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**SIGNALING AND MATCHING THROUGH LUXURY  
GOODS: THE MICROECONOMICS OF THE  
VEBLEN EFFECTS AND FASHION CYCLES**

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# CONTENT OVERVIEW

## 1.1 Rationalizing Conspicuous Consumption and Veblen Effects

Overpaying functionally equivalent goods in order to achieve status recognition is a phenomenon that is most evident in prestige seeking consumers environments like the market for luxury goods. The manifestation of this peculiar purchasing behavior was first identified and theorized by the sociologist and economist Thorstein Veblen in his treatise “The Theory of the Leisure Class: An Economic Study of Institutions” back in 1899. Even if the social causes of ostentatious consumption were largely discussed and clarified by Veblen himself and subsequent authors (C. Lury (1996), A.A. Berger (2000), R.H. Frank (2010)), it took quite some time to justify and translate Veblen effects into microeconomic theory. The first purpose of this thesis is indeed to shed light on the economic and behavioral causes behind conspicuous consumption; as a starting point, the model of Bagwell and Bernheim on wealth signaling through conspicuous goods will be analyzed. It will be shown that Veblen effects can emerge only under alternative assumptions on the properties of households’ preferences, more specifically under failure of the single crossing property. Exclusively by altering some of the features characterizing standard consumers’ preferences, it is possible to observe Veblen effects and consequently explain how some companies are able to charge a high markup on their products under competition. Even if not necessarily superior in quality with respect to lower priced items (e.g. premium products), luxury goods grant to the individual a social benefit through their capability of enhancing status: projecting consumers interactions into a signaling model helps understanding how luxury items serve as proper matching devices and how price determines their effectiveness as signaling tools. The study will then transition into a more complex model of countersignaling by Feltovich et al., that will show how information spillover affects the signaling strategies of some particular types of consumers who will deviate from the optimal strategic actions previously designed by Bagwell and Bernheim. The implications of this last model will be further assessed through a comparison with the

empirical findings of a marketing study presented by Han, Nunes and Drèze about the role of brand prominence on luxury goods; this last paper will be useful not only to conciliate the theory with reality, but also to show how the price differentials along the product line reflect different signaling needs of each customer category.

## 1.2 The Matching Process Duration and its Impact on Status Signaling Effectiveness

The second section of this thesis will be concerned with a deeper analysis of matching dynamics and their possible outcomes. The ultimate goal of publicly showcasing and consuming luxury goods is to be associated with an aspirational group; this is made possible through the use of conspicuous goods as screening and matching devices. Taking Pesendorfer's model on design innovation and fashion cycles as a reference, it will be shown how the anticipated or delayed availability of the luxury good affects the utility payoff of consumers by regulating the duration of each matching period, therefore determining the number of possible social interactions arising from the use of the design. According to the model, the longer the time available for interaction (hence, the longer the fashion cycle), the higher the value of the new design in the eyes of the consumers. It must be noted however, that the progressive advance in technology has triggered this assumption by changing the way in which people show their lifestyle and their status and, overall, by changing their consumption and signaling patterns.

On the basis of these considerations, the managerial strategies of two important players in the ready to wear and luxury market will be analyzed and compared to assess to what extent Pesendorfer's predictions fit today's evolving luxury world.

# FEASIBILITY AND REASONS BEHIND MARKUP PRICING IN THE LUXURY INDUSTRY

Before going into the details of the models, I would like to formally define the concept of conspicuous consumption: “conspicuous consumption, or Veblen effects, are said to occur when individuals increase their demand for a good simply because it has a higher price” (Creedy and Slottje, 1991). According to Veblen’s idea, public display of valuable goods is then a tool for differentiation, status achievement and recognition granted by society. As it will be shown, signaling interactions among individuals may or may not give rise to Veblen effects and to a consequent markup pricing strategy from firms’ side, depending on consumers’ preferences and indifference curves shape and properties; Bagwell and Bernheim’s model will serve as an overview on the different conditions needed for conspicuous consumption behavior to exist and to be an effective signaling tool. Later in this section, another model allowing for a more open and complex signaling environment will be introduced, in order to show subtler ways of signaling and countersignaling that reflect more accurately behaviors adopted by luxury brands customers, apparently in contrast with previous implied intuitions.

## 2.1 Bagwell and Bernheim’s Model:

### Why and how is premium pricing possible?

In Bagwell and Bernheim’s model, consumers have *private information* about their wealth, hence they attempt to show their financial position to the external environment by consuming conspicuous goods. Conspicuous goods consumption is then the one and only instrument to signal wealth to *every other* individual in this scenario. It is assumed that level of consumption  $x(q)$ , brand selection, brand price ( $p \in [ \underline{p}, \bar{p} ]$ ) and brand quality

( $q \in [ \underline{q}, \bar{q} ]$ ) are observable by the others. The players, or senders to be more specific, of this game are households who are classified on the basis of the level of their resources [ $R_H$  and  $R_L$ ,  $R_H > R_L$ ]; the distribution of people with high resources ( $\alpha$ ) and, consequently the distribution of people with low resources ( $1-\alpha$ ) is *common knowledge*. The signal that each type of household sends is the quantity-expenditure combo ( $q, s$ ) on conspicuous goods, being consistent with their budget constraint  $z \leq \gamma(s, R_i)$  [where  $z$  is the expenditure on inconspicuous goods consumed privately and  $\gamma$  is a generic function decreasing in  $s$  (conspicuous expenditure) and increasing in  $R$  (total resources,  $i = \text{High or Low}$ )].

For both high resources and low resources types, the utility function is the following:  $W_i(x, s, \rho)$ , where  $\rho$  is the action taken by the receiver in response to the sender's signal. Utility is increasing and continuous in all its arguments. Consistently with Veblen's idea that "esteem is awarded on evidence"<sup>1</sup> and that wealth showcase is rewarded through special treatment by social contacts, Bagwell and Bernheim incorporate this latter group into the model as receivers. Social contacts have a belief about the type of the household they are interacting with, represented by  $\pi$  which indicates the probability that the household is type H. The action that social contacts will take after observing the signal used by the sender, is either  $\rho_H$  if  $\pi = 1$  or  $\rho_L$  if  $\pi = 0$  and  $\rho$  will be chosen to maximize their payoff being a function of  $R$  and  $\rho$ , [ $\phi(R, \rho)$ ].

The question to be answered now is: when is premium pricing for luxury firms possible and why? The model shows that answer is to be found in the shape of the indifference curves of the two types.

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<sup>1</sup> Quote from "The Theory of Leisure Class: An Economic Study of Institutions", Thorstein Veblen, (1899).

### 2.1.1 The “No markup” situation

Bagwell and Bernheim define the slope of the indifference curves as a “benefit ratio”: “the ratio of the utility gains associated with another unit of conspicuous good, to the utility losses associated with another dollar of conspicuous expenditure”<sup>2</sup>.

Looking at Figure 1 it is easy to spot that high types have a steeper indifference curve compared to the one of low types *when single crossing property (SCP) holds*.

