BUSINESS MODELS: FROM DESIGNERS TO FAST FASHION RETAILERS

Module 2

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Business Models

Warning!

This document does not contain the interviewed companies' profiles, check the links at the beginning of this module for their specific slides.

M2 - Content

Business Models

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Introduction

Why are Business Models Important?

What is a Business Model?

> Luxury brands
> Fashion designer brands
> Premium brands
> Vertical retailers in the mass markets

Fashion Market Segmentation

Price is the most common criteria to segment a market.

The **fashion pyramid** has five market segments:

> Haute Couture

> Ready-to-wear

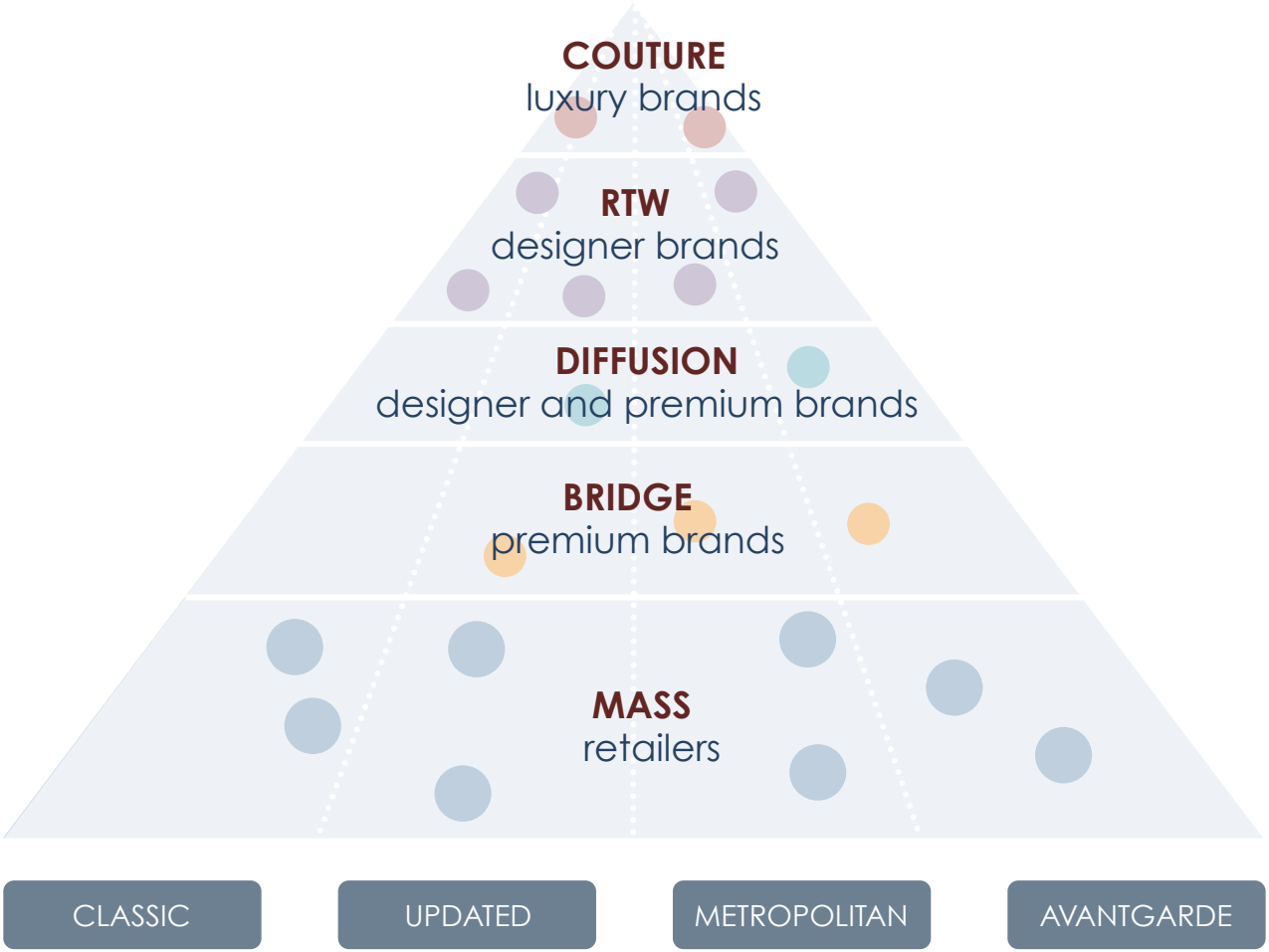
> Diffusion

> Bridge

> Mass Market

Fashion Market Segmentation

The Fashion Market Segmentation Pyramid



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Fashion Market Segmentation

The Fashion Market Segmentation Pyramid

Value proposition offered to customers

> Price

> Creativity

> Quality

Each element is increasing
going to the top of the pyramid

Fashion Market Segmentation

Haute Couture

> Price: Most expensive, it could be 10 times higher than the average market price

> Creativity: Maximum level,
always made-to-measure

> Quality: great attention to details,
maximum level of craftsmanship,
pieces of art

> Use: Mainly special occasions especially in the evening

> Target: Very few people, celebrities
international clients

> Idea
Build the image of the brand
Sell the dream

Fashion Market Segmentation

Ready-to-wear
also called Prêt-à-Porter

> Price: high price,
5 to 3 times higher than the average market price
> Creativity: high level of creativity,
designer's expression through the fashion show
> Quality: attention to details, industrialization,
usually "made in…"

> Use: wider occasions of use,
from daily to important events
> Target: wider selection of people, celebrities
international clients

> Idea
Develop the image of the brand

Fashion Market Segmentation

Diffusion
or second young lines

> Price: Priced 3 to 2 times higher than the average market price
> Creativity: inspired from ready-to-wear
