

MIGRATING TOWARDS A CROSS CHANNEL HIGH SPEED END-TO-END VALUE CHAIN

A supply chain study for leading Fashion and Lifestyle Companies

Commissioned by DHL Supply Chain and developed by Buck Consultants International

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Buck
Consultants
International



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EXECUTIVE SUMMARY

The European fashion and lifestyle sector operates in a highly competitive and fast changing marketplace. Ease of doing business and greater product choice play a key role in consumer buying decisions. Consumers demand high customer satisfaction across sales channels at lower prices. Retail changes from physical stores to e-commerce, to cross-channel retail, and from wholesale to greater brand management requires executives to adapt their business models and cost structures to take advantage of changing consumer buying behavior.

Key to this report is the notion that a company's value proposition must drive its supply chain strategy and not vice versa. The supply chain is a

strategic asset which should be seen as an enabler of top level growth and drive bottom line results. Speed to market, inventory costs and the cash to cash order cycle play a key role in a company's cost model. This industry report seeks to elaborate on key industry developments and combine these with best practice ideas and solutions from within and outside the industry, to address the key challenges that executives within the European fashion and lifestyle sector face today.

This study identifies and discusses eight key developments from a supply chain management perspective from within the European fashion and lifestyle sector.



First, overall growth in retailing will come more and more from online retailing and less from physical stores alone. Cross-channel retailing, a hybrid between online and physical stores, will require greater and more cost effective supply chain management.

Second, strong growth opportunities in new geographic markets will require a different supply chain strategy to that of more developed markets.

Third, greater visibility within the supply chain will enable companies to make more informed business decisions related to routing, pick/pack and postponement decisions related to key customers and markets.

Fourth, the ability to take new products to market faster than your competition requires speed and flexibility. Key is having an agile supply chain to support the business model to take advantage of opportunities and respond quickly.

Fifth, in reducing time to market it is equally important to look at the total time to market cycle, which includes the design and manufacturing phase. Near-sourcing closer to key markets is increasingly being explored as traditional production sources in the Far East become more expensive. Using a greater combination of transportation modes is another option to explore with regards to improving speed to market.



Sixth, moving the pick and pack process upstream to the point of origin allows orders to be picked/packed and shipped directly from source to key markets and/or customers, bypassing a European distribution warehouse.

Seventh, the hanging garment business in Europe seems to be on the decline from a logistics service offer perspective. Why is this, does it make sense and what solutions are still there?

Finally, having an excellent organization open to innovation and change is key to migrating to a high speed end-to-end value chain. Horizontal and vertical collaboration in which the supply chain professional plays an integral role is vital in this journey of change in which the future supply chain plays a more strategic role.

Our industry survey amongst leading European fashion and retail houses, underscores a number of these developments which supply chain leaders believe will form the agenda for the coming years. In a recent industry master class, organized by DHL, it was observed that the industry will learn more and learn quicker through greater collaboration, identifying common challenges and better sharing of best practices to overcome these.

The items on the agenda are not necessarily new to people inside or outside of the industry. Still, many companies are putting in place the basics or fundamentals to better coordinate and streamline their supply chain on a global level. The industry needs to make step changes in order to deserve a seat at the board level and be considered as a serious contender.



PART 1

The Fashion and Lifestyle Industry – Key Trends with Supply Chain Implications

The fashion and lifestyle industry is going through rapid change due to changing customer buying behavior, increasing brand awareness and new geographical growth markets. These developments are changing the fashion and lifestyle retailing landscape, and in turn the supply chain and distribution management requirements.

Retail Channels

The key retail channels are made up of wholesale, retail and online e-commerce. There is already a paradigm shift away from wholesale towards retail and e-commerce. Changing customer buying behavior and increasing brand awareness will mean that more and more product brands will choose to develop their own retail channels through their own physical stores and online e-commerce concepts.

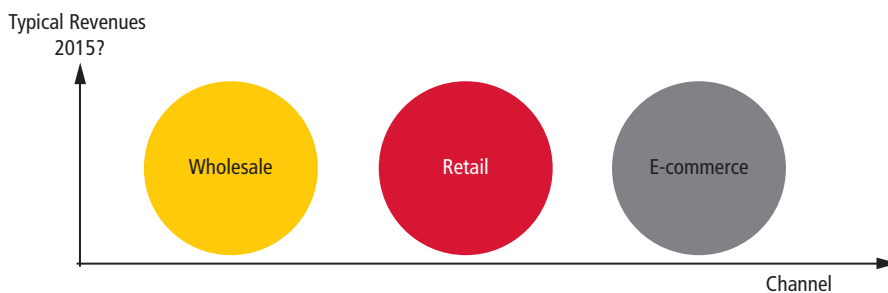
The online market has a large growth potential and yet many well-known brands still only have a relatively low market share in online retailing. This means that both business executives and the supply chain executives within fashion and lifestyle brands need to address robust solutions to embrace the online channel and grow the company's business in a profitable way. See figure 1 for the projected revenues for fashion and lifestyle companies (equally divided over the three channels). Today this split between the three channels is typically in Europe 55%, 35%, and 10% whereas in the US the split across these channels is already much more equally divided.

One Size Fits All – European Distribution Footprint

Most fashion and lifestyle companies still operate a simple “one size fits all” supply chain based on a single European distribution centre (EDC) to cover their Europe Middle East and Africa (EMEA) region. Only companies with very large volumes operate several regional distribution centers (RDC's). There appears to be limited supply chain diversification per product/market combination. Developments such as the emergence of e-commerce, more “demand pull” based supply chains based on lower inventory holdings, different channel requirements and order types, and new geographical growth markets such as Russia and Turkey will require companies' supply chains to be re-modeled to better align with changing business models.

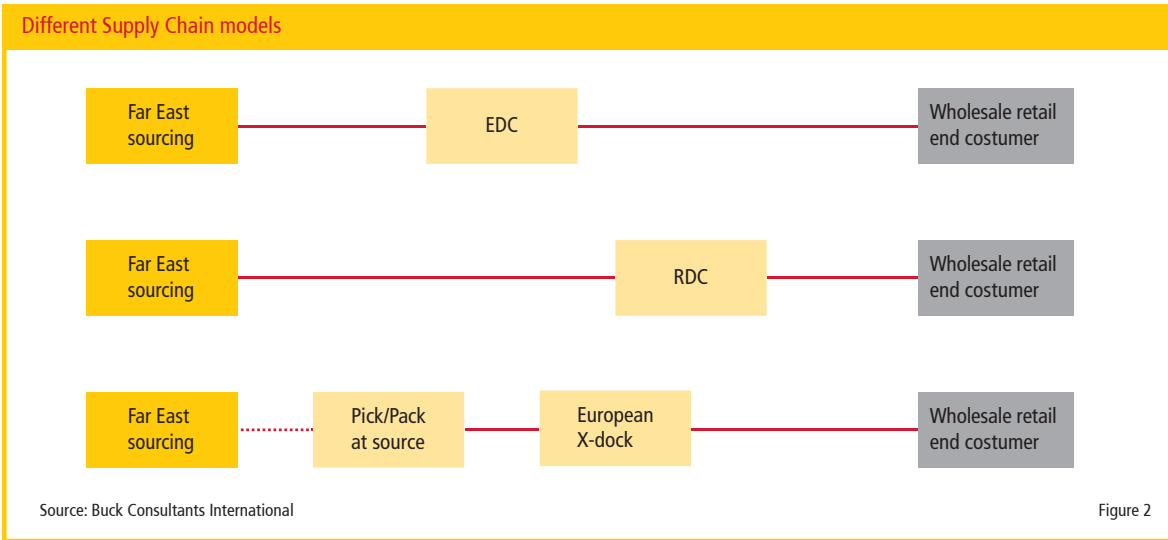
Multiple retail channels and product sources, reduced time to market, and growing geographical scope will force companies to address inventory holding points within the supply chain. Concepts such as order picking at source in a consolidation point and directly shipping to key markets or customers using single or multiple customs entry and cross-dock points within Europe will need to be investigated. Will higher costs of airfreight be offset by lower costs in inventory holding? What will be the impact on inventory costs and the cash to cash order cycle?

Traditional projected revenue sources for fashion and lifestyle companies



Source: Buck Consultants International

Figure 1

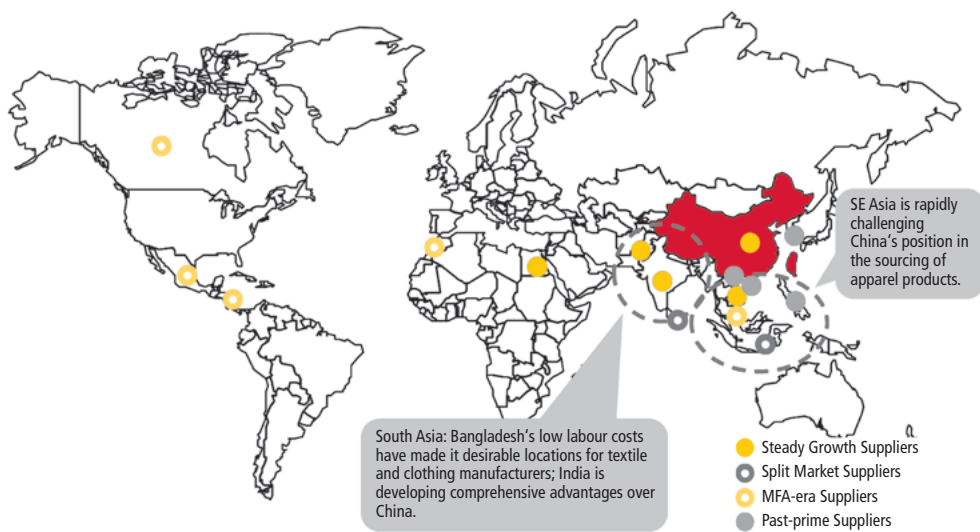


Product Sourcing

At present, Asia remains the biggest sourcing region for fashion and lifestyle goods. China is the main Asian production source. However, sourcing is on the move for a variety of reasons. Labor costs and other costs of doing business in China are rapidly increasing. For this reason sourcing is on the move to lower cost countries such as Vietnam, Indonesia, Cambodia, the Philippines, Bangladesh and India.

