

Hitting reset on luxury fashion

How to engineer a future-proof model

The luxury fashion industry is undergoing an important phase of transformation, initiated before the pandemic and now accelerated by it.

The restrictions caused by lockdowns and the halt in international tourism traffic have forced luxury businesses to make organisational changes and have highlighted the limitations of an inefficient and expensive business model.

Supplier engagement is as crucial as consumer engagement

A challenging 2020 has forced senior luxury leaders to pause and reflect about how they currently work. Above all, it has given them an opportunity to consider the structural changes they could make, how this would impact their brands, and how it would impact players both upstream and downstream in the value chain.

The acceleration of the digital channel and the growth of new distribution and consumer "engagement" models are the topics that are top of mind. Yet only limited thought has been given to how the upstream supply chain model could evolve for businesses across the industry.

For this reason, we conducted research to better understand the changes luxury companies and their suppliers will need to make to their way of working in order to deliver a winning response for the end consumer and for a supply chain still based on traditional models.

We interviewed CEOs from leading luxury businesses in France and Italy. Between them, their businesses account for annual revenues of €25bn, with individual revenues ranging from less than €100m to billions of Euros.

In the future, suppliers will play a fundamental role with their skills and services

We asked them about all key aspects of their operating model, addressing issues across collection structure, collection development, sourcing, logistics and sustainability. We also asked them to rank their most important issues.

One common factor emerged: all brands pointed towards the need for the increasing integration of suppliers upstream, in both the creation and development process and in planning and production.

The true differentiating factor for players in the industry is therefore the capability of involving both the consumer and the supplier in a process where the brand continues to convey intangible values.



Emerging needs

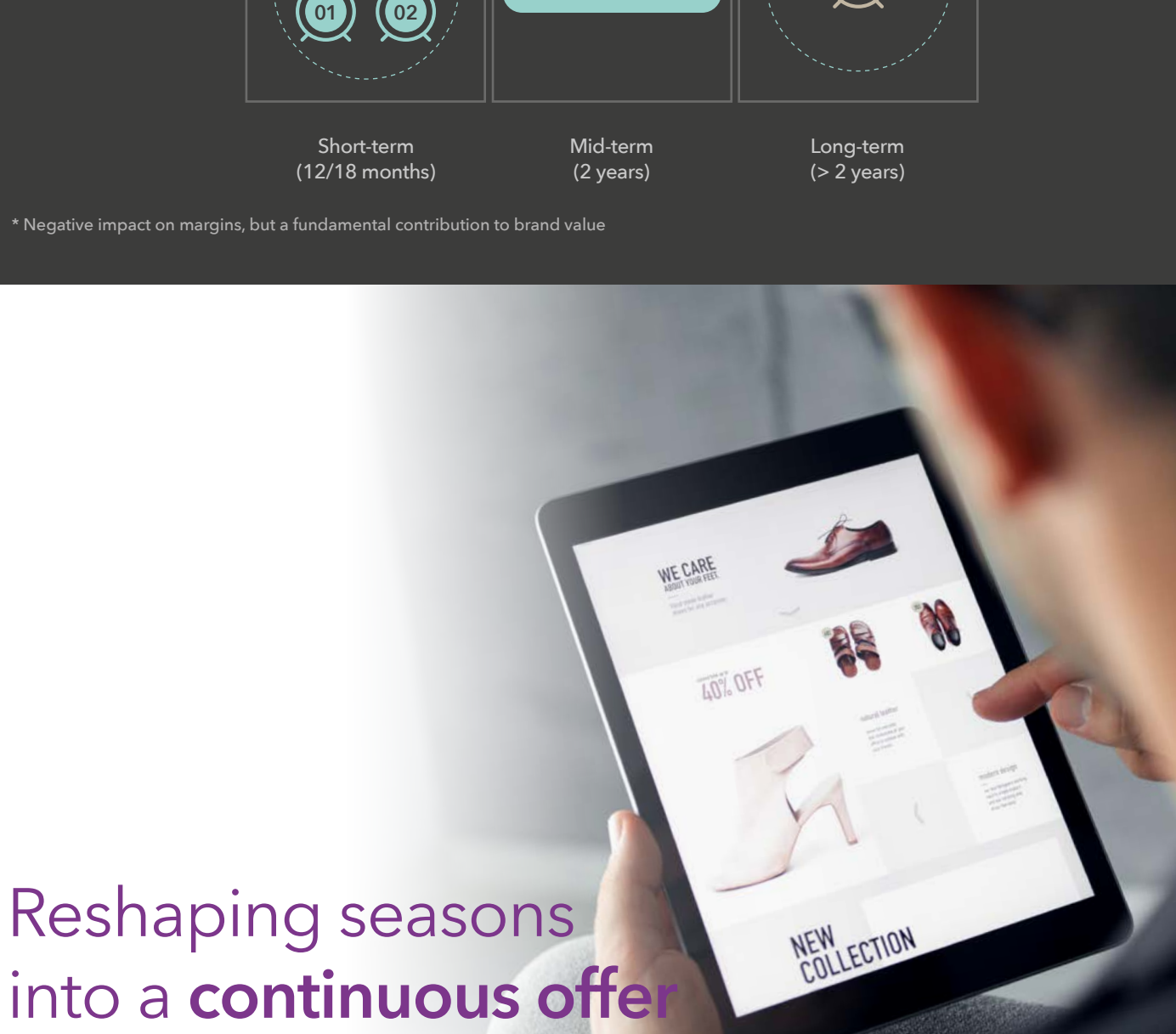
The following themes were identified as winning and differentiating factors for future operational models:

