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Fashion sense

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Spanish retailer, Zara, has crafted a sweet success story riding on its image as a low-cost, high fashion store. Nirmalya Kumar and Sophie Linguri take to the High Street to look at Zara's route from rags to riches.

In 1975, the first Zara store was opened in La Coruña, in Northwest Spain. By 2005, Zara's 723 stores had a selling area of 811,100 square metres in 56 countries. With sales of e3.8 billion in the financial year 2004, Zara had become Spain's best-known fashion brand and the flagship brand of є5.7 billion holding group Inditex. Inditex's stock market listing in 2001 turned Amancio Ortega, its founder and a self-made man, into the world's twenty-third richest man, with a personal fortune that Forbes magazine estimated at $12.6 billion.

Among the keys to Zara's success is its approach to the supply chain. Zara sources around half its garments from third parties in low-cost manufacturing locations like Asia. These are basic collection items or wardrobe "staples," with minimal fashion content, such as T-shirts, lingerie and woollens, and where there is a clear cost advantage. Externally manufactured items are shipped to Zara's distribution centre. The other half of Zara's garments, those that are more fashion-dependent, is manufactured in-house, in nearby Zara factories.

A team of 200 young, talented largely unknown designers create designs, based on the latest fashions from the catwalk and other fashion hotspots, which are easily adaptable to the mass market. In this way, Zara is adept at picking up the latest trends and churning them out to stores around the world in a matter of weeks.

After Madonna's first concert date in Spain during a recent tour, her outfit was copied by Zara designers. By the time she performed her last concert in Spain, some members of the audience were wearing the same outfit. In 2003, when the Crown Prince of Spain announced his engagement to Letizia Ortiz Rocasolano, she wore a white trouser-suit for the occasion. In just a few weeks, the same white trouser-suit was hanging from Zara's clothes racks all over Europe, where it was snatched up by the ranks of the fashion-conscious.

A new line in simplicity

Working alongside the market specialists and production planners, the designers for each of Zara's collections keep in touch with market developments, to create around 40,000 new designs every year, of which around one-quarter are manufactured.

Zara tries to keep its offering of any style simple, usually in just three sizes and three colours. Computer-guided cutting tools cut fabric, using patterns made from selected designs. The labour intensive sewing of the garments is outsourced to local subcontractors, which use seamstresses in cooperatives. Zara is usually their sole client, and they work without any written contracts. Subcontractors receive a flat fee per type of garment, and operate on short lead times and fast turnaround. They pick up the prepared fabric pieces from Zara, and return them to the 500,000 m^2 distribution centre.

At the Zara distribution centre, items are sorted and collected by trucks, which transport them to different destinations all over Europe (which make up about 75 per cent of deliveries). Products for more distant destinations are transported by air (about 25 per cent). Shipments tend to have almost zero flaws, with 98.9 per cent accuracy and under 0.5 per cent shrinkage.

Since Zara's garments are produced in-house, it is able to make a new line from start to finish in anywhere between two and five weeks, depending on the type of garment. As a result Zara can be responsive to fashion items that are selling well during the season, and to discontinue those that are not. By constantly refreshing the collection, and manufacturing items in high-intensity, short-runs, Zara is able to prevent the accumulation of nonsaleable inventories.

Unique selling proposition

It is estimated that Zara committed just 15-25 per cent of production before the season begins, 50-60 per cent at the start of the season, and the remainder is manufactured in-season. The percentage of Zara sales consisting of markdowns is 15-20 per cent. In some cases, stores run out of stock. However, this is not viewed as a negative since it contributes to customers' perception of the uniqueness of their purchase.

Thanks to the frequent refreshing of stock, customers constantly returned to stores, to browse new items. Zara's global average of 17 visits per customer per year is considerably higher than the three visits to its competitors' stores.

Visitors are also more likely to purchase, as one senior executive explains: "Zara's objective is not that consumers buy a lot but that they buy often and will find something new every time they enter the store."

