

AUXIS™



Accelerating Speed to Market for Proprietary Retail Brands

Strategies for Capturing Market Share and Improving
Margins

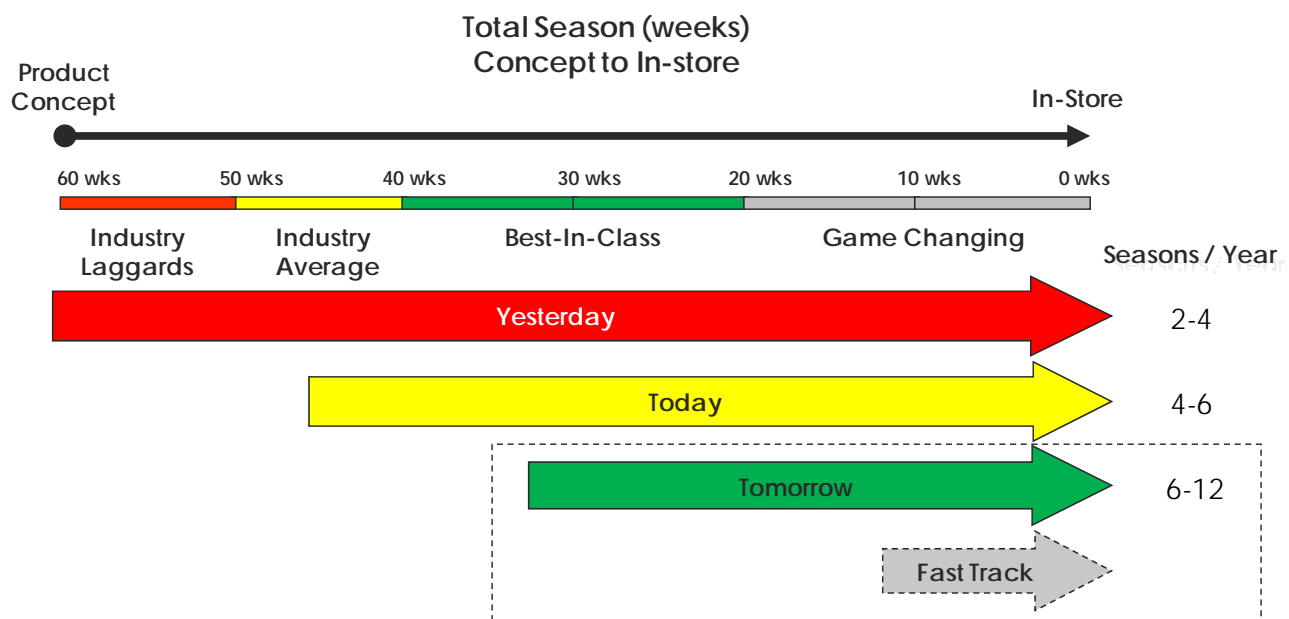
By: Jamie Mahoney and Marcos Corminas

Published: August 2009

Introduction

Leading global department stores and mass, discount and specialty retailers in the consumer products industry have been focusing in recent years in the reduction of cycle times for the development of their proprietary brand products. The typical development lead time of 50 to 60 weeks from “concept to in-store” for items such as furniture, home décor, footwear, kitchenware, apparel, luggage, bedding, etc. is no longer acceptable in a buying environment where consumers are becoming more fashionable and trend conscious. Products need to be designed, sampled, adopted, sourced/manufactured, shipped and available on the store shelves in reduced time to allow the design process to be as close as possible to the product launch date. This allows the incorporation of the latest trends in materials, themes, colors and concepts into the design process for increasing the newness and overall appeal of the product and for maximizing sales and profit margins.

In the last decade, leading global retailers have successfully decreased total product cycle times (concept to in-store) from 50-60 weeks to 20-40 weeks, with some “game changing companies” completing the entire process in 5-10 weeks (Fast Track process). This reduction in product development cycle times has allowed the incorporation of more seasons (or product launches) to refresh store assortments and incorporate “hot trends” into the new assortments. The benefits of reducing cycle times can be considerable, with industry estimates of 25-basis points in increase of profit margins for every week of cycle time reduction.



