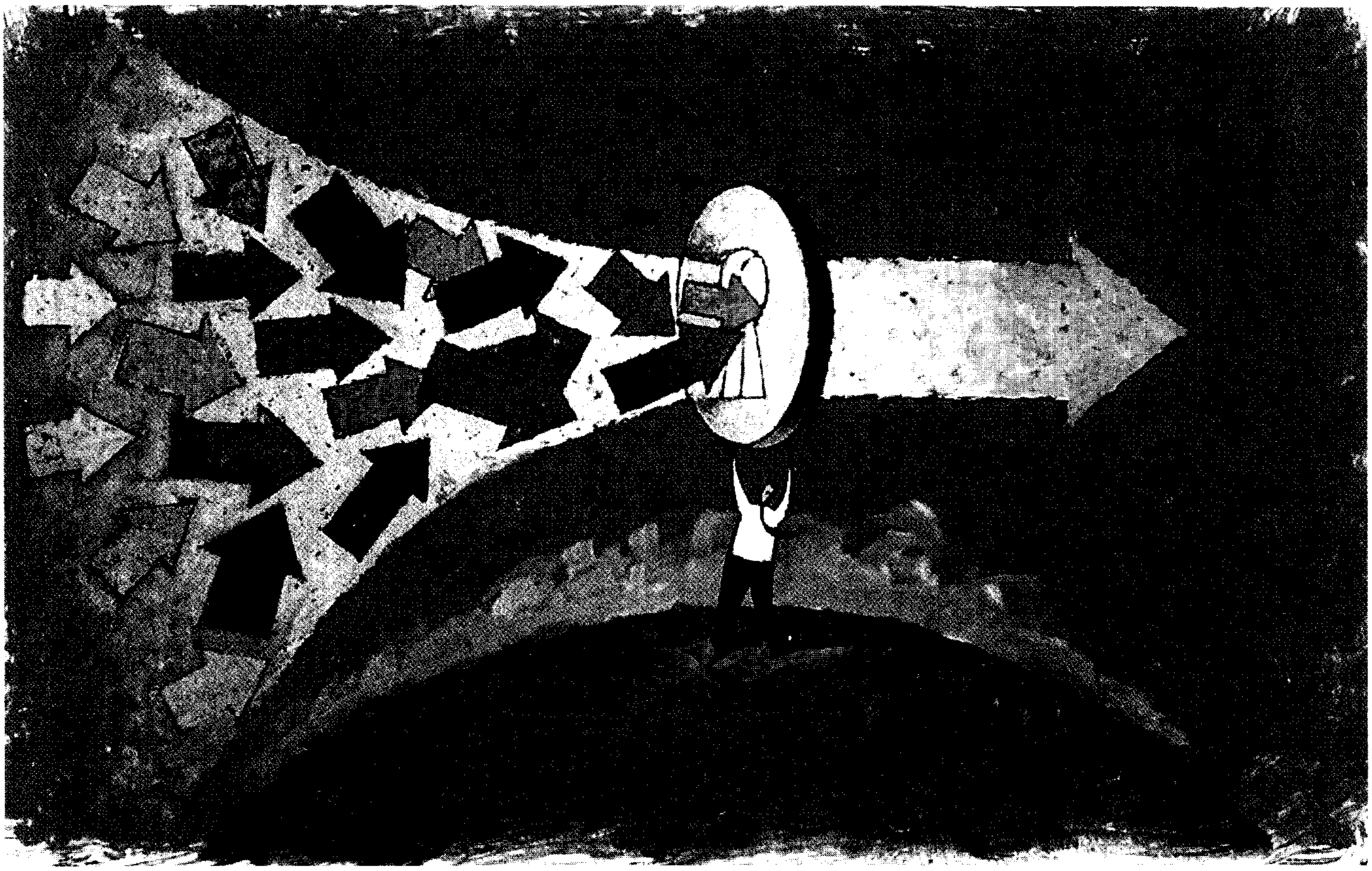
Back to the Future:

Benetton Transforms Its Global Network



Benetton is rethinking its global network of suppliers and distributors and defying conventional wisdom in the process. Its efforts may prove to be a model for other companies with far-flung operations.

