LUXURY BRANDS MESMERIZE EUROPEAN RUSSIA, MOLDOVA, UKRAINE, AND BELARUS

How Global Luxury Brands Enter the Emerging Markets of Eastern Europe

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Abstract

The seductive realm of luxury continued its triumphal march after the global recession, expanding by 10% to $275 billion in value in 2013 alone (Bain and Co. Luxury Goods Worldwide Markets Monitor Report, 2013). Behind its newly regained confidence were underlying structural changes, which were mostly prompted by the pressure of negative consumer sentiment inspired by the recent recession and by “guilt fatigue.” Additionally, profound socioeconomic differences became even deeper throughout the emerging markets and led new privileged legions of customers to be enticed into global luxury consumption. Issues related to the definition and nature of luxury and to the motivational and behavioral drivers of luxury consumption in the context of various political and economic dynamics in the post-Soviet era in European Russia, Ukraine, Moldova, and Belarus are the focus of our attention in this paper.

Introduction

Luxury consumption did not come to a halt during the recent global financial crisis as many retail analysts expected, but recession changed it structurally and incorporated a certain “guilt factor” into the luxury acquisition process. Still, iconic “absolute luxury” consumption proved resilient in the face of recession. Louis Vuitton, Armani, Hermès, and Chanel expanded and did well financially, especially in emerging markets. Mid-level luxury (or “high-fashion luxury”) sales (Marc Jacobs, Stella McCartney, Alexander McQueen, Gucci, Prada, Valentino, Versace, Bvlgari, Valentino, etc.) dropped, owing to their much greater exposure to the slowdown in luxury consumption by members of the middle class, waiting for “better times” and newer, more exciting celebrity endorsements. And some department-store items classified as “entry-level luxury” did poorly, moved down-market, or went on sale (Victoria Beckham DVB denim, Paris Hilton clothing lines, Jessica Simpson accessories, Simply Vera dresses, Just Cavalli outfits).

Further, in times of crisis, certain luxury items like jewelry are used as investments or hedges against inflation. With the cost of precious metals—and the perceived inherent value of jewelry—continuing to increase, planned jewelry purchases are most likely to be made now, to avoid further inflation. Similar consumer behavior is common in the luxury housing market. As that market is on hold and top luxury foreclosures à la The Queen of Versailles are still rare, prospective buyers with ready cash are expected to look at securing the best prospective investment properties. Their aim is well known: Buy low, anticipating that in a year or two they can turn a profit and sell high, or at least higher.

The evolution of a significant guilt constraint or “luxury shame” among wealthy customers has slightly delayed a full recovery in the luxury-goods industry. Because many consumers are less at ease with splurging than they were some years ago, new marketing strategies had to be devised: a blend of purchase with charitable donation (as a percentage of total purchase value or with a discount for donating already-used items); “green” living (by paying for environmentally safe products); even a change in store format (such as temporary luxury “pop-up stores” in non-luxury shopping areas).

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Some customers permanently moved online to various club sites that are accessible mainly by invitation, such as Guilt.com, GuiltMan.com, RueLaLa.com, and ShopItToMe.com, to avoid malls and to enjoy the casual, discreet convenience of “sample” or “flash” sale discounts during the lunch break.

Considering the uniqueness of their market situation, über-rich consumers are the last to feel the crisis and the first to overcome it. Further, the recent recession, like the previous ones, created “new rich” men and women, especially in the emerging markets of Eastern Europe, who are joining forces to expand the luxury consumption industry to new, once-unusual geographic destinations. How are they shopping for the pricy stuff in different countries?

LUXURY CONSUMPTION AND AFFLUENT BEHAVIOR IN EUROPEAN RUSSIA

Luxury consumption with regard to home, personal, and experiential luxuries has been evolving in Russia ever since the collapse of the Soviet Union, and such consumption is an ambition closely linked with Russia’s glamorous imperial past. High-end clothing, footwear, leather goods, jewelry, and eyewear command an overwhelming 65% of the Russian consumer goods market. It is common knowledge that Russians are highly attuned to explicit manifestations of wealth, have a deeply imbedded propensity for opulence, and interpret indulgence as an expression of their newly acquired freedom from the political restraints and limitations on travel to Western countries that were so restrictive in the past. This pattern has been supported by impressive macroeconomic growth and investment activity, low public debt, positive improvements in the banking and financial systems, healthy growth of general consumption, and unprecedented upward mobility of the upper middle class in recent years.

