ADOPTING A SUBSCRIPTION MODEL IN LUXURY FASHION WITH SAP®

CLARKSTON CONSULTING

As shopping landscapes shuffle fewer customers through storefronts and more through e-commerce channels, fashion outlets are hailing the signal to adjust their operations in the face of changing consumer behavior. The rising global cost of housing, education, and utilities cements this change, causing stagnation in high-end consumption. The decrease in consumer purchasing power (along with age-old subversive market tactics) has led to rapid growth in the pre-owned luxury goods market, with second-hand exchanges accounting for more than 27.3 billion USD in 2018.

While the sale of pre-owned luxury goods can proliferate a brand's visibility in the market, these sales fail to tangibly improve financial health and in some cases can actually harm a brand's equity if secondhand items fall prey to copy-cats or fail to maintain the company's material and design standards. The pre-owned luxury goods market is projected to increase at a compound annual growth rate of 10.8% between now and 2023. As this market subverts new sales and threatens to cannibalize market share, companies should look to consider subscription models to bring back revenue streams and uphold brand status.

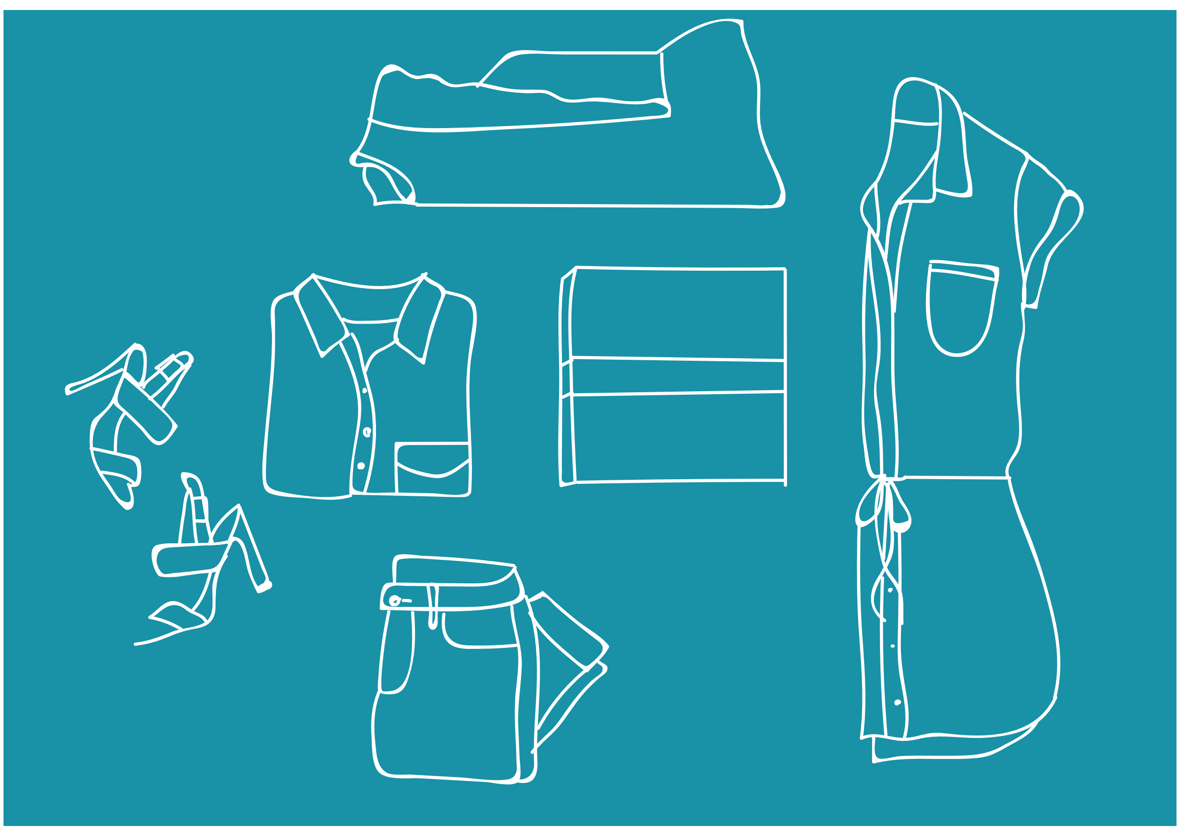
Reports show that non-luxury clothing rental services have a 25% operating profit margin, compared with traditional profit margins generally from 4% to 13%. For luxury brands, this operating margin and revenue could be even higher with a subscription model that combines both rentals and purchases to capture the widest breadth of sales. Rental items have high conversion rates into new purchases, and it's evident that the repeated exposure of consumers to a high volume of garments is an airtight way to solidify brand loyalty.

