. Chinese consumers who buy more than 20 percent of the global luxury goods; Asian consumers (which includes Japanese, Korean and Southeast Asia consumers) about 50%. Besides it, 30% of luxury sales now take place in emerging markets. The luxury industry will have a new generation of consumers due to the change in the average age of buyers. While Asian luxury customers are getting younger, in Europe and the United States, older ones purchase more luxury goods than others. The differences between ages also create the differences in tastes and preferences of buyers. If luxury brands can offer the right styles in the right market, they will survive and grow rapidly. As they become more independent and have higher earnings, women will start spending more money on luxury products and also become potential customers like men. “Men are increasingly likely to seek traditionally female brand dimensions around “fashion” and “beauty” as well as product functionality. Luxury product usage has crept in to more casual occasions, which in turn affects the kinds of products that brands develop (e.g. casual-chic apparel lines). Luxury is fueled by newer and bigger money. In turn, consumers’ insatiable chase for higher quality and greater craftsmanship/materials favors absolute luxury offerings. Premium and fast-fashion brands are forcing luxury brands to rethink their value proposition by competing directly with lower segment luxury. The convergence of stores, e-commerce, social media and mobile commerce is creating an “omnichannel” experience for consumers” (Bain & Company, 2012).

Hermès’s target customers are both young adults and teenagers who love fashion. Their customers look for high quality, good features, and wonderful after sale services in Hermès’s products. The buyers of Hermès have high incomes so they do not seem to care about expensive prices. What they are looking for in Hermès’ leather goods are limited edition items and differentiations. Luxury customers want to own something that not a lot of people can buy or afford.

The United States is one of the important markets that Hermès is working on. Due to high priced products, Hermès needs to target on high income customers. According to the Census Bureau, the median wage of males in the United States is much higher than females (almost 50% higher) (Exhibit 1). From this information, Hermès focuses more on male accessories and clothing than female. This target customer is not the same in all countries. It varies depending on location, geography and economy.

Besides selling products in physical stores, Hermès is expanding more into online shopping. The internet now allows everyone to shop at home rather than going to the store. It saves time and money for both customers and sellers. Shopping online makes purchasing easier and more convenient than ever. It brings sellers closer to customers by cutting distance and time. That is the reason why Hermès now starts selling their products online rather than only at physical stores.

Mainland China is a target market that Hermès really pays attention to right now. Every piece of information about Chinese consumers’ behaviors is important and valuable to Hermès. According to a study in China about luxury consumption, male customers purchase luxury goods online more than female customers. Wine and watches are the most purchased by the male buyers. 65.5% of online customers in China are male and they tend to purchase luxuries 10% higher than females (Exhibit 2). First, it is because males prefer to choose a convenient and highly efficient shopping options. Second, they prefer to buy high quality products which show unique taste rather than low priced merchandise. And third, they currently have higher income than female.

Talking about Hermès’ market specifically, they have more than 7 different types of products: leather goods, ready-to-wear clothing and fashion accessories, perfumes, watches,

tableware, silk and textiles, furniture, etc. Target consumers that Hermes wants to attract are extremely wealthy people who are looking for high quality, limited-edition products and excellent after-sale service. More than 47% of their sales are leather goods so they highly focus on this section and have launched many different collections to attract customers. They also have really high revenue from ready-to-wear clothing and silk items which are 20% and 12% respectively (Exhibit 3).

Hermes is trying to expand and have as many stores as possible. They have recognized the potential market in Asia. Instead of staying in Europe, they expanded more in Asian countries. Japan is one of their key markets, which contains 17-19% of their sale and even equal to sum of the sale in Europe countries excluding France. Even though France is Hermes's home country, French customers have not wearied of this brand and still satisfied with their products. French buyers still consume about 20% of Hermes's merchandise and this consumption remains constant year by year (Exhibit 4). Hermes knows how to maintain and improve their image by providing excellent quality items. They introduce different collections every season to refresh their products and satisfy varied tastes of customers.

Due to the hot development in economy in China, Hermes also focused on attracting more Chinese consumers who have a lot of money and are ready to pay thousands of dollars to own a unique and exclusive product. According to Bloomberg's News, Hermes decided to increase their growth target due to massive demand in China (Andrew Roberts, 2012). Chinese demand for luxury products is rising dramatically which explained why Hermes's first half operating profit in 2012 rose 22%. From this growth, their operating income increased from \$418 million to \$640 million.

During 2011-2012, Hermes had strong growth all over the world except in Japan. The Americas and Asia-Pacific are still their hot markets. From 2010 to 2011, in both of these markets, their sales grew about 27%. The market in France is not improving that fast but still has positive signs of development of 19.3%. (Exhibit 5) On the other hand, Japan, one of their strong markets, seemed to go down. It was the first year they had a negative growth rate in Japan. This report explained some reasons why Hermes started focusing more on China than Japan.

### **Strong Threat of Suppliers and Hermes's Solution**

In March 2012, Patrick Thomas, Hermes International's CEO, stated that their company now has an issue with the price of raw materials. Because cost of importing and producing materials increased during the first quarter, it had a negative effect on the company's operating margin. As sale in France and Europe grew slowly, their revenue in the second quarter was down to 13% from 18% in the first quarter (Nadya Masidlover, 2012).

Australia is known as a big crocodile market. They have a lot of salt water crocodile farms. This type of crocodile grows faster than others and it can grow to lengths of seven meters. The bigger the crocodile, the more valuable it is. Annually, just one fashion house can use about 12,000 skins to produce leather goods. This is a massive demand of crocodile skin. "Crocodile skin is popularly believed to be the finest quality leather available. Equally attractive to serious fashion shoppers are the markings displayed by every crocodile skin that, like human fingerprints, are unique to each animal, meaning that every handbag is slightly different" (Reality Sense, 2009). Hermes has to face a high cost of importing their raw material because of high demands and low supplies. The crocodile only reproduces during the wet season, each female can have no more than 60 eggs. Even under the good environment in a crocodile farm, just a very small number of baby crocodiles can survive and grow enough to provide good quality skin. This fact explained why Hermes has a huge threat of suppliers in luxury industry.

To reduce the threat from suppliers in Australia, Hermes also imported crocodile skin from Singapore. Heng Long, a local Singaporean company, is Hermes biggest partner. This company sells up to 75 percent of Hermes' crocodile skins. Heng Long is known as "one of the five largest croc-



skin tanneries in the world” (Karen Tee, 2012). The price of raw material keeps rising due to expensive and time consuming processes. From a \$250 raw crocodile hide, after tanning and dyeing it, the price will go up to \$1000. It can take up to two months to turn a raw skin to ready-to-use leather. Time consuming processes can double the price of crocodile skins.

Every year, Hermes produces about 3,000 crocodile handbags and their production will continue to grow due to massive demands and a long waiting list from customers. In addition, crocodiles do not rapidly grow to satisfy the demand. That is the reason why Hermes decided to have their own crocodile farm even though it is a risky and expensive investment. (Fudori, 2009)

### **Strongest Competitors in Luxury Industry**

Louis Vuitton is a French fashion company found in 1854. Louis Vuitton is the world most powerful luxury brand with \$19.78 billion of brand value. Louis Vuitton is one of the 50 luxury brands of LVMH group. According to Yahoo Finance, “LVMH Moët Hennessy - Louis Vuitton SA engages in the manufacture and sale of luxury products. Its wine and spirits product line comprises champagne, sparkling and still wines, cognac, and other spirits primarily under the Moët & Chandon, Hennessy, and Belvedere brand names. The company offers fashion and leather goods consisting of trunks, leather goods, ready-to-wear, shoes, watches, jewelry, accessories, sunglasses, and books principally under the Louis Vuitton, Fendi, Céline, and Berluti brand names. Its perfumes and cosmetics product line includes fragrances, make-up, and skincare products under the Parfums Christian Dior, Fresh, and Acqua di Parma brand names. The company also offers watches and jewelry under the TAG Heuer, Hublot, Bulgari, De Beers, and Fred brand names. In addition, it operates retail stores under the brand names of DFS, Miami Cruiseline, Sephora, Samaritaine, and Le Bon Marché for travelers. As of December 31, 2011, the company operated 3,040 stores worldwide. LVMH Moët Hennessy - Louis Vuitton SA is based in Paris, France” (Yahoo, 2012).