At the same time energy cost increases and time to market requirements mean that companies will also have to look closely at production locations. Near shoring is something a number of companies such as Inditex/Zara, Gap, and Adidas are already exploring for the entire part or parts of the assortment, or even by splitting the initial launch pre-order business from the in-seasons replenishment.

Major groups of apparel exporters



Source: Buck Consultants International

Figure 3

The Cost Paradigm - are we too cost focused?

The fashion and lifestyle sector is noted as one of the most dynamic and “glitzy” industries. It is a market noted for its sexy fashion models, trend setting fashion designers, outrageous advertisements and commercials, amazing shop decorations and product launches. Yet behind the glamour and the glitter hides an often “grey”, operational, sub-optimal, cost driven supply chain.

So the question is, how important are the costs of transportation and distribution in relation to the company’s product retail price and bottom line results? Is the supply chain utilized sufficiently to support time to market and the company’s growth plan? Is there indeed a strategic role within the company for the supply chain related to time to market, market share and growth?

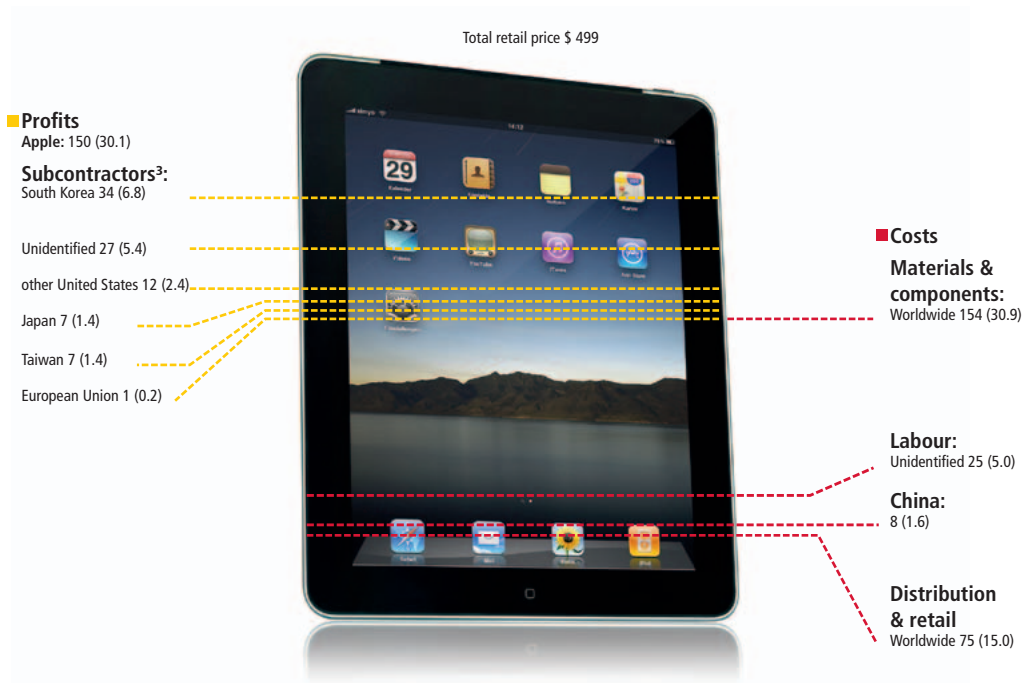
A company’s value proposition must drive its supply chain strategy and design. Horizontal collaboration

within the company and/or with supply chain partners is a sure way to optimize lead times, gain cost synergies and reduce waste.

An example from the high-tech sector illustrates an Apple iPad cost breakdown in which the labor costs in China are only 1.8% of the total retail price of the unit. Distribution and retail costs are 15%. Using airfreight to ship goods from the Far East is more expensive than using sea freight. Why do companies such as Apple fly most of their consumer orders from China to its markets in the US and Europe? It is all about the cash.

Independent of the type of industry or market, business fundamentals prove that it’s often all about the cash to cash order cycle which impacts cash flow and ultimately higher profits. Lower inventory levels, faster lead times to customers and a higher order cycle turnover lead to more sales, lower overall costs, and thus higher margins. Higher transportation costs or higher labor costs can be absorbed as long as

Slicing the Apple iPad



Source: Kenneth L. Kraemer, University of California, Irvine

- 1 1st generation, Wi-Fi only version
- 2 Numbers do not add to their respective totals because of rounding
- 3 Non-labour, components only. Assigned to corporate headquarters

Figure 4

overall costs of production are optimized and reduced. This is how Apple makes its profits and why it has managed to create cash reserves which would allow the company to operate without a single further sale for the next 19 years at its current cost level.

Industry Survey

Buck Consultants International (BCI) held an industry survey early in 2012 to gauge a number of supply chain developments within the fashion and lifestyle sector.

The objective of the survey was to capture the main trends and developments from supply chain executives working for a number of key fashion and lifestyle companies. The survey also set out to identify the main challenges for supply chain executives which form the agenda for the coming years to action.

The feedback received from industry executives has been used to table the Supply Chain Executive Agenda for 2012-2015 which is outlined in part 2 of this report.

The following companies participated in this industry survey.

Betty Barclay

LEDERUNDSCHUH[®]

URBAN OUTFITTERS

MICHAEL KORS



Foot Locker

IC COMPANYYS
HOME OF FASHION BRANDS

LC Waikiki

adidas[®]

VLISCO



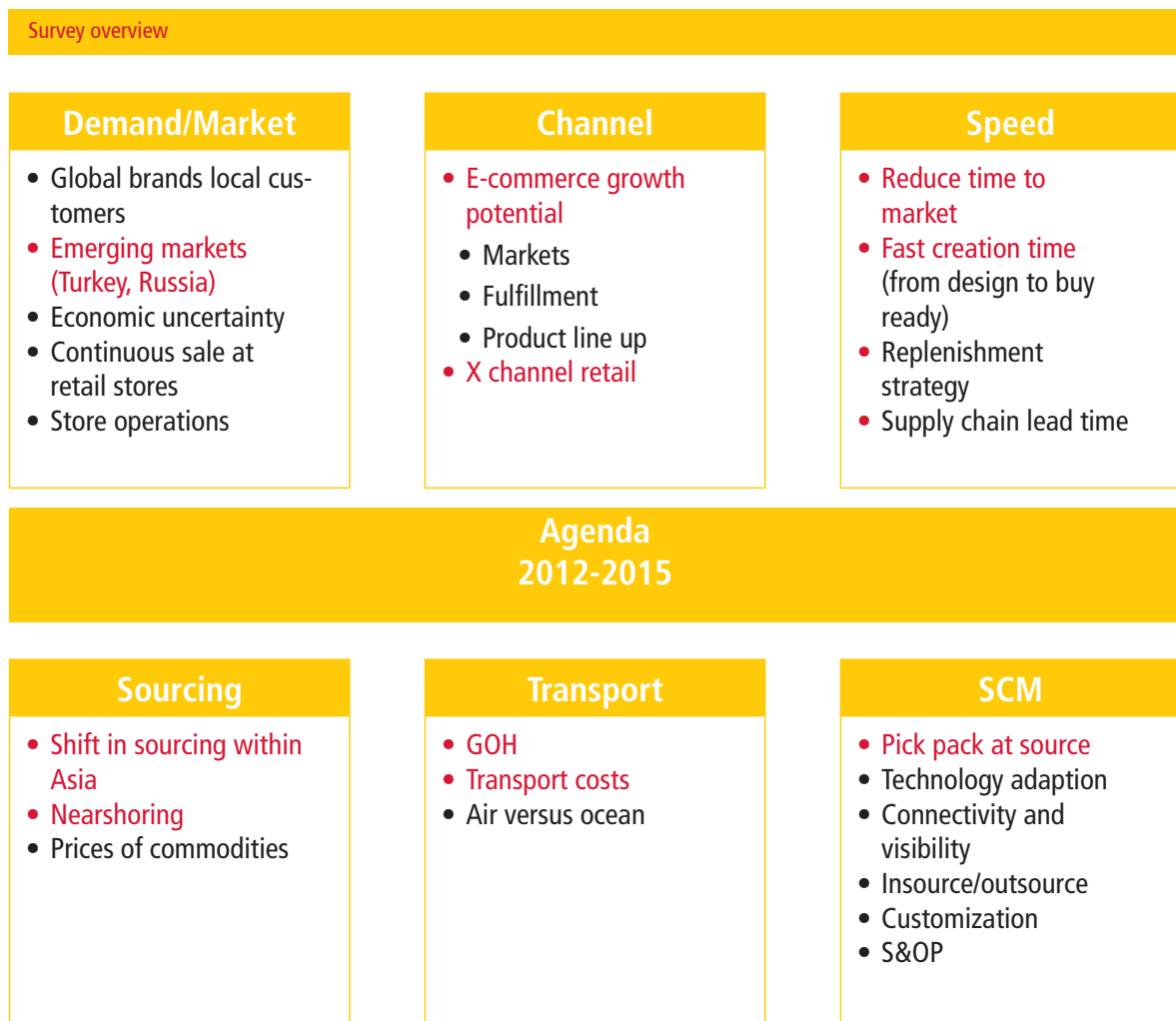
PART 2

The Supply Chain Executive Agenda 2012–2015

Buck Consultants International (BCI) organized an industry survey amongst a number of leading global fashion and lifestyle brands and retailers. The survey asked participants to identify their key supply chain “challenges” in the coming years in relation to market developments and their company’s business.

