

The demand of an apparel market commerce essay

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The demand in the market in which apparel companies operate and compete can be described as highly uncertain and difficult to forecast. The lead times in this industry are usually long, because the new products are created very frequently due to the short life span, hence there is also a high variety of products. Therefore, the companies are facing a problem concerning the supply chain management: how to match the supply and the demand as precisely as possible? The answer lies in minimising the time between the demand and supply i. e. the effective management of their supply chains. This report will analyse the Spanish based company Zara, the company that has managed to establish a supply chain that is close to perfection as it can possibly be in the apparel industry. The practices of Zara can be applicable in any industry where the life cycle of the product is short, hence it is useful to look into more detail the practice of Zara up to 2002. The post-2002 period is characterised by the expansion of production sourcing to East, mainly China, the time where explicit information about Zara's suppliers becomes vague because the company wishes to keep the notion of in-house production while outsourcing. Therefore, a possible solution to this problem will be presented, followed by a conclusion.

Analysis and recommendations

Zara has created unique supply chain management which is adapted to particular environment of the apparel industry – it provides quick response and is extremely flexible in design, manufacturing and distribution network. However, as Ferdows et al. (2004) noted, Zara did not discover any revolutionary innovations, but a self-reinforcing system that is erected on three principles: Close the communication loop – the main goal of Zara is

quick and direct transfer of information from the end of the supply chain i. e. customers back to the operations at the beginning of the supply chain i. e. sales, procurement, distribution, planning, production. Stick to a rhythm across the entire chain - the emphasis is on intensifying the responsiveness and adhering to the rigid timetable. Leverage your capital assets to increase supply chain flexibility - vertical integration of the supply chain to increase flexibility and ensure prompt reactions. Zara's supply chain begins at the design centre, which consist of three halls, one for women's, one for men's and one for children's line, thus separate design, sales, procurement and planning staff is dedicated to each clothing line (Ferdows et al. 2004). The store specialists from every line are continuously communicating with store managers which are regularly providing feedback from the market thus ensuring fluid information flow and ensuring rapid response. This direct stream of information allows the elimination of further production of a particular product if it presents with low sales. Nevertheless, if the product is in demand, provided that the fabric is in stock, more units could be manufactured within one week. However, the production runs are limited and in small quantities. If the store specialist notices the saturation of the market with a specific garment, the production is ceased and the product is not replenished. This creates the notion of scarcity, and causes the consumers to visit the stores more regularly, which leads to more frequent purchases thus supply-demand mismatch is reduced because the demand is increased. More regular visits to the stores diminish the need for advertising (only 0.3% of Zara's costs are attributable to advertising, in comparison to industry average of 3-4%). Zara cannot take the advantage of the economies

of scale due to the fact that products are manufactured and distributed in small batches. Nevertheless, this approach has proved to benefit the company: there is a short window of opportunity for purchasing the items and the customers are aware of the fact that if they don't buy the garment at that moment, the possibility that it will be in stock the next time they visit the store is small and possibility that they will purchase it at a discounted price is even smaller. This increased demand reduces the need for markdowns of the garments at the end the season. In comparison to other companies in the same industry, Zara collects 85% the of the full ticket price, while other companies in the industry collect on average 60-70% (Ferdows et al. 2004). The need for the price reduction is lower due to less forecasting errors. The shorter lead times and flexible and tight vertically integrated supply chain are the factors that lead to more precise forecasting. Zara also reacts rather than predicts and that is the reason that Zara commits only 15-20% of the season's inventory six months in advance and only 50-60% at the beginning of that season so that the inventory can be altered if it is required. Zara designs all of its products, owns a distribution centre and almost all of its stores, and only outsources the products which carry less uncertainty (basics and knits) to bring potential supply-demand mismatch to a minimum. This method provides more control from the first to the last link in the supply chain. The control over the supply chain and short lead times enable a high rate of weekly deliveries which are uncommon for the apparel industry. Store managers place orders twice a week and receive shipments twice a week, while competitors receive their orders once in 12 weeks (Newsweek 2001). They order items from the collection, but final