A managing partner of the consulting group Accenture, Richard Wildman, acknowledged that “consumers from the emerging markets have driven the bulk of [luxury goods] sales in recent years, averaging around 23% of the total from 2003 to 2008; in comparison, developed markets were flat or declining. […] revealed the relative luxury market growth rates for Russia – forecast to grow fourfold by 2015; China, six fold, from $2 billion to $11.2 billion; and India, where the luxury market is set to jump tenfold” (The Moodie Report, 2008). In Russia alone, sales of luxury products increased by 9% in 2012 and reached a very impressive €5.5 billion (Luxury Society Market Guide, 2012). The general retail boom in Russia is supported by attractive commercial rent values, endless consumer demand, increasing numbers of new mall openings (such as St. Petersburg’s DLT department store, a branch of the iconic retailer TsUM), and unlimited outsourcing opportunities for consumer products pouring in from neighboring Turkey, Egypt, India, and China.

Russia is notorious for its exorbitantly priced restaurants and fancy cars, and for the general addiction of the affluent elite to opulence and the most expensive merchandise available around the world. Muscovites buy more than 80% of Russia’s luxury goods, in luxury clothing and accessories stores with an estimated total worth between $4.5 and $5 billion. The other two centers of wealth and luxury consumption in the country are St. Petersburg in northwestern Russia and Yekaterinburg in the Urals, where branches of Moscow’s successful store chains usually proliferate first. Moreover, Russia is home to the world’s third-largest concentration of billionaires (after the United States and Germany) and to more than 100,000 millionaires with a combined $375 billion of cash on hand. Moscow, with its glamorous offerings, is the most expensive city in Europe; more rich people reside there than in New York (79 billionaires reside in Moscow, 59 in NYC), according to Forbes (Brennan, 2011).

The global economic downturn presented major challenges to the commodity- and energy-price-driven Russian economy. Crude-oil prices, within a single year, declined from $150 a barrel (July 2008) to a miserable low of $40 per barrel (March 2009). The total number of Russia’s billionaires was halved in the crisis years, and the Russian ruble started to fluctuate sporadically again. What was the impact on luxury consumption?
The worsening of the macroeconomic situation in Russia triggered some pessimism and confusion in the retail industry, even among the capital’s luxury-store management. Alexander McQueen, Stella McCartney, and Lanvin closed their stores fewer than 18 months after their respective grand openings in Moscow. Moscow’s sole Vivienne Westwood shop displayed a notice—“Closed for repairs”—taped to the door for some time: less embarrassing than admitting that the firm was “pulling out” of the country. Fancy British stiletto heels, majestic gowns, and Italian-made wool coats first disappeared and then were offered at a 70% discount in some neighborhood stores.

One symbol of the changing times was the opening of an H&M store in the former Alexander McQueen space, in a prime location in Moscow. Some luxury customers were lured away by this new “opportunity.” Donatella Versace and Tom Ford have not jetted to Moscow lately to share their amazing plans for operational expansion with enthusiastic crowds, as they both did back in 2008. Moscow’s answer to London’s Bond Street, Stoleshnikov Pereulok, buzzed with rumors of coming crisis-spurred shutdowns. The Russian franchiser Aizel, working for Diane von Furstenberg, Marc Jacobs, and Agent Provocateur, admitted that sales dropped by 10% during spring 2009.

The truth was that the consumer market was just slowing down and shifting modes: bigger discounts for the majority, and on über-luxury for the exclusive few. It takes time to adjust psychologically to the idea of bad times that affect even the wealthiest segment of the most affluent non-Western nation. Most of Russia’s traditional luxury consumers are feeling “guilty yet rich.” Things very well might get worse before they get any better. Finally, the Russian rich are Veblenian consumers, in the classification of Vigneron and Johnson (1999). They attach greater importance to price as an indicator of prestige because their primary objective is to impress others. This attitude endures tenaciously. For instance, when the annual Millionaire Fair was held in Moscow in 2006, a diamond-studded cell phone was sold for $1.27 million (“A fair for oligarchs with money to burn”, 2006). Just in case the glitter of the 120 carats of diamonds encrusting the white-gold phone failed to draw customers, there was a plaque declaring, “Certificate of the most expensive mobile phone ever.” The world’s largest exhibition of luxury goods continued at the Fair in 2007. Customers were eagerly buying $50 million worth of private jets, Bentleys, penthouses, and yachts, without showing particular remorse.