The company’s founder is Louis Vuitton who was born in Anchay, France in 1821. At the age of 16, he moved to Paris and apprenticed for Monsieur Marechal which was a luggage and trunk manufacturer. He was a luggage packer for high class family in Paris. This job’s experience helped him have large knowledge about the world of luggage and understand what the travelers’ demand. These knowledge and experiences were extremely useful for Louis Vuitton when he opened his own luggage design company to serve traveling, wealthy people in Paris. According to Biography, “[o]n the first day of tolerable weather in the spring of 1835, at the age of 13, Vuitton left home alone and on foot, bound for Paris. He traveled for more than two years, taking odd jobs to feed himself along the way and staying wherever he could find shelter, as he walked the 292-mile trek from his native Anchay to Paris. He arrived in 1837, at the age of 16, to a capital city in the thick of an industrial revolution that had produced a litany of contradictions: awe-inspiring grandeur and abject poverty, rapid growth and devastating epidemics. The teenage Vuitton was taken in as an apprentice in the workshop of a successful box-maker and packer named Monsieur Marechal. In 19th-century Europe, box-making and packing was a highly respectable and urbane craft. A box-maker and packer custom-made all boxes to fit the goods they stored and personally loaded and unloaded the boxes. It took Vuitton only a few years to stake out a reputation amongst Paris's fashionable class as one of the city's premier practitioners of his new craft” (Biography, 2000).

17 years after arriving in Paris, at the age of 33, Louis Vuitton opened his first store in Paris in 1854. The store mainly designed and manufactured the flat-topped trunks. One of his most important products was “Trianon” trunk. His trunk even was worn by France's Empress Eugenie, wife of Napoleon III. Due to the increasing in demand, Louis Vuitton opened a larger factory in Asnières-sur-Seine in 1860. Louis created many innovative design trunks during the next decade. The first Vuitton trademark was created by Louis and Georges Vuitton in 1888. Louis Vuitton died in 1892.

Louis's son Georges wanted to expand the family business into the worldwide market by displaying Vuitton product in Chicago in 1893. The company also started designing and selling handbags. Georges Vuitton created the classic "Monogram Canvas" design and the company's logo in 1896 to prevent the counterfeiters. The Vuitton family opened the largest travel-good store in the world at that time in Champs-Elysees in 1914. The Vuitton family opened more store in New York, Bombay, Washington, London and Alexandria in 1918. The company also expanded to Japan and eastern countries by opening two stores in Tokyo and Osaka in the late 1970s, one store in Seoul, South Korea in 1984 and its first store in Beijing, China in 1992. The Asian countries were important market for Louis Vuitton with half of its total revenue by 1980s. The company was merged with Moët et Chandon and Hennessy to form LVMH in 1987. Louis Vuitton had opened 130 stores all over the world in 1989. According to Prince, "In 1987, Moët et Chandon and Hennessy, leading manufacturers of champagne and of brandy, merged with Louis Vuitton to form the world's largest luxury goods conglomerate, LVMH. This successful integration of aspirational brands inspired many other companies to do the same. By 1989, Louis Vuitton had opened 130 stores throughout the world. The following year, Yves Carcelle was named president of the company. 1996 marked the centennial of the Monogram Canvas. Seven cities across the world held extravagant parties at stores and Louis Vuitton asked seven prestigious designers to imagine new products in monogram. Azzedine Alaia, Manolo Blahnik, Romeo Gigli, Helmut Lang, Isaac Mizrahi, Syvillia and Vivienne Westwood created seven original and functional objects in limited edition series" (Prince, 2006).

Louis Vuitton have used some different strategies such as opening stores in unsettled markets such as Ulan Bator, the capital city of Mongolia, or selling limited edition product. They also use celebrity, famous models and actresses in their marketing strategy. According to Phenomenon, "luxury analysts and marketing consultants agree that the company has managed to shore up both ends of its market in a way that no other luxury brand—not even Gucci, Hermès nor Chanel—has done. (Vuitton is so canny that it has the solidity to take risks in potentially unsettled markets: It recently opened a store in Ulan Bator, the capital city of Mongolia, which has been betting on mining contracts to bring a rush of wealth to its emerging economy)" (Phenomenon, 2010). The long list of celebrity, famous model and actresses who have participated in Louis Vuitton marketing campaign and often seen with Louis Vuitton's products include Gisele Bundchen, Kate Moss and Naomi Campbell, Jennifer Lopez, Scarlett Johansson, Chloe Sevigny, Lindsay Lohan, Jessica, Ashlee Simpson, Paris and Nicky Hilton and sport star Anna Kournikova and Maria Sharapova.

Louis Vuitton has some similar strategies like Hermes does such as price strategy, service and personnel differentiation, and distribution channel strategy. The price of Louis Vuitton and Hermes' products are only going up. The two companies never ever sell their products with any discounts or lower the price in any circumstances. This price strategy builds up the two companies' brand name and image as the leaders in luxury brands. Louis Vuitton and Hermes deliver a superior customer service. Customer can place special orders or customize their products. Louis Vuitton and Hermes pay well for their staffs that motivated their employees to work harder and deliver the highest quality products and service. The companies give the strict and serious training sessions to all of their employees. Louis Vuitton and Hermes' products are only sold through limited distribution channels. According to Nagasawa, "The likes of LV and Hermès are commended for the fact that they exercise immensely tight control from production to sales and do not produce outlet products. This is because artisans who have been cultivated on their own account are creating them in the company's workshops. If one is able to attain a structure of not buying and not letting others buy its products in stores other than officially sanctioned stores, then performing independent manufacture and independent distribution will increase costs. Even so, this still pays off if you consider this as the cost of maintaining and controlling brand value" (Nagasawa, 2009).

LVMH group is listed on Paris stock exchange as LVMH Moët Hennessy Louis Vuitton. Its stock price was 128.70 EUR in Paris Exchange Market. The company is in great financial position. According to Yahoo Finance, the company's market capital is €63.9 billion and €67.7 billion in enterprise value. LVMH's revenue was €26.33B from Jun 30, 2011 to June 30, 2012. During that period of time, LVMH's revenue per share was €52.8 with 6.86 in EPS ratio and its gross profit was €10.89 billion. Company's net income was €3.44 billion. The most current quarterly revenue and earnings growth are 26% and 28.3%. The company's P/E ratio is 18.76. LVMH currently has €2.74 billion in cash. The company has €8.44 billion of debt that accounted 34% of its equity. LVMH's share currently listed in Paris Stock Exchange Market and S&P500. Its stock price went up 6.18% in Paris Stock Exchange and 11.97% in S&P500 Index for last 52 weeks period. The total share outstanding is 499.03 million shares. The company current annual dividend yield is 2.1%.

In addition, Gucci is also one of the largest competitors of Hermes. Gucci is an Italian fashion and leather goods brand which is owned by PPR, a French company. Gucci Group N.V. designs, manufactures and distributes personal luxury goods. There are four segments operation of Gucci Group: Gucci Fashion and Accessories; Gucci Group Watches; Yves Saint Laurent; and YSL Beaute. Each segment provides different product categories. Gucci Fashion and Accessories sells leather goods, luggage, shoes, clothing, and jewelry. Gucci Group Watches segment provides variety of watches and clocks that were designed with gold, silver and stones, throughout the Gucci and Yves Saint Laurent brands. According to Yahoo Finance, "It operates in four segments: Gucci Fashion and Accessories; Gucci Group Watches; Yves Saint Laurent; and YSL Beaute. Gucci Fashion and Accessories segment provides leather goods, including handbags, small leather goods, and luggage; ready-to-wear; shoes; ties and scarves; and jewelry. Gucci Group Watches segment, through its brands Gucci, Yves Saint Laurent, Bédat & Co., and Boucheron, offers a selection of quartz and/or mechanical watches, and clocks designed with various materials, including gold, silver, and stainless steel, as well as precious and semiprecious stones. Yves Saint Laurent segment's products include primarily women's and men's ready-to-wear, leather goods, and shoes sold under the Rive Gauche label. It also provides men's apparel, accessories, and eyewear. YSL Beaute segment offers Yves Saint Laurent brand perfumes and cosmetics; Roger & Gallet brand toiletries; and Boucheron, Alexander McQueen, and Stella McCartney brand fragrances, as well as perfumes " (Yahoo Finance, 2012).