> Quality: wider volumes of production,
production outsourced,
country of origin is not a key success factor

> Use: casual, "sportier"
> Target: younger audience,
wider than RTW,
mix of retail and wholesale distribution

> Idea
Expand the target audience

Fashion Market Segmentation

Bridge
born in the USA with department stores

> Price: right value for money, 2 to 1.5 times higher than the average market price
> Creativity: trendy not too radical/extreme products
> Quality: production outsourced,
right delivery in stores

> Use: mainly daily occasions
> Target: usually a mix of wholesale and retail distribution, both international and local brands with local customers

> Idea
Connecting the high end to mass market
Right marketing mix (product, communication, service)

Fashion Market Segmentation

Mass Market

> Price: below the average market price

> Creativity: basics or fashionable items depending on business model

> Quality: importance of costs control

> Use: different occasions

> Target: different targets,
from teenager to sophisticated women

> Idea

Supply chain management is key

Segmentation is the new trend

Masstige communication

Role of the store

Entertaining shopping experience

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Business Models Framework

Business Models

"***Business models describe, as a system, how the pieces of a business fit together***"
Magretta | 2002

The way you design:
> customers
> communication channels
> distribution channels
> Supply chain
> how you build the revenue model

Business Models Framework

The Four Pillars

Customers [Who?]

The **value proposition** (exclusivity, value for money, fashionability, status…) that is also identifying the segment of clients targeted by that value proposition (affluent, fashion victims, connoisseurs…)

Product Offer [What?]

The **product** offer that is delivering a certain value proposition (timeless/ iconic leather goods, fast fashion apparel, designer shoes...)

Infrastructure [How?]

The way the **value chain** is organized (degree of vertical integration, role of key suppliers, international scope)

Revenue model

How a company will **earn income and generate profits** (margins versus volumes, licensing fees..)

