Consulting-Outsourcing-Capability Building

MAKE IT WORK

Weave Services Limited presents:

Regaining competitiveness in the Chinese footwear market

Breakthrough from traditional FOB model to Total Cost of Ownership

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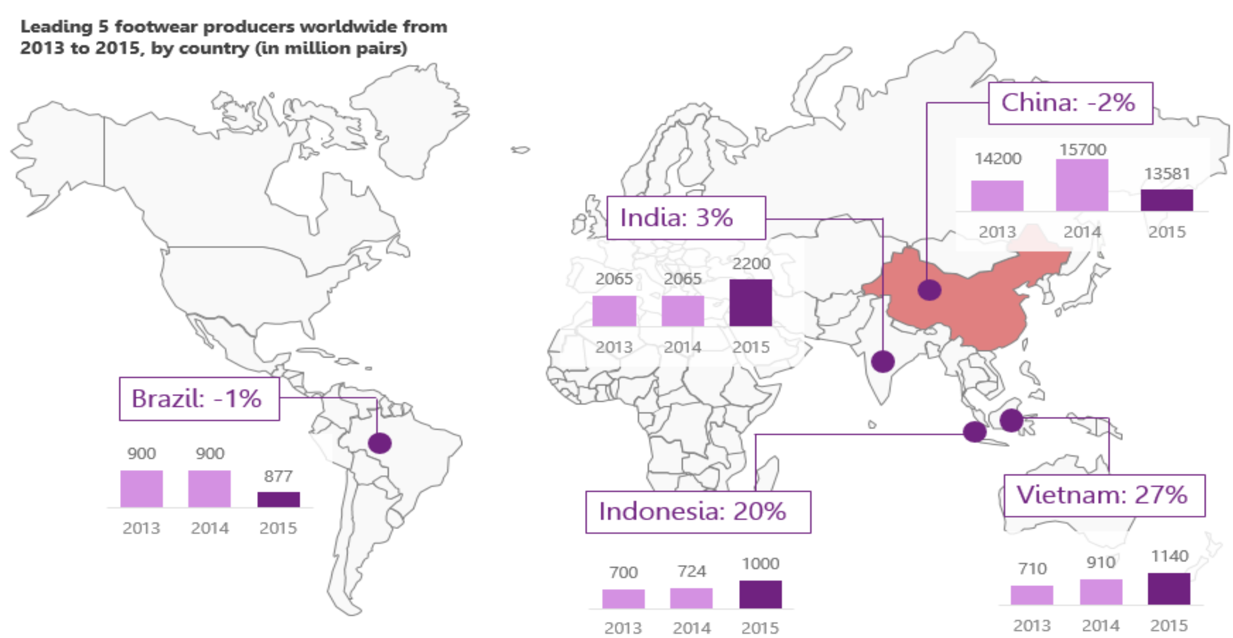
To relocate, or not?

Brands and retailers expressed their concerns over the rising production cost in China. A number of brands have migrated their footwear production facilities out of the country. 42% of VF shoes are manufactured in Vietnam. Lacoste uses Vietnam as the main manufacturing hub currently. Sportswear giant Nike, Adidas and New Balance also moved production for highly functional shoes back to their home countries supported by automation.

On the surface, China seems losing her competitive advantage. However, **what are the key criterion that drive buyers' decision?** This paper would provide the insight on how buyers make sourcing decision. As change agents with manufacturers, we will provide practical tips to allow Chinese manufacturers to stay ahead of the competition.

Despite decrease in volume, most companies need to make china work



The latest trend in footwear production indicates that China continues to be the largest manufacturer in the world. It vital for most brands and retailers to find an operating model with Chinese factories that allow **retention of profit margins due to the large scale export volume.**

Source: Statista – Leading footwear producers worldwide, 2016 China & Asia footwear conference

The key for Chinese factories is to remove cost in the supply chain beyond initial FOB price

FOB price cannot be the only decision making criteria for buyers

FOB price of a pair of shoe consists of labour cost, raw material cost, factory overhead and manufacturer's margin.

Today, labour cost in China is higher than other development countries. Yet, labour cost only contributes to **11% of the total cost**. The biggest contributor to FOB price is raw material cost.

