CHAPTER 3: The Essence of Luxury, Unveiling the luxury value creation process

1. Types of benefits:

- Value creation is when something is worth more to you than what you pay for it.

(what you get compared to how much you give or pay)

- From the customer's POV: value is created when what they get is worth more to them than what they paid for it.
- From the company's POV: value creation is when they can make something that's worth more than what it costs to make.

(turning their inputs such as materials and labour to something more valuable).

3 types of benefits:

- **Functional (what the product can do)**
- **Emotional (how it makes you feel).**
- **Expressive (what it says about you or helps you say).**

Example: you're buying a pen. You might want it because it writes well (functional benefit), because it reminds you of your childhood (emotional benefit), or because it looks cool and shows off your style (expressive benefit).

- **These benefits cannot be separated, kind of like Aristotle´s way of persuading people through Ethos (Credibility), Pathos (emotion), and Logos (Logic).**

2. The functionality trap:

- Value can come from different types of benefits.
- Just like a speaker can convince people through EPL, companies create value using a mix of functional, emotional, and expressive.

This is called the functionality trap (using all 3 benefits).

Capsule 3.1:

- NYC Garbage selling cubes filled with garbage.
- Making people see garbage differently.
- Instead of just focusing on what something can do (practicality), NYC Garbage focuses on how it makes people feel.
- The company uses luxury language to make garbage seem special and valuable.

Example: they called their product ¨100% authentic¨ and ¨hand-picked from the fertile streets of NY¨.

➢ **This teaches us that even things without a practical use can be valuable if they make people feel something or say something about them.**

3. Normal competition:

Covers how luxury goods value differently from other products.

There are 2 competitive spaces where companies compete to crate value:

- **Normal competition:**
  - o The usual way in which companies compete.
  - o Focused on solving customers problems or needs.
  - o Mostly functional benefits.
  - o Logic and rationality play a big role in assessing value.
  - o **Limitations:**
- Price Premium (limits to how much they can charge). These premiums are relative to the average price in the market and breaking them is challenging because of consumer expectations based on functionality.

➢ **Normal competition sets the rules for how companies compete and create value, focusing on functionality, logic, and rationality.**

Functionality is key	• Functional benefits are fundamental and dominate the assessment of value.
Normal does not mean basic	• The product or service is not necessarily simple or basic. It represents any kind of offering, including sophisticated and innovative ones. • Normal refers to value creation and does not describe the product or service.
Emotional and expressive benefits are relevant, but not dominant.	• Emotional and expressive benefits are present, but not dominant in the assessment of value.
"Common sense": the importance of logic and rationality	• Together with the importance of functional benefits, we find the importance of logic and rationality.
Competition sets normality.	• Competition takes place the among many players providing a similar value offering where supply meets demand. • Differentiation is complex to achieve. This refers to the "normality" of the segment/market.
Breaking normality: price premium & economic logic.	• Breaking "normality" is complex. As companies try to differentiate the functionality tights prevent price from escaping (significantly) normality. • Premiums refer to the normality conditions (or average price). The limitation to increase price is influenced by the economic logic (price and cost must be related).

4. Excess competition:

- When luxury goods create value differently from regular products.

- Its about going beyond what’s normal or expected.

- Excess isn't about improving normality but breaking its boundaries.

- **To understand excess competition, we need to understand that:**

- Going beyond normality by breaking rules of regular competition: One way to break the rules is by **shifting away from functionality as the main reason** for buying something. Luxury often challenges the idea that things need to be practical to be valuable. Instead, it **focuses on emotional or expressive benefits**.

- Still creating value.

- Breaking functionality alone isn't enough to create value. For example, putting diamonds on toothpaste wouldn't make it valuable. Similarly, breaking social norms by making something expensive doesn't guarantee value either.

- True excess competition achieves extraordinariness. It goes beyond the ordinary by emphasizing emotional or expressive benefits. Luxury items like cars, watches, or bags are valued for reasons beyond their practical use.

- Understanding extraordinariness is complex because it's not about solving a specific problem or following logic. It's about tapping into emotions and personal enjoyment.