allocations are made centrally taking into account new items, current demand and inventory. Distribution of all garments (both outsourced and in-house manufactured) is handled by a single distribution centre, which is strategically located in the centre among fourteen manufacturing plants in Spain. The products are either distributed by truck (Europe) or by air-freight (outside Europe). All the items are pre-priced and tagged, either hanged or packed in the boxes, ready to be displayed in the stores as soon as they are delivered. The frequency of the shipments leads to half empty trucks distributing products around Europe, however the efficiency is the main objective of the company. The shipments are 98.9% accurate, hence less control is needed at this stage (Ferdows et al. 2004). As a result of precise shipping timetable, the problem of waiting between steps in the supply chain was alleviated and it resulted in no inventory held centrally and almost no inventory held in the stores i. e. mitigating inventory risk. Unlike other companies in the same industry, Zara's supply chain is vertically integrated and it manufactures about half of the total products in-house. The company's managers realised that the investment in capital assets would result in flexibility, quick reactions to meet market demand, and in control over schedules and capacity (Ferdows et al. 2004). Inditex (Zara's parent company) owns a company which handles 40% of Zara's fabric procurement, several textile production companies and share in fabric finishing company. Simpler operations which require a lot of labour, such as sewing, was subcontracted to 400 smaller firms. Zara does not have to provide these firms with garment specifications in advance, but just reserves their time. Majority of Zara's factories operate on one shift, therefore the production of

a specific product can be increased or decreased rapidly depending on the demand (Ferdows et al. 2004). This approach allows the elimination of unsuccessful lines, preventing the accumulations of inventories and unnecessary markdowns (Newsweek 2001). Zara's distribution centre and factories have lower capacity utilisation rates during the most of the year which managers even encourage because this provides the company with the capability to quickly react to the market demand. The managers rely on queuing models, which state that "waiting time shoots up exponentially when capacity is tight and demand is variable" (Ferdows et al. 2004 p. 110). Zara's practices are counterintuitive. Albeit the fabric production and garment manufacture is less expensive when outsourced, about half of the items are made in-house. Three totally distinct lines are run which incurs excess labour costs. It produces and ships in small batches, hence not taking the advantage of economies of scale. It encourages not having enough inventory in stores, having ample capacity in both distribution centre and factories. It ships products on hangers twice a week by air-freight and truck, even though less frequent shipments, with higher capacity utilisation rate of trucks and air-planes (packing products in boxes) and shipping by train would reduce distribution costs. Nevertheless, this fast, fresh approach combined with rapid and frequent transfer of demand info from stores back to design centre and having excess capacity in their production is what makes Zara capable to respond quickly to demand changes and obtain high profits through end-to-end control of supply chain. All the excess costs are compensated for by reduction in markdowns and higher demand. This constant stream of information through Zara's supply chain, the reduced

lead times, more accurate short-term forecasting, orders in small batches are factors that prevent the occurrence of bullwhip effect - the phenomenon of small change in demand being amplified in orders placed upstream i. e. cause large variation. Zara also allows 40% to 50% adjustment of the orders since the beginning of the season (the industry average is up to 20%) therefore circumvents overproduction and markdowns of the garments (Ferdows et al. 2004). The apparel industry is a labour-intensive, so it does not come as a surprise that Zara announced in 2002 that the proportion of global sourcing would grow, to take advantage of lower production cost, especially in China. Inditex has established 3 companies in Hong Kong and signed an agreement with Hong Kong based garment supply agency. The aim was to establish a strategic position for purchasing of fabrics garments from the region and for intelligence gathering on fashion, which meant that garments would be designed in China, while the ideas for designs would come from the surrounding countries - Japan, South Korea, Malaysia etc. (hktdc. com 2001). That was the point when Zara began to move away from their in-house manufacture. This strategic decision was followed by a few minor setbacks which some were attributed to production expansion in Asia such as slower stock turnover over the years (International Herald Tribune, 2005 in Tokali, 2007). According to Tokali (2007) the exact information related to Zara's external suppliers is scarce, and in my opinion a bit secretive. The conclusion that can be drawn from this is that the company wishes to keep the impression of in-hose manufacture, while still exploiting the lower labour costs around the globe. The potential solution to Zara's problem could easily be solved by creating a replica of their in-house

manufacture in Asia, so it would still be " in-house" manufacture but in another Inditex owned house. The idea is to create a new design centre, distribution centre, subcontract smaller firms and to acquire the factories in Asia which would be able to satisfy the demand of the growing Asian market, while the European sector would satisfy the European market and the rest of the world. By doing this, the end-to-end control of both supply chains would be possible and the flow of information would be fluid. This strategy could potentially aid the total growth of the Inditex company, as the full capacity of the company would grow. As designs would be made both in Europe and in Asia, the initial collections would be the same, however it is safe to assume that the fashion preferences are not the same all over the world. The products in each " house" could be altered and additional styles could be added to meet the specifications of the customers in that part of the world, and vice versa. This would give even more flexibility to Zara and it would capture more customers.

Conclusion

The key to Zara's success is a unique approach to enhancing the entire chain not every link and that is the reason why counterintuitive practices are compensate for. The effectiveness and responsiveness of the chain is constantly increased by improving the communication, following the rigid schedule and by investing in the production assets. Zara's problem of trying to keep the climate of in-house manufacture, but take advantage of lower labour cost can be achieved by creating the sibling design, manufacturing centres in Asia and making another " house" thus possibly reaping higher profits.