While it's expected that exclusivity concerns may arise when considering subscription models, the trade-off to increasing access is only slight when considering the damages that subversive markets do to luxury fashion brands. The allure of luxury fashion items is relatively constant, and as incomes stagnate and costs increase, providing shoppers with clean-market, direct-to-consumer items can proliferate your brand's desirability while maintaining a high enough price point to remain exclusive. Consumers will find a way to get ahold of luxury goods by any means necessary, so why not give your consumer base access to the real deal in a model that proves profitable for your business?

1. What has created an environment ripe for luxury fashion subscription models?

CONVENIENCE AND PERSONALIZATION

Global demand for convenience and ease of purchase is heightening, and as shoppers are avoiding the experiential trip to the store in droves, luxury brands should consider opening new channels through which they can funnel this lost foot traffic. The decline in brick-and-mortar visits is further augmented by the growing number of on-the-go consumers. As shoppers face increasing competition for their time and attention, personalization becomes key in directing this focus to worthwhile shopping experiences. The hyper-personalization of fashion has long been central to design operations, but now that sustainable, off-trend, and diverse sizing options permeate stores everywhere, consumer expectations have found new horizons that glow with the promise of precisely tailored products.



REACHING THE CONSUMER

As the subscription model trend has risen in the food and beauty industries, consumers are becoming accustomed to applying similar conveniences in other areas of their lives. For companies in luxury fashion where sales are often unpredictable, a subscription model provides a much more stable and calculable revenue stream that can be used to sustain and attract customers while gathering insightful data to better personalize these shoppers' experiences.

To maintain and grow a consumer base, fashion retailers must extend through every avenue to reach the end consumer. Subscriptions models allow both for consumer access avenues and product personalization, as digitalization and e-commerce platforms minimize transaction costs.

2. What are the risks in moving to a subscription model?

SUBJECTIVITY

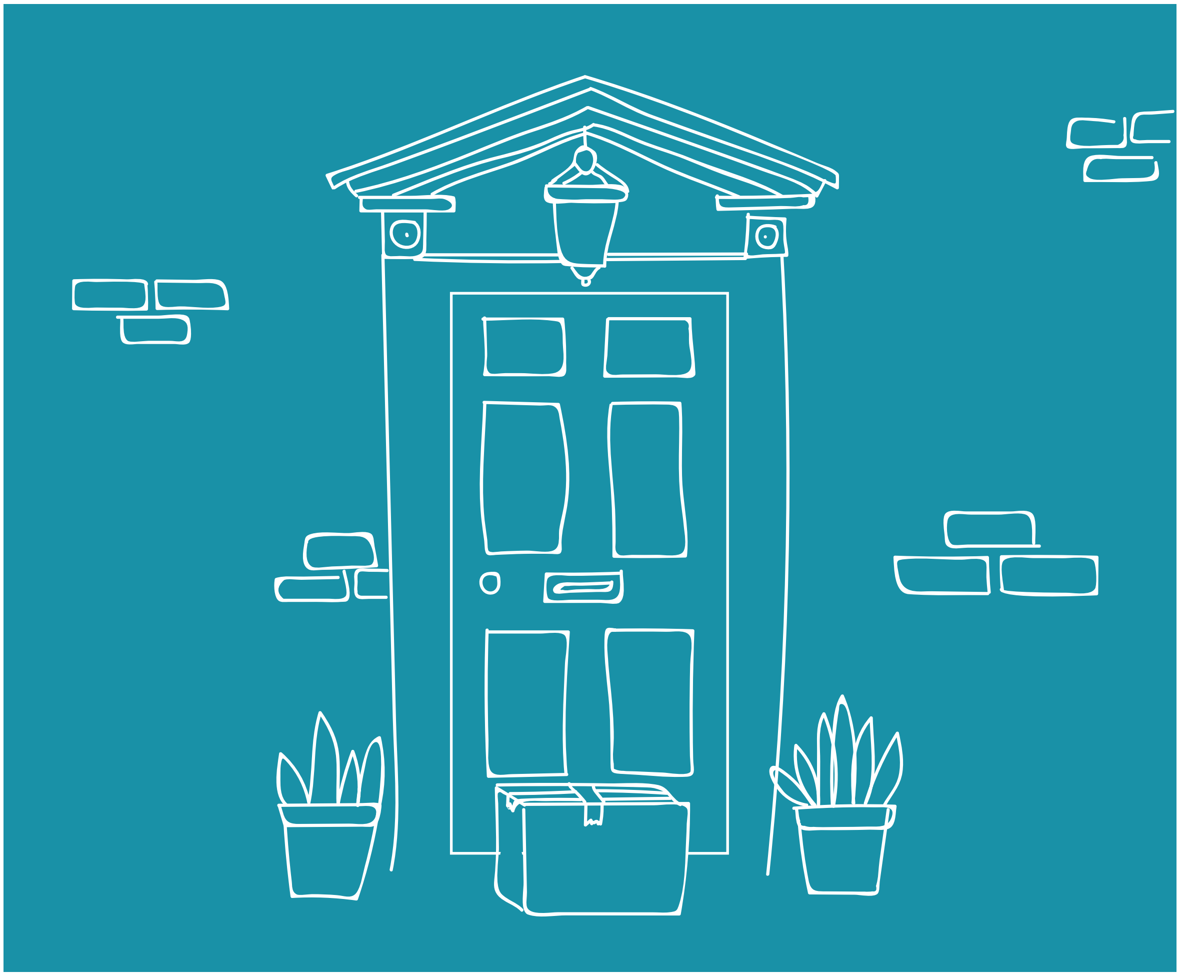
Logistically, one of the most prominent risks in adopting a subscription model is that consumers have narrow tastes. Clothing is inherently personal and subjective, and choosing the same garments that a consumer would choose for themselves becomes the algorithmic challenge of the modern era. On top of style, proper sizing can be difficult to judge for e-commerce apparel. At-home measuring has low consumer confidence, and because global sizing systems are loosely-regulated, it can be difficult to get all facets of a garment right when shipping it to a subscriber.

