Sportswear

It had been quite a day for Ms. Leslie Olivera, a sourcing manager with the Foxtrot Company. The day started as all Mondays at the beginning of the month did with a visit to Sportswear. As she walked in the door, the owner of Sportswear, Charles Richards, greeted her with a question, "Leslie, how would you like to buy my business?"

The Apparel Industry: 1980-1994

To understand the value of Sportswear (and other garment assemblers offering similar services) to the apparel industry in the 1990s, a look back to the previous decade is necessary. Apparel manufacturers enjoyed a boom during the go-go Reagan years. While fashion trends may periodically drive apparel growth in certain areas, overall demand for apparel is driven largely by economic growth. According to government statistics, Americans average disposable personal income grew at an average annual rate of 7.8% from the end of 1980 to the end of 1988.[1] During this period, apparel sales surged 7.4% annually, on average. Apparel items of choice bore high-priced labels and were purchased at department stores.

During the late 1980s, however, several events occurred that changed the way the apparel industry conducted business. For one, the retail industry consolidated, primarily due to easy money and entrepreneurs that saw an opportunity to turn a quick profit. Most of these entrepreneurs made what proved to be fatal miscalculation: namely that the retailers they purchased would generate enough volume to support the funds borrowed to pay for these leveraged buyouts.

Then, in late 1989, amidst fears of an imminent recession, consumer spending on apparel ground to a halt. In addition, consumers' income growth slowed. From the end of 1989 through the end of 1992, disposable personal income rose at an average annual rate of 5.4%, according to government statistics. Expenditures on clothing during this period increased even more slowly, at only a 3.6% average annual rate. While the growth rate slowed, recorded retail apparel sales in 1994 were more than $128 billion.

[1] All figures quoted in this section were taken from various reports produced by the U.S. Department of Commerce.

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When the recession hit in late 1990, many retailers could not generate enough cash to pay the interest owed on the funds that banks had loaned in a healthier economy. Desperate to increase volume and raise cash pay off their debts, retailer slashed prices. As a result, shoppers became accustomed to such sales ploys. Presently, most consumers are unwilling to purchase an item unless it appears to be a bargain, either marked down or "valued-priced", in retailing parlance. Furthermore, consumers in the 1990s spend only 4.2% of their disposable income on apparel, compared with 4.5% in the 1980s. This difference represents a loss of billions of dollars in potential sales annually for the retail apparel industry.

While the overall apparel industry lacked excitement, certain niches enjoyed above-average growth. The apparel industry was divided into two tiers. The first tier consisted of more expensive national brands and accounted for 30% of overall industry sales. The larger second tier, 70% of total industry sales, consisted of more moderately priced private label and secondary brands. Industry sources believed that well-capitalized companies producing second tier apparel would enjoy substantial growth in the future, as consumers increasingly preferred moderately priced apparel expensive "status" brands.

Thanks to several challenges the industry faced – high debt levels incurred in the late 1980s, consumers' expectations of a bargain, and the mediocre level if demand for apparel – retailers became more savvy money managers in order to turn a profit. In addition, traditional apparel retailers, such as department stores and specialty outlets, were also faced with increased competition from discount stores (e.g., Wal-Mart) and chain stores (e.g., Sears) for the consumer's dollar (See figure 1). In the past, apparel sales had not been a source of growth for these mass merchandisers. This changed as these firms spruced up their apparel offerings. At Sears, for example, apparel sales accounted for 26% of total sales in 1992, but 60% of operating profits. Future plans called for apparel sales to become as much as 40% of total revenues at Sears.

