Zara: expanding overseas | swot, porter's five and pest

Zara is one of the most well known brands in the world and is also one of the largest international fashion companies. They are the third largest brand in the garment industry and are a unit of Inditex. It their flagship range of chain stores and are headquartered in Spain. Zara opened its first outlet in Spain in 1975. The headquarters of the company is based in Galicia. There are more than 2600 stores across 73 countries in the world. The Zara clothing line accounts for a huge bulk of its parent group’s revenues. There are other clothing brands owned by Inditex such as Kiddy´s Class (children’s fashion), Pull and Bear (youth casual clothes), Massimo Dutti (quality and conventional fashion), Bershka (avant-garde clothing), Stradivarius (trendy garments for young woman), Oysho (undergarment chain) and Zara Home (household textiles). Inditex owns all Zara outlets except for places where they are not allowed ownership of stores (that’s where Franchises step in).

Zara is renowned for coming up with products on a short timescale instead of taking forever. They are known for taking around 2 weeks to develop products and have been known to come up with around 10, 000 new designs every year (which is an industry record). They have bucked the trend by making productions in Europe instead of shifting their entire production to Third World or Developing countries. However some of their clothes are manufactured in parts of Asia due to the fact that they have a longer shelf life. They make most of their own products inside Spain or other European Countries as they own a large number of factories in both Spain and Portugal. They also don’t have to depend on anyone else as they can get everything done by themselves.

Zara is unique in the way that it does not spend money on marketing and instead concentrates on opening new stores instead. Their brave experiments have led them to be labeled as one of the most innovative retailers in the world.

Zara started out with low priced products which were pale imitations of high end fashion products. This move led to Zara being a smashing success and allowed them to expand by opening more stores in Spain. The company management also managed to reduce the time it took to create new designs and came up with the term " instant fashions" which allowed them to capitalize on new trends really fast. Zara is known to use teams of designers instead of individuals.

Zara has to face a lot of competition from H&M, Gap and Bentton internationally. Fortunately Zara is considered to be more fashionable than the rest of the brands despite the fact that its price is less than Benetton and Gap. H&M is still cheaper than Zara but is equally fashionable as Zara. Gap and Benetton are less fashionable and more pricy.

SWOT Analysis

(S)trengths

Zara's biggest strength is the fact that it provides cost leadership strategy by aiming at efficiency and cost reduction on products. There is a lot of efficiency merely due to the fact that products are put on fast track and costs are kept really low. They don't take a long time to come up with new collections. Zara is able to come up with collections really fast (around 2 weeks to get a collection ready).

Zara focuses on what its customers want and that’s why they have managed to do so well. They are able to get the opinions of its customers on a daily basis. The data is sent over to the headquarters where it is analyzed. This is a great way of saving time and helps them understand what sort of trends to follow. Since it does not take them a long time to come up with products they are able to cash in on the trends. They are also able to design, manufacture and send out the new products in less than 2 weeks. They are also very efficient when it comes to delivery of the products.

Zara employs a huge team of designers who are able to design the clothes they require. Most of these designers are fresh out of Fashion schools and are able to do more for less. Most of the clothes manufactured are made in Spain and there is no need for outsourcing. Zara manufactures and distributes its clothes so it manages to cut out the middle man. This is one reason why they are able to get clothes out there so fast. They also have a great Information technology solution in place which allows for decentralized decision making.

(W)eaknesses

Zara does not spend any money on marketing or advertising. This is a huge weakness for them as its competitors spend a lot of money on advertising. Zara relies on goodwill and word of mouth so that people can shop at their stores. This is a weakness which can be exploited in the future by its competitors.

Another weakness is the fact that Zara only has one manufacturing and distribution centre in the world. This is a double edged sword as it is both a weakness and strength. The fact that they have a huge distribution centre makes it an asset but then if it is hit by some sort of natural disaster or some logistical problem then it can have an adverse effect on its revenues.