One of the most famous products of Gucci is luxury footwear for both men and women. The company uses variety of distribution channels from directly operated stores to franchise stores like duty free stores, department stores or outlet stores. Gucci was founded in 1923 by Guccio Gucci. The company headquarter is in Amsterdam, Netherlands. Gucci Group NV was bought by PPR in 2001. Guccio Gucci was born in Florence in 1881. He opened his first luggage store and a leather goods company in Florence in 1921. Gucci and his son expanded the company by opening more stores in Milan and Rome. The company even went to international market when his son, Aldo Gucci opened the first American store in New York in 1953. Gucci started to build its global image as a luxury brand. Guccio Gucci died in 1953 at age 72, few days after the New York store opened. After the death of Guccio Gucci, his sons Aldo, Vasco, Ugo and Rodolfo took over the family business. As a result of its expansion strategy, Gucci opened stores in London, Palm Beach, Paris, Monaco and Beverly Hill in 1960s. Gucci continued its global expansion by opening more stores in Asian countries such as Japan and Hong Kong in 1972. Gucci also expanded its product lines by first introducing ready-to-wear collections besides developing more products in footwear and leather goods segments. Maurizio Gucci, Rodolfo's son, took over the company. He had 50 percent of Gucci's shares. A Bahrain - based investment company, Investcorp, bought 50% of the company's shares in 1987. In 1993, Maurizio Gucci sold his shares to Investcorp. This was the ending of Gucci family's involvement in the Gucci Group. Demenico De Sole became CEO of

Gucci in 1995. He transformed Gucci to a fully public company. Gucci became a strategic alliance with PPR Corporation in 1999. Patrizio di Marco became the company CEO in 2009. Gucci and Reena and Ashok Wadhwa opened a new company together under a joint venture agreement. Gucci accounted 51 percent stake of the new company. Gucci also took another joint venture agreement with Jacopo Focardi, owner of Pelletteria Annalisa, in 2010. Gucci held 51 percent stakes of the new company, GPA, or Gucci Pelletteria Annalisa.

Gucci is the second largest luxury brand in the world after Louis Vuitton. The company had \$3.61 billion in sales in 2010. Gucci is owned by a PPR, a French corporation. Gucci has 345 stores internationally. The company opened 40 stores in mainland China. China market accounted 21 percent of company's revenue. According to Morrisroe, "While one might think that balancing such disparate worlds might be tricky, like satisfying a wife and a much younger mistress, nobody does it better than Gucci. Today it is the second-largest luxury brand in the world (Louis Vuitton holds the top spot), and in 2010 it had \$3.61 billion in sales. Owned by the French conglomerate PPR, also home to Yves Saint Laurent, Bottega Veneta and Alexander McQueen, Gucci has 345 stores internationally, including 40 in mainland China. Gucci entered the China market early, in 1994, and today it accounts for 21 percent of the company's revenue. "What happened in Japan in ten to 15 years is happening in China at an incredible pace," says Patrizio di Marco, Gucci's president and CEO. "You have nouveaux riches that want to show their status and the first step is to have a canvas bag with the original 'GG'" (Morrisroe, 2012). Gucci Group is same with Louis Vuitton. Both companies are fully public firms. They open a mass number of stores around the world. Gucci Group and LVMH have multiple brands. LVMH has almost 50 luxury brands include Louis Vuitton, Christian Dior, TAG Heuer, Hublot, Bulgari and Fendi. Gucci Group also has more than 10 luxury brands include Yves Saint Laurent, Bédar & Co., and Boucheron. Gucci and Louis Vuitton are different with Hermes. About 75 percent of Hermes stakes are held by private people. Hermes is not a fully public company. Hermes also opened much less stores than Gucci and Louis Vuitton did. Hermes does not have multiple brands like Gucci. Gucci has strong position in luxury industry due to its strong brand image, quality products and international presence. Gucci Group's strategy is expanding to developing countries to have access in new market such as India, Vietnam, Thailand or South American. These developing markets are the huge opportunity for Gucci Group due to the high number of population and the increasing of income in these countries.

According to Yahoo Finance, Gucci Group currently listed in OTC Markets under code GUCG. The company's share price was \$140 per share. The company market capital is \$14.15 billion with the enterprise value of \$14.27 billion as November 2, 2012. In 2004, Gucci's revenue was \$3.35 billion. Its net income was \$225.6 million in 2004. The company had \$2.14 billion in cash and the total debt over equity ratio is 51.91 percent. The company's stock price has increased 13.91% over last year. Gucci Group had 101.11 million shares outstanding.

Channel S.A. is one of the main competitors of Hermes International. Channel S.A. is a private French fashion design and cosmetics company. Channel S.A. was found in 1909 by Gabrielle "Coco" Chanel. The company's headquarter is in Neuilly sur Seine, France. The company sells fashion, jewelry, eyewear, watches, clothing and cosmetics products such fragrance, makeup, beauty products through its department stores and specialty stores. The company also offers an online boutique. Channel S.A. has more than 160 boutiques around the world. The company opened its stores in Asia, Europe, North America, South America, Oceania and the Middle East. Channel is one of the leaders in the perfumes and cosmetics products. Chanel No.5 has been the world's top selling perfume for long time. The company currently held by Alain Wertheimer and Gerard Wertheimer. According to St. James, "Chanel SA is one of the legendary names in perfumes. The company has parlayed its prestigious brand name into a world-leading retail empire. In addition to its flagship perfume brand Chanel No. 5--which has long been the world's top-selling perfume--Chanel

has expanded its line to include women's fashions, jewelry and accessories, handbags, leather goods, and other products. Chanel has also begun building up a portfolio of luxury brands, including gunsmith Holland & Holland and high-end French bathing suit maker Eres, bought in 1997. In 2002, rumors began circulating of a possible marriage with the famed house of Hermès. During the new millennium, Chanel has stepped up its purchases in the luxury sector, acquiring A. Michel et Cie, exclusive hat maker for the haute couture set and the famed Les Broderies Lesage, which provides embroidery for the haute couture industry. These acquisitions complement the company's existing fashion industry holdings, such as the Lemarie, a flowers and feathers craftsman and Desrue, producer of buttons. Meanwhile, Chanel has been attempting to break into the skin care segment, launching its own line under the Precision brand. Chanel SA is a private company wholly owned by the Wertheimer family. The company's revenues are estimated to top EUR 2 billion per year” (St. James, 2003).

Chanel S.A. most famous product is perfume No.5 de Chanel. Coco Chanel created perfume No.5 in 1921 which was first sold in 1922. After the success of perfume No.5, Coco Chanel continued expanding perfume product lines.

Chanel S.A. opened more than 40 stores worldwide during the 1980s. The company sold high price and super luxury products such as \$200 per ounce perfume, \$11,000 dresses and \$2,000 handbags. Chanel S.A. continued to introduce new products such as Chanel watches, high-priced clothes, and cosmetics during 1990s. The company continued expanding with purchasing high-end swimsuit maker Eres in 1997 or acquiring watchmaker Bell & Ross in 2001. Chanel S.A. still expands its number of store worldwide during 2000s. The company opened a new jewelry and watch and one 1,500 square foot handbag and shoe store on Madison Avenue in New York City. Chanel S.A. opened 25 stores in the United States. The company also opened more store in Asian countries such as Japan, Hong Kong and China. According to St. James, “Chanel continued to expand its retail holdings at the beginning of the century. In 2001 the company's U.S. subsidiary launched a new retail concept, featuring only accessories bearing the Chanel name. In July 2002 the company rolled out a new jewelry and watch flagship store on New York's Madison Avenue, and expected to build up these sales with the expansion of its network of independent retailers. Shortly after, the company opened a new, 1,500-square-foot handbag and shoe flagship store next door to its jewelry and watch store in New York, bringing the total number of Chanel stores in the United States to 25. The company also targeted the Far East, opening a new 2,400-square-foot boutique in Hong Kong, and paying nearly \$50 million to acquire a building in Japan's Ginza shopping district. After 80 years, the Chanel name continued to attract customers from around the world” (St. James, 2003). The company estimated revenue is about \$1.8 billion. Chanel S.A. has 1,220 employees. Chanel S.A. is one of the strongest competitors of Hermes International because the company has great brand image, high quality products and excellent management. Chanel S.A. competes directly with Hermes International in luxury clothing, accessories, watches and leather goods such as handbags and wallet. However, Chanel S.A. outperforms Hermes International in cosmetic and perfume products. Chanel S.A. is one of the top ten cosmetics makers in the world. The company's cosmetic revenue is \$413 million in 2002. Chanel S.A. was the seventh largest fragrances maker in the world with revenue of \$570 million in the world in 2000. The company's No.5 perfume is the top selling perfume worldwide. The company held 2.8 percent of fragrances sector in 2000.

