

Kurt Salmon 

Redefining Fashion Business Models

Today's Challenges, Tomorrow's Competitive Edge



It is no news that being a fashion retailer or fashion brand these days is not a bed of roses. In fact, it may sometimes appear to be a constant and exhausting struggle. The marketplace is characterised by ever growing complexity and dynamic change. New markets are on the rise, fashion trends come and go at enormous pace, the consumer is savvier than ever and continues to browse and shop multiple channels at a time. Consumers have a virtually unlimited choice of products coming from many different retailers available anytime and anywhere. To top it all off, the economy remains volatile and competition is fierce. The days when traditional business models held a sufficient competitive advantage and successfully drove year-on-year growth are long gone (see Fig. 1).

But what is next? What has to be done to embrace complexity and turn current market dynamics into a sustainable competitive edge? What does the next generation business model look like that can drive integration of channels, leverage specific market potentials on a global level, provide rapid scalability and flexibility, and ensure customer centricity without sacrificing efficiency?

Latest Kurt Salmon research reveals that the majority of fashion brands and retailers have not yet found a satisfying answer. This also holds true for several major players that had set the best practice standards for the fashion industry for a long time

and are now lacking key capabilities in terms of business structures, processes and technology given current market developments.

Trends Re-Shaping the Fashion Industry

The fact that fashion brands and retailers are struggling to find the right business model answers might be startling, given that there has been little controversy regarding the key trends that are shaping and will continue to shape the industry. However, considering the scale of change it does not surprise that only very few industry players have yet managed to realign the way their business operates in a comprehensive and integrated manner. The key drivers of the paradigm change can be summarised as follows:

1. The Rise of Multichannel

The future of fashion retail will be driven by the growth dynamic of multichannel, which will soon outperform both pure online and pure store sales. Traditional wholesale businesses are developing their own retail channel, brick-and-mortar retailers strive to expand their online business, and vice versa. The potential reward is promising: multichannel customers are known to generate significantly higher sales volumes - retailers report up to 100% sales increase compared to single channel retailers. To tap this potential, however, retailers and brands

