Pace-Setting Zara Seeks More Speed To Fight Its Rising Cheap-Chic Rivals

By CECILIE ROHWEDDER and KEITH JOHNSON
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ARTEIXO, Spain -- Zara stores have set the pace for retailers around the world in making and shipping trendy clothing.

Now Pablo Isla, chief executive of parent company Inditex SA, says Zara needs to speed up.

As rivals catch up, Mr. Isla is attempting one of the fastest global expansions the fashion world has ever seen, opening hundreds of new stores and entering new markets.

To do that, as an economic downturn threatens sales, Inditex is changing the systems that have driven its success at Zara and its other store brands, to save time and money. Among the innovations, it's introducing new methods to enable store managers to order and display merchandise faster and adding cargo routes for shipping goods.

"There has been a clear change of mentality in the company," Mr. Isla, a former tobacco executive who arrived at Inditex in 2005, said in an interview at the company's headquarters here.

The world's second largest clothing retailer by sales after Gap Inc., Inditex is responding to a predicament shared by other companies that come up with game-changing formulas: Eventually competitors catch up, forcing the pioneers to do even better to keep their edge.

(Please see related story on page B9.) Low-cost carrier Southwest Airlines Co. is making big changes to fend off rivals that have copied its efficient operating model. Inventory-control methods at Wal-Mart Stores Inc. are being mimicked around the world, and Google Inc. is updating its search engine to keep users loyal.

The consumer slowdown is adding pressure. Inditex shares have fallen nearly 24% in the last 12 months, in large part because investors are worried about an economic downturn in Spain, where Inditex generates over a third of its $12 billion in annual sales.

The company is pressing ahead with its expansion plans even as consumers are slowing down. In the U.S., retailers had their worst monthly sales results in nearly five years in January, and some chains are planning to close stores and cut jobs. U.K. retailer Marks & Spencer PLC recently reported its worst quarterly sales performance in two years, and warned the pain could extend into 2009. Next month, Inditex will report results for its fiscal year ended Jan. 31.

The industry is watching the company's logistical makeover. Though it sells inexpensive trendy clothing
"fast fashion" in industry parlance -- Zara has been so successful in luring high-paying customers that luxury fashion brands such as Gucci, Burberry and Louis Vuitton have overhauled their own practices to send new fashions to stores more frequently.

"They're a fantastic case study in terms of how they manage to get product to their stores so fast," Stacey Cartwright, chief financial officer of Burberry Group PLC, says of Zara. "We are mindful of their techniques."

In recent years, competitors across the globe have adopted Zara's methods. Italy's Benetton Group SpA now replenishes stores up to once a week. Los Angeles-based Forever 21 Inc. and Japanese apparel giant Fast Retailing Co., owner of the Uniqlo chain, can get new looks to their stores within six weeks. Even outdoor clothing maker Patagonia Inc. has doubled the number of new styles it offers every year.

As the popularity of cheap-and-chic chains has zoomed, Zara's rivals Hennes & Mauritz AB of Sweden and Mango of Spain have also become fixtures on U.S. shopping streets.

In addition to Zara, which makes up 60% of its business, Inditex owns seven smaller store brands, including the more upscale Massimo Dutti and the youth-oriented Bershka. In the last 12 months Inditex added 560 stores, including entering new markets in Croatia, Colombia, Guatemala and Oman, to reach 3,691 stores in 68 countries. It plans expansion of a similar scope over the next year.

The first Zara store opened in 1975 in La Coruña, a port town near Arteixo in a remote corner of northern Spain. Its two key traits were an eye for customer tastes and a production process that started with the final price and worked backward to the most-efficient production. In the mid-'80s, local business-school professor José Maria Castellano, a technophile, joined Inditex as right-hand man to founder Amancio Ortega Gaona, and the company became a world-class logistical outfit, peddling "fast fashion." The first foreign store, in Portugal, opened in 1989, followed by New York. In 2001, Mr. Ortega took Inditex public and its stores are now on prime shopping streets around the world.

Stores are stocked with new designs twice a week. Collections are small and often sell out, creating an air of exclusivity and cutting down on the need for markdowns. The company ships clothes straight from the factory to stores. Unlike competitors who manufacture most of their wares in Asia, Inditex makes two-thirds of its goods in Spain and nearby countries such as Portugal, Morocco and Turkey. The retailer says the higher labor costs are offset by the flexibility of having production close to its warehouses and distribution centers, which are all in Spain.

At "the Cube," as employees call their futuristic-looking headquarters outside La Coruña, sales managers sit at a long row of computers, monitoring sales at every store around the world. When a garment sells well -- or flops -- they quickly tell designers sitting nearby to whip up fresh designs. In the basement, stylists decide store layouts and window displays. One room is built like a shopping street, its walls lined with lit and decorated store windows that dictate how storefronts will look from New York's Fifth Avenue to London's Regent Street. Every two weeks, new decorations are photographed and emailed to stores to replicate.

To speed up new store openings, Mr. Isla needed to cut start-up costs. Inditex now avoids store openings in slow months such as August. In the past, stores opened year-round, accruing costs from the first day even if sales took longer to build.

Mr. Isla's goal is for Inditex is to reverse a trend of costs growing faster than sales. It met that target in the first half ended July 31, 2007, when costs grew 16% over the same period the previous year, while sales increased 19%.
In another move to cut costs, Mr. Isla installed software in store computers to schedule staff based on sales volume at different times. As a result, more salespeople work at peak times such as lunchtime or the early evening. Inditex says the more flexible schedules shaved 2% off the hours staff work.

Alarm tags are now attached to garments at the factories. In the past, at a big Zara location such as the four-floor store on Madrid's Alberto Aguilera shopping street, 10 people spent an average of 12 hours a week putting on the tags. Now, Inditex estimates, those salespeople spend 3% more time serving customers.

"In the past, a shipment would come in the morning, and the staff wouldn't have it unpacked till noon. They were just giving away three hours of prime selling time," Mr. Isla says.

Shipping papers now label the newest collections "NEWC." Those pieces are often rushed to the shop floor on plastic shipping hangers and only later switched to Zara's customary light wood hangers. Zara regulars know to look for the black plastic hangers with the latest looks, says Dilip Patel, U.K. commercial director for Inditex.

Store managers also use new hand-held computers that show how garments rank by sales, so clerks can re-order best-sellers in less than an hour -- a process that previously took about three hours. These orders arrive, together with new pieces, two days later.

Also, each of the company's various store brands shipped merchandise separately in the past, concerned that mixing even behind the scenes could dilute their images. Combining the brands into larger volumes has allowed Mr. Isla to launch twice-weekly air shipments with Air France Cargo-KLM Cargo. Planes from Zaragoza, Spain, land in Bahrain with goods for Inditex stores in the Middle East, fly on to Asia, and return to Spain with raw materials and half-finished clothes. The company also started new shipments with Emirates Airline.

Despite Mr. Isla's efficiency gains, some experts caution that Zara faces challenges it is not addressing. Keeping a large amount of production close to home, some warn, loses its benefits when a growing number of stores are far away. "The efficiency of the supply chain is coming under more pressure the farther abroad they go," says Nirmalya Kumar, a professor at London Business School.

For now, the company makes up for some of the cost by charging more for goods sold overseas. In the U.S., for instance, Zara clothes cost up to 40% more than they do in Spain. However, that could lead to an inconsistent brand image, a risky strategy in a globalizing world, some critics warn.

Mr. Isla says that when he joined the company, he considered a logistics center in Asia, where the company produces around a third of its goods, but decided it would only make sense if Zara had more stores in the region. He says the group's current logistics capacity will suffice until 2013.

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