BUS478

ZARA

Synopsis

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ZARA’S HISTORY

Zara is one of the most well-known international fast-fashion companies, owned by the Spanish fashion group Inditex (Zara, 2012). The first Zara store was opened in La Coruña by Amancio Ortega Gaona in 1975. From that moment forward, Zara’s expansion has been unstoppable. By the year 1990, Zara had opened stores in Oporto, Portugal, New York, USA, and Paris, France (Inditex, 2012). Utilizing Zara’s strong brand image, Zara Home was introduced in 2003, providing housewares. Later, in 2007, the first online store was launched to sell Zara Home products (Inditex, 2012).

After 38 years of operation, Zara now has 1,830 stores in 82 countries across Europe, America, Africa, and Asia. The number of stores that Zara has only accounts for approximately one-third of stores that Inditex has; however, they generate more than 64% of Inditex’s sales (Inditex, 2011). Zara classifies itself through its commitment as a fast fashion brand rather than high fashion, and quickly adopts high fashion styles from the catwalk to reach the public at an affordable price.

Unlike other fashion brands, which outsource their production, Zara has successfully developed a vertical integration model including design, just-in-time production, marketing, and sales (The Economist, 2001). With vertical integration, Zara is able to meet consumer demands within a relatively short timeframe and respond to market trends quickly. Because the fast fashion industry is constantly changing and hard to predict, the flexibility and efficiency provided by this model is becoming the key factor in Zara’s success.

EXTERNAL ENVIRONMENT

The fast fashion trend in the apparel industry has been revolutionized in recent decades by companies such as Zara, H&M and Topshop (London Business School, 2008). Accordingly, factors influencing the apparel industry at large will also influence the fast fashion apparel industry.

General Environment Summary

In the apparel industry, the customers’ demands differs according to their ages. An aging population may increase the demand for looser-fitting styles (Keane & te Velde, 2008). Additionally, population sizes may affect the demand in different apparel categories. An increase in birth rate and the proportion of pregnant woman may stimulate the growth of baby clothes and maternity clothes (Suttle, 2011). Demographic trends are important considerations in this industry.
Economic conditions are another key factor which affects the apparel industry, as clothing purchase can be a luxury purchase or “splurge” for many individuals rather than simply a necessity purchase. For instance, an economic recession may lead to a decrease of consumer’s disposable incomes which is followed by a decrease in spending on clothes. In addition, an increase in rates of personal savings may have a negative impact on demand in the apparel industry.

In regards to political aspects in the apparel industry, worker’s rights and child labour laws are important to consider in order to create a legal and sustainable work environment in manufacturing (Suttle, 2011). Additionally, since the spread of international trade, many manufacturers are now established in developing countries. The cost effect of import and export taxes on the apparel industry directly affects the success of international retailers.

In terms of the sociocultural segment, consumers tend to spend more on healthcare, electronics, education, travel, and leisure, and less on clothing, which drives apparel companies to develop their businesses ecologically to meet consumers’ demands (Jasuja, 2012). Most employees in the industry are women, and they are responsible for jobs in weaving, spinning, or hanging fabrics, while men take charge of technical jobs such as machine supervision. The ratio of male to female employment in these industries shows a big difference across countries and regions (Keane & te Velde, 2008).

Regarding technologies in the apparel industry, there is wide use of human intelligence instead of computers in the manufacturing process. Also, digital technologies like Location-Based Mobile Technology, which allows retailers to track and communicate with customers, are used to meet the rapid changes in the apparel industry (Ziv, 2010). According to Sorescu, Frambach, Singh, Rangaswamy, & Bridges (2011), a key component to success in retailing is keeping abreast of new technologies, especially those which could make the retailer’s product outdated. With the rapid pace of technological change in the 21st century, it is vital that Zara fully understands the technological enhancements made internationally by other fast fashion retailers.

