Strategic change at bata pakistan

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Introduction

In August 2003, Doug Hearns, MD Bata Pakistan, was considering the efforts necessary to realign Bata Pakistan's manufacturing outsourcing, distribution, and brand strategy in the light of increased local competition and Chinese imports. Traditionally Bata had catered to the lower middle and middle class market. In 2001, however, Bata decided that instead of competing at the lower end of the Pakistani market, it would concentrate on the higher end, through new fashion brands such as Marie Claire and licensing global brands such as Slazenger and Hush Puppies. This decision entailed increasing manufacturing outsourcing from 17% to 70%; and building up a premium retail network, including mega stores, and most importantly building up a new cadre of management capable of leading Bata in the twenty-first century.

Doug realized that in the rapidly changing Pakistan shoe industry, key players such as Servis, Shafi and Firhaj and business Chinese exporters would all be realigning their business strategies to compete effectively with each other and possible new entrants. Thus, to him it appeared that (paraphrasing Shakespeare), Bata was approaching a tide in the affairs of its business, which if taken at the flood would lead to fortune, but if omitted might leave Bata in the shallows of the industry.

Company Background

The Bata Shoe Organization was originally established by Thomas Bata in 1894 in Czechoslovakia. During a visit to Michigan, he observed the use of assembly lines to mass-produce automobiles at the Ford Motor Company. He saw how all the components were made at different departments and assembled at one place. He took this idea back and started Bata on the same lines, and in doing so revolutionized an age-old industry characterized by individual cobblers who made a complete shoe, to teams of workers who assembled shoes using a conveyor belt. In 2002, Bata, with headquarters now in Canada, was the largest footwear manufacturing and marketing organization in the world, having sold over 14 billion pairs of shoes over the previous century. The company had a network of 75 shoe factories and tanneries in 95 countries, 6, 300 company-owned retail stores, 10, 000 franchised outlets and another 40, 000 independent dealers. Bata Pakistan reported to Bata International Group (BIG) East headquartered in Singapore.

In the early 1940s there were hardly any tanneries capable of producing consistent, quality finished leather. So the company had established tanning operations within the Batapur factory. Doug Hearns, Bata's MD, commented that setting up tanneries was consistent with Bata’s policy in that, “ wherever we went globally, we were fully integrated to feed our distribution”.

Throughout the six decades since its establishment in 1942, Bata remained the country’s largest manufacturer of shoes, with a share of 11% of the 150 million pair shoe market. In 2002 Bata had two plants, 3, 322 employees, sales turnover of Rs. 2. 3 billion, and profits before taxes of Rs. 79 million. Bata produced 14 million pairs and procured another 3 million from outside suppliers. Bata’s closest competitor was Servis with domestic sales of 5 million pairs.

Bata had established a plant to make rubber tires and bicycle tubes as part of the Batapur factory in 1951. In 1987 Bata decided to discontinue production of tires and tubes, due to continued losses over the last several years.

Manufacturing

Footwear manufactured by Bata could be grouped into six broad categories, based primarily on the nature of manufacturing technology and material used. The production technologies varied from processes like ‘ lasted stuck-on sole’ which involved labour intensive stitching, to the complex, capital intensive ‘ direct injection’ process for producing joggers.

In 2002 Bata carried about 1, 500 Stock Keeping Units (SKU) at any one time, of which two-thirds (representing 17 per cent of total pairs sold) were procured from outside vendors, known as Associated Business Units (ABU).

Doug Hearns commented on the factors that had resulted in increased outsourcing:

The media revolution in the 1990s resulted in increased awareness of global brands and demand for greater variety. We responded by increasing the number of SKUs from 400 to 2, 200. Production costs started increasing, productivity went down, and defects went up, because every time there was a variation in product design, we had to go through a new learning curve. As a result, we started outsourcing both complete shoes and stitched uppers. In 1998 the biggest decision we took was to bring down the number of SKUs from 2, 200 to 1, 000. In 1997 the government introduced a 15 per cent sales tax which practically applied only to the formal sector. Our profits plummeted, and we decided that we could not compete with the non-tax paying cottage industry and so we had to come out of the lower end of the market.

The decision regarding whether a particular product line would be outsourced was based on several considerations. SKU’s involving specialized equipment, higher volumes, and stable demand were sourced in-house, with a 12-month planning cycle, compared to a 6- month planning cycle for outside orders.

According to an executive in the production department:

We prefer to produce women’s shoes in-house. However, we prefer to outsource complicated and trendy fashionable shoes because of the small volumes involved: small volumes just increase costs. Similarly, we prefer to produce children’s shoes, particularly our popular line of Bubble Gummers, in- house except for small volume lines. But even for many of the shoes we produce in-house, we may procure the complete stitched upper. Thus Bata imports stitched uppers for joggers and school shoes from China. If we were to outsource, the labor would be free, and the machines would not be utilized to their full capacity. Once someone is employed at Bata, he or she is here forever. We don’t fire people just because business is not doing well or they are causing extra overheads.