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In the 1980s, while the provocative magazine and billboard advertisements of Italian clothing company Benetton caught the consumer's eye, the company's tremendous growth, outstanding financial performance and innovative strategies were captivating the press, scholars and practitioners around the world. (See "The Benetton Group.") For many years, it was the archetypal example of the network organization — that is, an organization based on outsourcing, subcontracting and, more generally, on relationships developed between a large company and several small producers and distributors, or both.[1]

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Several factors contributed — and, to some extent, continue to contribute — to Benetton's success. First is its innovative operations-management techniques, such as delayed dyeing. Benetton postpones garment dyeing for as long as possible so that decisions about colors can reflect market trends better (the tinto-in-capo strategy). Second is its network organization for manufacturing. A network of subcontractors (mainly small and midsize enterprises, many of which are owned, completely or partly, by former or current Benetton employees) supply Benetton's factories. That structure has lowered Benetton's manufacturing and labor costs, has reduced its risk (which shifts to its suppliers) and has given it unbeatable flexibility. Third is the network organization for distribution: Benetton sells and distributes its products through agents, each responsible for developing a given market area. Benetton does not own the stores; its agents set up a contract relationship (a licensing agreement similar to a franchise) with the owners, who then sell Benetton products. Benetton supports the retailers with services such as merchandising.

But Benetton is not resting on its laurels. It is not waiting for a financial crisis or a performance slump to transform itself. True, overall performance has remained excellent. (See "Benetton's Financial Health.") Benetton's managers believe, however, that if the Treviso-based company is to remain competitive in the new global arena, it must have firsthand contact with the end customer, respond in real time to market changes and find new ways to ensure direct control over the supply chain.[2]

To that end, the company is retaining its network structure but is changing the nature of the network. Whereas its main competitors have stuck with outsourcing, Benetton is gambling on vertical integration and centralization. It is betting — perhaps counterintuitively — that it can remain flexible and achieve a high level of performance with a more complex network architecture in which it directly oversees key business processes throughout the supply chain.[3] Benetton also is diversifying into sports — another move not entirely in keeping with conventional wisdom, which suggests companies should focus on their core businesses. The company's choice shows, however, that an enterprise can adapt its knowledge and competencies to a different, though closely related, industry. Finally, although it has embraced globalization, Benetton believes that sustainable value creation cannot be built merely by exploiting cost differentials between nations. It is committed to maintaining key functions at its base in industrialized northeastern Italy; even in its overseas locations, it has established production practices based on its Italian model. The aim is to achieve overseas profits not just from cheap labor, but from sound systems.

Slipping Into Something More Vertical: Transforming the Casual-Wear Business

Globalization is one of two phenomena changing the name of the game in the textile and apparel industry. With globalization comes increasing homogenization of consumers' lifestyles and market preferences worldwide. Homogenization encourages companies to offer globally appealing products, with no major national customization. Brand equity and economies of scale in marketing become ever more important, leading to concentration of market share in the hands of large companies that can control markets through capillary retail structures. Globalization also affects manufacturing, causing companies to bring certain operations in-house (in order to maintain control over the supply chain and to take advantage of economies of scale) and to relocate production abroad to take advantage of cost differentials, particularly for labor.

The other phenomenon is the breathtaking development in information and communications technologies, which dramat-

