EcoParc Model – Questions from AAPN Membership: Bill's Response

Retailer Questions

- What retailers have participated in a proof of concept? Have any signed up for the working group? What type of commitment are you asking from them?

From Bill: While I was still at PVH the initial plan was to stand this concept up in Europe. At that time, we had a number of Group calls with all the Major UK and EU Brands. The concept was very well received at the C-Suite level, because it tackled most of the core challenges, they were all struggling with and Increase profitability. BUT all of them questioned if the supply base was willing and capable of operating on the new model.

I retired.

These initiatives require first movers to build it and then the retailers will come.

With the MDDO model we can eliminate the start up risk by producing product that already meets the criteria for the Eco Parc. Product produced offshore and being aired into the USA.

Brands are not supply chain infrastructure builders, never have been, but they will use it when it is built.

What we have been asking from the Brands is:

- They own any pre-positioned Raw materials.
- They commit to consume the production capacity or Pay the costs of any unused capacity.
- That the improvements in Margin are shared with the supply base.

- Does this lend itself to all size brands (ie. Small/Med/Large)? Or specific sized companies?

From Bill: Quick answer is Yes. We clearly see the benefits to the large Brands on Inventory reduction, lower markdowns, lower out of stocks, higher profits. But we also see this as valuable all the way down to individual designers, who today find it difficult to scale any winners and find it impossible to take those winners global. The MDDO network allows that to happen.

One of the fastest growing apparel segments on shore is the digital printing or value add for Influencers, celebrities, etc. But these are generally constrained to T-shirts, Hoodies or Caps that can be held as Blanks. The Eco Parc will open this up to many more categories, exponentially increasing what's on offer to this new retail segment.

- Post covid, do retailers really have OTB like they had before? What trends are you seeing?

From Bill: Remember that OTB is a mechanism that the finance teams use to reduce risk and constrain buys to what Stores, B&M, can process. With the B&M and DTC models we have today, every CFO would happily lower the OTB constraints if they had a much higher level of certainty of selling the goods at full Margin. In fact, if you could guarantee 100% sell through; almost all restrictions would be lifted, fully funded by the cash they would realize from much lower inventories. This would open up the current OTB by at least 12.5%, significant!

I see the MDDO model as helping Brands unlock all the financial controls, they have in place to minimize downsides of low sell-through styles. One of which is pushing the price to the lowest level the supplier will accept as they need to factor in low sell throughs.

- Do you envision 1 retailer per parc or multiple sharing it?

From Bill: Multiple Brands; But, TBD, I could imagine a park specializing in a few categories so materials, equipment and skillsets could be leveraged across the park.

- How are retailers going to plan for this in their business model – blended cost?

From Bill: Great question and one of the biggest to solve for. I am at a meeting in Miami this month with a number of Brands touching on this topic. I personally don't like the Blended model. I would like to see a product have 3 quoted values, which I think could be auto generated once all the parameters are established. This allows planning to calculate cost versus time value. This is the work I do with O9 Solutions, supporting the development of that tool set.

Note: The Brand would only negotiate the price with the initial supplier, typically Offshore or Nearshore. The other 2 costs would be autogenerated and nonnegotiable.

- Would this be proposed as an innovation center or a test/run center for each retailer with the option of scaling production? How has it been pitched to retailers? What specific issue is it targeting for them?

From Bill: The high-level initiative is to allow Brands a rapid response, where needed, but lower / slower supply where speed isn't of the essence.

But, yes, we do see this as becoming a primary Design, Development and test center for new products.

Nike announced it's looking to pull its development capability back to the US, Levis did the same years ago and saw a big benefit from it.

The key elements are:

1: Develop locally, bringing Suppliers and designer together, working in real time.

2: Allow Brands, Suppliers, and advanced Machine manufacturers to work together on new technology.

3: A place for the Suppliers and advanced machine manufacturers to support innovators develop their concepts for our industry. Similar to a Plug and Play innovation model.

