The Footwear Industry: Stepping into the Future

Chris M. Abess, Deloitte Consulting LLP

What? You Only Own 50 Pairs of Shoes?

Bonnie, a 38 year old consultant in San Francisco, takes a break and sets down her shopping bags. "Who knew I needed four pairs of running shoes and three pairs of golf shoes". "I have over 50 pairs of shoes in my closet -- some of which I'll only wear once or twice – I guess there's a little Carrie Bradshaw in all of us."

Bonnie is not alone. The pace of footwear purchases in the U.S. has quickened over the last decade. While the U.S. population has grown at approximately 2% per year, footwear sales volume has increased at twice that rate, at about 5% per year. In the 1990's, approximately five pairs of shoes were purchased for every man, woman, and child, but in 2004 those same consumers are buying almost seven pairs each. While the increase in volume can be viewed as good news, growth often comes with a price. Increased sales volume, with over 1.9 billion pairs of shoes expected to be sold in the U.S. in 2004, does not always translate into healthier profits.

The footwear industry is facing many of the same challenges as the consumer products and food industries. To meet the fickle needs of customers like Bonnie, footwear companies must continually introduce new products to keep consumers coming back for more. We have seen a fragmentation and specialization of offerings that continues to accelerate. In the recent past, a consumer owned a few pairs of shoes, some for exercising and others for work or fashion.

But today's consumer demands specialized options for footwear. Workplace fashion changes have led the way to this new reality. For most, workplace attire has shifted from the predictable to the eclectic, requiring more footwear. Bonnie agrees, "Compared to when I started working (we wore suits), there is far more opportunity to wear variety on my feet." Instead of waiting for the latest fashions from Paris and Milan, consumers are buying footwear for specific events and to make shorter lived pop culture statements. Where the athletes of yesterday got by with a couple of athletic shoes, today's athlete needs specialized shoes for running, trail-running, mountain biking, road cycling, aerobics, walking, short distance hiking, multi-day hiking - you get the idea.

All of this means that consumers will demand more specialized and option-rich footwear in greater numbers. The demand for newer, fresher, more innovative footwear will continue because it hits at the heart of the human condition. People, particularly in developed countries, are continually seeking ways to advance, feel better, perform better, and improve their overall quality of life. Footwear manufactures will need to work smarter to stay relevant and succeed in this demanding and fickle market.

I Feel a Pinch

With the increased purchase volume, you'd think footwear companies would be experiencing a steady stream of growth and profitability. In fact, the opposite is true. Several of our nation's footwear companies have seen either flat or declining EPS over the past 10 years.

To address a sagging bottom line, footwear companies must step up to three key challenges.

Being quick to market - The footwear industry's standard product development cycle is increasingly unacceptable. Current product development times, from concept to store shelf, will come close to "missing the market", particularly in trends heavily influenced by pop culture. If your product becomes irrelevant before it hits the shelf, you are faced with clearing dead inventory, which means markdowns, credits, returns and other margin busting actions.

Staying relevant - As the pace of change in the marketplace increases, profits will flow to the nimble. Those companies that identify or *establish* consumer trends, and get to market first will win the race. But speed alone isn't enough. Relationships with the direct customer – the retailer – will also need to change. It's time to drop the historical "us vs. them" model, which focuses on getting the best deal on a "buy", to a partnership model with a common goal of collaboration for combined revenue/profit maximization.

Executing flawlessly – Simply put, operational excellence will allow footwear companies to maximize revenue on great products and limit damages on poor products. While long term success of a company resides with consistent product excellence and marketing savvy, a poorly operated company may have great products, but declining financial performance.

Sensible Shoes…Sensible Business…

To meet the challenges faced by a more demanding marketplace, successful footwear companies will be paying attention to the following areas:

Responsible growth - Regulators are looking to make sure consumers are protected against monopolistic threats stemming from the continued consolidation in the retail and footwear manufacturing sectors. Ironically, the consolidation experienced in recent years has benefited the end consumer with lower prices at the shelf. However, the effect on consumer price is only one dimension under the scrutiny of public opinion. In fact, some of the largest companies experience challenges more similar to those faced by nations and governments, than their closest commercial competitor. The key for these corporate titans will be to stay focused on social responsibility and global citizenship. While access to capital will allow these large companies the capability to innovate and execute, a continual focus on social responsibility will be required to ensure new products are able to compete on their own merits without inappropriate distractions in the market.