From this survey, BCI filtered the key challenges which were identified most frequently by the participating companies. These are summarized in the overview below. Those highlighted in red were

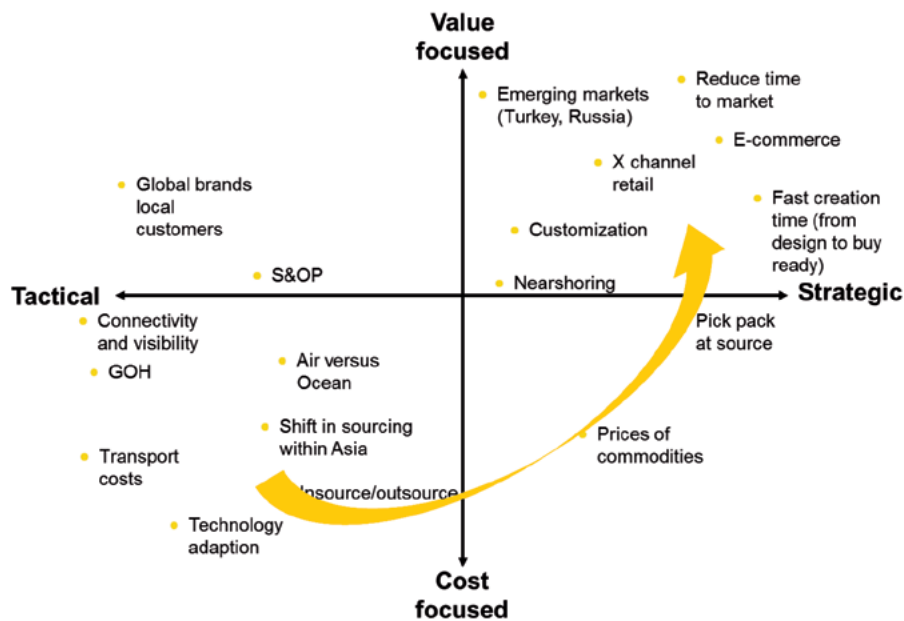
the challenges that were raised most frequently. The key drivers behind these challenges are clearly cost and time to market. Based on this feedback, BCI made a value chain overview and positioned the various points from a supply chain management perspective. It illustrates the wide scope of challenges supply chain executives face in their roles and responsibilities. It also illustrates the importance of prioritizing strategic initiatives versus the daily balancing of many operational tasks and responsibilities, as shown in figure 6.



Source: Buck Consultants International

Figure 5

Challenges from a supply chain management perspective



Source: Buck Consultants International

Figure 6

Within the fashion and lifestyle industry a number of the more strategic topics have been on the radar and on the agenda for the last few years, but why has the industry not been able to make step changes forward? From BCI's experience only a few companies with scale and/or with the proper investment in competence development have been able to bridge the gap and make changes to advance their supply chain maturity. Most companies within the industry still see supply chain management as a daily operational, execution entity to ensure goods get shipped out, stored and distributed on a daily basis. In the latter case it is evident that the supply chain management executive will not be invited to join the boardroom and drive changes.

From the industry survey, BCI noticed that a number of elements related to improved planning and sales and operations processes (S&OP). Sustainability and risk management did not come up as strategic challenges for which to formulate plans and actions. Technology solutions such as Radio-Frequency

Identification (RFID) to enhance end-to-end visibility did not come up as opportunities to investigate either. Initiating a number of strategic challenges will bring the quickest and largest value gains. However, initially these points will require more effort of supply chain executives to action. They will require internal collaboration between departments and require board level executive sponsorship to ensure they succeed. They will perhaps also require more collaboration with logistics service providers to develop new and innovative solutions and capabilities. However, the results will be a better aligned supply chain in which lead times and margins are improved overall, and in which customer satisfaction plays a pivotal role. Companies are increasingly realizing that their supply chain today is a strategic asset to the company in the execution of the company's business model and key to driving top level growth and bottom line margins. This makes prioritizing and moving forward on the various supply chain challenges an important responsibility for the whole company and not just a task for the supply chain department to manage and push forward.

Risk Management

Over the past year the world has seen some global disruptions to supply chains such as the Tsunami in Japan which subsequently triggered a nuclear crisis and energy shortage. Major flooding occurred in countries such as Thailand, Indonesia, Bangladesh, China and the Philippines – all key sourcing regions for apparel, footwear and accessories. Other more predictable risks impacting companies include rising oil and energy costs, sustainability and corporate governance legislation, the financial crisis within Europe and risks to the Euro zone beyond 2012. Increasingly, executives within the fashion and lifestyle sector recognize the need for better risk management in their supply chain.

As part of the process of enhancing risk management methods, many companies have begun to monitor their suppliers' financial status and mitigate default risks, whilst they aggressively manage their own working capital. Today, risk has become a management challenge across the entire supply chain. Dealing with cost pressures, many customers have increased their efforts in asset management and have started

shifting supply chain risks upstream to their suppliers. To mitigate end-to-end supply chain risk, companies should develop an integrated approach that includes the customer perspective. Partnering with key customers involves more frequent or even real-time demand forecasting, or applying newer practices such as demand sensing and scenario modelling. The goal is for all supply chain partners to share the risks for demand fluctuations, inventory, and other cost drivers equally. This end-to-end perspective is critical for success.

Companies should not only be managing the risk at each node of their own supply chain but should also consider their key partners' supply chain. Essential to joint supply chain management are integrated S&OP, which are based on a joint database and involve immediate notification to all partners if key parameters, like delivery dates of components, change. End-to-end supply chain visibility and immediate corrective actions are essential for reducing risk and financial exposure across the supply chain network.



PART 3

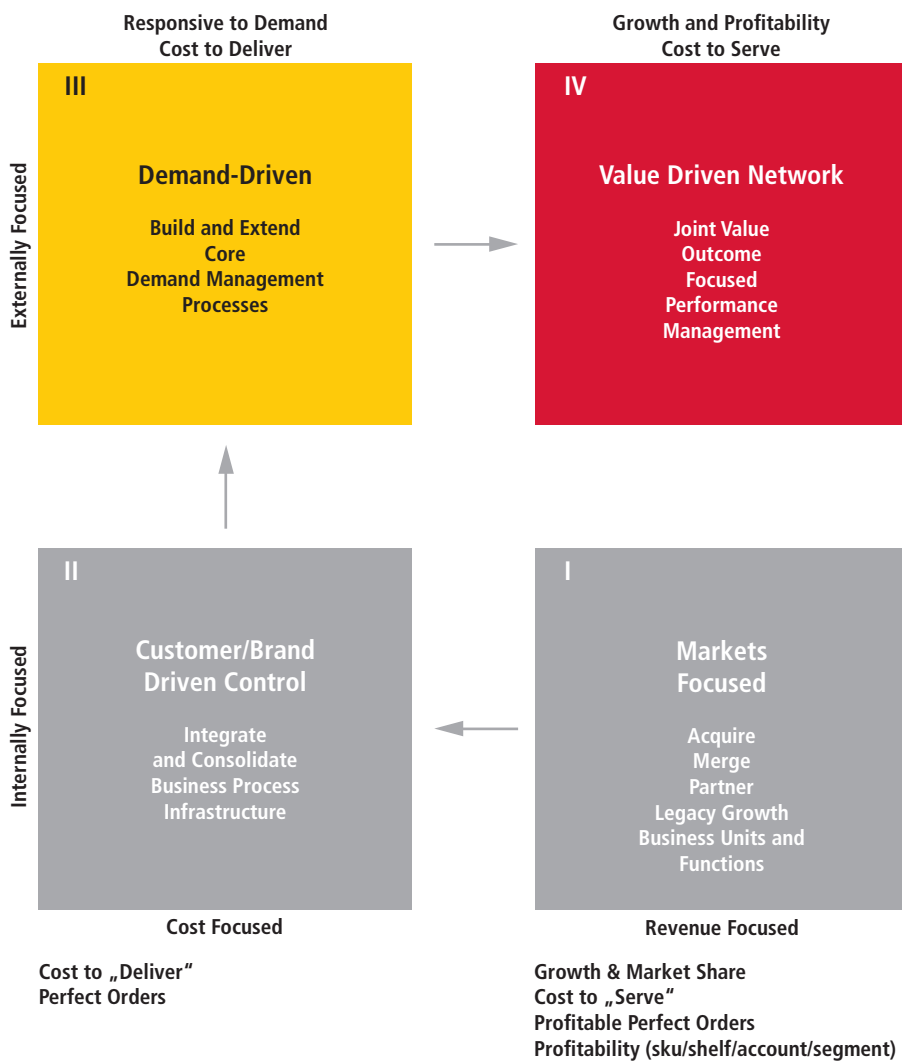
Towards the Future – Making a Step Change in Supply Chain Maturity

Leading fashion and lifestyle companies have been growing their supply chain maturity over the past few years. The top performers have shifted their focus from an internal towards an external orientation. Furthermore, they have shifted from a purely cost centric approach towards creating value to grow their business and building a value driven network. This does not happen overnight. The majority of fashion and lifestyle companies are still in quadrant I

and II shown in figure 7 below. Key in this journey towards step changes in supply chain maturity is, amongst other factors:

- Alignment with customers (demand visibility, customer-brand owner performance metrics).
- Focus on growth and market share and the role supply chain management can play to achieve these goals (cross functional).
- Visibility on cost to serve to generate profitable perfect orders and rationalize / change business parameters when required.

Stages of value chain transformation / Change maturity



Source: Buck Consultants International

Figure 7

Framework for the Future – Key Developments

From the supply chain executive survey the following eight key challenges were identified by BCI which, in their opinion, will form the supply chain agenda within the fashion and lifestyle industry in the next few years. Figure 8 below highlights these challenges and illustrates how they might impact shareholder value with regards to revenue growth, cost reduction and time to market.

Supply chain executives within fashion and lifestyle companies are invited to explore these key themes further within their own company.