(O)pportunities

There are a lot of opportunities for Zara lying ahead. They need to expand their presence in the USA where they face competition from the likes of GAP. They only have around 49 stores in the US which is not bad but then based on the size of the US that is equivalent to around one store per state. In comparison there are more than 300 stores in Spain which is a fraction of the size of the US. They may have conquered Europe but they still need to expand into the US market so they can give Gap a run for its money. They can grow properly if they expand their presence in the US.

Zara is only going for markets where it is doing well such as Italy. However there is a huge opportunity for them to tap into the Indian market. The Indian Economy is doing really well and people over there love to buy good quality brand names at a reasonable price. Zara already has 2 outlets in India but then it wouldn’t hurt to expand a bit more and form alliances with local manufacturers. This will make it easier for them to slowly grow within the Indian market.

(T)hreats

The biggest threat facing Zara is the fact that it is Europe Based. Zara is based in Spain and has a huge number of stores in Europe. Critics believe that there is an over saturation of stores in Europe and that having such a huge number of stores will dent the revenues over the longer term. The other reason is the fact that the Euro tends to be stronger than the Dollar. This is one reason why merchandise from Zara tends to be more expensive in other countries. This can be a big turn off and can have an adverse effect on their revenues in the longer term.

Porter's Five Forces

Porters Five Forces allows us to look at the five forces which help us determine the competitive intensity and the attractiveness of a market. Some of these forces are related to competition from external sources while the rest are internal threats. These are basically all related to the macro environment. The various Forces are threat of substitute products, the threat of established rivals, the threat of new entrants, the bargaining power of suppliers and the bargaining power of customers.

Porter's Five Forces Analysis

Threat of Competitors

Zara faces a lot of competition in the market. There are a large number of competitors in the market such as H&M, Benetton, Gap, etc. Fortunately The high level of competition makes it tough for everyone as they are all struggling to get a piece of the pie . The biggest problem is that due to the large number of competitors the growth rate is low due to the number of manufacturers around. The clothing industry has peaked and it is very difficult for people to stay in the industry as the competition is cut throat. Customers are spoiled for choice due to the number of brands within the market. They are also very fickle minded and base their buying habits on the basis of new trends. They will only buy based on price and brand recognition and this is why the manufacturers have to keep changing what they do and come up with new ways of gaining customers. The costs of manufacturing new goods are quite high plus it is not easy to procure raw material so that's why the ones who have the resources and the ability to do so are able to survive within the market.

Threat of New Entrants

There is always the threat of new entrants but then the risk is not so much as Zara already has a huge presence in most parts of the world. The barriers for entry for distribution are quite low in Spain (where the bulk of their clothes come from.) New entrants will have it easy as the cost of distribution is quite low as they only need to rent a shop and need a bit of capital to start out. However when it comes to manufacturing then the barriers of entry are really high mainly due to the fact that it requires a huge investment to get started within the market.

Substitutes

There is no threat of substitutes as it is a basic necessity for everyone.

Customer's Bargaining Power

Customers have varying levels of bargaining power as they can decide what they want. Customers are quite fickle when it comes to buying clothes. However the good thing is that each customer has a love purchase volume and that means that even if some tend to change their brand there will still be some who will buy Zara. It is not an item like a burger or a snack which is available easily anywhere for a low price. The good thing about the clothing business is that there is no risk nonpayment because customers pay for clothes during purchase.

Supplier Negotiation Power

There are too many suppliers in the market which is one reason why the suppliers don’t have much negotiating power. The fact that Zara procures or makes most of the stuff itself is also another factor which doesn’t work in the suppliers favor. If the supplier decides to cut down the supplies the manufacturer can easily go to another manufacturer.