Faster development cycle times also provide significant benefits in inventory reduction, improved material procurement, optimization of design and sourcing resources, improved vendor relations and reduced logistics costs among many others, which in turn result in lower supply chain costs and improved overall product quality, performance and availability. In the end, the incorporation of supply chain processes focused on increasing “speed to market” support the development of the “right products, for the right consumer, at the right time and with the right cost”.

However, many mid size and small retailers still have not been able to reduce the cycle time of their proprietary brand products, and operate under long development cycle times of 50-60 weeks per season. A multitude of issues and suboptimal processes experienced throughout the supply chain in the areas of product development, sourcing/manufacturing and logistics cause product cycle times to be long and inefficient, resulting in the design and development of unappealing product lines and assortments, and reflecting in higher costs, lower quality and late delivery times. Some of the main issues experienced in each of the main supply chain functions are listed below.

1. Product Development

The product development process starts with the creation of conceptual designs envisioned by a product designer and guided by the merchandising team through specific product attributes to develop a desired product line and assortment. The conceptual designs for each item are reviewed by the merchants and, if approved, passed on to the technical design team for the development of detailed technical specifications with manufacturing requirements, such as sketches and instructions for construction, materials to use, desired measurements and labeling requirements, etc. These instructions are distributed to selected manufacturing vendors to create samples that will meet the tech spec requirements. The samples are then reviewed by the merchant and design teams, who can request changes or adjustments until the samples are approved and authorized to go into production.

Some of the challenges faced by retailers during the Product Development process that impact the product cycle time of their proprietary products are:

- a. Unclear guidance on key product attributes and number and/or type of concepts to develop. This issue can cause the development of product lines and assortments that are not commercially viable or cohesive across product lines, or that are not aligned with the strategy of the brand. In most cases, the merchandising team intervenes during the presentation of conceptual designs and proposes changes to ensure the concepts meet all commercial and brand requirements. However, this request typically requires the design team to start creating conceptual designs once again, causing delays in the product development process and in the overall product cycle time.

A Conceptual Assortment Plan (CAP) is a merchandising tool commonly used by leading retailers that allows merchants to provide guidelines to the design team on how many concepts to develop by product category and what key attributes need to be considered to achieve the desired product assortment. This tool promotes an efficient development of concepts by the design team and reduces the number of iterations required for approval.

- b. No pre-costing of product concepts prior to sampling. The lack of an adequate pre-costing methodology early in the development process prevents designers from creating initial concepts that will meet the cost and margin constraints. This issue typically results in the “over design” of products by preselecting materials that are not aligned with cost and margin expectations and/or adding features into the design that cannot be afforded. Merchants will correct these issues by requesting changes to materials and design, but this typically does not happen until the first samples arrive with the initial vendor quotations. This problem requires the design team to make modifications to the conceptual and technical designs and resend to manufacturing vendors to re-sample and re-quote, which also delays the product development process and overall product cycle time.

An accurate pre-costing tool supported by a powerful costing data base provides guidelines to the design team on the materials and design features to use based on the projected retail price of each item, which leads to a faster and smoother sampling process.

- c. Inadequate or incomplete technical specifications. The lack of detailed and clear instructions for suppliers on how to make the requested samples and/or the lack of complete materials specifications and components to use can cause severe delays in the final approval process. Not having detailed information upfront results in the need for going through multiple sample iterations and revisions to meet the business requirements of the merchants and the conceptual vision of the designers. In addition, important time is wasted in attending to multiple questions from manufacturing vendors and in providing oversight to ensure product specifications are clearly understood and properly executed.

Leading retailers provide a set of technical specifications that are detailed and easy to understand to facilitate the communication of requirements and speed up the sampling and production activities.

- d. Ineffective product development calendar. The product development process includes a long list of interlinked activities (meetings, approvals, commitments, requests, etc.) which require precise coordination, effective scheduling and on time completion. Not having a formal seasonal product development calendar, or lacking compliance of activities and dates, are some of the most critical issues that prevent retailers from significantly reducing their overall product cycle times.

Leading retailers manage all product development activities through a well structured product development calendar and track timely compliance of all activities to ensure that the process flows accordingly and that lead times are minimized.