Currently, “serious” luxury brands—Chanel and Louis Vuitton—are expanding rapidly in Russia. Chanel opened a new boutique in Yekaterinburg (though on July 22, 2013 Chanel store in Yekaterinburg was unexpectedly closed) and is seeking more sales opportunities in Moscow, where it already has two stores. Louis Vuitton is also opening a store in the fast-growing city of Yekaterinburg, and the company’s further plans include new store openings in the booming Black Sea resort Sochi, host to the 2014 Winter Olympics, where Christian Dior and Dolce & Gabbana are already situated; the southern city of Rostov-on-Don; and the Samara area of the Volga region. The Economist cleverly explains this counter-intuitive phenomenon as follows: “When people have less, they spend what they have on the best quality. Shoppers are going for fewer, more classic items. Vuitton always gains market share in crises” (The Economist, 2009). Profits may be lower, but revenues are about the same as last year. Vuitton items have never been on sale at a discount anywhere in the world. The price of the ultimate luxury is founded on LV’s machine-like discipline, strong manufacturing copied from auto-assembly lines, professionally skilled personnel who set up stores in advantageous locations, and, obviously, appealing advertising. LVMH, LV’s parent company, counts on emerging markets for 15% to 22% of its revenue annually (Money Week, 2011).

The recent trend in Russia is to move luxury shops to the fancy dacha suburbs of the big cities. The Moscow suburban village of Barvikha, home to members of the business and political elite, including President Putin and his entourage, accommodates Lamborghini and Ferrari dealerships and Tiffany, Prada, Ralph Lauren, and Giorgio Armani shops that are never empty.
Though the average Russian earns only $5,000 a year, the so-called “new Russians” still have a healthy appetite for the luxury items miraculously displayed there. Families enjoy the opportunity to shop in stores that finally are located in close proximity to their upscale summer homes. Nick Nelson, an equity strategist at London’s UBS, suggested that Russian sales can offset a great deal of lost revenue in the United States and worldwide. No wonder Russians are the fourth-largest consumers of luxury goods after the Japanese, Americans, and Chinese.

Affluent Russian consumers have the greatest top-of-mind awareness of foreign luxury brands, in comparison with customers in other major emerging markets, China and India. The Russian luxury market is more developed and more ‘European’ in nature. The top brands are recognized by Russians in the following order (in percentage of total people surveyed): Chanel – by 39%, Giorgio Armani – 37%, Dior – 35%, Dolce & Gabbana – 29%, and Versace – 27%. The best-known luxury brands in Russia are Versace, Dior, Chanel, Zaitsev (Russia), Yudashkin (Russia), and Giorgio Armani. When considering purchases, Russians look above all for high quality (53%), good reputation (53%), and famous fashion image (44%).

The most popular luxury items in Russia are watches and jewelry, electronics, art and antiques, marine items (yachts, speed boats, marinas, and submarines), luxury cars and car accessories (including amphibious vehicles), private jets and helicopters, high-end real estate properties, interior design items and luxury furniture, exclusive spirits and gourmet food, luxury cosmetics, beauty and health products, designer clothes, and upscale travel and leisure opportunities (such as golf). Many well-educated Russians with good management jobs have sufficient financial security and like to buy beautiful things. The Russian mentality historically supports a carpe diem attitude, a tendency to spend money madly. Russian Vogue suggests that it is now “consumerism time” in Russia. According to the Russian Golf Association, the number of golf courses—20 at present—soon will double. The majority of them are located on the posh outskirts of Moscow. The golf market, growing by a remarkable 75% a year, was estimated at $1 billion at the end of 2008, and that amount is expected to double soon.

The Russian luxury real estate market is growing by a healthy 20% per year. Marketed homes are designed with private zoos, golf courses, and big aquariums. The most expensive Russian apartment sold in Moscow thus far was priced at $22 million, and the demand for luxury apartments far exceeds the supply. Plenty of buyers are willing to pay more than $100,000 per square meter (average price per square meter in December 2012: in Moscow – $42,500, Hong Kong – $47,500, and London – $43,650). New elite construction in downtown Moscow is expected to raise this price to $40 million per apartment. Newly erected apartments will have indoor swimming pools, enclosed gardens, private yacht piers, and up to eight floors per unit with private elevators for family members. New infill construction and land development in central Moscow is limited, and this boosts demand to an even higher level. A million dollars could buy you a one- or two-bedroom apartment in a decent area (“Russian Luxury Estate Market Is on the Rise”, 2013).

Russia has become the second-largest market for luxury automobiles in Europe after Germany, and is expected to become Europe’s largest car market by 2014 (“The Top 50 Most-Searched Luxury Brands in Russia”, 2012). Most transactions are made in cash rather than on credit as is typical elsewhere. An imported luxury car is a must-have accessory for any successful Russian businessman. Daimler-Benz’s latest Mercedes models are the market favorites, and sales have jumped 90% from the level recorded in 2008. Russia is the third-largest market for company cars, after the United States and the Arab Gulf countries. Rolls-Royce has a lengthy waiting list for the first golden-plated models (some are also encrusted with Swarovski crystals). Originally Bentley alone sold 240 cars in the country, and the company plans to double this number within the next couple of years by operating five dealerships in Moscow, Krasnodar, Yekaterinburg, Novosibirsk, and Rostov-on-Don. Bentley expects to make Russia the third-biggest market for the brand in the world, after China and Japan.
Even the Russian government is feeling uncomfortable with the situation, and has adopted legislation to sharply raise (double and even triple) luxury taxes on cars worth more than $160,000 (Russian Luxury Car Tax. 2013.)