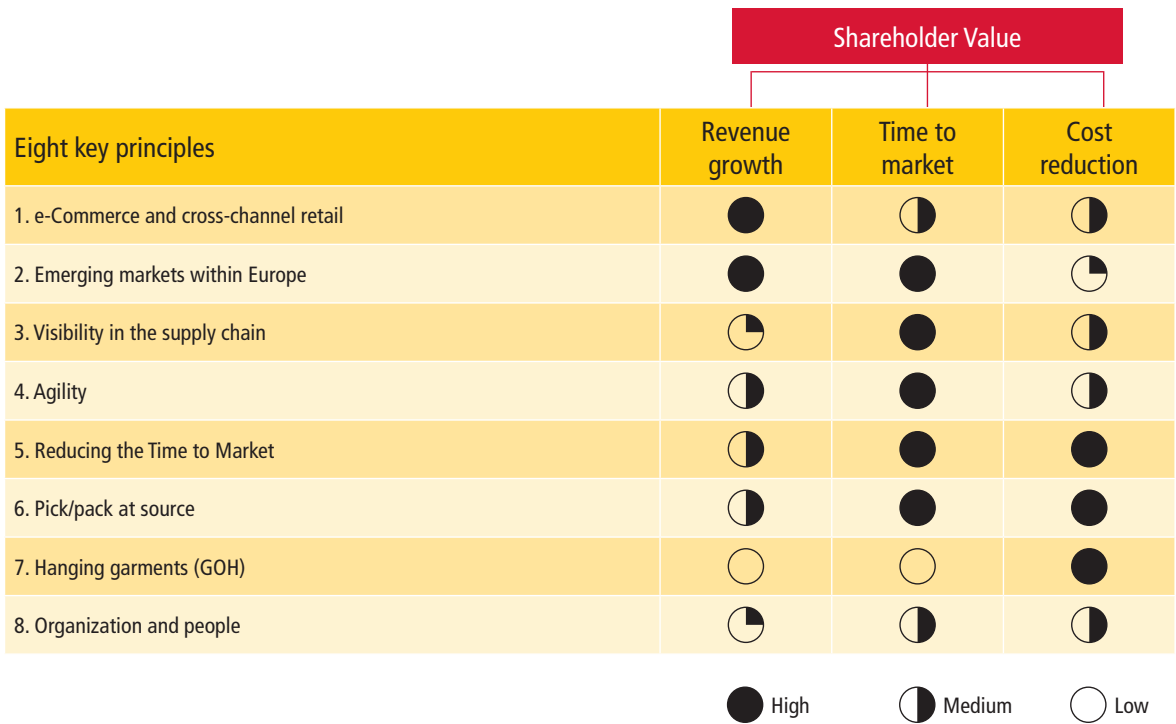
1. e-commerce

Online retailing is the largest growing retail channel in Europe today. The fashion and lifestyle sector is the strongest growing online retail channel in Europe.

Online retailing has allowed companies to tap into new types of customers and geographical markets. In addition, it has also allowed companies to develop more enhanced and wider product programs to complement existing product portfolios. This, in turn, helps build brand loyalty which over time provides more growth.

There is rapid online retailing convergence and growth across Europe, led by North Western Europe in particular, that is now also starting to develop strongly in Southern Europe and some of the emerging markets such as Russia and Turkey.

Eight key supply chain challenges affecting fashion and lifestyle companies.



Source: Buck Consultants International

Figure 8

Forecast of Online Sales in Europe, 2011-2015 (E)

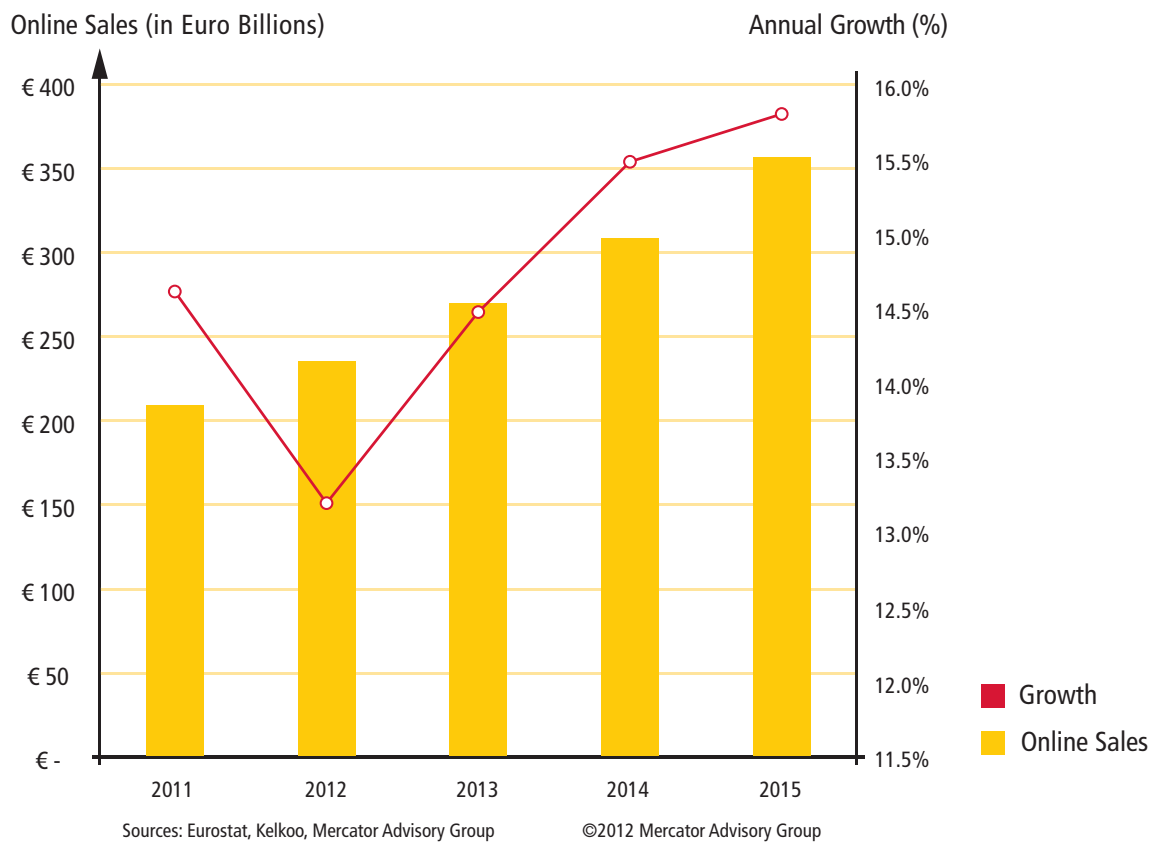


Figure 9

Cross-Channel Retailing

The cross-channel retail concept is a “hybrid” business model. It is a combination of retail choices made available to customers to maximize choice and revenues. More and more customers use the combination of choices to make a “final purchase”. This can typically start with online research on what to buy, where and at what price; they then go into the physical store to see and buy the final product. A recent report by ABN Amro, “Cross Channel Retailing – the Future 2015”, identified cross-channel retailing as the future business model within retailing. The report concludes that pure online shopping has reached its saturation point, and that in the future consumers will make more use of both online and offline retail concepts in combination to make purchasing decisions.

Cross-channel retailing from a supply chain perspective creates greater complexity as consumers have more choice in how to receive/collect and/or return the goods they purchase. Think about stores in high streets where back rooms are limited and how these stores need to integrate the physical brick and mortar business with the online business.

The combination between the physical store and the online e-commerce model means that retailers need to find greater cost synergies between warehousing, transportation, return and handling processes.

The cross-channel concept is definitely a concept for the next years to come as, if executed correctly, it can create customer experience and loyalty, cost synergies and thus improve margins. It is obvious that cross-channel retail is more than placing an internet shopping experience in a physical store.

An example of a cross-channel retail model is one where a fashion brand runs stores where customers can buy their product physically from the store or online. In this example, the fashion company operates one EDC from which distributes both store and online orders to one or more countries using the same transportation flow. Online customers can collect their purchase order from a physical store for free, or choose a low cost, home delivery option using a domestic courier. For the return management process, consumers can elect a free physical store return or elect for a low cost courier collection. This creates increased customer satisfaction and synergies in transportation costs.

Many fashion companies currently have a multiple channel strategy in place where decisions are being made on a channel level. From a supply chain perspective the integration across channels is hardly there: IT systems are different, fulfillment models are different and logistics processes and physical infrastructure are separated from each other. Therefore, migrating to a cross-channel strategy will heavily impact the supply chain infrastructure of a fashion company.

Given the customer demand for cross-channel retail, retailers and fashion companies need to rethink this strategy and set up an aligned channel and supply chain strategy.



Advantages relate to transport cost synergies and increased store collections. Another advantage relates to in-store collections and returns in that it increases in footfall and creates new opportunities for sales.

Challenges relate to in-store staff having to handle online orders and returns. A second point is that retail space in shops is often limited, which makes storage difficult.

Key Building Blocks for the Cross-Channel Model

The cross-channel retail model brings more complexity to the e-fulfillment backbone and company supply chain. Think about IT systems that need to be cross-channel enabled. Think about

customers buying online in one country and returning the goods to a store in another country. Through customer studies, BCI identified a number of key building blocks across internal departments and disciplines, which form the basis for any scalable cross-channel business. The key question is, whether the majority of the fashion brand companies are ready to embrace this model given the current set up in Europe?

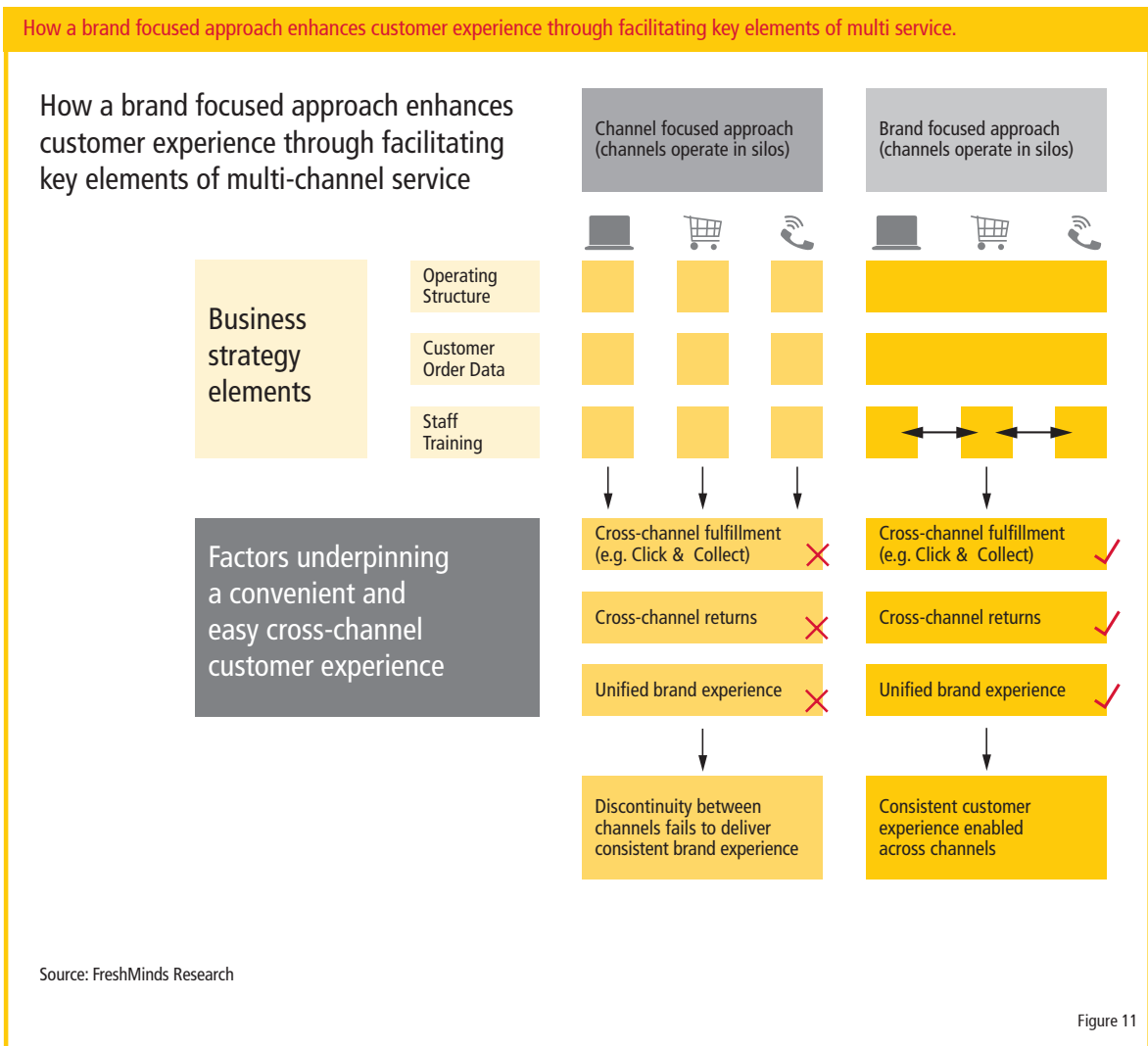
The blunt answer to this question is ‘No’. A DHL study conducted recently concluded that the majority of retailers and fashion brands have been focusing their efforts primarily on the front-end and not on the backbone and related supply chain infrastructure.