There are numerous analytics solutions that can tackle this problem, but it's also important to consider the potential consumer base. Providing a back-up size or additional stylistic consideration pre-shipment can assuage some of the logistic hurdles associated with satisfying customers. Furthermore, shoppers who regularly engage in e-commerce will likely be aware of the unavoidable risks, and for many subscribers the ease and comfort of trying on in their own home with friends or family present will outweigh the uncertainty inherent to ordering online.

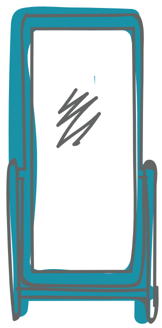
INVESTMENT

Perhaps the biggest risk that luxury fashion subscription models face is the investment and inventory necessary to uphold such an operation. Unlike non-clothing subscription models that may send a sample or reduced portion of the full product, a fashion subscription would need to send the entire garment to the consumer. Here's where much hesitation can arise, because it's inherently risky to send highly coveted products out to consumers without full confidence in the permanence of their purchase.

But unlike the value diminishment that occurs to a car once it's driven off the lot, luxury brands can protect their inventory by implementing strict return requirements so that consumers understand the risk in damaging the item. Because items have such exclusive pricing, charging higher premiums and encouraging customers to purchase garment rental insurance can further mitigate both the company's and the consumer's risk in a subscription model.

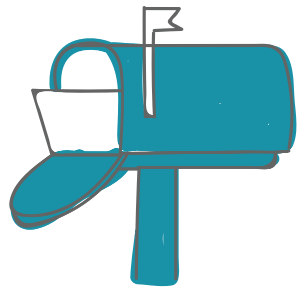


What kinds of subscription models exist?



TRY BEFORE YOU BUY

In this model, consumers have a set number of clothing items sent to them with no explicit commitment to buy. They're able to try on the clothes in the comfort of their home and then purchase the items at will, returning any unwanted garments. If a decision is not made within a specific time frame, the customer is charged for the bundle of items at full price.

