

INDUSTRY OUTLOOK 2017

# 5 Key Things We're Watching

INSIDE FASHION





# 5 Things We're Watching this Year

## OUTLOOK 2017

We are experiencing significant market changes: shifts in consumer attitudes and purchasing habits, geo-political changes, and new developments in supply chain management are keeping executives in the apparel and footwear industry on edge as we head into what looks like it will be an 'interesting' year.

We identified five key areas that we feel have the most impact on the apparel and footwear supply chain this year. These are not the only things that will impact the supply chain, but they are important and we see them as being long-term trends. Unlike materials prices, for example, which can fluctuate throughout the year or over several years, the factors discussed here are seen as being slower, long-term shifts.

## KEY LONG TERM TRENDS

**Smaller, more frequent orders**

**Quality becomes a priority**

**China becomes a buyer**

**Vietnam rising**

**New routes to new markets**

*We are facing a season of uncertainty - in terms of the economic environment, political risk and shifting consumer preferences.*

*There is also the start of a shift in export markets as Asian suppliers look to diversify into new markets and as Asian nations become consumer markets.*

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# Downsizing Orders

## Order sizes are Continuing to Shrink

There continues to be downward pressure on order sizes. In some cases, the total amount a supplier is getting from a client might be the same within a year, but often times it is not. In general, we are seeing a lot of downsizing – even from the big brands and retailers. Everyone wants more flexibility and less carrying costs. On the retail side, buyers want to reduce the risk of carrying inventory, while also being able to respond quickly to new trends and restock bestsellers. On the consumer side, people are shopping less frequently and buying more thoughtfully. The “shop until you drop” phenomenon that fueled the big volume business upon which Asia’s garment industry was built, is steadily eroding.

In China, as well as most of Asia, factories were originally set up to handle big volumes of fairly basic garments. Back then, factories could get orders for ten thousand dozen of a garment in one style and a few colors with six month lead times.

Now what we see happening is an entire business model, which has been set up and running for decades, facing a radical shift in the market. Today buyers are saying to those same factories: “We need small orders, we need more complex orders, we need faster delivery.”

The feedback that *Inside Fashion* has gotten from Asian mills is that order sizes have decreased by about 20-30 percent over the past three years.

## IMPACT ON INDUSTRY

For many factories, re-engineering their business to meet these new demands is too big of a hurdle. For even the most agile, it is a long-term process, yet they still have to survive in the short term. To hold on to some of the volume orders, Chinese factories are drastically cutting their prices. Manufacturers from other nations are complaining about this, but companies will do what they have to do in order to stay alive.

At the same time, we are seeing more of the more sophisticated factories trying to re-engineer themselves to become high-end producers. They are trying to leverage their advanced skills and go after more complex orders where there is more price flexibility.

Moving up market is a critical part of the equation. In order to offset the reduction in order size, factories are looking to trade up to higher value orders. That is exactly what an increasing number of the best manufacturers are doing.

We are also seeing China becoming more of an artisan producer. One supplier told us, “We are trying to become the Italy of the East.” Even Bangladeshi manufacturers are looking for better orders these days. It is an important trend and one that we’re taking a deeper look at in our next issue of *The Current Situation in Sourcing*.



# China Becomes a Buyer

## From Supply to Buyer

For over two decades, China has been the world's factory, the go-to place where you can get anything made – usually at a very competitive price.

That's changing, and now China is becoming a buyer of consumer products. A very *big* buyer.

Despite naysayers in the media, China's economy is growing steadily. Even if it is growing at a decreasing rate, it is still growing at an enviable 6-7 percent annually. While the very high end of the market might have seen a downturn in the property sector and other financial areas, the mainstream market continues to enjoy a stable and prosperous economic environment.

There is a very high level of employment in China that helps to give Chinese consumers the confidence to spend, and there is a lot of pent up demand for consumer goods. While the China market is still well behind the US and Europe in terms of the purchasing power of its consumers, it's growing quickly – and it is 1.3 billion people strong!

Looking ahead, China will need to use more of its domestic manufacturing capacity to serve its home market.

## IMPACT ON INDUSTRY

For suppliers outside of China, there will be growing opportunities to sell to China's domestic brands. Already, leading Asian and European suppliers are finding a growing market in exporting to China. European mills now tell us that Chinese buyers are willing to pay a premium for better quality materials. They have told us, "When Chinese buyers see something they like they buy and accept the price, in contrast to Western buyers where price always comes into play."

Part of the reason is that in China's hyper competitive domestic retail market, it really does come down to 'differentiate or die' and fabrics and trims can make a vital difference in a garment's consumer appeal.