According to Encyclopedia, “Despite its status as one of the top ten cosmetics makers in the world, Chanel held only 1.2 percent of the global cosmetics market in 2000, compared to the 16.8 percent held by leader L'Oreal SA. Chanel's cosmetics sales that year totaled \$413.3 million. The firm was also the world's seventh-largest maker of fragrances, with sales of \$570.4 million and a market share of 2.8 percent in that sector in 2000” (Encyclopedia, 2002). Chanel S.A. uses the same marketing strategy with LVMH. The company has a group of model, actress and celebrity which is

called the Chanel Girl. The company uses model, actress and celebrity for its marketing campaigns. The Chanel Girl includes Lindsey Wixson, Bianca Balti, Toni Garrn, and Sasha Pivovarova.

Another dangerous competitor that all high-end brands have to deal with include Hermes is replica products. As following differentiation strategy, Hermes has to take some risks and great difference in prices is one of them. Not all of customers are extremely wealthy to afford a \$5,000 handbag or \$400 scarf. High priced products create opportunities for replica merchandise to exist. Instead of spending too much money for a handbag, buyers now can buy a duplicate one which is normally look and feel similar to the authentic product. To distinguish today's replica handbag from the real one with naked eye is no longer easy because the duplicate items also have number-coded key and closure, or authentic certificates. These facts have negative effect to customers' behaviors. "Why do I have to pay hundred times more expensive for an item that looks almost the same?" question is asked and lead buyers to black market and purchase duplicate products. According to market statistic, there is only 1% of Louis Vuitton handbags are authentic. This situation is a very strong threat to all of the luxury brands includes Hermes. They have to spend a lot of money for copy right to protect their designs but it is impossible for them to wipe away the duplicate products in black market where both buyers and sellers are beneficial.

### **What made Hermes success?**

According to the Bloomberg report in May 2012, Hermes is the second strongest brand in the luxury industry with \$9.1 billion in earnings. (Teofilo Killip, 2012) "During holiday seasons, a Hermes scarf is sold every 20 seconds in the Paris Hermes boutique" (Tie-a-scarf.com, 2012). Hermes's brand is a valuable, rare, and precious intangible asset that is costly to imitate. They have a variety of product lines such as: leather goods, silk, clothing, watches, perfumes, etc. All of them have their own strengths and create a great contribution to Hermes's total revenue and net income. Their handbags are fashionable, durable, and made with excellent quality. Customers can rarely get the same quality from other competitors. Extremely wealthy customers feel satisfied with their purchase because Hermes's merchandise is very prestigious. Hermes's products will never go on sale or be discounted so their value will be retained from the day they were purchased until the day they were sold out in stores. Hermes International not only cares about the quality of their products but also about the tastes of their customers. They always provide items with different colors so their customers can have more choices and options.

In addition to superior variety, Hermes Company offers one of the best customer services to their buyers. Anyone who stops by a Hermes location will first be greeted by friendly and helpful sales employees. They will assist the customer in finding the products he or she needs. Hermes's stores also offer many options for customers. They can ask to customize the items to meet their desires. Hermes's after-sale service is even better. Kelly is the name of Hermes's most popular handbag. "It has a lifetime warranty. You can send your handbag back to a Hermes workshop in Paris at any time and it will be refitted and returned to you like new" (French Girlin Seattle, 2011). This awesome service is the reason why customers keep coming back to Hermes even though their products are extremely expensive compared to other brands.

Hermes also has a strong financial position. Their revenues increased every year from 2008 to 2012. Their stock price on September 24<sup>th</sup> 2012 was €213.40 per share which is high compared to other companies. Hermes's distribution network is also one of their competitive advantages. They have about "5,632 Women's Accessory & Specialty Stores" (M.L. Cohen, 2011) all over the world which is a huge distribution network that costly and difficult for other competitors to imitate.

Independent supply is also one of the competitive advantages that Hermes possesses. They have their own crocodile farm which brings them high quality materials with cheaper prices. This resource is valuable, rare, and costly to duplicate. Hermes also has loyal customers who do not mind

buying expensive items with long waiting times. A lot of extremely rich customers prefer to own a \$7,000 to \$140,000 Birkin Bag even though they have to wait up to 6 years or longer. This fact proved how loyal Hermes's customers are. They do not mind waiting for a long time to get the products that they want because they know it is worth it.

According to Hermes's annual presentation in 2011, their investment grew rapidly from €154 million in 2010 to €214 million at the end of 2011. Despite bad economy situation, Hermes International had a strong financial situation. While a lot of big companies in Europe had big debts, Hermes still retained a large amount of cash at about €1,048 million as of December 2011.

Hermes created a great competitive advantage by knowing how to control human resources. A massive demand from all over the world causes Hermes to increase the number of craftsmen to maximize their capacity. During 2011, they hired 715 employees in the areas of production and management. Hermes is known as a fantastic working environment because of high safety standards and a very professional atmosphere. Hermes also pays their employees well enough to keep them working hard and passionately for their company.

Hermes also has an excellent store distribution network. From 2007, they only had 267 stores in total. In the end of 2011, they already had 328 stores which included 123 concessionaries and 205 branches (Exhibit 6). They are opening a store in Mumbai and Geneva, and working on the construction of Hermes House in Shanghai. Hermes did a good job in expanding their distribution network throughout the world. They did it step by step to avoid unnecessary risks and wasteful spending. Everyone from all over the world now knows about Hermes' logo, brand name, and products.

### **Leadership-the key of success**

Hermes International Company has 12 members in their Supervisory Board. Éric de Seynes, and Jérôme Guerrand both hold Chairman and member position. Maurice de Kervénoaël and Ernest-Antoine Seillière are Hermes's Vice-presidents. The rest members of Supervisory Board are Charles-Éric Bauer, Matthieu Dumas, Julie Guerrand, Olaf Guerrand, Renaud Momméja, Robert Peugeot, and Florence Woerth. "The Supervisory Board exercises ongoing control over company management. The Supervisory Board determines the proposed earnings appropriation for the financial year to be submitted to the Annual General Meeting. The Active Partner is jointly and severally liable for all the Company's debts, for an indefinite period of time. The Active Partner has the authority to appoint or revoke the powers of the Executive Chairmen, after receiving the considered recommendation of the Supervisory Board. The Active Partner makes all decisions pertaining to the Group's strategic options, consolidated operating and investment budgets, and recommendations to the General Meeting with respect to the distribution of share premiums, reserves and retained earnings, on the recommendation of the Supervisory Board" (Hermes Annual Report, 2011). Hermes' Active Partner's members are included Émile Hermès SARL (Management Board, Bertrand Puech (Executive Manager, Chairman and Member of the Management Board), Philippe Dumas (Vice-Chairman), Hubert Guerrand (Vice-Chairman), Henri Louis Bauer, Sandrine Brekke, Frédéric Dumas, Édouard Guerrand, Agnès Harth, Laurent E. Momméja, Pascale Mussard, Guillaume de Seynes.

There are two different Executive Chairmen who works for Hermes which are Patrick Thomas and Emile Hermes SARL. Their task is to manage the group management and follow its common interest. "Hermès International's executive management is comprised of the Executive Chairmen and the

Executive Committee, which consists of six Managing Directors, each of whom has well-defined areas of responsibility. Its role is to oversee the Group's strategic management" (Hermes Annual report, 2011)

## **Improvement in Advertising Strategy**

While other competitors are producing a lot of different advertising strategies, Hermes seems to not focus much on their advertising. Understanding customers' behaviors, Louis Vuitton produces excellent advertising plans by signing contracts with different actors and actresses to advertise for their products. A new collection will be highly desired if it is used by someone who is famous, fashionable, and attractive. In June 2011, "Hollywood actress Angelina Jolie strikes a pose in Cambodia for Louis Vuitton's 'Core Values' campaign" (White, 2011).

Learning from this experience, Hermes should start generating a better advertising strategy. Having products named after well-known people is not attractive enough to persuade customers to make a purchase decision. They should have some contracts with famous actors, actresses, politicians, or singers. Hermes's advertising will vastly improve when these individuals appear more in the media. Young adults and teenagers now are affected a lot by celebrities. These individuals will mimic the shopping behaviors of their favorite singers or actors in the near future.

This advertising strategy is a general plan that will be customized to different locations. Each target market has different people who have influence on customers. In Korea, using Angelina Jolie to endorse Hermes's products is not as good as using Park Jae Sung who is really famous with Gangnam Style performance. People now tend to skip reading advertisements in newspapers and watching them on television, so sometimes it is not necessary to use those types of media. Asking famous stars to use Hermes handbags, wallets, or accessories at important events, in movies, and music videos will be a fast way to bring Hermes's products closer to their customers. Choosing the right person, at the right location, and with the appropriate media will be the key to make this advertising strategy successful.