PEST Analysis

The PEST analysis is a study of the environment before a company begins its marketing process. It is a study of the external macro environment. It stands for “ Political, Economic, Social, and Technological analysis” and is an environmental scanning component of strategic management

- (P)olitical –The political factors affecting Zara are when the government intervenes into the economy and comes up with laws which change the way things are done in the country. The government can easily change its policy and change the ways a business can operate in the country. They can change the laws and do drastic things like changing the interest rate. Zara needs to know the entire system and to be prepared for any potential problems it can face from the government due to a change in policies.
- (E)conomical –Economic factors come into play as they are related to factors such as interest rates, taxation changes, economic growth, inflation and exchange rates. These have the potential to create many problems in the future. There are different duties and levels of tariffs in different countries and this can cause the prices of products to vary in

different countries. The price of goods will also vary based on the country of origin and that’s what Zara needs to keep in mind.

- (S)ocial –If there are Changes in social trends it will have a huge impact on the demand for Zara’s products and the availability and willingness of individuals to work. However that is not likely to happen as it’s not as if Zara makes niche products. They focus on a huge market and make different types of products so it is quite unlikely that there will be a social shift in this part. However the company still needs to work on trends and to make sure it’s updated with the times so that it can satisfy its customers and meet the demands of its demographics.
- (T)echnology –Due to advances in technology companies have to make sure that they keep up. Zara has to make sure that they have the latest technology and that they are innovative in every way. The more advanced the technology the more it can bring about some quality. Zara has invested in technology and it has to keep improvising because if they don’t then their competitors will get a head start on them.

Part 2:

Zara is the biggest contributor towards Inditex’s profits. It’s the most well known brand in the group and has played a huge role in the growth of the group as well as bringing about huge sales and profits. Zara’s success has brought about a large number of case studies and reports. It has consolidated its position in the fashion industry and has made a good name for itself.

Zara’s business model is basically based on the principle that it can sell “ medium quality fashion clothing at affordable prices”. Basically vertical integration and the ability to come up with a quick-response is a key factor to Zara’s successful business model otherwise they would be no where without it. The process for Zara has been designed in such a way that it has the various functions within the business system such as designing, sourcing and manufacturing, distribution and retailing. They do all of these themselves and that is one reason why their growth is at a good rate. However what goes up must come down and Zara is not immune to the problems in the world. The way they operate can also prove to be their undoing due to the model they are currently utilizing. The fact that they have their own distribution centre and manufacturing unit is a very weak point. This can be discussed further in this document.

The management at Zara have come up four fundamental success factors: short cycle time for creation of product, small quantity per product (and not too much of the same stock) , extensive variety of product every season (so that users can choose easily) as well as a huge investment in information and communication technology to allow them to stay on track .

Zara knows what its customers want by tracking their preferences on a year round basis. They have their own team of designers who have been recruited fresh out of fashion school. It is not a tough job to tell them what they want based on the input they receive. They make around a limited quantity of clothes based on the 11000 various items designed by its in-house staff. Zara does not make any losses as they only order a limited quantity of each item which they believe is stylish and will be more restricted season wise.

For example if they have miniskirts in design they will only be available for a short time due to the short summer period in Europe. Other clothes which can work the year around and for which the trend does not change are outsourced to Asia as the cost won’t be so high. The outsourcing operation is very handy mainly because these clothes have a longer shelf life. It does not take a long time for the clothes to be prepared as it merely takes around 4 weeks total for the whole process : from design to the finished product in the stores.

The fact that Zara knows what sort of trends are there in the market and are quick enough to change their strategy to match the trends in the fashion industry gives them a huge advantage. They are able to modify their timetable easily to adjust for a change in the trends in the market. Normally it takes around 8 to 12 months for any normal retailer to forecast trends and come up with a style and send it for production. They are unable to match what Zara does and they end up losing big time. Even if a style fails to sell much, Zara can easily sell the clothes on a discount. The fact that they quantity of clothes manufactured was so low that they lose much. Their low volume strategy has helped them have a very low number of discount sales every year as compared to a high rate for the rest of the industry.