- A product offer enhanced with continuous newness and less tied to seasonal schemes
- A more structurally flexible supply model, built side by side with suppliers
- An improvement in the management of physical flows and service timing
- A growing focus on sustainability and steps to improve it

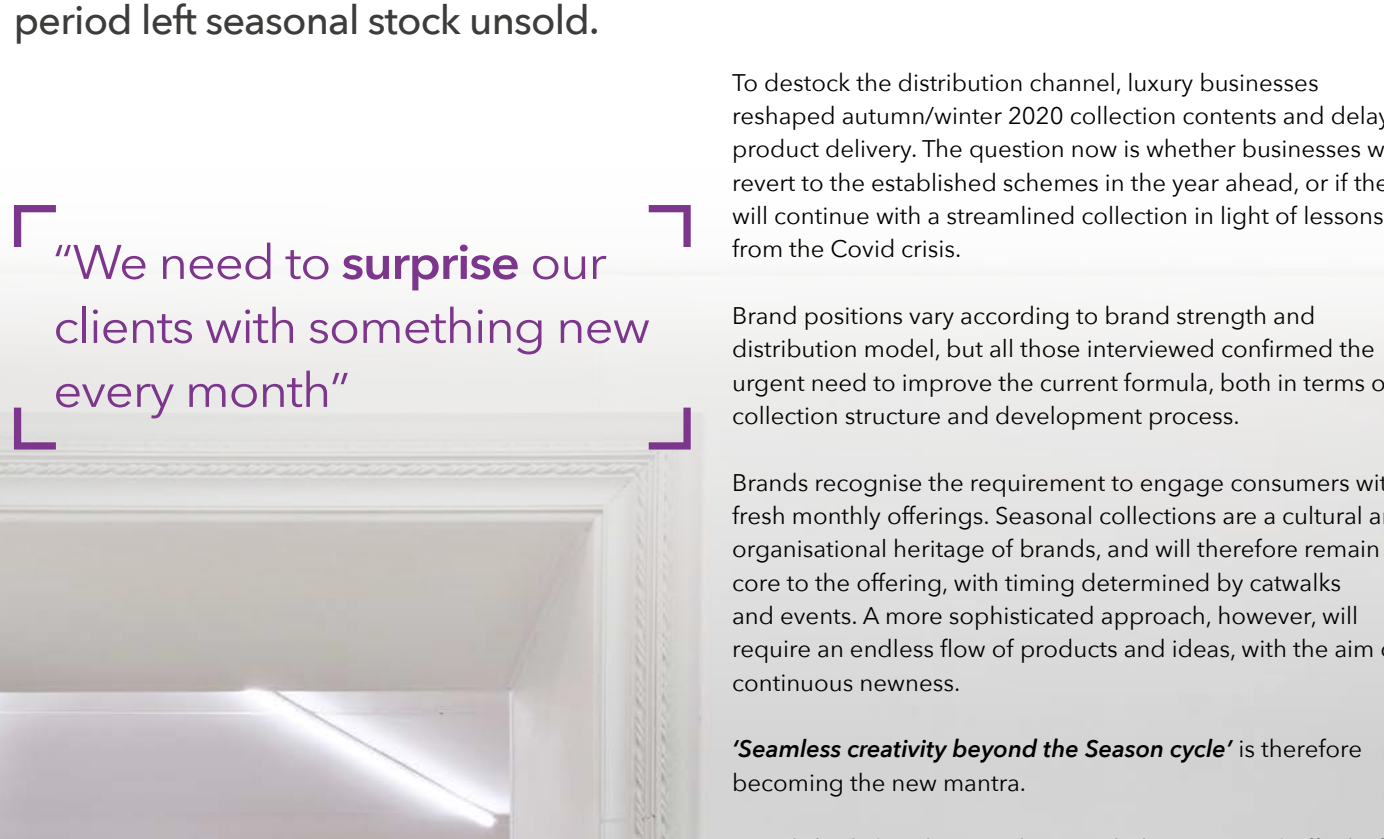
These themes have very different economic impacts and varying time frames for implementation. Brands of various sizes and with multiple strategies and growth plans will have to choose how to redesign investment programmes accordingly. The changes they make to their operations and supply chain model will impact their long-term performance; such change will increasingly become a priority for CEOs and not solely for operational heads.

