# External Analysis

* Consolidating retailers = purchasing power squeezing down margins
* Fast growing competitors with lots of means (10x larger)
* Compete in high end outdoor apprel.
* Main competitors: North Face, Marmot, Mountain Hardware, ARC’TERIX

# Internal Analysis

## Operations management

Production partners selected based on values

1/3 COGS comes from manufacturing (calculate $ amount from financials)

2/3 from raw materials

* Supply side / supplier relations
  + Trimmed from 200 to 41 suppliers in 2003
* Production process
  + Focus on reducing environmental footprint of production process
  + 85% outsourced outside NA; labor costs in NA are 4-10x higher than elsewhere
  + Order 2-5000 units per style
* Cost controls
* Distribution Network(s)
  + During the 80s, grew sales from 20M$ to 100M$ and expanded internationally to Europe and Japan
  + Suppliers ship products to distribution center in Reno Nevada; used as service center
* Risk Management (Financials)
* Financial ratios
* Capital requirements
* Cash flow
* Z score
* Company worth
* Funding / sources of capital

1400 employees (exhibit 2 eomplyee/$ sales comparison)

Spend less than 1% on marketing/advertising (industry average?)

Cost of environmental commitment: 3.8M$ in 2009 (exhibit 10)

Gorilla marketing tactics:

* Amex spent 3M$ for a Patagonia commercial
* Offered to donate 10$ per protesters picketing

Sales:

* Annual growth of 6% in net sales, donate 1% to environmental causes
* Targets 10% annual growth in sales for the next 5 years
* Growing ~200M$ in sales by 200
* 4 channels:
  + Wholesale: 1000 dealers, compared to Columbia 4000 dealers, including department stores and mass market (not used by Patagonia). Generated ~145M$ in 2010
  + Retail 33% sales, only offer 80% products: Patagonia own 26 retail stores in US; 52 WW. Earned $100M with 65% margins; used as point of contact with customers
  + Catalogue/internet 23%. Catalogue only 60% sales, other reserved for lifestyle

Organic cotton:

* Reduced product lines from 91 to 66 styles in 1995/6 following use of organic cotton
* Prices are 50-100% higher than conventional cotton
* Some fabric vendors had resistance because of limited availability of organic cotton; Patagonia had to go the start of the supply chain
* Let to some losses in quality
* Sale price ~8% higher

Following table – assume 1/3 of costs is mfg, and 2/3 is raw materials as stated in case. Out of material costs, 80% is fabric rest is buttons and zippers

Fabric cost for performance is 10-15% higher than competitors

## Customer management:

Customer median age 38 and average household income of $160,000

* Has the company figured out who they want as customers?
* Have they segmented the market properly?
* Have they figured out who they don’t want to attract?
* Does their marketing and sales operations accomplish what it should?
* Any loyalty programs?
* How are they building lasting relationships?
* Are they cross-selling?
* How are they attempting to get customers to buy more?
* Customer Selection
* Customer Attraction
* Customer retention
* Getting customers to buy more

## Innovation / products

4 main categories of products:

* Sportsware: Casual clothing including cotton shirts.
* Technical outwear: Insulation and technical shells.
* Technical knits: Base layers with fabric treatment
* Hard Goods: Packs, accessories

Gross margins for all product lines ranges between 50 and 55%

Products focused on simplicity

Criteria for product development:

* Quality:
  + Spend 100k$ annually on field testing
  + Only update product when major jump in features
* Environmental impact:
  + Focused at every step of the process (including packaging dyes)
  + 1996 started using organic cotton (1/5 products are cotton); increased COGS and limited availability
* Innovation:
  + Invest 3M% Annually in R&D (Need % sales and industry average)
  + Have a lab to develop and test new materials

Charge roughly 20% higher than other outdoor apparel, and 50% higher than mass market

[do positioning map]

* Do they know what the next generation of products is like?
* Do they have great R&D partners?
* Review design and testing methods
* Analyze cost and time controls of innovation
* Are they successful at bringing new products on stream?
* Review their coordination efforts between innovation and operations
* Product research
* R&D
* New product prototyping
* Go to market for new products

Removed anti odor chemical agents in 98 although trending in market, only reintroduced in 2004 when environmentally friendly solution invented.