Commenting on future manufacturing strategies at Bata, Doug remarked:

The future is no longer in traditional labor-intensive manufacturing. We will continue to do specialized manufacturing in-house but gradually increase the level of outsourcing to cater for up to 70 per cent of our sales. We will focus on new Air Molding Injection Machine technologies. Traditional manufacturing requires 27 persons per conveyer, while the newer technologies only require two people.

Retail Distribution

Bata marketed shoes through three main distribution channels: retail, wholesale, and government and export. In 2002 the retail department operated through 256 company- owned stores, 25 K-scheme stores and 91 agencies. A company-owned store was owned, managed and run by company employees. Typically, shoes sold through retail outlets carried a 42% gross margin. Expenses averaged 28% of sales and included fixed salaries, commissions, utilities and rent. Store managers received about 20% of their pay as fixed salary and 80% in commission.

An agency was similar to a company-owned store in that it carried only Bata brands. Bata provided shoe racks and some other furnishings. In addition, Bata owned the inventory in the store. However, the agency (franchisee) was responsible for all operating expenses. Bata paid the agency a 14% to 16% commission on each pair of shoe sold. Additional expenses averaged 12%, which included the cost of insurance and other commissions. Finally there were K-scheme stores, which were started in 1994. The concept was that of a leased store, whereby the inventory and utilities plus rent were the responsibility of the company. However, store managers and salesmen were ex-Bata employees and received commissions rather than salaries.

In 2002 Bata employed 900 retail sales employees and another 600 indirect retail sales employees. During 1999-2002 Bata increased the number of company-owned stores from 160 to 256, while the numbers of agencies were decreased from 100 to 91, and K-scheme decreased from 60 to 25.

For purposes of merchandising and setting sales targets, Bata divided retail outlets into four major categories: A, B, C, and D type stores. Category A stores catered to a higher class of customers who preferred premium shoes.

Category B stores catered to middle and upper-middle class customers, while category C stores catered to low and lower-middle classes. Category C stores did not carry premium brands, and stocked larger quantities of rubber slippers and PVC slippers. Table A shows a comparison of each store category.

Marketing and Merchandising

The marketing functions at Bata reported to the Commercial Director. The merchandising department acted as a liaison between the sales departments, factory production, purchasing and advertising departments. Other major departments included wholesale and retail sales departments.

The merchandising manager acted both as a merchandiser and brand manager. The department had three brand managers, one each for Hush Puppies, sports shoes (Slazenger, Power), and women's shoes (Marie Claire), and also four merchandising officers, one each for other shoe categories such as men's formal shoes, children's shoes, PVC, and Sandak. Another position being considered was for non-footwear items such as clothing.

New lines of premium products (SKUs) were launched through category A stores, while economy products were launched through category C stores and then later through B stores. SKUs which were to be discontinued after having remained in retail stores for a few seasons would then are pushed through the wholesale department.

We had expanded from 4 brands in the early eighties to 40, and now we are coming back to 5 global brands, i. e., Bata, Marie Claire, Power, Bubble Gummers and Weinbrenner, in addition to our local brands such as Sandak and Hawaii. We have decided to discontinue several brands including Emozioni in women's fashion, King Street in men's, and North Star in joggers. In the future we will go for global brands, using BIG (Bata International Group). These could include Barbie a fashion shoe for young girls, Hush Puppies for men, and Dr Scholl's for women.

Human Resource Management

Bata's Managing Director (MD) was typically appointed by Bata headquarters in Canada. Doug Hearns was the fifth MD since 1981, following Paul Kos (1981-84), Raymond Gasser (1984-90), Derek Barton (1990-97), and George Stricker (1997-2001). Commenting on the impact of a new MD on the organization, a manager who had served in the company for several decades commented:

Every new MD brings in his own management style and area of focus. For instance, one MD had a strong interest and experience in operations, and focused on improving production processes and introducing new lines and designs. The current MD is particularly strong in marketing. We are consolidating our brands and focusing on building our brand equity. It is good to have changes every 4-5 years. Pakistan is one of Bata's bigger operations, and the MD is selected carefully. Each MD brings rich experience and global best practice, and sets new goals and targets. However, all this comes at a cost. The continuity of leadership is broken, unlike Servis for instance, where the company may have been functioning under the same top executives for several decades.

Bata traditionally had encouraged the retention of loyal employees, with the result that most personnel remained at Bata until retirement; most senior managers had served for over 20 years. Bata provided a wide range of employee benefits including an extensive housing colony in Batapur, a provident fund to which both the employee and the company contributed 7 per cent of salary, a gratuity scheme, an annual bonus, subsidized canteen facilities and children's scholarship programme. Since the early 1990s Bata had gradually allowed the number of employees to decrease, through a process of natural attrition as employees retired. Between 1990 and 2002, the number of employees in the Batapur plant had decreased by 30 per cent while the number in the Maraka factory had increased by 32 per cent, resulting in an overall decrease of 25 per cent.