On the downside, payment is still a problem in China's domestic market. Gradually, this will improve as the banking system and legal system develop.

China-based suppliers are selling an increasing part of their production into China. "Many report selling up to 30-50 percent of their production domestically, up from 0-10 percent three years ago. We are also seeing foreign suppliers getting serious about selling to Chinese brands," said Ms. Singer, explaining that this is something she's hearing more frequently from Asian and international mills.

Long term, we are likely to see more of a floor on prices. There will be more buyers competing for materials and factory capacity



# Vietnam Rising

## An Alternative to China

Vietnam has established its niche in the global supply chain. On the one hand, it is less expensive than China. On the other hand, it has better skills than Bangladesh and is more efficient than Cambodia. It can also handle orders that are too small for Bangladesh.

The nation's productivity is continuing to improve and workers are willing to do overtime and eager for advancement.

While most of the talk surrounding Vietnam during the past two years has centered on the prospects of duty-free access to the U.S. under Trans-Pacific Partnership Agreement, the nation will still be a key exporter to the U.S. market because its prices and productivity—even without duty-free status—are still competitive for many items.

Further, with newly signed free trade agreements with Europe, Russia, and many Asian countries, Vietnam is poised for steady growth.

## IMPACT ON INDUSTRY

The thing that we're watching in Vietnam is wages. A rush of investment from multi-national companies (not only in the textile industry), as well as the investment in increasing factory capacity, will put upward pressure on wages (as we have seen in China).

Already factories are complaining about increases in the actual wages they need to pay to attract good workers.

The more forward thinking factories are investing in automation to boost productivity.



# The Quest for Quality

## Fewer and Better

This is something that is more on the consumer side. Inside Fashion does a lot of consumer research, and when we do our research, it's all open-end questions. It's a challenge to analyze the data, but this is the only way that we can understand what's in the consumer's heart and mind, which is a critical part of developing products that they'll want to buy

We are constantly hearing about issues with quality. People are very quality aware; the internet has enabled people to understand what makes a product better, and to read reviews of it from other people.

In our seminar "Why Apple Wins at Retail – and How You Can Too" we pointed out that Apple changed the consumer market when in 2006 they introduced the iPhone. It was the first time most mainstream consumers were able to experience a luxury product. Before that, luxury was far removed from the mass market. When the iPhone launched in mobile phone shops around the world, consumers got to experience quality first hand. And the retail world has not been the same since.

## IMPACT ON INDUSTRY

Since that first iPhone entered the market, consumers started to care about and understand quality.

Today, whatever products we are making, we have to figure out how we can add quality; how we can trade up a little bit; how we can find a way to personalize the product.

We have to move away from basics and into something that adds value. People are buying fewer, but better. We have to keep that in mind when designing products.

Quality includes fabric, durability workmanship and fit. Today's consumer cares about all of these things.

# New Routes to New Markets

## China's Growing Railways

China, as both a massive global exporter, and increasingly an important importer of high end products, has spawned the development of new transportation routes. Speed to market remains important. There is a trade off between price and speed, and increasingly speed is winning. This has created the impetus to the development of alternative routes and more sophisticated logistics.

One thing we've been watching for a number of years is China's Eurasia rail, a rail link that goes from China across middle Asia into either Russia or Europe.. Of course, China already has its "one belt, one road" project, where it aims to connect western China with the inland central Asian countries.

The cost of shipping goods using the Eurasia rail is in the middle between ocean and air. At this time it hasn't taken a lot of garments or home textiles shipments, instead it's seeing more traffic from tech and other sectors. However an increasing number of apparel manufacturers are testing it for shipments to Europe – and the feedback is positive.

We feel it is going to be important in the development of northern and western China, which always had the hindrance of being isolated from the coastal cities, making it hard to create an efficient supply chain.

## IMPACT ON INDUSTRY

This will be impactful in developing inland and western China, as well as providing opportunities for shipments from Europe into China.

There are many other railways under discussion, however at this time the Eurasia is the most successful.

The trans-Asia railway looked promising however it runs through too many countries (from China to Singapore) and so everything from investment to maintenance is very complicated. For now, the project is essentially stalled.



R. Jane Singer is Director & Head of Market Intelligence at Inside Fashion (part of JDT Research Ltd). The company provides market insights into the apparel and textile industry – from sourcing

through to retail. Inside Fashion's market reports help some of the biggest manufacturers and buying offices understand 'the why behind what's happening' in the market.

Reports include The Current Situation in Sourcing, Inside Fashion, Frontline Reports and Consumer Lab.

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