Let me formalize the concept of SCP in terms of consumers’ preferences first:

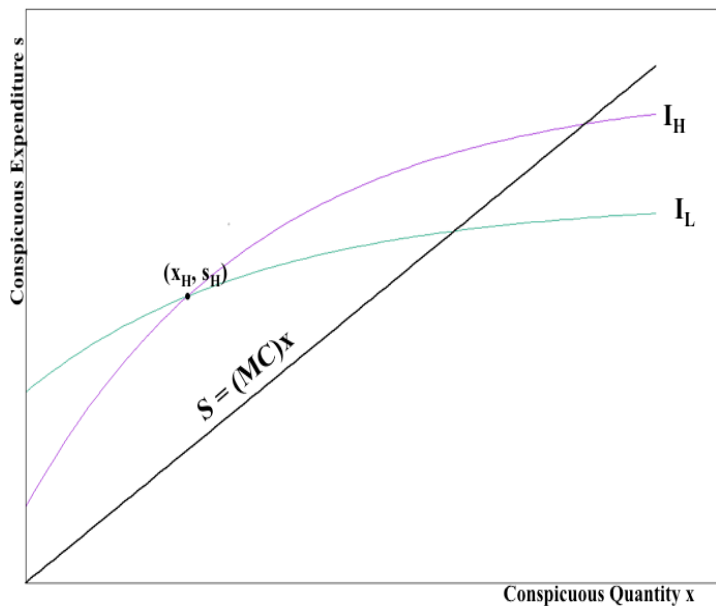


Figure 1: SPC and Absence of Veblen Effects

**Preferences satisfy the SCP if, for any feasible  $(x, x', s, s', \rho)$  with  $0 \leq x < x'$  and  $0 \leq s < s' \leq \bar{s}$ ,  $W_L(x', s', \rho) \geq W_L(x, s, \rho)$  implies  $W_H(x', s', \rho) > W_H(x, s, \rho)$ .**

To give a rough explanation of these conditions it can be said that whenever a low type *weakly* prefers to signal with a higher value of  $x$  and  $s$ , then the best response of a high type is a *strict*

preference of signaling with higher values of  $x$  and  $s$  as well. This particular feature has two important implications on consumers’ behavior: the first one is that the signaling strategy is monotonic in the sender’s type (the higher the type, the higher the quantity purchased or the total expenditure), the second one is that high types can deter imitation of low types choosing to signal solely with higher quantity ( $x_H$ ) even if purchased at the lowest available price ( $p$ ). Social contacts will recognize this deviation in quantity as a status enhancement signal and will consequently differentiate them from low types. Indeed, the flatter

<sup>2</sup> Quote from “Veblen Effects in a Theory of Conspicuous Consumption”, Bagwell, Bernheim; The American Economic Review (1996, p. 357).



indifference curve of low types shows that this group incurs a higher cost (with respect to high types) to acquire an extra unit of conspicuous good, hence they would be better off by avoiding to imitate the consumption choice of high types.

This argument can be expressed in the following incentive compatibility condition:

$$W_L(x_L, s_L, \rho_L) \geq W_L(x_H, s_H, \rho_H)$$

$$W_H(x_H, s_H, \rho_H) \geq W_H(x_L, s_L, \rho_L)$$

Again, this shows that for low types pretending to be high types is not worth it, due to the weak preference of lower quantity-expenditure consumption bundles.

These conditions together allow for a *separating equilibrium*, hence for an efficient signaling outcome where all types are correctly recognized according to their signal.

*Equilibrium under single crossing property: All L-types will purchase  $x_L$  units of conspicuous good at a total cost of  $p$  lower bar  $x(\underline{p})$ . Luxury firms will sell their products at a price equal to the marginal cost (MC) since no high type is incentivized to signal through overpayment of the good.*

Any choice of high types consisting in some value of  $x_H, s_H$  such that  $s_H/x_H > MC$  is indeed *feasible* but **does not** constitute an equilibrium. Customers would conveniently deviate from such a choice since there are consumption bundles below  $I_H$  and above  $I_L$  characterized by lower price and higher quantity that would offer to high types a higher utility payoff. The result is that no Veblen effects arise and hence premium pricing is not possible under these circumstances.

## 2.1.2 The Tangency condition and feasibility of markup pricing

Now it is clear that for firms to be able to charge a markup price, different conditions must hold. A crucial finding of Bagwell and Bernheim is indeed the rise of Veblen effects under violation of the single crossing property. Another condition instead, must be proved to be true: the *tangency property* of the indifference curves. Quoting the definition:

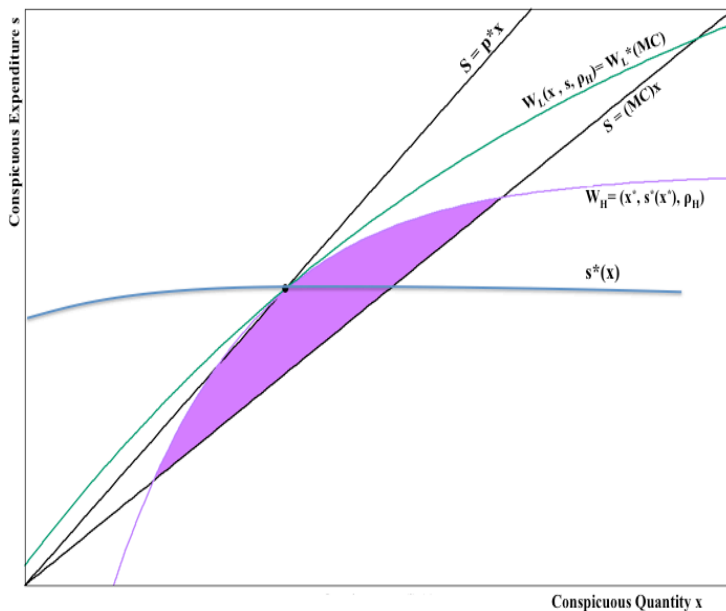


Figure 2: Tangency Property of Indifference Curves

in conspicuous expenditure  $s$ . Observing  $W_H(x, s, \rho_H)$  in Figure 2 it can be noticed that for certain values of  $s$  exceeding  $s^*(x)$  the benefit ratio is gradually decreasing in  $s$ . This time, the low-type indifference curve lies above the high-type one and strictly above the marginal cost expenditure line  $s=(MC)x$  at the point  $x_L^*(MC)$ ; higher utility levels are still reached moving down and to the right. It is important to point out that, in this particular case, the shaded area represents feasible consumption options for *both types*.

The tangency point shown in the graph implies a conspicuous expenditure made at a price well above marginal cost, hence in such a case Veblen effects arise since

**“Preferences satisfy the tangency property if there exists a continuous function  $s^*(x)$  such that for any  $(x, x', s')$ , with  $s' \neq s^*(x)$ ,**

**$W_L(x', s', \rho_H) = W_L(x, s^*(x), \rho_H)$  implies**

**$W_H(x', s', \rho_H) < W_H(x, s^*(x), \rho_H)$ ”<sup>3</sup>.**

When does this definition apply?

For instance, whenever high types have decreasing marginal returns

<sup>3</sup> Quote from “Veblen Effects in a Theory of Conspicuous Consumption”, Bagwell, Bernheim; *The American Economic Review* (1996, p. 361)

$[s^*(x^*)/x^*] \equiv p^* > MC$ . What is the equilibrium in this case and what is the best signaling strategy? High types still want to be recognized by social contacts, while keeping their utility level high; however, since the tangency property holds, this time it will not be possible for them to buy the luxury goods at marginal cost as in the single crossing indifference curves case. Doing so would be quite risky in terms of imitation: choosing to buy at any price  $p$  such that  $MC < p < p^*$ , would not allow for a separating equilibrium since all the  $(p, x)$  combinations are placed in the *common shaded area* where low types would have the incentive to move.

The only possible quantity-expenditure choice that would not appeal low types is then the one made at a markup price: such a choice implies a slightly lower quantity level of conspicuous good, but it is perceived by social contacts as a move that only high types would make.

### 2.1.3 Considerations about The Model

The two cases described above have different implications on luxury brands manufactures' price setting strategies. With single crossing indifference curves, a large pie, if not all, of the customers would rather choose *variety* of luxury goods owned to signal their status without caring much about the price they had to pay for each item possessed, in this case price has low to no signaling value and setting a high markup would just cut the customer base. Vice versa, whenever the tangency property characterizes the indifference curves of the two different types, price becomes a crucial tool for the luxury brand to guarantee to its customers exclusivity and prestige. The existence of the shaded area in this last case might well represent the "*threshold effect*" (Kapferer & Bastien, 2009) describing the price zone that divides luxury goods from "mass prestige products" (Silverstein & Fiske, 2003), products resulting from a downward brand extension, that characterize for more affordable prices with respect to luxury. Overall, the "tangent indifference curves case" seems to be the one whose equilibrium dynamics are most common and most observable across luxury brands manufacturers and their customers.

