e-Commerce Fulfillment Models for Luxury Brands in Asia

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Abstract

Asia-Pacific countries have experienced a rapid rise in Internet usage in recent history. China, in particular, has seen 40% of its population (or 500M people) connect to the Internet in the past 10 years, and continues to experience an increase in its user base. This large user base, coupled with a rise in wealthy households and per capita spending, is driving a dramatic increase in e-Commerce retail, specifically in the luxury goods space. Consumption of luxury goods in China has reached $9.4B in 2010, second only to Japan in the world. As luxury purchase rates continue to increase in China, luxury fashion brands are investing many resources to understand the customer, develop the market, establish the supply chain, and deliver the products.

Polo Ralph Lauren (PRL), in order to continue its growth in China, is expanding aggressively through license reacquisitions and retail store developments. Furthermore, to provide its existing customers with additional products and enhanced services, and to capture consumers who live in cities without access to PRL’s brick and mortar stores, PRL has set its vision to develop an e-Commerce business in China. This thesis provides a fundamental understanding of PRL’s current business operations and of current e-Commerce fulfillment models for luxury apparel brands in China. An assessment of gaps was also conducted between current fulfillment operations of PRL and those of other luxury brands and 3PLs operating in China, specifically on delivery lead-time, last mile delivery options, end-to-end customer service, and return logistics.

From this research, we recommend general methods for luxury brands to manage and provide best in class fulfillment service. For PRL, we specifically recommend the company maintain ownership of all customer-facing activities to ensure quality. We also advise PRL to integrate all customer information from retail to e-Commerce, further strengthening its service offering and brand image. Furthermore, we recommend PRL to locate and outsource its initial DC in Shanghai and partner with FedEx and EMS for fulfillment.

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We would also like to take this opportunity to acknowledge the people we interviewed for this research. While we cannot mention the companies or names here, we appreciate all the time each and every one of you took to provide us with industry data and practices.

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Table of Contents

ABSTRACT ......................................................................................................................... 2
ACKNOWLEDGEMENTS ...................................................................................................... 3
TABLE OF CONTENTS ...................................................................................................... 4
LIST OF TABLES .................................................................................................................. 6
LIST OF FIGURES ............................................................................................................... 7
INTRODUCTION .................................................................................................................. 8
POLO RALPH LAUREN ...................................................................................................... 12
  POLO’S CURRENT OPERATIONS IN ASIA ................................................................. 13
MARKET INFORMATION ................................................................................................. 19
  THE CHINESE E-COMMERCE MARKET ................................................................. 19
  CHINESE LUXURY CONSUMERS ........................................................................... 21
  LUXURY APPAREL ....................................................................................................... 25
  SERVICE LEVEL DEFINITION .................................................................................... 26
  PAYMENT OPTIONS ..................................................................................................... 28
  IT ........................................................................................................................................ 29
  INVENTORY MANAGEMENT AND RISK POOLING ................................................ 29
  THIRD-PARTY LOGISTICS ........................................................................................... 30
  SUMMARY ..................................................................................................................... 32
METHODOLOGY ................................................................................................................ 34
CASE STUDIES ................................................................................................................... 40
  COMPANY A .................................................................................................................. 40
    Strategy ....................................................................................................................... 40
    Service Level .............................................................................................................. 40
    Customer .................................................................................................................... 42
    Distribution / Fulfillment ........................................................................................... 43
    Delivery ....................................................................................................................... 44
    Technology ................................................................................................................ 45
    Next Steps .................................................................................................................. 46
  COMPANY B .................................................................................................................. 46
    Strategy ....................................................................................................................... 46
    Service level ............................................................................................................... 48
    Distribution and Fulfillment ....................................................................................... 49
  COMPANY C KOREA LTD. ............................................................................................ 51
    Strategy ....................................................................................................................... 51
List of Tables

TABLE 1 PER CAPITA RETAIL SPENDING ONLINE IN CHINA BY C2C AND B2C, 2005 TO 2010 (ASIA ACCESS LIMITED, 2011) ................................................................................................................................. 20
TABLE 2 MAJOR TIER 1 AND TIER 2 MARKETS IN CHINA, Oligively Reference .................................. 21
TABLE 3 DELIVERY RATES THROUGHOUT CHINA WITH SHANGHAI OR GUANGZHOU AS CENTRAL DC LOCATION .................................................................................................................. 67
TABLE 4 DELIVERY RATES THROUGHOUT CHINA WITH BEIJING AND FUZHOU THE CENTRAL DC LOCATION .......................................................................................................................... 68
TABLE 5 RECOMMENDATION MATRIXES BY CUSTOMER TYPE ................................................................. 84
List of Figures

Figure 1 Internet Penetration Rate in China (Polo Ralph Lauren, 2011) ..................... 8
Figure 2 Forrester Research: China Online Retail Market Forecast 2009 – 2015
(Wigder, Sehgal, Evans, & Johnson, 2010)................................................................. 9
Figure 3 PRL’s Asia Supply Chain Service Structure..................................................... 14
Figure 4 PRL’s Current outbound Logistics and fulfillment for retail stores (Polo Ralph Lauren Asia Supply Chain, 2010) ................................................................. 17
Figure 5 Current and projected number of luxury shoppers in Asia (Bain and Company, 2010)................................................................................................................. 19
Figure 6 Luxury consumer type and spending breakdown (Atsmon, Dixit, Leibowitz, & Wu, 2011) (Atsmon, Dixit, Leibowitz, & Wu, 2011).................................................. 24
Figure 7 Using Shanghai as the central DC, average delivery rates are shown for
PRL’s tier 1 and tier 2 markets Green: FedEx demonstrated the lowest rate Teal:
SF-Express demonstrates the lowest rate Purple: Rates were similar between
FedEx and SF-Express............................................................................................................ 69
Figure 8 Using FedEx as the primary carrier, colored cities denote lowest shipping
rate from respective DC. Red: shipped from Beijing Yellow: shipped from Shanghai
Green: shipped from Guangzhou......................................................................................... 70
Figure 9 Recommended DC for PRL in its initial e-commerce launch ....................... 73
Figure 10 Customized dressing room allows the user to choose different tops,
bottoms, and shoe; the website will automatically fit the clothing to the model
that is of appropriate size of the customer and offer feedback on his/her
selection.................................................................................................................................. 82
Introduction

Nowhere in the world is online shopping growing as quickly as in Asia. The region now includes more than 40% of the world’s online population. This user base, coupled with a growing percentage of online shoppers and increasing per-capita online spending, is outpacing the North American and European e-Commerce market (Asia Access Limited, 2011). As shown in Figure 1, the greatest Internet penetration is occurring along the coast of China, but is moving in-land at a fast pace. Experiencing a 33% increase in users every six-month, China is expected to see its total sales triple over the next five years (Wigder, Sehgal, Evans, & Johnson, 2010). To gain a better understanding of this shifting trend in Asia-Pacific e-Commerce and what that will mean for the luxury apparel companies, we conducted focused research on the e-Commerce market in China, paying specific attention to market dynamics, consumer behavior, e-Commerce technology readiness, and fulfillment capabilities.

Figure 1 Internet Penetration Rate in China (Polo Ralph Lauren, 2011)
Prior to 2010, consumer-to-consumer (C2C) sales growth dominated e-Commerce retail. Websites such as Taobao.com, Alibaba’s business-to-consumer (B2C) and C2C marketplace, had an estimated 75% of the e-Commerce market share. As of 2011, however, B2C has accelerated to become the fastest growing segment of total Internet transaction volume, leading e-Commerce to become an ever more-structured business channel in China (Asia Access Limited, 2011). As shown in Figure 2, Forrester Research estimates that the combined B2C and C2C revenues in China to reach $159B by 2015 (Wigder, Sehgal, Evans, & Johnson, 2010).

This rapid rise in B2C e-Commerce has given brands that traditionally operate brick and mortar retail shops the opportunity to better serve their existing customers and reach new consumers in regions of China they currently do not operate in. Therefore, it is of little surprise that the luxury apparel companies is investing a great deal of resources in Internet technology, logistics infrastructure, and transaction systems to build a robust supply chain that will allow them to secure a significant slice of this market.

At the start of this study, no luxury brands offered e-Commerce services in China. For example, many of the leading brands including Louis Vuitton, Gucci, and Chanel have multiple
retail stores, but only operate non-transactional websites in China. Armani was the first true luxury brand to launch e-Commerce in November 2010. This trepidation to enter the e-Commerce space highlights the industry’s lack of experience of how best to serve the Chinese consumer.

Polo Ralph Lauren (PRL) has operated in China through joint ventures with department stores and franchisees for many years. Recognizing the importance of the growing Chinese market, PRL has recently begun to reacquire its operating licenses in China to retake control of the brand and to expand its presence in the country. With over 50 physical stores fronts in China’s top cities, PRL is looking to further expand its sales in country via the Internet while maintaining its strong adherence to service, quality, and timeliness. To develop the market and grow the business, PRL is examining innovative fulfillment strategies to service the Chinese e-Commerce market. PRL looks to differentiate itself in China as a leader in the e-Commerce channel by providing a luxury shopping and fulfillment experience to its customers.

Because B2C e-Commerce is a relatively new concept in China, few proven supply chain models exist to deliver luxury service throughout the country. Major cities with well-developed infrastructure require different logistics and fulfillment services compared with emerging inland cities. Similarly, payment and return services also differ based on geography and city tier. To fully understand the market complexity, we conducted interviews with luxury apparel brands and third party logistics providers (3PL) in China on their supply chain operations. Through these interviews, common industry practices were compiled into case studies. Lastly, we generated new ideas to improve supply chain services for luxury fashion.
In the following chapters, we will discuss Polo Ralph Lauren, the current state of e-Commerce in China, and the Chinese consumer to provide a fundamental understanding of the marketplace. We will then highlight the importance of the supply chain both as a strategic and operational lever to help PRL achieve its Internet growth objective in China.
Polo Ralph Lauren

Polo Ralph Lauren, a luxury apparel and accessories, home furnishings and fragrance company, was started in 1967 by the American icon Ralph Lauren with the opening of his first retail store on Rodeo Drive in Beverly Hills, CA. This maiden store only carried a women’s line; however, in the next forty years PRL has expanded into the $4,978.9MM luxury group we know today. PRL currently has 14 business units that include Polo by Ralph Lauren, Purple Label, Black Label, Blue Label, Accessories, Fragrance, Home Furnishing, Children, Chaps, RRL, Rugby, Club Monaco, American Living, and watches. Currently, PRL is sold in 9,000 stores world-wide including 350 of its own Ralph Lauren, Club Monaco and Rugby retail stores. PRL’s largest account is Macy’s, which makes up 18% of its wholesale revenue. Additionally, PRL launched its first online stores, ralphlauren.com and rugby.com in the U.S., in 2000 making up 10% of its revenue (Hoover’s Online, 2011).

Over the past few years, PRL has been aggressively expanding into new markets and buying back licensees outside of the United States. In 2006, PRL launched its flagship Japan store in Tokyo. Similarly, PRL purchased its greater China license from Dickson Concepts in 2010 as well as its Korean license from Doosan Corp in 2011. PRL believes Asia is a large growth market; however, it currently represents less than 10% of sales for the company. Moreover, PRL has also been aggressive in creating visible international partnerships. For example the company is the official outfitter for the US Olympic Team, United States Tennis Association, US Open, and Wimbledon. These partnerships and acquisitions have positioned Polo Ralph Lauren to take advantage of new global markets (Hoover's Online, 2011).
PRL operates based on two main seasons, Spring and Fall, and three sub-seasons, Summer, Cruise, and Holiday. To manage the inventory for these seasons, production orders for all regions are placed at the same time and shipments are made 6-8 weeks prior to the season. The inventory that arrives is segmented by wholesale, retail, e-Commerce, and basic stock replenishment. In the US, PRL’s business is broken down to 70% wholesale, 20% retail, and 10% e-Commerce. Conversely, 98% of PRL’s business in Asia is retail (Kimpton, 2010).