Offer repair/refund/replace guarantee; costs $350,000 annually to repair 12,000 garments

Return rate is 2.6% for wholesale and 12.9% for direct (compare with industry average)

## Social and legal policies

* Environmental issues and solutions
  + Known as a worldwide leader of environmentally responsible business
  + Donate 1% of revenues to environmental causes
  + Invest in reducing environmental footprint of production process
  + Patagonia is an experiment to challenge conventional wisdom and present a new style of responsible business; distanced from typical corporations to blame for environment issues
* Health and safety
* Employment diversity
* Being a good social citizen
* Playing ethically
* Compliance with regulation
* Social reputation

## Leadership / Management

* Patagonia owned by Lost Arrow, a holding company owned by Yvon and Malinda (sole shareholders)
* Private = easy to maintain sustainability (but hindering growth – if were public, shareholders would exige better returns and growth)
* Board (Yvon, Malinda, 2 children, Kristine McDivitt Tompkins) drives changes (vision) while CEO (Sheahan) executes and manages day to day. –issue: Board doesn’t really have inpendent board members; bias and unchallenged ideas

## Overheads

* Hiring and training the right employees
  + Major turnover of CEOs in the 90s and 2000s, difficult to find a CEO that shares and can execute the vision
* Effective IT systems
* Review how effective top management is
* Is the culture suitable?
* Does management work as a team and share ideas and help each other?
* Are all parts of the company working toward the same goal?

Voted best company to work for; 10k resumes for 100 jobs (100-1 ratio)

<5% turnover ratio

53% employed > 6 years

1400 employees

All buildings engineers eco friendly

Unconventional benefits:

* Offer paid sabbaticals of 2 months for employees for volunteer work for environmental organization
* 2000$ for hybrid car
* Bail you out of jail for peaceful protest

## Competitive advantage

* Does a firms resources and capabilities add VALUE by enabling it to exploit opportunities and/or neutralize threats?
* Even if the capabilities are valuable they must be RARE to give a firm a competitive advantage over rivals. How many rivals possess the same capabilities?
* Can these capabilities be IMITATED? Can rivals eventually catch up to us at a reasonable cost? If capabilities can be imitated, the competitive advantage may be short-lived
* Is the firm ORGANIZED to take full advantage of its capabilities and resources?

## Strategic approach / result

Be environmental, good for brand but hurts growth

# Identify issues / key points

Implement a new radical environmental initiative: “Product lifecycle initiative”:

* Expand existing practice such as repairing and recycling old garments and establish swap market for customers.
* Tell customers to buy less and think twice before replacing. Encourage customers to limit consumption to essential products but focus on quality; Patagonia promise high quality reparable goods
* Patagonia focus on repairs, then facilitates reuse by giving it away or swapping
* Extension of Common threads recycling program (launched in 2005): recycle polartech and organic cotton from all brands (Check financials 2005/2006)
* Implementaiton: establish online swap market, hold retail swap events, donate still useful products to environment charity.
* When worn out completely, return to Patagonia for recycling
* Patagonia to provide postage paid repairs/returns
* Implement swap market – partner with eBay or MEC? (check values of those companies to ensure matches)
* Risk: Limit sales growth by selling used
* Repair/recycle:
  + increases costs by 60k$ first year of implementation (labor + shipping)
  + Also needs investment in increased capacity (capex): currently stores can’t even process existing repairs. – need to increase staff of partner up with 3rd party regional repair center
* Recycling: Currently only allows recycling of ½ garnments collected. To increase from 65% to 90% in 1 year = lots of investments in R&D
* Consider offer service to other products (like currently the case for Polartec fleece)

Other:

How to achieve 10% annual growth in next 5 years (currently hitting 6%)

Address inventory management since shortages cause inability to satisfy demand for many products

Product mix (Hard goods only 6% sales; divest?)

Distribution: Focus on retail – high margins low returns

Fix – why 13% return on direct sales?

# Strategy

Push sales towards catalogue/internet (higher margins)

DO something about returns

# Implementation:

Further segment customers – beyond just one outdoorsy wealthy dirtbag

High return rate – open flagship stores to try our merchandise? Trial program? App-enter measurements and will tell you what might fit best

Add at least 1, optimally 2 independent board members to challenge status quo: bring in new ideas but maintain majority voting and control

$350,000 to repair 12,000 garments annually = 30$/ garment

Sell repair kits

In forecast – add additional cost to borrow

Assume borrowing at 7% (no data provided)