Innovation - Innovation is a "ticket to entry" for competing in the footwear market. The fact is that few brands today truly resonate with shoppers. Putting together a creative combination of elements that establish image, quality, variety, and pricing, makes the difference between a brand that succeeds and one that fails. Successful companies will integrate innovation into the core of their business.

Expect to see "Innovation Zones" formed by manufacturers, which are a combination of technology and process to capture and assess ideas. Well formed innovation zones expand the "ideation" process outside the confines of R&D and product development to all potential sources of inspiration, including consumers, competitors, and other industries.

In some cases, innovation will not necessarily always add features and functions to a product line. Several product ideas give the consumer what they want without "over engineering" the solution (e.g. low fare airlines, return to the classics, etc.). Innovation will continue to be about identifying or establishing the best application of new ideas, exploiting the window of opportunity of an ever shortening shelf-life, and managing the process by thinking three moves ahead and having the next wave of innovation in the pipeline before a trend fully matures. Successful companies will ensure a well developed culture and process for innovation are core to the organization.

Channel cooperation - The traditional buyer/seller relationship will need to give way to more cooperative planning and joint success metrics (GMROI – a function of gross margin dollars and inventory turn, for example.). The footwear industry can take some lessons learned from other industries such as consumer electronics, which arguably has a shorter shelf-life product and more challenging pricing scenarios. Some consumer electronics retailers and manufacturers have created shared/common teams that promote joint motivation on common financial results and are at times co-located for quicker more nimble interaction.

With an increasingly fickle consumer, footwear manufacturers will need to gain intelligence on trends, desires, and feedback from as many sources as possible. Expect smaller footwear manufacturers with a strategic focus of being leading edge innovators to team with smaller retailers with a similar strategic intent to push the envelope on trend setting, new product introduction, and stellar marketplace responsiveness.

Consumer connection - Having a cooperative go to market relationship with customers (retailers) is not enough. In the spirit of "the one closest to the consumer is king" philosophy, successful footwear manufacturers must have a direct point of connection with the end consumer. By creating a sense of community, and connectivity, the manufacturer will not only endear themselves to the consumer, but establish a loyal base for gaining market feedback. Innovative consumer direct programs will need to be developed to attract, continually impress, and retain the end consumer. Many automotive and food manufacturers have established successful programs to connect directly with consumers, increasing loyalty to the product.

Given the trend toward more frequent footwear purchases and an increased pace of product innovation, expect to see footwear "trade-in" programs with credit toward a new pair of shoes, consumer direct premiums, consumer driven design teams, and other programs designed to connect manufacturers and consumers.

Association and affiliation - Consumers are inspired to act based on what they observe around them. Successful footwear manufacturers will have thoroughly developed product endorsement and placement plans. While large scale endorsement deals will continue to capture headlines in the battle of the titans, smaller and mid-size manufacturers will need to carefully craft their marketing deals. Developing a plan ranging from formal advertising to inspiring personality endorsements will require a well refined marketing competency and leveraging as much consumer intelligence as possible. Expect well run companies to establish innovative and cost-effective marketing initiatives along with processes for analyzing and measuring the ROI across all of their marketing programs.

Operational excellence – Some manufacturers are plagued by rising SG&A costs and excessive premiums in COGS and inventory as a result of misreading market conditions. Successful companies will couple well defined marketing and product development engines with equally nimble business case analysis throughout the product development lifecycle. Executives need to establish clear go/no go decision points throughout the product development lifecycle to leverage the expected benefit of concepts that continue to gain energy based on marketplace feedback, and to redirect programs and product development for products that show less promise. Expect an almost fanatical management of the supply chain and continued devotion to cost reduction with top performing footwear manufacturers. The companies with the ability to leverage these new sourcing and supply chain opportunities the quickest will be the best positioned to win with consumers.

Run don't walk

One thing is certain, the pace of change continues to speed up - not slow down. Footwear companies will need ever improving business processes, management discipline, and accountability to ensure speed to market, market relevance, and business execution keep them ahead of the competition.

About the Author

Chris M. Abess is a Principal with Deloitte Consulting, LLP. He specializes in consulting to consumer businesses and has assisted numerous companies to develop business strategies and improve operations for the past 18 years. Chris serves some of Deloitte's large apparel and footwear clients. cabess@deloitte.com.