**Polo’s Current Operations in Asia**

To best serve its customer and meet its business objectives, PRL’s supply chain team is guided by five core principles (Kimpton, 2010). These principles are:

1. No operational constraints on business development
2. Minimize investment in infrastructure
3. Scalable
4. Leverage full global network capability
5. Service measurement and alignment

These five principles have been utilized by PRL operations around the world; however, because the Chinese market is vastly bigger in size and faster in growth rates, the five principles have been tailored to fit the market dynamics (Kimpton, 2010). The guiding principles have become:

1. Flexibility to support growth and diversification
2. External partner capital for start-up
3. Operating costs appropriate to scope of business
4. Synergize with partner operations in region
5. Match solution to requirements

These tailored approaches are intended to encourage growth with minimal investment in scalable and integrated operations to meet service goals, and will also be the cornerstone for PRL’s e-Commerce supply chain going forward.
The overarching objective for PRL’s Asia Supply Chain and Global Transportation team is to make certain products are available for Polo Ralph Lauren’s customers. The team’s customers are the store and sales associates. In order to provide the right merchandise to the right stores at the right time, the operations team manages vendor compliance, inbound operations, inbound transportation, DC operations, outbound transport creative logistics and supply chain finance. From an internal operational review report, we were able to recreate PRL’s supply chain service structure shown by Figure 3 and outline PRL’s current operations (Polo Ralph Lauren Asia Supply Chain, 2010).

![Figure 3 PRL’s Asia Supply Chain Service Structure](image)

Vendor compliance is an integral part of production because each country within Asia has unique import regulations. These regulations differ in China, Korea, Japan and the other APAC countries, and as a result pose challenges to taking advantage of pooled inventory. Pooling inventory is important because it decreases holding cost by allowing PRL to carry less inventory; however, this approach only works if the product can be universally used. Between different end users and country requirements, PRL has had to understand how to take advantage of pooled inventory while still remaining flexible to meet the various regulations. Since many of these regulations have to do with product labeling, PRL has acquired the capability to create
country specific labels in the DC and attach them to its garments as one of the value added steps before shipping to stores. In order to coordinate these requirements, the vendor compliance team must work with the following internal teams: New York manufacturing, Hong Kong sourcing, US vendor compliance, inbound operations, trade compliance, and supply chain operations. This cross-functional approach has worked well for PRL, and as a result, the company has been able to decrease its inactive stock by three weeks over the past year (Polo Ralph Lauren Asia Supply Chain, 2010).

Similar to the vendor compliance team, the inbound operations group works with many cross functional groups to support the customer and manages a core set of services. The inbound team works with manufacturing, New York buying and planning, Hong Kong merchandising, technical services supply chain operations, and Hong Kong merchandise operations. The four core services the group provides are purchase order and delivery management, supply – supply matching, supply – demand matching, and product eligibility.

In order to manage the actual movement of goods into Hong Kong, PRL has a team working on inbound transportation. Half of PRL’s products that enter the Hong Kong DC come from approximately 120 manufactures based in China. The majority of these manufactures are located in southern China near the coast, but a trend is afoot of manufacturers moving inland. The remaining product comes from other Asia (25%), Europe (10%), South America, North America and Africa (15%) countries. These products are delivered to Hong Kong by DHL through air, sea and truck with the majority by truck. The inbound team works closely with global transportation, inbound operations, marketing, DC operations, finance, inventory control, and IT. Since requiring the licensed operations in China, PRL has cleared 3 million units with a 99.99% service level in on time delivery to its retail stores.
PRL has outsourced its DC operations in Asia to Om Log, a 3PL that specializes in fashion logistics including receipt count and sorting, warehousing, retail shop delivery and distribution (Om Log Supply Chain Solutions, 2010). PRL was able to leverage its working relationship with SNATT Logistics, Om Log’s parent company, in Europe to quickly expand into Asia without having to recreate the trust and service expectations with a new 3PL. With its DC located in Hong Kong, Om Log has offered impressive results with 99.9% on time to store delivery and carrier handover to date while remaining flexible. The company has room to expand with the increasing demand in Asia; however, its current location is limited in space. Om Log’s warehouse capacity is 1 million units, and it has achieved 3-4 inventory turns per year and growing. From this DC, Om Log manages creative storage, DC inbound operations, DC outbound operations, and local Hong Kong deliveries.

We had the opportunity to visit PRL’s DC and interviewed the Distribution Director of Supply Chain, who conducts outbound audits and performance. This facility has a fairly sophisticated automatic sorter and a solid staff to manage hundreds of thousands outbound documentation to meet all vendor compliance regulations. The DC communicates with the local stores twice a day and regional stores regularly to manage shipments, including end of season returns and current season slow movers.

From the DC in Hong Kong as in Figure 4, 45% of the products are sent to China, 24% to Hong Kong, 26% to Taiwan, and the rest to other Asia-Pacific countries. The outbound transportation team works with merchandising and distribution, retail, inventory control, global trade compliance, DC operations, and finance to ensure products are delivered to the customer. The objectives for this team are to develop the China network, enhance distribution lanes and options, as well as ensure port of entry flexibility on demand. The challenges with port of entry
mostly lie in customs regulations, which are always changing. The key to success for this department given customs control is the usage of pool points. Pool points allow PRL to keep some physical products in China without having to go through the import process by storing them in bonded logistic parks. Once it is decided where the products will go, then the necessary paperwork for importation will be processed. This delay in importing goods allows PRL to stay flexible and take advantage of common inventory; however, there is a 4-5 day lead-time to clear customs. Currently, PRL has pool points in Malaysia, Singapore, Macau, Taipei, and Shanghai. From these locations the outbound transport team will also manage last mile delivery. The key aspect for the outbound logistics team to focus is to maintain visibility of all products because data are coming in from multiple sources, but they need to be extracted and centralized.

![Map of Asia showing PRL's current outbound logistics and fulfillment for retail stores](image)

Figure 4 PRL's current outbound logistics and fulfillment for retail stores (Polo Ralph Lauren Asia Supply Chain, 2010)

The Creative logistics team provides support for all retail store build outs and interior design. This cross-functional team works with PSD/Creative teams, New York and European
creative logistics, freight forwarders, retail operations transportation team, and AP Finance to ensure the storage, delivery and pick up of non-merchandise retail items. These products can also be stored at pool points to service nearby stores.

PRL also has a supply chain finance team that works with supply chain operations, Hong Kong finance, planning team, US supply chain finance, Om Log, and DHL to manage all supply chain related finance. Additionally, the team manages cash flow for custom clearance, weekly freight costs, budget forecasts, and daily financial management. This department translates business strategy into financial facts to aid decision making.

In summary, the current objective of the Asia supply chain team is to serve the sales associates in PRL’s retail stores and make sure they have the right product at the right time to sell to PRL customers. Because PRL has only recently re-acquired its licensed brand in Asia, the company is in the stage of building a platform that provides high service levels while remaining flexible to the ever changing business environment.

PRL’s current operations team has laid a solid foundation for its e-Commerce business; however, in order for PRL to succeed in this new channel, the company needs to address certain gaps we have identified. These gaps are: ordering policy for the e-Commerce channel, inventory management at the DC level, warehouse location, integrated information technology, fulfillment for non-bulk orders, delivery to end user and finally, customer service.

In the following chapters, we will discuss general market and supply chain information to provide context for our findings and recommendations.
Market Information

The Chinese e-Commerce Market

We are in the midst of a technology revolution that is paving the way for businesses to reach new markets and consumers. China's online retail growth results primarily from the sheer size of the country's population and the increase in per-capita spending as living standards improve. As of 2010, Internet users in China have reached 450 million, the highest number in the world (Asia Access Limited, 2011). In addition, consumption of luxury goods topped $9.4B, approximately 27.5% of the global market, making China the second largest luxury goods market behind Japan (Yoox Group, 2011).

As shown in Figure 5, 20 million luxury consumers in China account for $130MM in e-Commerce sales of luxury apparel product. Double-digit growth rate in consumer base is projected per year between the present at 2015, with sales number projected to increase almost 30% year over year (Bain and Company, 2010).

![Figure 5 Current and projected number of luxury shoppers in Asia (Bain and Company, 2010).](image-url)
While the percentage of online shoppers in metropolitan China remains significant smaller than in Japan or mature markets such as UK, and US, per-capita online spending is increasing quickly. Even through the economic downturn between 2008 and 2010, China was one of the few markets where online spending continued its upward trajectory. However, online shopping revenues remain geographically concentrated, with the overwhelming majority of e-Commerce taking place in China’s largest cities (Wigder, Sehgal, Evans, & Johnson, 2010).

The Internet is seen as a shop window by most users, and as the technology of online shopping improves, the shop window has increasingly becomes a shop door. Growing confidence among consumers about the safety of buying goods online is illustrated by the rapid rise in per capita online spending as seen in Table 1. Consumers are gradually learning to trust the services and reliability of an increasing number of established online retailers and are adapting their habits to spending more money with them. That confidence has especially helped sales from B2C site accelerate markedly (Asia Access Limited, 2011).

Table 1 Per capita retail spending online in China by C2C and B2C, 2005 to 2010 (Asia Access Limited, 2011)

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>% period growth</th>
</tr>
</thead>
<tbody>
<tr>
<td>C2C</td>
<td>13.48</td>
<td>24.04</td>
<td>51.59</td>
<td>121.23</td>
<td>237.30</td>
<td>434.75</td>
<td>3,126.33</td>
</tr>
<tr>
<td>B2C</td>
<td>1.78</td>
<td>3.59</td>
<td>6.14</td>
<td>12.38</td>
<td>27.51</td>
<td>60.69</td>
<td>3,314.51</td>
</tr>
<tr>
<td>Internet users (million)</td>
<td>111</td>
<td>137</td>
<td>210</td>
<td>298</td>
<td>384</td>
<td>450</td>
<td>305.41</td>
</tr>
<tr>
<td>C2C retail per capita RMB</td>
<td>121.40</td>
<td>175.51</td>
<td>245.67</td>
<td>406.82</td>
<td>617.96</td>
<td>966.12</td>
<td>695.83</td>
</tr>
<tr>
<td>B2C retail per capita RMB</td>
<td>16.01</td>
<td>26.17</td>
<td>29.26</td>
<td>41.53</td>
<td>71.83</td>
<td>134.86</td>
<td>742.24</td>
</tr>
</tbody>
</table>

Along with growing consumer confidence, the number of wealthy households in China is increasing as well. McKinsey & Co. projects that by 2015, China will have 4 million wealthy households, making it the world’s 4th largest behind the United States, Japan and the United Kingdom. Currently, the majority of the wealthy concentrate near the East and Central South
region of the country, and around 30% of these households reside in China’s four largest cities, such as Shanghai, Beijing, Shenzhen, and Guangzhou. By 2015, however, a larger proportion of the new wealthy will come from smaller tier 2-4 cities, making expansion to serve the newly wealthy from inner China a top priority for many brands (Atsmon, Dixit, St Maurice, & Suessmuth-Dyckerhoff, 2009).

Table 2 lists major tier 1 and tier 2 cities in China that are undergoing major economic growth in the coming years.