Besides FOB price, other supplier performance indicators like, **lead time, on-time in-full and quality also contribute to the cost of managing the product.**

Understanding Total Cost of Ownership (TCO) is the first step to identify opportunities to help brands to mitigate costs

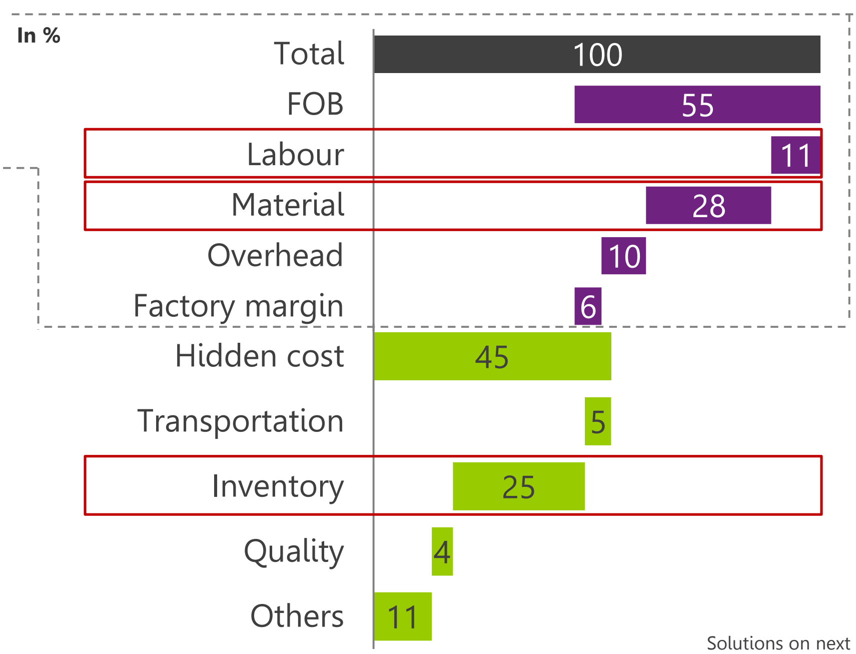
Total cost of ownership (TCO) provides a complete view to buyers regarding all visible and hidden cost associated with a product. It includes the cost paid by brands in managing the product from the start to the end of the product life cycle. Every activity along the supply chain impacts TCO.

Within the hidden cost, inventory costs the most to brands due to uncertainty with demand and suppliers' performance.

How much is it costing you to source from low labor cost countries?

Footwear cost contribution to brands from the TCO perspective

Opportunity to optimize

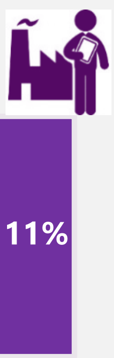


Solutions on next page

Source: Weave analysis: Total cost of ownership

Manufacturers in China will only succeed by developing advanced planning capabilities and value added services

FOB cost %



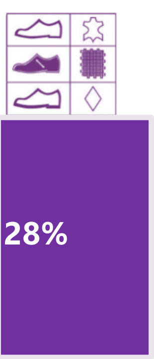
Transform yourself from traditional make-to-order production...

Manufacturers tend to face challenges on receiving **unstable orders** throughout the year. The uneven loading will cause **extra labour cost** due to over time / idled labour. In addition, traditional batch manufacturing process flow may also result in workload imbalance within the production lines.

... to planning production using advanced planning techniques

Manufacturers can leverage stable items to achieve production levelling through pre-production. That requires an accurate sales forecast, a refined production bucket considering labour and machinery capacity and other constraints. Line layout and blancing may need to be redesigned to minimize WIP along the line.

Save 20%-40% DL cost



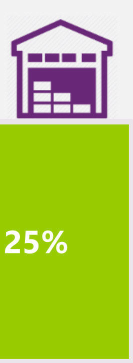
From issuing fragmented orders to your raw material suppliers...

In MTO, traditionally raw material gets ordered once a customer order is received. However, **small order** quantity could lead to MOQ penalties and prevents economies of scale in order negotiation

... to increasing your order sizes through MRP

Material resources planning allows order consolidation amongst the same style. Very often, the ship windows is set to minimize inventory exposure. **Leveraging MRP** to group the raw material orders can help with efficient management of material and cost.

Reduce 3%-10% RM cost



From reactive management of inventory for brands...

Besides demand volatility, suppliers' **risk in lead time and on-time in-full** performance contributed to inventory level. The **inventory** that carries by brand till end of the season would involve high level of extreme markdowns, write off and handling cost.

... to providing value added services to mitigate inventory cost for brands

One of the value added services that suppliers can offer to brands is **Direct-to-Store (DTS).** Suppliers can manufacture according to store demand. The role of the warehouse would be for cross-docking. It allows **zero inventory** for rolling items and the picking cost could substantially reduce by 40%.

Save 30-50% picking cost

Source: Impact are case examples from multiple projects conducted by Weave

Transform yourself today or your edge to lower cost countries

Act now before it is too late

The transformation of traditional Chinese manufacturing requires not only the technical capability in planning, but the willingness to embark the journey.

Successful transformation programs often come with the dedication from top management and the change management processes in place.

Are you ready to take up the next challenge?

Our perspective:

- Managing risk without adding buffer
- Understanding read & react in a fast fashion context
- The future of Chinese manufacturing

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