Among the truly exotic Russian luxuries is the “Express,” a hotel on wheels that travels between Moscow and St. Petersburg. It is the first VIP train operated by a state-owned company in Russia. A ticket costs about $800 per person. It has state-of-the-art amenities to accommodate travelers’ every wish: air-conditioning, flat-screen TVs, DVD players, appliances, a gourmet food selection, and even full showers. The second route, from Moscow to Sochi, is planned to open by the beginning of the Olympic Games in 2014. The demand among business people, tourists, and foreign guests lends full support to the project. Another luxury train connects Moscow with Yekaterinburg, Novosibirsk, Irkutsk, and Vladivostok: The “Golden Eagle” Trans-Siberian Express, operated by Britain’s GW Travel, is a joint project of England and Russia. Passengers travel in great style and enjoy the masterpieces of Russian gourmet cuisine. The floors are heated, and plasma TV sets hang in every cabin. A two-week holiday on the “Golden Eagle” costs about $10,000 per person. But it is the world’s longest transcontinental railway line!

In the luxury timepiece category, the legendary firm Breguet successfully re-entered the Russian market after 200 years of absence. Tsar Alexander I of Russia, Napoleon Bonaparte, and Leo Tolstoy all owned Breguet watches. The new store location is in Red Square, right across from the Kremlin. The cheapest item in the store costs $14,000, and watches from the Imperial Collection are priced slightly under a million dollars. The watch market is moving toward more distinct, art-oriented, intimate, and expensive pieces in the best traditions of the renowned jeweler Fabergé. Wealthy men just love this!

The Russian gourmet food market recently welcomed the specialty food chain Globus Gourmet, which operates the first luxury hypermarket in Moscow, as well as France’s exclusive grocery chain Hédiard (with 320 stores in more than 30 countries), now owned by Russian billionaire Sergey Pugachev. The average shopper there spends about $80 per visit, which is a large amount by local food-buying standards. Among gourmet professionals and connoisseurs, this move triggered great interest in the further development of the gourmet food market.

In the high-society gossip market, the Russian “equivalent” of Paris Hilton and the country’s most notorious TV personality, Ksenya Sobchak, released a guidebook on “how to marry rich.” She and her coauthor, Oksana Robsky, stated in the book that there are at least 35 billionaires in Moscow alone worthy of female attention. The sky’s the limit, ladies!

All this means that Russia is becoming well accustomed to opulence and glamor in the best traditions of the crème de la crème lifestyle enjoyed by the world’s most fortunate consumers. And this state of affairs seems likely to persist and expand. Moscow and St. Petersburg lead in luxury-store, restaurant, and hotel openings. In June 2013, Four Seasons Hotel Lion Palace became the first Four Seasons hotel in Russia. The third city with a highly developed luxury market is Yekaterinburg, where most of the international top luxury brands, including Chanel, Dior, Gucci, Louis Vuitton, and Prada, operate a stand-alone store. Krasnodar and Ufa represent the third-tier luxury-market cities, with a potential that has already been tested by successful multi-brand stores.

The phenomenon of luxury living is becoming more widespread in Russia, while the gap between “the super-rich” and “the rest” is widening, as everywhere around the world. To support their newly acquired social status, the rich “spend richly” and revel in doing so. Luxury brands and exotic, self-gratifying items are seen as a way to entice more and more customers to enjoy the utmost in chic and an utterly desirable existence. This concept of living has great appeal and is positively regarded in the mainstream value system of modern Russian society.
Though the recent global financial crisis affected the coffers of the rich in a negative way, it did not significantly deter luxury consumers from the pursuit of their exclusive *modus operandi*. Meanwhile, the near-rich had to look for other alternatives. Some of them opted out in favor of discounted consumption; some had to concentrate more on “intellectual vs. material” life; some simply fell too far and were excluded from the upper-middle-class category for the time being.