Table 2 Major tier 1 and tier 2 markets in China (Oligively reference)

<table>
<thead>
<tr>
<th>Tier 1 Cities</th>
<th>Tier 2 Cities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beijing, Chongqing, Shanghai, Tianjin, Changchun, Chengdu, Guangzhou, Hangzhou, Harbin, Jinan, Nanjing, Shenyang, Wuhan, Xian, Dalian, Qingdao, Shenzhen, Xiamen</td>
<td>Changsha, Fuzhou, Guiyang, Haikou, Hefei, Hohhot, Kunming, Lanzhou, Lhasa, Nanchang, Nanning, Shijiazhuang, Taiyuan, Urumqi, Xining, Yinchuan, Zhengzhou, Ningbo, Suzhou, Wuxi, Wenzhou, Nantong</td>
</tr>
</tbody>
</table>

**Chinese Luxury Consumers**

With increasing wealth, Chinese consumers are becoming more comfortable with purchasing luxury goods and displaying their newfound wealth. These new luxury consumers, of which a growing number are residents of lower-tier 3 and 4 cities, are reshaping the luxury market landscape in China. Upper-middle-class consumers in China are now stretching their disposable income to purchase luxury watches, jewelry, handbags, shoes, and clothing, goods that until very recently were the exclusive domain of the very wealthy. Although upper-middle-class consumers only make the occasional luxury purchase, they already account for 12% of the luxury market. With their number and purchase frequency steadily increasing, the upper-middle-class consumers are expected to account for 22% of the luxury market share by 2015 (Atsmon, Dixit, Leibowitz, & Wu, 2011).
A closer look at the Chinese luxury consumer will reveal four distinct consumer types. Mckinsey and Co. in a 2011 report defined them as core luxury consumers, luxury role models, fashion fanatics, and middle class aspirants. These character types dictate their disposable income spent on luxury items and their purchase patterns:

**Core Luxury Buyers**

According to the report, the first consumer type is the core luxury buyer, these are households that spend between 12% and 20% of their income on luxury goods – a total of RMB20,000 – 60,000 (US$6,000-9,000) on luxury goods a year. In 2010, this group accounted for 45% of all luxury shoppers in China (9MM) and consumed 65% of all luxury goods sold that year ($6.1B).

**Luxury Role Model**

The next consumer type is the luxury role model consumer. They are rich, young and fashionable, living the ideal luxury lifestyle. They make up only 1% of luxury consumers but are projected to account for 24% of spending by 2015. Most are self-employed or corporate executives and many live in tier 1 cities like Beijing or Shanghai. Many have studied or worked overseas, and they have had long-term exposure to luxury brands. These luxury consumers on average spend more than RMB 150,000 annual on luxury goods, or 10% of their disposable income. Many have been buying luxury items for some time and they often buy to indulge themselves and to feel unique rather than to simply display their wealth. These luxury consumers also tend to buy spontaneously, snapping up an item if it catches their attention. Good service is paramount to these consumers; they are sensitive to the attitudes of the sales people and often prefer to shop in stores outside of China, where they believe the sales staff is more courteous (Atsmon, Dixit, Leibowitz, & Wu, 2011).

**Fashion Fanatics**

The next group of luxury consumers is considered fashion fanatics. They are not rich and make up only 3% of the luxury consumers; however, these consumers spend a much larger portion of their income on luxury goods, up to 40%. These consumers spend a great deal of time learning about the latest fashion trends and closely follow seasonal offerings. They tend to exert a strong influence on peer consumers, sharing their purchases and opinions in social circles and online. Because these consumers want to be fashion forward, they tend to purchase more luxury items on credit. Fashion mavens enjoy window-shopping at stores and tend to care less about store services than do the luxury consumers. They are also more likely to buy a product after a recommendation or when they see celebrities wearing it (Atsmon, Dixit, Leibowitz, & Wu, 2011).
Middle Class Aspirants

Middle class aspirants make up the largest share of the luxury goods purchasers at 51%, a number that will continue to rise as income and living standards improve. By 2015, these consumers will account for 16% of spend in the luxury sector. Many of these consumers live in tier 2 or tier 3 cities with lower living expenses, which allow them to occasionally splurge on luxury goods. Their relatively conservative attitudes toward money often means after spending money on a luxury item, they are likely to reduce spending on other things to keep their budgets on track. This group spends between RMB 5,000 to 15,000 per year or 9% of their household income on luxury items. They tend to have less experience with luxury items than other groups, but aspire to higher social circles and seek to stand out from the crowd. Purchases of luxury items for this group make these consumers feel successful. Because luxury items constitute a larger share of their income, these consumers are more cautious and spend a great deal of time researching an item before purchase, up to two to three months before deciding to buy. These consumers are not as well traveled internationally and are currently more inclined to purchase traditional Chinese Brands (Atsmon, Dixit, Leibowitz, & Wu, 2011).
Figure 6 shows a breakdown of luxury consumer types as well as their spending profile on luxury goods in 2010 and forecasted spending in 2015.

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**Figure 6** Luxury consumer type and spending breakdown
Luxury Apparel

In order to understand the specific challenges luxury apparel companies face with launching an e-Commerce platform, we will attempt to define luxury apparel. This seemingly simple task is actually quite difficult because luxury has a different meaning for people across socioeconomic levels. A senior lecturer from the University of Brighton in the UK states, “the word luxury originates from the Latin term ‘luxus’ signifying, ‘soft or extravagant living, indulgence, sumptuousness or opulence’. However, luxury is quite slippery term to define because of the strong involvement of human element and value recognition from others” (Shukla, 2010). It’s about history, experience, and identity as much as it is about design, quality and performance. Brands that quickly come to mind are often Italian and French like Prada, Gucci, Armani and the largest of the group, Louis Vuitton Moet Hennessy (LVMH). A common thread in these brands is the fact that they have a lineage and a vision for fashion and excellence. They connect with the end user and create more than just a wardrobe; they create a lifestyle. Ralph Lauren strives to achieve the same experience with his designs. In 1992 Audrey Hepburn distinctly introduced Ralph Lauren with his Life Time Achievement award from the Council of American Fashion Designers by saying, “There is no one adjective or ten adjectives, for that matter, that can describe all that you represent. But your consistency and integrity always remind us of the best things in life. As a designer you conger up all things we most care about” (Rose, 1993). “Luxury wasn’t simply a product,” Ms. Thomas from the New York Times writes. “It denoted a history of tradition, superior quality, and often a pampered buying experience” (Hurt III, 2007). Similarly, when speaking with the PRL staff in Hong Kong, it is evident that there is a real admiration for Ralph Lauren, himself, and the vision he has for PRL. One way we heard it explained is that through PRL, Ralph Lauren creates the movie lifestyle we
all want to live in. Ralph has said, "Designers do clothes, I do life" (Rose, 1993). In other words, he designs clothes to fit his aspirations. Like a character in a movie dresses for the part, Ralph Lauren designs for a lifestyle people dream of.

**Service Level Definition**

Companies strive to service luxury fashion consumers through both high service levels in the stores and high service levels in their supply chain. Supply Chain service level is the typical measure used to quantify a company’s market conformance. In practice, the definition of service level can vary from company to company, but service level is usually related to the ability to satisfy a customer’s time to market expectation. In other words, it is the measure of how often a product is delivered on or before the promised delivery date. Many companies consider this measure so critical to their ability to succeed in today’s market that they invest in decision-support systems that allow them to quote delivery dates accurately by analyzing information from the entire supply chain. According to Dr. Simchi-Levi, “Customer value drives changes and improvements in the supply chain, some forced by customers and competitor activities and others undertaken to achieve competitive advantage” (Simchi-Levi, Kaminsky, & Simchi-Levi, 2008).

He goes further and breaks the customer perception into five dimensions of service level (Simchi-Levi, Kaminsky, & Simchi-Levi, 2008).

1. Conformance to requirements
2. Product selection
3. Price and brand
4. Value-added services
5. Relationship and experiences

While consumers in Asia differ from those in North America or Europe, these dimensions still hold true in both cultures and even more for luxury fashion brands. Because fashion varies season to season, luxury fashion companies require even more of a responsive supply chain, which values short lead times, flexibility and speed over costs. (Simchi-Levi, Kaminsky, & Simchi-Levi, 2008)

In addition to high service levels throughout the said supply chain, e-Commerce consumers place great values on their Internet shopping experience, namely convenience of the transaction, confidence in the exchange and control of the purchase decision (Walsh, Gazala, & DeMoulin, 2001).

First, luxury fashion companies need to focus on creating a convenient shopping environment for their customers, whereby research, consideration, purchase, and return tools are all easily available. e-Commerce shoppers often purchase online to save time, shop 24x7, and purchase from the comfort from home or office.

Second, security of the transaction should never be a concern for the customer. Luxury shoppers’ focus on convenience often leads them to store their billing information with the retailer compared with non-luxury shoppers. Therefore, luxury fashion companies should consistently communicate the quality and confidence in its transaction security.

Third, luxury shoppers want more control online. From FAQs to emails to click-to-call-back, luxury shoppers want the tools and the website tailored so that product selection, purchase decision, transaction and product tracking are all easily within reach (Paderni, Favier, & Neurauter, 2005).
Payment Options

As part of a great shopping experience, convenient payment options are necessary. In North America, one of PRL’s primary e-Commerce markets, many different payment methods are available. These methods include credit card, debit card, alternative payment systems such as PayPal and prepaid gift cards.

Conversely, in the Chinese market, consumers utilize different methods to pay for their online merchandise. The most readily used payment methods are Alipay, Cash on Delivery (COD), credit cards, and online bank transfers. A 2010 Forrester Research study demonstrates that more than half of Mainland Chinese e-Commerce consumers pay for online purchases using Alipay, a leading alternative payment system in the country. Alipay is owned by the Alibaba Group, and is the primary payment method for Alibaba’s highly successful consumer e-Commerce site Taobao.com (Wigder, Evans, & McGowan, 2010).

Aside from Alipay, COD is prevalent in China, with over 40% of e-Commerce buyers using this form of payment where a local courier is hired to collect payment on behalf of the merchant. This model relies upon a considerable amount of two-way trust. Dangdang.com, an online retailer, provides customers with a door-to-door return policy within seven days and allows exchange of goods within fifteen days (Asia Access Limited, 2011). Another alternative is Postal remittance where consumers can pay online for purchases by providing payment at their local post office. Consumers can also replenish their Alipay accounts at China Post locations (Wigder, Evans, & McGowan, Understanding Online Payment Preferences In International Markets, 2010).
IT

IT can take a variety of forms such as EDI, direct link-ups with suppliers, Internet, electronic catalog ordering and email. To support sharing of information and resources between point of sale, warehouse, and company central, communication and coordination need to be maintained. IT has a pivotal role in improving communication and coordination by acting as an enabler. The Internet helps to manage supply chain activates by offering information about what kind of product is demanded, what is available in the warehouse, what is in the manufacturing process, and what is entering and exiting the physical facilities and customer sites. For example, ERP systems such as SAP can only connect different functions within a firm but also connect the firm’s suppliers, distributors and 3PLs, enabling the partners to share information such as order status, product schedules, and sales records, all to integrate major supply chain processes and to plan production, logistics and marketing promotions (Gunasekaran & Ngai, 2004).

In addition to facilitating information up and down the supply chain, IT has become instrumental in use for purchasing. Cost savings resulting from reduced paper transactions, shorter cycle time and the subsequent inventory reduction resulting from speed transmission of purchase order related information, and enhanced opportunities for the supplier/buyer partnership through establishment of web of business-to-business communication networks. The adoption of more integrated IT models would further strength global supply chain management (Gunasekaran & Ngai, 2004).

Inventory Management and Risk Pooling

While technology can drive great efficiencies in the supply chain, risk pooling—aggregating inventory and demand to decrease variability—can significantly cut costs by lowering
safety stock and average inventory. There are three critical components that will impact the effectiveness of risk pooling. First and foremost, centralizing inventory will reduce safety stock and average inventory because it allows companies to use items that are in low demand in one region to fulfill high demand in another. Secondly, the higher the coefficient of variation, the greater the benefit obtained from centralized systems. Higher variations lead to higher safety stock and since risk pooling decreases the need for safety stock the greater potential to cut costs. Lastly, these benefits also depend on the correlation between market demands. If two markets are positively correlated then the benefit of pooled inventory will decrease because both markets will experience high or low demand at the same time (Simchi-Levi, Kaminsky, & Simchi-Levi, 2008).