The Benetton Group

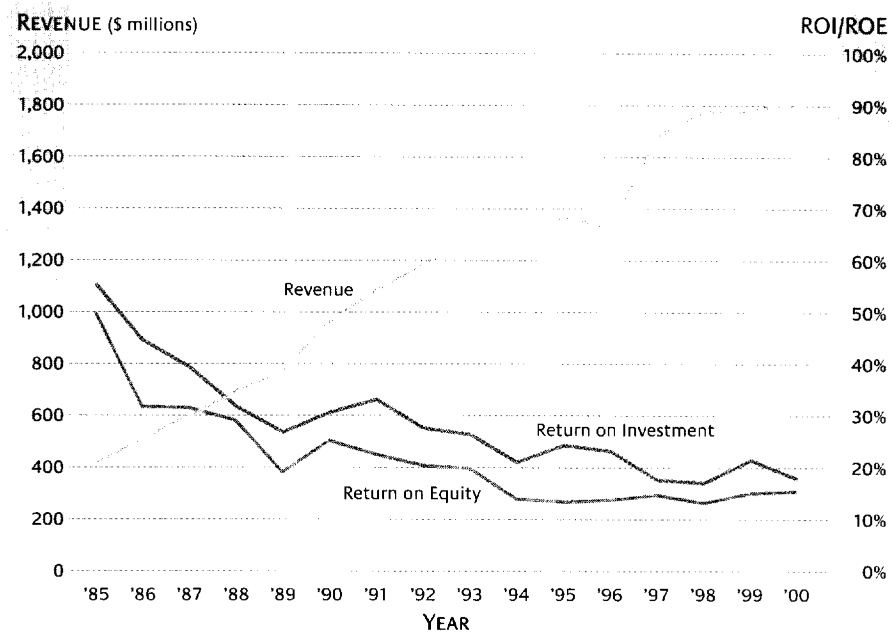
The Benetton Group, a garment producer and retailer based in Italy, has approximately 5,500 shops in 120 countries, 7,000 employees, manufacturing facilities worldwide and annual revenue of more than $1.8 billion. It is controlled by Edizione Holding, the Benetton family's holding company, which owns businesses not only in garment making but also in catering (Autogrill), telecommunications (Telecom Italia and Blu), services (Host Marriott Services) and highways (Autostrade). Benetton Group's interests can be clustered into three distinct areas:

- casual wear (garments, accessories and footwear), distributed under the United Colors of Benetton and Sisley brands and accounting for 74% of total revenue in 2000;
- sportswear (the Playlife and Killer Loop brands of clothing, accessories and footwear) and sports equipment (ski boots, skis, in-line skates, skateboards, snowboards, scooters and tennis rackets, marketed under such brands as Nordica, Prince, Killer Loop and Rollerblade), accounting for 20% of total revenue in 2000; and
- complementary activities (royalties, sales of raw materials, industrial and advertising services), accounting for 6% of total revenue in 2000.

ically reduce information costs, facilitate communications, eliminate distance barriers and allow a real-time response to market change.[4] The new technologies enhance product development and manufacturing, making possible better quality, more efficiency and faster time to market.

In its core business, casual wear, Benetton has addressed such new developments by making big changes in its product design, in its supply and production network and in its retail network. In essence, Benetton has gone for increased direct control and vertical integration. In its retail network, that has meant becoming more like its competitors, but in its supply and production network, Benetton's direction is original.

Benetton's Financial Health



Note: The authors converted the revenue numbers from euros using a fixed exchange rate of €0.9 per $1.

Product Design An international company from the start, Benetton has tended to offer the same or a similar range of products in all the national markets it has entered. However, until recently, more than 20% of the styles in its ranges were customized in order to satisfy the specific demands of each country (smaller sizes for the Far East, for example, or specific colors for Middle East countries). The task of selecting the designs best suited to each clientele was left to the independent retail agents that lead and develop Benetton's estimated 5,500-retail-outlets network. The result was a different image of Benetton in different geographical areas. Today, however, in order to communicate just one image all over the world, Benetton has decided to differentiate only 5% to 10% of the styles it offers in each collection.

Even the number of articles offered in the two basic collections (spring/summer and fall/winter) has been reduced as part of the brand-strengthening strategy. In addition, the company has adopted sophisticated marketing techniques, such as in-store testing, for a more thorough understanding of customers' expectations and lifestyles. It also has increased the number of flash collections launched during each season.[5]

As a result, the basic collections for the year 2001 were reduced, in terms of the number of articles offered, by as much as 35% to 40%. By increasing the number of flash collections and by reducing basic product variance, Benetton can do a better job of capturing customers' last-minute needs and expectations and can avoid offering unappreciated and therefore useless variety.

In 2000, Benetton also streamlined its brands, eliminating labels aimed at babies, children and expectant mothers, including 012, Zerotondo, Corredino and Mamma of Benetton. All garments are now sold under the United Colors of Benetton and Sisley brands. The range is now divided on the basis of age, with different collections for children, men, women and expectant mothers.