Widespread social stratification is also actively going on in other, much poorer, parts of the former Soviet Union. Belarus, Moldova, and Ukraine remain the poorest parts of Eastern Europe, struggling both with the awkward, still-obvious post-Soviet influences that strongly affect all aspects of life there, and with a moderately popular flirtation with the European Union, which so far has yielded mainly undelivered promises. International retailers generally still harbor reservations about this region because of its unexpected political shifts, the low purchasing power of the population, bureaucratic restrictions on focal retail developments, and local customers’ lack of a true understanding of brand image and equity. Most price-conscious customers pay more attention to the functional side of the premium pre-luxury brands—quality, packaging, and design—than to the exclusive image component and refined service aura, because a conspicuous lifestyle as an enhancer of social status is not yet a factor here. Genuinely wealthy customers from this region mostly shop overseas, where they can afford to travel regularly, and reject what they apparently see as the boredom and bleak appearance of the local retail outlets.

**Ukraine**

By European standards, Ukraine is a big country. It has a population of 45 million and possesses strategically important natural resources. Some Western countries have expressed interest in investing locally and in exploring the country’s market opportunities. GDP in Ukraine, on a PPP basis, is $334 billion. The low per capita GDP of $7,300 kept the country at 134th place in the world for years, but in 2011 Ukrainian GDP expanded by 5.2%, pushing it to 64th place worldwide, and to second place (after the Republic of Moldova) in the region (Ghedrovici & Ostapenko, 2013). Immediately after declaring independence, Ukraine announced a liberalization of consumer prices and created conditions for mass privatization. As in Russia in those days, shock-therapy measures produced many negative socioeconomic consequences: output in 1999 declined by 40% in comparison with 1991; the reduction in the number of jobs, due to restructuring of the factories, was catastrophic; in 1995-1999 poverty reached a peak historical level. The new century has brought little improvement of Ukrainians’ gloomy economic prospects. Consumer spending in local currency is slowly growing, in statistical terms, but booming inflation accounts for much of the growth.

The consumer market is far from the saturation point, with huge potential for growth. Kyiv, the capital, has more than 4 million residents, and is very much “under-retailed” by European standards. Ultra-wealthy customers represent about 0.3-0.5% of the population, and such customers are concentrated in the cities of Kyiv, Donetsk, and Odessa. The new upper-middle class is experimenting with consumption of *starter* luxury goods such as scarves, sunglasses, key chains, perfumes, and handbags before graduating to pricier and more extravagant items. The average Ukrainian brings home less than $360 a month, but the desire to show some confidence and financial independence in times of political uncertainty and economic turmoil leads customers to at least dream about expensive purchases.

Value and brand image are steadily attracting more attention from the local residents. There are at least four identifiable periods in the development of the country’s luxury market. The initial phase, from 1990 to 2003, included the first attempt to introduce luxury brands via black/gray market distribution, accompanied by an influx of counterfeited merchandise. Lack of market consistency alarmed some wealthy customers and signaled to others that the retail barrier was broken and choices were now available. Between 2004 and 2008, the luxury market experienced a boom, which peaked in 2006, with sales reaching €500 million for the first time.
Brands like Tiffany, Chanel, Louis Vuitton, Dior, Prada, and Boucheron enjoyed enormous success among well-heeled Ukrainians, increasingly in the market for luxury cars, watches, and jewelry. Every brand was opening a shop in Kyiv. The economic decline in the recession years of 2008-2009 caused luxury sales to drop by 30-40% (with some exceptions, as super-expensive accessory sales rose about 60%). Expansion in the luxury retail sector was put on hold, because Ukrainian customers had to exercise caution when spending. Subsequent years brought relative market stability and supported a slow return of luxury sales to the level of 2008.

Ostentatious public display of material wealth, as in Russia, stimulated the demand for true luxury in Ukraine, though shoppers had learned their lesson. Ukrainians had become more “globally plugged in,” and were not always oriented toward conspicuous consumption rather than personal gratification. In recent, post-recession, years, luxury sales in Ukraine increased by 150% annually, with more customer attention to product design, quality, and value (What’s On? Your No. 1 Guide to Kyiv, 2013). Smaller luxury brands like Alexander McQueen and Rag & Bone have been introduced by the luxury boutiques Sanahunt, IKON, and Helen Marlen. Meanwhile, sales of traditional luxury offerings such as iconic Christian Louboutin shoes have shown no signs of slowing. The Chanel, Bentley, Rolex, and Gucci brands reign supreme among consumer preferences there.

Trying to capitalize on Ukraine’s untapped luxury market, Chanel, Louis Vuitton, Dior, Ferragamo, and Prada set up their own brick-and-mortar stores in Kyiv. Hermès and Fendi have also announced plans to open flagship stores in the coming years. Talented local designers like Victoria Gres, Elena Burenina, Victor Anisimov, Kamenskaya Kononova, and Artem Klimchuk are demanding their share of the Ukrainian luxury market.