Figure 1
Percentage Distribution of Market Share by Retail Outlet

	1991	1994	Market Share Change
Discount Stores	**29.3%**	**31.7%**	**2.4%**
Department Stores	**24.2%**	**22.7%**	**-1.5%**
Specialty Stores	**19.2%**	**17.6%**	**-1.6%**
Chain Stores	**14.8%**	**15.3%**	**0.5%**
Direct Mail	**5.4%**	**5.7%**	**0.3%**
Other Outlets	**7.1%**	**7.0%**	**-0.1%**

One response by many retailers was to turn their vendors, the apparel manufacturers, for improved efficiencies. Retailers and vendors historically have had an adversarial relationship. In the 1990s, however, retailers strained the relationship even further by asking vendors to pay for things that in the past were not the vendor's responsibility. For example, some retailers asked vendors to pay for advertising, to build in store displays,

or to pay special override commissions to sales clerks that sell their merchandise. Another example of the way retailers strained the relationship with vendors involved inventories. Stocking inventories had been one of retailing's highest costs. Increasingly, retail stores don't even have stock rooms. Instead, retailers required frequent deliveries of non-fashion items and two to three deliveries of fashion merchandise during a season to keep their departments stocked with fresh merchandise.

Some vendors struck back by taking matters unto their own hands. Designers like Ralph Lauren and Liz Claiborne responded to pressures from retailers by operating their own chains of exclusive stores. Most vendors, however, choose not to open their own outlets, and discovered ways of their own to reduce costs.

Because labor was such a significant cost component in apparel manufacturing, most vendors focused on either automating production or sourcing offshore. VF corp. and Fruit of the Loom, two of the largest apparel manufacturers in the U.S., (see Figure 2), reduced cost substantially through efficient automated manufacturing. Other apparel manufacturers shifted sourcing out of the country, most recently to the Caribbean, Central America, or South America to take advantage of low hourly labor rates. At the same time, major companies produced an estimated seventy percent of their sales in U.S. plants in 1993.

Figure 2
Ten Largest Apparel Markers (1994)

Company	Sales (Mil. $)	Company	Sales (Mil. $)
1. VF Corporation	3,824	6. Russell Corporation	931
2. Liz Claiborne	2,194	7. Leslie Fay	772
3. Fruit of the Loom	1,855	8. Hartmax	732
4. Kellwood	1,078	9. Warnaco	6,225
5. Phillips- Van heusen	1,043	10. Crystal Brands	589

Both responses – automation and offshore production – had penalties associated with them for fashion conscious segment of the apparel market. The down side of automation was the the reductionof differentiated merchandise offered consumers. Automation was most effective at reducing cost when the same or similar products were made in long production runs.

On the other hand, offshore production was efficent at providing short production runs of more differentiated merchandise. However, lead times were as long as nine months. The producers had to decide, therefore, nine months in advance of the season how much of eachitem to order by size, color, style, and so forth. Not surprisingly, this led to an under supply of those items that became "hot" during the season and an over supply of the "not so hot" items which had to be marked down significantly. While resupply during the season from foreign sources was possible, it required air freighting garments which was not economically feasible except for the most expensive items.

For these reasons and others, a number of firms in the apparel and related industries developed the "Quick Response" program. The objective of this program was to enable apparel manufacturers to act rapidly on smaller and more frequently recurring orders if the many styles. While this program entailed numerous initiatives, it also enhanced the situation for some garment assembly companies (called finishers) such as Sportswear.

Sportswear was one of many small firms which performed garment assembly operations on a quick turnaround basis for the large apparel manufacturers. These small firms employed less than 50 people, in general, and had come a long way since their depiction as "sweat shops." Essentially, they filled the role for the rapid assembly of garments during the sale season for items which have some fashion element. By supporting Sportswear and other similar firms, the apparel manufacturers provided frequent response to the retailers without having to carry large inventories of the finished goods.

In addition to offering quick response, the items produced by these small firms provided similar revenues per garment to those produced offshore. The labor cost portion of the Sportswear garments was higher for the apparel manufacturers than what would have been incurred had production taken place in a low hourly wage developing country. These cost were offset somewhat by the reduction in transportation, duty, administrative, and holding costs. However, the main advantage was increased sales revenue since firms adjusted to what was selling. Production during the sale season by companies like Sportswear led to enhanced sales for the retailers by increasing availability of items that were selling beyond initial projections. In addition to increasing the availability of what was selling, the amount of stock for items selling less than forecasted was reduced also. Merchandise selling at mark down decreased from 53.6% of the total apparel market in 1991 to 50.7% in 1993.