2. Sourcing

The sourcing activities begin outside of the seasonal development process by leading the effort of identifying, evaluating and certifying materials and manufacturing vendors to build up a solid vendor base. Once the design concepts for the season are completed, presented and approved by the merchants, the sourcing team identifies the right vendors to consider per concept for the development of samples, and later for production. When samples are finalized and approved, and the vendors for production are selected, the sourcing team can manage the procurement of materials, the production and quality assurance processes and the shipment of the finished products from the vendor to the distribution center or to the store.

Some of the main challenges faced by retailers during the sourcing process that impact the product cycle time of their proprietary products are:

- a. No strategic procurement of materials. Many retailers allow their manufacturing suppliers to procure the materials and components required to manufacture the sample and product concepts as long as

the materials comply with the specifications provided. Suppliers submit pre-production samples with the proposed materials and components to be approved for production by the merchandising, design and sourcing teams. However, it is not uncommon that the materials presented during the sampling process are not within the required specifications, or even worse, that the materials presented during the sampling process comply with specifications but at the time of production the materials used do not meet the spec requirements. In both cases, the sampling or production processes are delayed and the cycle time extended.

Leading retailers typically develop a material procurement strategy for key materials, which includes activities such as identifying reliable material suppliers, reserving capacity to ensure on time delivery, and even leading negotiation efforts for achieving better pricing for an improved total product cost.

- b. Lack of a formal and effective vendor management process. Many sourcing organizations lack structured vendor identification, evaluation and certification processes to support the development of a reliable vendor base for a quick and effective pre-selection of materials and manufacturing facilities. Suppliers are frequently pre-selected for sampling based on unreliable vendor data and/or buyer's perceptions or relationships, only to discover during the sampling or the production processes that the manufacturing capabilities, production capacity and/or the level of performance of the pre-selected vendors are not adequate for meeting product spec requirements. This problem can cause severe delays in the sampling and production processes, which lead to the need of finding alternate suppliers for production in reduced time, and typically result in premium manufacturing costs and delays in delivery dates.

A well structured and comprehensive Vendor Management process and a detailed Vendor Matrix promote the development of a dependable vendor base to optimize the vendor selection process, compress cycle times and achieve overall superior performance.

- c. Under utilization of overseas sourcing resources. It is common for sourcing organizations to have overseas offices and support staff in the major country(s) of source to help manage tactical sourcing activities such as quality assurance or production tracking. However, overseas sourcing resources are typically under utilized by limiting the type of responsibilities and decisions in which they can participate. In some cases, this is motivated by the lack of expertise of the overseas sourcing team and potential lack of training, but in many cases it is triggered by the lack of trust and/or fear of losing control by the head sourcing office.

Leading global retailers are transferring more responsibilities and decisions to the overseas sourcing offices, making key decisions closer to the source (supplier) and achieving significant reduction in lead times, and also in labor costs.

- d. Inaccurate product costing. Another responsibility of the sourcing team is to project the final cost of each item after getting quotes from suppliers to ensure that the initial margins budgeted by planning and merchandising will be met. Sourcing proceeds to negotiate with suppliers to meet (or improve) profit margin expectations by reducing the quoted price or by making modifications to the product if budgeted margins are not met. Negotiation is a critical process in sourcing, not only to ensure that the price of the product is within expectations, but also to ensure that the negotiations are done quickly to prevent long cycle times and potential delays in delivery. Most retailers rely on past experience for determining if vendor quotations are within acceptable ranges or not. This high level and empirical approach does not provide much leverage for negotiation to the sourcing team and can delay the negotiation process.

Leading global retailers use detailed costing tools for projecting the total cost of the product building the cost from the bottom up, which provides powerful information on cost by line item to the negotiation team and increases their negotiation leverage with suppliers, significantly reducing negotiating time and total product cost.

3. Transportation and Distribution

The transportation and distribution operations begin once the products are available for pick-up at the manufacturer in the origin country. Depending on the product's destination and quantity, a decision on consolidation and mode (air/ocean) selection is made. The logistics team defines the optimal flow for delivering the goods to the distribution centers (DC's) and to the stores, and manages activities such as freight movement, customs clearance, DC operations, store delivery, store returns, and more.