Doug commented on the need to continuously develop new managers:

It used to be that the average age in our merchandising department was 50. Now it is 30. We want to develop a new cadre of managers, particularly in merchandising. We need to groom dynamic young individuals who are goal-oriented, self-starters for senior general manager positions in 5 to 10 years and who are ready to take on international assignments in 7 to 12 years.

How Bata translated its new vision?

As mentioned in earlier section, new MD wants to realign Bata Pakistan. New management had some objectives in mind while critically analyzing the whole market scenario. Bata Pakistan intended to achieve these objectives:

To minimize its cost

To become more customers centric

To be more responsive towards changing consumer behaviors

To increase turnover

To maintain its market share

However, there was a big question mark that how these objectives are to be accomplished; for the sake of this, new management decided to put more emphasize on its manufacturing process and went for cost cutting from its manufacturing operations. For this purpose they took decision to outsource its manufacturing processes. Followings are some crucial reasons for which they chosen this strategy:

Bata Pakistan wants to cater entire market of Pakistan for its products. Since Pakistan is characterized by having low income level so through increase in outsourcing, low cost of production will lead to affordable prices.

Currently Bata's cost of sales are 66% of its net sales. This reduces the profit margin for the company (Exhibit – 1).

Bata has been facing a stiff competition from Servis, Shafi group, and Firhaj group.

China is the continuous threat for Bata because it provides low cost shoes and has emerged as the largest player in the global shoe industry.

Hence, Bata benchmarked a world famous brand Nike for its outsourcing facilities in various regions of all around the world. The outsourcing of Nike resulted in lowest cost of production for the company and ultimate growth in its profits. The key success factor of the Nike is the ' reduction in cost of production through outsourcing' (Exhibit – 2). Therefore Bata Pakistan needed to be like Nike and therefore MD and his team decided to run Bata on a strategic track.

MD took the charge of this effort and engaged two directors and one personnel from its Marketing, Production and Procurement departments. They realized the core stakeholders of these change process which are People of the organization. It was not an easy task because there could be substantial resistance from the employees particularly related to production and manufacturing because the processes were going to out of their hands. Therefore, MD prioritized the things and then implemented step by step. For instance, he asked his coalition partners to communicate the benefits of this change and assure the good performer employees that they will not lose their jobs because these are prestige of Bata. Employees were also communicated that there were some alternative jobs available within the Bata. Company redesigned the reward system and created more jobs in shape of increasing the number of its owned retail stores which are run by company's employees.

An other interesting move made by MD that they did not outsourced their manufacturing once at a whole, rather first of all they outsourced their small volume lines like fashion oriented shoes in order to ascertain cost and benefit analysis. Team also decided to revolve its technology for in-house production processes and brought a new shoe manufacturing plant " Air Molding Injection Machine". This equipment was required to use in in-house production.

There were some reforms in structure of company as well, like senior employees were given retirement, golden shake-hands and new cadre of young employees were hired for streaming up the processes of Bata and work according to objectives set by the management. The new structure of the Bata is given in (Exhibit – 3).

By the end of year 2005, company outsourced its 50% of manufacturing lines, later on by the end of next one and half year they completed 70% outsourcing of manufacturing lines and gained great success towards accomplishment of goals as designed. Bata Pakistan Ltd. has been able to grow revenues from Rs. 5. 1billion to Rs. 6. 4 billion. Most impressively, the company has been able to reduce the percentage of sales devoted to income tax expense from 3. 65% to 3. 54%. This was a driver that led to a bottom line growth from Rs. 477. 8 million to Rs. 585. 5 million. The implications are advent from the financial highlights which given in (Exhibit – 4).

Bata in current age

During the last year Bata produced over 17. 2 million pairs and sold 16. 9 out of them with the help of their large distribution network of 400 Retail Stores and Agencies, 13 Wholesale Depots, 23 Distributors and about 400 Registered Wholesale Dealers who are selling goods as independent retailers. In 2009 the company generated turnover of Rs. 6. 5, billon showed an increase of 26% against previous year. The Company has an organized Export Department which is constantly engaged in exploring new export markets in order to earn the foreign exchange for the country. During the current year i. e. 2010, it is expected to export 1 million pairs of various styles of footwear to European and African countries. It has transferred sophisticated technology and business skills to the country and provides direct and indirect employment to about 10, 000 people. Bata also supports a large number of local manufacturers by buying raw materials from them.

The company has not only maintained a reputation of manufacturing high quality footwear for all the socioeconomic segments of the society but has also been designing shoes in accordance with the changing fashions and trends. The list of brands of Bata and size chart is given in Exhibit – 5 and Exhibit – 6 respectively.

Conclusion

Strategic change implementation is not an easy task at all but in this company it happened and results are in front of us. Bata is still market leader of footwear in Pakistan catering the needs of its customers and providing quality footwear.