Cross channel model requirements	
IT	One centralised inventory for all channels Line level visibility One integrated IT system (Order management, WMS, TMS)
In-store	In-store staff have to be able to manage online orders (collections and returns) Sufficient storage space for online orders and online returns Create instore online order terminals for customers to use
SC	Supply chain network design flexibility
OPS	Centralized handling processes
Finance	How to manage accounts receivable

Therefore, huge gaps exist within the current supply chain infrastructure and the full cross-channel requirements. Companies need to assess their needs and invest in their supply chain infrastructure and related backbone to build an infrastructure that enables cross-channel retail. Given the pace of the current marketplace, the supply chain executive needs to develop a clear, pro-active strategy, sooner rather than later, in conjunction with business owners to support the business.

Essential to any solution is a strong IT backbone which integrates the various functionalities from order management to warehouse management and transportation. Preferably in combination with full

order level visibility to be able to match orders, deliveries and returns in a single system. In turn, this system should be linked into the company's financial system for payment and refund purposes. Operationally, bringing the two sales channels closer together into a centralized warehouse management process allows inventory and handling processes between both channels to be shared both in the outbound and in the returns process. This minimizes inventory and double handling costs. The supply chain functionality needs to be able to support the cross-channel business model with scalable yet flexible solutions, in which consumer choice plays a central role against which the distribution and return processes are managed.



Retailers should prepare, plan and pilot

Prepare: Given the complexity of the challenge, a phased approach to channel launch is extremely beneficial.

Plan: Retailers should involve both suppliers and logistics providers at a very early stage in the decision-making process.

Pilot: Once a launch strategy is identified, a pilot approach to actually entering the market can be advantageous. It might be by geographical region; only offering the new channel in one locality or by product range.

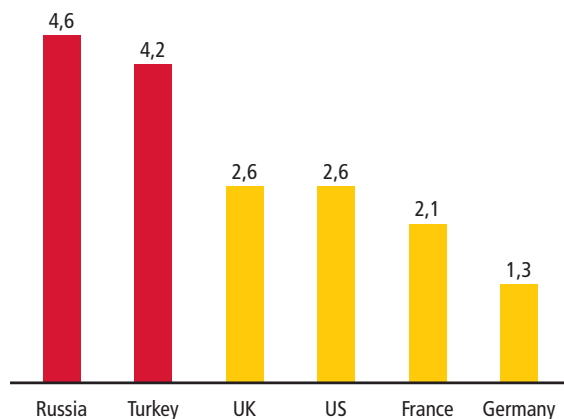
2. Emerging Markets within Europe

It is fair to say that Europe in 2012 is experiencing different levels of growth in its various geographies. At the time of this report, North Western Europe is still showing some signs of retail growth, although most of this growth is generated through the online

retail model. Southern European retail markets are showing signs of decline with lower sales and in some instances closure of businesses and retail stores. This report highlights two growing economies such as Russia and Turkey, which in contrast, are showing relatively strong economic growth and a strengthening retail sector. Fashion and lifestyle companies are lagging behind other sectors in penetrating these developing markets compared to other fast moving consumer goods (FMCG) and consumer product groups.

Many small to mid-sized fashion companies do not fully explore the opportunities in these markets and only use exclusive or multiple distributors. Over the last three years large companies such as Nike, Adidas and Levi's have set up, supply chain operations in Russia to support their own business model in this market.

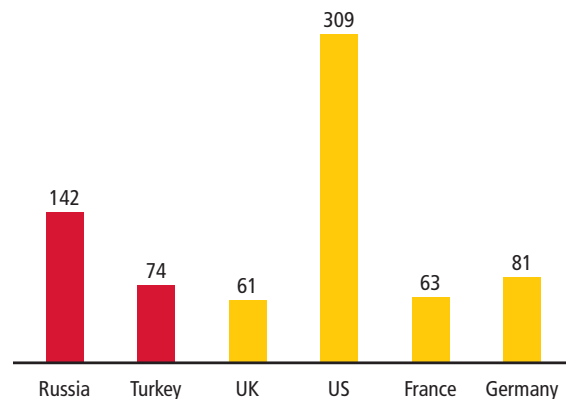
BRIC, N11, G7:



Source: Buck Consultants International

Figure 12

Population 2011, in Millions



Source: Buck Consultants International

Figure 13

The Russian Market

In Russia, the retail sector has shown two clear trends in recent years. First, the Russian retail sector as a whole has started to mature beyond the initial “set-up” phase experienced by many Western companies. Second, there is an expansion further into Russia beyond the key cities of Moscow and St Petersburg. Russia has a population base of around 145 million people. There are at least 15 cities in Russia with a population above 1 million and more than 40 cities with a population above 500,000 people that have a hunger for western brands, and are willing to pay premium prices to obtain Western branded goods.

Besides Moscow and St Petersburg, key urban centers with a strongly developed retail environment include Novosibirsk, Yekaterinburg, Kazan, Samara and Rostov.

Scaling up to seize the growth opportunities in Russia means new challenges relating to the design of the supply chain.

Given the customs related bottlenecks and relatively long lead times, does it make sense to set up a local distribution centre (DC) to enable faster processing of local orders? How do you establish a scalable and cost effective distribution network throughout Russia outside the Moscow and St Petersburg

region? How do you deal with replenishment orders and returns? These are all relevant questions which should be addressed.

Turkish Market

Turkey also represents a relatively high growth market based on a population almost the size of Germany. Turkey acts as a geo-strategic link between Europe and the developing Middle East. The Turkish government is working on a number of strategic projects to further develop its logistics infrastructure in rail, road and ports to bridge the link between Europe, Asia and the Middle East. Turkey also forms an interesting production market of textile goods as a “near sourcing” alternative to the Far East. A limited number of brands have directly penetrated the Turkish market to date.

3. Visibility in the Supply Chain

Many industries, such as the automotive and high-tech sectors, are able to manage their supply chain with complete end-to-end visibility. From the survey and industry research it is evident that product visibility is still not a subject high on the agenda of fashion and lifestyle companies. However, the potential is large, given the long lead times, mix of air and ocean shipping, fragmentation across the supply chain and the on-the-move sourcing base.

Population 2011, in millions



Source: Buck Consultants International

Figure 14

Visibility at purchase order (PO) or line item level allows much better management of the supply chain related to product availability, liability, costs and obsolescence. To enable line item visibility there needs to be more focus on

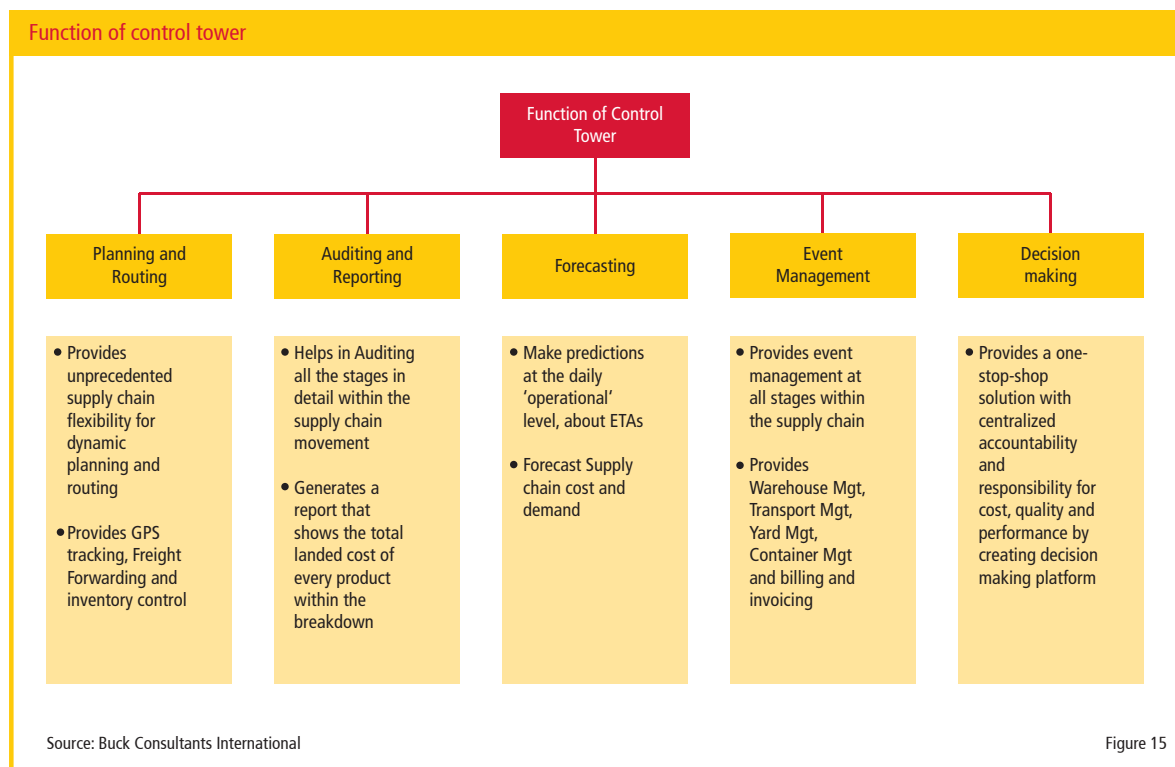
- A. integrating the companies IT systems into one overall management system
- B. integrating suppliers and logistics service providers into such systems and processes.