Some of the main challenges faced by retailers during the logistics and distribution process that impact the product cycle time of their proprietary products are:

- a. Suboptimal flow of products through the supply chain. Many retailers still operate under one single product flow, in which all items are flowed through the same logistics channels from supplier to store. This one-dimensional practice prevents time sensitive products from being flowed more rapidly to the stores for meeting product launch dates in reduced time and/or for replenishing items more effectively. Major retailers develop a comprehensive Flow Path Strategy that includes at least 3 different product flows depending on the physical, demand, financial and supply characteristics for each item, with some leading retailers using up to 10.

An effective Flow Path Strategy identifies if the product should be flowed through regional warehouses, directly to the stores or directly to the consumer to ensure that transportation costs are minimized while considering the importance of meeting delivery times and reducing overall cycle times.

- b. Inefficient distribution network. An un-optimized distribution network can also have an impact on the extension of product cycle times. Distribution Centers lacking the appropriate design, layout and material handling equipment can result in high costs and low productivity and contribute to the extension of cycle times within the supply chain.

Engineering DC operations for improving overall productivity allows for products to flow through the DC more rapidly and contributes to the concept of improving “speed-to-market”. In addition, more efficient DC operations results in lower distribution costs, lower inventory levels and improved service levels.

- c. Inefficient freight consolidation process. Consolidation of products at key geographical locations promotes the optimization of container utilization and reduces overall transportation costs. However, if the consolidation process is not effectively planned and managed, supply chain cycle times may be lengthened and store deliveries delayed, resulting in higher costs and potentially lost sales.

The implementation of a well structured and holistic freight consolidation strategy and program is key for capturing significant transportation cost reductions, while also considering the importance of meeting delivery dates and reducing overall supply chain cycle times.

- d. Lack of supply chain visibility. The process of moving product from suppliers to consumers is highly complex, with multiple touch points, transfers and transactions that need to be managed closely to minimize transportation costs and delivery times. Many retailers utilize tools and processes to track and manage the activities and events that happen during the transportation and logistics process, but in many cases these tools and processes are limited and do not provide full visibility across the supply chain, resulting in delays and added costs.

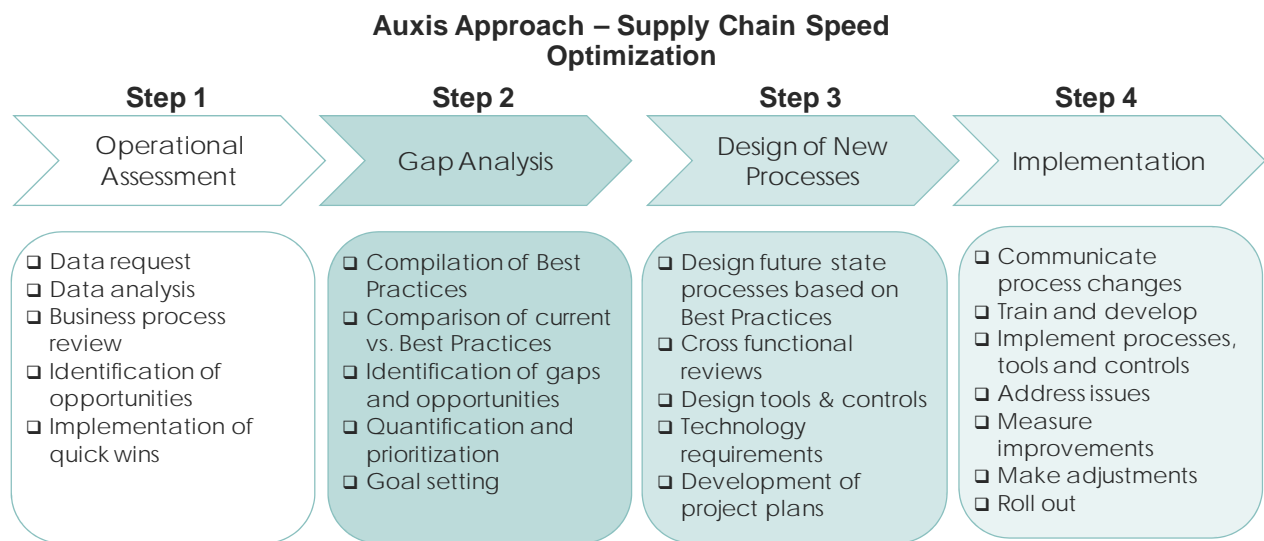
Leading global retailers manage all their transportation and logistics events and exceptions utilizing supply chain visibility software or global trade management (GTM) software, which provides real time visibility and information on the location and status of each item on the purchase order, down the SKU level. These software applications provide the retailers the end-to-end visibility and added agility needed to effectively manage the flow of the product and to optimizing time, cost and service constraints.