In terms of retail availability and concentration, it probably will take at least a decade before major foreign apparel brands operate their own stores in the country instead of relying on franchisees. Fashion House Group is planning to build a new 20,000-square-meter mall—Fashion House Kiev—that will house 150 shops and a food court, and provide parking for 800 cars. The company is a leading builder of malls in Eastern Europe, including Poland, Bulgaria, Russia, and Serbia (Gerden, 2012). Another mall—Kyiv Designer Outlet—is to be built by Rioja Developments, a UK company. So far, the big question is: Will it be filled by the retailers?

Local customs regulations, taxation systems, and rules of doing business present a challenge in Ukraine. Leasing, distribution, franchising, marketing, inventory, and retail management, too, can be difficult to deal with. From the customer’s standpoint, lack of personal transportation, road congestion, and a spread-out retail pattern create inconveniences in terms of customer service and logistics. Ukrainians are accustomed to shopping near the metro stations in the city’s high street stores. Instead, many shops now are scattered around the city, and it can be difficult for customers to reach them. Dnepropetrovsk, Zaporozhye, Donetsk, and Makeevka, other large cities in Ukraine with attractive retail potential and a significant concentration of shoppers, are still waiting to be discovered by Western retailers.

Moldova

Moldova has long been the poorest country in Europe. The unpredictability of political developments there has adversely affected the country’s economic stability. One quarter of the population lives below poverty level. In the retail sector, Moldova is developing a multi-brand approach. There are about 40 popular Turkish, Polish, and Chinese brands that dominate the retail industry there. Customer interest so far focuses on centrally located small boutique-type shops with moderate to high prices and good personal service. Top luxury brands from the source are not yet available in the country.
Fluctuating demand makes even inexpensive Western volume operators like Zara and H&M reluctant to expand and establish a local presence. Meanwhile, franchisee-run Adidas, Benetton, Sisley, Mango, Reebok, and Sinéquanone are operating, but struggling to find and retain customers. They are trying to target middle-class expectations but offer prices and selections that are beyond the regular customer’s reach.

In the capital, Chişinău (Kishinev), the recent opening of the shopping mall Dova was expected to launch a retail revolution. It was designed for customers able to spend at least 1,000 leu (about $80) per visit. A good ladies’ coat costs 8,000 to 9,000 leu (about $700) there. Smaller boutiques are targeting customers with much less discretionary income who spend about 300 leu per visit. The lack of “qualified” customers forced some more-expensive stores like German Steilmann and Basler to close their doors shortly after opening.

There are many popular small boutiques in the city selling a variety of mid-level foreign brands that seem to be a better fit for the market needs of customers. We conducted a survey with several owners to identify their advantages and the growing problems of selling expensive clothing in the city. We learned that their clients are mostly women between 30 and 50, wives of politicians, bankers, and businessmen. Recently, some women entrepreneurs have appeared among the boutique customers. Their shopping priority appears to be brand appeal, with the item itself ranking second, and quality being least important. Purchases are often motivated by the convenience of having everything available in one place: dresses, shoes, accessories, and bags. These customers will not shop at the big, mass-market clothing stores, because they can afford more-upscale, branded apparel. They wear this apparel practically everywhere, both for work and for special occasions.

According to our survey, in their style choices customers were guided mainly by traditional local fashion magazines such as Aquarelle and VIP and by prestigious foreign magazines such as Elle, Cosmopolitan, and Vogue. The Internet was also named as a source for discovery of trends in women’s fashion. Brand selection depends mainly on the age of the customer. Younger people shop at Mango, Motivi, or Mexx (there are also H&M and Zara outlet stores); middle-aged customers prefer Italian brands like Liu Jo; mature women favor German brands such as Betty Barclay, because the dresses are a better fit for Moldovan women’s body types.

Are Moldovan men interested in style? There are some monobrand shops for men: Pal Zilleri, Ted Lapidus. Other men’s brands are available in multi-brand boutiques. There are also some selections from D&G and other serious designers available for males. But the majority of men buy luxury watches, sunglasses, or cars, rather than expensive clothing items.

Top luxury brands such as Chanel or Hermès are too expensive for Moldovans. Only a very few, mainly the families of politicians, can afford these brands, and they prefer to travel to Milan or Paris for their occasional seasonal shopping. From the perspective of small retail management, our survey revealed three important problems: high business taxes, the low purchasing power of buyers, and ongoing economic instability. In Moldova, the VAT is 20%, and customs duties on imported clothing items can be as high as 18%. Therefore, taxes, in combination with transportation expenses, add a surcharge of about 40% to the price. Rent and other expenses account for another 30%. In general, the markup from the wholesale price is as high as 70%, and that puts the retail price beyond the reach of most customers.

