

THE TWO FACES OF FASHION-INDUSTRY PERFORMANCE

Top-quintile companies are the engines of value creation. Digitization and better in-store experiences will drive future gains.

by Achim Berg, Saskia Hedrich, and Johnattan Leon

Fashion is one of the world's largest and most fragmented industries, divided into multiple product segments and categories, housed in many different types of organizations, and widely dispersed across geographies. We've recently put the spotlight on value creation, measured as economic profit,¹ and found, as in so many other sectors, a striking and contrasting tale of winners and losers. As the exhibit shows, 20 percent of fashion players created 100 percent of economic profit over the past decade, while the bottom 20 percent of companies went backward.

Economic-profit growth of 8 percent outpaced sales growth over the same period, with a handful of companies (Adidas, Chow Tai Fook, and H&M, among others) taking advantage of the winner-takes-all market dynamics. They did so by hammering down costs, investing efficiently, and executing better than competitors. The losers were midmarket players, which struggled in the slow-growth environment of the past five years, experiencing sharp declines in margins and wide variations in operating performance.

Looking ahead, the bifurcation seems set to continue. McKinsey research and our recent survey of industry executives,² for example, suggest some segments of the market, such as affordable luxury and premium brands, should grow much faster than top-of-the-line luxury or discount products. All players, regardless of focus, will need to step up their digital efforts, with better omnichannel distribution and in-store experiences at the top of the list, accompanied by investments in customer-relationship-management systems. 

¹ Economic profit is a measure of value creation taking into account explicit and opportunity costs. It is defined as invested capital times the spread companies make on that capital (the return on invested capital minus the weighted average cost of capital).

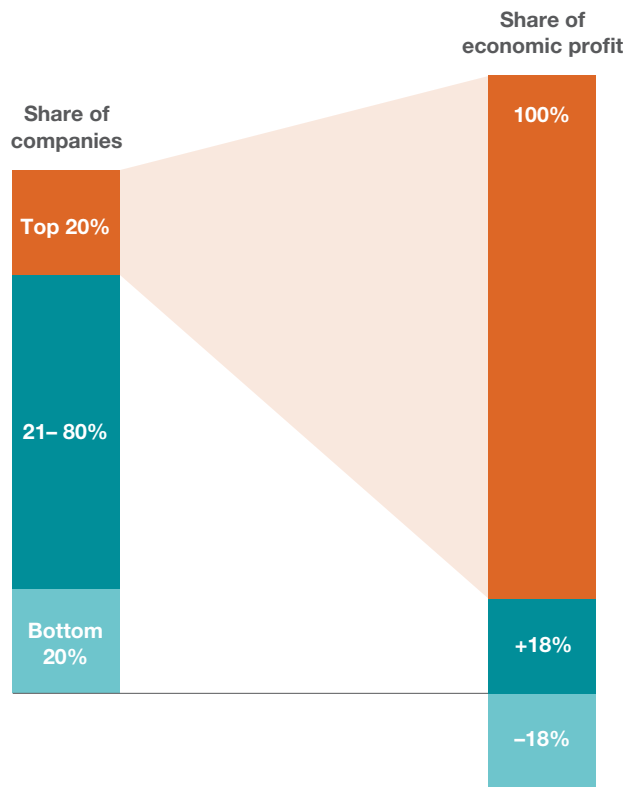
² In our broader research effort, we partnered with *The Business of Fashion*, a leading digital resource that provides daily business intelligence on technology, brands, and designers for industry executives and creative talent worldwide.

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 For a complete analysis of the industry's prospects, see *The state of fashion 2017*, on [McKinsey.com](https://www.mckinsey.com).

Exhibit

Fashion is a winner-takes-all industry.



Source: McKinsey Global Fashion Index, 2016

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