Fig. 1: Business Model Evolution Drives Growth

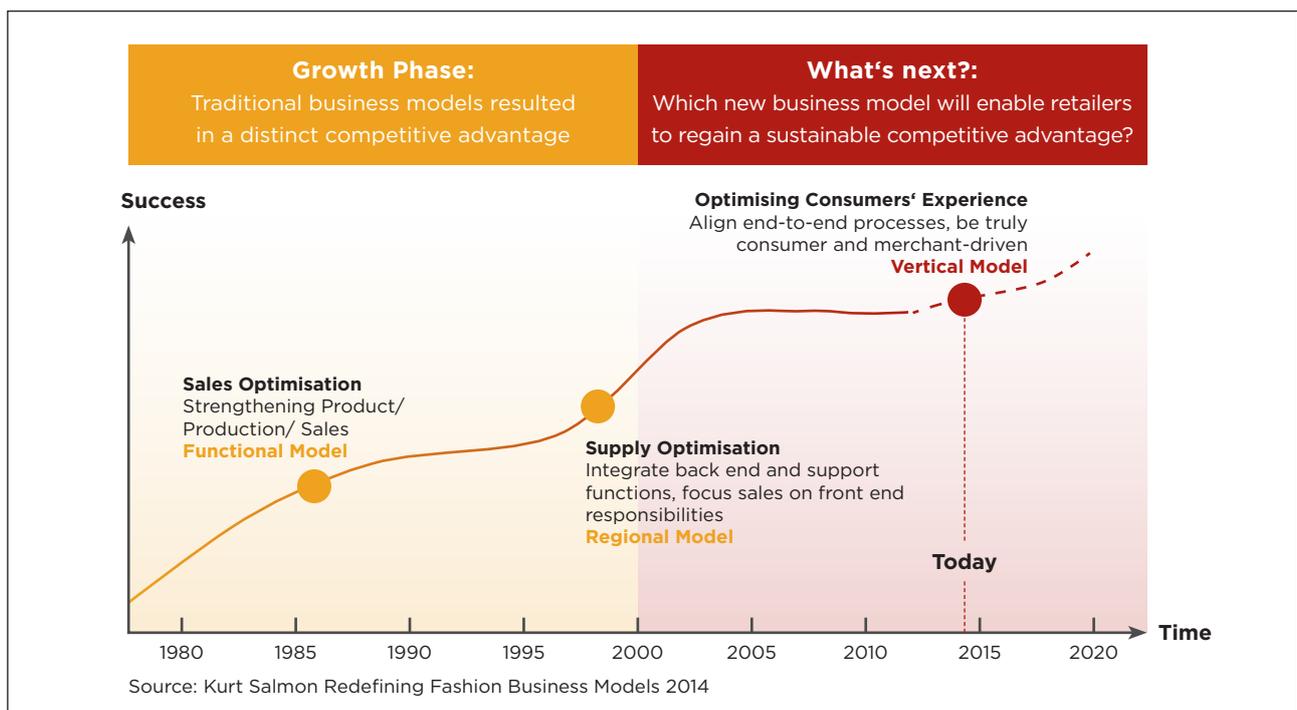
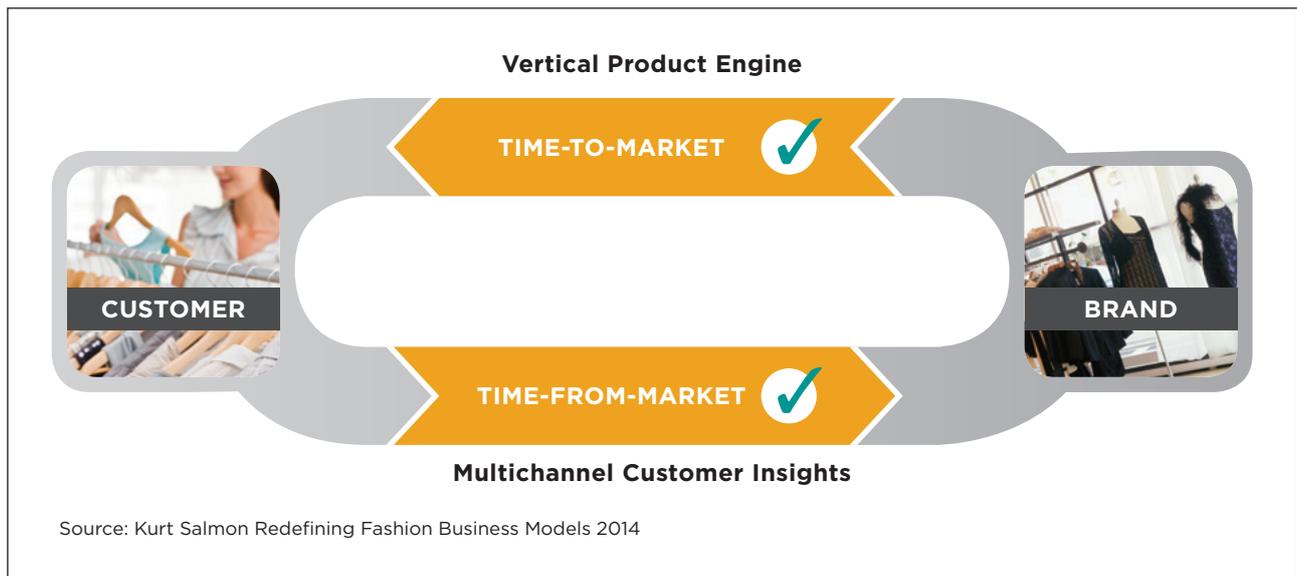


Fig. 2: Time-from-Market & Time-to-Market as Key Competitive Advantages



alike need to offer a compelling proposition across channels and individualise customer interactions. This requires appropriate structures to enable an integration of merchandise and assortment planning processes, pricing optimisation across channels as well as coordination of communication measures and service offers, to name a few. A vast majority of players in the fashion industry are still far from finding sustainable solutions for these challenges.

2. Geographical Differentiation and Localisation

Aiming at future growth, brands and retailers are targeting emerging markets which are experiencing significantly faster growth rates compared to mature and saturated markets. Some of these markets are quickly evolving into new fashion hubs. With annual growth rates of 5% to 10%, Brazil, India and China are growing up to 10 times as fast as Europe and the US, thus offering immense opportunities for fashion products. However, successfully entering and penetrating the new markets requires understanding the specific culture and local consumer behaviour: while globalisation of fashion trends allows global ranges, consumers in emerging markets show region-specific preferences and requirements that need to be addressed, e.g. through regional assortment add-ons. Defining merchandising processes and organisation structures, which ensure commonality while exploring local market needs and potentials, is a key challenge. Future standard processes and structures must be appropriate to operate in both saturated as well as fast growing markets.