## **More Stores-More Customers**

In addition to a better advertising strategy, Hermes also needs to have a better growth strategy. China is a potential market that will bring high revenue for luxury brands without taking too much risk. This location is promising for all the luxury companies including Hermes International. It means Hermes will have fierce competition from other companies which are entering China as well. That is the reason why investing money and expanding into China will bring Hermes higher levels of revenue but not guarantee a better profit. Hermes should take some risks and enter other markets besides China. There are lot of countries that Hermes does not have any store there such as Vietnam, Laos, etc. where a lot of rich people are willing to pay huge money for their products. Hermes should spend more money on market research to open and expand more stores like other competitors. Louis Vuitton has stores in about 65 countries and they still want to open more. 2013 will be a good moment for them to enter new market after a healthy growth in financial. They also have great cash amount which is ready to invest. In the end of 2011, they have about 100 million euros available in their account.

Limited in store location is their only issue. Limited in opening time is also one of their problems. In New York City, people are working during weekday and only have time to go out and shopping during weekend. While all most all of the stores try to open longer time during the weekend to increase revenue, Hermes's store closes both on Saturday and Sunday. This store hour does not make sense at all. Hermes will lose their customers due to this unreasonable opening time. When customers go to a store for shopping and get disappointed because of inconvenient store hours, they will not want to come back for the second time. Hermes accidently loses their potential customers to other competitors without knowing it. Studying from this fact, Hermes not only should focus on expanding stores by quantity but also improving store hour more suitable with customer's shopping behaviors.



### **Create Partnership, Avoid Competition, and Increase Product Line**

Contacting Louis Vuitton and become a partner with Hermes is not a bad development plan. This partnership will eliminate their toughest “army” and create a great partner for Hermes International. It will help both of them to become the strongest luxury brand all over the world and almost unbeatable. Right now, Hermes only wants to build their company under a family size without any control from other stakeholder. They do not expect Louis Vuitton buy their stake and build it big enough to control their private company. Hermes feels that they will lose their control power if Louis Vuitton tries to swallow them. According to The New York Times, David Jolly wrote Hermes “is accusing LVMH of insider trading and share-price manipulation as it built its stake in Hermes from zero in 2000 to 17.1 percent in 2010. Mr. Arnault acquired those shares with the aid of opaque financial instruments that allowed him to shield his growing acquisition from the market and from Hermes. LVMH has since raised its stake to more than 22 percent, giving it 16 percent of the voting rights. To ensure that Mr. Arnault cannot further increase his portion, the family created a holding company giving it the first right to buy any shares that family members choose to sell” (Jolly, 2012). This is not the time for Hermes to raise a battle with Louis Vuitton. Create a partnership is a better way to solve problem than get involve in law suit. Hermes can sit down and discuss with Mr. Arnault to make sure that the acquisition of his stake is completely legitimate. They also need to have a better stake management to ensure that they always have the strongest control power to Hermes International. Competing with someone who is stronger than yourself at a bad time will have bad consequences to Hermes.

Beside problems with competitors, Hermes also gets involved in a lot of environment concerns. Many animal protection organizations warned Hermes about killing animals to get skins is unethical and will not last long. Instead of ignoring this warning, Hermes should invest more money on research and development to look for other alternative materials rather than animal’s skins. This project will take long time but till help Hermes survive better when customers start boycotting real leather goods due to ethical concerns.

Every collection or design of Hermes cost them a lot of time, money and human resource. To protect them, Hermes is willing to pay a lot of money to protect their own intangible assets which are their intellectual property rights such as brand name, trademark, logo and patent. In 2011, “the shapes of the Kelly and Birkin bags have been registered as three-dimensional trademarks in France and in other countries” (hermes.com, 2011). Cannot use Hermes name in Chinese is a good lesson for Hermes. From now to so on, they will be more careful with this sensitive area and be ready to purchase their name in different languages in order expand their distribution all over the world.

Opening more stores is not only one important task that Hermes needs to do right now. They also have to increase the number of product lines. Extreme rich consumers not only shop for themselves but also for their family members and their pet. Wealthy people even spend more money on their kids than themselves. Jennifer Lopez’s bought \$2,400 worth of Chanel accessories for her 4 years old daughter (Abraham, 2012). Or “The daughter of Tom Cruise and Katie Holmes is famous for her varied and expensive clothing, valued at \$3 million” (Searchgi.com, 2012). It is obviously that investing on kids’ clothing and accessories right now can bring to luxury companies a lot of money and Hermes will not be an exception.

Talking about Hermes items for pets, they only have couple designs of dog carriers which do not fulfill customers’ demands. People now spend a lot of money to buy clothes, or accessories for their pets so Hermes should take some risk to enter more in this market. For example “In the seven years she’s had her diva dog, Louise has splashed out more than £100,000 on all sorts of extravagant treats” (Mirror.co.uk, 2011). Pets’ items will be a gold mining market for Hermes in the near future

if they willing to take risks, spend time and money to do research and development about it. Their starting point will be study about qualifications that customers are seeking such as price range, color, sizes, or styles. Then, hire special designers who have good experience in pets' collection to start with ideas, models, and materials. From that, Hermes can start production and distribution process.

While other competitors such as Burberry or Channel have their own cosmetic products, Hermes has not invested any money in this market yet. This project contains many risks to them because they do not have any experience about this type of merchandise. In order to produce it, they not only have to spend a lot of money to hire more experienced employees and build manufacture, but also wait for long time to receive the reaction from customers. To avoid these unnecessary risks, Estee Lauder Company is a promising partner that Hermes can work with. In the most recent report, Estee Lauder's net sales in 2012 is \$9.7 billion which grew two times faster than the global prestige beauty (Estee Lauder, 2012). They have a large contribution network in The Americas, Europe, Middle East & Africa, and Asia/Pacific. The Americas as always is their target markets where contributes about \$4,000 million in net sales for Estee Lauder in 2012. This company has more than 5 product categories such as skin care, makeup, fragrance, hair care and other. Their most popular product lines are skin care and make up which created more than \$1,200 million in operating income. It is a perfect combination where both sides have their own benefits. M.A.C is a high quality and famous brand of Estee Lauder Company which was purchased from Frank Toskan and Frank Angelo in 1998. In the beginning, this brand focused on designs for professional makeup artists but right now, it is a worldwide brand where every buyer can buy. Compare to other cosmetic brand, M.A.C has higher price with much greater quality so they already success with a massive demand from market. Create a partnership with M.A.C, Hermes will have no need of new employees, or manufacture but still own a cosmetic product line. M.A.C is a well-known brand enough to promise good revenue in near future. On the other hand, Hermes will bring M.A.C from a consumer good market to luxury market without wasting time and money. This new product line will need to be extremely attractive, high price, and has excellent quality to fulfill the desire of wealthy customers. These products will be named under Hermes instead of M.A.C's brand.

### **Bright and Successful Future of Hermes International**

Even though Hermes is a family company, they have an excellent leadership which most is Hermes family members except their Chief executive officer, Patrick Thomas. In May 2012, "HERMÈS has named a new CEO, enlisted from within the family that controls the label. Patrick Thomas, the current chief executive officer of Hermes, announced at the annual shareholders' meeting today that Axel Dumas- a member of the sixth generation of the Hermes family - will succeed him upon his retirement. Dumas, currently chief operating officer, will become joint CEO and COO from next month - and will work alongside Thomas during a transition period" (Milligan, 2012).

This might not be a good decision for Hermes International Company. Having someone who is not a Hermes family members will bring to their company more creative views and opinions. It is easily to understand that Hermes does not want to lose control power to a stranger that does not belong to their family but they absolutely can find someone to work for them as a CEO and still under their control. Considering hiring someone to replace Patrick Thomas beside Axel Dumas will be a better idea. Besides changing in leadership, Hermes also needs to add some more divisions to work with kid and pet projects. It is not a smart choice to put it under leather or ready to wear divisions because they serve different target customers.

