

Principles of Supply Chain Management
Crandall, Crandall and Chen
Instructor's Guide
Company Profile

Chapter 2 – Supply Chains as a System
Inditex - Zara

This chapter is about a supply chain as a system. A system is a regularly interacting or interdependent group of items forming a unified whole toward the achievement of a goal (Blackstone 2010). A supply chain is a system that moves product from the point of origin at a mine or farm, through a series of value-adding activities such as manufacturing and distribution, until the product reaches the ultimate consumer. The supply chain also moves information upstream from the customer back to the supplier and also downstream from suppliers to customers. The supply chain assures the flow of funds from customer to supplier. In order to achieve these flows effectively, the supply chain is composed of links between individual participants (members) of the supply chain, forming a system to move goods, information and funds.

Zara shows its revamped image based on four guiding principles: beauty, clarity, functionality and sustainability. Simplicity is the byword throughout the store as part of Zara's mission to bring customers into direct contact with fashion. Inditex opens its first stores in Armenia, Bosnia-Herzegovina, Ecuador, Georgia and the Former Yugoslav Republic of Macedonia and reach 6,000 stores worldwide.

http://www.inditex.com/en/who_we_are/timeline

Inditex is a company that has built a supply chain system that is extremely successful. They were first listed in the Gartner Top 25 Supply Chains in 2012 when they were ranked No. 19. In 2013, they moved up to No. 15. (Gilmore 2013) They have reached this level of recognition by developing a supply chain that emphasizes fast response times and agility in meeting variability in their marketplace – high fashion clothing. Their growth confirms their success. From their beginning in 1975, they have grown to over 6,000 stores throughout the world.

Zara is their leading brand, with nearly 2,000 stores, serving 86 markets and generating net sales of €10,541 million, or approximately \$13.7 billion. (Inditex 2013) They do this by managing a supply chain with the almost unbelievable response time of two weeks (instead of an industry average of six months) from the time they begin to design the new product until that new product is available in the store. They use a pull system that produces what customers want instead of a push system that designs a product and then tries to figure out how to sell it. Their somewhat unorthodox supply chain system is designed to be agile and react quickly to changes in the marketplace.

They are able to achieve a fast response through developing and maintaining “shared situation awareness, a team’s ability to recognize a pattern in a fluid situation and use it to anticipate what might happen next.” (Sull and Turconi, 2008, p.8) Teams develop shared situation awareness in three steps (1) observe the raw data, (2) spot patterns to form hypotheses about how the situation might unfold, and (3) test the hypotheses (Sull and Turconi, 2008).

The employees at Zara achieve their results through a combination of cultivating customer awareness, communicating between stores and corporate, collaborating among organization functions, and committing to meet rigid design, production and delivery time schedules.

Information gathering. At the store level, the store manager is responsible for finding out what customers buy and what they don't buy. They do this without a plethora of written reports, but by talking directly with salespersons and observing the racks to see what is selling. The manager and employees even look at the clothes tried on but not bought to see if they can detect patterns – colors, styles, etc. The

store manager is responsible for deciding what items to carry in the store, not a centralized computer. They communicate upward through regional and country managers, most of whom have been store managers, to the central design teams. At the same time, corporate-level designers are also reviewing daily sales to determine trends or patterns. The information gathering combines hard data with informal inputs to get a sense of the changes taking place among consumers. One of the strengths of the system is that new designs come quickly and on a regular schedule.

Product design. Ideas for new items flow from the stores to headquarters at LaCoruna, Spain. There, teams consisting of designers, marketing specialists and production planners collaborate to convert the idea into reality. The layout of the building is designed to facilitate the “togetherness.” There are three long building areas – one each for men’s, women’s and children’s clothing. Within each, there are no offices, only open spaces with desks and tables to encourage cross-functional discussions. Employees are hired to be team players, not prima donna designers. The team comes up with a design concept, has a prototype sewn, and employees model the clothing item. If the item doesn’t meet approval, it is discarded; if it does, it goes on to the production area. Only about 25% of the prototypes finally reach the stores; however, the teams generate over 10,000 new designs each year (Petro 2012). Team members are changed often to encourage the flow of new ideas. They also test their prototypes by displaying them in an area called *Fashion Street*, located in the same building as the designers. *Fashion Street* is a long parade of stores, with existing and proposed shop formats. This makes it possible for architects, designers and visual merchandisers to visualize not only the clothing but the store format and layouts to see how they work together as a system. (Sull and Turconi 2008)