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Business Models Framework

Market Segments and Business Models

Market segments and business models from bottom to top

> Mass Market: Mass Basic Retailers and Mass Vertical Retailers

> Premium: Premium Brands and Fast Premium Brands

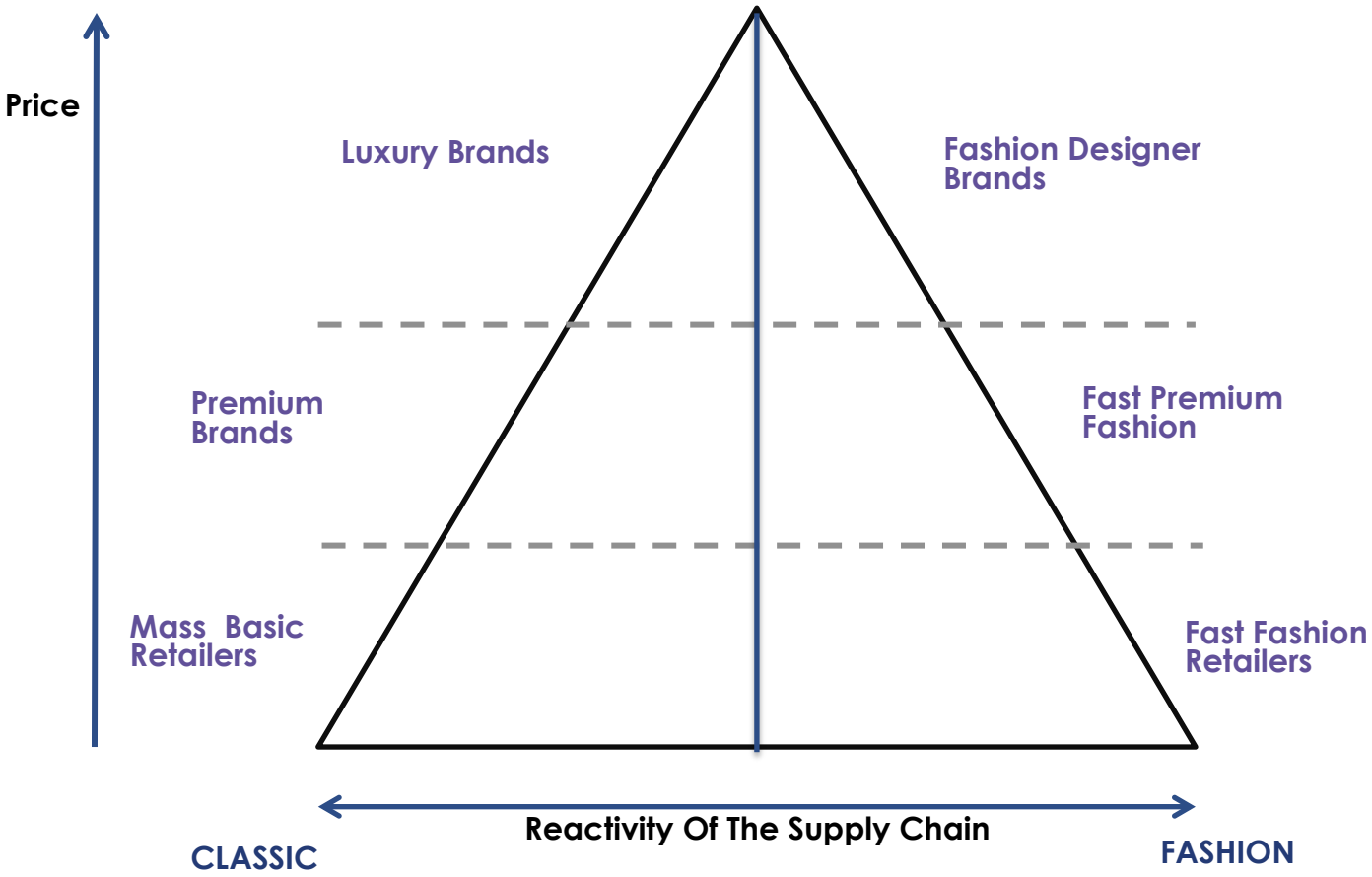
> High-end: Luxury and Fashion Designer Brands

