

w h i t e p a p e r

Is Your Supply Chain Fashion Forward?

Maximizing Performance in the Fast Moving World of Fashion Retail

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Quantum Retail



INTRODUCTION

Fashion retailers' supply chains and distribution networks often constrain their ability to always have the right product, in the right size and color, in the right store. And in fashion more than almost any other branch of retail, there is an additional challenge to ensure stores do not have overage at the end of the sometimes very short selling period that will have to be marked down, thus eroding margin. Fulfillment processes have been developed as a compromise between the financial and merchandising goals of the retailer and the operational constraints they face, but it is a compromise that comes with a price.

The first question that a retailer faces when it comes to a new product within the assortment is how much should they buy. This is an important question, as in most cases they only have a single production run of this merchandise and will not be able to get more. This is because fashion retailers selling in North America or Europe typically have their products manufactured overseas due to the low cost of production. Shipping products cost effectively across the world has to be done in bulk and takes so long that it is usually only done in one shipment, or perhaps in a series of pre-planned shipments to arrive in a two to three week window. When the order for the product is placed, retailers also have to determine which stores are going to receive how much product from each shipment. This is known as pre-allocating the merchandise.

Depending on whether they have one or more distribution centers, retailers may hold back anywhere from 0-50% of the inventory which they can use to 'fill in the holes' as stores begin to sell down. Among fashion retailers this hold back is likely to be in the 10-30% range of the original shipment. As stores sell through sizes or colors, this inventory is used to fill back up to pre-determined target inventory levels. Hold back helps to ensure that stores neither have too little nor too much of the inventory to meet customer demand. There can be great benefit in using hold back to help minimize stock outs and overages, but if you do not allocate enough to the correct stores at the outset, you can also lose sales. In North America where it typically takes much longer to move stock from the distribution center to the store, this can be a much greater risk than in Europe, where distances are generally shorter.



How can fashion fulfillment be improved?

The methodology fashion retailers employ for determining the buy quantity can be less than scientific and often based on historical sales rather than demand. Typically such historically-based projections are not good at reflecting the impact of seasonality on expected sales, or the unique localized requirements of any specific store.

Most of the inventory is pre-allocated, even though the goods may be received at the distribution center over a period of two or three weeks. During this initial period, sales may have already started to take place, but none of the information on new product sales is used to re-plan how to best utilize the inventory that has not yet been put on trucks going out to stores. There is no flexibility within the system to respond to the way the product is actually selling. For most retailers, the hold-back inventory is just used to fill to pre-set and arguably arbitrary target inventory levels, without qualification as to where it might best be placed and whether that target inventory level is correct. A single item at a particular store may have a planned eight week life cycle yet take seven weeks to sell its first unit, only for a store to be given another one that will inevitably end up being sold at markdown. This is a waste of limited resource.

Apart from helping to create the initial buy, none of the information from the assortment and range plan is used to drive the inventory decision process. This means that the product goals and merchandising strategies are lost as soon as the buy is made. Fulfillment ends up being driven by the supply chain team, who work to their own (and oftentimes less merchandising centric) goals. These might include getting all product to stores by a pre-determined date, or pushing out product to stores to make space in the distribution center, regardless of where the product is actually selling or not selling.

Operational Constraints

To make informed decisions that can apply financial and merchandising strategies or objectives to the fulfillment process requires the assimilation of huge amounts of information. Ideally, it also needs to be dynamic enough to respond to demand in the real world and in real time. Among retailers today, there is very little information driving the critical decision-making process. Averages and volume grade groups prevail and the result is predictably "average performance". Fashion retailers facing the pressures of growth and same store sales targets can attest that "average" is simply not good enough.



Technology that is in place to assist is too often unable to help for somebody who is trying to determine how best to use the inventory available. This means that those making the retailer's allocation decisions are always focussed on the next assortment of products because they simply do not have the time or resources to focus on what is currently actively selling in stores. If they could, they might take a moment and stand back to re-evaluate how best to service stores with today's product.

In many cases allocators have un-reactive systems surrounded by un-reactive processes. Lags in information and decision making mean they are not able to make and execute informed decisions on how to better allocate the inventory they have. In the fast-moving real world of fashion retail there is not enough time to process information on what is selling and replenish product out to stores. So what happens? Fashion retailers resort to a "Something is better than nothing" mentality thinking can become entrenched and exclusively focussed on pumping product out to stores rather than meeting the business's true financial and assortment objectives.

The root cause is that currently there is no way for retailers to translate their merchandise and financial goals into fulfillment decisions designed to meet the company objectives. This is because with current processes and tools it appears to be simply not practical to establish a link between the assortment and range planning process and inventory execution. But what if it were?