4: Small orders to test the consumer appetite so more accurate Bulk orders can be placed offshore or nearshore for seasonal floor sets or new core items. "Test & Chase"

5: Read and React; Instead of Retailers having to place 100% of the buy offshore, then keep their fingers crossed they got it right, this allows them to place 70% of the order in the Blind, then as soon as they have a few days of sales they react. Placing quick upside needs into the EcoParc while nearshore offshore reacts on a slower turn. This works for fashion items and Seasonal Core items. It also eliminates the excess goods from slow sell through styles.

6: Eco Parc would produce small fashion runs so that the established US Brands can compete with SHEIN, H&M and Zara's fashion edge.

7: Finally, we see it as helping address the challenge of a widening Size offering that Brands are struggling with. The fringe Sizes are very difficult to keep in stock without abnormally high "Weeks-of-On-hand Inventory in their DC's. These are expensive and often unprofitable due to the high excess or out of stock rates. These could be made in the Eco Parc on a Made-to-Demand basis.

<u>Supplier questions:</u>

- Most of the examples are calculated from 100 units, we understand that's for easy math purposes – what do you envision the unit volumes being for on/near/off?

From Bill: This would very much depend on the size of the Brand, the total style volume etc.

But directionally I would say:

Offshore: 10,000 upward

Nearshore: 2,000 – upward.

Onshore: Made-to-order units of One, Made to Demand Up to 2,000, read and react up to 10,000

- In the today models, we are seeing that the near-shore never receives more than 20% of the future demand, is that an adjustable number or have all your models come to that conclusion?

From Bill: Take the 20% as directional. The higher a Brands' share of pure fashion, the higher the % Nearshore / Onshore. Over time these numbers will increase as we see a rise in the costs across the traditional offshore supply base. The de-globalization of trade (Shipping issues, Duty threats on China etc) will keeping shifting supply from the east to the west, where the consumption is in the west.

- What value do you see in participation for the Near-shore producers?

From Bill: I see 3 primary value sources for the Nearshore suppliers.

1: Most Brands and retailers develop their large volume (Global) styles with their Global suppliers based in China, BD, India, Sri-Lanka, Vietnam etc. They offer the ability to ship any level of volume anywhere and sit within the Raw material base. By creating the MDDO model with the Eco-Parc Brands would now be free to develop styles locally knowing the Near-shore suppler is connected into the Global supply base so capable of delivering any volume anywhere. The Supplier who developed the product gains additional volume and is able to receive an income from products sold globally

Note: The US, Canada, EU, Canada, and Japan will have virtually no projected growth in apparel sales through 2050. The next $ 5 Trillion of apparel sales growth happens across, China, India, South America and the Rest of the World. The MDDO model allows Near Shore Americas suppliers to participate in that growth.

2: Near Shore players produce quick response orders for the Global suppliers, capturing more volume and income.

3: By participating in the model, it reduces the risk of the Global suppliers simply entering Latin America and the US to set up their own models. To date this has been the ask of most Brands.

- How do peripheral participants factor in (like a Lectra or Kornit)

From Bill: Kornit, Lectra, Jeanologia, etc have all been engaged in the discussions from the beginning and are ready to support. The technology can be expensive if not fully utilized. We see the Eco-Parc model as a place these types of high investment equipment could be leveraged across suppliers.

- How do you envision trust being built between participants (on/near/off)?

From Bill: Not easily, nor quickly; but I have 2 past experiences where this worked.

1: At VSS we set up a mutual capacity model across our top 5 suppliers and asked them to collaborate on the production of our "Launch" collections. These required millions of units to be produced for the floor set. The challenge was that we developed 3 concepts for any floor set, each with a different supplier. When the final collection was selected it meant 2 suppliers lost out big-time and one supplier won but didn't have the capacity to meet our demand.