Value proposition defined by:
> Price
> Creativity
> Exclusivity
> Image
higher level from bottom to top

Responsiveness of supply chain to fashion trends and seasonality
Classic > less responsive
Fashion > more responsive

Business Models Framework

The Business Models Framework



Business Models Framework

Four Business Models

> Luxury brands
> Fashion designer brands
> Premium brands
> Vertical retailers in the mass markets

How are they organizing these four pillars
> Who
> What
> How
> Revenue model
to have a sustainable positioning
and an income flow?

Luxury Brands

Definition

Oldest business model
Originated in France

Hard luxury categories
> Watches
> Jewelry
> Leather goods
> Silk accessories

Value proposition of luxury and what customers expect:
> Timelessness
> Heritage of the brand
> Uniqueness
> Exclusivity
> Craftsmanship

Luxury Brands

"***The main strength of Hermès is the love of craftsmanship…We see ourselves as creative craftsmen…The philosophy of Hermès is to keep craftsmanship alive***"

Axel Dumas, CEO Hermès

"***We call Cartier a maison, not a brand. We have the mission to be an artist and create jewelry and watches that are universal and eternal. Universal in that it appeals to connoisseurs all over the world; timeless in that it is revered and dreamed of today and also 50 or 100 years from now***".

Stanislas de Quercize, President & CEO of Cartier

Read an interesting article about Hermès | http://www.forbes.com/sites/susanadams/2014/08/20/inside-hermes-luxury-secret-empire/

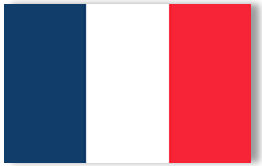
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Luxury Brands

Value Chain:

companies are usually vertical integrated
> Design
> Manufacturing
> Retail

French brands:
usually fully integrated



Italian brands:
focused on design and manufacturing
have a network of selected suppliers



Luxury Brands

Characteristics of Luxury Brands

Center:
The brand with its heritage and tradition
VS
Fashion brands center:
The designer persona
with the personal interpretation and creativity
expressed in the fashion show

Timing:
Born two centuries ago in France, Italy and Switzerland

"***Ferragamo is one of the few brands with a long history, heritage, and absolute integrity… really the epitome of what luxury should be in the new century***"
Michele Norsa, CEO Salvatore Ferragamo

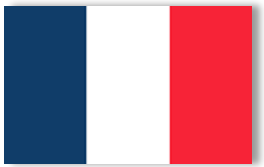
Read an interesting article about Salvatore Ferragamo |
http://luxurysociety.com/articles/2013/07/in-conversation-with-michele-norsa-ceo-salvatore-ferragamo

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Luxury Brands

Geographical and Cultural Differences in Value Chain Design

French brands:
Vertically integrated in production and distribution
> Louis Vuitton, Hermès



Italian brands:
Focused on design and manufacturing,
not totally integrated in distribution,
mix of retail and wholesale channels
> Tod's, Ermenegildo Zegna, Salvatore Ferragamo



American brands,
Referring to accessible luxury,
Focused on design and retail
Not integrated in manufacturing
> Coach, Michael Kors



Luxury Conglomerates

Luxury Conglomerates

in the last fifteen years their establishment is one of the most interesting phenomenon in terms of governance and business models

In fashion and luxury

> LVMH

> Kering

> Richemont

Luxury conglomerates

are diversified groups, or holdings, with a very wide portfolio of brands in different product categories

that manage their portfolio in order to enjoy economies of scale backward while maintaining brands independence in the front-end

Luxury Conglomerates

Luxury Conglomerates

Some of the luxury brands decided to enter in the portfolio of conglomerates

Such as the Italian:

> Loro Piana
> Bulgari
> Emilio Pucci
> Pomellato

Some advantages:

> Savings on media spending
> Better accessibility/negotiation on retail location
> Professional management

A key success factor is how to mange a portfolio

Luxury Conglomerates

Italian Indipendent Brands

Many Italian brands are still independent, such as:

> Ermenegildo Zegna
> Tod's
> Giorgio Armani
> Salvatore Ferragamo
> Prada

They are family owned

Designer Brands

"***I always wanted to be different.***
I always wanted to be first"
Miuccia Prada

Fashion designer brands
anticipating and creating new trends
the core business is clothing

Designer Brands

For fashion designer brands **clothing**
is the or one of the most important source of the revenue

Role of the designer
is key for assuring to the brand a consistent positioning in the market place

Designer (Art Director)
> creates new collections
> is the final decision maker
for every single aspect of the brand

Designer Brands

Fashion Designer Brands

Started in the ready-to-wear now cover different segments from Upper Bridge to Haute Couture conveying always the idea of seasonality

Business Models

Fashion houses started with small *maisons* where the designer had the creative role and there was a strong use of licensing for manufacturing and distribution

With the development of the business they decided to take the direct controls of their clothing lines

Licensing

Has a strong use in eyewear, fragrances, watches.. where different levels of expertise are needed

Designer Brands

Fashion Designer Brands

Include usually

> RTW line, highest in term of price positioning and seasonal creativity

> Diffusion line, second line more affordable and more casual

Designer Brands

Repositioning Strategy of Second Lines

In the past second line were very successful and the major source of revenues

With the increasing competition of fast fashion retailers something changed and designers brands understood that to be competitive they need to focus

As a consequence in the last years some of the designer brands decided for one of the two choices:

> Shut down the second line
despite the big success

> Transform the second line in a RTW brand
with a strong and autonomous personality
as the master brand

Premium Brands

Premium Brands
also called **Contemporary Brands**

A heterogeneous group of companies
born under an entrepreneur's vision
with the control of manufacturing
and distribution aspects

Characteristics:
Most of them born with a fantasy name, also some designer brands with a more affordable concept, but not too extreme in terms of fashion
with a right value for money, a good customer service and a strong communication strategy, extensive use of digital media

Competitive advantage based on marketing mix

Premium Brands

Premium Brands

They mainly occupy the Bridge segment and represent a very fast growing cluster today because:

> offer the right mix and match products

> are perceived less as a commodity compare to the Mass Market

> are more affordable than designer brands

Vertical Retailers

Vertical Retailers

this business model has grown a lot
in the last decade all over Europe and globally