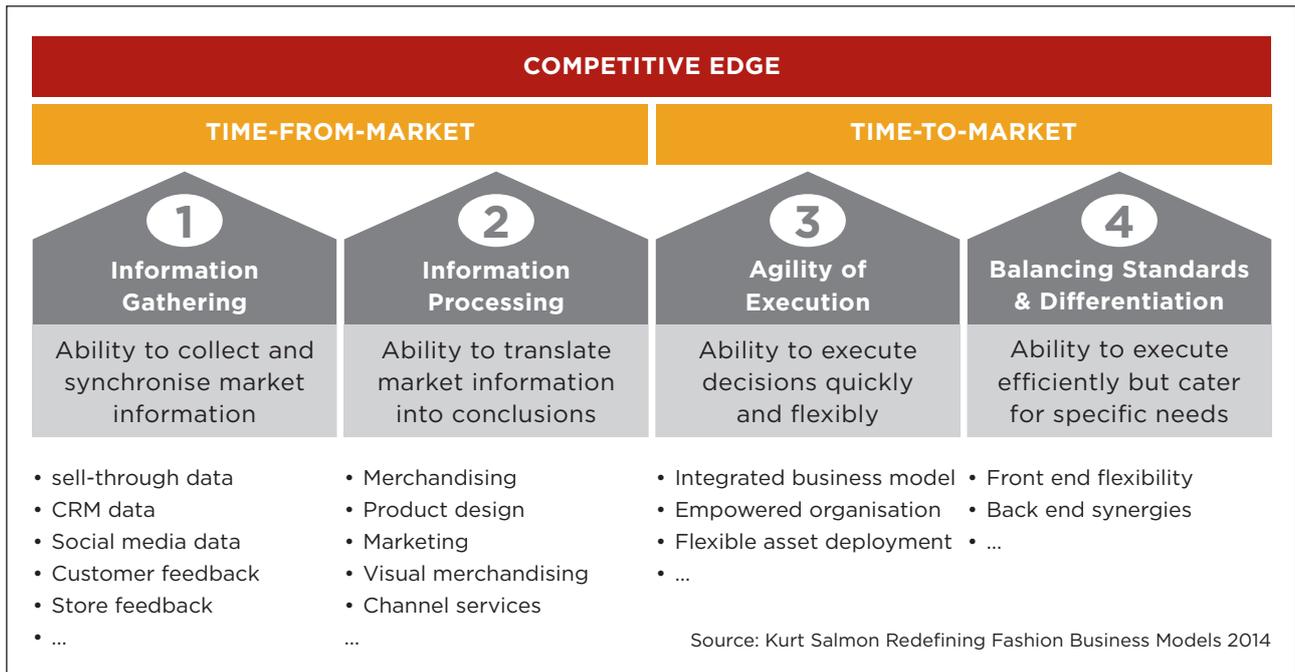
3. Need for Customer Centricity and Individualisation

At the same time, even within developed markets, the requirement for differentiation is increasing in line with progressing fragmentation of lifestyles and consumer preferences. Mass customisation models as Converse's customised shoes or M&M's individualised candies are prime examples for retailers and brands trying to cater to diverse customer requirements. The pre-condition for serving consumer preferences in an increasingly dynamic market is for retailers to have customer-centric data, processes, and structures in place that allow a continuous monitoring of relevant market segments and integration of almost real-time consumer information into decision-making. Classical organisational models, which are aligned based on product and/ or supplier market characteristics, insufficiently support the required target customer focus in markets with abundant choice of products for any type of customer lifestyle and need.

4. Speed of Innovation and Information

Advanced information gathering and processing capabilities are also critical for keeping up with fashion trends which will continue to come and go at increasing pace - think of UGG boots and Crocs, charm bracelets, candy-coloured chinos, aviator sunglasses or Kate's engagement dress. The smaller and bigger hypes are intensified by a growing speed of information, fuelled, for instance, by social media such as Facebook, Twitter, YouTube or location based services such as Foursquare. As retailers strive to develop appropriate mechanisms to capitalise on latest market developments, they

Fig. 3: Four Capabilities Drive Time-from-Market and Time-to-Market



also need to continue optimising their calendars, reduce time-to-market and establish fast track programmes that enable them to react on and exploit rising trends.