Globally, since lower labour costs and sufficient raw materials are available in some developing countries such as China and India, more and more apparel companies seek to cooperate with manufacturers in these countries (The Economist, 2011). Furthermore, sustainability strategies will be developed in the apparel industry under the lead of the Sustainable Apparel Coalition, which includes Nike, Gap Inc., H&M, Levi Strauss, Marks & Spencer, and Patagonia (Kaye, 2011).
Industry Environment: The Fast Fashion Apparel Industry

Fast fashion is an industry innovation. Instead of using the “designer-push” collections model, these companies adapt to current and emerging trends according to shifts in customer demands in just a few weeks, versus industry average of six months (London Business School, 2008).

Threat of New Entrants

In fast fashion, the threat of new entrants is low. The reasons for this are twofold. Marketing, production, and distribution costs are spread over large production units in the fast fashion industry, which lowers overall production costs. Small players find this extremely difficult to achieve, making it difficult for them to compete, especially when considering the huge initial investments required to enter this industry.

Bargaining Power of Suppliers

The bargaining power of suppliers is low because there are a lot of suppliers in the apparel industry, and raw materials are sufficient and widely offered in some developing countries such as China, Vietnam and India. Besides, it is not possible for a given supplier to dominate raw materials such as cotton and cloth in the apparel industry, which negatively affects the bargaining power of suppliers.

Bargaining Power of Buyers

The bargaining power of buyers is moderate. Since customers’ switching costs are low and there is a lack of high brand loyalty in the apparel industry, customers can be very flexible in choosing products across brands. However, the large number of customers compared to fast fashion retailers, along with the low possibility of customer integration, lowers the bargaining power of customers.

Threat of Substitute Products

The threat of substitute products is high. The substitute sources for fast fashion apparel retailers are high-end luxury retailers, discount retailers, and department stores. This high availability of substitute products poses a huge threat for fast fashion retailers. What is worse, the switching costs in this industry are low since customers can easily find substitutes that have the same levels of price and quality.

Rivalry among Competitors

Rivalry among competitors is intense in the fast fashion apparel industry. There are a large number of global apparel retailers adopting the fast-fashion model (e.g. Zara, H&M, Topshop, etc). Moreover, most fast fashion companies are listed companies, and so their managements cannot decide to exit the industry at will.
INTERNAL ENVIRONMENT

Tangible Resources

Financially, Zara gets strong support from its parent company, Inditex, which has reached revenue of $1.9 billion Euros (Inditex, 2011). Zara has many different trademarks worldwide. In fact, according to Waterlow (2012), Zara recently defeated Louboutin in French court for the trademark on red soles, which allowed Zara to increase their sales from shoe production. Logos and exclusive brands are tangible resources that can help Zara maintain its strong brand identity. With rapid growth in recent years, Zara has become one of the most recognized fast fashion brands in the world (Helm, 2008).

Intangible Resources

Zara has a 200-person professional designer team who constantly update new information on fashion trends for Zara in order for them to continuously pursue the fast fashion market (Inditex, 2011). In addition, efficient information technology communication systems help Zara to be trendy (Mihm, 2010). Also, integrated IT systems allow for a strong relationship between Zara’s designers, suppliers, and manufacturing facilities. Zara has a unique in-store inventory model which gives Zara a competitive advantage on brand image, as they continue to be seen as a company that can rapidly change and keep up with changing fashion trends. Rapid inventory turnover also brings a sense of freshness and exclusiveness to customers (Caro & Gallien, 2010).

Capabilities

In order to give customers a fast fashion image, Zara creates a time-compressed production process. It only takes four weeks for a cycle, from design to availability in stores, instead of the traditional six-month cycle (Mihm, 2010). The vertical integration model (with its own designers, manufactures, and logistics) also brings a flexible structure for Zara to adopt fast fashion (Deschamps, 2012).