Sportswear

Sportswear was incorporated in 1963 by Mr. Charles Richards, the original and current president. At that time, the firm performed assembly operations for several of the large apparel manufacturers, and competition was based on price. During the late 1980s, price competition became intense for reasons noted earlier. Mr. Richards did not have the capital to automate, and without this he did not believe Sportswear could compete on the basis of price against producers in low wage developing countries. Instead, he approached a major client, one of whose divisions was a large mail catalog firm for women's fashions. A major problem for the catalog firm was forecasting how many of each item to order in advance of the sale season. Mr. Richards suggested that the firm purchase approximately 80% of what it thought it would sell form foreign sources, and that he would fill in the remainder of the items during the sale season. In 1988, a trial was conducted, and the mail catalog firm was very impressed with the results.

Once Sportswear demonstrated the ability to respond within two weeks with few errors on a regular basis, the firm became the finisher of choice for certain apparel items for the mail order firm. Other divisions of the client learned of this success, and sought or established finisher with similar capabilities.

Mr. Richards continued in his role as manager of the 35 employee firm located in 3000 square feet in a warehouse district near downtown Boston. Sportswear has continued to process orders for women's shorts, skirts, pants, etc., known in the trade as women's bottoms. (See Exhibit 1 for further information on the women's segment of the apparel industry.) Pre-cut material was received from a contract cutter, assembled into bottoms, prepared for sale ("bagged and tagged"), and held until collected by the shipper. Based on the operations in 1994, sales revenues were almost $500,000 (See Exhibit 2 for details).

The Production process at Sportswear

The assembly process at Sportswear was the same whether the product was women's shorts, skirts, or pants. The time needed to perform each step in the assembly sequence was determined by engineers from Foxtrot when they had first certified Sportswear as a supplier.

At the start if the assembly process, belt loops were attached to the garment using a special piece of equipment designed exclusively for this task. This highly specialized machine placed the necessary belt loops on the garment in five seconds which included the time needed to put the piece on the machine and to remove it from the belt looper.

After looping, the lining is pressed and then serged. Pressing required twenty seconds per unit. At serging, or side stitching, the back and front of the garment were attached to one another. The serging equipment was capable of processing six units per minute.

One worker performed the belt looping, pressing, and serging operations for each unit or garment. After that worker had processed five garments through the belt looping, lining, and serging, the five units were collected into bundles before the garments were sent to the seamstresses. When bundling, the operator also made certain that all the pieces for each unit were present, and that the pieces for each unit matched in terms of color. The task of bundling five units can be performed at the rate of sixty bundles per hour.

The bundles were placed on a distribution table. The seamstresses went to the table and picked up a bundle after completing their previous bundle. Twenty-eight sewers were employed, and each was able to assemble seven units per hour.

The units then went to the button placement machine. This machine operated in a similar fashion to a paper stapler; that is, the button was stamped onto the material and secured in place at the same time. The machine was able to process 450 units per hour.

The next operation was performed at the buttonhole maker machine. The total time for performing this operation was six seconds. Currently, one worker was assigned to those two tasks of button placement and buttonhole making.

Units then went to one of the two final pressing machines. Each of these machines was able to process thirty units in an hour. Each of the machines had an operator assigned to it.

Price tags were then placed on each item after final pressing at the rate of 360 units per hour. A final visual inspection was performed which took seven seconds per unit. Any garments found to be defective were separated from those which passed inspection. Price tagging and the final inspection were performed by a single operator.

At the next step, packaging, items that passed inspection were placed in clear plastic coverings while those found defective were placed in blue plastic. Regardless of whether blue or clear plastic wrapping was used, a worker required two minutes per unit to perform this task, and were two employees assigned to this task.

Selected information about the equipment used at Sportswear is provided in Exhibit 3. While the equipment was old, it had been well maintained. Equipment experts from Foxtrot who had visited the plant were very impressed, and they believed that the equipment would mot require replacement for at least fifteen years if the current level of maintenance was continued.

