

Retail Practice

# Fashion's digital transformation: Now or never

Some apparel, fashion, and luxury companies won't survive the current crisis; others will emerge better positioned for the future. Much will depend on their digital and analytics capabilities.

*by Antonio Gonzalo, Holger Harreis, Carlos Sanchez Altable, and Cyrielle Villepelet*



**The COVID-19 pandemic** is simultaneously an unprecedented health crisis and a global economic shock. Amid the pandemic, the apparel, fashion, and luxury (AF&L) industry has moved quickly to address urgent public-health needs—closing stores, manufacturing much-needed items such as face masks and hand sanitizer, and making donations to healthcare and community organizations. At the same time, AF&L companies are grappling with COVID-19's business ramifications, including widespread job losses in an industry that provides livelihoods for millions of people worldwide.

Although no one in the industry foresaw the intensity of this crisis, some fashion companies are finding that they are better equipped than others—largely because of their digital know-how. In this article, we touch on COVID-19's impact on the AF&L industry to date. We then propose a set of actions that AF&L companies can take to build their digital and analytics capabilities—not just to ensure business continuity and minimize the downside of COVID-19, but also to emerge from the crisis in a position of strength.

## A deepening digital divide

Our consumer-sentiment surveys, conducted in April, show declines in purchase intent of 70 to 80 percent in offline and 30 to 40 percent in online in Europe and North America, even in countries that haven't been under full lockdown.<sup>1</sup> E-commerce is clearly not offsetting the sales declines in stores. Nevertheless, it has been a lifeline for fashion brands as stores have been shuttered—and it will continue to be critical during and after the recovery period. In China, the return of offline traffic has been gradual, with 74 percent of Chinese consumers saying they avoided shopping malls in the two weeks after stores reopened.<sup>2</sup> This suggests that some percentage of offline sales could permanently migrate to e-commerce.

Digital is not only an increasingly important sales channel; it can also help companies adapt

cost structures and make each step of the value chain better, faster, and cheaper. For example, digitization can enable new logistics and sales-fulfillment options (such as click-and-collect and drive-through), fuel innovative ways of customer acquisition, and help predict and manage inventory to create a more resilient supply chain. The fundamental enabler to all this will be data—the transparency, governance, and accuracy of which have never been more important.

This all portends a deepening digital divide. Even before the crisis, companies that were digitally and analytically mature outperformed competitors that hadn't built robust digital and analytics capabilities (Exhibit 1). The COVID-19 crisis has only widened the gap between industry leaders and laggards. For leaders with the ability and willingness to invest, the pandemic has clearly been an accelerator. As a top executive of a leading apparel player recently declared, "We've accomplished two years of digital transformation in two months."

Thus, for executives in the AF&L sector and all related subsectors (such as beauty products and sporting goods), the imperative is clear: make digital and analytics a core element of your company's strategy.

A number of trends in the post-COVID-19 world—the "next normal"—could make digital and analytics play an even more important role.<sup>3</sup> Physical distancing could continue, making consumers less likely to visit brick-and-mortar stores, and a contact-free economy could emerge—raising e-commerce and automation to a new level.

The implications of these trends will differ for each company, depending on its digital starting point and strategic orientation. Digital and analytics leaders (companies in which online sales account for 30 to 40 percent of total sales, parts of the value chain are significantly digitized, and online and offline channels are integrated to some degree) have an advantage today but could quickly lose it if other players accelerate their transformation.