## 2.2 The quiet signaling strategy

### Adding noisy information to standard signaling

In order to better understand the main differences between the model just discussed and the one I am about to introduce, it is fundamental to point out some implications derived from Bagwell and Bernheim's idea about consumers' strategies and the environment they play in:

- 1) Signaling always results to be *monotonic in type's quality*; that is to say: the higher the type's profile, the higher and the stronger the signaling action chosen. Indeed, the equilibria shown implied either a *higher quantity* or a *higher price* choice for high types.
- 2) There is no information available about types other than the signal they decide to use to interact with social contacts.

According to these statements, what should be observed in reality is an ostentatious and explicit showcase of wealth from high status types, realized through the purchase of luxury goods that can be *easily* recognized by the mass as such.

However, the relation between the strength of the signal in terms of its *explicit* informational value and the type's quality is not always so obvious and straightforward; the availability of information in real life actually changes strategic choices made by consumers when choosing the right way to associate with the desired aspirational group or with the one they belong to. This creates some deviation from the results that have been predicted so far.

### 2.2.1 Feltovich, Harbaugh and To Model: A Non-Monotonic Strategy

A twist to the regular signaling models has been introduced by Feltovich, Harbaugh and To (2002) who allowed in their model for the introduction of additional *exogenous information* about the sender's type. It is actually quite reasonable to say that people in the everyday life might usually infer one's social class by his or her family background, income or occupation when this information is available. The structure of the model is as follows: types are classified in terms of quality (Q), where  $Q = \{\text{High, Medium, Low}\}$ ; as senders they face a cost of signaling which is increasing in  $s$  (the signal) and decreasing in  $q$  (the sender's quality). Note that this implies that  $c_s(s, q) > c_s(s, q')$ , where  $q' > q$ , which is in line with what was already pointed out in the previous model: signaling costs incurred by low quality types are higher than costs incurred by higher quality types. Hence, in this circumstance the SCP is assumed to hold. The new element introduced in this model with respect to Bagwell and Bernheim's, is *extra noisy information* about the sender's type available to receivers; this information, represented by the continuous variable  $x$ , is unknown to the sender at the time of signaling and is characterized by the conditional probability distribution function  $g(x | q_i)$ . For  $x$  to have informational value at least two types must send the same signal.

Note that now receivers have more tools to evaluate the sender's type and their beliefs will then be built not only on the basis of the signal  $s$  itself, as in Bagwell and Bernheim's model, but also on  $x$ ;  $\mu(q | s, x)$  is then defined as the "probability distribution representing the receiver's beliefs about which types  $q$  send observed signal  $s$  and information  $x$ "<sup>4</sup>. After observing the endogenous signal sent by the type, the receiver will reward the sender with the sender's expected quality. Ideally, in a signaling equilibrium with perfect separation, each type's expected payoff should equal her true quality:  $E\mu[q' | s_{q,q}] = q$ . Yet, as the authors point out, there might be some level of uncertainty related to the efficiency of type recognition.

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4 Quote from "Too cool for school? Signalling and countersignalling", Feltovich, Harbaugh and To; Journal of Economics (2002, p. 635).

Analyzing a case in which senders play the following strategy:

$$s^* = (s^*, s_M^*, s^*), s_M^* > s^*$$

Medium type's payoff will then simply be:  $E\mu[q' | s_M^*, q] = M$ ; on the other hand it is challenging under these circumstances to recognize high and low types since they are sending the same signal, as it might happened in an imitation scenario.

Low and high types expected payoff will then have to be weighted for the beliefs of the receiver and the probability distribution of information  $x$ :

$$E\mu[q'|s^*, q] = \int_{x \in X} [\mu(L|s^*, x)L + \mu(H|s^*, x)H] g(x|q) dx$$

In a standard signaling game without extra information, high types would be better off just by deviating from signaling with  $s^*$  and choosing a higher level of  $s$  avoiding the risk of being associated with low types; however, in this model, allowing for extra information to be known to receivers means that high types might be recognized anyways even without signaling. As a result, if Highs and Lows are sufficiently separated by the exogenous information available, Highs would prefer a *non monotonic signaling strategy (countersignaling)*, rather than choosing a level of  $s \geq s_M^*$  and pooling with medium types. Formalizing the conditions under which this is possible according to Proposition 3 of the model:

*In a separating equilibrium where Highs do not signal  $\int_{x \in X} |g(x|L) - g(x|M)| dx$  and  $\int_{x \in X} g(x|L) g(x|H) dx$  are sufficiently small.*

The urgency of medium types to signal their status is explained by Proposition 3 which shows an insufficient amount of information to allow receivers to distinguish Mediums from Lows. High types instead, face a different situation: the distribution of exogenous information is such that Highs will be distinguished from Lows without the need of sending a signal; indeed the probability of having the same exogenous information about a low and a high type is assumed to be very in Proposition 3. Actually, choosing to signal in this case might be risky for the ones with higher status, since when information is already sufficient

to differentiate low types from high types, signaling can lower a high sender's estimated type.

### 2.2.2 Comparison and Considerations about the model

Opposite to Bagwell and Bernheim's model, this time signaling from high types is *strictly non-monotonic*, since lower levels of signals (or no signaling at all) are chosen by the higher class as an optimal strategy; this shows how introducing more information into the standard signaling model has important implications in terms of findings. As counter intuitive as it might seem, this behavior is frequently observable among luxury goods consumers: sometimes subtler ways of status showcase are preferred by the wealthier clients, who purposely select a less explicit luxury good compared to what other buyers would purchase. Still, this kind of buyers are far from being understated due to their unusual choice, why is that so?

### 2.2.3 A Marketing Study

*“Logos often fill the need for communicative synthesis pushed to its extreme: a maximum amount of information in a minimum number of signs”*

Chevalier & Mazzalovo, “Luxury Brand Management: a world of privilege”, 2012

A recent study published on the American Marketing Association<sup>5</sup> about *brand prominence* shows an interesting tendency of high types towards a “quiet signaling” strategy. In this study, the social classes were divided into four groups according to the type of signal (loud or quiet) they were most likely to use and their aspirations and need for status. Proletarians, as the study calls them, have low need for status and no interest in signaling through luxury goods consumption. This group appears to be new with respect to the models discussed so

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<sup>5</sup> Signaling Status with Luxury Goods: The Role of Brand Prominence, Han, Nunes and Drèze; Journal of Marketing (2010).

far, which just considered low types willing to signal and having the need to pool with and to be recognized as high types. A group that is well identified with the concept of low type instead, is the Poseurs group, these individuals characterize for a high need for status, willing to mimic the higher classes but not having the necessary financial resources to do so. We then have a sort of in-between group, the Parvenus, which might resemble to some extent the medium types group described by the previous countersignaling model. Parvenus are described as having the same financial resources as Patricians (the highest class) and manifesting a high dissociation need from lower classes (from poseurs in particular) and strong association need with Patricians. Surprisingly, or maybe not, this last class, the high types group as it has always been address so far, shows a somewhat lower need for status and hence a considerably subtler way of signaling. This particular group uses a *horizontal, quiet signaling* addressed to the members of their same class only; again, this is indeed a case of non-monotonic signaling choice, for what might appear an understated piece to some people, might actually be recognized by others as a superior good. This is due to some distinctive features of the good, that only members of the same social class can recognize since they are the only ones able to afford such a piece. It is quite interesting to see how in this case the signal loses part of its informational value which is sacrificed in favor of status recognition from a narrower group. This kind of dynamics have indeed been addressed by luxury brands manufacturers who pay serious attention on the way their brand is displayed on the goods they are selling; such concerns are indeed widespread among many sectors like luxury cars and high end fashion in particular. Most of the fashion houses have different lines which are characterized by a different way of marking the product and consequently by different price tags; it is not surprising that regressing the price of the good on brand prominence shows a negative relation between the two variables (Figure 3).