Supply and Production Most of Benetton's competitors are international retailers with basically no in-house operations. (See "How Benetton and Its Competitors Configure Their Business Networks.") For its part, Benetton used to outsource the labor-intensive phases of production, such as tailoring, finishing and ironing, to small and midsize enterprises (SMEs) located mainly in northeastern Italy, especially in Treviso county. However, the company always kept in-house any strategic activities and operations that required heavy investment (weaving, cutting, dyeing, quality controls at entry and on finished goods, quality control of intermediate phases and packing).

In the mid-1990s, as volumes increased, that strategy led Benetton to set up a high-tech production pole at Castrette, not far from the headquarters at Ponzano, near Treviso. The production pole at Castrette is among the most advanced in the apparel industry. It covers an area of more than 1,184,040 square feet and is responsible for all Benetton's garments and accessories, both in casual wear and sports clothing. Its overall production capacity is about 120 million items per year.

To take advantage of labor cost differentials, Benetton has established relations with new outside contractors, located abroad. (See "Benetton's Foreign Production Poles.")

Interestingly, Benetton has adopted its Castrette model in the countries where it has relocated, recreating, on a smaller scale, directly controlled production poles. Foreign poles are composed of a subsidiary (totally or partially owned and directly managed by Benetton) that coordinates the production activities of a group of SMEs, often set up and managed by ex-Benetton employees or Italian contractors. For example, Benetton Hungary coordinates the production activities of outside contractors in Hungary, Ukraine, the Czech Republic, Poland, Moldavia, Bulgaria and Romania. The production poles produce to order. The Castrette pole chooses what is to be made by each of the foreign production poles, which then, independently, decide how to allocate production tasks among their SMEs. To ensure high quality, the foreign production poles focus on one type of product and use skills already existing in the area. (T-shirts are made in Spain, for example, and jackets in eastern Europe.) Articles produced abroad return to Italy, where they are prepared for shipping to the final customers.[6]

Recently, the Castrette pole has begun transferring to subsidiaries various activities that used to be kept in-house, such as quality controls at entry and on finished goods, cutting out and dyeing. The Castrette pole's current operations include elaboration (composition and development) of the marker sheets for the computerized fabric-cutting system, which are then sent, using electronic support, to foreign production poles. It also focuses on cutting out prototypes and on quality control of intermediate phases. Through improved communications, Castrette and the foreign production poles can coordinate the timing of the phases so as to reduce production lead times to a minimum.

However, in the apparel industry, time compression does not depend so much on the tailoring phase as on the supply of raw materials. Therefore over the years, Benetton has gradually increased upstream vertical integration to consolidate its textile and thread suppliers. Today, Benetton's main supplier of raw materials — which guarantees that it will provide 60% of the woven fabric, 90% of cotton knit fabric and 90% of carded and combed wool — is 85% controlled by Benetton itself. Both upstream vertical integration and partnership relationships with external suppliers have made it possible for Benetton to exercise quality control over textiles and thread sooner. The materials then can be sent directly to workshops and external producers without further controls, reducing transport costs and production lead times overall.

Nevertheless, Benetton has decided to maintain direct control of the logistics phase and has invested heavily in automating logistics processes in order to achieve total integration within the production cycle, from customer orders to packing and consignment. Today, the average time for consignment is seven days; 10 million garments can be sent out worldwide each month.

Reshaping the Retail Network For many years, Benetton's traditional approach of direct retailing entrusted to third parties was