Staffing at Sportswear

All production was performed on a single shift which ran from eight in the morning until four in the afternoon. All production personnel at Sportswear were paid for the eight hours, except for the seamstresses who were paid on a piece rate basis. Of these eight hours, workers were given thirty minutes for lunch and two fifteen minute breaks during the day.

Because of the short times required to perform many of the production steps, certain production steps had been grouped into clusters (See Figure 3). Workers had been cross trained so that only a small number of them were needed to complete the different tasks un each cluster. At present, only seven workers were needed to perform the work, excluding the sewing operation.

Figure 3
Task Clusters and Number of workers Assigned to Each Cluster
(noted in parentheses)

Cluster 1 (1)
- pressing of lining
- belt looping
- serging
- bundling

Cluster 2 (1)
- button placement
- button hole making

Cluster 3 (2)
- final pressing

Cluster 4 (1)
- price tagging
- final visual inspection

Cluster 5 (2)
- packaging

Each of these seven employees received $6.50/hour. With the cost of fringe benefits and other factors included, the cost to the firm was $8.50 per hour. These seven workers also shifted between different clusters to alleviate the boredom involved. In general, personnel were trained in less than an hour to perform any task listed above.

The seamstresses, on the other hand, only performed the sewing operation. For each unit produced that passed inspection, a seamstress received $2.50. The firm incurred another $0.50 per item in other labor related costs. Experienced seamstresses, such as those at Sportswear, were able to sew at the rate of seven units per hour. However, the level of work had never required them to produce at this rate over the course of a day.

The Future

Over the two years that Leslie had worked for Foxtrot, she and Charles Richards had become friendly and they ate lunch together monthly. During their conversations, Leslie had expressed an interest in owning her own business one day. Generally, sourcing managers remained in that role for three years, and, if successful, were then given responsibility to develop, rather than manage, sources and sourcing arrangements. That Charles made the offer to her came as a bit of a surprise that day since he had not mentioned selling Sportswear before.

Leslie was aware that the opportunity to grow the business at Sportswear existed. As a sourcing manager at Foxtrot would be pleased for Sportswear to perform more work. Performance by Sportswear had been outstanding. Never had a shipment been late and never had goods been damages. The only items returned in blue bags were defective because of the materials supplied by another of Foxtrot's suppliers.

Managers at Foxtrot had raised the possibility of expansion with Charles in the past but he had declined. He was satisfied with the returns he was making and saw no reason to take on more work. However, he had recently experienced health problems, and was concerned about the future of Sportswear. Much of his concern stemmed from his interest in the work force, many of whom had been with the firm for ten years or more. If Sportswear closed, some of these persons would have difficulties finding work. In addition, most employees lived near the firm. Hence, even if they did not find other possibilities, most would have to travel from their local community which they did not want to do.

Foxtrot was willing to double the volume allocated to Sportswear at almost anytime. Furthermore, given the firm's performance, Foxtrot was willing to sign a three-year contract for this increases volume subject to Sportswear continuing to meet high levels of delivery and quality standards. (The standards to be included in the agreement would be 95% on-time delivery and 99% performance to standard in teams of garment assembly.) If, after one year, sportswear met the conditions of the contract, Foxtrot would be willing to increase further the volume allocated to Sportswear.

As Leslie thought about Charles' offer, she realized that the only way to make a financial success of this or any other acquisition was through growth. Financial returns were not her only concern, but they had to be considered heavily. Charles was asking for $250,000. In addition, he did not require any money down, and would accept payment over a six-year period. For this price, Leslie received title to the Sportswear name, all equipment, and assumed the remaining ten-years on the building lease.

In her two-years with Foxtrot, Leslie had seen several similar situations where sourcing personnel had acquired successful small supplier firms whose owners wished to sell their business. In these situations, Foxtrot had paid for shipments in advance for up to three months if the previous owner remained on as an advisor for this period. When asked about this, Charles agreed to remain as an advisor for the firm for the first three months if Leslie bought the firm. Hence, the working capital required to enter the business seemed to be in place.