However this leads to higher costs which is a disadvantage but then they don’t have to worry about having higher inventories. This method allows for a low inventory and high profit margins. They don’t save any money here with costs but then they get the maximum out of their clothing line. A problem they face is the fact that since Zara controls everything it is not easy for them to expand or relocate as they have to stay put in one place or the whole operation will suffer and the goods will cost more to distribute.

Zara’s business model is wonderful in the sense that it has a very fashion forward line as they know which trends to cash in on. They seem to have the midas touch of turning everything into gold. Their policy is to have a mostly young and fashion conscious staff so that they will also be able to double as trend setters. If for instance a certain item in a store sells well then the management decides to sell the same item in other locations as well. The key is that most of the items are in short supply and people presume that there is a shortage of items which ends up making consumers want to buy more.

A key factor in Zara’s success is the fact that it has sourced its products from the right places. They have based their procurement offices in a couple of fashionable cities in the world. This allows them to witness the trends first hand and then to quickly come up with a solution of their own. They don’t buy all the raw products on their own as they use one of their parent group’s procurement units to do all it’s purchasing. One clever move on their part is that they buy most of their fabric in grey so that there is greater flexibility. It doesn’t take long for the fabric to be prepared.

The main distribution artery is in Spain where they have their biggest distribution centre. They also have some smaller distribution centers in countries such as Argentina, Brazil and Mexico. The problem with the distribution centre is that it is purely based in Spain and does not have the capacity for a heavy load. It is a huge distribution centre and occupies around 500, 000 square feet in total. They only have the capability of processing around 60, 000 folded garments in an hour. They need to find a new distribution centre or increase their operations so that they can save more time. However the biggest advantage for them is the fact that they have vertical integration which allows them to manufacture and distribute their own stuff without having to be at the mercy of any supplier. It is not tough to move any of their products as they have their own railway network which allows them to move goods easily to its distribution centre. Once the goods are ready they are shipped out immediately though the shipping schedule is only twice a week. European stores get their goods early (around 24-36 hours) while other destinations get them within 2 days. This system has allowed them to achieve a very high level of accuracy in its shipments. The other good thing is that the outlets don't take long to display the new outfits once they reach their destination and this allows them to show new stock to their customers. The clothes are also coded according to their color so that the staff knows where to place them. This makes it easier for the customers to go around color matching the items they want to buy.

Problems with Zara

Zara is facing a large number of issues which can cause them a number of problems in the future. Despite the fact that Zara has a consistent business system which gives them a competitive advantage it is always in the danger of tanking badly. Zara's biggest advantage is the fact that its economies of scale are really good and that they have been able to ramp up their distribution system. The continued growth is good for them in every way. They have been helped a lot by their expansion in the international market.

However their growth in the international market will be curtailed due to the reason that Zara has a very centralized logistics model. It is understandable that Zara has to expand its distribution centers and to increase its capacity. Zara has its main distribution centre in Spain and it won't be easy going trying to expand when their base is only in Spain.

This will affect their plans to go international and to target more regions. They can't simply survive with a European presence alone. It is true that they do have a presence in other countries but then it is not as much as it should be. They have a huge presence in Spain but quite limited when it comes to other countries. They can easily target the North American region where they don't have much of a presence compared to the huge size of the region. The problem is that there are a lot of outlets there and a lot of competition coupled with the need for plus sized clothing, high cost of operations and a very mature market. Zara needs to come up with a strategy so they can compete very aggressively over there. They can also target South America but the problem is that it is not a very stable region and any geopolitical problems can lead to profits being low. A good market would be the ever reliable Middle East where Zara already has a small presence. However with talks of revolution in the air and other geo political problems it can be a risky bet. There are a few countries in the region which will lead it to be profitable but then the market is small compared to other regions. They can easily opt for countries such as the South East Asian markets and South Asia which have a lot of potential.