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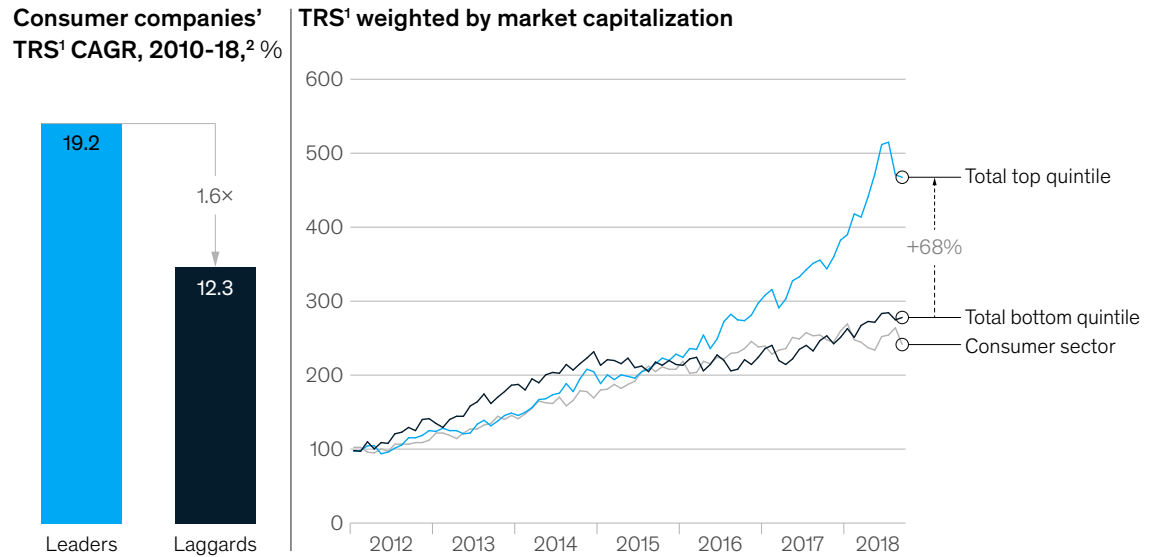
<sup>1</sup> For survey findings by country, see "Global surveys of consumer sentiment during the coronavirus crisis," April 2020, McKinsey.com.

<sup>2</sup> McKinsey Chinese COVID-19 consumer-sentiment survey with field work March 21–23, 2020.

<sup>3</sup> Shubham Singhal and Kevin Sneider, "The future is not what it used to be: Thoughts on the shape of the next normal," April 2020, McKinsey.com.

Exhibit 1

## Digital and analytics leaders outperform their competitors in total returns to shareholders.



<sup>1</sup>Total returns to shareholders.

<sup>2</sup>S&P 500 index, consumer sector.

Source: Capital IQ, McKinsey analysis

On the other hand, laggards (companies with less than 20 percent of total sales coming from the online channel, low digitization levels across the value chain, and siloed online and offline operating models) have an opportunity to make an “all in” bet on digital and analytics—and perhaps gain market share with smaller capital-expenditure investments, which used to be a limiting factor for many brands.

That said, digitization won't be a panacea. Companies should direct investments to areas in which the highest business value lies—which might not be in sales but rather elsewhere in the value chain. Equally important, companies should avoid “gold plating,” aiming instead for the fastest minimum viable digital solution that will achieve the business goal. Finally, the sequencing of initiatives will play a big role in making a company's digital transformation as self-funding as possible.

### Navigate the now: Immediate priorities

The health and safety of employees and customers, of course, has been—and remains—the absolute priority. By now, AF&L companies have closed stores, introduced new hygiene and safety processes in warehouses and distribution centers, and set up digital tools for remote working and collaboration.

Although the situation remains uncertain and is evolving daily, there is a clear set of actions involving digital and analytics that AF&L players should implement now to keep the business going, stem sales losses, and plan the comeback.

### Engage with customers in an authentic way

Email, social media, and other digital channels have seen significant spikes in usage during the crisis (Exhibit 2). AF&L brands must therefore continue to communicate frequently with consumers, even

if most consumers aren't currently spending. Use digital channels to launch genuine, purpose-driven communications regarding health, safety, business continuity, and community building. If you decide to send consumers relevant content, be sure to do so in an appropriate and empathetic tone (for example, a global sports-apparel player now offers yoga lessons on Instagram).

Whether it's a personalized offer or outreach from a personal stylist, the best brands are maintaining customer relationships even while stores are closed. Staying in touch with your most loyal customers doesn't just keep your brand on top of mind but

also helps to boost sales. On a leading Chinese e-commerce platform, transaction volume for fashion-brand miniprograms (brand-powered apps embedded within the platform's interface) more than doubled between January 2020 and February 2020, during the peak of China's outbreak.