During 2010-2012, Hermes has some issues with Louis Vuitton and tries to prevent this company to swallow Hermes. It is the time that Hermes should partner with another strong luxury brand such as Gucci who they at least they can trust and do not try to talk the controlling power

from them. Even Hermes is a famous brand, they are still a family company with much smaller size in physically and financially so trying to compete with someone stronger will only harm to their business. Besides changing in partnership, in the end of 2013, Hermes will find them successfully entering kids and pets' clothing and accessory market. It will bring to Hermes's revenue at least couple hundred million euros. It is a good start and will develop more in near future. By 2013, when Patrick Thomas already retired, Axel Dumas will become Hermes's Chief executive officer. He will bring new leadership to the whole company and start new project about alternative materials. Axel will invest more money to look for other raw materials to replace crocodiles' skin. This plan not only help Hermes get rid of environment problems but also reduce cost of goods sold. The more they depend on suppliers, the higher price they have to pay for materials.

**Exhibit 1**

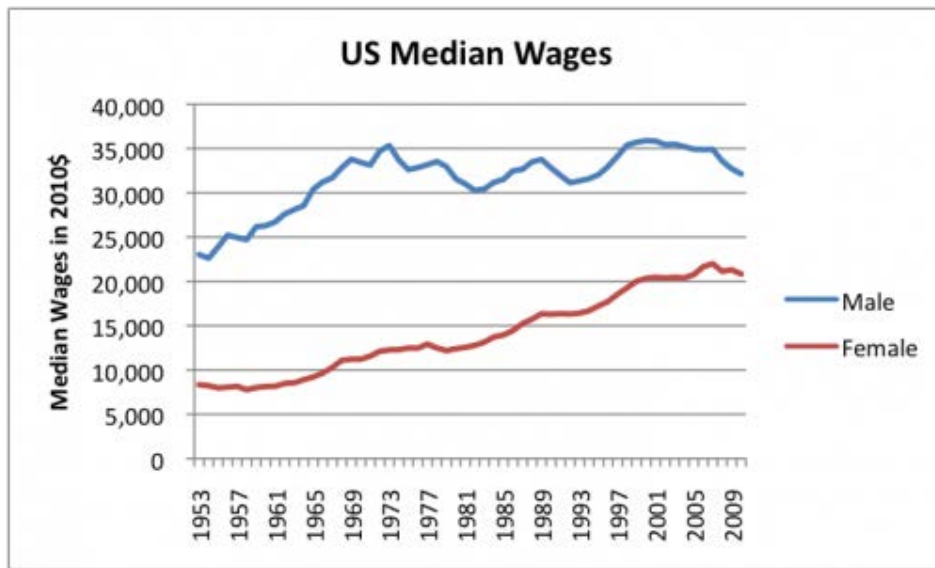


Figure 10. US Median Wages, separately for males and females, in 2010\$.