- This distinction between normal and excess competition helps us understand why luxury is different and how it creates value. It's a crucial foundation for any luxury strategy, helping us navigate the complexities of luxury consumption.

5. The essence of luxury: Excess as extraordinariness to ensure luxury competitiveness.

- Luxury value creation means aiming for something extraordinary.

- About going beyond normal competition but in a valuable way, not just for the sake of it.

- Achieving extraordinariness is complex: Some luxury companies might lose it over time, others may pretend to be extraordinary without delivering, and some might not even try.

- To build a successful luxury strategy, it's essential to have a valuable form of extraordinariness.

- The firm's essence: This forms the basis of a luxury firm's competitive advantage. It's the unique source of extraordinariness that helps the firm compete effectively.

- Identifying the essence of a luxury firm is challenging. It's not just about claiming superiority or rarity. Luxury value comes from emotional and expressive benefits, which are hard to quantify and communicate.

- To analyse a firm's essence, we look at two main things:
  - how extraordinariness is understood.
  - how it's achieved.

6. Conceiving extraordinariness: Luxury as a choice.

a. Extraordinariness is not an improvement and is hardly measured:

- In excess competition, the focus isn't on making things better or improving functionality. Extraordinariness is about satisfying needs differently, not necessarily making them more efficient.

- Unlike in normal competition, where improvement can justify a higher price, in excess competition, it's about offering unique emotional and expressive benefits.

- Measuring extraordinariness is challenging because emotions are harder to quantify than objective features. For example, consider mechanical watches.

- They're less accurate and more expensive to make than quartz watches. But people buy them for the emotional and expressive benefits they offer, like appreciation of craftsmanship or conveying a certain lifestyle or status.

b. Extraordinariness is not ¨only¨ about quality:

- Simply improving quality isn't enough to achieve extraordinariness.

- o While quality is often associated with luxury, it's not the sole determinant.

- o In luxury, emotional and expressive benefits must be the main focus, with quality being just one component.

For instance, the iPhone is a high-quality product, but its luxury status is debatable because its appeal is largely driven by functional benefits rather than emotional or expressive ones.

Key characteristics to describe luxury:

- Quality
- Price
- Trust in brand
- Excellence
- Beauty
- Creativity
- Better service
- Buying experience
- Global prestige.

c. Extraordinariness is hard to assess, and it required a learning curve:

- o Appreciating luxury often involves a personal journey, starting from valuing its status to later enjoying it for personal pleasure or emotional fulfilment.
- o While technical knowledge isn't necessary, learning about the values and beliefs behind luxury can enhance appreciation.
- o This appreciation is sensory and detailed, focusing on experience rather than explanation.

Examples of Extraordinariness:

- Pagani: Horacio Pagani, a passionate engineer, moved from Argentina to Modena to pursue his dream of creating extraordinary sports cars. He revolutionized the industry with innovative designs and composite materials, delivering the ultimate driving experience.

- Krug Champagne: Founded by Joseph Krug in 1842, Krug Champagne is known for its pursuit of excellence every year. Krug believed that great champagne wasn't just about a single exceptional year but rather the result of blending different base wines. He mastered the art of blending to create consistently excellent champagne.

- Maximilian Busser established MB&F in 2005 with his personal savings. His approach to watchmaking, known as "Kinetic Art," combined mechanical expertise with artistic vision. By redefining watchmaking as an art form, MB&F pushed the boundaries of what extraordinary mechanical watches could be.

- Loewe's use of high-quality leather and dedication to expressing their artistic vision through their products exemplify their extraordinariness.