Growing the business was another question. How much more equipment would be needed? How many more workers would she need to find, recruit, select and train? The current foreman had managed groups as large as forty persons in previous situations successfully. The foreman had indicated that if the firm employed more than forty persons in production, an assistant foreman would be need to be added. As Leslie thought about this comment and others, she wondered if the opportunity would be financially rewarding, and, if so, whether the rewards would be worth the responsibility and concern.

Also on Leslie's mind was her situation at Foxtrot where she was doing well. Leslie's supervisor indicated that Leslie's performance had been very good, and that she was being considered for early promotion. With this in mind, Leslie wondered if it made sense to buy Sportswear now. If not, she thought, would she ever do something like this?

EXHIBIT 1
APPAREL MARKET MONITOR
1992-1994

	TOTAL MARKET SIZE – MILLION $						PCT. CHANGE VS PRIOR YEAR			
	JAN-JUN 1992	ANNUAL 1992	JAN-JUN 1993	ANNUAL 1993	JAN-JUN 1994	ANNUAL 1994	JAN-JUN 93/92	ANNUAL 93/92	JAN-JUN 94/92	ANNUAL 94/93
TOTAL WOMENS APPAREL	30967	64991	31169	67636	33309	71841	.7	41	69	62
TOPS	8035	17890	8495	19545	9242	20943	5.7	97	88	72
WOVEN SHIRTS AND BLOUSES	3730	7510	3883	8209	4046	8433	4.1	93	42	27
CASUAL KNIT SHIRTS	2897	5674	2872	5801	3112	6384	.9	22	8.4	10.1
SWEATERS	1117	3928	1312	4288	1250	4116	17.4	92	4.7	4.0
OTHER TOPS	291	697	429	1247	834	2010	47.4	78.8	94.5	61.2
BOTTOMS	4759	9687	4753	9866	5197	10731	.1	1.8	9.3	8.8
JEANS	870	2184	953	2373	994	2540	9.6	8.7	4.2	7.1
SLACKS AND PANTS	1829	3694	1749	3690	1971	4204	4.4	.1	12.7	13.9
SHORTS	1469	2341	1373	2148	1510	2356	.65	.82	10.0	9.7
LEGGINGS/STIRRUPS	281	918	372	1099	395	1042	32.1	19.7	6.2	5.2
OTHER BOTTOMS	310	551	306	556	328	588	.12	.8	7.0	5.9
TAILORED CLOTHING	8748	16370	8442	16312	8839	17300	.35	.4	4.7	6.1
SUITS	1334	2435	1337	2610	1417	2934	2	7.2	6.0	12.4
DRESSES	4068	7289	3689	6848	4036	7700	93	.60	9.4	12.4
SKIRTS	2008	4012	2021	4130	1982	4061	7	2.9	1.9	.17
OTHER TAILORED CLOTHING	1338	2635	1395	2724	1404	2605	42	3.4	.6	.44
OVERCOATS AND JACKETS	1477	3683	1411	3784	1532	3818	.45	2.7	8.6	9
INTIMATE APPAREL	3499	7634	3508	7938	3690	8527	.3	4.0	5.2	7.4
BRAS	1288	2591	1231	2626	1325	2850	.44	1.3	7.6	8.6
SHAPEWEAR	158	338	182	349	153	324	156	3.1	15.8	.70
DAYWEAR	329	633	316	637	316	637	.38	6		
PANTIES	619	1333	616	1370	674	1515	.5	2.8	9.5	10.6
SLEEPWEAR	753	1918	834	2158	887	2351	108	12.5	6.3	8.9
ROBES AND LOUNGEWEAR	352	820	328	798	334	849	.68	2.7	1.8	6.4
HOSIERY	1857	3794	1971	4019	2028	4083	61	5.9	2.9	1.6
SOCKS	354	878	394	969	436	1073	114	10.3	10.7	10.8
SHEER HOSIERY AND TIGHTS	1504	2916	1577	3050	1592	3010	49	4.6	.9	.13
SWEATS AND WARM-UPS	667	2274	763	2369	743	2430	144	4.2	.27	.26
SWIMWEAR	817	1209	771	1164	769	1166	.56	3.7	.3	.2
OTHER APPAREL AND ACCESSORIES	1108	2531	1055	2640	1270	2844	.48	4.3	20.3	7.7