Manufacturing. Zara is able to move the new designs through the manufacturing phase because they use a number of local subcontractors in the LaCoruna area. Approximately 50% of their manufacturing is done close by in Spain, Portugal, and Morocco, for the fashion items that have short life cycles and which they want to move into stores quickly, with minimum inventory. Some of these factories are highly automated; hundreds of others are small subcontractors who can respond quickly to Zara’s time schedules. The factories also operate with Just-in-Time production systems developed in cooperation with logistics experts from Toyota Motor. More staple items, such as T-shirts, are outsourced to low cost countries such as Eastern Europe, Africa and Asia. (Capell 2008) Zara also produces in small batches with high variety. They keep some excess capacity in the factories to be able to move quickly when new designs are needed. (Ferdows, Lewis and Machuca 2004) In 2012, they purchased from a total of 1,434 suppliers with 446 in the European Union, 136 in Non-EU Europe, 48 in America, 112 in Africa and 672 in Asia. (Inditex 2012 Annual Report, p. 63)

Distribution. Once the clothing is produced, it is shipped to the stores, twice each week, to keep the stock fresh and the inventory low. Their logistics system provides continual replacement and guarantees that stores will receive new products in no more than two days (24-36 hours in Europe and 48 hours in the rest of the world). (Inditex 2012 Annual Report, p. 43) Many of the items are already priced and on racks to reduce the time required at the stores to make them ready for sale. The distribution of goods is on a rigid schedule to assure new items arrive in the stores quickly and on a definite schedule. Stockouts offer an opportunity to introduce new items and encourage customers to visit the store often.

Stores. In 2012, their 1,763 stores were located throughout the world, with 1121 in Europe, 218 in America, and 424 in Asia and the rest of the world, including 140 in China and 88 in Japan. (Inditex Store Location 2013) Their stores are spacious, 10,000 sq. ft. or so, but are not crowded with endless racks of clothes. In fact, there may be a limited number of items, conveying the impression that a customer should buy now, because it may not be there later. (Ferdows, Lewis and Machuca 2004) Stores are located in fashionable, high traffic areas. The company describes their new store concept, introduced in 2012 this way:

“This innovative interior design was presented at the brand’s 666 Fifth Avenue store in New York. The new image revolves around the principles of beauty, clarity, functionality and sustainability. The store turns around two long axes, hallways, or ‘walkways’, leading to individualized spaces or ‘cubes’ on each side, in which the various collections are shown in an individualized way. The wood of the furniture has been finished in textures that are reminiscent of fabrics such as linen or silk, in elegant

and neutral colours. In addition, with regard to sustainability, the store is in line with the guidelines governing the Inditex Group's eco-efficient stores." (Inditex 2012 Annual Report). In addition to the Fifth Avenue location, in 2012, they opened stores in the Park House area of London at 460-490 Oxford Street and on no. 92, Champs Elysées, Paris.

Results. Does this tightly integrated supply chain produce results for Inditex and Zara? There are a number of indicators that it does. Inditex SA is now the world's largest clothing retailer with revenue of over \$19 billion in 2012. It has higher inventory turns, fewer markdowns, and a higher average gross margin on sales than its competitors. Although they operate contrary to some of the conventional practices of clothing retailers – less low country outsourcing, more spare production capacity, air shipments instead of ocean carrier, and a higher concern for supplier working conditions – they end up with a higher return on investment.

System. They have a self-reinforcing system built on three principles: Close the communication loop, stick to a rhythm across the supply chain, and leverage the capital assets to increase supply chain flexibility (Ferdows, Lewis and Machuca 2004) Zara puts all of the pieces together into a system that gets the job done. Sanford C. Bernstein offers advice to rivals who hope to mimic Inditex's results: "Don't follow the Zara Pattern halfheartedly. The Inditex way is an all-or-nothing proposition that has to be fully embraced to yield results." (Capell 2008)

References

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