If done properly with the right market conditions, pooling inventory in a centralized DC can have many benefits, but there are also some trade-offs. A centralized system allows a company to provide higher service levels with fewer inventories on hand, which decreases overhead costs. Conversely, decentralized DC’s are closer to customers and allow for shorter deliver lead times. However, the impact on transportation costs is unclear because it depends on whether it is more costly to ship products from suppliers to warehouses or from warehouses to customers (Simchi-Levi, Kaminsky, & Simchi-Levi, 2008). There are obvious advantages to pooling inventory, but with these trade-offs it is important to thoroughly assess the priorities of the company and the market characteristics.

**Third-Party Logistics**

Third Party logistics (3PL) providers are external companies who manage, control and deliver logistic activities on behalf of a customer or shipper. The activities performed can
include all or part of the logistics activities required for the client, such as warehousing, distribution, and pick & pack. Three types of 3PLs exist in the market place with different strategies on how to serve their customers and are described below.

The 3PL acting as a service provider is seen as to offer advanced value-added services. This activity could involve differentiated services for different customers, performing specific packing, cross docking, track and trace, and offering security systems. An advanced service package often involves several sets of more standardized activities turned into modules that could be combined according to each client’s demands. With more advanced services, a capable IT system is often necessary to facilitate such development.

The customer adapter could be described as the 3PL firm taking over clients’ existing activities and improving the efficiency in the handling. This type of provider might take over customers’ total warehouses and the logistics activities and relies on a few very key clients.

The customer developer is the most advanced 3PL service provider. It involves a high integration with the client often in the form of taking over its whole logistics operations. The possibilities to coordinate customers lie in the know-how, the methods, the knowledge development, and the design of the supply chain. The number of customers would be limited and the work for each customer extensive (Hertz & Alfredsson, 2003).

In the Chinese market currently, finding a 3PL capable of providing any and all of the services mentioned above is still rare.

Not only will delivery be important for shaping success and failure in the online retail market in China, but managing inventory also proves to be an increasing headache for many online retail companies as their business, and trade volume increases. When the companies find
their retail transaction volume rapidly rise from 10 a day to 10,000 a day, they have to react quickly to find a solution. This solution is usually outsourced, as the time and investments necessary to build the capacity to distribute large volume of goods takes considerable amount of time, which is short in an online market that is growing at over 100% a year (Asia Access Limited, 2011).

The growth of the Internet retail business has led many 3PL businesses to enter the field; however, with so many firms short on experience, problems with quality often arise. Because 3PL operations often lie outside the control of customer companies, poor service often results. Poor quality and service, if persistent, can kill an online business in China just as quickly as it can help it grow. China’s Internet users utilize social media greatly, and bad press about any company can often spread quickly. When the market is growing as fast as online retail in China, bad press surrounding fulfillment can hinder consumer confidence effectively killing the online retail channel. Hence, it is of great importance to control logistics and establish cooperative relationships with 3PL providers (Asia Access Limited, 2011).

Many companies have grown in China recently into significant logistics providers to fill the gap that has existed in the domestic economy. Previously, the only logistics companies providing effective China-wide coverage were China Post and EMS, but others have emerged since then, such as Zhongtong and Shanghai Yuantong, along with foreign imports such as FedEx, UPS and DHL.

**Summary**

As B2C sales of luxury fashion continue its fast growth in China, PRL is entering the field to capitalize on this opportunity. The challenges PRL faces are that no luxury fashion
companies before now have launched e-Commerce in China and; thus, no standard supply chain models exist for the luxury e-Commerce channel reinforcing the need for this study. We used interviews with Polo Ralph Lauren staff, research journals, consultancy studies, and industry interviews to document luxury e-Commerce and the gaps that exist to offer this service across China.
Methodology

A market review was conducted initially through journal research to gather current information on the following topics: luxury apparel, luxury apparel supply chain, Asia market place general trends, Asia Luxury apparel space, and e-Commerce fulfillment in China. This search and compilation allowed for a fundamental understanding of the brands operating in the luxury apparel space in China as well as the current state of their e-Commerce fulfillment. Primary sources of information for the market review were conducted through Forrester Research, academic journals, interviews as well as consulting reports prepared for PRL.

Next, companies were selected for interviews to gain specific insights on their practices in the e-Commerce fulfillment space. The choice of companies was not limited to luxury brand companies only, but also to third party logistics (3PLs) that serve to fulfill orders for luxury brand companies both in the traditional retail channel as well as the e-Commerce channel. Questions were designed to not jeopardizing their strategic or operational advantages in the current marketplace. Still, many companies we approached for this study declined to be interviewed to protect their competitiveness; however, we were able to interview five companies and gain insight into current practices.

The following people and resources were used to gather and compile data on current e-Commerce operations in China.

- Market Feasibility Study Conducted By Consulting Firm
- Interviews With Polo Ralph Lauren Staff
• Vice President of Global Supply Chain PMO

• Vice President of Global Transportation & Logistics Asia

• Senior Director, Supply Chain

• Inbound Operations Director

• Transportation Director

• Senior Director, Global Transportation

• Director Global Transportation

• Vice President Information Technology

• Distribution Director Supply Chain

  o General Manager / Representative Director – Company C Korea Ltd.

  o CEO and Senior Operations Director – Company A

  o CEO – Company B Asia

  o Yoox

    • China Group Press Release

    • General China Presentation

The luxury brands interviewed were selected based on the criteria of length of operating time in the luxury space, consumer perception, and history. These criteria were used for several reasons. For example, consumer perception of the brand and its overall history dictated whether
the company is a long-standing brand or a newly established venture. While established brands offered the closest comparison to PRL in history and value, newly established ventures offered strategies and solutions that are both exciting and innovative.

Within the 3PLs, companies were selected based on past histories of working with luxury brands, operational capacity to fulfill a given volume of orders, technology platform capability, local knowledge of culture and customs, and experience working in China.

Interviewees were selected based on their position within these companies and their overall experiences in the luxury goods space. We chose these individuals because they often had a great deal of experience working in the luxury space from a strategy and operational perspective, as well as in setting up previous e-Commerce ventures.

Interview questions were kept deliberately open ended to allow the speaker to answer from his/her frame of reference as to take advantage of his/her experience in the field. Interviewees were encouraged to describe in as much detail as he/she felt comfortable about the general company strategy and established operations. Additional discussions focused on how the company strategy and operations have evolved as it entered the Chinese luxury market place. Furthermore, follow up questions were directed at specific areas within operations to gain a more clear understanding of on the ground tactics vs. top line strategy; because often times, “what companies do is a more clear reflection of their fulfillment strategy rather than what they claim their strategic intent to be” (Weiss, 1994; Rubin & Rubin, 2005; Holstein & Gubrium, 1995).

A sample of interview questions is below.
Questionnaire for luxury brand e-Commerce in Asia

Strategy

1. When did you enter the Asia e-Commerce market?
2. What are the key similarities and differences you see between Asian e-Commerce customers and those in North America and Europe?
3. How has the introduction of e-Commerce in Asia changed your operations in terms of location, volume and customer reach in new regions?

Service Level

1. What regions in China do you provide e-Commerce service to?
2. Do you provide different service levels for different cities (tier 1 vs. tier 2, vs. tier 3)?
3. Did you enter every region at the same time?
4. What are your service level goals in Asia and how are they unique to the luxury market?
5. How do you manage returns?
6. What are the challenges you face with providing a luxury service with your current model and service providers?

Distribution

1. Do you hold your inventory in a centralized DC or in multiple country DC’s?
2. How many DC do you have in China?
3. Where are they located?
4. Do you have a strategy for opening more DC’s as the market grows?
   a. Active or Reactive approach to increase fulfillment to new markets.
5. Do you own and operate these DC’s or do you outsource?
a. If you outsource what are the requirements in terms of logistics, IT, and experience?

b. How many options did you have to choose from and can you share with us who those companies are?

**Fulfillment**

1. Do you work with a 3PL or in house staff for the integration of fulfillment, front end operations, and the last mile delivery?
   a. If working with a 3PL what kind of option do you have to tailor the inbound and outbound operations?
   b. What is the volume handled per DC?

2. Do you utilize pool points or other fulfillment locations that vary from your DC locations?

3. Are any of them located in bonded logistic parks?

4. What kind of service options do you offer for the last mile of delivery?
   a. What do your customers want and what would you like to be able to offer?
      i. Examples: Next day deliveries, time specific delivery, return options.

5. What is your return policy and what options do customers have to return a product?

**IT**

1. What IT systems are you currently working with and are they integrated across all sales regions in Asia or globally?

2. How are your MRP, ERP, and WMS for e-Commerce merged with the traditional sales channels?
Each interview was recorded with permission and transcribed to ensure accuracy. Qualitative data from these interviews were gathered and compiled. Trends were then explored within the responses to look for strategic goals of the company, operational focus, as well as metrics for success.

These trends are then aggregated to present a high level snapshot of the practices that are currently done within the Chinese e-Commerce industry. Following an aggregation of the data, further analysis was conducted to determine whether these firm’s current practices fit with PRL’s corporate goals for its e-Commerce business within China. This procedure was done through the perspective of maximizing service level for PRL’s customers.
Case Studies

Three companies were interviewed for this study; Company A, Company B and Company C. One 3PL provider, Yoox was studied through its publications, and finally, a luxury fashion consultant provided industry feedback. The responses to interview questions were condensed and presented below.

Company A

Strategy

Person A is the Founder and CEO of Company A, an online private sales website for luxury lifestyle and fashion brands operating in Japan and China and looking to expand to Korea in 2012. Prior to launching this e-Commerce business, Person A was the President of Company B Asia, the Vice President of Company X. He has five years of e-Commerce experience in Asia. Now at the helm of Company A, he uses online flash sales—limited products sold for a limited time at a discount—to sell a diverse range of luxury goods. The company has five categories that include: previous season fashion, shoes, cosmetics, accessories, and leather goods. Company A rotates the brands it works with every week and will work with each brand 3-4 times per year. Since launching in early 2009 in Japan, Company A has developed working relationships with 450 brands. China’s market is growing, but having launched more recently in July 2010, it is only working with 130 brands.

Service Level

Service level is an important factor to the success of Company A, for this reason all customer service is managed by Company A employees. Company A has 35 dedicated customer
service employees who operate out of the company’s warehouse. One unique market characteristic in China is the large number of orders that are paid for by cash on delivery (COD). For Company A, this constitutes half of its sales. Remarkably, its rejection rate, the rate at which customers either do not pay for the item upon delivery or are not there to pay for the product is less than 1%. Person A contributes this to Company A’s customer service agents who actively reach out to customers to make sure they are informed about the purchase and delivery time. This customer touch gives people the confidence in their purchase and the comfort of knowing they are getting a quality product. Additionally, Company A will cover the cost of any returned product again easing any doubt for a customer to purchase a product.

While COD is a major concern for customer service and assurance of an actual purchase Person A has seen a decrease by about 5% of customers opting to pay for their products by COD in tier one cities. However, in tier 2 and 3 cities COD continues to be much more prevalent due to the lack of trust in authenticity and lack of credit card services. So, while there is a decrease, in tier 1 cities with large growth in tier 2 and 3 cities managing COD orders will continue to be a significant role for customer service agents. To manage all these orders Company A has created multiple avenues for its service agents to talk to customers through phone calls and online chat.

Overall Company A has received very positive feedback from its customers. One complaint Company A does receive is that the products are not available for long enough. However, this is part of Company A’s strategy to drive sales because if customers wait to buy, they understand they might miss a chance on a great deal.