Exhibit 2

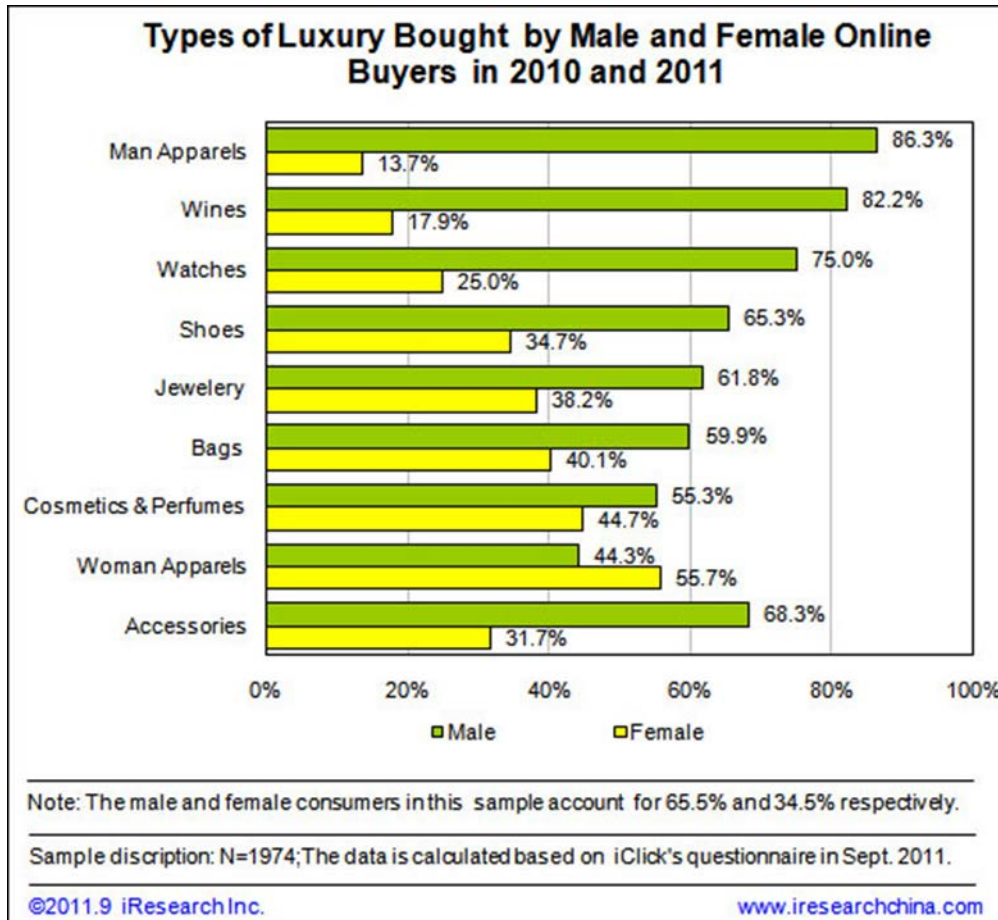


Exhibit 3

# GENERAL ASSESSMENT OF THE YEAR 2011

## INFORMATION BY SECTORS 2011 / 2010

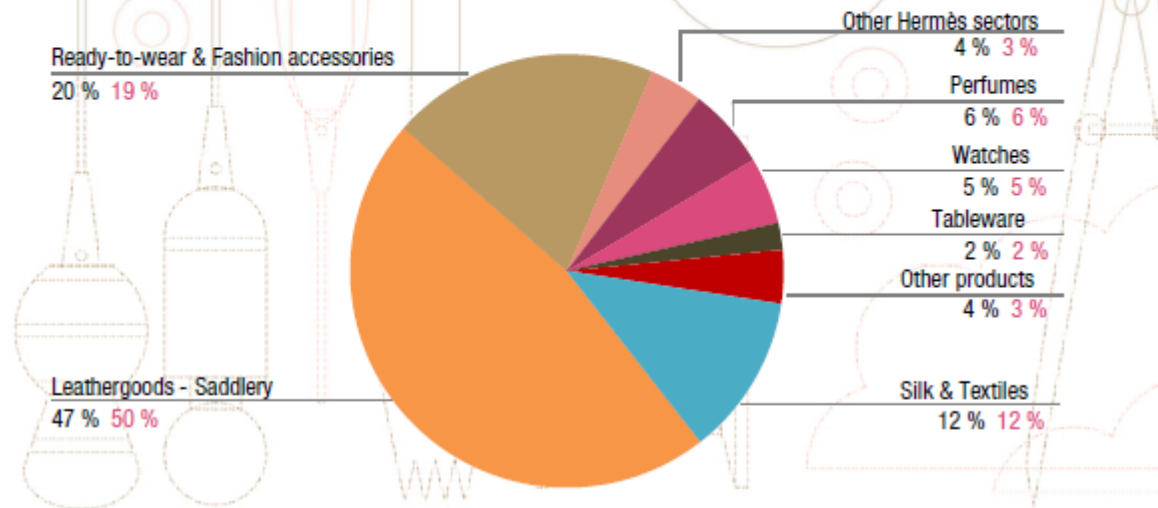


Exhibit 4

# GENERAL ASSESSMENT OF THE YEAR 2011

## BREAKDOWN OF SALES IN 2011 / 2010

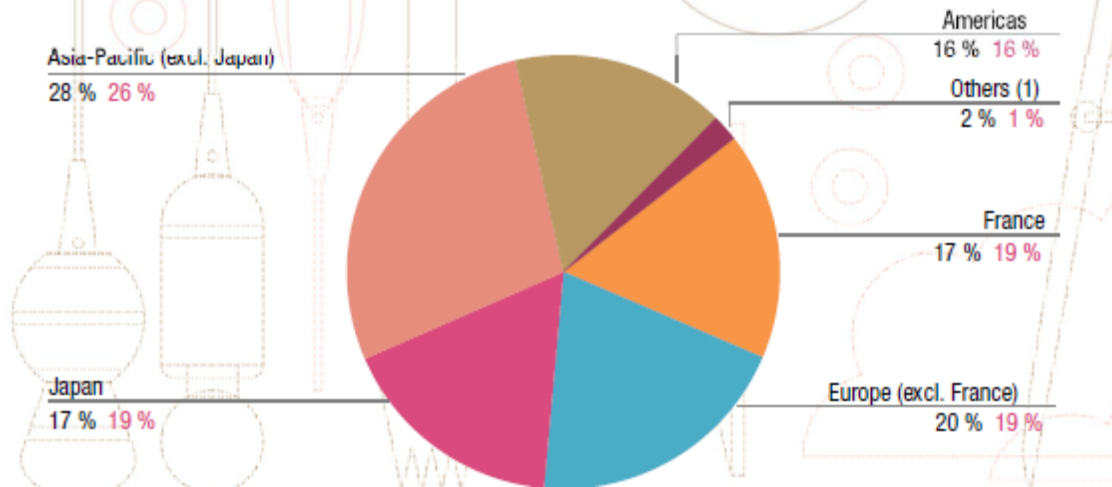


Exhibit 5

# GENERAL ASSESSMENT OF THE YEAR 2011

## STRONG GROWTH IN ALL GEOGRAPHICAL AREAS EXCEPT JAPAN

### ACTIVITY BY GEOGRAPHICAL AREAS

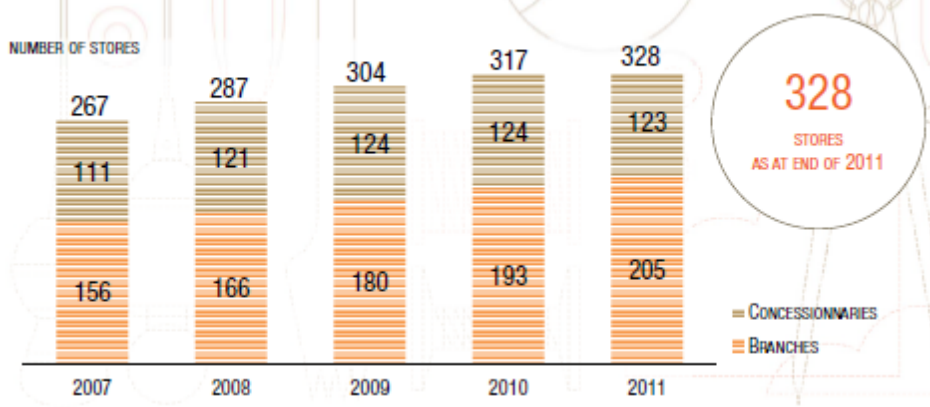
CHANGES AT CONSTANT RATES  
2011 / 2010

FRANCE	+ 13.2 %
EUROPE (EXCL. FRANCE)	+ 19.3 %
AMERICAS	+ 25.8 %
ASIA-PACIFIC (EXCL. JAPAN)	+ 29.4 %
JAPAN	- 0.7 %
OTHERS*	+ 35.9 %

(\* including sales to airline companies)

**Exhibit 6**

**2011 : THE PACE OF STORE CREATIONS REMAINED SUSTAINED**





## Exhibit 7

### KEY STOCK MARKET DATA

	2011	2010	2009
Number of shares as at 31 December	105,569,412	105,569,412	105,569,412
Average number of shares (excluding treasury shares)	104,556,945	105,162,445	105,128,870
Market capitalisation as at 31 December	€ 24.32 Bn	€ 16.54 Bn	€ 9.85 Bn
Earnings per share (excluding treasury shares)	€ 5.68	€ 4.01	€ 2.75
Dividend per share	€ 7.00 <sup>1</sup>	€ 1.50	€ 1.05
Monthly average daily trading volume	86,174	124,790	117,933
12-month high share price	€ 272.50	€ 207.75	€ 106.70
12-month low share price	€ 142.05	€ 92.00	€ 64.84
12-month average share price	€ 200.23	€ 125.67	€ 92.91
Share price as at 31 December	€ 230.35	€ 156.75	€ 93.31

## Exhibit 8

### CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2011

#### ASSETS

(in millions of euros)	31/12/2011	31/12/2010
<b>Non-current assets</b>	<b>1,377.1</b>	<b>1,354.8</b>
Goodwill (Note 10)	38.7	37.2
Intangible assets (Note 11)	96.7	75.2
Property, plant & equipment (Note 12)	869.4	774.2
Investment property (Note 13)	98.8	98.3
Financial assets (Note 14)	29.8	151.7
Investments in associates (Note 15)	12.9	14.3
Loans and deposits (Note 16)	35.0	24.3
Deferred tax assets (Note 8.3)	194.2	178.1
Other non-current assets (Note 18)	1.7	1.5
<b>Current assets</b>	<b>1,871.3</b>	<b>1,563.8</b>
Inventories and work in progress (Note 17)	534.5	468.6
Trade and other receivables (Note 18)	175.7	159.0
Current tax receivables (Note 18)	0.8	1.1
Other current assets (Note 18)	94.4	69.5
Fair value of financial instruments (Note 22.2.3)	17.7	21.7
Cash and cash equivalents (Note 19.1)	1,048.2	843.8
<b>TOTAL ASSETS</b>	<b>3,248.4</b>	<b>2,918.6</b>

The note numbers refer to the Notes to the Consolidated Financial Statements in Volume 2 of the 2011 Annual Report.

#### EQUITY & LIABILITIES BEFORE APPROPRIATION

(in millions of euros)	31/12/2011	31/12/2010
<b>Equity</b>	<b>2,325.5</b>	<b>2,163.2</b>
Share capital (Note 20)	53.8	53.8
Share premium	49.6	49.6
Treasury shares (Note 20)	(304.1)	(33.0)
Reserves	1,881.2	1,621.3
Foreign currency adjustments (Note 20.1)	67.1	42.7
Derivatives included in equity (Note 20.2)	(29.1)	(5.9)
Net income attributable to owners of the parent (Note 3)	594.3	421.7
Non-controlling interests (Note 21)	12.7	12.9
<b>Non-current liabilities</b>	<b>147.6</b>	<b>130.8</b>
Borrowings and debt (Notes 22.3 and 22.4)	18.4	17.9
Provisions (Note 23)	14.5	14.4
Post-employment and other employee benefit obligations (Note 25)	60.8	56.3
Deferred tax liabilities (Note 8.3)	17.5	12.1
Other non-current liabilities (Note 26)	36.4	30.1
<b>Current liabilities</b>	<b>775.3</b>	<b>624.6</b>
Borrowings and debt (Notes 22.3 and 22.4)	20.5	26.0
Provisions (Note 23)	28.8	31.0
Post-employment and other employee benefit obligations (Note 25)	6.2	6.2
Trade and other payables (Note 26)	299.7	234.6
Fair value of financial instruments (Note 22.2.3)	58.3	30.1
Current tax liabilities (Note 26)	89.9	76.3
Other current liabilities (Note 26)	271.9	220.3
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>3,248.4</b>	<b>2,918.6</b>

The note numbers refer to the Notes to the Consolidated Financial Statements in Volume 2 of the 2011 Annual Report.

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## Hermes International Case Analysis

Hermes International Company is the second strongest brand in luxury industry. They have spent more than 100 years to make Hermes name as famous as today. With 3,000 million euro in average revenue, Hermes has a very strong financial position and potential growth compare to other competitors. Their products are always well-designed, high quality, and fashionable. They do not make good products but extremely good ones. Hermes' target customers are wealthy people who have high level of income and are interested in luxury items. With more than 300 stores all over the world, Hermes is working on their ways to expand their distribution network and make their products available more in different markets.

Besides the threats of strong competitors such as Gucci or Louis Vuitton, Hermes International has to deal with replica products which are selling with a huge amount in black market. These duplicate products have negative effect to Hermes not only in sales revenue but also in brand image. For now, all luxury brands are still looking for the solution for this problem.

With a great system of management, Hermes has achieved a lot of success. Patrick Thomas's leadership helped Hermes expand a lot in Asian countries and will expand more in the near future. He also decided to have their own crocodile farm which reduces cost of raw materials and threat from suppliers. Due to using massive amount of crocodile's skin, Hermes also has unsolved problem with animal protection organizations. This unethical production will also harm to Hermes's image and create negative reaction from some parts of consumers.