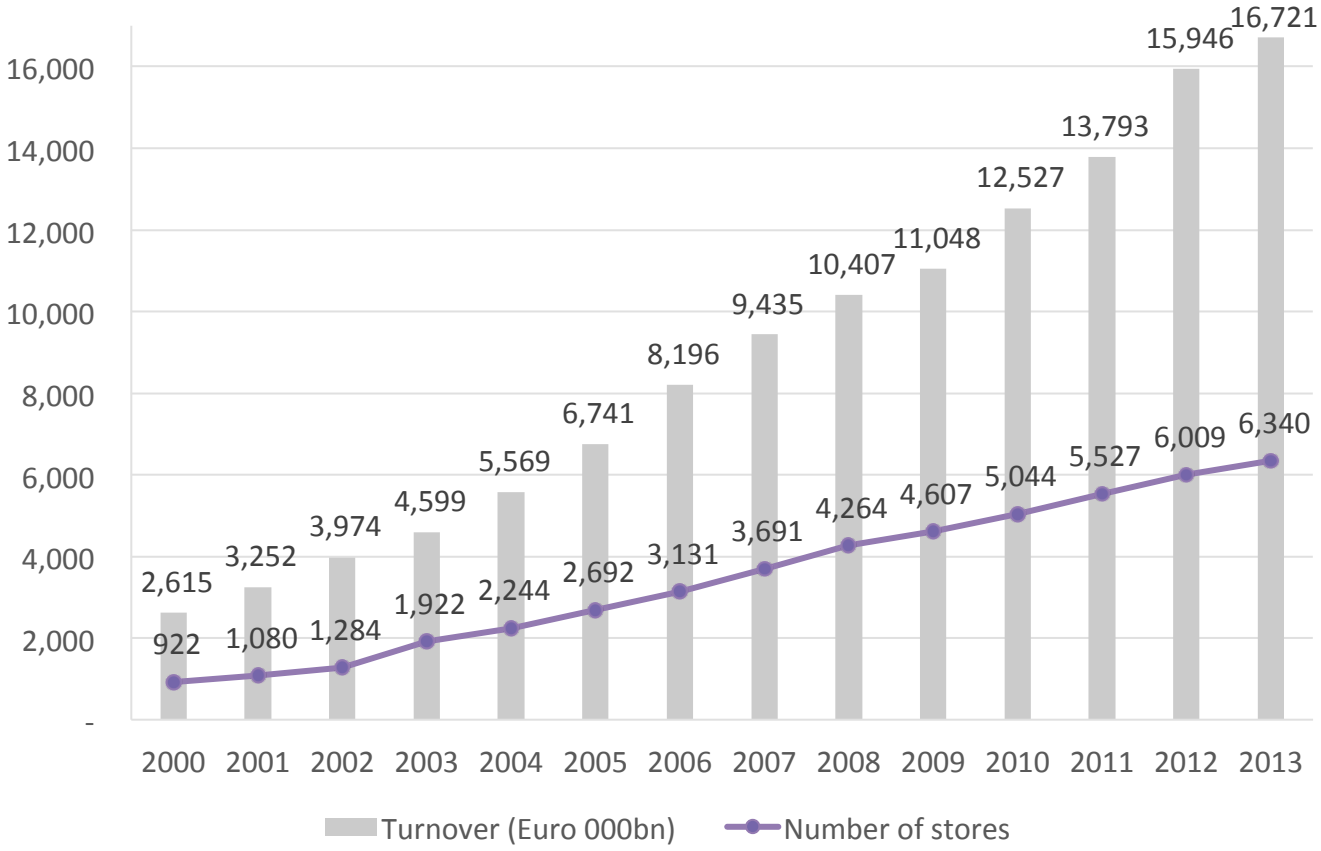
Examples are:
> Zara
> H&M
> Uniqlo
> Mango
> Promod
> The Gap

Not limited to retail and distribution activities, but integrate also design process,
brand image and communication

The value chain can be more or less responsive to the market trends, that means incorporate different levels of fashionability:
> **Mass basic retailers**
> **Fast fashion retailers**

Vertical Retailers

Inditex Number of Stores and Turnover



Graphic Based on Inditex Public Data

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Vertical Retailers

Mass Basic Retailers

offer a wide products range
with many iconic styles and carry overs
in large and welcoming stores
at convenient price

Example:
> The Gap
> Uniqlo



Vertical Retailers

Fast Fashion Retailers

offer a flow delivery of
new fashionable merchandise
in large and welcoming stores
at convenient price

new fashion products every two weeks

example:
> Zara

Vertical Retailers

Vertical Retailers (How)

have different percentage of vertical integration

high degree of vertical integration:
manufacturing, design, distribution and retailing
> Fast fashion retailers such as Zara

control of only some activities:
do not own factories, but have production offices next to the main suppliers in local counties
> Mass basic retailers such as H&M

Vertical Retailers

Fast Fashion Retailers: Zara

is part of Inditex Group

the company brings a great innovation:
> Customer centricity
> Products lifecycle of two weeks,
small production, small orders
and frequent deliveries
> Efficient logistics, strong investments in 4/5 logistic platforms in Spain
> Flexibility, close to the market in terms of manufacturing, in Spain and Europe