Variable	Parameter	t-Statistic	p-Value
Intercept	4401.83	15.34	<.01
Surface	-.24	-.50	.61
Canvas	-3039.76	-9.83	<.01
Leather	-2534.13	-8.38	<.01
Surface × canvas	1.10	2.15	.03
Surface × leather	.90	1.74	.08
LV	-481.60	-3.20	<.01
Prominence	-122.26	-4.95	<.01
Prominence × LV	95.89	3.44	<.01
N = 417, R <sup>2</sup> = .54, F = 60.05			

Figure 3: Statistics for the Relationship between Brand Prominence and Price. Source: Signaling Status with Luxury Goods: The Role of Brand Prominence (2010).

interaction term between brand and prominence “ProminenceLV”. The range of prices of handbags sold in 2008 spanned from 225\$ to 3,850\$ for LV and from 295\$ to 9,690\$ for Gucci, indicating a much wider price variation for Gucci than for Louis Vuitton; this last fact is indeed reflected into the two different regression slopes: the  $\beta$  value for Gucci is -122.26 and the one for LV is -26.37 (-122.26 + 95.89). The numbers show that other factors being equal (the handbag fabric, the handbag dimension), varying just for the degree of brand display yields, on average, a decrease in price up to a 856\$ for the loudest (Prominence = 7) Gucci bags and a decrease up to 185\$ for Louis Vuitton’s. Even though the price differential implied by a change in the style of the bag from quiet to loud is much greater for Gucci, in both cases a subtler brand identification is priced with a higher markup.

This study can be summed up with two main implications consistent with the theoretical models discussed in this section:

- (1) Different social groups willing to signal and to differentiate, do so according to their economic possibilities; the big variation in price observed moving from the bottom to the top of the product line allows the brand to satisfy such an heterogeneous customer base.

The data shown were collected from the authors in 2008 from Gucci and Louis Vuitton websites and they are relative to 417 handbags sold online by the two brands in that year; brand display was scaled from 1 (quiet or no logo display) to 7 (loud logo display) and represented by the variable “Prominence” along with the

- (2) The higher markup charged for the “quieter” luxury pieces seems to reflect a non-monotonic signaling tendency of wealthier customers who pay a conspicuous amount to be further distinguished and recognized, but just within their very own social group.

These two main findings are well in line with the main intuitions behind both of the previous models about Veblen Effects and Countersignaling; it is important to note, however, that the fit of this regression is not particularly strong (54%) meaning that brand prominence, handbag fabric and handbag dimension alone do not fully explain and justify the price differentials that characterize different bags styles. There must be some other factors like the popularity of some staple iconic pieces of the brand or some managerial considerations behind the price of particular items that are more difficult to take into account into data driven studies.

# FASHION IMMEDIACY: A GAME THEORY PERSPECTIVE

*“[Fashion] satisfies in no less degree the need of differentiation, the tendency towards dissimilarity [...], because fashions differ for different classes”.*

Georg Simmel, “La Moda”, 1985

In light of the recent shift of some high-end fashion brands to the “*see-now, buy-now*”, I would like to explore an industrial organization model on fashion cycles by Pesendorfer to analyse the consequences of immediate availability of designs and shortened fashion cycles. After a brief overview on the causes behind fashion immediacy, I will go through the predictions of Pesendorfer’s model and then compare the strategies of two important players in the fashion market to assess to what extent the model adapts to reality.

The “*see-now, buy-now*” approach has developed throughout 2016 in response to the overwhelming request of consumers to make collections available straight after appearing on the catwalk<sup>6</sup>; this need for *instant gratification* has been largely boosted by the constant presence of the social media in the everyday life of buyers. The Internet has been sensibly shaping the luxury world reducing the perception of product scarcity, and inducing many high-end brands to sell online moving the luxury experience from the store to the website. In this ever changing and uncertain scenario, companies started to increasingly rely on selling entry level goods to enlarge the customer base appealing new (and most of the times younger) buyers, threatening their long term profit potential. Overall, technology has made fashion more “democratic”, in the sense that decisions and judgements about the brand are no longer up to a small portion of VIP customers, but they are also in the hands of a larger and growing stake of *aspirational buyers*: the middle class. In February 2016, Burberry was the first major fashion house to publicly announce the adoption of the “*see-now, buy-now*” model in an attempt to capitalize on the raising demand for fashion immediacy; the British

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<sup>6</sup> “The State of Fashion 2017”, McKinsey & Company (2016).

luxury brand was then followed by Tommy Hilfiger, Paul Smith, later on by Moschino, debuting with its capsule collection “Designer Drug”, and many others<sup>7</sup>; fashion shows have never been the primary source of revenues, on the contrary, they are a huge but necessary investment which constitutes one of the most burdensome costs (along with flagship stores) for the companies operating in the luxury world. Embracing fashion immediacy might represent a clever move to increase the return on running fashion shows, but how does this instantaneous availability of the products match with the luxury world (if the two things match at all)? The industry has not been united on such an issue: the two biggest luxury groups, Kering and LVMH, and the Camera Nazionale della Moda Italiana all agree on the fact that the “see-now, buy-now” model negates the *luxury dream* and that the brands adopting it are overestimating the spike generated by fashion shows and underestimating the importance of time to create desire in the minds of consumers. On the other side, Avery Baker, Chief Marketing and Brand Officer of Tommy Hilfiger, stated that relying on status quo nowadays is a “risky illusion” and that this transition period that the whole fashion and luxury industry is facing, represents the right occasion to be disruptive and realign with the needs of the customers. Also Christopher Bailey, current CEO of Burberry, showed to be of the same line of thought, seeing no real threat of fashion immediacy for the image of his brand, but actually conceiving an harmonious coexistence of luxury’s timelessness and speed of technology. The strategies of these last two brands will be subject of study later on in the section. There is no doubt, however, that fashion, even if ephemeral, has a great signalling power and serves as a very effective social signifier in many circumstances; it is then possible to go back to some already explored signalling and matching dynamics to analyse the implications of disruptive changes in the length of fashion cycles. The following is a model about this issue.

### 3.1 The Screening Role of Fashion in Pesendorfer's Model

In his “Design Innovation and Fashion Cycles”<sup>7</sup> Pesendorfer develops a complex model built on “dating game” - matching dynamics, where designs are used by consumers as signalling devices. Unlike the Bagwell and Bernheim's model, this particular game allows for the use of the conspicuous good in a “one unit at a time” manner, therefore the option of signalling through higher quantity (for a lower price) cannot be taken into consideration. In this section, the equilibrium outcomes of two different competitive scenarios along with their implications on the efficiency of the matching process, will be compared and explained.

#### 3.1.1 The Monopoly Case: Elitist and Egalitarian Fashion Cycles

In the first scenario, the designer is assumed to be a monopolist in the market; he can create a new design (call it  $n$ ) every period at a cost  $c$  ( $c > 0$ ) and can decide, after a sufficiently large number of consumers has adopted his style, to innovate again and start a new fashion cycle making the old design obsolete. The design worn by each player is publicly observable. Consumers are still divided into high types (H) and low types (L), in particular: call a general consumer  $q \in [0,1]$ , if  $q \leq \alpha$  then  $q$  is a high type, while if  $q > \alpha$  then  $q$  is a low type. Both kinds of player prefer (and aim) to be matched with a high type *but* high types get a greater benefit from dating their own type compared to low types. Formalizing the last assumption:

$$U_H(H,H) - U_H(H,L) > U_L(L,H) - U_L(L,L)$$

Call the left-hand part of the inequality  $v_H$  and the right-hand part of the inequality  $v_L$ .

Since  $v_H$  is greater than  $v_L$ , it is implied that the loss faced by a high type who is “mismatched” with a low type, is greater for the former. Utility is then a function of both

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<sup>7</sup> Design Innovation and Fashion Cycles, Pesendorfer, The American Economic Review (1995).

the other player's type and the player's own type; total utility is derived by subtracting the money spent in purchasing the new design to the matching payoff.