5. Transforming Sourcing Environment

Increasing speed on the demand side requires differentiated supply models which provide sufficient flexibility to leverage latest market impulses. However, the traditional supply side set-up is not only challenged by increased demand side requirements, but also by a transforming sourcing environment. Most prominently, rising labour and production costs in traditional regions like coastal China trigger shifts to less developed markets like Bangladesh, Cambodia or Myanmar. Increasing global proliferation of products requires supply chain and sourcing structures which allow serving Europe and the US, but also South America, Asia, the Middle East and Russia, considering needs in terms of lead times, quality, and cost. To top it all off, the sourcing environment remains extremely unstable with regards to raw material cost, freight rates, and political environments, as well as social and environmental risks. Both demand and supply side volatility emphasise the need to manage supply chains in an integrated way from demand plans down to capacities, materials, and production.

Success Factors that Separate the Wheat from the Chaff

In the light of the dynamic developments and new challenges that retailers are faced with, it is not only speed-to-market that poses a distinct competitive advantage; it is a combination of both speed-to-market and speed-from-market that makes some players more successful than others. The ability to bring product into the store quickly is worth nothing, if the quality and timeliness of information do not support the right decisions. Being able to integrate a large amount of data from multiple sources, channels, and geographies and draw the right conclusions within a short period of time is the key to reaping the rewards of a continuous reduction of time-to-market (see Fig. 2, page 3).

Although the described trends are obvious and industry best practice examples are available, it is not surprising that most retailers find it difficult to adopt these practices as each brand has its own DNA, which does not allow simple duplication of processes and organisational structures. Retailers still need to carefully review how they can learn from best practices to align their processes, organisational structures, and systems with the levers that are critical for the brand's success in the changing market environment.

What the concepts of time-from-market and time-to-market boil down to, is the combination of

four basic capabilities that provide retailers and fashion brands with a competitive edge these days: information gathering, data interpretation, agility of execution, and balancing standards and differentiation (see Fig. 3).

Information gathering refers to the capability of tapping and synthesising various information sources such as sell-through data, social media data, CRM data, and feedback from multiple channels on a continuous basis and in almost real-time to enable sound understanding of diverse markets and consumer segments at critical decision points. For instance, rather than conducting store feedback sessions as part of an isolated hind sighting exercise, speed-from-market champion Zara has set up structures to collect qualitative store feedback at any point in time.

The global proliferation of access to data and the direct relationship of retailers with the consumer make it relatively easy to gather information. The crux is usually the capability of **interpreting data**: screening a vast amount of available data from various sources, channels and geographies, filtering relevant information and finally translating knowledge (i.e. quantitative and qualitative data points) into decisions and concrete measures across market-facing functions is key to optimising assortments, products, pricing, and customer interactions. In this context current discussion around **“Big Data”** and related systems gain increasing business relevance.

On the flip side, knowing what to do, but not being able to do it in time and on budget, is useless. Operating on a short go-to-market calendar and being able to execute decisions quickly requires the capability of **agility of execution**. The basic prerequisite for agility is to balance central decision making across functions and business units with empowerment of the organisation. Agility of execution also requires flexibility in terms of asset deployment, e.g. through pooling of resources such as product development and design teams and allocating to purposes based on current priorities. Agility also includes sales and operations capabilities e.g. by opening and closing pop-up stores within short timeframes to connect to customers on a situational basis and leverage according potentials.

Executing quickly and efficiently also depends on retailers’ ability to establish standards and leverage synergies where possible, without compromising differentiation of market-facing activities, i.e. the capability of **balancing standards and differentiation**. While front end functions need to be flexible and close to markets, back end operations (i.e. supply chain, sourcing, logistics, and administrative functions) can be centralised and operating on defined standard procedures to optimise efficiency and effectiveness. On a side note, balancing standards and differentiation must also be applied at micro level. For instance, being locally oriented and providing required levels of range differentiation also means leveraging