To enable end-to-end visibility, all parties in the supply chain need to build in management processes which ensure all goods are, for instance, scanned. In turn, this will enable the development of control towers to manage the data related to all the physical flows within the supply chain and to measure these against pre-set key performance indicators. PO management and PO visibility will provide fashion and lifestyle companies with clear visibility of the performance of current vendors, ability to

meet scheduled milestones for product launches and shipment information. Too often, providers are executing logistics activities upstream but without an entity managing this activity. The perception is that it is not important whether the fashion company conducts this activity, outsources it to a lead logistics partner (LLP), or outsources it to a sourcing agent. However, vital to this activity is management, to ensure there is overall visibility across the supply chain.

From the industry survey, it can be concluded that over 80% of companies are "managing" their upstream part of the supply chain in Microsoft Excel.

Given today's IT software as a service concept, and the fact that implementation and hardware and software costs of such control Tower/TMS have been reduced, the return on investment (ROI) for many fashion companies will pay off.



4. Agility

Agility is all about the ability to be responsive within the supply chain to changes in demand and supply. Speed and flexibility are key to the capability of an organization in order to respond quickly to market opportunities and threats.

Being able to take an idea to market faster than a competitor and to take full advantage of new technologies to get closer to customers is vital to future growth in today's marketplace. Quicker response times help companies to react to consumer needs faster.

Speed of action is one of the great attributes of the high performer. Lower performers can see the same opportunities, or can even bring together the right insight with the right authority to take a decision, but it is the speed of action that really matters.

Apple has demonstrated this year-on-year with its supply chain model having been regularly awarded the world's best performing supply chain by AMR Research.

Zara introduces approximately 11,000 more new items a year than its direct competitors. Zara designs products much faster than many of its competitors. The design to delivery turnaround time for new designs is often between 2- 4 weeks.

Gaining business flexibility requires a company to establish the right balance between adaptability, agility and stability in their operating model, cost structure and processes. It is vital to be able to make these changes without compromising the underlying stability of the company.

5. Reducing Time to Market

In the fashion and lifestyle sector, time to market is of the essence with regards to seasonal changes in product line ups and new product launch events across the various marketing channels. More often than not, the production sources are far away from the markets, which means transportation and distribution lead times need to be considered as part of the design and production process. In

general, time to market is for many brands more important than saving a few Euros on logistics and transportation. What has the supply chain community in the fashion industry done to date? What do they need to do to support the business?

A. Vertical Integration

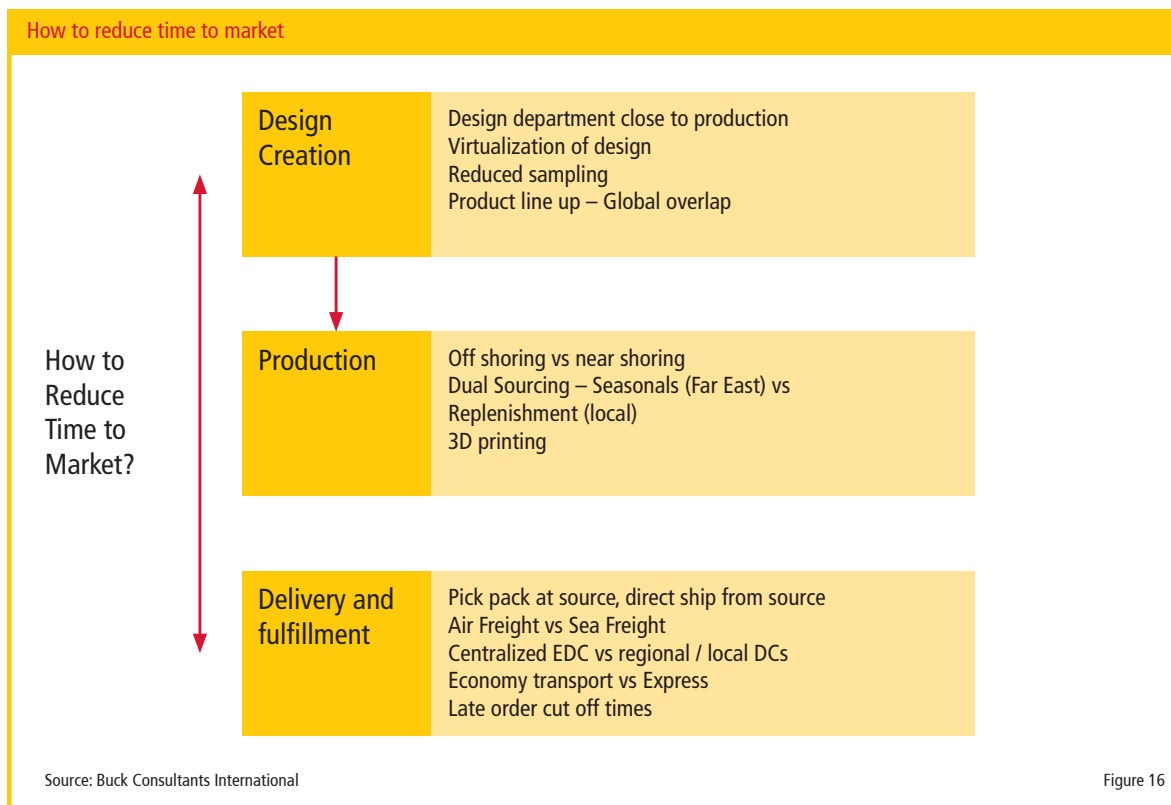
Some fashion companies now operate their design centers close to their supplier base in order to speed up the design phase and shorten the sampling time required before production. Zara claims to be able to design new garments within two weeks, which in combination with its production in Europe allows for a four week turnaround time from design, to production, to in-store delivery across Europe. This in turn allows them to very quickly introduce many new items during the year. Average fashion companies, applying the traditional "demand push" model require up to nine months turnaround time. In other words, a holistic understanding of speed to market is required in order to be able to optimize the role the supply chain can play in this process. Intercompany or vertical collaboration should be part of this process. There are many elements that are part of the design to delivery development process. Each can play a role in optimizing the speed to market and the role the supply chain can play within this process.

B. Near Sourcing

At the same time, longer lead times out of Asia and increasing energy related transportation costs are forcing companies to look at sourcing closer to their markets, looking more closely at sea, rail and air options and combinations for inbound transportation choices from the Far East.

Near shoring from a logistics perspective is typically not done, but should be implemented from a business strategy concept. Over the last 10 years Zara has been the leading example in this. However, more recently near shoring for in-season replenishment has been explored by other companies such as Gap, Crocs and Adidas.

It is interesting to note the development of near sourcing in the United States. With rising costs in



China, increasing productivity of U.S. workers, supply chain risks and weather unpredictability, U.S. fashion brands are progressively increasing their manufacturing capability in the United States. From small start-ups to large corporations, more and more companies are cutting ties with China and re-shoring manufacturing back to the United States. Besides cost, consumers are increasingly supporting “Made in America” goods, which are creating jobs in the U.S. The Obama administration has specifically used the fashion industry to promote a “Made in America” campaign to bring manufacturing jobs back to the U.S. and double exports by 2014. U.S. apparel and textile exports grew 13.7% in 2011.

Each company will need to make the holistic trade off, on time and reliability to market, quality of the vendor base and landed costs. For some this means off-shoring to find the lowest cost production, for others this means sourcing closer to the home markets, paying higher labor rates but benefiting from flexibility and reduced time to market.

C. Transportation

There is an increasing choice of transportation modes and routes of transportation between production sources in the Far East and markets across Europe. This allows fashion and lifestyle companies to become much more creative in how they manage seasonal demand, versus in-season replenishment and product launches. Given that cash is often king and lead times are imperative, applying different modes of transport to service market and customer priorities is a more comprehensive way of looking at the “cost of service” than the cost of transportation alone.

Many in the industry have been quite negative about the recent development of slow steaming, offered by major shipping companies, as they move to next generation cargo ships. Apart from the downside in slower sea freight lead times there is possibly one upside worth considering. Slow steaming can provide a relatively low cost “portable” warehouse facility, versus fixed cost warehousing facilities for slower moving or standard goods, for which demand is steady and/or predictable across the season. Options

such as slow steaming can be combined with in-season replenishment via sea-air or air transportation, allowing a faster time to market. The pick/pack at source model, in combination with Direct Ship using various sea/air or airfreight options allows for faster time to market for high value goods and/or in-season product launches.

A number of new transportation corridors are becoming alternatives to traditional trading routes between the Far East and Europe. There are various rail options between China and Europe through which more and more cargo is being transported by large logistics and rail operators. Sea corridors into Russia through the Black Sea or via the Balkan states, such as Estonia, with excellent inland road and rail connections, are increasingly becoming viable alternatives to traditional routes and increase the flexibility needed to operate scalable supply chains across many markets.