Company A does reach a wide consumer base across China and therefore differentiates its service depending on the season, type of product, and customer climate. The company offers
special packaging for various holidays and seven different packages for all its categories. Additionally, Company A has different packages for the different climates it ship to. For example when shipping a product from Shanghai to Mongolia, Company A considers temperature sensitivity and makes sure the package arrives in pristine shape. However, Company A has not differentiated its service on individual customers or price of the product.

Another way Person A tries to provide a great service is through Company A’s website. To accomplish this, Company A has invested in strong marketing campaigns with celebrities and reputable brands. This approach achieves two objectives. First, it draws people to the site, and second, it convinces the customer that the products Company A is selling are in fact authentic and of quality. To prove the latter, Company A also keeps the original price tags on the products so the customer can see how much they are saving. Currently, Company A splits its marketing efforts, with half online and half offline, including magazines, TV commercials, bus stops, and other public relations outlets. But as Company A’s web presence grows, the company will shift its marketing to 80% online and 20% offline.

In order to meet customer expectation, Company A has identified four areas it wants to provide best in class service. These four areas are: display, answering questions, time to market, and handling returns.

Customer

In order to know how to provide great service it is important to know who the customer is. For Company A, 40% of its customers are based in tier 1 cities, 35% are from tier 2 cities, and the remaining 25% are scattered in tier three and four cities. The customers living in tier 1 cities are primarily business men and women with white collar jobs and the customers residing in
the remaining tier 2, 3, and 4 cities are entrepreneurs who have money, but do not have access to luxury goods. The age of Company A’s customer base ranges from 25 to 40 year olds, with 40% of them repeat customers. These customers purchase on average 900 RMB per transaction. From Person A’s experience, he has not observed a disparity between how much customers spend online and off. The one difference he has recorded is that the average age of a customer shopping in retail stores is 35 years old and the average age online is 28 years old. He believes that people buy online because they are looking for authentic products at a discount.

**Distribution / Fulfillment**

Currently, Company A operates a centralized warehouse based in Shanghai, China. Being located in Shanghai allows Company A to closely monitor the quality control process and position itself to service the majority of its customers with short lead times. Company A has subcontracted its fulfillment operation to Arvato, a German based 3PL that has been working in this market for 4-5 years. Arvato is responsible for all the receiving, picking and packing, but Company A has decided to keep all customer service in house. Company A holds its entire inventory on consignment with 90% of the goods coming from China and 10% being imported. Acquiring inventory on consignment allows Company A to keep its working capital free, manage obsolescence risk, and invest more in sales and marketing. By sourcing the majority of its products in China, Company A is able to keep ordering costs down and ensure the products meet customer preferences for local style, color and size. Because Company A does not produce any of its own products, quality control is a significant operation for the company. Company A checks every piece on inbound and before the product is shipped to a customer to make sure that the product meets Company A’s quality standards and customer expectation. This process has proved beneficial as Company A achieves single digit percentage returns. However, as
Company A continues to grow, it looks to establish regional distribution centers and have suppliers ship directly to those warehouses bypassing the central DC in Shanghai. Company A’s warehouse expansion initiative will be guided by regional sales volume and customer profile. For customer service, Person A chose to maintain complete control because of its critical importance in Company A’s ability to provide the highest level of service possible.

**Delivery**

Company A ships to thirty one provinces through Federal Express (FedEx), but in the case where customers reside in remote locations, Company A works with World Wide Express Mail Service (EMS). EMS is mandated by the Chinese Government to service every postal code within China. While EMS can reach all postal codes in China, the company lacks the ability to provide similar service levels as FedEx and it usually take seven to ten days to deliver products through its network. For customers in remote areas this longer deliver time is acceptable; but for customers in larger cities, they expect to receive products in two to three days. Person A believes this is fairly standard across e-Commerce businesses except for the large players such as Amazon.com, DangDang.com, and 360 Buys who use their own curriers.

Company A’s goal is to deliver all its products within five days; for large sales regions like Shanghai and Beijing, Company A offers next day and two day guaranteed delivery. Person A believes that time to market is an essential component of providing a luxury service, hence Company A is looking to expand its warehouse footprint to three or four regional DC’s that will be able to provide even faster time to market. At the moment, Company A is collecting and analyzing sales data to decide where and when it will open these regional distribution centers.
Another way to insure customer confidence in the authenticity of the products and to ease any anxiety about purchasing a product they may not like is to provide a great return policy. Chinese law mandate that consumers have seven days to return a product for any reason, but Company A goes above and beyond. Company A accomplishes this by making the return process free and as easy. Conversely, it is not just the customers who are worried about the return process; Company A also has to be careful of receiving counterfeit product in possible scams. In order to prevent such an event, Person A’s operation team has devised a method of tracking each product and ensuring that the product returned is the same that was sent out. If the product is damaged, Company A will return it to the brand; but if the product is still in good condition, Company A will keep the product for an additional week to cover exchanges. After the sale and exchange period is complete, Company A will ship all unsold products back as per the consignment contract.

**Technology**

The use of mobile technology varies in Asia and is quite different from that of the US or Europe. For example, 25% of Company A business in Japan comes through mobile e-Commerce. Company A has not launched mobile e-Commerce in China, but the company is planning to sometime in 2011 and expects to see similar sales patterns.

Because Company A outsources its warehousing operations, the company does not have a single integrated IT platform. Instead Company A syncs its ERP systems twice a day with the Avarto’s warehouse system. Company A does manage the e-Commerce platform, allowing the company to manage orders real time.
Next Steps

At the pace Company A and e-Commerce is growing in China Person A is uncertain what changes the company will need to make to keep up with demand. The company is evaluating its supply chain to make sure that its operations are scalable to meet the demand. Issues Company A are looking into include: distance between the warehouses the manufactures (for example, it has occurred where products are shipped from Guangzhou to the central DC in Shanghai only to be shipped back to a customer in Guangzhou), working with partners who have subject matter expertise in fashion, improving time to market, sales in new cities, increasing demand in cities far from Shanghai, ability for all customers to track orders online, and balancing the costs associated with high service levels.

Company B

Strategy

Person B joined Company B Asia three years ago as the Head of Operations and is now the CEO of Company B Asia. Prior to working with Company B he was in charge of Company X’s supply chain operations in Asia.

Company B has structured its operations in Asia as subsidiaries and is looking to expand into Singapore by July 2011. To date, Company B has operated its e-Commerce business in Japan for one year and is working to launch in China as soon as possible. Person B wanted to launch Company B’s China e-Commerce platform in May 2011, but the launch date has become a moving target. Person B believes the sooner Company B can launch the better because Company B already has a website that allows people to view the products, but does not allow them to purchase the products. Working with luxury products has afforded Company B large
margins; therefore, any incremental supply chain costs the company incurs through its e-Commerce operation will unlikely overshadow the incremental profit. The reason Company B has not launched its e-Commerce business is simply because the company is growing so fast in China that there are many other competing opportunities. Company B is opening one store every two weeks in China and plans to continue this pace for five years. This type of growth puts a strain on building organizational capacity necessary for a different sales channel.

Company B’s e-Commerce business in the US accounts for 5% of its total business, with Manhattan, New York drawing the highest traffic. This is an interesting fact because there is no shortage of Company B retail stores in Manhattan. This leads Person B to believe that e-Commerce serves a wider range of customers including those who already shop at Company B retail stores and not just those who do not have access to the retail channel. Similarly, Company B has a strong concentration of 170 stores in Japan, and still sees a positive response to e-Commerce.

The major difference between Company B Asia and Company B US is that the competitors are different. In the US, Company B sees companies like Michael Kors and Marc by Marc Jacobs as its main competitors, whereas in Japan Company B competes with European luxury giants like Louis Vuitton and Gucci. Person B has seen a distinct difference in the perception of luxury brands in Japan and China compared with the US. These brands are more iconic and display a status that customers are willing to save for months to portray. It is less about the value of a product and more about the status that wearing the product gives you.

There are many differences between Japan and China. For example, mobile technology is taking off in Japan and now constitutes 50% of Company B’s e-Commerce sales. He has also observed many customers utilizing e-Commerce as a way to resale products. One of the most
significant differences between Japan and China is that in Japan, promotions do not play a large role in generating sales. Conversely, Chinese shoppers go online to find the best deal or a brand name product at a discount. Another difference between Japan and China is the market penetration Company B enjoys. In Japan, Company B is the number one brand in the number of bags sold and number two in value after Louis Vuitton. On the other hand, Company B has a much smaller footprint in China and is looking to build its brand. The challenge for Company B to build its brand lies in the sheer size of China and the uniqueness of each region. Person B compares China in this regard to Europe than to Japan.

The purchase profile of e-Commerce customers compared to retail shoppers varies slightly in Japan. One difference that has proved beneficial for Company B is that their e-Commerce platform has been able to attract more men to purchase products online. A plausible conclusion is that the retail stores are set up to attract more female customers and it is easier to differentiate men’s product lines on an e-Commerce site. Customers are looking online to find less expensive products, but the purchase amounts are very similar. One key difference is that customers who place an order via a mobile device tend to spend less than if they were to make a purchase through the official website.

Service level

There is a misperception that Chinese customers are less demanding. Chinese customers know what good service is and they expect it. Therefore, Company B strives to provide a high service level not just in their retail stores, but online as well. Person B has explored many ways to enhance the customer experience online, such as free return shipment, the option for e-Commerce customers to pick their orders up in a store, and repair and cleaning services. Company B also offers an expediting service, but only if a customer requests it.
From experience working in Japan, Person B noted that customers are fine waiting three to four days for their order to be delivered. In China, however, because e-Commerce is a new venture, Company B has found it difficult to predict consumer behavior. Thus, they have set up a system to gather customer feedback to better understand customer expectations.

**Distribution and Fulfillment**

In general, Company B prefers to keep its distribution and fulfillment operations in-house because the company has a very high standard of service. From its experience managing a 3PL in the past, Company B has learned that it can take just as much labor and time to manage as to operate the distribution and fulfillment themselves. For these reasons, Company B operates under a structure that will allow it to keep e-Commerce distribution and fulfillment in-house, but will look at outsourcing options for fulfillment potentially. The company has not yet completed an in-depth study of potential 3PL partners, but will look to see which companies other comparable brands are working with. According to Person B from Company B, “The important thing is to do it right the first time and to find the resources necessary to execute a scalable model” (B, 2011).

China has such a vast geography that Company B does not expect to reach all the tier 3 and 4 cities. Instead the company expects that the majority of their e-Commerce business will come from the cities they already have a presence. Company B currently has two warehouses in Shanghai, one that is duty free and one hub that is duty paid. Its only other warehouse is in Hong Kong. Currently, Company B runs half of its products through Hong Kong and the other half through the Shanghai warehouse. It is interesting to note that the volume handled in Shanghai is growing at a much faster rate.
As Company B continues to grow and expand its reach into China, the company is looking to couple its e-Commerce inventory with that of retail and to develop a hub and spoke model with regional DC’s located in the North, South, and West. This model will evolve over time; however, Company B will continue to fulfill its e-Commerce orders from the same warehouse that serve its retail stores in order to take advantages of inventory pooling. This approach will allow Company B to keep up with any unforeseen growth in e-Commerce. Currently, e-Commerce makes up only 1% of their Japan business, so even if China jumped to 5%, Company B believes its operations is capable to handle demand. In Japan, Company B does not pool its retail and e-Commerce inventory; instead the company treats e-Commerce as a single store and keeps a separate inventory. Company B has considered working with regional distribution centers and bonded logistic parks, but has left these as last options due to the long lead times and lack of experience working with them.

Company B will choose to only work with shippers that provide the best service and are willing to pay extra for it. Company B will look for companies that have experiences working with fashion brands and understand the quality of service that is expected.