### **1. What are some pressing key issues? What is the most critical general environmental dimension? What does the industry look like?**

Hermes International Company has some major issues that they need to solve as soon as possible. Louis Vuitton is one of their issues. Understand how successful Hermes is, Louis Vuitton try to "swallow" this company by buying more and more Hermes's stake. From 2000 to 2010, LVMH has since raised its stake to more than 22 percent, giving it 16 percent of the voting rights. Hermes did not have any early action to prevent this issue to happen until 2011. Hermes decided to sue Louis Vuitton about purchasing stakes which are not legitimate. This is not a smart move of Hermes. First, Louis Vuitton is a big and experienced company who is smart enough to prove all of their Hermes stakes are legitimate. Second, Hermes should not compete with a stronger and bigger competitor alone. Hermes is only a family company with small size in both production and finance. They should look for other strong competitor such as Gucci Corporate to create a partnership. This way will help Hermes strong enough to protect themselves from Louis Vuitton's bad intention.

In addition, a small distribution network is also one of their issues. Even though Hermes has a very strong brand name, their products and stores are still not available all over the world. This absent creates an invisible distance between them and their potential customers. As Hermes's healthy financial situation, they should find a way to expand more and make their brands closer to extremely wealthy customers who are desired to own their products.

The luxury industry is an attractive one which has high entry barriers, few threats of substitutes and new entrants, weak power of buyers, moderate rivalry among competitors and moderate power of suppliers. It is not easy for a new firm to start in luxury industry due to strong rivalries such as Louis Vuitton, Hermes, Gucci, Chanel, etc. It required new entrant to have large amount of well-trained craftsmen and great distribution network. These requirements not only cost a lot of money and time to do. In addition, the power of buyers in this industry is low because they have high level of income, and they do not mind paying high price or waiting for long to get the products they want. Luxury brands usually do business follow differentiation strategy. Their products are different from each other and offer special features that customers cannot find the

similar between brands. The power of supplier will be a threat for new entrant but not strong rivalries like Hermes or Gucci. Heng Long company is “one of the five largest croc-skin tanneries in the world” (Karen Tee, 2012). Louis Vuitton now purchased enough shares of this company to have strong power to control this important supplier and make it to become their advantages. The power of this supplier is now longer a threat to Louis Vuitton. Hermes also found their ways to reduce supplier’s power. They built their own crocodile farm and become supplier for themselves. Due to these facts, the power of supplier in luxury industry is from moderate to low. Luxury industry clearly is an attractive one.

**2. What are the firm’s strengths and weaknesses? What does the firm have a sustainable competitive advantage in? Who should the firm pursue a joint venture with?**

<b>Strengths</b>	<b>Weaknesses</b>
High quality products and services	Extreme expensive products
Good distribution network	Limited in production
Effective research and development department	Does not offer opportunity for private retailers
Second position in top ten luxury companies	Less stores than other strong competitors
Great skilled craftsmen	Brand still not available in so many countries
Healthy financial position	
Have their own crocodile farms	

Hermes has a sustainable competitive advantage is Hermes family’ experiences.

	Valuable	Rare	Costly to imitate	Non-substitutable
Hermes Family’s Experiences	Yes	Yes	Yes	Yes

Hermes International is a private company which is running by Hermes’s family members so it creates a great management system. Hermes family has long time experience working within the luxury industry. They know how to produce excellent products which satisfy customers’ desire. These experiences were passed and improved from the 1900 until now. They are not only valuable and rare but also very costly to imitate or even impossible. No other competitors can make a Hermes family member to come to work for them and share their experiences of production processes. And nothing can substitute these experiences.

To be stronger and able to compete with Louis Vuitton Hermes should pursue a joint venture with Gucci Corporation. While Hermes has many experienced craftsmen and extremely high quality products with great design, Gucci is a strong luxury brand which has huge distribution network, and solid financial situation. Hermes International also can joint venture with Make-up Art Cosmetics (M.A.C). M.A.C is known as one of the greatest cosmetic producer in the world. This partnership is not only helping Hermes have their brand now product line that they have never had before. High end cosmetics have a very large and potential demand. It will increase Hermes’s revenue without costing them money to build new manufacture and hire more employees. In additional, it will bring M.A.C from consumer goods industry to luxury industry, and make this brand become much more valuable.

	<b>Joint Venture with Gucci</b>	<b>Joint Venture with Make-up Art Cosmetics (M.A.C)</b>
<b>Potential benefits:</b>	Start producing kid clothes product line. Gucci's huge contribution network can bring Hermes's brand name all over the world.	Producing high end cosmetics. Helps Hermes to have a brand new product line without having new manufacture and employees. Brings M.A.C from consumer goods industry to luxury industry.
<b>Costs:</b>	Need to spend about \$100,000 to design and look for new materials	N/A
<b>Risks:</b>	Gucci might want to "swallow" Hermes like Louis Vuitton	M.A.C brand might bring down Hermes's image.
<b><i>Should move ahead?</i></b>	yes	yes

### **3. What is the firm's business-level strategy? Is the firm using a blue ocean strategy?**

Hermes's business-level strategy is differentiation. They provide non-standardized products and services. For example, if you purchase a Kelly or Birkin handbag from Hermes, you will not only enjoy a high quality, fashionable and limited edition product, but also life-time guarantee service. Hermes offers "spa treatment" to renew customers' old handbag, and make them look like new. It differs their products to others'.

Hermes's customers are normally extremely wealthy people who value differentiated features more than they value low cost. Their customers can spend from \$5000-\$100,0000 to buy a handbag and even wait for 6 years to get one of the limited edition one. Hermes's scarf is also high desired demand. "During holiday seasons, a Hermes scarf is sold every 20 seconds in the Paris Hermes boutique" (Tie-a-scarf.com, 2012). Each scarf can cost up to \$300. Hermes prices their items sky high but their sale is still growing because each scarf was handmade 100% with 30 different colors. These factors cannot be found in any other scarves.

Hermes International does not have a blue ocean strategy but their products stand out from other competitors' in both quality and outlook. Hermes is not making good products, they are making excellent merchandise.

### **4. Is the firm diversified? What are its ethics and values? Is the firm optimally organized?**

Hermes is not diversified like they should do to reduce risk and maximizing opportunities. Only focusing on luxury items will become a high risk investment to Hermes. What will happen if customers change their tastes or economy goes down and people looking for cheaper price items? Diversifying is a great way to reduce risk for Hermes and make their future much more stable. They can start opening a business that sells cosmetic items which many wealthy customers are desired, too.

Hermes International also got involve in some problems with general environment. Killing crocodile to get skin now becomes their most critical general environmental dimension. PETA organization already gave a warning to Hermes about this unethical production. It is a big challenge not only to Hermes, but also a lot of luxury brands who use animals' skins as raw materials. Due to the high quality, durable and nice looking of crocodile's skin, it is not easy to find other materials to substitute for it with similar quality. For now, Hermes decided to build their own crocodile farm to avoid the complaint from animal protection organizations. This action is only useful for short term



not long term because “breeding crocodile is still murder – even if the crocs belong to” Hermes (Elena Gorgan, 2009).

Hermes is optimally organized. They have more than 14 product divisions which produce a lot of different merchandise. Even Hermes is only a family own business, they do a very good job in managing, controlling and organizing. All the divisions are working individually and bring to Hermes massive sales every year.

### **5. What about the additional areas?**

Hermes is still missing kid and pet sections in their product lines which can create million dollars each year for them. They should have their kid and pet divisions which focus on designing and production of these special products. These are promising projects for Hermes. Wealthy people tend to spend much more money on their pets than before. For example: “In the seven years she’s had her diva dog, Louise has splashed out more than £100,000 on all sorts of extravagant treats” (Mirror.co.uk, 2011).

In addition, extreme wealthy customers are normally busy and do not have enough time to shop. To create a convenient shopping stop, Hermes should have their cosmetics product line so their customers can find all items that they need to have a perfect outlook which includes make up, clothing, and accessories. Make-up Art Cosmetics (M.A.C) is a promising partner that Hermes can work with. M.A.C is known as a high-end cosmetic brand which has massive demand in consumer good industry. This company was founded in 1984 by two Canadians. The first state side store was opened in 1991 in New York City. In 1998, M.A.C became a part of Estee Lauder family brand. This company had a sale of \$7,795.8 million in 2010 which is one of the top ten cosmetics sellers nowadays. Hermes will eliminate unnecessary risk when become a partner with a big and experienced company like Estee Lauder. This partnership is a perfect combination. It not only complete the missing product line of Hermes but also brings Estee Lauder from consumer good industry to luxury one. This project will promise millions of dollars in benefit.