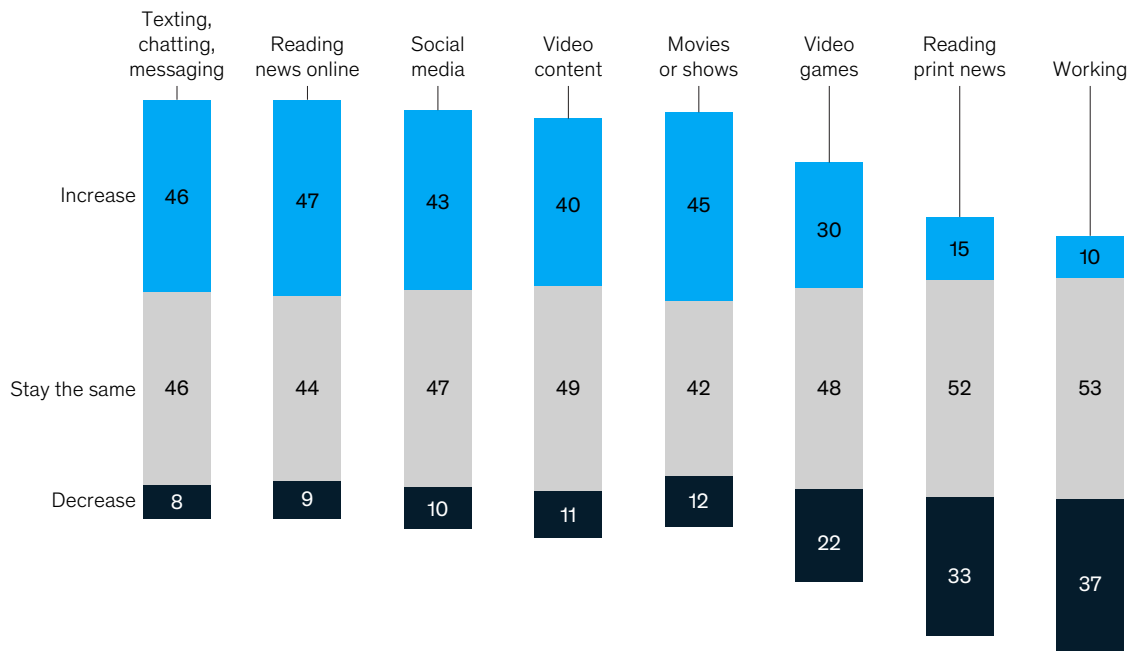
**Refine and scale up your online operation**

We expect the online share of fashion and apparel in Europe and North America to increase by 20 to 40 percent during the next 6 to 12 months. In April, traffic to the top 100 fashion brands' owned websites rose by 45 percent in Europe.<sup>4</sup> Some of the larger players have even reduced their promotion intensity to be able to handle the volume of orders.

Exhibit 2

**Consumers are spending more time online during the crisis.**

Change in time spent on select activities,<sup>1</sup> % of respondents



**35%**

of consumers browse for fashion inspiration in online shops at least once per week

**22%**

of consumers state they will browse for inspiration online more often in the next 4 weeks

**10%**

of consumers think brands should not promote their own interests at this time of crisis

<sup>1</sup> Question: Over the next 2 weeks, how much time do you expect to spend on these activities compared to how much time you normally spend on them?

Source: McKinsey COVID-19 Consumer Pulse Survey, Apr 1–Apr 6, 2020, n = 5,000+; McKinsey COVID-19 Apparel & Fashion Survey, Mar 27–Mar 29, 2020, n = >6,000

<sup>4</sup> Similarweb, April 19, 2020, similarweb.com.

Delivering an excellent customer experience online is crucial, so reallocate your resources and shift management attention from offline to online. Also, scale up capabilities in both demand generation and fulfillment (Exhibit 3). Seek to eliminate points of friction in every part of the online customer journey—for example, by improving your website’s search function and expanding your online assortment. Some retailers have redeployed store personnel from closed stores to support online fulfillment or to assist consumers via digital call centers.

While most AF&L players already have an e-commerce presence, some still don’t. Companies without one can launch a basic online platform in 10 to 15 weeks. A private-equity-backed retailer did it in 13 weeks (Exhibit 4).

**Prioritize digital-marketing levers as demand rebounds**

In anticipation of a shift toward online sales, allocate more of your marketing budget to digital channels. Establish or improve your digital-marketing “war room” and increase its visibility in the organization—for instance, by establishing a C-level digital-performance dashboard that provides a cross-channel view of e-commerce, customer relationship management, and social media, thus enabling rapid identification of opportunities for efficiency optimization or growth.