- Understanding a brand's essence is crucial for recognizing its extraordinariness, and learning plays a vital role in appreciating the unique path each brand takes towards achieving it.

d. Extraordinariness requires leadership: The Creator Effect:

- Reaching extraordinariness in luxury is not a straightforward process.
- Achieving extraordinariness requires leadership to navigate these possibilities.
- Different luxury companies can claim extraordinariness in the same category without being direct rivals because luxury isn't a zero-sum game.
- The values and beliefs of the founder often shape a luxury firm's path to extraordinariness.
- This leading figure, whether called a creator or designer, guides the journey to extraordinariness.
- Art plays a crucial role in this process, as it's about expression rather than following a set path. Luxury begins with someone's belief in breaking norms and envisioning something new. This requires an extraordinary personality to lead.

e. Extraordinariness is a choice not a goal:

- Extraordinariness should be seen as a choice rather than a goal.
- Goals are measurable and clear, but achieving extraordinariness requires more than following a set plan.
- It involves subjective decisions, leadership, and expression.
- Choosing to pursue extraordinariness means breaking away from normality and finding meaning and appreciation in the process.
- As shown in Capsule 3.2, the journey to extraordinariness is better understood as a deliberate choice.

f. Learning extraordinariness by examples not by imitation:

- To understand extraordinariness, we shouldn't just copy others.
- By looking at different luxury firms and their approaches, we can see how they make choices and what values they prioritize.
- The examples in Capsule 3.2 and throughout the book show us real-life instances of how luxury firms have pursued extraordinariness in their own unique ways.

g. Achieving extraordinariness: the role of resources and capabilities:

- It's important for luxury firms to make sure their extraordinariness is **<u>tangible and credible</u>**, not just a vague idea or claim.
- To achieve this, they need strong organizational capabilities. These capabilities are determined by the firm's resources, including tangible, intangible, and human resources. By analysing these resources and capabilities, firms can assess their potential for creating value.
- Organizational capabilities are evaluated using a supply chain logic, focusing on efficiency. However, in the luxury industry, competition is **<u>based more on unique skills rather than simply being better than others</u>**.
- Therefore, luxury firms should identify capabilities that support emotional and expressive benefits, aligning with their values and creative approach.

Example:

A luxury car company like Pagani focuses on using composite materials to create extraordinary driving experiences, rather than just aiming to make a better car. Similarly, Joseph Krug's vision for his champagne brand goes beyond simply making a good product each year; it involves a quest for the best blends and winemaking skills to ensure excellence.

Essence: conception of self approach to extraordinariness		
Firm resources		
Tangible	Intangible	Human
• Financial. e.g. Cash • Physical. e.g. Manufacturing facilities, stores • Raw Material. e.g. Cashmere	• Technology. e.g. Patents • Reputation. e.g. Brand, relationships • Firm Culture	• Skilled Labor force.
⇩		
Organizational capabilities: Identification not based on sequential activities (Value Chain), but on activities linked to self conception of extraordinariness		
– What organizational capabilities support or enable the firm's beliefs? – What organizational capabilities support or enables the firm's creation?		
Extraordinariness through the Making	Extraordinariness through Delivery/Service	Extraordinariness through Talent.
How Tangible resources are applied to achieve extraordinariness.	How Intangible resources are applied to achieve extraordinariness.	How Human resources are applied to achieve extraordinariness.
Manufacturing expertise (Watchmaking, winemaking). Financial management. Access or master key components (raw material, manufacturing techniques)	Culture of excellence Service, after-sale expertise Relationship with clients Communication skills	Values and Beliefs about extraordinariness. Leadership Individual talent relevant to source of extraordinariness

VRIO analysis is a strategic framework used to assess a firm's internal resources and capabilities to determine its competitive advantage. The acronym VRIO stands for:

Value: Is the resource or capability valuable? In other words, does it enable the firm to exploit opportunities or mitigate threats?

Rarity: Is the resource or capability rare or unique among competitors? If competitors also possess it, it may not provide a sustained competitive advantage.

Imitability: Is the resource or capability difficult to imitate or replicate? If competitors can easily replicate it, it may not lead to a competitive advantage.

Organization: Is the firm organized to exploit the resource or capability effectively? This refers to whether the firm has the structure, processes, and culture to leverage the resource or capability for competitive advantage.

By analyzing its resources and capabilities through the VRIO framework, a firm can identify which ones contribute to its competitive advantage and focus its strategic efforts on leveraging those advantages effectively.

h. Achieving extraordinariness takes time, a lot of time:

Why achieving extraordinariness takes a lot of time?