The rules of the game are as follows:

1. Consumers wearing the same design will be matched randomly with each other;
2. If a consumer is the only one wearing a particular design she will be matched with a consumer who did not purchase any design ( $n=0$ );
3. There is always a small group of consumers who uses no design ( $n=0$ );

Call  $\mu_i(n)$  the fraction of consumers of type  $i$  ( $i = H, L$ ) using the design  $n$ ; the following assumptions on matching outcomes probability can be made:

(1) For a consumer using the design  $n$ , the probability of meeting a high type will be:

$\mu_H(n)/[\mu_H(n) + \mu_L(n)]$  where  $\mu_H(n) + \mu_L(n) > 0$ .

(2) If everybody is using a design [ $\mu_H(0) + \mu_L(0) = 0$ ], then for a consumer who chooses to use no design ( $n=0$ ), the probability of being matched with a low type is equal to 1.

(3) On the other hand, if nobody is using a design [ $\mu_H(n) + \mu_L(n) = 0$ ], a consumer who bought a certain design will have the same probability of meeting a high type as in the case in which she is using no design ( $n=0$ ).

### 3.1.2 The Demand Function

So, what happens when the designer introduces a new design? Given that each consumer cares exclusively about her utility, the demand for the new fashion introduced will depend on its capability of increasing the probability of meeting a high type.

$$f(q) = \begin{cases} \frac{1-\alpha}{1-q} v_H & \text{if } 0 \leq q \leq \alpha \\ \frac{\alpha}{q} v_L & \text{if } 1 \geq q \geq \alpha \end{cases}$$

If  $0 \leq q \leq \alpha$  then  $q$  is a high type and if she chooses to use the new design she will be matched with another high type with probability 1. Whereas, if she decides not to use the design, she will have to face a more uncertain outcome where the fraction of high types is given by  $(\alpha - q) / (1 - q)$ .

Under these circumstances a high type's reservation price for the design will be given by the benefit gained from meeting a high type times the increase in probability of being matched with a high type through using the design:  $v_H \cdot [(1 - \alpha) / (1 - q)]$ .

If  $\alpha < q \leq 1$  then  $q$  is a low type and if she chooses not to purchase the design she will be matched with another low type with probability 1. On the other hand, if she decides to use the new design she will have a  $\alpha/q$  probability of matching with a high type. The highest price a low type will be willing to pay for the design will then be:  $v_L(\alpha/q)$ .

For  $q \leq \alpha$  the demand function is increasing, representing a Bandwagon<sup>8</sup> effect where the more high types purchase the good the more demand raises. Also, under these conditions the importance of the design is crucial since there is a small chance of being matched “with the right people” without it.

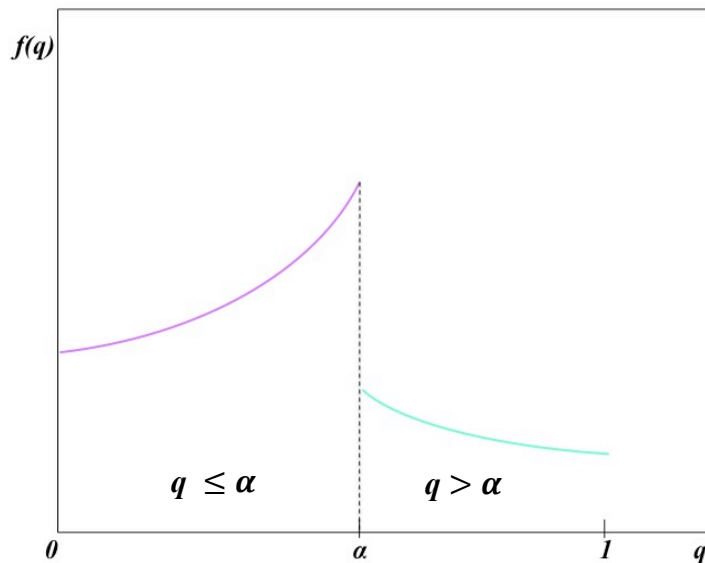


Figure 4: Bandwagon & Snob effects in the demand for the new design

<sup>8</sup> Bandwagon, Snob and Veblen Effects in the Theory of Consumers' Demand, H. Leibenstein, The Quarterly Journal of Economics (1950)

At  $q = \alpha$  demand reaches its maximum, at this point all high types have purchased the new design while low types have not, due to this clear separation in this particular situation whoever decides not to use the new design is matched with a low type with probability 1. For  $q > \alpha$ , the probability of meeting a high type conditional to the use of the design progressively decreases due to the enlarged pool of people owning the new fashion, which, this time, includes low types as well. The negative slope of demand pictures the Snob effect arising from these circumstances.

### 3.1.3 Length of Fashion Cycles under Monopoly

The designer decides whether or not to start a new fashion cycle every period. Innovating implies a cost for the designer hence, for a new design to be worth being created a condition must be met: innovation costs must be lower than the present value of revenues at the beginning of the period. Whenever the benefit from innovation (positive net present value of profits, call it  $R(q)$ ) exceeds the gain from selling the old design for one more period (extending the previous fashion cycle), a new design will be created with probability 1 ( $\pi = 1$ ). For the design to be valuable in the eye of the consumer, it must increase the chance of achieving each type's desired match; this is only possible if a coordination problem is solved inducing a large enough number of consumers to purchase the design. Solutions to this coordination problem are marketing and PR actions. The speed at which the design spreads across consumers is also up to the designer, this decision turns out to be crucial in determining the type of fashion cycle, which can be either elitist or egalitarian in the monopolist designer case.

In an *elitist fashion cycle*, all the high types use the design, while low types never purchase it or can afford to own it only after a new fashion cycle has already started (and that design is made obsolete). As explained in the above section, the designer faces an increasing demand function up until a certain  $\alpha$  level, however, in an elitist fashion cycle, not all high types get to own the design in the first period straightaway. An elitist fashion cycle would require the designer to innovate as soon as all the high types use the design. Making the new fashion immediately available to all the high types would imply that the designer will



innovate again soon. In a matching perspective, the *length* and the *number of social interactions* resulting from the dating mechanism would be heavily restricted whenever the pace of diffusion of the new design is set to be fast by the designer. Due to this time reduction, the signaling value of the new fashion, hence part of its economic value, would decrease as well. An elitist fashion cycle is characterized not only by a longer duration, but also by higher prices; such a cycle is more likely to take place whenever the spread between  $v_H$  and  $v_L$  is high and the designer incurs in higher innovation costs upfront, which would make frequent creation of designs unprofitable.

An *egalitarian fashion cycle* instead, allows for the spread of the new fashion among all the social groups; high types will purchase the design sooner at a slightly higher price and in the following periods low types will have access to it as well. The acquisition of the good from high types is faster in this case and the innovation cost for the designer is lower as well as the established prices.

To define the consumers' payoff from purchasing the design call  $x_t$  the consumer's endowment of the current design,  $y_t$  the consumer's purchase made in the current period  $t$  and  $v_t(x_t)$  the probability of meeting a high type conditional on using the design. Let  $\delta$  be a discount factor and  $1 - \delta$  indicate the length of one period.

To get the consumer's expected payoff each utility outcome must be weighted for its probability and multiplied by the period length, the expenses related to the purchase ( $p_t y_t$ ) will be subtracted:

$$\pi_i(x_t, y_t, p_t, v_t) = (1 - \delta) \cdot \{v_t(x_t) \cdot u(i, H) + [1 - v_t(x_t)] \cdot u(i, L)\} - p_t y_t$$

As in a repeated game, the overall consumer payoff will be given by taking the sum of all the periods discounted payoffs:

$$\sum_{t=1}^{\infty} \delta^{t-1} (x_t, y_t, p_t, v_t)$$

Other things equal, the longer the fashion cycle, the higher will be the consumer payoff, this is because the matching time is expanded in a longer fashion cycle and so are the interaction possibilities; overall it is easier to charge customers more for fashions that are created to last rather than for those that spread quickly and that are replaced straightaway.

In a similar way, the payoff of the designer will be given by the discounted sum of profits raised throughout the current and past fashion cycles.

To sum up, monopoly allows for the realization of either of the two fashion cycles outcomes described above, leaving to the designer the freedom to set the different price levels for every period and the speed of the acquisition of the design.

