

Sector View

Consumer durables

FASHION: Towards more local sourcing

	1 M	3 M	6 M	31/12/15
Consumer Gds	5.3%	-0.4%	4.6%	-3.0%
DJ Stoxx 600	5.8%	5.4%	10.9%	-1.9%

*Stoxx Sector Indices

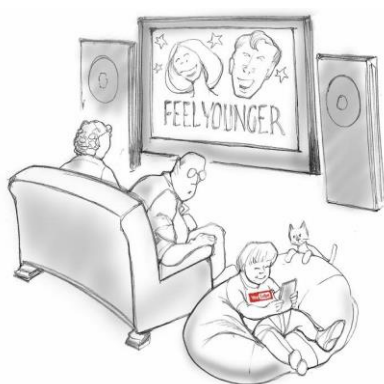
Companies covered

Company	Rating	Market Cap.
ADIDAS GROUP	NEUTRAL	EUR136
Last Price	EUR143,7	EUR30,064m
H & M	NEUTRAL	SEK295
Last Price	SEK259,9	SEK430,153m
INDITEX	BUY	EUR38
Last Price	EUR32,015	EUR99,780m
YOOX NET-A-PORTER	BUY	EUR33
Last Price	EUR27,04	EUR3,670m
ZALANDO	NEUTRAL	EUR39
Last Price	EUR35,755	EUR8,841m

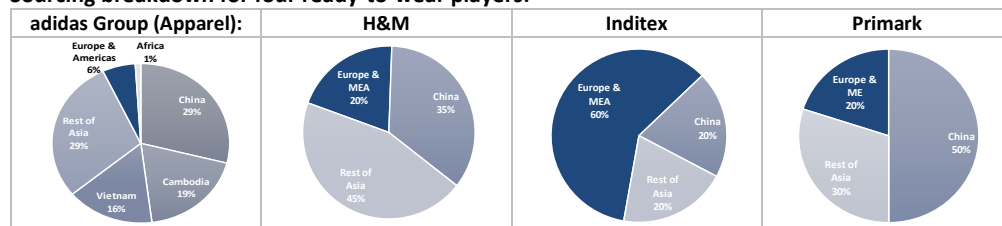
A few days ago, the UK's largest online fashion retailer ASOS announced its plan to double its UK manufacturing (~4% of total production currently). This quest for local sourcing is being increasingly adopted by apparel groups mainly to reduce lead times and decrease their exposure to USD/CNY currencies. ITX's unique supply chain (60% of production in "proximity countries") is definitely a key competitive advantage but for the other groups, the rebalancing would take time.

ANALYSIS

- **Most of the ready-to-wear (RTW) brands locate their manufacturing in Asia...**, as seen in the following charts: nearly 80% of **H&M's** sourcing is from Asia, which is close to that of **ADS Group** (~93%) and **Primark** (~80%). China still accounts for a big part of this Asian footprint, representing ~29% of ADS' apparel production, 35% for H&M and half of Primark's sourcing. Yet, these groups have been impacted by increasing labour costs locally as salaries in the textile industry have been growing at double-digit rates every year over the past decade. Consequently, production was gradually moved to SEA countries (Vietnam, Indonesia, etc.), with more attractive labour costs.
- **... making their supply chains more complex and less agile.** Indeed, supply chains are not responsive enough considering lead times of 3-6m to manufacture and ship their collections in stores. These groups are therefore highly sensitive to shifts in demand (fashion changes, weather conditions, etc.).
- **ASOS to double its UK manufacturing from 4% to 8% in the MT.** ASOS was not spared by these issues as production in Eastern Europe, Turkey and Asia accounts for approx. 80% of ASOS' own brand (~45% of group sales). Since it is an online fashion retailer, its success also relies on fast and efficient execution and doubling UK sourcing will have several advantages: (i) more affordable production costs thanks to the plunge in the GBP, (ii) shorter lead times as 70% of ASOS' sales are generated in Europe and (iii) efficiencies and cost savings (lower USD/GBP transactional exposure, lower logistics costs) that could be reinvested in price cuts to increase ASOS' competitiveness.
- **adidas Group's Speedfactory and Futurecraft 3D projects.** At the moment, it typically takes 18m for ADS to develop and finally sell a new style of shoe. But the German group is speeding up its supply chain thanks to the **Speedfactory** (fully automated shoe plant) and **Futurecraft** (3D-printing) projects. Speedfactory, its first robotic shoe manufacturing plant in Germany (Ansbach) is now up and running and a second factory will open in Atlanta (US) next year. Production capacity is set to be modest in the ST (~1m pairs vs. 301m pairs produced by ADS every year) but it due to ramp up as the Group intends to grow this **Speedfactory** network across the world over the MT. The aim is to bring ADS products as quickly as possible and offer unprecedented customisation opportunities to consumers, while saving costs and improving its level of sustainability.
- **ITX really stands out with 60% of its manufacturing in European/neighbouring countries** (Turkey, Morocco, Africa). This local sourcing enables ITX to be highly responsive to any changes in fashion trends and to keep its markdowns low (c.15%-20% vs. industry average of c.30%-40%) together with a very low unsold inventory rate (c.10% vs. c.15%-20% for the industry). In our view, this responsiveness is ITX' main competitive advantage, not only compared with traditional retailers but also with the internet players.



Sourcing breakdown for four ready-to-wear players:



Source: Company Data; Bryan, Garnier & Co ests.



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