Exhibit 1 (continued)
PRODUCT CATEGORY DEFINITIONS

Product Category	**Description of Products Included**
TOTAL WOMENS APPAREL	All clothing and accessories worn by females ages 14 and over except if garment was size Girls 7-16
Tops	
Woven Shirts and Blouses	Woven Shirts and blouses
Casual Knit Shirts	Placket shirts, tee shirts, turtlenecks, other casual knit shirts
Sweaters	Cardigans, pullover, sweater jackets
Other Tops	Tube tops, halter tops, shirt jackets, other casual shirts, vest, bodysuits
Bottoms	
Jeans	Blue denim, other colored denim, corduroy and other fabric (khaki, twill) jeans
Pants	Dress and casual slacks
Leggings/Stirrups	Leggings/stirrups (not hosiery, tights)
Shorts	Walking shorts, tennis shorts, running shorts, bike shorts, other shorts
Other Bottoms	Overalls, coveralls, shortalls, jumsuits
Tailored Clothing	
Suits	Pants and skirt suits
Dresses	Dresses, jumpers
Skirts/Skorts	Skirts and culottes
Other Tailored Clothing	Blazers, Tennis dresses, uniforms
Outercoats and Jackets	All weather coats, raincoats, dress coats, other coats of fur, leather, wool, etc., ski jackets, golf jackets, windbreakers, snowsuits, other jackets, outer vests

Intimate Apparel	
Panties	Panties
Shapewear	Girdles, control panties, hip shapers
Bras	Bras, nursing bras
Daywear	Slips, camisoles, teddies
Nightwear	Nightgowns, pajamas, nightshirts, blanket sleepers, other nightwear
Robes/Loungewear	Robes, housecoats, hostess gowns, caftans, other loungewear
Hosiery	
Socks	Knee-hi's, crew socks, anklets, footsocks, athletic socks, dress socks, casual socks
Pantyhose/Hosiery	Pantyhose, opaque pantyhose, tights (not used for activewear), stocking and sheer knee-hi's
Sweats and Warmups	Sweatshirts, sweatpants, sweatshorts, sweatsuits, warm-up suits
Swimwear	Swimwear
Other Apparel and Accessories	Scarves, mufflers, hats, gloves, belts, handbags, wallets, leotards, unitards, exercise tights, long and thermal underwear, other accessories or apparel items.

Exhibit 2

ABBREVIATED INCOME STATEMENT

Sales: 300 units/day x 240 days/year X $6.50/unit	$468,000
Expenses	
Material Costs	0
Direct Labor (fully costed)	
Cross-trained personnel	114,240
(7 persons x $8.50/hour x 8 hours/day x 240 days/year)	
Seamstresses	216,000
(300 units/day x 240 days/year x $3.00/unit)	
Foreman's' salary and benefits	40,000
Occupancy costs	
Lease payment	30,000
Utilities	10,000
Maintenance	5,000
Resulting Contribution	$52,760

Exhibit 3

EQUIPMENT INFORMATION FOR SPORTSWEAR

Equipment Type	Number In Use Now	Total in Firms	Time per unit	Cost per machine
Belt Looping Machine	**1**	**1**	**5 sec/unit**	**$15,000**
Liner Presser Machine	**1**	**1**	**20 sec/unit**	**$13,200**
Serging Machine	**1**	**1**	**10 sec/unit**	**$14,210**
Distribution Table	**1**	**1**	**space for 100 bundles**	**$100**
Sewing Machines	**28**	**40**	**514 sec/unit**	**$1,200**
Button Placement	**1**	**1**	**8 sec/unit**	**$11,850**
Button Hole Maker	**1**	**1**	**6 sec/unit**	**$11,320**
Final Pressing Machines	**2**	**2**	**120 sec/unit**	**$17,500**