Vertical Retailers

INDITEX

ZARA 1975	**Pull and Bear** 1991	**Massimo Dutti** 1991
Bershka 1998	**BRANDS**	**Stradivarius** 1999
Oysho 2001	**Zara Home** 2003	**Uterqüe** 2008

Read an interesting article about Inditex|
http://www.ft.com/intl/cms/s/2/a7008958-f2f3-11e3-a3f8-00144feabdc0.html#slide0

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Additional Remarks

Womenswear vs Menswear

Main differences between the womenswear and menswear businesses are:

> **Top of the pyramid**, exclusive tailored brands in menswear vs designer brands in womenswear

> **Level of fashionability**, higher seasonality for womenswear

> **Level of integration** and possibility for production standardization, higher for menswear due to the importance of the inner quality, fabrics, construction

> **Product lifecycle**, higher attitude vs. seasonal innovation in womenswear

> **Shopping drivers and behaviors**, emotional in women vs rational in men; importance of the service for men

> **Business models**, more vertically integrated in menswear; wider diffusion of subcontracting in womenswear

Additional Remarks

Business Model Evolution

Business models are a way to simplify the reality

Companies are constantly learning from each other:

> Luxury Brands improve their supply chain, following Vertical Retailers (the same can be said for other business models)

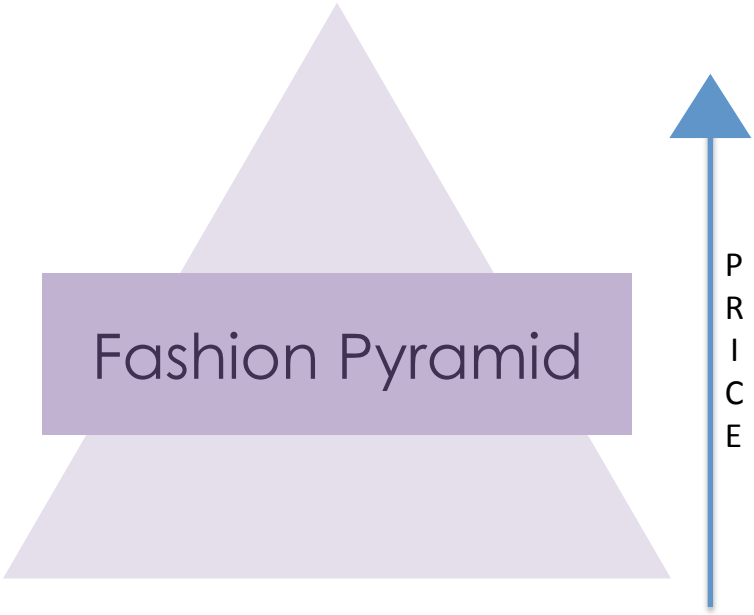
> Fast Fashion Brands invest in their unique style, following Fashion Designer Brands (the same can be said for other business models)

The fashion and luxury industry is very dynamic, so we can only take a picture of single moment

Wrap-up

Module 2

Market Segmentation & Business Models



The **Fashion Pyramid** refers to a market segmentation combining **price range** and **style** and applies especially to womenswear.

The various segments of the Fashion Pyramid can be occupied by brands with different business models

Business Model

The **Business Model** framework is more general and can be applied to almost all businesses: womenswear and menswear, sportswear, footwear, accessories, as well as jewelry, watches, etc.

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Market Segmentation & Business Models

Designer Brands can have as well lines belonging to the **Couture segment** such as
> Giorgio Armani
> Versace

The same happens with **Luxury Brands** that also have a **RTW** (ready-to-wear) line such as
> Chanel
> Dior

Most **Luxury Brands** are now **Retailers** such as
> Louis Vuitton
> Prada

Some **Retailers** collaborate with Designers of Luxury and Designer Brands for capsule collections such as
> Karl Lagerfeld for H&M
> Giambattista Valli for Macy's