Changes to the business model will reshape brand interaction with suppliers; the added value and contribution suppliers make to a brand's success will shift significantly away from elements tied to costs only.

WHAT ARE LUXURY COMPANY PRIORITIES ALONG THE VALUE CHAIN?



TIMING, COMPLEXITY AND FINANCIAL IMPACT OF BRAND STRATEGIC GOALS



Reshaping seasons into a continuous offer

In 2020 the traditional race to anticipate the delivery of the commercial offer stopped. The long lockdown during the traditional spring/summer selling period left seasonal stock unsold.

“We need to surprise our clients with something new every month”

To destock the distribution channel, luxury businesses reshaped autumn/winter 2020 collection contents and delayed product delivery. The question now is whether businesses will revert to the established schemes in the year ahead, or if they will continue with a streamlined collection in light of lessons from the Covid crisis.

Brand positions vary according to brand strength and distribution model, but all those interviewed confirmed the urgent need to improve the current formula, both in terms of collection structure and development process.

Brands recognise the requirement to engage consumers with fresh monthly offerings. Seasonal collections are a cultural and organisational heritage of brands, and will therefore remain core to the offering, with timing determined by catwalks and events. A more sophisticated approach, however, will require an endless flow of products and ideas, with the aim of continuous newness.

“Seamless creativity beyond the Season cycle” is therefore becoming the new mantra.

Brands had already started to enrich their seasonal offer before the pandemic, increasing the number of in-season ‘drops’ or developing collaborations with stylists (such as Moncler’s ‘Genius’ project). This trend will accelerate. As a result, upstream partners will need to adapt their operating model to supply products in small volumes, on very tight time schedules and at competitive costs.