The Auxis Solution

Auxis follows a 4-step approach for improving supply chain processes focused on increasing speed-to-market for enhancing overall business performance:

1. **Evaluation of supply chain processes and performance by business function.** Auxis performs a detailed operational assessment of your product development, sourcing and logistics operations to evaluate current processes, tools, controls and organization with a focus on opportunities for improving cycle times. Key supply chain data is compiled through an initial data request, and validated during the operational assessment, to evaluate current business performance across supply chain functions.
2. **Comparison of current processes and performance to leading practices.** A detailed Gap Analysis is performed to help identify opportunities for improvement based on industry best practices and benchmarks from leading speed-to-market retailers. The opportunities for improvement are prioritized and quantified, and a cross-functional project implementation plan is designed to bridge the gaps and achieve cycle time and performance goals.
3. **Design of new processes, tools and controls.** Best-in-class processes, tools and controls are designed and customized for improving key areas by business function with a focus on reducing supply chain cycle times and improving overall supply chain performance.

4. **Implementation of new processes and measurement performance.** Auxis leads the implementation of new processes, tools and controls through one full season for achieving a rapid and smooth implementation, and oversees the continued implementation of processes through subsequent seasons. Your product development, sourcing and logistics/distribution resources are fully involved during the implementation process for achieving an effective process change, effectively transferring knowledge and industry best practices, and ensuring sustainability of results. Supply chain KPI's are measured, tracked and compared to predefined performance goals to ensure the projected goals and economic benefits are achieved or surpassed.



Summary

It is evident that consumers are becoming more trend conscious, fickle and cost aware in their purchasing decisions, and this is a trend that is likely to continue as consumers grow more sophisticated and seek more freshness and variety in their purchases. Top retailers have taken multiple strategies for optimizing and compressing their supply chain processes, to design products as close as possible to the product launch date, and allow time to incorporate the latest trends and market ideas. Some of these strategies include: leveraging multiple process tracks, re-aligning and re-sequencing activities, developing strategic relationships with suppliers and automating process tracking with PLM tools.

Leading global retailers that have reduced their concept-to-store cycle time from 50-60 weeks down to 20-40 weeks have experienced significant benefits in improved market share, profit margins and inventory turns, among other benefits. Nonetheless, they are still looking for ways on how to keep improving and refining their supply chain processes to reduce cycle times. There are already a number of retailers that have implemented a formal Fast Track process, in which a small percentage of the assortment is conceptualized, designed, sampled, manufactured and shipped to the stores in 6-8 weeks, and it is only a matter of time before most of the assortments are put through similar cycle times.

Retailers that keep operating under long supply chain cycle times of 40+ weeks, and that delay making significant efforts for improving and compressing their product cycle times, are destined to lose the appeal of their product assortments and brands, resulting in loss of sales and market share.

Auxis is a leading Management Consulting firm headquartered in Coral Gables, Florida. Auxis' Supply Chain Excellence Practice believes in a practical, "back to basics" approach to help our clients buy, ship, store and sell right. Our methodology is designed to provide our clients with real-world business solutions anchored by solid financial analysis.

Auxis can help you improve your supply chain for the benefit of your customers, business partners, and shareholders through service offerings for excellence in product development, manufacturing, sourcing and procurement operations, strategic evaluation, network design, 3PL provider selection and outsourcing, warehousing and transportation management and supply chain planning.

Auxis, Inc.

55 Miracle Mile Suite 300

Coral Gables, FL 33134

Tel. +1 (305) 442-0060

Fax + 1 (305) 442-8259

www.auxis.com