According to Mihm (2010), Zara spends very little on advertisement in comparison to their competitors. For example, Gap has many television advertisements and magazine ads while Zara keeps advertisement to a strict minimum, allowing for more cost-effective marketing strategies. Zara focuses on bringing reasonable-quality products to their consumers and creating brand awareness through word of mouth, and maintaining a reputation for rapidly adapting to changing fashion trends.
Core Competencies: Valuable, Inimitable, Rare, Organized to be Exploited (VIRO)

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<tr>
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<th>Fast Responsive &amp; Powerful Designer Team</th>
<th>Unique In-Store Inventory Storage</th>
<th>Fast Fashion Brand Image</th>
<th>Time-Compressed Production Process</th>
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<td>Valuable</td>
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The strong human resources team is very valuable and organized, and new entrants would need a certain amount of capital to imitate it. Although, one of Zara’s main competitors, H&M, also has a solid designer team creating a diverse range of fashion for men, women, and youth (H&M, 2012), Zara’s fast responsive designer team is considered rare in the fast fashion apparel industry. Hence, overall, the fast responsive and powerful designer team is a core competency for Zara.

Secondly, VIRO suggests that the unique model of in-store inventory is valuable, rare, organized, and costly to imitate, and is a key core competency for Zara. Zara ensures that its inventory is fast-moving and adapts rapidly to current fashion trends.

Most importantly, The time-compressed production process is another key core competency for Zara.

CURRENT SITUATION

Summary of Strategies

Business Level Strategy – Cost Leadership

In order to achieve low costs but maintain high fashion, Zara imitates the latest haute couture designs and makes similar clothing with less expensive fabric (Ferdows, Lewis, & Machuca, 2005). Furthermore, for each new design, Zara only produces small quantities to sell. By doing this, Zara can cut losses quickly when a certain design is not popular, and it can also cut inventory costs effectively (Tiplady, 2006).

Corporate Level Strategy – Single Business

More than 95% of Zara’s sales revenue comes from its clothing business. Although Zara also makes home furnishing under the brand Zara Home, this only contributes 2.3% to total revenue (Inditex, 2011).

International Strategies – Transnational Strategy

Zara seeks to achieve both global efficiency and local responsiveness. Due to vertical integration, Zara has more flexibility than its rivals in terms of moving products from the designing
stage to the store shelf (The Economist, 2001). In order to respond to local customer preference changes, Zara transmits customer feedback directly to its massive design team in Arteixo in Spain, facilitated by information technology (Hume, 2011).

According to researchers Sorescu et al. (2011), “the three elements that comprise a Retail Business Model are format, activities, and governance and can help retailers to think strategically about the optimal locus of business model innovation” (p. 13). These three factors are crucial to Zara’s success within a transnational market. For example, the format of activities may vary depending on the technological advances within the industry and the cultural implications of activities in a particular country. Governance and quality structures are vastly different internationally, and Zara must do a thorough strategic analysis before moving into new markets.

One major opportunity for Zara is the implementation of “Web 2.0” into their marketing strategy. Berthon et al (2012) suggest that in the 21st century, we have “creative consumers” that contribute to internet communications about products more than retailers themselves do, through forums, and can be used to create value (p. 263). For example, Zara consumers could contribute YouTube videos in a fashion modeling contest using Zara products, contribute to a forum on their favorite Zara product of the season, or engage in an interactive website or blog in another way. However, Berthon, Pitt, Plangger, and Shapiro (2012) cautioned that both the culture of the country in which social media is being implemented and government regulations for advertising and marketing need to be considered before implementing social media (p. 264).