- First, it's because extraordinariness is tied to emotional and expressive benefits, which are hard to explain.
- Second, it's because extraordinariness is something that's appreciated rather than easily explained. This means that both consumers and managers might take time to understand why a company is extraordinary. Communicating the source of extraordinariness requires patience, especially in today's fast-paced digital world.

In the examples of Horacio Pagani, Maximilian Büsser, and Joseph Krug, we see that luxury firms are often closely linked to their founders, who have a vision to break normality and the talent to make it happen.

- Scarcity is also important in achieving extraordinariness. If something extraordinary is easy to achieve, it's not really extraordinary because many firms can do it. Luxury is often associated with scarcity, whether it's in raw materials, expertise, or know-how. But not all scarce elements make a company luxurious; they must also pass the VRIO framework test.

- A luxury brand isn't a goal itself but a consequence of achieving extraordinariness. A brand reflects that a company has successfully achieved extraordinariness through its organizational capabilities.

- It's important to distinguish between being truly extraordinary and just appearing extraordinary.

- Without essence, a luxury company can't compete meaningfully.

- **In conclusion, not every company can be extraordinary. Many use the term "luxury" lightly to set themselves apart, but true luxury requires creative ways**

to break normality and solid organizational capabilities to realistically achieve extraordinariness.

How to conceive extraordinariness?	How to achieve extraordinariness?
• Understanding better the sources of extraordinariness: - Is not an improvement and is hardly measured. - Is not only about quality. - Is hard to assess and it requires a learning curve. - Requires leadership: the creator effect. - Is a choice not a goal. - Can be learned by examples, not by imitation.	• Requires extraordinary organizational capabilities. • Takes time. • Is based on capabilities. Looking extraordinary is not based on realities.

THE LIMITS OF LUXURY:

a. The role of consistency: the fine line between normality and excess:

The line between normality and excess is hard to see for two reasons:

1. Emotions and expressions matter more than measurable qualities in luxury, making it tricky to judge extraordinariness.

2. The term "luxury" is used too often in marketing, making it hard to tell what's truly luxurious. People want to seem luxurious, so they use words like "premium" or "new luxury" to make themselves look better. But luxury isn't just about products or companies; it's a social thing that changes with society.

To understand the difference between normal and excess competition, luxury managers need to focus on being exceptional, not just trying to keep up with others. They might be tempted to follow what normal competitors do, but they should stay focused on being extraordinary. Price isn't what makes something luxurious; it's about delivering value in a special way, not just charging a high price.
To know where the limits of luxury are, we need to be consistent. This means staying true to what luxury really is, not just copying what others do. And it means making sure everything about a company or product fits together well, so that people feel the luxury in every aspect.

Capsule 3.3: Is Coach a luxury firm?

Coach started as a small leather goods workshop in New York City in 1941. Miles and Lillian Cahn bought the company in 1961 and made it famous by creating durable and high-quality leather products. They also introduced fashionable handbags for women. Coach became more successful under new leadership in the 1980s, but it started to lose its luxury reputation due to changes in manufacturing and sales strategies. Although Coach claims to be a luxury brand, it has struggled to maintain consistency with luxury standards, often resorting to discounting and sacrificing quality control. Despite its origins, Coach's current image doesn't fully reflect its journey to becoming a respected brand.

b. Managing the “entry-level” category

It is challenging because it's easy to blur the line between normal and excessive. If done poorly, it can harm the brand's perception of extraordinariness.
Luxury brands must focus on excess competition rather than mass appeal to maintain consistency.
The entry-level products should still reflect the brand's extraordinariness, even if they are more affordable versions.

- Examples like the Jaguar X-type and Aston Martin Cygnet show how brands can dilute their image by compromising on extraordinariness for growth. Luxury brands need to protect their extraordinariness, even in entry-level offerings, to avoid brand dilution. Pricing plays a crucial role in communicating the level of extraordinariness. There's no fixed rule for defining entry-level products; it's about maintaining consistency with the brand's essence and commitment to extraordinariness.