### 3.1.4 Competition: An Efficient Matching Outcome

So far, only the monopolist designer case was analyzed, however when the author relaxes this assumption allowing for a more competitive environment, important implications arise. Let  $N$  indicate the number of active designers in the market,  $2 \leq N < (\alpha v_L)/c$ , and let  $c$  be the cost of innovation faced by each designer  $c < (\alpha v_L)/2$ . Pesendorfer designs a subgame-perfect equilibrium in which: all the  $N$  designers come up with a new design each  $T$  periods;  $v_L(1 - \delta^{T+1-t})$  will be the price of the design  $t$  periods after its creation with  $t \leq T$ , for all  $t > T$  the price of the design will be 0. Each high type chooses to purchase a design among those currently offered in the market, low types never make a purchase for a strictly positive price. In the monopoly case it was shown how the designer could afford making the new fashion available at lower prices to low types performing a sort of price discrimination, however in this case reducing price under its equilibrium level is very risky. High types will perceive the lower markup as a sign that the design is going out of fashion, hence it is being sold off; however now there is a larger pool of firms creating new designs, which means that it is possible for high types to sell their current design and buy an alternative one from a competitor. Once this process starts, the design progressively loses its value until its price reaches 0, at this point low types will start to buy it. It would make no sense for high types to keep using the design especially after the price reduction since there would be a higher chance of being mismatched at that point, so the equilibrium outcome would imply selling the design and using a different one.

Competition ensures the efficiency of the matching mechanism through the imposition of a minimum price threshold  $[(2c)/\alpha]$ , derived by the assumption that  $c < (\alpha v_L)/2$  under which the designer would make no profits; overall competition enhances the power of fashion to

be an effective screening and matching tool. Indeed, the equilibrium outcome under competition is an elitist fashion cycle, while under monopoly both elitist and egalitarian outcomes were possible making more uncertain the effectiveness of design innovation as a differentiation instrument. Competition yields longer fashion cycles, where  $\delta$ , which is defined as the “minimum amount of time that elapses before the designer can change the price of its design”, is close to 1, implying a less rapid decline of price.

### 3.1.5 Implications of The Model

Going back to the dispute about whether the fashion immediacy strategy should or should not be adopted, it is possible to make some considerations in light of the model just analysed.

Pesendorfer shows that in either case, under monopoly or competition, a shorter fashion cycle reduces the signalling power of the design, so of the collection, that has been launched; this is mainly due to the reduced number of interactions that people can make before a new cycle is started and the current fashion becomes obsolete. A design that takes more time to spread is also a design that can be better understood and that acquires more cultural significance as the time passes; it is perceived as scarce due to the slow and long time that passes before having the chance to be acquired. Luxury brands are known to build their sales slowly and increasingly over time, while traditional fashion follows a cyclical pattern based on “seasonal obsolescence”. Luxury ready-to-wear has the difficult task to combine the two things together, following the fashion cycle but at the same time creating iconic pieces that never go out of fashion, in this view the “see-now, buy-now” model seems a too risky move for many high fashion brands, which explains why the two big luxury groups LVMH and Kering took such a stance against fashion immediacy.

Many high fashion designers relied on the traditional approach to build a stronger image of the brand, also luxury goods usually take a long time to be produced since no process in the value chain is delegated: true luxury is about “total control” on every step of the creation, development and distribution of the product (Kapferer & Bastien, 2009). Chanel opened its own production factory when stretching and expanding into the watch industry; such an

investment implies lower volume of units produced (controlled scarcity), higher prices and a long-term orientation of the life of the product. A brand that faces such times and costs of production would not create an item destined to be replaced in a six months time, cost of innovation was indeed a crucial element in the Pesendorfer model determining the length of the fashion cycle.

The time factor is for sure another very important element, if not the most important, that traces the line between luxury and fashion: luxury sells timeless value whereas fashion is ephemeral and continuously adapting and evolving.

However, with the advent of fashion immediacy the boundaries between these two worlds have been blurred and some brands are actually merging features of both models to better adapt to today's technology driven consumer behaviour. The following section analyses the case of two very different brands choosing the same strategy.

### 3.2 Disrupting the Fashion Cycle: Opportunity or Threat?

As anticipated earlier in this section, Tommy Hilfiger and Burberry have been the first among the most well known fashion houses to pivot towards the “see-now, buy-now” model; even if adopting the same strategy, the two brands are not only different in their culture, target and positioning but also in the business model they have employed so far.

Kapferer identifies three main branding models on the basis of positioning and strategy: Luxury, Premium and Fashion<sup>9</sup>; this classification will be used to assess where the two companies have been positioned before their switch to fashion immediacy and where they are heading to through this strategic choice.

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<sup>9</sup> Kapferer, J.N., “The New Strategic Brand Management: Advanced Insights and Strategic Thinking”, Kogan Page Publishers (2012)

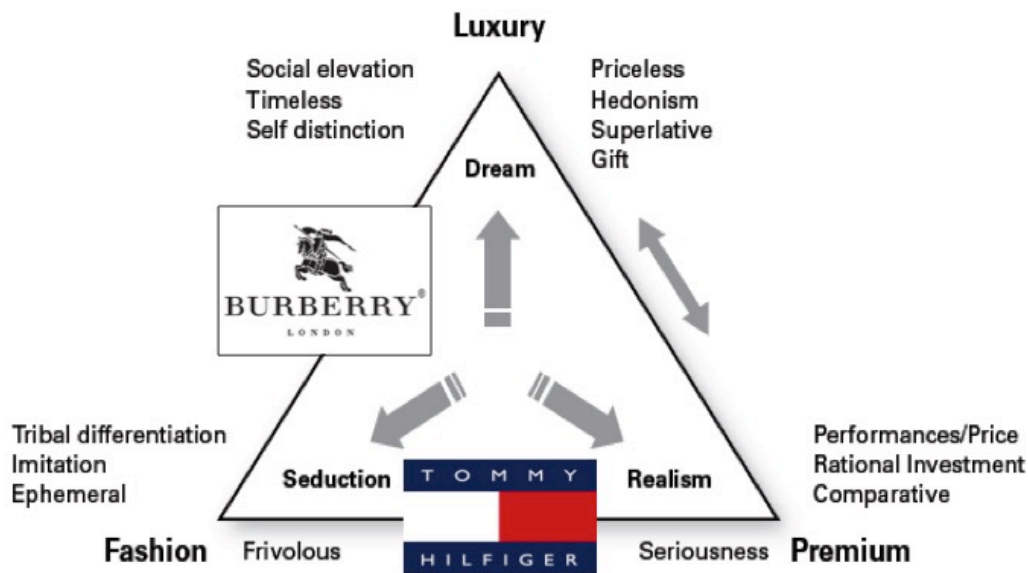


Figure 5: Kapferer’s Luxury, Fashion and Premium Positioning Triangle Applied to Burberry and Tommy Hilfiger

### 3.2.1 Embracing the Risk: Tommy Hilfiger’s Strategy

*“We are in this incredible time of transition. [...] Consumers’ behaviours and mindsets are changing by the minute, and we really felt that if there was ever a time to be disruptive this was it; because the status quo can be a very tempting but a very dangerous illusion.”<sup>10</sup>*

Avery Baker, Tommy Hilfiger’s Chief Marketing and Brand Officer

#### ❖ Company Profile and Positioning

During Wharton Retail Conference in 2010, Hilfiger defined his brand as “Premium, affordable, accessible, cool, American classic”, indeed this “quintessential American” lifestyle brand is for sure a good example of what has been addressed as the new-luxury (Silverstein & Fiske, 2003) or, more specifically, as an example of premium brand.

<sup>10</sup> Avery Baker’s speech “How can fashion immediacy really work?” at BoF Voices | Retrieved from: <https://www.youtube.com/watch?v=sPuPcyHoIMA>

With its three main lines (Tommy Hilfiger, Hilfiger Denim and Hilfiger Collection) Tommy Hilfiger is priced well below luxury but still above fast fashion and mass prestige brands such as Zara: a TH's denim is much more affordable than Armani's, more expensive than Zara's and yet very similar in price range with Levi's.