Retrain your look-alike models to capture value from the new consumer segments and behaviors that have emerged during the crisis. Upgrade your digital-marketing activity to be best-in-class—for example,

Exhibit 3

**Companies must accelerate their online capabilities in both demand generation and operations management.**

**Example levers**



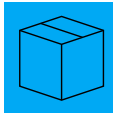

Accelerate demand		Manage operations	
			
<b>Relevance, awareness, and traffic</b>	<b>On-site and conversion</b>	<b>Stock and fulfillment</b>	<b>Loyalty</b>
<ul style="list-style-type: none"> <li>● Simplify range, prioritize essentials to meet immediate demands of new customer traffic</li> <li>● Launch contextual and personalized campaigns across marketing channels</li> <li>● Allocate budget to highest-impact targeted paid channels (eg, Facebook, Instagram, search-engine advertising)</li> <li>● Adjust search-engine optimization and other nonpaid channels to situation (eg, refine keywords)</li> <li>● Shift focus from brand building to performance marketing (including budget reallocation)</li> </ul>	<ul style="list-style-type: none"> <li>● Tailor on-site messaging to address current situation (eg, contextual landing page with special content for COVID-19 situation)</li> <li>● Launch and optimize targeted markdowns and promotions to wind down forecasted stock excess</li> <li>● Optimize on-site product assortment and display (eg, focus on top SKUs)</li> <li>● Introduce bundles (eg, family boxes), special offers (eg, free shipping, 3-for-2), and innovative discounts</li> </ul>	<ul style="list-style-type: none"> <li>● Strengthen supplier relationships, especially for priority SKUs (eg, CEO meeting)</li> <li>● Prioritize SKUs and ensure sufficient stock allocation (eg, longer inventory days for high-demand SKUs)</li> <li>● Ensure omnichannel management of stock, fulfilling online orders from best online or offline location to optimize overall stock positioning</li> <li>● Prepare fulfillment and customer-support capacity for increased demand</li> <li>● Staff temporary resources as needed</li> <li>● Identify scenarios and plan for worst case; work with government authorities to understand guidelines</li> </ul>	<ul style="list-style-type: none"> <li>● Focus on user interface and user experience (more important than ever as customers are more willing to switch brands at this time)</li> <li>● Leverage customer relationship marketing and maximize frequency of email and app push campaigns</li> <li>● Investigate opportunity to create special offers for loyal customers</li> <li>● Focus on contactless delivery (delivery staff training, communication) to match customer expectations</li> <li>● Communicate proactively with customers (eg, email from CEO to address situation)</li> </ul>

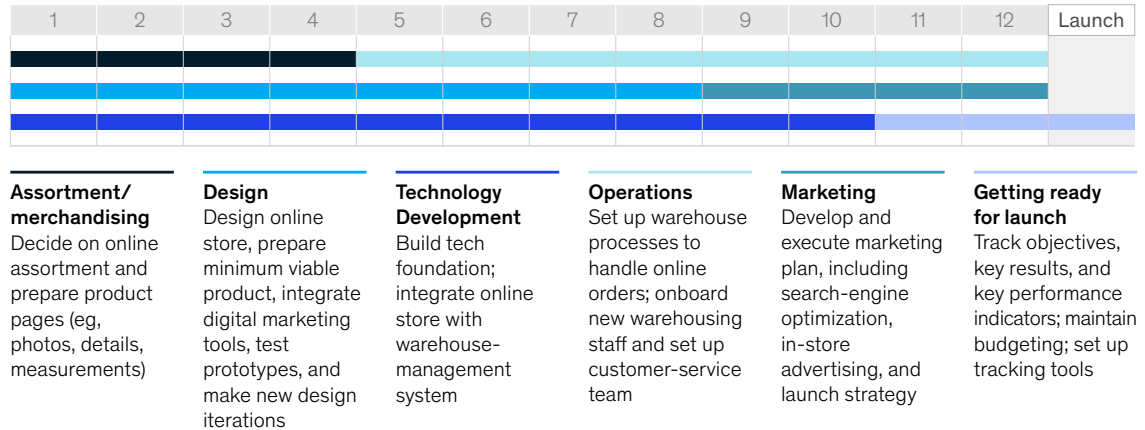
Exhibit 4

## A retailer built and launched an e-commerce platform in 13 weeks.

### Launch timeline, weeks

**Company** Private-equity-owned retailer with 1,000 physical stores but no online presence

**Impact** More than 400% week-on-week growth rates in online sales within the first month



by adding sophisticated imagery to your social-media posts and conducting “social listening” to inform the development of new services and offers.