Comments by Luis Blanc, an Inditex director, illustrate how Zara stores foster an environment of immediacy: "We want our customers to understand that if they like something, they must buy it now, because it won't be in the shops the following week. It is all about creating a climate of scarcity and opportunity."

Affordable prices help to encourage purchases, and Zara's offering is often referred to as clothing to be worn six to ten times. Zara's pricing differs across country markets. It sets prices according to individual market conditions, rather than using cost plus margin as its basis (which is the formula used by most of its competitors). In Spain, Zara products are low-cost, while in the US, Japan and Mexico, they are priced as a luxury fashion item. Prices in France are somewhat higher than in Spain, since the average French consumer is willing to pay more for fashion than most other European consumers. For example, in 2003, the price of jeans in Zara stores in France was $34.58 compared with $24.87 in Spain and $54 in Japan. Until 2002, Zara used one price tag listing the price in different currencies, to simplify tagging of items. In 2002, however, it implemented a system of local pricing, using a bar code reader that printed the correct local price for items.

Compared with its competitors, Zara generally prices its products somewhat higher than C&A and H&M, but below Gap, Next and Kookai. For example, a similar shirt cost $26 at Zara, compared with a price of $29 at Gap and $9 at H&M.

Managing the brand

In comparison with other clothing retailers, who spend 3-4 per cent of sales on advertising, Zara spends just 0.3 per cent. The little it does spend goes to reinforcing its identity as a clothing retailer that is low-cost but high fashion.

Zara relies on its shop windows to communicate its brand image. Displays are changed regularly, according to designs sent by headquarters, and are critical for Zara to remain visible and entice customers. Store locations are generally busy, prestigious, city centre shopping streets.

The remuneration of store managers is partially dependent on the accuracy of their sales forecasts and sales growth. Each evening a handheld PDA displays the newest designs sent by headquarters, which are available for order. Order deadlines are twice weekly, and are issued via the handhelds. Store managers who fail to order by the deadline receive replenishment items only. Deliveries arrive at stores twice per week from Zara headquarters, a few days after the order is made, and contain both replenishment items as well as new products. Failure rates of Zara's new products are reported to be just 1 per cent, considerably lower than the industry average of 10 per cent.

Technology is a key part of enabling communications and information flow. Zara's IT infrastructure is relatively simple, which means that its IT expenditure is as much as five to ten times lower than that of its rivals.

Expand to fit

Besides Zara, targeted at trendy city youngsters, Inditex grew its portfolio of apparel chains throughout the 1990s with each chain targeted at a specific segment:

- Massimo Dutti – Young businessmen
- Pull & Bear – Elegant male clothing
- Berksha – Elegant fashion for young women
- Brettos – Trendy young suburban women
- Oysho – Lingerie
- Stradivarius – Youthful fashion
- Kiddy's Class – Trendy children

Future shopping

Following Zara's success, competitors sought to reduce their own lead times. The competitive advantage achieved by Zara's vertical integration appears to be eroding. As it opens stores in increasingly distant markets, will Zara be able to retain its flexibility in adjusting production to accommodate differences in local trends?

Might Chinese clothing manufacturers prove to be a competitive threat to Zara, with their high capacity and continuous improvements in quality? José María Castellano Ríos, the company's deputy chairman, discounts this threat: "Being a Zara or Gap is not just about designing fashionable clothes and manufacturing them cheaply. You must also make the transition to being a retailer. It is a big step from manufacturing to distribution. There is also the question of managing the location and presentation of stores, training staff and so on."

The Zara model seems to work better in markets where customers have an appetite for fashion (such as France, Italy, Japan and the UK). In other markets, where consumers are less fashion-focused (for example, Germany and the US) Zara seems somewhat less successful. Among the key questions Zara must now face are whether it would be better served in the long run by increasing penetration in these fashion-sensitive markets, or by extending its global reach through increased presence in more markets?

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Their case study, "Zara: Responsive, High-Speed, Affordable Fashion", is available from the European Case Clearing House (www.ecch.co.uk).