The most popular foreign brands usually are Italian and German. Interestingly, some years ago Mango and Mexx had big shops in the city center, but now they sell in a large mall where the rent is high. How do they survive? Years ago the items were made in Italy; today they originate mainly in China. What is special about China?
Prices are low, and sellers usually allow an even lower wholesale price to be stated in cross-border documents, so that Moldovan companies pay less in import taxes at home.

There are almost no company-owned store chains in Moldova; the sole exception is the United Colors of Benetton. Multi-brand resellers such as Calina, Vernisaj, and Promenad (selling Maxx Mara, D&G, and Valentino) also maintain a few locations in different parts of the city. The customer appeal here is based on a generous, loyalty-based return policy. One woman purchased a skirt, wore it for a month, and then brought it back because she disliked the fabric. The store accepted the return in order to retain the client.

In terms of prices, Italian brands offer their representatives abroad prices that are as much as 20% lower than prices for local Italian distribution. That discount is intended to offset the VAT that Moldovan companies pay. Owing to the high rents common in Italy and the relatively low ones in Moldova, however, Moldovan shops can set retail prices equal to or even lower than prices in Europe. Many Russians who come to Moldova on business buy outfits in local boutiques, where prices are generally much lower than in Russia.

Interest in, and demand for, prestige cosmetics is also increasing in Moldova, and luxury cosmetics companies are making inroads into the market. Product imports and sales are being handled by Shiseido’s Parisian subsidiary, Shiseido Europe S.A.S., and Shiseido products have been introduced in three cosmetics specialty stores that handle prestige cosmetics products in Moldova. That suggests a healthy trend in the development of the cosmetics market.

All in all, Moldovans have demonstrated considerable potential for branded consumption of European style. It will take time and many changes in retail management to persuade customers to shop more, however. One positive indication is that privately owned retail outfits are growing and becoming more customer-oriented in their selections, prices, and customer service. Western brands are taking the wait-and-see approach, and some were forced to simply pull out of the country. They will have to partner more with the locals and develop trust and brand recognition in the years to come.

**Belarus**

Belarus has a less-developed economy and retail market, in comparison with the other countries in the region. Since the breakup of the USSR, there has been little change for the better. According to local statistics, Belarus ended 2011 with the rate of inflation climbing to 120%. Officially, inflation for 2012 was stated to be 22%, according to the Belarus Ministry of Finance. Average unit prices in retail in 2011 were twice what they had been in 2010, and that jump exacerbated the price sensitivity of Belarus consumers. Price inflation supported an increase in retail turnover. Besides poor economic conditions, in 2011-2012 the development of the retail industry was also hampered by the complex Belarusian tax laws, insufficient infrastructure, high retail rents, and a sharp decrease in disposable income for the majority of the population. These factors resulted in low purchasing power for buyers and stronger government price regulation.

The Stolitsa underground shopping center provides evidence of a positive shift in local retail. The shopping center, which covers 75,000 square meters, lies below the city’s central square and houses around 100 shops and outlets, including a grocery store, fashion and electrical goods stores, cafes, restaurants, banks, and a movie theater. To accommodate customers, the center has four levels and a 500-space parking garage. Moreover, it is located 50 meters from a metro station and 400 meters from the city’s main railway and bus terminal. The center, which opened in 2007, has a central glass dome to let in natural light from Minsk’s central square above. As well as shopping, the center offers visitors plenty of entertainment, including frequent pop and classical music concerts, exhibitions, and food- and wine-tasting events.
Luxury boutiques are practically nonexistent in Belarus, and the few that are available normally buy wholesale two-year-old inventory in other countries and mark it up by 200-300% for Belarus distribution. For instance, for $350-500 you can buy a dated pair of shoes allegedly made in Italy but actually produced in a factory in China. There are many reasons for the limited availability of luxury in the country: the weak purchasing power of local customers, the absence of an upper middle class, the limitations of the historical downtown area of Minsk, where luxury stores normally would congregate, the outrageous retail lease rates in more-or-less prestigious locations, the traditional government bureaucracy, the dreadful infrastructure.

But even here, things are changing. Surprisingly, a decision was made to open the country’s first Bentley dealership, Bentley Minsk, this summer. It will offer the full range of these exclusive cars, from the powerful and elegant Continental GT and GT Convertible v8 and v12 to the refined and dynamic Flying Spur and the Mulsanne luxury models (“Bentley in Coming to Belarus”, 2013). Each model offers Belarus’s wealthiest automotive fans an unrivaled blend of effortless performance, peerless refinement, and hand-crafted contemporary luxury from Britain. We will have to see how many fans show up for the grand opening.