Engineering flexibility into the production process

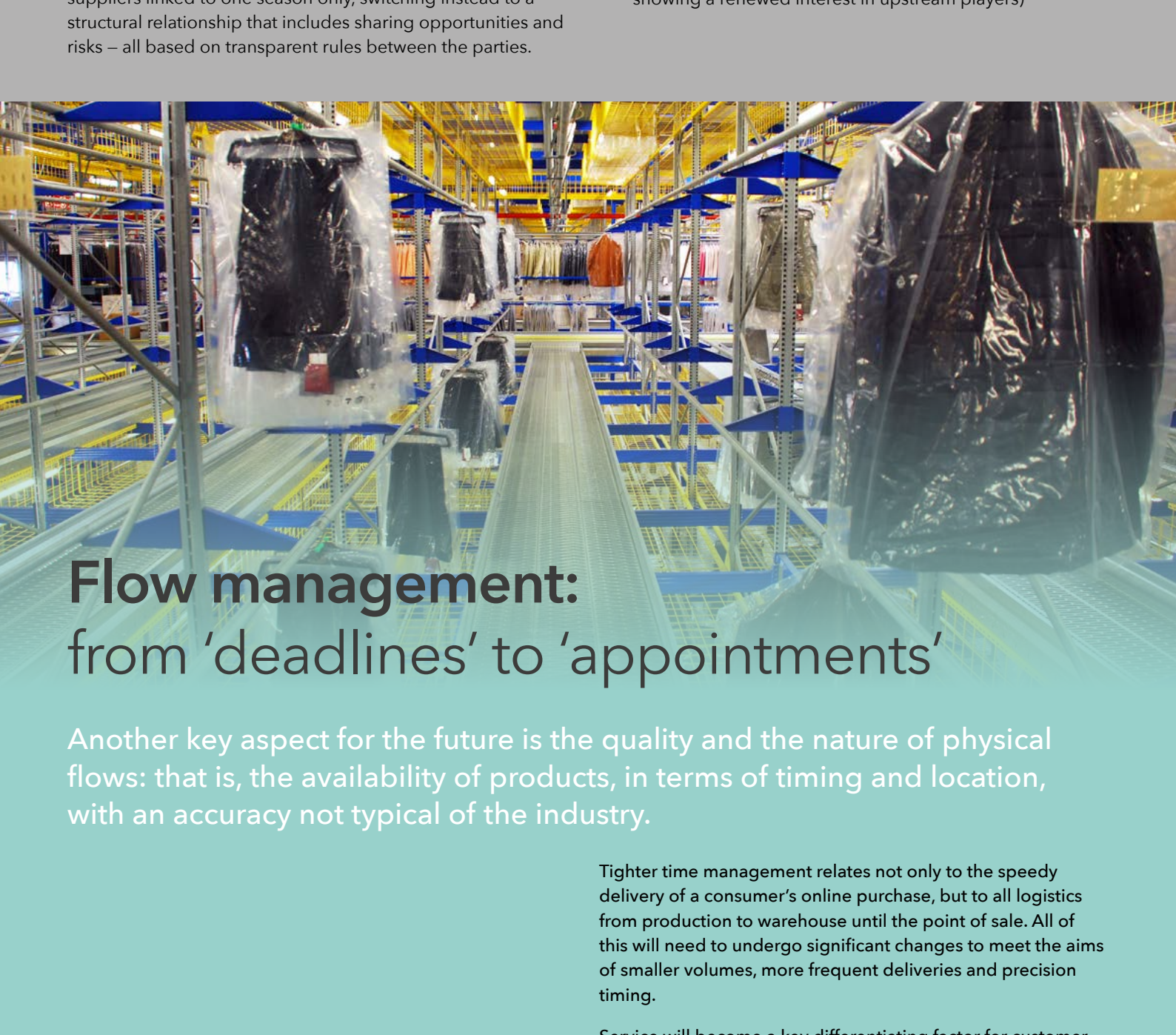
2020 has highlighted the rigid structure of the current luxury business model. While designing products 12 months ahead of when they are sold is challenging, sequencing volumes and mix is like driving a lorry from the back seat through tight curves on an unpredictable road: it is only a matter of time before it will almost certainly end up off-road.

The driving model needs to evolve. Luxury businesses need to become nimble go-karts built specifically to zip around a competitive market. How can the sector make this possible? Leaving the metaphor aside, it is a matter of reviewing the nature of relationships with suppliers. Luxury businesses will be required to work with suppliers in planning; and to work together to balance the supply risk and the cost of flexibility. They will need to manage inevitable forecasting changes at a reasonable cost; every product (permanent, seasonal, flash) comes with questions on how to manage variances in volume and mix, and therefore how to limit (and share) the subsequent costs.

Above all, brands need to move beyond relationships with suppliers linked to one season only, switching instead to a structural relationship that includes sharing opportunities and risks – all based on transparent rules between the parties.

The cost of flexibility is lower than the cost of going off-road: this is the pandemic’s true lesson.