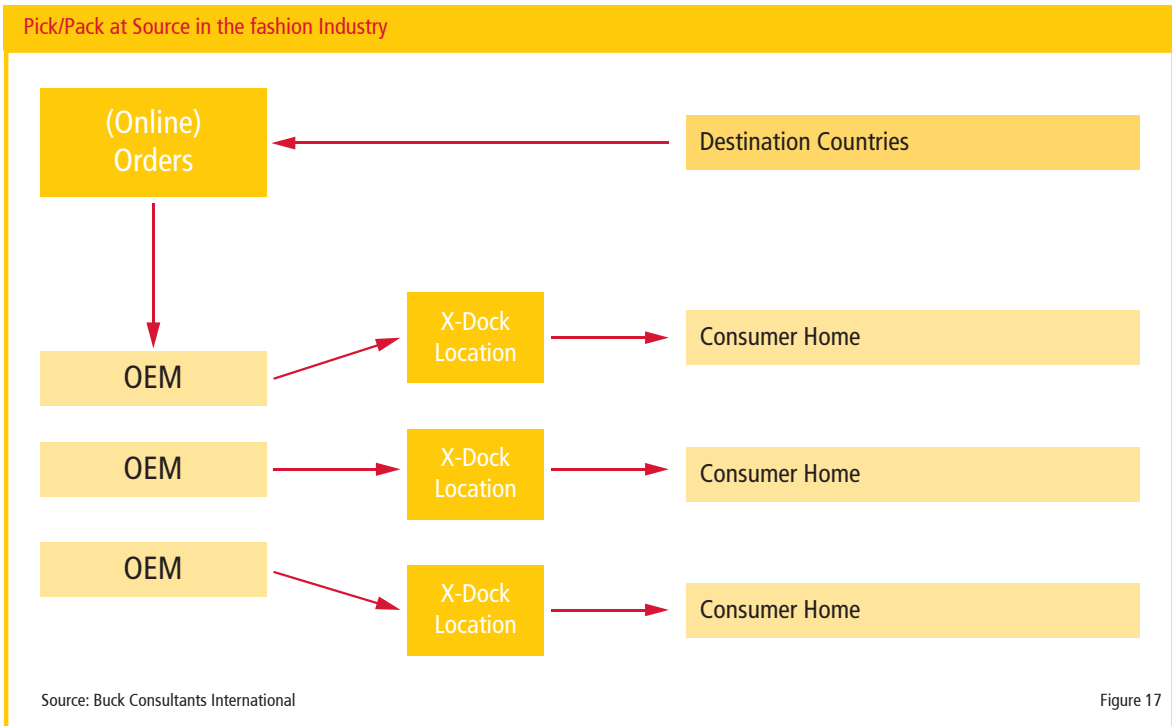
6. Pick/Pack at Source

A number of industries such as the high-tech and automotive sectors also produce their goods in the Far East and operate supply chains in which the

“ship to order” point is located at source. Picking and packing orders at source allow companies to ship high volume goods directly to key markets and customers instead of having to channel all orders through a regional DC.

Talking About Speed

Apple Computers claim that their “ship to order” model to online customers allows them to reduce the cash to cash order cycle down to 20 minutes. In financial terms this means that Apple carries the inventory for only 20 minutes in its accounts. In practice this model implies that their Far East original equipment manufacturer (OEM’s) produce and own the goods until the moment of shipping. Ownership of goods is then electronically transferred to Apple who in turn swipes the consumer’s credit card. At the same time the goods are picked/packed and shipped from origin to markets across Europe using break bulk airfreight. Several European cross dock locations are used to import the goods into key markets. Typically from there they are delivered directly to customers through an integrated Express network. The results are higher



transportation costs but lower inventory holding costs and faster turnaround time. As a result, Apple is able to reduce its cash to cash order cycle to a bare minimum, which has an enormously positive impact on cash flow and margins.

The pick/pack at source model is also starting to have an impact on the fashion and lifestyle sector. Some companies have started to test picking and packing orders for customers in certain markets at source in consolidation centers. These consolidation centers are typically available from logistics service providers who can also offer other value added services such as merging of orders, labeling, packaging and storage before shipping. Logistics service providers typically manage the break bulk concept for customs clearance and shipping. Consolidation of orders allows for product or line item visibility to be introduced more easily. This is more difficult if shipping in bulk directly from production sources. Visibility allows for better management of inventory throughout the supply chain.

To enable pick/pack origin decisions to be made it is important to understand a few parameters:

- Fragmentation of vendors (i.e. many suppliers spread across the globe) means bringing products into a single hub might not be practical.
- Minimum order quantities of vendors (this is particularly relevant when vendors have minimum order quantities. When placing a PO per market by vendor, a consolidation hub will provide more value).
- Channel requirements – e.g. typically initial launch or pre-sold items classify at first for direct ship from consolidation center.

What are some of the key advantages of pick/pack operations at source for companies operating in the fashion and lifestyle sector?

- A. Transit time reduction. The ability to ship direct from source to markets and customers and bypass a distribution hub (DC bypass) will reduce valuable lead times.

- B. Lower inventory holdings. Direct ship models to customers allow for lower inventory holdings in warehouses and other possible inventory points throughout the supply chain. Apart from lower costs it means lower complexity in running DCs.

- C. Improved quality. Making more quality checks at source and/or transferring more of this responsibility on to suppliers means that fewer checks need to be performed later in the process. Quality issues can be dealt with directly at source which means less quality problems further along the supply chain process.

- D. Lower warehouse related costs. Conducting pick/pack at source and shipping directly to key markets requires lower volumes to be transferred via European based DCs. Lower volumes require less warehouse space and handling of orders, which in turn reduce warehousing costs.



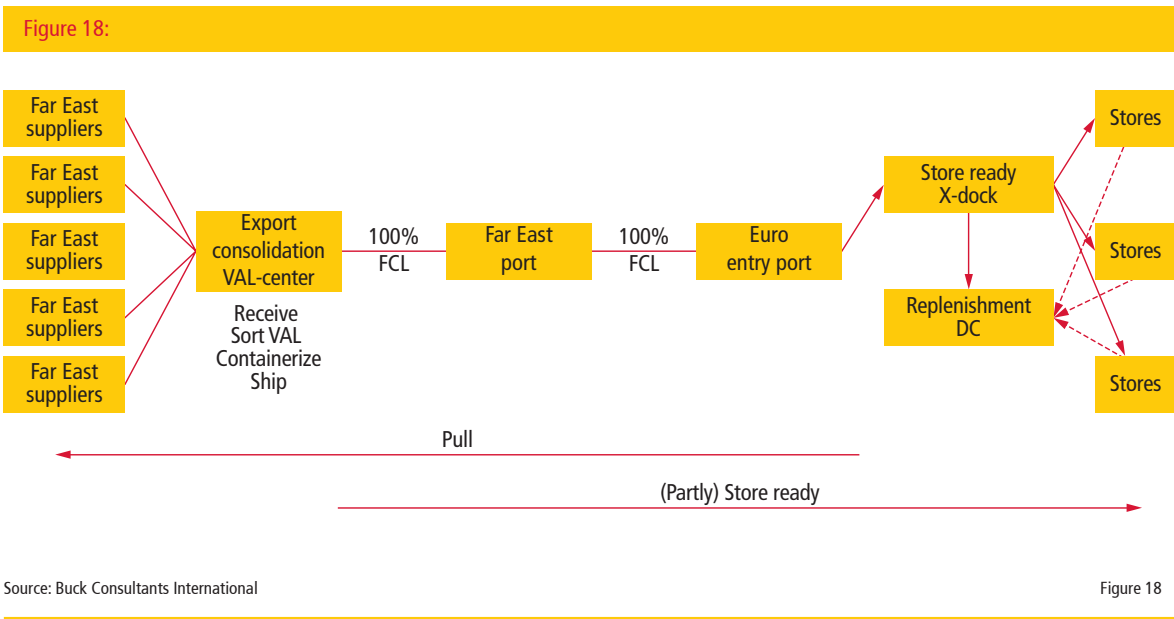
- E. Lower overall supply chain costs. Direct ship models may carry higher transportation costs (especially in lower replenishment orders) shipped directly to key markets and/or customers. However, inventory holdings are significantly reduced, both in value and in time, having a positive overall impact on costs and cash flow.
- F. Improved visibility within the supply chain. Moving from bulk transportation to enabling pick/pack processes to be implemented successfully at source requires upfront efforts to ensure that order management data is linked to visibility of product throughout the supply chain. This enables better tracking of goods in the supply chain which, in turn, lowers loss rates, reduces rework and replenishment.
- G. Generic PO's for multiple markets - instead of a single PO by market by vendor - with no minimum order quantities, allows allocation to markets much later in the process.

When fashion companies place their PO at the supplier level by market, combining all markets that flow through the hub will result in several benefits including taking away the so called minimum order

quantities of the suppliers especially for small to medium markets. Having a generic PO placed at the supplier, the fashion company can allocate items to the respective markets much later in the process, which allows for maximizing sales opportunities and flexibility.

The diagram below depicts how such a model can work in reality.

Although this concept is not new and companies in the high-tech sector have adopted this for quite some time, the adoption rate by fashion brands is quite low. Yet many fashion retailers have adopted this model as they have the critical size (e.g. Target, Carrefour, Auchan, Best Buy). However, most fashion brand owners still do not utilize this concept very actively. Companies that have successfully implemented this concept include Crocs, G-star, Rivers, and Coach. Some of these companies have been able to ship 80% of their pre orders/ launch items from the sources or hubs directly to the markets and use their European infrastructure as a cross dock, to guarantee quality as well as the ability to steer or hold orders (e.g. in the case of customers with a payment issue).



7. Hanging Garments Dilemma

The majority of the fashion brands have garments on hanger (GOH). Whether this number is 5% or 25% of their total business is less relevant, as the main point is that many brand owners are struggling on how to best cope with the GOH in Europe. Over the last few years, the general GOH market has declined and from a transport and logistics industry perspective the GOH has become a very local - often customer dependent - solution.

Meaning a solution that works in Germany does not work in France or the Nordics.

It is interesting to note that in the United States GOH is not seen as an issue as almost all brands ship GOH-F (Flat packed).

When the business requirements clearly state GOH transport and handling, the question is how best to

coordinate this on a European level. From a packaging perspective, different container and carton boxes exist to deal with the hanging garments issue. From the survey and subsequent roundtable discussion with a number of fashion companies, many indicated that these solutions are either too expensive, too regionalized or simply haven't been tried yet. Given that the business volumes are generally low, the impact and potential headache is relatively limited.

As several companies face this issue and the logistics and transport landscape is very fragmented and with no single European solution, the key question is if one cannot learn from collaborating with others like the business case study below from a different industry demonstrates?



Case Study: Is Horizontal Collaboration a Potential Solution?

As well as supply chain management being seen as a cost savings opportunity, it is also an opportunity to differentiate the organization, based upon competitive customer service or implementing a competitive market strategy.

A solution can be found by looking to other industries where supply chain organizations collaborate vertically and horizontally.