A unique characteristic of e-Commerce in China is that a majority of consumers prefer to pay by COD rather than with credit cards. For products that that cost over $40USD, this becomes a risk. Company B’s bags, for example, easily cost upwards of $400USD per piece; therefore, the company has to ensure that the customer will be present and will be able to pay upon delivery. Fortunately, Company B has not experienced problems with this in Japan, as there are a number of steps a customer has to go through to complete an online transaction. Returns rates are quite low and Company B remains confident there will be a similar trend in China.
Another challenge associated with COD is that a trusted courier company to deliver and to collect the cash in the various regions is needed. This remains difficult because there is not a single courier service that can provide delivery to all postal codes; and the ones that reach more remote locations do not always provide the level of service Company B and its customers expect.

**Company C Korea Ltd.**

**Strategy**

We interviewed Person C, the General Manager of Company C Korea Limited. Person C has worked with Company C for 11 years, four of which have been in Korea. He started his career with Company C in sales out of the London office and has moved up to General Manager. Company C started to launch its international business units in 1970 through franchises. Japan, Korea and China have only been subsidiaries for four, three and two years respectively. Even though these country branches are subsidiaries of Company C, they operate very independently.

One reason Company C has decided to operate the country markets independently is because of the wide range of market characteristics. From his experience, Person C has not seen a Pan-Asia distribution network that has the capability to serve all the countries in Asia because of the significant differences that exist in trends, technology and consumer behavior. He has recognized a pattern in that most trends start in Japan and work their way to Korea, China and then to the rest of Asia, often taking up to 2 years to complete. Conversely, Australia is much more tied to the US market. In the e-Commerce space, Company C recently launched its Internet business in Japan and is now planning to launch in Korea and China later this year.
Service Level

In order to provide high service levels, Company C Korea focuses on customer service, inventory management and ensuring the return policy meets the same standards as its retail business. Company C Korea does have the ability to provide next day delivery anywhere in Korea and for an additional $12-$15, customers can have their orders delivered same day. Company C is able to offer this level of delivery service because Korea is small enough geographically and technologically advanced that express delivery is only restricted by the willingness of customers to pay extra. One major difference between Korea and China is that in Korea, Company C does not have to deal with customers paying by COD. In fact, there are tax benefits for customers who use credit cards.

Company C Korea will also uses its e-Commerce store to offer products that are not available retail everywhere and to offer limited edition specialty items that are only available online. While there will be more products online, Company C will not offer the option for customers to pick up their online orders at a retail store.

Another area Company C Korea provides service to its customers is by focusing on sustainability. Company C has introduced a new packaging system that saves over 8,500 tons of paper and 5,000 tons of plastic per year. In an attempt to reduce the product’s carbon footprint, customers have the options to return products to the stores rather than shipping them back to a warehouse. These sustainability initiatives drive value to the customer and help Company C save on material and other related costs. However, these initiatives are largely driven at the corporate level and Person C has yet to see a strong response from consumers in Asia. His projection is that environmental impacts will begin to influence customer behavior, and Company C will be ahead of the curve and the leader in this space.
**Distribution and Fulfillment**

While Company C Korea has not yet launched its e-Commerce business, the company has decided to outsource all operations. Company C Korea recognizes that it does not have the in house expertise and is not sure how the market will respond. The company is happy to partner with a more experienced 3PL in the Korean market. From our conversation, it is apparent that Company C is very risk adverse when it comes to launching a new business and the company views working with a 3PL as necessary to hedge possible risks. This is a decision that is specific to Company C Korea, as Company C US and Europe manage their e-Commerce business all in house.

Currently, Company C Korea is working with CJCLS for its Korean fulfillment. CJCLS is located on the south side of Seoul, in Incheon. Company C Korea will also keep its e-Commerce and retail inventories separate, but will offer the same styles, except of course, for the few limited editions items offered only online.

Company C also plans to outsource its operations for the China launch. China’s large and diverse geography poses a challenge, to counter this, Company C is looking at two companies, Nan Yang and Hong Ying, who have experience with competing brands like Nike to run its distribution and fulfillment. Company C has recognized that different regions will require working with different partners who have experience in that particular area.

**IT**

Company C does not have an integrated IT system that can interface with all its fulfillment partners.
 Strategy

Yoox is a global Internet retailing firm for fashion and designer brands. The firm not only sells past season fashion items at discount prices on yoox.com, but also sells current season fashions on thecorner.com. Yoox also provides technology platforms for brands to host their own mono-brand e-Commerce websites. Yoox achieved its leading position within the online fashion retail through its longstanding relationships with designers, manufacturers and retailers worldwide. Since 2006, the firm has offered services such as website design, fulfillment, global logistics and customer service management to fashion brands looking to offer their latest designs through the e-Commerce channel. Some of the brands utilizing Yoox’s mono-brand service offerings include Diesel, Emporio Armani, Valentino, Roberto Cavalli, and Ermenegildo Zegna. (YOOX Group, 2010)

 Service Level

In the Chinese marketplace, Yoox is poised to lead the market and has established its regional office in Shanghai in September 2010, focusing on Technology & CRM, buying and merchandising, communication & retail marketing, content management, interface design, digital production and customer care. Through third party service providers, Yoox has also established a call center, logistics facilities, online payment vendor and also transport, COD and point of sale payments in Shanghai.

Lastly, Yoox delivers dedicated customer care through its central customer service team in Shanghai where customers can receive support via Chinese language both in email and telephone.
**Distribution and Fulfillment**

Yoox also provides premium return service and high-tech anti-fraud seals on all of its merchandise. The company offers free 7 day return guarantee with no questions asked and provides FedEx return labels. Yoox also offers premium waiting service where clients are allowed to try on the product on delivery.

Yoox offers fast and reliable shipping with luxury packaging through FedEx to over 400 Chinese cities and Express Mail Service often in next day and 2nd day service.

Yoox also offers safe payment though local alternative payment systems as well as COD. The company also supports international credits if needed.

**IT**

Throughout its expansion into the Chinese luxury retail space, Yoox has maintained its focus on creating fully localized websites, where all contents are displayed in Chinese, all sizes are converted to local sizes, and all currency are set in RMB.

**e-Commerce Consultant**

**Strategy**

Person D is an e-Commerce strategy and management consultant for luxury brands. His past experience includes launching and managing global e-Commerce platforms for leading luxury brands including Michael Kors, Emilio Pucci, Baccarat, Moschino, Valentino, D&G, Juicy Couture and others. He also has held executive-level merchant positions at Neiman Marcus, Yoox, Henri Bendel and Kate Spade.
Having many years of experience in the luxury space, Person D describes luxury fashion as designer brands with a rich heritage, a high price point and most importantly, a high level of service or experience in all senses. The challenge then is for these luxury brands to transfer this high service to e-Commerce. This is one reason why many luxury brands have been late to the game. There is only so much a company can do online to differentiate themselves from other brands.

**Service Level**

One area that Person D identified as a key component is to make sure that a e-customers can actually speak to a real person if they have any issues and that that person is well train and knowledgeable. It is important that this service gets translated online, so brands need the flexibility to keep up with new trends and technology. Luxury brands are expected to spend considerable amounts on marketing, email campaigns, images, photography including 360 degree product shots, and well written copy.

From Person D’s experience in Japan, he identified the packaging as being critical to the luxury experience. This component includes the box itself, how it is wrapped, whether it includes personal notes, and making returns as easy as possible.

**Distribution and Fulfillment**

Most luxury brands tend to outsource part or all of their e-Commerce operations because they need to have significant volume (he estimates upwards of $15-20MM in sales) to make it worth running their own operations. However, the experience a customer has is so important to a luxury brand that most will opt to keep the operations in-house and make sure they perfect it before launch. Person D believes this is one reason why Prada, for example, has yet to launch an
e-Commerce site. However, e-Commerce technology is to a point where most platforms are flexible enough to meet the needs of any luxury brand and allow these brands to wrap a first class customer service around it. There was some concern that consumers would not purchase products at such a high price point online, but this has proved not to be an issue.
Analysis

Strategy

As income levels and per capita spending continues to rise throughout China, consumption of luxury apparel will increase. To capitalize on this rapid rise in luxury apparel purchases, luxury brands are investing resources to build e-Commerce platforms. Fashion retailers hope to utilize this new retail channel to better serve existing customers as well as reach new ones.

Of the companies we interviewed, all are actively pursuing Chinese e-Commerce business through a variety of entry strategies. Company A and Yoox are the only two companies to have active operations at this time. Company B is actively exploring all options to launch its e-Commerce business in China; however, because other in-country expansion opportunities have taken priority, the schedule to launch e-Commerce has been readjusted. Company C is also exploring e-Commerce options in China, but the company is in the early stages of planning and has focused most of its attention on the Korean marketplace.

The trend among the companies interviewed is their e-Commerce strategies will revolve around service level, distribution, fulfillment, delivery, technology, and the shopping experience. Their intense focus on these areas is aimed at decreasing time to market for their products and providing the best experience possible for their customers. With these disciplines in mind, we will compile current industry practices and explore relevant approaches for PRL to enter China e-Commerce.
Service Level

The online shopping experience, consisting of convenience, confidence, and control of the products and services provided, will often dictate whether a customer will return to a website for future purchases. In the Chinese market where the consumers not only understand what good service is but also demand it, the ability to deliver is critical to the success of a company or brand. We observed through our interviews that most brands recognize the importance of service level, given their fairly high margins earned on luxury fashion items, and are willing to pay the necessary costs to guarantee great service. With that in mind, we examined what services luxury fashion retailers offer currently and what are planned for in the future. These services run from customer care both online and off, special last mile delivery of high-end items, and return services. We also examined whether these services are kept in house by the retailer/brand or are outsourced to a 3PL partner.

In Company A’s perspective, service means the ability to ask for and receive help at any moment during the shopping experience, both online and off. To satisfy this requirement, Company A’s in-house customer service staff regularly contacts customers to make sure they are informed about their purchase and delivery times. In addition to frequent customer contact to actively manage customer expectations, Company A will bare all costs associated with returns, further easing any anxiety an e-Commerce customer may have. Beyond keeping the customer well informed, Company A also imparts value added services through other channels. Because the company’s products have been sold to customers all over China, Company A differentiates its service level based on season, type of product, and customer locations. These services are critical because of the inherent value of the products sold. For example, products sold during Chinese New Year or Christmas will get holiday packaging, while products shipped to harsh
environments such as Mongolia will get temperature sensitive packaging. Finally, Company A makes its service level standout through online marketing campaigns with celebrities and other luxury brands, engaging the customer and further substantiating its product value and authenticity.

Yoox.com, the only other active luxury e-Commerce retailer in China offers up some great services as well to its customers. Not only does Yoox.com offer dedicated in-house customer service live in person, but also through email and live chat support via the Chinese language. Additionally, when the customer receives a product purchased from Yoox.com, he or she is given the opportunity to try on the garment before accepting it from the courier. Yoox in recent years has also invested heavily in technology platforms, allowing its customers to safely shop yoox.com via mobile devices.

Company B views its service critical to its success in China. Because Company B in China competes with brands like Louis Vuitton, Gucci and the like, offering luxury service is a must. While Company B has not started its e-Commerce business at this moment, the company plans to implement best practices and lessons learned from its previous e-Commerce launch in Japan. Company B plans to provide free return shipment, offer in-store pickup of Internet orders, as well as repair and cleaning services. Expedited shipping is also an option if the customer requests it. In a quest to continually improve service, Company B will include a personal note with every purchase and often will conduct telephone surveys with customers asking for feedback on how to further improve its offerings. From its experience in Japan, Company B’s e-Commerce channel has not only better served its existing customers throughout the country; it has generated a great deal of male customers, a trend not seen in its retail stores.
One theory is that most Company B retail stores are laid out with the female shoppers in mind. Therefore, male shoppers feel much more at ease and in control when shopping online.