Case study for Porsch Macan:

At the end of 2013, Porsche, the luxury carmaker, introduced two new models: the Porsche 918, a high-performance sports car, and the Macan, positioned as an entry-level offering. This marked a significant expansion of Porsche's product line, which had traditionally focused on the iconic 911. With the addition of models like the Cayenne, Panamera, and now the Macan, Porsche aimed to attract a wider range of customers. The Macan, priced lower than other Porsche models, was designed to appeal to new customers while maintaining the brand's exclusivity. However, expanding the product line also brought new challenges, such as manufacturing complexity and the risk of diluting the brand's luxury image. Porsche had to carefully navigate these challenges while capitalizing on its past successes and maintaining its reputation as a manufacturer of luxury cars.

Questions:

1. **A value offering can be better understood as a combination of different types of benefits. Can you identify a value offering (product or service) where functional benefits are predominant, And another one where emotional or expressive benefits are predominant?**

-Value Offering with Predominant Functional Benefits: A practical example of a value offering with predominant functional benefits could be a basic household appliance like a toaster. Its primary function is to toast bread efficiently and reliably, providing convenience to the user without much emphasis on emotional or expressive benefits.

-Value Offering with Predominant Emotional or Expressive Benefits: An example of a value offering with predominant emotional or expressive benefits could be a luxury spa experience. While the functional aspect might include services like massages or facials, the main appeal lies in the emotional benefits such as relaxation, pampering, and indulgence.

2. **What is the managerial limitation that the functionality trap is aimed to highlight?**

-Managerial Limitation Highlighted by the Functionality Trap: The functionality trap aims to highlight the limitation of solely focusing on functional benefits in product or service development. This approach overlooks the importance of emotional or expressive benefits, which are often more influential in consumers' purchasing decisions, especially in luxury markets.

3. **Luxury cannot be described as normal competition; what best describes normal competition? Can you identify an industry where normal competition clearly explains how companies compete?**

-Description of Normal Competition: Normal competition can be described as a competitive environment where companies primarily focus on operational efficiency, cost-effectiveness, and meeting the basic functional needs of customers. An industry where normal competition is evident is the fast-food industry, where companies compete based on price, convenience, and standardized products.

4. **Based on what you have read in the chapter, what difficulties do companies face when in the conception of extraordinariness?**

-Companies face several difficulties in the conception of extraordinariness, including the challenge of defining and maintaining a unique brand identity, understanding and meeting the complex emotional or expressive needs of luxury consumers, and managing the balance between exclusivity and accessibility in their offerings.

5. **Why consistency can be a sound approach to ascertain the fine line between normality and extraordinariness?**

-The Role of Consistency in Ascertaining the Fine Line: Consistency can be a sound approach to ascertain the fine line between normality and extraordinariness because it ensures that a luxury firm's actions, messaging, and overall brand experience align with its core values and vision of extraordinariness. Consistency helps maintain the authenticity and integrity of the brand, preventing dilution and confusion among consumers.

6. **Why entry-level offering can be a threat to a luxury firm’s strategy?**

-Threat of Entry-Level Offering to Luxury Strategy: Entry-level offerings can be a threat to a luxury firm's strategy because they risk diluting the brand's exclusivity and perceived value. By introducing products or services at lower price points, luxury firms may attract a broader customer base but risk alienating their existing high-end clientele and undermining their brand image of exclusivity and luxury.

7. **Can you find a current example of a luxury firm with a successful entry level offering? And an example of a firm that fails to offer a meaningful entry-level offering?**

- *Successful Entry-Level Offering*: Rolex offers entry-level watches like the Rolex Oyster Perpetual, which provides consumers with a more accessible entry point into the brand's luxury timepieces while still maintaining the quality, craftsmanship, and prestige associated with the Rolex brand.

- *Unsuccessful Entry-Level Offering*: In the luxury automotive industry, Jaguar's launch of the X-type sedan in the early 2000s was considered unsuccessful. The X-type aimed to attract new, younger buyers to the brand with a lower price point, but it lacked the distinctiveness and luxury features expected from a Jaguar vehicle, leading to a dilution of the brand's image and a failure to resonate with luxury consumers.