Some leaders in fashion retail are changing their business processes in order to overcome these operational constraints. Particularly in Europe, rather than sourcing all products from Asia Pacific, retailers are making calculated decisions to manufacture closer to home, either in the Near East, Eastern Europe or North Africa, even in some cases Western Europe. Manufacturing costs are higher admittedly, but this is more than made up for by the increased responsiveness in the supply chain. These retailers have the ability to manufacture additional quantity to meet demand or to manufacture less initially in order to minimize overage and markdowns. US retailers are likely to follow this trend in the near term, shifting a proportion of their manufacturing contracts closer to home in Latin or South America. Implementing structural change to overcome operational constraints can be an expensive and high-risk process, so retailers are understandably keen to be sure that any decision they make is the right one.

Overcoming Complexity

Q from Quantum Retail presents retailers with a unique way to overcome the seemingly insurmountable complexity of factors affecting decision making in their fulfillment processes.



By using advanced algorithms to understand trends from historical sales, Q has the ability to drive initial buying decisions through visibility to product lifecycle projections right down to the individual store and SKU.

Furthermore, Q has detailed and frequently updated views on seasonality that help to drive corrective behavior and cater to localized inventory requirements. It also updates expectations of product location lifecycle sales continuously once the product has started selling.

The system creates a plan of what it expects to do with the inventory that will be available throughout the selling life of the product. Uniquely, Q then continues to change and update that plan as lifecycle expectations change, adjusting target inventories and prioritization between different store requirements. This dynamic re-planning continues in an automated way until such time as a firm decision needs to be made, when it is shared with users for review, approval if necessary, and execution.

To effectively minimize the need for human intervention and control, Q works in an automated way where possible and on an exception basis when required. This means that users are directed to those areas where performance differs greatly from expectations where they can learn and possibly add value to the decision making process. Where there is little or no change, there is no involvement needed.

The Unfair Advantage

Using such a truly dynamic and self-learning system allows fashion retailers to make better utilization of limited available inventory to achieve higher full price sales capture and reduce the need for markdowns to shift excess stock towards the end of the lifecycle. Better sell through equals more revenue and margin.

Even more powerfully, Q can identify early on products that are selling too fast, in which case a decision can be made to bring in replacement product early or reduce the stores that are carrying the product to those that can most profitably sell it at full price. It can likewise identify a product that is selling too slow, in which case the retailer can try a price drop or extend the number of stores that are carrying the product to share the pain.

By reducing the complexity of the decision-making process, Q also reduces workload for allocators. There is no need set initial stocking levels and no need to create pre-allocations. All inventory transactions are recommended by Q and a user can check or modify before execution. Management is by exception and workflow.



Q is uniquely able to ensure retailers are executing to their merchandise and financial goals. It enables them to get the inventory in the places where it is best placed to support these objectives and ensure that they do not make decisions that seem good now, but will be sub-optimal over the life-cycle of the product.

This new approach is able, like no other before it, to identify and support the winners whilst diverting resources from the losers that suck the profit from the business. A typical retail clothing business will lose about 15% of its turnover in markdown and perhaps 10% due to lost sales. If we assume a turnover of \$300 million, then we are looking at a loss of \$75 million. Reducing each of these figures by only 1%, adds \$8 million to the bottom line. Being able to make that sort of difference to a business is worth a lot more than a second look.

About the Author, Chris Allan

Working exclusively in the retail industry for the past 12 years has allowed Chris to work with a wide variety of leading retailers around the world. Cumulative learning from some of the world's best apparel, hardlines, grocery and convenience retailers, has helped Chris define and shape the next generation of retail software solutions. At Quantum Retail Chris is responsible for product strategy and innovation with a combination of art and science.

Prior to Retek, Chris held a variety of senior leadership positions in retail technology strategy, software development, and technology implementation at Accenture. His experiences have covered most of the key areas of retail management, including: forecasting, replenishment, decision support, store systems, product design and product life-cycle management. Chris holds a Masters degree in Engineering, Economics and Management from the University of Oxford.

About Quantum Retail Technology, Inc.

Quantum Retail Technology, Inc. is a leading provider of software solutions that enable demand driven supply networks. Quantum's flagship solution, Q, helps retailers continually achieve the merchandise and financial goal for every item in every location. By leveraging item assortment strategies and goals, Q links the art of merchandising with the science of inventory fulfillment. Quantum Retail solutions allow retailers to optimize inventory availability and supply network performance with low risk and high ROI.



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