For Company A, Yoox, and Company B, service is the most critical element of their business and must be executed flawlessly to their exact standards. Because service directly affects a customer’s experience with the brand, these companies have chosen to keep all activities related to customer interaction in-house. Company C, a shoe company with some luxury product lines, is also focused on service; however, they have taken a different approach.

Company C, currently pursuing its market in Korea, has China in its long-term plan. For its Korean operations, Company C is focused on customer service, inventory management, and handling returns. Given these disciplines are of high priority for Company C, the company plans to outsource its e-Commerce operations. Company C recognizes its lack of experience in the marketplace and plans to hedge against market risks by working with a trusted 3PL partner.

When Company C does eventually enter China, the company also plans to outsource all e-Commerce operations for the same reasons, to hedge against possible market risks in the larger Chinese market.

**Distribution**

To better serve luxury consumers, time to market is critical for these companies. Distribution centers must be located in areas that minimize shipping time to end consumers. Based on current sales trends, the majority of e-Commerce purchases are located in or near the Shanghai region. For this reason, many companies have chosen to place their central DC in or near Shanghai.
For Company A, the decision to place a central DC in Shanghai is a reflection of the company’s sales figures. Of Company A’s customers, 40% are based in tier 1 cities, 35% in tier 2 and the remaining 25% in tiers 3 and 4 cities. Having its DC located in Shanghai gives Company A two primary advantages. First, this location allows Company A to quickly satisfy orders in Shanghai and neighboring high sales cities, maintaining a high service level where the company sees most of its sales. Second, this location also allows Company A to closely monitor the quality of the products as they are transferred in and out of China.

Yoox.com, also operating its DC out of Shanghai currently has outsourced its operations to a 3PL partner. Because all the information about Yoox was gained through its press guide, no further information was available about whom its 3PL partner is in China.

Company B plans to keep its DC operation in house in order to maintain accuracy, quality and service level. From its experiences, Company B has had to spend just as much time and resources managing its 3PL partners as managing its own distribution. Company B will maintain the option to outsource distribution if a capable 3PL partners in China is available, but prefers to operate its own. Company B views its e-Commerce business as an added source of revenue, not a channel that must be optimized right away. Therefore, any incremental cost generated through the supply chain is justified as long as additional profits are realized. Company B’s distribution plan is to utilize its existing duty paid DC in Shanghai for the retail channel to service its sales for e-Commerce, implementing pooled inventory to improve service and save on costs. In addition, because the products in this warehouse have already cleared customs, Company B will be able to guarantee delivery times to the customer, maintaining its high service levels. In summary, Company B hopes to create the right distribution and
warehouse management system that delivers accuracy and quality the first time, and is scalable with increasing demand.

For Company A, Yoox, and Company B, distribution is a key element in enhancing service because it directly affects the accuracy and lead-time of the order fulfillment. In order to minimize lead-time to customers, all companies have placed their DC in/near Shanghai, the region with the highest sales volume, and have employed a hub and spoke system to service other regions in the country via courier services.

**Fulfillment**

To provide the highest service level for a luxury fashion shopper, an efficient fulfillment operation that can pick and pack online orders is not enough; rather a combination of payment services and delivery options combined with flawless fulfillment is required to achieve the best shopping experience possible for the consumer.

Most companies we interviewed did not share the details of their fulfillment operation with us; however, they did share the names of certain fulfillment partners they are potentially considering. Therefore, we recommend PRL to conduct similar assessments in 3PL capabilities and determine whether these potential partners are capable of providing the service required to handle PRL fulfillment.

One company that did share some fulfillment information was Company A. Company A’s fulfillment operation is outsourced to Arvato, a Germany based 3PL that has been operating in China for four years. Arvato is responsible for all pick and pack operations within the DC and all warehouse management operations. At this time, Arvato has helped Company A achieve great accuracy in all order fulfillments. As Company A’s sales volume continually expands into
other regions of China, namely north, south and west, the company is considering going from a centrally located hub and spoke model in Shanghai to opening regional warehouses, to better serve new growth regions.

More consumers are beginning to use credit/debit cards to make online purchases, the majority of Chinese shoppers still prefer to use cash and COD. In order to guarantee payment for products and provide service to these consumers, fashion retailers have employed a variety of methods to achieve both. Company A employs a dedicated in-house customer service staff who will communicate with customers opting for the COD option multiple times throughout the purchase. This type of service will not only alert the customer to where the product is in the fulfillment chain, but also helps Company A to make sure the customer will be there to pick up the order when it is delivered. Company B will again take its experience from Japan and tailor it for the Chinese market. The company will offer COD for all of its customers and utilize individual user accounts to verify their legitimacy.

**Delivery**

Once the payment method has been agreed upon through phone confirmations, orders are sent out to the consumer via FedEx to tier 1-4 cities. Average delivery times range from next day and 2-day service for tier 1 and 2 cities to 3 – 5 days delivery times for tier 3 and 4 cities. From our interviews, it is apparent that FedEx has shown the capacity to provide the service levels necessary in terms of timeliness and courtesy. Companies are also starting to segment its customers based on their registered location, offering different shipping options based on postal codes.
For more remote locations outside of FedEx’s coverage area, EMS is used; however, retailers displayed concern that EMS is not able to provide the same luxury service FedEx is able to provide. Aside from delivering orders to the end consumer, some retailers have contracted for additional services with FedEx at no cost to the customer. For example, products ordered from Yoox.com can be tried on before accepting and paying the courier.

Our initial belief that delivery time was the most critical factor in the e-Commerce shopping experience has been proven incorrect. While it is true that customer want their products as soon as possible, they are reasonable in their demands if the delivery service is courteous and timely. From our interviews, we have learned that it is good to offer next or even same day delivery, but in general people are okay waiting 3-5 days. For customers who live in remote cities where international carriers do not service, 7-10 days is the generally accepted delivery time frame because consumers understand they live in a remote area and that deliveries take longer to get there.

With the help of PRL’s logistics team, shipping rates were gathered for both next day and 2 day delivery service throughout tier 1 and tier 2 cities in China. The carriers quoted were DHL, FedEx and SF-express, a specialist Asia forwarder. The assumptions we made for delivery quotes are as follows:

- Carton Size – 60 x 40 x 40 cm
- Chargeable weight – 20kg per carton
- Tier 1 city – 1 working day turnaround
- Tier 2 city – 2 working day turnaround

Table 3 and Table 4 show quoted delivery rates from Shanghai, Guangzhou, Beijing and Fuzhou. An examination of these rates highlights FedEx and SF-express to offer the best prices.
A comparison between FedEx and SF-express shows that when FedEx is the cheapest option, it is typically 10RMB cheaper. Conversely, when SF-express is the cheapest option, it is often 40 to 50RMB below FedEx. In addition, Figure 7 demonstrates that FedEx offers the best price in cities where PRL is forecasted to have the highest e-Commerce sales, and SF-express offers better pricing in markets that are not PRL’s top selling regions. Finally, Figure 8 uses quoted FedEx shipping rates to determine DC location; however, sales volume is not considered in this consideration and has to be weighted accordingly to account for total delivery costs. Per market estimates, Shanghai will have the highest demand for products. Therefore, more weight should be given to Shanghai’s quoted rates.
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Figure 7 Using Shanghai as the central DC, average delivery rates are shown for PRL’s tier 1 and tier 2 markets.

- Green: FedEx demonstrated the lowest rate
- Teal: SF-Express demonstrates the lowest rate
- Purple: Rates were similar between FedEx and SF-Express
Figure 8 Using FedEx as the primary carrier, colored cities denote lowest shipping rate from respective DC.
Red: Shipped from Beijing
Yellow: Shipped from Shanghai
Green: Shipped from Guangzhou
IT integration can help luxury fashion companies further the service levels offered to customers. By understanding consumer purchase patterns and analyzing trends in aggregate, companies can not only better forecast for future sales but also can shape future demand through planned promotions and other events. Currently, customer profile and order information are not shared between physical stores and Internet sales for any company we interviewed, and no supply chain optimization is done in that respect.

Additionally, IT integration is critical to the distribution and the fulfillment operations within a luxury fashion company’s supply chain. While many businesses did not share their information technology practice with us during the interviews, they all agreed that having the right systems in place will be critical to implement the correct ordering policy, accurately count inventory levels, understand sales trends in real time and anticipate possible changes in the market place.
Recommendation / Conclusion

Based on our analysis of the information collected from industry interviews and research journals, we present our recommendations for an e-Commerce fulfillment model to meet PRL’s operational values and corporate objectives. Based on PRL’s operational objectives—flexibility, minimal infrastructure investment, scalability, partnerships, and service—we have placed PRL’s time to market and ability to provide a luxury service for its customers top priority.

Distribution

Our first recommendation is for PRL is to locate its distribution center in or near Shanghai, leveraging the brand’s established presence in the area and strong continual growth. Our study has shown that with the distribution operation in the Shanghai region, PRL will be able to reach the most number of customers in the shortest amount of time. While the long term growth in China will lead to interior tier 2 and 3 cities, PRL’s initial e-Commerce customers will mostly be in locations with established retail store presence. At the same time, PRL should explore areas near Shanghai that would offer similar operational capabilities and efficiencies while lower in cost.

As shown in Figure 9, the placement of a DC in or near Shanghai would allow PRL to service its biggest retail and e-Commerce market, Shanghai and Beijing, in the shortest possible time and lowest delivery cost. Table 3 and Table 4 highlight the exact rates for typical shipment size.

Once the e-Commerce business is operational, PRL will be able to analyze other growth regions and determine whether to open additional regional DCs to improve service time.
Inventory Management and Risk Pooling

While our interviews with luxury apparel companies did not provide us any direct knowledge on their inventory policies and DC practices, we were able to glean factors they considered critical to their business. These factors are inventory management and costs associated with the DC operations. Given these considerations, we recommend PRL to keep its inventory management and DC operation part of the supply chain in house to ensure high quality and to utilize the correct working capital appropriate for its e-Commerce business. In addition, PRL should aggregate its sales forecasts in wholesale, retail and e-Commerce, to create an overall forecast at the China country level. This practice would allow for PRL to carry less
inventory throughout its selling season, decrease its chances of stock outs at the SKU level, and quickly react to fluctuations in country without sacrificing the brand’s service level.

An example of this is already practiced with Company B in Japan, where an e-Commerce order would be pulled from the shared inventory with retail. This practice has helped Company B avoid issues with minimum order quantities and separate ordering management fees.

Similarly, PRL can benefit greatly from this practice of pooling its inventory between the various sales channels and sourcing its products at the country level. For example, imagine China’s e-Commerce forecasted sales of 40,000 units of a particular SKU, but because of minimum order quantities, the sourcing team is forced to purchase 80,000 units instead. Aside from doubling the inventory value, PRL’s inventory holding costs, obsolescence cost, ordering fees, manufacturer’s fees, shipping, auditing and vendor management fees all increase, greatly decreasing PRL’s working capital. Now imagine if this scenario is applied to all 10,000 SKUs within PRL’s product portfolio in a given year, minimum-ordering costs alone would result in millions of dollars lost. Conversely, if inventory pooling was implemented across all sales channels, minimum order buy challenges, stock outs occurrences, and inventory costs would all decrease.

**Fulfillment**

Because e-Commerce is very new in China and the learning curve will be steep, all companies we interviewed have outsourced or are considering to outsource their fulfillment operation to 3PL partners, namely Arvato, Om Log, NanYang and HongYing. While fulfillment is an important aspect of the supply chain, ensuring accuracy and speed in moving the product to
the consumer, we believe PRL should maintain its focus on value driven activities for the brand such as inventory management and customer service.

Fulfillment is an operation critical to the success of e-Commerce; however, it is not one of PRL’s core competencies. Therefore, we recommend PRL to outsource its fulfillment operations to one of the many 3PLs operating in China. “Generally, the functions to be outsourced are those that are not core to the business or critical to the mission of the business” (Rosenfield & Beckman, 2008).