This is common practice in other industries like FMCG to reduce cost and increase service level.

The biggest tire retailer in the UK decided to set up a central warehouse and take the outlet distribution into their own hands as they have a huge flow of old tires to collect. While this retailer’s volume increased the load efficiency of the distribution, their competitors distribution costs increased. The response of the manufacturers was two-fold. Firstly, some of them set up a joined distribution network to combine volumes at the same service and cost

level as before. Secondly, one of the manufacturers aligned inventory with the retailer to increase product availability in the network. By doing this the market share of this manufacturer within the portfolio of this retailer increased.

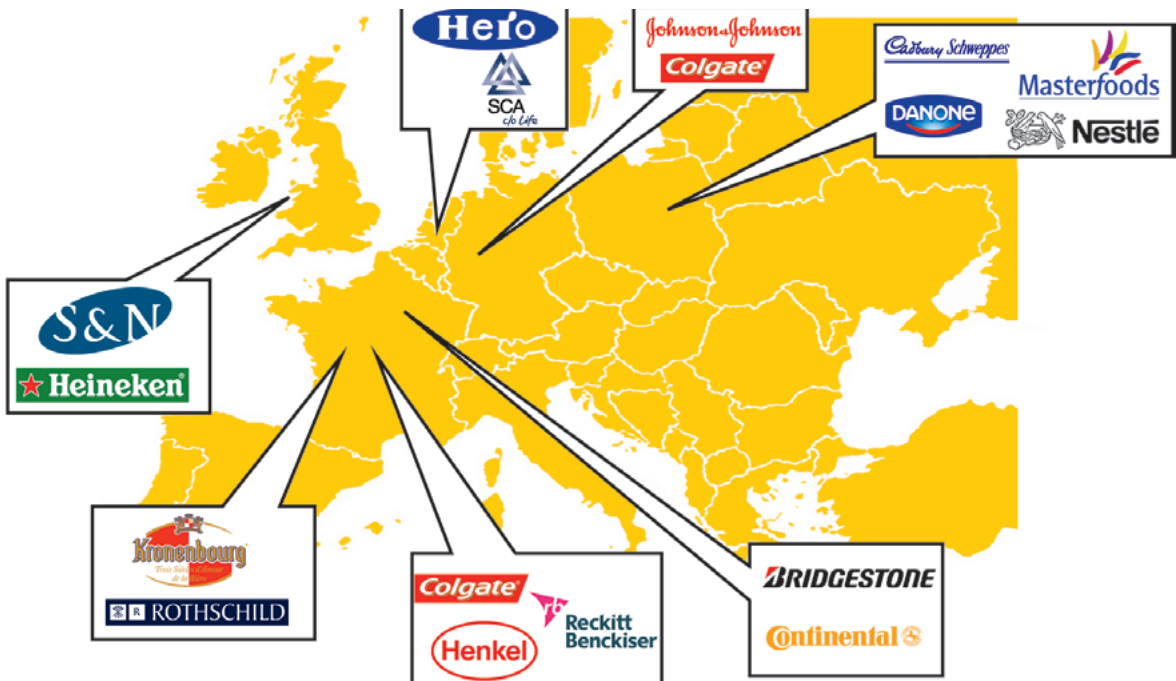
8. Organization and People

The Role of the Supply Chain Executive

Little can be achieved without a supply chain organization that is truly integrated across all functions and empowered with the right incentives to take action.

Leading companies understand that break-through improvements and innovation are not possible unless the decisions made are optimal for all supply chain functions. Managing all the functions of the supply chain as a single resource under one joint responsibility is part of this understanding. Leading companies are making sure the organization has a strong end-to-end optimization focus and are integrating supply chain partners up and down-

Examples of industry collaboration within FMCG are illustrated below.



Source: Buck Consultants International

Figure 19

stream as a result. Applying the right incentives to steer behavior and creating the right company business culture is key in this respect.

Supply chain management executives in fashion and lifestyle companies do need to put the right basic fundamentals in place. Doing that alone won't provide them with an invitation to join the board. Like in other industries, one needs to earn his or her seat at the table.

T-Shaped Supply Chain Professionals

This is where T-shaped supply chain professionals come in. T-shaped people are open to the needs of the wider business rather than only their own direct work responsibility. The vertical bar on the T represents the depth of related skills and expertise in a single field, whereas the horizontal bar is the ability to collaborate across disciplines with experts in other areas and to apply knowledge in areas of expertise other than one's own. I-shaped people only understand their own function, but T-shaped people understand the process and wider business model they are part of, and also the functional strengths they bring to the table.

T-shaped professionals are crucial in this respect as the supply chain of fashion companies encompasses many processes that are interlinked and typically owned by the supply chain and other functions within a company. Being a sparring partner pro-actively for other disciplines is key, in order not to become a day-to-day fire fighter.

One of the enablers for both internal and external collaboration is strong communication skills. Many supply chain executives are focused on operational aspects of the supply chain, so measuring cost-to-serve and performance are key. Soft skills to communicate better with other business partners, both internally (e.g. with Sales & Marketing) and externally, will be as important as the hard technical skills.

The future will need the T-shaped executives to move supply chain forward. T-shaped people understand the drivers and challenges of their peers in other departments and are able to bridge these towards joint goals.

Business intelligence is important in order to understand what is happening in the operation. Furthermore, it gives the supply chain executive tools to discuss with other functions in the organization or even with business partners. In the example of migration towards next steps of supply chain maturity it is about cost to serve and the parameters that influence the joint profitability between the brand owner and the customer(s). This collaboration is key to be able to migrate products continuously into the right segment to remain profitable in the value chain.



CONCLUSIONS

In conclusion, the role of the supply chain executive is of increasing importance in contributing to the company’s business model. Many of the “backroom” processes related to the customer experience are managed by supply chain professionals – on-time delivery, quality and costs. High top-line growth prospects within the fashion and lifestyle sector relate to new markets and channel concepts, as well as the ability to influence and manage the total costs involved in running the supply chain and managing levels of inventory. This means that the T-shaped supply chain executive needs to play a more strategic role within the organization.

Supply chain management executives in fashion and lifestyle companies need to implement and manage the right operational fundamentals. However, this alone will not give them an invitation to join the board; the supply chain executive will need to do more to earn his or her seat at the table.

With influence comes the responsibility to move beyond the operational day-to-day tasks of running the transportation, storage and distribution side of the supply chain and moving up the company value

chain to add value in providing solutions to strategic developments impacting the wider organization.

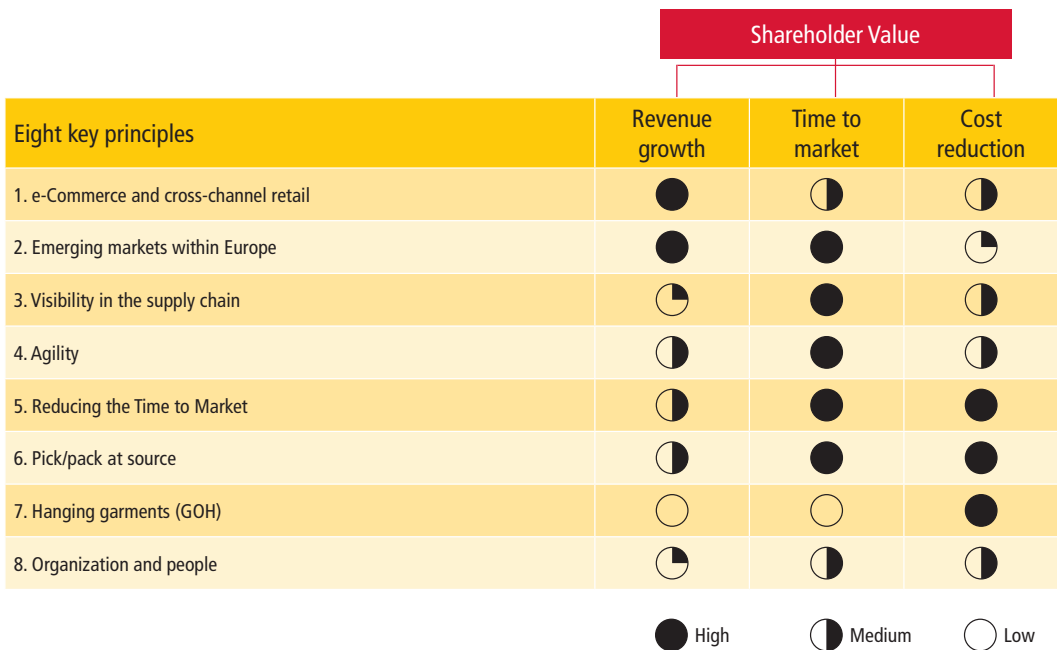
With respect to the industry survey, key elements that the supply chain executive can pro-actively focus on are developments such as the cross-channel retail supply chain infrastructure, PO visibility and more upstream visibility and pick/pack at source.

The successful T-shaped supply chain executive will get the mandate to drive these strategic developments as they impact the company’s business model by growing sales and market presence and increasing bottom line results. However, he or she should pro-actively drive the supply chain agenda in the coming years to make this contribution.

Based on the industry survey this report identifies a number of key areas for supply chain executives and their peer colleagues from other disciplines such as Finance, Operations, IT and Sales & Marketing to collaborate on to develop more integrated solutions to meet the challenges of the industry.

In summary, the supply chain executive agenda for the coming years is:

Eight key principles



Source: Buck Consultants International

Figure 20

REFERENCES AND SOURCES

Finding supply chain solutions to all these challenges is a process that will take time and will be different for each company. Not all solutions will be found immediately, however it is important to embark on this journey sooner rather than later.

Certainly this journey will hold setbacks and challenges that need to be overcome. However, vertical and horizontal collaboration are certain to take the journey forward in a forever vibrant and changing global fashion and lifestyle landscape.

BCI presentation roundtable, Berlin, 10 May 2012
Freshminds Survey – Multi-Channel Matters –
A route to next generation retailing



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Buck Consultants International (BCI, www.bciglobal.com) is a leading specialized international supply chain and location consulting and implementation firm.

Since 1985, BCI has been instrumental in re-designing and implementing the manufacturing and distribution footprint of many companies.

The Lifestyle / Fashion industry is one of BCI's key industry verticals with many leading and fast growing brands as our clients.

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