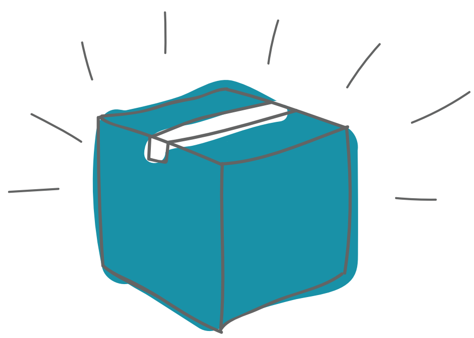


FLAT FEE

The customer pays a single fee, usually billed monthly, and has access to rent a pre-determined or unlimited number of clothing items. The customer may wear each item as many times as desired and choose to either return or buy (typically at a reduced rate) each of these items. Once the determination is made and typically the clothes are returned the consumer receives a new bundle of clothing.

CURATED SELECTION

A personal stylist sends the customer items based on a profile they create, with specific inputs regarding size, style, color, and other garment preferences. After receiving the selected garments, the customer chooses those which they'd like to keep and pays the listed price for these items.



SURPRISE BUY

Here, the customer subscribes to a one-time or repeating shipment. After some stylistic profiling and price range specification, customers are sent a shipment containing a number of selected items with no option for return.

4. What are the key measures for success in moving to or establishing a subscription model?

The major appeal of a subscription service is the idea that a consumer can receive items that they personally choose or that they would normally have picked out for themselves according to their preferred style. This makes a robust analytics program integral to the success of the model. Collecting the direct data provided by the consumer is only the tip of the iceberg, as evolving tastes and changing stylistic preferences will create a feedback loop of customer preferences in need of management. Having a strong, well formulated algorithm with AI capabilities can provide a company with the necessary insights specific to each customer's profile.

Furthermore, a subscription model only works when it's backed by a strong e-commerce foundation. Having a long-standing e-commerce platform can ease a company's transition to a subscription model, and for younger platforms, the continual alignment of online operations can serve to jump-start a successful subscription service. Stores with a heavy brick-and-mortar presence may have a more difficult transition when integrating technology but can use these physical stores as catalysts in promoting the subscription model and attracting more potential customers.

Ultimately, a platform with the capability to support the complex logistics, financial, and operational needs of a subscription model is critical to a successful operation. Every consumer will have a personalized profile in need of stylistic and financial maintenance, making strong customer service capabilities a necessity. With merchandise flowing both directions through the supply chain, tracking and visibility become obvious priorities as logistics directly contribute to consumer satisfaction.

5. How can SAP support an organization's transition to and management of a subscription model?

FINANCIAL

SAP Subscription Billing supports recurring payments and subscription models, controlling products, rate plans, subscription management, and billing. As a public cloud solution built on micro-services, it's designed to help companies rapidly implement and deploy subscription services in a scalable environment while leveraging other SAP cloud and on-site resources.

The billing application automatically generates billing data for subscriptions, reflecting accurate rates and aggregating this data into bills containing gross amounts. The integration of SAP Subscription Billing enables the automatic processing of generated bills and sends these as external billing document requests (EBDR) to SAP S/4HANA Cloud Sales Billing. The automated system links the financial records of every transaction to your sales platform, pulling data through both operations to simultaneously track revenue and number of sales.

SUPPLY CHAIN

As you move from a traditional consumption model to a subscription model, reframing supply chain operations is essential as items will now be moving both up and down the chain when consumers receive and return items. SAP platforms carry a standard process for returns, where every order generates a Return Delivery Document. Returned merchandise are recaptured with reference to their corresponding Sales Order, allowing the items to ultimately be returned to the respective seller.

These returned goods are received into Blocked status to allow your quality department to assess the product appropriately and direct it down the correct channel. If the product is approved in saleable condition, quality can release the product back into inventory. Once the items are cleared, SAP tracks and labels them as fresh inventory available to fulfill other orders, creating a closed ecosystem with detailed tracking and checks-and-balances.

SALES/MARKETING

The SAP Sales Cloud creates a complete view of customer profiles and alerts you to customer-specific opportunities by automatically monitoring shopper activity. Using real-time predictive analytics, this software amplifies your sales strategy by prescribing content recommendations for each consumer based on their profile. Furthermore, it has the capability to automatically replicate billing data from the SAP Subscription Billing to SAP S/4HANA Cloud Sales Billing, effectively combining customers' financial and behavioral data. This Sales Billing not only automates resource-intensive financial processes but can also fortify the customer's experience with highly personalized predictions and customer service.

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For more information about how we can help your company with the challenges and opportunities in luxury retail, please contact us.

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