Further assessments need to be conducted to choose the right partner, but outsourcing this operation will allow PRL to enter the market sooner and learn from a company with local experience operating in Shanghai and with e-Commerce. In choosing the appropriate fulfillment partner, PRL has to consider the 3PL’s ability to handle style velocity (the number of SKUs made available in a given selling season). For instance, PRL is a high style velocity brand, carrying thousands of SKUs over its five selling seasons, and will need a partner with robust fulfillment capabilities. Based on our interviews, some of the companies exhibit lower style velocity, different from that of PRL, thus we do not recommend a specific 3PL fulfillment partner at this time. In the long run it may be advantageous for PRL to own and operate its own fulfillment operation, but we believe outsourcing will save PRL time and money in the short-term.

**Delivery**

Delivery in China is much like Europe in that there are many regions with different customs, consumer expectations, and regulations. These market characteristics pose a challenge in trying to find a delivery partner who can work across all of China. Our conclusion is that PRL
will have to work with multiple carriers to reach all of its customers. The two carriers utilized
the most amongst the companies we interviewed are FedEx and EMS.

FedEx provides timely and consistent service, and has experience working with return
logistics and COD. Therefore, it should be strongly considered as the primary carrier. While
FedEx does not provide the cheapest rates everywhere in China, it does provide the best rates
and service to PRL's largest markets in Shanghai and Beijing. However, further analysis should
be conducted to determine demand level in given cities and the available service options
provided by other carriers.

For remote interior markets outside of FedEx's network, PRL should consider working
with EMS, as it guarantees delivery to every postal code in China.

Within in major city centers, PRL should leverage upscale locales such as PRL stores,
high-end hotels, and country clubs to allow customers to pick up their online purchases. These
options allow PRL to control the last mile delivery experience and integrate its clothing with the
luxury lifestyle. Upon pick up, customers should also have the ability to try on the product and
return it on the spot if they are not satisfied.

Returns are an important aspect of service and need to be handled with as much care as
the delivery of the product. PRL's interaction with each customer does not end when a sale is
made, but continues through fulfillment, delivery and possible return of the product. We
recommend PRL to provide free returns of all products within 7 days, and work with the
customers to understand their reasons for return for continuous improvements.
Premium Delivery

As identified, time to market and last mile delivery are the most important components to providing a luxury service, we recommend PRL to provide a few unique services for its high value customers. To improve the current state of last mile delivery and provide a true luxury experience for the luxury role model customer, PRL should consider keeping the last mile delivery in house in its largest market regions, such as Shanghai and Beijing. “An experience occurs when a company intentionally uses services as the stage and goods as props, to engage individual customers in a way that creates memorable events” (Simchi-Levi, Kaminsky, & Simchi-Levi, 2008). We believe PRL has a lot to gain by engaging the luxury role model customer with a differentiated service as these customers truly care for the shopping experience. And while they only make up 1% of the luxury consumer population, the luxury role model customers are projected to constitute 24% of total luxury spending by 2015 (Atsmon, Dixit, Leibowitz, & Wu, 2011).

We propose that PRL hire and train retail sales staff to provide a personal concierge service for its highest spend customers in its top performing cities. These employees could also be retail sales people. Customers would have the convenience and experience a true luxury service by specifying delivery times at their home, office, PRL store, or luxury hotel where a personal concierge would deliver their order with additional products to match. As explained by Simchi-Levi, “Service and support not only can generate additional revenue, but, more importantly, they can bring the company closer to the customer and provide insight in how to improve its offering, tailor support, and find the next idea to add value to its products and services” (Simchi-Levi, Kaminsky, & Simchi-Levi, 2008). PRL can use this type of service to
differentiate itself from competitors, up-sell its luxury role model customer, and strengthen
customer relationships to continually offer better service.

**IT**

To successfully launch its e-Commerce business, PRL will have to link all of its
opérations tightly through the use of information technology. Inventory level data, point of sale
information, delivery schedule, customer information, and customer service will all have to be
available and accurate so that PRL can provide the best possible service and achieve its business
objectives. In order to accomplish this challenging task, a robust enterprise resource data
management system will have to be utilized to manage inventories, schedule operations, manage
customer information and services, and anticipate possible changes in the market place.

To maximize customer service, PRL should integrate its customer service, e-Commerce
and retail platforms. This will allow PRL to know who the customers are and how it can best
serve them. “Companies learn about each customer through databases and interactive
communications, and sell to one customer as many products and services as possible throughout
the lifetime of the customers, tracking the customer’s preferences and needs, and further tailoring
the company’s offering to the customer” (Simchi-Levi, Kaminsky, & Simchi-Levi, 2008). In
addition to managing communication online, PRL should facilitate for customers to speak and
interact with staff, answering any questions and concerns over the phone. Hand written notes
and courtesy calls are also great ways to further connect with the customer.

Integrating these platforms will allow PRL to leverage customer profiles and personalize
communications based on the customer’s purchase history, interest and lifestyle. The concept is
to treat each individual as an account. To ensure customer service agents and sales reps utilize
this system, we recommend incentivizing them with commission for each ‘account’ they have. This approach will allow them to receive commission for on and offline sales while creating a relationship with the customers. Making this connection with the customers will help PRL collect information outside of purchasing habits, such as hobbies, lifestyle, and aspirations, allowing PRL to target them with special offers, promotions, or advertisement. Additionally, surveys and questionnaires should be used to gain customers’ feedback and shape service to meet their needs and expectations.

Another reason for an integrated IT system is to give customers up-to-date information on where their products are in the fulfillment supply chain, such as when product are shipped and expected delivery times. “An important value-added service is information access. Allowing customers access to their own data—such as pending orders, payment history, and typical orders—enhances their experience with the company. For example, it is well known that customers value the ability to know the status of an order, sometimes even more than the actual turnaround time” (Simchi-Levi, Kaminsky, & Simchi-Levi, 2008). This understanding needs to happen in real time and syncing systems once a day will not be sufficient especially with the rise of mobile applications.

Aside from utilizing an integrated IT system to improve customer service functions, IT can be an important lever to improve operational efficacy of PRL’s supply chain. For example, inventory management can be greatly improved with up to date sales information, both in store and online. If PRL implements pooled inventory in China, this information will be all the more critical for the allocation team to manage channel fulfillment. Similarly, with a robust IT system, sales volumes and trends across the country can be visualized in real time, allowing PRL to constantly improve its sales forecast in country. Finally, the appropriate IT platform would alert
appropriate personnel of possible issues and help PRL prevent possible shrinkage and loss of products along the supply chain, aiding PRL’s bottom line.

**Mobile Technology**

Chinese consumers are increasingly using mobile devices to interface with the Internet; they are not necessarily sitting in front of a desktop at home or in their offices when making online purchases. More and more, they are shopping online from a mobile phone while traveling to and from work on a train or bus. China’s online population is not only going to be bigger than any other market, but will also adapt quicker to new technologies and Internet interfaces than people in many other markets. This uptake of technology and willingness to shop through the mobile device presents both opportunities and challenges for PRL. The challenge for PRL will be to keep up with these technologies; however, mobile applications present opportunities to increase product accessibility and marketing.

**Customer Service**

In order to provide the best experience for a customer, PRL should keep all the customer service in house. According to the CEO of Company B Asia, Chinese consumers know what good service is and they expect it. PRL cannot expect an outside company to provide the level of service that it demands itself to provide.

Through our work we have developed additional ideas that PRL can implement to fully capitalize on an e-Commerce business. For example, there is a false assumption that e-Commerce customers are radically different from retail customers, but that is not always the case. Understanding that e-Commerce customers differs only slightly from retail customers leads us to recommend PRL to utilize retail store marketing to promote its e-Commerce business.
This can look many different ways, one idea is to host in store events with celebrities and Chinese figureheads to promote the PRL lifestyle. At these events, PRL can promote the new e-Commerce business and demonstrate the ease and effectiveness of buying online. To accomplish this, PRL should create a website that meets customer needs and preference, such as an online dressing room where customers upload an image of themselves, enter their measurements, and virtually try on different products as shown in Figure 10. With the ability to mix and match their own outfits, the customer will also receive suggestions and style feedbacks from predetermined popular wardrobes. With this tool, customers will know what they are getting; how it fits them, and even receive comparisons to celebrities and models that have previously worn similar outfits. This customization will also help PRL shape demand by offering style suggestions to purge items that are slow movers in its inventory if certain matches are made within the selected wardrobe.
Figure 10 Customized dressing room allows the user to choose different tops, bottoms, and shoes; the website will automatically fit the clothing to the model that is of appropriate size of the customer and offer feedback on his/her selection.

Another way to draw people to e-Commerce and shape demand is to offer limited edition or exclusive online products. These products will target fashion fanatics, a group of consumers who search for the latest and most fashionable products and who often will shape consumer preferences. Offering these products online will allow PRL to test the market for large release of new styles and create online buzz about its products.
Conclusion

The opportunity for Polo Ralph Lauren to grow its business through China e-Commerce is undoubtedly great. However, this is a new market for PRL, and launching successful e-Commerce business is far from simply creating a localized website. Successful e-Commerce for PRL will require scalable distribution, flexible inventory, close to market warehouse, accurate fulfillment, speedy delivery, secure payment options, integrated information technology and best in class customer service.

For these reason we have recommended that PRL keep the DC operation, inventory management, customer service and the premium last mile delivery in house. However, for its fulfillment operation, we believe it is best for PRL to outsource this to companies with local experience. As PRL grows and learns from its partners, it can look to take over these operations. This approach will allow PRL to increase the accessibility to its products, provide best in class service and minimize the time to market for its products.

In addition, we believe PRL should focus on understanding and segmenting the different consumers in the market, while offering customized services to each group.

Table 5 highlights our recommendations based on customer segmentation and service level.
<table>
<thead>
<tr>
<th>Customer Type</th>
<th>Strategy</th>
<th>Service Level</th>
<th>Distribution</th>
<th>Fulfillment</th>
<th>Delivery</th>
<th>Technology</th>
</tr>
</thead>
<tbody>
<tr>
<td>Polo Ralph Lauren</td>
<td>Segment services by customer and region</td>
<td>In-house customer service</td>
<td>Locate near largest customer base in Shanghai</td>
<td>Outsource to FedEx and EMS for regular deliveries</td>
<td>Keep premium deliveries in house</td>
<td>Online/offline integration</td>
</tr>
<tr>
<td>Luxury Role Models</td>
<td>Best in class service for purple label or high spend customers</td>
<td>Concierge Service, Customized delivery times, Exclusive Preview Events</td>
<td>Offered in tier 1 cities</td>
<td>Regular or concierge Service, Up-sell at delivery with matching garments</td>
<td>Online Wardrobe, Exclusive Product Previews, Target advertisements with mobile apps</td>
<td></td>
</tr>
<tr>
<td>Core Luxury Buyers</td>
<td>Significant percentage of customers (45%) and the majority of revenue (65%)</td>
<td>Handwritten notes, beautiful packaging, and on time delivery are key</td>
<td>Future DC locations will be determined based on their purchasing patterns</td>
<td>Further assess potential partners to handle high style velocity</td>
<td>Inventory Management</td>
<td></td>
</tr>
<tr>
<td>Fashion Fanatics</td>
<td>Fashion forward customers wearing the latest PRL products</td>
<td>Access to product is more important than delivery time</td>
<td>Offer limited edition products and colors</td>
<td>Incentivize longer delivery time with free shipping</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rising Middle Class</td>
<td>On-time and courteous delivery, Free return service</td>
<td>Offer loyalty program and discounts</td>
<td>Future DC locations will be determined based on their purchasing patterns</td>
<td>Incentivize longer delivery time with free shipping</td>
<td></td>
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