- For the **largest groups**, the key guideline is ‘vertical integration’ with strategic suppliers (we are witnessing a wave of upstream acquisitions that will accelerate in 2021)
- For **smaller brands**, the challenge lies in building strong and long-lasting relationships with suppliers, despite limited volumes and sizes
- For **upstream players**, the new engagement model with brands will force investments in processes and systems that imply larger scale and better managerial skills (funding may come in the form of Private Equity, which is showing a renewed interest in upstream players)



“We require full transparency on processes and costs, on a mutual trust basis”

Flow management: from ‘deadlines’ to ‘appointments’

Another key aspect for the future is the quality and the nature of physical flows: that is, the availability of products, in terms of timing and location, with an accuracy not typical of the industry.

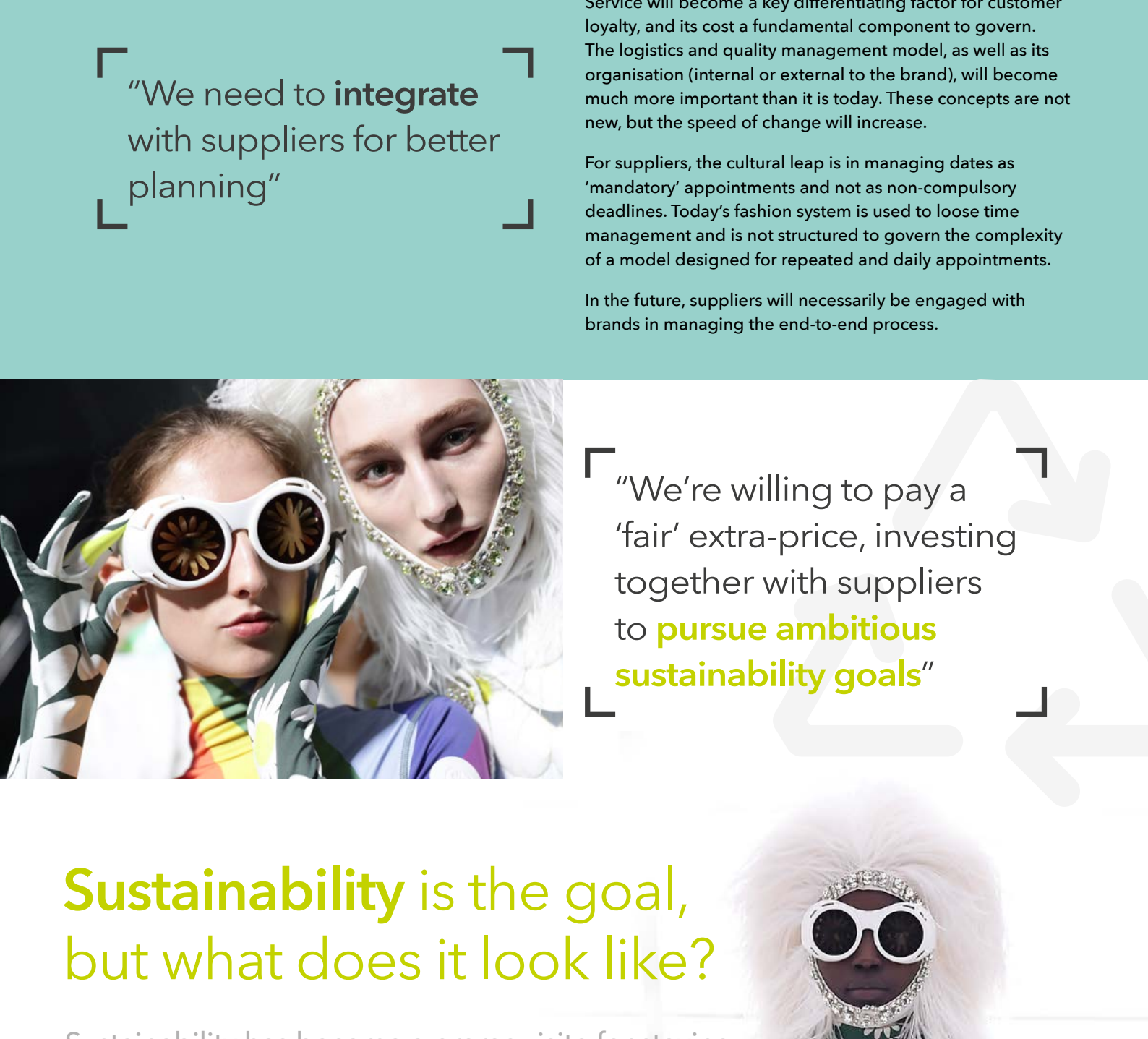
“We need to integrate with suppliers for better planning”