### Use granular data and advanced analytical tools to manage stock

The value of excess inventory from spring/summer 2020 collections is estimated at €140 billion to €160 billion worldwide (between €45 billion and €60 billion in Europe alone)—more than double the normal levels for the sector. Clearing this excess stock, both to ensure liquidity and to make room for new collections, will become a top priority.

At the best-performing companies, an “inventory war room” uses big data and advanced analytics to first simulate dynamic demand scenarios specific to locations (channel, country, store) and SKUs, then to synthesize the resulting inventory risk—thus enhancing decision making. The war room decides, for example, whether to redistribute SKUs, transfer inventory to future seasons, or accelerate markdowns (Exhibit 5). A company’s

investments in developing advanced analytical tools to steer markdowns during the crisis will pay off almost immediately.

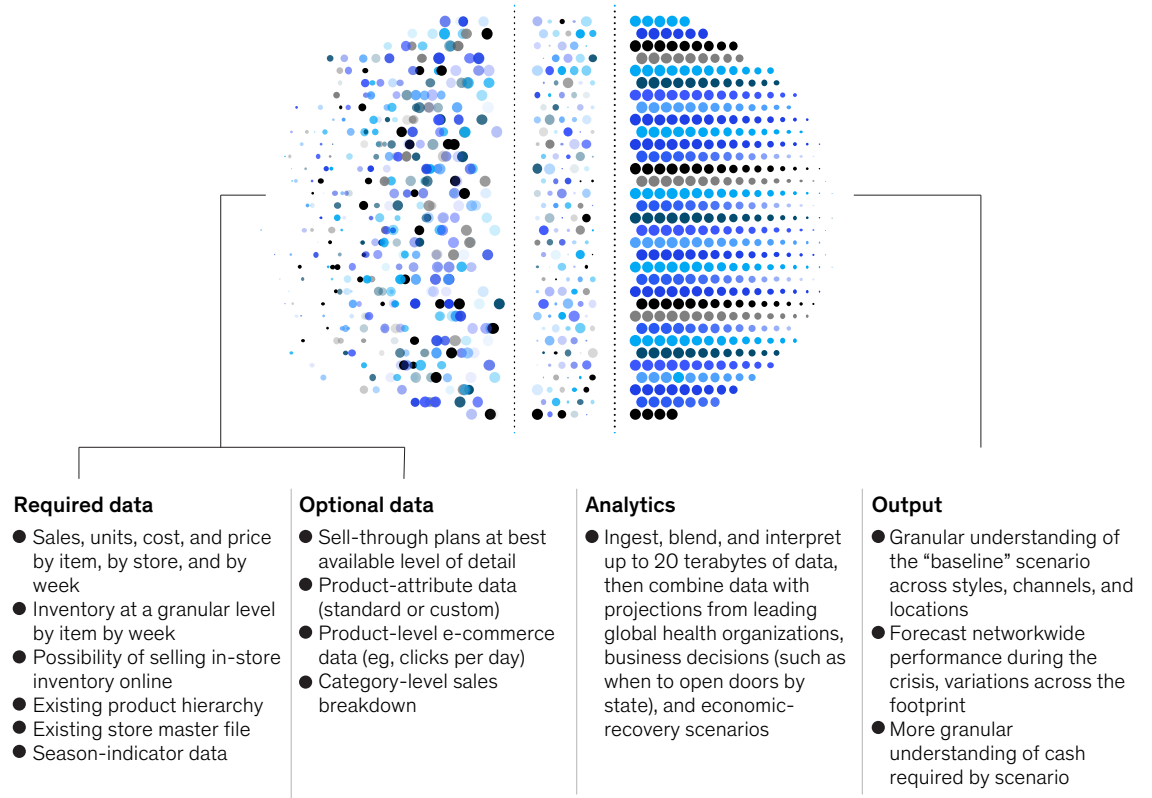
### Optimize costs using a zero-based approach

In light of crisis-related sales decreases, cutting costs is an obvious imperative for most companies. However, reducing all budget lines across the board is risky. We recommend a zero-based budgeting approach instead.

Identify two categories of projects: critical projects linked to core digital and analytics priorities that must proceed as planned or at a slightly lower speed (for example, building a new data lake to enable personalized marketing) and core projects that can be delayed (such as those that don’t enable emergency response). Continue only the projects that fall into those two categories; stop all others. A range of savings levers—such as vendor renegotiations and tactical moves to the cloud—can help dramatically reduce your operating costs. Reset your digital and analytics priorities and budget and adapt them to a post-coronavirus world.