**Synthesis Summary**

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<tr>
<th>Strengths</th>
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<tr>
<td>1. Effective information technology investments to help reduce costs</td>
<td>1. Resist outsourcing, which creates high labour costs</td>
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<td>2. Fast and responsive communication within the entire supply chain</td>
<td>2. Minimal advertising</td>
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<td>3. Minimal inventory, which creates a sense of exclusivity</td>
<td>3. Low in-store inventory</td>
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<td>4. Inspired, fast, and responsive design team</td>
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<td>5. Up-to-date designs at attractive prices</td>
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<th>Opportunities</th>
<th>Threats</th>
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<td>1. Fast-growing demand from Asian markets</td>
<td>1. Fierce competition from H&amp;M and The Gap</td>
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<td>2. Advantage of Spain joining the EU</td>
<td>2. Increasing labour costs at its own manufacturing facilities</td>
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<td>3. Outsourcing when necessary to further cut costs</td>
<td>3. Changes in consumer behaviour</td>
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<td>4. Launch more advertising campaigns</td>
<td>4. Saturation of retailers of the clothing industry</td>
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MAIN STRATEGIC CHALLENGES

Rising Production Costs

Fast fashion retailers are feeling the pressure of rapidly-rising raw material costs and higher wage demands in producing countries. Cotton spot prices reached new highs in China and Pakistan in 2011. As Bernstein Global Wealth Management discussed in their article “Inditex and H&M: Very Different and Very Similar” (2011), prices of other major raw materials for apparel, like wool, nylon, and spandex, also increased over 20% per year over past 2 years. Profit margins have been further squeezed in major producing countries by rising labour costs, making the situation worse.

Unemployment rates worldwide have decreased sharply in the past two years, as reflected by Euromonitor International’s worldwide unemployment graphs (Euromonitor, 2012). Also, wages have been pushed up to new highs by tighter labour market conditions. One example of this is shown by Chinese apparel manufacturers, of which 90% of 300 manufacturers were forced to increase wages simply to keep their employees (Bernstein Global Wealth Management, 2011). Labour costs in Bangladesh, which is the cheapest commonly-used outsourcing country, were driven up by the government’s decision to raise the industrial minimum wage from $25 to $44 per month (Bernstein Global Wealth Management, 2011). Zara’s profit margin has been placed under pressure by the rising labour and raw material costs, forcing them to employ a cost-leadership strategy, which is difficult to pursue in a rapidly-evolving industry (Sorescu, Frambach, Singh, Rangaswamy, & Bridges, 2011).

Transnational Strategy - Cultural Implications

Expansion on a global scale can increase Zara’s product awareness and market share. However, there are challenges. Compliance with local regulations in other countries is not an easy task due to ambiguous rules and different regulations. For example, in China the government targets foreign firms for inspection before accepting their business. Last year China’s consumer watchdog attacked Zara for poor quality of clothing material, and foreign enterprises like McDonald’s and Carrefour were penalized for very minor lapses (The Economist, 2012). Developing key relationships with local stakeholders is vitally important. On the other hand, the illegal market for imitation brand-name apparel in Asia, products with apocryphal labels of famous brands, is a common challenge that brand-name retailers face.
In addition, illegal markets have increased in recent years. According to Wilke and Zaichkowsky (1999), both low- and high-quality imitations significantly lower the value of a brand, as there is less appeal in owning the real brand for luxury consumers if they are likely to be asked whether the item is an imitation (p. 17). Furthermore, in considering the cultural context, Wilke and Zaichkowsky suggested that it is in the nature of Chinese history to copy and imitate form in order to learn and express artistic appreciation (p. 12). This may suggest a proliferation of businesses that intend to copy popular or brand-name designs.

To make matters worse, consumer brand loyalty may be difficult to find in China. According to Uncles and Kwok (2009), “. . . not even the dominant chain in Shanghai commands exclusive loyalty levels in excess of 25%” (p. 79). For a foreign chain to establish high customer loyalty would be a challenge. Loyalty programs or incentives may help increase repeat customer visits.

**Transnational Strategy - Logistical and Business Set-up Implications**

Having a production base in Europe may not work in emerging markets since shipping costs would further push prices up, so retailers have to develop production and logistics support in newer regions. Both logistical and human resource issues could be challenging, as companies such as Zara would have to build factories, employ workers, comply with local regulations, and operate in a foreign context. Regulations in regards to unions in Chinese markets may also be a challenge.
References