Fig. 4: Fashion Retailers and Brands by Capability Status

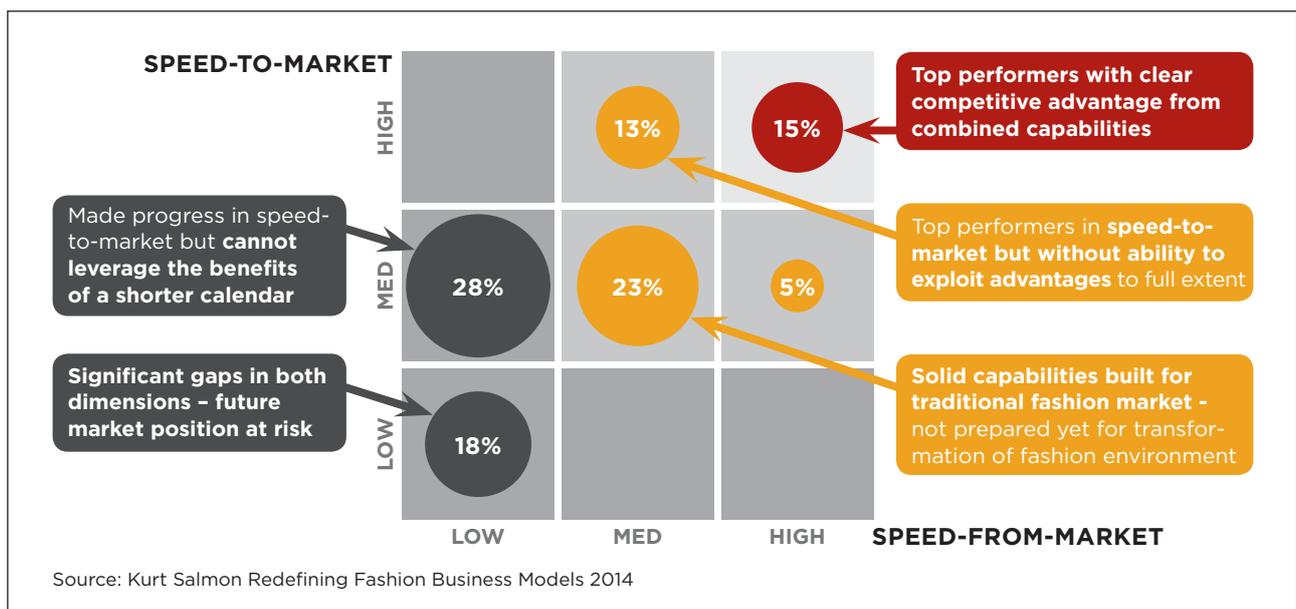
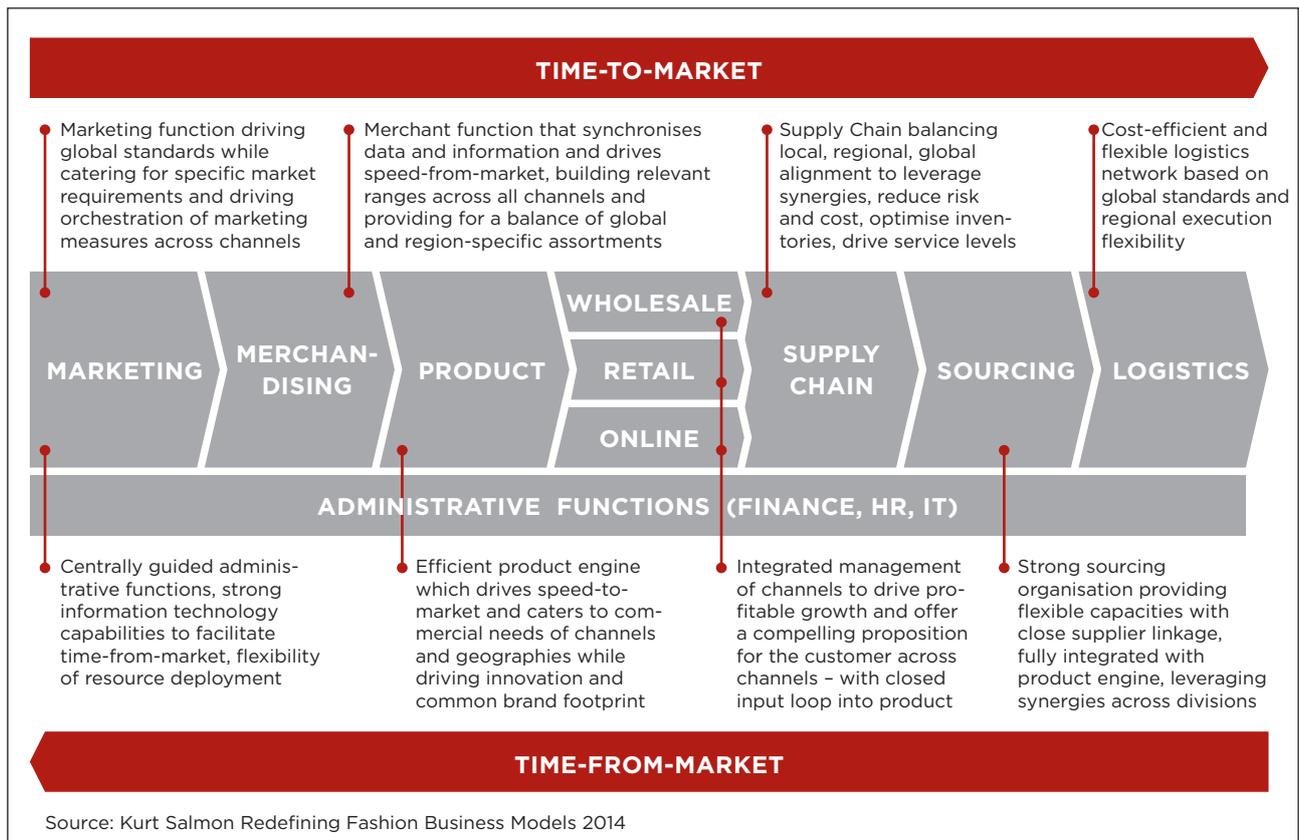