Exhibit 5

**Using analytics, a company can quickly build sell-through scenarios and synthesize resulting inventory risk.**



**Shape the next normal: Longer-term strategic actions**

Although time frames remain uncertain for now, AF&L players should start planning how they'll compete in—and perhaps even influence—the industry's next normal. Consumer habits, companies' interactions with consumers, and the number and types of touchpoints will all change. The requirements for supply-chain speed and flexibility will continue to increase. Digital and analytics will play a critical role in helping companies emerge stronger from the crisis.

**Set an ambitious aspiration and define a clear road map**

A digital and analytics transformation is typically an 18- to 24-month journey, requiring an ambitious

aspiration, a clear plan, and concrete milestones. In our experience, successful digital and analytics transformations have the following elements in common:

- Strong support (or even direct sponsorship) from the CEO during the entire journey.
- A pragmatic approach that starts with an understanding of the consumer and the drivers of value creation; digital for digital's sake will not deliver results.
- A clear road map and prioritization of initiatives, combining actions that help set up the enablers for the organization with the implementation of use cases that generate quick wins.

- A focus on getting to a minimum viable product (MVP) within two to three months—a rapid timeline that allows the company to iterate while generating value, avoiding large up-front investments.
- A central team to monitor value capture. This team also helps build the road map by scanning opportunities, allocating budgets, and coordinating implementation, ensuring that all efforts are focused on delivering tangible impact rather than gold plating.
- Well-defined key performance indicators (KPIs) to measure success.

The first step in the transformation program should be the definition of digital priorities, which will differ based on each company’s business model and digital starting point. Digitization is much more than just selling online; a quick diagnostic may be required to select and align on key value areas.

Typically, digital and analytics priorities can be categorized according to their place in the value

chain: customer experience (front), distribution and supply chain (middle), and product development and support functions (back). Exhibit 6 shows high-impact use cases in each of these three areas.

**Provide an excellent omnichannel experience**

The pandemic has elevated digital channels as a must-have for AF&L players. Therefore, take this opportunity to leapfrog into the digital arena by making it the center of your operating model: move your traffic- and engagement-generation engine to digital, and leverage digital channels to drive store traffic and vice versa.

Besides scaling up digital sales efforts, reconfigure your store footprint accordingly—for example, by reducing presence in “B” areas (markets with lower population density and lower profitability per square meter), devoting less store space to product categories with high online penetration, experimenting with innovative formats (such as drive-through windows or pop-up stores), and making it easy for customers to perform any omnichannel operation, including complex ones (such as buying online from a store if the product isn’t in stock there,

Exhibit 6

**Digital and analytics can transform domains in every part of the apparel value chain.**



**Customer experience (front)**

- Seamless omnichannel experience
- Personalized customer journeys, activations, and promotions to maximize customer value
- Prescriptive merchandising optimization
- Online artificial-intelligence-powered sales associates
- Markdown optimization powered by advanced analytics (AA)
- Shelf, format, and macro space optimization
- Store of the future



**Supply chain and distribution (middle)**

- Allocation of new collection merchandise (no sales historical record)
- AA-powered granular demand forecasting and replenishment
- IoT-enabled warehouse optimization and automation
- Optimal warehouse picking and slotting
- End-to-end digitized supply-chain planning
- AA-powered network, transport, and route optimization
- Platform for last-mile delivery



**Product development and support functions (back)**

- Digital collection development and management
- End-to-end digitized product management (including design, virtual sampling, production visibility)
- Digitized and robotized finance and back-office processes
- Talent and HR analytics



# Digital and analytics can not only drive top-line growth but also significantly improve speed, cost, flexibility, and sustainability across the supply chain.

and then picking it up from another physical store in the next 12 hours). Use data and analytics to tailor the assortment in each store and to streamline and optimize assortments overall.

In our experience, fully integrated management of stock in stores and warehouses is core to any omnichannel operation. Making all stock (even stock shortly arriving to warehouses) visible to customers in any channel has proved to boost sales.

## **Bet on personalization**

Personalization has helped several industry players achieve 20 to 30 percent increases in customer lifetime value across high-priority customer segments. It has proved even more valuable in subsectors with more stable and predictable purchasing patterns, such as beauty products.