When we suggested they work together to share the orders and meet our demand; the supplier who "Won" never wanted to share, the suppliers who "Lost" always thought it was a great idea. Only when every supplier had become a loser did they get it. VSS committed that their growth would match VSS growth, we would never dilute our value to them by introducing new suppliers. The suppliers committed to share all technical data and would work together on capacity plans, they told VSS where to place the orders. It was this model that allowed VSS to scale so rapidly its launch styles. A committee was set up that consisted of the 5 suppliers and VS, all of whom were considered peers. I took a year to get to a place where everyone trusted each other, because everyone held to their commitments.

2: Similar situation in Ethiopia where VF. H&M and PVH came together to set up the world's largest Green Industrial Park with 20+ of common suppliers. We, brands and suppliers, met every month until we all established trust, and again the key was "Said / Did".

Everyone must be transparent as to why they want to be part of this work, no hidden agendas. That said I have also learned that if you are given reason to question someone's integrity or that their agenda is different to yours; Walk Away.

- What products would you envision starting with?

From Bill: There is already product that Brands are trying to manage across this model. PVH and probably RL make the same product offshore with large suppliers, near shore and downtown LA. But they have to coordinate this across multiple players. We could quickly consolidate this and prove the value, then scale.

Specific Ownership & Financial Questions:

- How will duties be sorted/allocated

Duties would be included in the 3-level cost quoted to the Brands

- What type of capital investment is needed from each participant (ballpark)? How does it get shared across the investment groups?

From Bill: Using an approach that we applied in other locations, we would look to have a state support the building of the Eco Parc base infrastructure and buildings. They recover the income through a rental / leasing model. With the US committed to bringing back industry to the Americas, nearshore and Onshore + the value this delivers on Waste reduction, I believe there are Fed and local funds to support this.

The build-out of the individual facilities within the Parc would be at the expense of the supplier or joint supplier JV's.

The Cutting room, advance machinery facilities could be under the management of the machine companies or a 3rd party. i.e. Lectra Runs the cutting room and charges on use basis, Kornit runs the print facility and changes on a use basis.

Take this as directional as I see this as the detail the working team will get into

- Have you thought about doing this as an investment club model – ie multiple manufacturers invest and each can utilize as needed?

From Bill: That is definitely an option, for all or some of the elements of the model. The question to consider is "what happens when a supplier wants to Exit the Eco Parc or a new supplier wants to enter the Eco Parc"? certainly, do-able but needs thought through.

- Where does the fabric come from? Concerned with so much cash being tied up in piece goods, but concern is pending ownership.

From Bill: Initially we see the fabric coming from outside the US and a lot from outside the region so there is a need for material prepositioning, A model I actually disagree with and one that people like Shein and Temu use against the large Brand, but needed in the medium term.

But we can accelerate the shift of the key materials onshore / near-shore through a collective engagement with mills, something any one supplier or Brand would find difficult.

I would like to see the raw material risk be held by the Brands NOT by the suppliers. The Brands benefit greatly by being able to delay a decision on the material conversion. In the Current model they not only take on the material liability months out, they take on the full FOB value and high level of Risk.

- Doesn't a Hansae or Sae-A already have this model in near/off, would it be easier to work with one of them to insert an on-shore partner?

From Bill: I personally haven't seen Hansae or Sae-A apply this model. They have global facilities and near shore facilities, but they tend to do their own thing and aren't coordinating across an MDDO model. I could be wrong.

They should be part of this work, if they are willing to engage! But as big as they are they still represent a relatively small part of the total supply.

- Who owns the inventory at each stage?

From Bill: As stated above; I would like Brands / Retailers to co-own the Pre-Positioned Raw materials. There is a way to model this for them, so their ownership is based on a rolling forward view of demand.

- Who owns the recycling in the Eco-Parc?

From Bill: With new apparel in the US projected to be flat / decline and resale growing at +30% this is an area that is a large new income opportunity. We have already had enquiries at the state level for this model. I see this as something WM, Waste Management, Thread-Up, Poshmark, Depop etc having a high level of interest in.

But the working team would include this in their work and decide if the Suppliers own it or it's a separate effort that leverages & pays the Suppliers for repair services.

Note: when I refer to working team; I see a group of interested Suppliers forming a working group to drive this forward with project support.