With its inclusive and youthful spirit, the brand has always appealed middle-market, young consumers, through a strong attachment and celebration of pop culture and a laid back but classic style.

From the very debut, Tommy Hilfiger has always been a very competitive and *comparative* brand, in contrast with a traditional luxury label that by definition is *superlative* and cannot have any equivalent (Kapferer & Bastien, 2009).

Evidence of this comparative nature can be found in TH's very first advertisement for Times Square in 1985, also known as the "Hangman Campaign": a plain white billboard featuring the initials of three well known designers, the first one being Ralph Lauren ("RL"), which is still one of the brand's major competitors, followed by Perry Ellis ("PE") and Calvin Klein ("CK") along with the initials of Tommy Hilfiger being announced as the next great menswear designer.

Such a marketing campaign would not fit very well with the image of a luxury brand, but Tommy

Hilfiger has never pretended or claimed to be one, even if its designer has definitively "looked up to those brands" (referring to Louis Vuitton, Gucci and other big names in the luxury industry) as models to aspire to; however the main strategy chosen throughout the years has always been to prioritize on being an affordable premium designer brand and always keeping a careful eye on reality to better anticipate and satisfy the ever changing consumers' mindsets. Overall, Tommy Hilfiger is a very inclusive and accessible brand,



Figure 6: The "Hangman Campaign" by George Lois for Tommy Hilfiger, 1985; Source: anothermag.com

which makes “preppy, cool and casual” its characterizing vibes, using reality and its “learning experiences” as the main drivers for managerial choices. These considerations led me to position Tommy Hilfiger in the rightmost part of Kapferer’s triangle, in the Premium business model section, due to its strong awareness and constant adaptation to reality (the Realism element) and to its comparative nature; however the brand has been recently shifting towards a more fashion oriented business model which makes me view the brand as halfway between the Premium and the Fashion positioning (Figure 5).

#### ❖ TommyxGigi: Rationalizing The Fashion Cycle

In February 2016, the brand has brought its “always evolving” philosophy to the next level publicly announcing a radical change in its fashion calendar: the adoption of the “see-now, buy-now”. Aimed at recovering the customer engagement that the traditional fashion cycle has always constrained by disconnecting the consumer’s excitement for the new collection from its actual availability, the embracement of fashion immediacy was a brave and disruptively innovative move. During the BoF Voices conference, Avery Baker, TH’s Chief Marketing and Brand Officer, talks about the very ambitious goal behind the brand’s strategy: repositioning Tommy Hilfiger’s half a billion worth women’s business, bringing a whole new range of fans to the brand. Due to the dimensions of the company, switching to fashion immediacy was extremely challenging in terms of logistics and supply chain: the TommyxGigi collection, accounting for a total volume of 4 Million products, had to be available in the stores and “livestream shoppable” on the same date, at the same time all over the world.

Baker identifies four key steps that led the company to succeed in its objective, the first one being “*unlocking the entrepreneurial spirit of the company*” ensuring free flow of ideas in every division of the business, the second step was “*investing in retail partners*” making sure to deliver an equally pleasing customer experience in the wholesalers’ channels as in their own ones. The third and main step was to “*invest in digital commerce innovation*”: an AI powered conversational commerce chatbot named TMY.GRL was created in partnership with Facebook to better engage with the fans of the brand and bring a whole new level of accessibility and personalization; moreover interactive digital selling screens were available

both in New York South Street Seaport, where the fashion show took place, and in several other cities. The fourth and last step was “*great teamwork, collaboration and trust*” which were crucial to allow fast track production to work smoothly and ensure the correct and timely execution of all the activities related to the collection and its distribution.

Another distinctive aspect to mention is for sure the “Gigi Effect”: the model Gigi Hadid, the face and partner of the collection, really added a tremendous amount of visibility to the brand’s initiative due to her strong following and presence on the social media; she truly represented the new woman Tommy Hilfiger wanted to connect with and the new demand for social immediacy.

#### ❖ The Results

According to what reported by Avery Baker during BoF’s Voices conference in 2016, Tommy Hilfiger women’s business grew globally by 20% in terms of sell out versus the prior year (2015); the company not only had a great success in selling the Fall 2016 line but it was also able to drive more sales in their higher level product offerings. Many key wholesale partners of the brand, after only two months of having the products on the floors, registered a 60% sell through. On social media the initiative of the brand had great resonance, generating 2 Billion impressions of which only the 20% was caused by the company’s own posts.

Lastly, it was observed an overall increase in Tommy.com website traffic, the most relevant one being in the US platform whose visits increased by 900% compared to the previous year; furthermore the company found out that the 70% of the new traffic (still relative to the US platform) was generated by consumers completely new to the brand: this percentage is really impressive and meaningful of the effort that Tommy Hilfiger put into raising more brand awareness and gaining an enlarged pool of customers. Overall the “see-now, buy-now” strategy turned out to bring to the company outstanding results even beyond the predetermined goals.



### 3.2.2 Burberry: Merging Creativity and Craft with Technology and Speed

*“There is no rulebook, there is no formula. What I do know is that everyone around us is changing: the way they live, work, shop, engage, are entertained. [...] Everything is changing. Our industry is not immune to that change.”<sup>11</sup>*

Christopher Bailey, Chief Creative Officer and CEO of Burberry Group

#### ❖ Company Profile and Positioning

Originally born as an outerwear attire manufacturer in 1856, Burberry has become an outstanding representative of the British luxury market and culture.

Through the years, the company has progressively gained tremendous notoriety in high fashion by expanding its product offerings into ready-to-wear, fashion accessories, fragrances and, recently, into cosmetics; the brand is best known for its distinctive check pattern and its iconic trench coats. The expansion into fragrances and cosmetics was a strategy of the brand aimed at constituting a robust entry level products category; brand extensions such as these ones are common to many luxury manufacturers and used to boost sales and build awareness in buyers new to the company. “Burberry Brit” and “This is Brit” fragrances are two examples of how the company successfully engaged with a new target audience (Millennials and Generation Z); Burberry’s make-up line was introduced later on in 2010, with the intent to enlarge the entry level product offerings, but has struggled to take off in today’s very competitive beauty business. In 2013 the company bought back the licences on its cosmetic products bringing the beauty business in-house to better control its trademark; however, four years later, in April 2017, Burberry reversed its strategy partnering with Coty Inc., one of the world’s leading beauty companies, agreeing on a long-term exclusive global license on its beauty products<sup>12</sup>. According to the deal, the British luxury house will continue to handle the marketing side and any other consumers-facing

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<sup>11</sup> Bailey, Christopher for “Tim’s Take: Burberry Autumn/Winter 2017”. Blanks, Tim | The Business of Fashion, Sept. 22, 2016

<sup>12</sup> Coty Inc. Declaration on coty.com website, News Section, Apr. 3, 2017. Accessed on June 2, 2017 | Retrieved from: <https://www.coty.com/news/coty-enters-strategic-partnership-burberry-acquiring-exclusive-long-term-license-rights-0>

aspects, while Coty will be crucial in helping with the distribution thanks to its extensive network and industry expertise<sup>13</sup>. This partnership is expected to make Burberry's beauty category grow and reduce the company's fixed costs related to the direct control of this product category.

Overall, Burberry is very classic and traditional in its own values and image but, at the same time, has always been in the frontline of technological innovation, increasingly blurring the lines between physical and virtual throughout its evolution. In an interview for the "Future of Storytelling"<sup>14</sup>, Angela Ahrednts, previous CEO of Burberry, now vice president of retail at Apple Inc., talks about how the Regent Street Burberry flagship store was conceived: "We wanted you to feel when you walked in the front door as if you were actually walking into the website"; indeed the store itself is very avant-garde mirroring in digital screens some of the sections of the brand's website like Burberry Acoustic (a project involving young British bands, another initiative of the brand aimed at achieving a deeper connection with Millennials).