Tighter time management relates not only to the speed of delivery of a consumer’s online purchase, but to all logistics from production to warehouse until the point of sale. All of this will need to undergo significant changes to meet the aims of smaller volumes, more frequent deliveries and precision timing.

Service will become a key differentiating factor for customer loyalty, and its cost a fundamental component to govern. The logistics and quality management model, as well as its organisation (internal or external to the brand), will become much more important than it is today. These concepts are not new, but the speed of change will increase.

For suppliers, the cultural leap is in managing dates as ‘mandatory’ appointments and not as non-compulsory deadlines. Today’s fashion system is used to loose time management and is not structured to govern the complexity of a model designed for repeated and daily appointments.

In the future, suppliers will necessarily be engaged with brands in managing the end-to-end process.



Sustainability is the goal, but what does it look like?

Sustainability has become a prerequisite for staying in business: a fact that is increasingly recognised by consumers, brands and production chains alike. The time for action is now.

Some brands have taken it upon themselves to develop sustainability initiatives but true sustainability remains an elusive and largely unexplored area, with space for new business models.

The role of suppliers will be decisive in helping the luxury sector get to grips with sustainability. Suppliers have the technical competences in process and material and the ability to combine process/material innovation to creative propositions. This is what design departments look for and expect.

All brands interviewed recognise the need to invest in pursuing ‘sustainability’ in collaboration with suppliers, without reversing the cost onto the consumer. There are already many examples of projects and initiatives to embed circularity into the projects – for example from Max Mara, Moncler, brands in the Kering Group and in the LVMH Group. However, the industry still lacks scale, a shared infrastructure and a common set of rules and standards for the most relevant product platforms.