Not quite that lucky is the local luxury fashion market. The Grand Fashion Mall, sponsored by JSV Avtobusiness, is in the process of opening. The mall is designed for midlevel retail brand names, but the spaces are slow to fill. It is expected that at least 20 locally unknown brands will be introduced there, though only three requests for space have been submitted thus far (“Where are new fashionable brands located in Minsk?”, 2010). The new mall is supposed to combat the “shopping tourism” so popular now among Belarusians, who frequently travel to Moscow, Vilnius, or Warsaw to make purchases. A related problem is posed by the counterfeit items pouring into the country from Asia to fill the current retail void. Sadly, “anything goes” is the approach of Minsk’s retailers today. No retail strategy is expected from the Belarus government soon. “Save yourselves,” a Soviet-style attitude, dominates the Belarus retail sector, which sorely needs major changes.

**Conclusion**

Luxury consumption in Eastern Europe’s emerging markets, especially in Russia, is regaining strength after the recent financial storms. The Russian market is becoming more and more important to luxury retailers in Europe and worldwide. The recession caused consumption to lose some steam, but most wealthy Russian buyers actually increased their purchases of opulent items. The new wave of luxury-brand expansion is moving now from the saturated traditional centers, Moscow and St. Petersburg, to the more remote cities of Yekaterinburg, Krasnodar, Rostov-on-Don, Sochi, Samara, and Ufa. The luxury market is becoming more mature and sophisticated. Hermès, Chanel, Louis Vuitton, and Prada comfortably operate their own stores in the country; Gucci is now transitioning from its franchise-operated stores to a direct presence. Other luxury companies such as the Aeffe Group (Alberta Ferretti, Pollini, etc.), Burberry, Giorgio Armani, and Ermenegildo Zegna are pursuing long-term franchising agreements with Russia’s famous luxury retailer, the Mercury Group.

The luxury market has expanded from traditionally consumed luxury items like expensive cars, watches, jewelry, fashion, and leather goods/accessories to include high-end electronics, art and antiques, yachts, private jets, prime downtown real estate (including architectural and design services, with fine furnishings), spectacular country houses (dachas), distinctive foods, extravagant restaurants, elite liquors, fantastic boutique hotels, unique personal services, and very special vacations. The latest in wealthy splurging is concierge service that puts a personal butler at your back, just in case you require a private jet to use your first-row ticket for the latest Madonna concert while sitting on a designer sofa and consuming a fine glass of Moët.
Because income disparity is growing, we see increased consumption of true luxury by the very rich and the upper middle class, and simultaneously observe growing attention to pre-luxury, discounted luxury, and even mass-manufactured Western brands among Russians in the middle-middle class, who cannot afford extravagant expenditures. This signifies an important shift of many Russian customers from lavish conspicuous consumption, just for the purpose of pretentious display, to a more self-gratifying and smarter approach that resembles Western consumption, a balance found somewhere between opulent chic and daily practicality.

Though the enticing idea of living and breathing luxury gained a footing in the more-developed parts of the former Russian empire, the remote provinces are still struggling to keep up with the Joneses in Moscow and St. Petersburg. The economic situation in the provinces, though recently improved, still does not give full assurance to international retailers. They are not getting a green light to enter the market and cannot outline a future entry strategy. A luxury retail boom in Ukraine, Moldova, and Belarus is not expected to come at once, and it will require multiple, steady economic, regulatory, and market changes, which are yet to be implemented by local authorities. Thus far, luxury market opportunities there are wide open, though many corporate, logistic, and financial risks are involved. Those risks are scaring away Western volume fashion retailers, even though fancy malls are multiplying in every capital city in Eastern Europe.

References


Key Terms and Definitions

*Luxury consumption:* A consumer market trend characteristic of wealthy countries but recently found in the capitals of the emerging economies; it entails purchase of big-ticket items for various reasons, such as self-indulgence, public display of wealth, and social competition.

*Luxury brand:* A symbol of consumer popularity and the exclusiveness of a product or service; its strength commonly results from years of successful market presence and consistent promotion of an expensive image.

*Luxury customer:* A customer who normally belongs to a wealthy group of consumers, accustomed to buying elite products and services at all times, and not in search of discounts or “deals.”

*Pre-luxury customer:* A buyer who is struggling to become truly wealthy and therefore is eager to buy luxury on sale or through alternative distribution channels to boost his or her social status.

*Luxury tiers:* These tiers include ultimate top luxury (a very few global, iconic, distinct brands, with supply usually tightly controlled), midlevel luxury (spin-offs of major luxury brands, more widely available at lower prices, and positioned for younger consumers by capitalizing on the success of the mother-brands), and department-store luxury (luxuriously positioned and expensive brands that lack exclusive distribution channels and/or have no particular, distinct image in place).