Fig. 5: Business Model as Enabler – End-to-End Integration and Control



common assortments where possible to keep supply chains lean and efficient, thus reducing risk and cost significantly.

To date, only few players in the industry have fully developed all four core capabilities required to drive both speed-from-market and speed-to-market. Kurt Salmon recently conducted a study based on a sample of more than 40 European retailers and fashion brands. According to our research, only 15% of companies already inherit the full set of critical capabilities to drive time-to-market and time-from-market. While many fashion businesses have focused on agility of execution and successfully squeezed time from concept to in-store (leading retailers take between 30 and 40 weeks), many of these do not have the right structures yet for information gathering and processing in place to also drive time-from-market and turn short calendars into real competitive advantage (see Fig. 4, page 5).

The current situation marks a tipping point for many companies in the fashion industry – with a significant share of retailers and brands in need of significant realignment of their business models as a prerequisite to sustain growth. Depending on existing capabilities, the extent of change for the

individual functions across the value chain may differ. For example, focus can be on the front end to build a merchandising function with the right processes and tools in place to synchronise data and information to create relevant ranges across geographies as well as wholesale, retail, and online channels. In other instances, the largest potential lies in centralising supply chain functions to optimise inventories, reduce risk and drive service levels for flexible execution (see Fig. 5).

Based on the capability framework, Kurt Salmon offers retailers and fashion brands a Quick Scan, which evaluates the relative strength of their businesses on all four capabilities compared to competitors. Key improvement opportunities with regards to the respective business model (processes, organisation, systems) are highlighted. Pulling the right levers optimising the business model will result in significant performance enhancements across the entire value chain and lastly driving top line sales, margin, and EBIT improvements. Doing it now and getting on top of the trends that are challenging traditional business models is key for securing the current market position and developing a lasting competitive advantage ready for the future fashion industry environment.

Proven Success

While more than 80% of fashion brands and retailers do not inherit the full set of critical capabilities to leverage time-to-market and time-from-market, some industry players actually have already set the foundation to also succeed in the future fashion market environment. Kurt Salmon has supported several of them in this journey.

Kurt Salmon Success Story

A leading apparel and footwear brand experienced sluggish sales performance, as well as massive increases in markdowns and inventories due to long calendar lead times and insufficient capabilities to leverage market insight. This led to issues with regards to meeting market requirements as business decisions were forced prior to having sufficient and targeted market information available. Kurt Salmon supported the client with setting up a comprehensive programme to transform the business model across key functional areas of the value chain, including Merchandising, Product, Supply Chain, Wholesale, and Retail. The programme encompassed:

- Evolving the merchant function and designing and implementing a consumer-driven merchandise and assortment planning process that allowed building a focused range across channels and geographies
- Evolving the product engine and driving speed-to-market based on an enhanced calendar and additional fast track development process to capitalise on latest market information
- Centralising supply chain operations and optimising forecasting and inventory management processes to improve demand reactivity

The project resulted in shorter production lead times, improved EBIT margin by 4% points in Retail and 2% points in Wholesale while reducing overall inventories by 16%.

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