Use cases for personalization have mostly centered on personalized offers, personalized promotions and benefits (such as access to new products), and reductions in generic traffic-generation costs. To go further, add personalization capabilities to your digital war room—for example, by collecting and analyzing all the available data to generate detailed insights about your customers. Build actionable microclusters based on customer behavior. For instance, entice the highest spenders with special incentives (such as triple loyalty points for purchases of at least \$1,000), target customers who tend to buy in the categories where you have the largest inventory buildup, and give online

customers coupons to redeem in-store once physical stores reopen.

Prioritize use cases based on your business context, advanced-analytics capabilities, and customer segments. Create a prioritized use-case road map and a technology-investment plan. Integrate personalization into all delivery channels to ensure consistency in your customer communications.

## **Leverage big data and analytics to manage the supply chain**

Digital and analytics can not only drive top-line growth but also significantly improve speed, cost, flexibility, and sustainability across the supply chain. For instance, some leading companies are using radio-frequency identification (RFID) to track products more precisely and reduce in-store merchandising manipulation. Companies' RFID investments typically yield operations simplifications and service-level improvements.

In addition, automating logistics through digital warehouse design and predictive exception management can significantly increase efficiency. The benefits will flow to consumers as well—in the form of better product availability and faster, cheaper, and more accurate deliveries. Leading online players, for example, are using models powered by artificial intelligence (AI) to predict sales of specific products in certain neighborhoods and cities, then stocking the predicted amount of inventory in nearby warehouses.

### **Digitize product development and support functions**

During the COVID-19 crisis, the digitization of product development has proved to be a competitive advantage. Companies that were already using cutting-edge tools such as 3-D product design, virtual sampling, digital material libraries, and AI-supported planning have fared better than their peers during the crisis. Their designers and merchandisers can react faster to market trends, significantly reduce both sample costs and time-to-market, and collaborate remotely across teams. The past several weeks have shown that it's possible to do much more on this front than some in the industry initially thought. Indeed, the pandemic may have shattered historical preconceptions and biases against digitization in core product-development processes.

Digitization of support functions is another key lever for improving efficiency. By automating repetitive tasks in back-office functions such as indirect purchasing, finance, legal, and HR, you can simultaneously reduce costs and free up time and resources to reinvest in more valuable activities. Companies that have automated their finance processes—such as claims collection and financial reconciliation—have found that they've also increased the agility and accuracy of these processes while capturing significant synergies. Speed up the digitization of all support functions through robotic process automation and other leading-edge technologies.

### **Build data and tech enablers to support your transformation**

Technical enablers play a key role in powering digital and analytics growth. In our experience, three core principles are the most relevant:

- Use cloud infrastructures to sustain scaling and to access best-in-class services, particularly for use cases that best benefit from the cloud's features (for instance, data consumption across the globe, very high storage and processing needs).

- Think data from the start. Build solid data foundations as part of every digital and analytics initiative in a way that allows rapid scaling and forward compatibility. Design and build out pragmatic data governance focused on enabling business value by helping to ensure data breadth, depth, and quality. Establish a strong data culture and ethics.
- Design your technology stack for faster integration and development, with applications broken down into microservices and isolated through the use of application programming interfaces; use unified DevOps toolchains to enable automation and reduce time-to-market to a matter of hours instead of weeks.

These enablers shouldn't become causes for delay. Rather, they should follow the same agile timelines and sprints as the core initiatives. Implementation should be pragmatic and clearly linked to value generation.

### **Attract and retain top digital talent**

After the crisis, financially stable companies may be able to attract top-notch digital talent, including in-demand profiles such as digital-marketing specialists, data scientists, data engineers, user-experience and user-interface designers, and software and data architects. Retaining these kinds of employees will require AF&L companies to develop new talent processes—with tailored initiatives in recruiting, career growth, learning and development, and performance management—specifically for engineering and digital talent, similar to what many fashion players already do for designers and creative directors.

In addition, AF&L players should adopt agile ways of working to speed up development of digital and analytics products and projects. Agile techniques enable companies to release MVPs into the marketplace quickly and refine them iteratively based on consumer feedback.

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There's no denying that the COVID-19 pandemic will make for a difficult 2020. For some AF&L companies, even survival may be a struggle. However, if they lead with empathy and undertake bold actions in digital

and analytics—particularly around e-commerce, data-driven stock management, and digitization of key functions—we believe they can not only endure the crisis but also build competitive advantage and strengthen their business for an omnichannel, digital-centered next normal.

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