It is clear that this British fashion house has kept through the years a very technology forward perspective while still being characterized by a very traditional and classic taste; every customer of the brand not only buys excellent craftsmanship but also a piece of "britishness" and heritage that make both the company and its clients feel special, elevated and unique. Burberry is definitively to be positioned in the luxury section of Kapferer's triangle thanks to many of its creations, like its classic trench coat, that contributed to build an iconic and timeless aura around the brand; the company showed to have invested quite some effort in communicating with the younger generations especially through the use of innovation. The company's choice to transition into the "see-now, buy-now" is then consistent with the strategies adopted so far, but many have wondered how a luxury brand of Burberry's calibre would have dealt with the ephemerality implied by this more fashion-oriented approach.

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<sup>13</sup> Limey Hoang, "Burberry Retreats on Beauty Strategy, Signs Deal with Coty", *The Business of Fashion*, Apr. 3, 2017. Accessed on June 2, 2017 | Retrieved from: <https://www.businessoffashion.com/articles/news-analysis/burberry-signs-beauty-deal-with-coty>

<sup>14</sup> Ahrednts, Angela for *The Future of Storytelling 2013: "Authentic Branding for a Global Audience"*, Sept. 16, 2013, Accessed on May 30, 2017 | Retrieved from: <https://www.youtube.com/watch?v=krQG2Hceov4>

## ❖ Art: Burberry's Way Of Escaping The Ephemeral

It was unexpected, but not totally surprising, that Burberry would have caught the “see-now, buy-now” as an opportunity to bring even farther its process of innovation and digitalization.

The Spring/Summer 2017 show was already the second runaway-to-retail collection of the brand and merged, as in the Autumn/Winter one, menswear and womenswear together on the catwalk, another very unusual (but cost efficient) thing for the traditional fashion calendar. If combining the two shows into the same runaway was something that Burberry never did before, livestreaming was definitively not new to the company: back in 2009 the collection Burberry Prorsum Spring/Summer 2010 was the first fashion show that the brand broadcasted live.

Differently from Tommy Hilfiger, Burberry had a very important issue to deal with: giving to the customers the immediacy they were asking for, without compromising the creation of timeless, long term value, crucial for keeping high the name and the status of a luxury brand. The way the company escaped this “immediate but timeless” paradox is really fascinating. Burberry's first “see-now, buy-now” collection was the result of an attentive study on Henry Moore, an English artist best known for his monumental bronze sculptures, who heavily influenced and shaped the vision of Christopher Bailey, currently in charge of the dual role of CEO and Chief Creative Officer. Infused with this strong artistic content, the whole collection echoes the structure and monumentality of Moore's creations and appears to be very permanent, almost immortal like a work of art. By establishing this bond, Burberry overcame the boundaries between fashion and luxury and merged craftsmanship, art and culture with technology immediacy. The result was an extremely sophisticated collection, highly valuable for its artistic content, which was made available in a more innovative and customer oriented way; the image of Burberry as a luxury brand did not seem to be questioned or threatened at all, on the contrary the company proved its ability to embrace change without losing its core values.

## ❖ The Results

Burberry did enjoy a 40% boost in UK sales at the end of 2016<sup>15</sup>, however this was not a direct consequence of the “see-now, buy-now” strategy, but was rather generated by the post Brexit weak pound. As a result of leaving the European Union, the depreciation of the British currency made the local luxury market relatively more affordable for tourists that increased their spending on goods denominated in pounds.

Due to this economic scenario, it is more challenging to assess whether the company has enjoyed an immediate benefit from its strategic decision, however it is undeniable that Burberry will serve as an important example to other luxury brands that will choose in the near future to break the traditional rules, embrace the change and innovate without losing their status. Key to the company’s strategy towards fashion immediacy are the strong relationship with art and the constant worship of the brand’s history and heritage operated both through Burberry’s online and offline channels.

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<sup>15</sup> Angela Monaghan and Sarah Butler, “Burberry sales soar”, The Guardian, January 19, 2017 Accessed on May 30, 2017| Retrieved from: <https://www.theguardian.com/business/2017/jan/18/burberry-sales-surge-thanks-to-weak-pound>

# CONCLUSIONS: CONCILIATING THE MODELS WITH REALITY

## 4.1 Pricing

With the contribution of Bagwell and Bernheim model it has been possible to identify the microeconomic conditions needed in order to explain conspicuous consumption behaviour of prestige seeking consumers; not only that, the tangency condition also helps identifying the price threshold differentiating luxury items from other categories like entry-level luxury, premium and mass prestige. This latter product category, mass prestige, is the one characterized by prices below the equilibrium threshold, constituting consumption bundles that are feasible for a greater variety of consumers and that lay in the “imitation area” identified in Figure 2. “Masstige” positioning allows to reach a wider customer base with respect to luxury by selling at attainable price points and offering products that are somewhat similar to the high-end ones.

Transitioning into a more complex signalling environment it was possible to explain variations in price related to variations in display of the logo of the brand; according to the countersignalling theory of Feltovich, Harbaugh and To, a certain category of consumers might want to communicate their status only to their social group of belonging or might not even have the need to signal due to information spillover. This situation is most likely to occur when dealing with buyers endowed with a higher level of resources, that will demand for exclusive pieces, branded in a subtler way, but provided with particular features identifiable only by individuals having the same status. Indeed, the data analyzed relative to Gucci and Louis Vuitton showed that both luxury houses charged a higher markup for pieces with less prominent brand display, probably due to the different level of sophistication, brand culture and signaling needs of that particular market segment.

## 4.2 The Impact of Technological Innovation on Matching Dynamics

All the luxury manufactures operate in a sort of monopolistic competition environment: there are few, well established and successful brands, each one producing unique (therefore not comparable) goods; even if each luxury house is one of a kind, everyone who plays in this scenario is able to influence through its strategic choices the other firms behavior and, potentially, the evolution of the whole industry. Pesendorfer's considerations about the length of fashion cycles and design innovation are a good starting point to analyze the current state of the luxury fashion industry. As the model points out, fashion is cyclical and each period length affects the efficiency of the matching process generated by the use of the design. For the most part, the predictions of Pesendorfer are very much in line with the traditional luxury approach which sees the fast spread of fashions as a threat to the core values of the industry. The less time people have to match with their desired group, the lower the value of the design as a social signifier; still according to the model, to guarantee a separating equilibrium and an elitist matching outcome, the diffusion of the conspicuous good should be slow even among the high type customers and is most likely to be achieved with a moderate level of competition. However, in a world where technology is the main driver of change and innovation, consumption habits have evolved quickly and social interactions are easier to make and happen at a faster pace than before. It might not be the case anymore that the duration of the fashion cycle affects so heavily the number and quality of social connections and, in turn, the value of the luxury good; today the showcase of expensive items and the achievement of status recognition is not limited to the physical world only but has progressively expanded into the virtual world of social media. As a result, status signalling in the modern environment can reach a greater audience in a sensibly shorter amount of time. These conjectures could not be anticipated at the time Pesendorfer's model was conceived, however taking into account the impact of technological innovation on matching dynamics could possibly lead to different implications from the ones the author predicted. The advent of the "see-now, buy-now" in the luxury world is the result of this technology driven evolution of consumers needs; the fashion immediacy model has been welcomed not only by premium brands like Tommy

Hilfiger, but also by notorious luxury manufacturers such as Burberry, that allowed for the instant availability of their collections without fearing a possible damage to the image of the brand.

These considerations about the actual evolution of prestige seeking consumers behaviour might provide the basis for the construction of a new matching model accounting for both kinds of social interactions (physical and virtual). The new features of the game would be translated in Pesendorfer's model with a decrease in the value of the term  $(1 - \delta)$ , however if in the original model this would lead to a decrease in the players' payoff, in the potential revised version of the game the impact of shorter matching periods on consumers benefit would be much lower if not inexistent.

Still, the debate about whether or not luxury brands should adhere to the "see-now, buy-now" model depends on factors that cannot be completely captured by industrial organization models and remains an important topic of discussion in today's evolving luxury industry. Both the traditional and the revised matching models could potentially offer a guideline to firms operating in this sector depending on the core values and on the propensity to innovate of the single organization.

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