Recommendations

Zara can easily go around and expand its operations in many ways. The best thing would be to take it easy for the short term and to go for further expansion in Europe. Spain and Italy are neighbors and the fact that Zara has its main distribution centre in Spain will make it easy for Zara. For the time being they don't need to open any more distribution centers as they can work with regions which are quite near in proximity to them. Italy is one of the most fashion savy countries in Europe along with France. Zara already has 70 plus stores in the country but then they can do a lot better. They can enhance their presence in the market and try and take some share from some of its know rivals such as Benetton and H&M. the biggest way for Zara to expand is to try and open another Distribution Centre in Eastern Europe and to be able to expand its operations in Eastern Europe. A number of countries are coming into the European Union and are ripe for the picking. They already have a presence in some countries but the number of stores per region is not as much as it should be.

Zara should expand further in the Asian markets once they have been able to do their bit in Europe. They have already tested the waters in Asia despite the fact that there is a lot of competition from local vendors there. However the fact that people in the developing countries and with surging economies will be sure to try out Foreign brands and that would be one reason why it's a good idea to expand further in Asia. The only problem is that Zara is based in Spain and that all their designs come from that region. The fact that they make items in limited quantities ensuring a low inventory will scuttle their plans to expand easily. If Zara decentralizes its manufacturing policy it can easily set up its own operations and distribution centre in Asia. It won’t be easy as they will still have to procure items via local vendors. If they are unable to create a distribution centre in Asia they can still create a larger upscale distribution centre in Spain where they are able to take the load of supplying to a larger number of stores. In this way they will be able to keep up with the demand and supply. This will help in the growth of the company and allow them to face challenges.

It wouldn’t be a bad idea to expand in the US market in the long term even if it is not so friendly towards European labels. Competitors such as Benetton and H&M have faced problems with the US market in the past. However Zara has the resources and the ability to be able to expand within the market.

They can expand easily in the US market only if they manage to curb their costs which are quite high at the moment. They also need to invest in a proper high end IT system which can help them go with the trends. They will not have the advantage of the system they have in Spain as it’s a totally different ball game over there. There will be different political and economic circumstances which will dictate the way they do everything. It won’t be easy to change their entire business model just for another region. This would mean that they have to decentralize the way they work so that they can work in the US. They would have to establish a distribution centre in Mexico or another cheaper place so that they can cater to the needs. The cost of labor won’t be so much but the fact that it is decentralized and not under the control of the Spanish HQ. On the bright side it will be cheaper to ship products and the tariffs will be low.

This will allow them to save a lot on costs and they will be able to keep their prices the same way they are in the origin countries. They will also be able to enjoy greater margins in this way. They will also be able to resolve other matters such as retailing overcapacity, less fashion-forwardness, need for larger sizes, and considerable internal variation.

Risks

The risks associated with expanding overseas are that it will require a lot of capital. They need to establish new facilities and it is not an easy task. They have to do a number of studies and research the market properly before they go ahead. It won’t be an easy feat setting up everything from scratch. They will also have to train people the way they operate in Spain. However they can still keep the design and procurement process centralized as technology will allow their units to do what they want. It’s just the units which need to be decentralized. There is the huge possibility that they will face a number of obstacles and losses before they can actually do something.

The only problem is that they will face problems with their margin while they are at it. They will have to face increased costs and will have to pass on the buck to consumers so that their bottom line is not affected. Hypothetically they can also opt for joint ventures or franchising if they don’t want to go and expand in the US. The only problem is that joint ventures and franchises don’t always pan out as required. It can create problems for their brand name and can cause many unforeseen problems in the future. It is never a good idea to give out a franchise or work in a joint venture unless there is synergy between the two partners.

Conclusion

In the end it is highly recommended that Zara keep its house and affairs in order before they can think of expansion. Due to the environmental factors and the fact that the Euro Zone will not always be so stable should shake it out of its comfort zone. Expansion is the key but they have to play their cards right and plan their move properly before they end up making some costly mistakes.