



Home > Topics > Sourcing

OCTOBER 23, 2019 7:50AM ET

# Excess Apparel Inventory Will be a ‘Major’ Obstacle Plaguing More Than Margins in 2020

By Tara Donaldson



CREDIT: Jennifer A. Uihlein/Girl in a Camera Productions

The apparel industry's festering [inventory](#) problem is expected to worsen in 2020.

## RELATED ARTICLES

- [Nordstrom Opens Long-Awaited NYC Flagship and Plans 3 New Local Markets](#)
- [How Designers are Injecting Creativity and Reinventing Denim](#)

And if brands and retailers can't get to the root of the excess inventory issue that has been years in the making, the glut of garments may threaten to plague the sector even beyond that.

"When we talk about inventory, often times we talk about it as if it's a style issue or a seasonal issue or a pricing and a cycle issue, and this problem hasn't gone away for several years and it only seems to be getting worse," John Thorbeck, chairman of Chainge Capital, which builds speed-to-market analytics for the retail supply chain, said speaking on a panel at [Sourcing Summit New York](#) last week. "It isn't a matter of selling your way out of inventory, or this is going to cycle through to the next season. This is the industry's obstacle...It's a major, major obstacle for 2020."

## Inventory in the beginning



As mass production took over apparel, making “more” the M.O. and cutting costs the only way to deliver, brands and retailers focused on growth, which naturally meant more inventory.

“The traditional way to grow is grow the number of stores, and it has been acceptable to invest in inventory forward because you’re going to grow stores and the key metrics were more sales,” Thorbeck explained, adding however, “Those metrics are not as relevant today.”

It’s a model Forever 21 latched onto at the outset fueling, both its growth and its eventual demise.

“They got into a lot of long-term leases and expanded rapidly both in terms of real estate and the inventory investment and I think eventually that...really just came to get them,” said Janine Stichter, vice president and equity analyst for apparel and footwear retail at Jefferies.

H&M, the heavily SKU’d fast-fashion chain, has become the poster child of sorts for the industry’s excess inventory problem and, like its cohorts in the same predicament, the retailer made its bed several years back.

Shifting its sourcing to make more offshore, H&M bet big on manufacturing in Asia—Bangladesh in particular—to keep up with its cheap and chic promise.

“They made a bet on additional margin to sort of work their way out of a slowdown around a decade ago and that decision has come back to be very, very costly,” Thorbeck explained. When its designs started missing the mark and sales growth slowed, leaving inventory sitting around longer, what was expected to be a margin win turned into a \$4 billion mound of unsold stock at the end of 2018.

But H&M is far from the only retailer that went down that road.

“Other people have said ‘well, we’re going to shrink our footprint,’ Kohl’s said, ‘we’re going to reinvent the store experience, we’re going to reduce the number of stores, we’re going to change our assortments,’” Thorbeck said. “All of these are inventory strategies trying to reduce the level of uncertainty, but these are just partial fixes for a problem that really is overwhelming.”

## The landscape today

While inventory was up in the first half of 2019, Stichter said most apparel and footwear retailers she covers have bought inventory “flat to down” for the back half of the year and into next year.

“It might be conservative,” she said, but “I think there’s a lot of risk when you’re buying flat to slightly down, and if sales don’t materialize as companies expect them to, you could be subject to major markdowns.”

It’s a lack of visibility, really, that has gotten the industry into this inventory conundrum.

“Even if you’re planning your lead time six months out, you still have generally little visibility into what the consumer picture will look like at that point and what kind of inventory levels you need, so I think there’s still a lot of looking onto the supply chain to get inventory an appropriate position,” Stichter said.

“And then on top of that...companies have huge fixed expenses with their real estate...then they have to do more selling online,” she added, “which just adds incremental expense if they have to pick, pack, ship all these goods that maybe once were being sold in store... and it just adds expense to their P&L.”

Add to that tariffs, economic shifts and a sustainability problem, and the pile-up of uncertainty only nourishes the garment glut and the costs that come with it.

Tariffs, in particular, have created a lack of predictability, according to Stichter.

Companies looking to skirt that and get ahead of the Tranche 4 tariffs—which have been held off as President Trump negotiates “Phase One” of a trade deal with China—brought goods in early, which “created a huge amount of surplus inventory at the end of the second quarter,” Stichter said.

And that was just more fuel for the fire.

“Excess inventory, plus speed and uncertainty and rising costs, is certainly not a great formula. And it isn’t just the cost of the markdown on excess inventory, it’s also the cost of lost sales, which is almost as significant as the cost of markdowns, and yet that isn’t a common metric measured,” Thorbeck said. “The sort of total cost of uncertainty is high, so the question is how do you deal with that? There’s going to be a lot of price promotions at holiday and well into 2020.”

So how did the apparel industry get here? If you ask Thorbeck, it hasn’t been about bad management.

Offering Gap as an example, he pointed out that 10 years ago, the company was bringing in \$16 billion in revenue. Four CEOs later, plus countless supply chain changes and efforts to realign inventory, that number hasn't changed and the company is still working on a way forward.

"Now is that commentary on the individuals who are the leaders, or those cultures? I don't think so," Thorbeck said. "There's something deeply flawed about the business model of the industry and I think that's what we've got to be looking toward."

### Surviving SKU-maggedon

To climb out from under all of this inventory, the apparel industry will have to realign its efforts around process improvement instead of its long-standing focus on location, location, location.

"Location shouldn't matter. Driving your sourcing strategy by where your factories are located is a deeply flawed strategy," Thorbeck said. "You're telling me that the culture is still bound on a cost of goods sold or ex-factory basis? You really have to consider not what the cost of that location is, it really is: What are the economics of speed and flexibility? That speed and flexibility more than compensates for cost of labor, cost of material and cost of location."

The industry, he continued, isn't giving enough attention to process innovation. And while companies spend hours mulling how Zara does what it does where supply chain efficiency is concerned, and what technology they'll need to get there, too many are still missing the mark.

"[Zara] didn't build that model on a technology, they built it on a process difference," Thorbeck said. "And there's a lot of process opportunity that technology can enable, but the idea of reducing lead times from a typical six to nine months down to one to three months, that's all process innovation, and this industry has been slow to pick up those lessons."

The cost of uncertainty, whether surrounding tariffs and economic conditions, or what to cut into and whether the consumer will buy it, is "overwhelming," Thorbeck said. And if the apparel industry can surmount its inventory problem, it will take an overhaul that goes well beyond robots and blockchain. Chasing cheap will have to be a thing of the past.

"It's a lowest cost strategy, and I would now call it the high cost of low cost," Thorbeck said. "You really have to look at the end-to-end process, which is no longer working."

**TAGS**

■ INVENTORY

■ SOURCING SUMMIT 2019