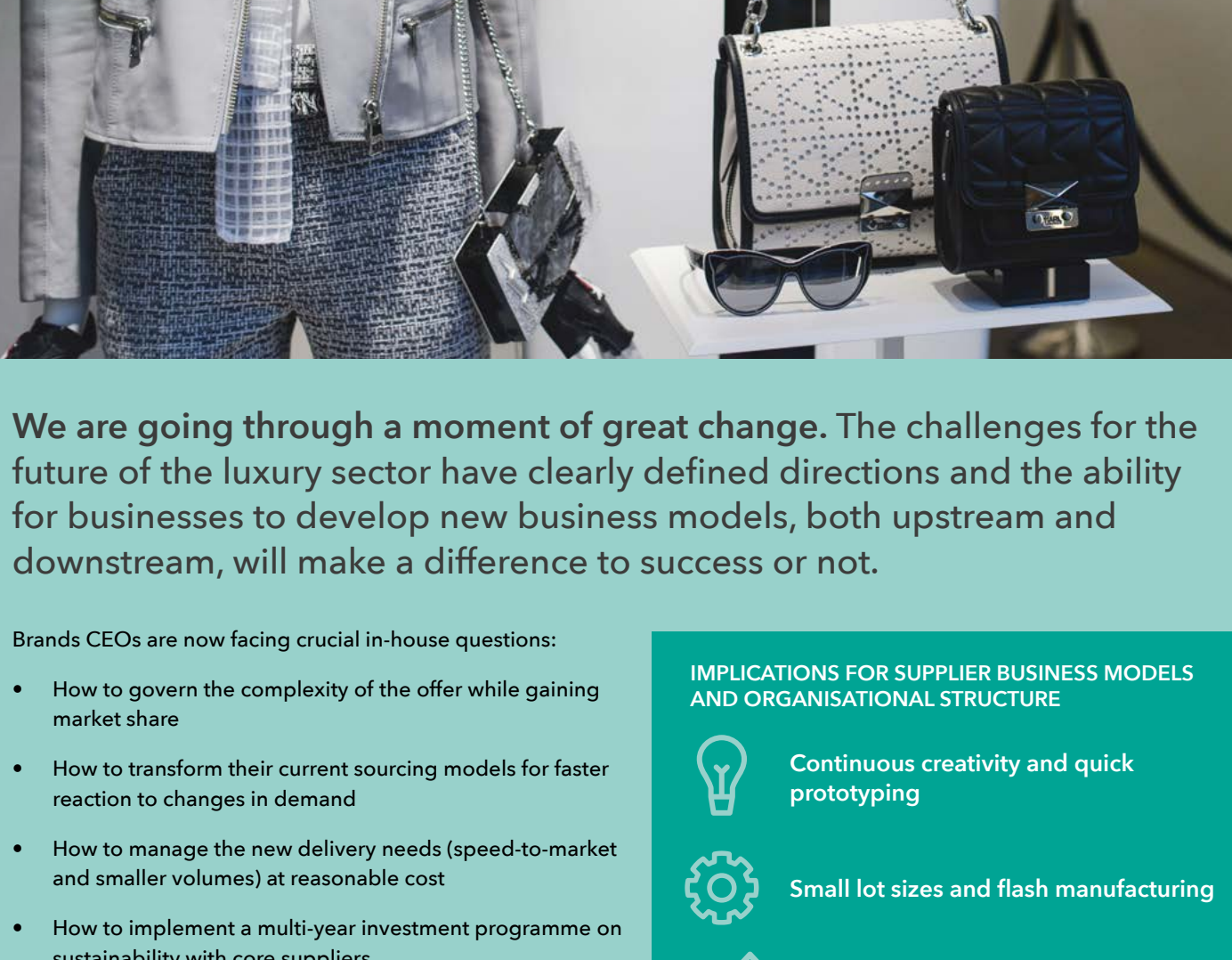
For suppliers in key sourcing geographies, there is a unique opportunity to work together and build new leading-edge production platforms, combining their manufacturing quality and innovative operational models in a new unbeatable manner.

The focus on sustainability will be fuelled by the €750bn Next Generation EU recovery fund to support member states by the pandemic. We expect these unprecedented funds to be partially spent in investments to support the restructuring and launch of local areas of manufacturing excellence, such as Italy’s textile, apparel and fashion industry.

“We’re willing to pay a ‘fair’ extra-price, investing together with suppliers to pursue ambitious sustainability goals”



This is true downstream for brands, but above all upstream for the world of supply, which is still strongly characterised by great fragmentation of the offer. We expect a period of profound transformation and consolidation of the production platforms within the sector.



In summary

We are going through a moment of great change. The challenges for the future of the luxury sector have clearly defined directions and the ability for businesses to develop new business models, both upstream and downstream, will make a difference to success or not.

Brands CEOs are now facing crucial in-house questions:

- How to govern the complexity of the offer while gaining market share
- How to transform their current sourcing models for faster reaction to changes in demand
- How to manage the new delivery needs (speed-to-market and smaller volumes) at reasonable cost
- How to implement a multi-year investment programme on sustainability with core suppliers

Brands will need to review their organisational models, redefine rules of engagement with suppliers and share long-term programmes.

On the other hand, suppliers, at any level of performance and quality, will need to undergo a challenging transformation programme too, that will become a prerequisite for survival.

Most of the changes are not new topics: they have been the subject of debate in recent years but the pandemic has accelerated the process.

The nature of the challenges makes the size and scale of companies an enabling factor. It is clear that more structured organisations with financial clarity can guide the changes in direction and timing, and with greater incisiveness.

IMPLICATIONS FOR SUPPLIER BUSINESS MODELS AND ORGANISATIONAL STRUCTURE

- Continuous creativity and quick prototyping
- Small lot sizes and flash manufacturing
- Flexible production processes
- Multi-year investments in sustainability
- Scale through consolidation

If you would like to discuss any of the themes covered in the report we’d be delighted to talk.

Luca Bettale, Partner
l.bettale@longtermpartners.it

Anna Miranda, Partner
a.miranda@longtermpartners.it

uncommon sense