How Benetton and Its Competitors Configure Their Business Networks

Company	Supply and Production Network	Distribution and Retail Network
Benetton (Italy)	■ strong upstream vertical integration ■ in-house production in 32 production centers: 22 in Italy and 10 abroad ■ outsourcing of production to a network of small and midsize enterprises directly controlled by the Italian and foreign production poles	■ annual revenue of $1.8 billion ■ retail outlets managed by third parties, with about 5,500 stores in 120 countries (old pattern); retail outlets managed directly, with about 60 worldwide (new pattern) ■ average size: 1,292-square-feet traditional shops (old pattern); 10,764-square-feet megastores (new pattern)
The Gap (USA)	■ complete outsourcing of production	■ annual revenue of $13.7 billion ■ retail outlets managed directly: about 3,700 stores, mainly in North America ■ average size: 7,535 square feet
Hennes & Mauritz (Sweden)	■ complete outsourcing of production	■ annual revenue of $3.6 billion ■ retail outlets managed directly: about 700 stores in 14 countries ■ average size: 13,993 square feet
Zara (Spain)	■ partial upstream vertical integration ■ in-house production in 23 production centers ■ outsourcing of production to a network of small shops in Spain and Portugal	■ annual revenue of $1.8 billion ■ retail outlets managed directly: about 450 stores in 29 countries ■ average size: 8,072 square feet

one of the organization's most successful strategies. However, that strategy no longer seems able to sustain Benetton's presence in the market. The company risks seeing its locations suffocated by the aggressive market-penetration strategies of its international competitors, whose retail outlets have a much larger average size. Ever adaptive, Benetton has wisely decided to align with its competitors. Its new retail strategy includes:

1. enlarging its retail outlets, where possible, to enable display of the whole range of Benetton (or Sisley) products, garments, shoes and accessories;

2. where such expansion is not possible, focusing each retail outlet on one market segment or product (only men's products, for example, or only women's products, or only knitwear or underwear);

3. opening large retail outlets (7,535 square feet to 21,528 square feet) on the main shopping streets and in the main shopping districts of big cities.

To implement the third element of its strategy, Benetton developed its Retail Project in November 1999. By the end of 2000, the company had set up more than 60 large retail outlets (megastores) throughout the world, and a further dozen have been opened so far in 2001. Benetton plans to have 100 megastores worldwide by the end of 2002. The aim is to develop a network of medium to large shops directly owned and managed by Benetton itself.

With the Retail Project, which entails complete downstream integration, Benetton is seeking to challenge its main competitors on their terms, focusing on large display areas, on continuous rotation of the displayed products and on selling garments with a high level of styling content. By opening and directly managing its own retail outlets, Benetton can get closer to final consumers, obtain more information about them and reinforce its image. Those are important advantages, because as fashion becomes more subject to lightning changes, quick response to the market is crucial. Moreover, through an information system that links the directly controlled outlets with headquarters, the company knows precisely what is selling and what is lingering on the shelves, and can design and produce collections on the basis of that continuously updated information.

Benetton's Foreign Production Poles

Name	Headquarters	Workshop Locations	Benetton's Equity Share
Benetton Spain	Castellbisbal, Spain	Spain	100%
Benetton	Maia, Portugal	Portugal	100%
Benetton Tunisia	Sahline, Tunisia	Tunisia and Morocco	100%
Benetton Hungary	Nagykallo, Hungary	Hungary, Ukraine, the Czech Republic, Poland, Moldavia, Bulgaria and Romania	100%
Benetton Croatia	Osijek, Croatia	Croatia, Slovenia and Serbia	100%
Benetton Korea	Seoul, Korea	Korea	50% (joint venture)
Egyptian European Clothing Manufacturers	Alexandria, Egypt	Egypt	50% (joint venture)
DCM Benetton India	New Delhi, India	India	50% (joint venture)

Diversifying Into Sports

In 1998, Benetton merged with Benetton Sportsystem, a completely separate company also owned by the Benetton family. The merger has meant facing competition in an industry that is very different from the casual-wear industry. In casual wear, Benetton has a special relationship with its retailers, whereas in the sports business, Benetton must deal with a variety of different players: big distribution chains, small specialized shops and retail agents. None, apart from the agents, have an exclusive relationship with Benetton, which must compete with the other producers in each distribution channel. The distribution chains, in effect, dictate the rules of the game. Typically, all the competing sports brands are arranged in large display areas where they can be compared directly by customers. Furthermore, the sports industry, although differentiated, is highly competitive, and the world market is already virtually saturated.

Benetton has tackled the challenges of the sports business in a number of ways. It sees the greatest and most easily realized synergies as coming from activities linked to sportswear. Moreover, because margins in sportswear are greater than those in sports equipment, Benetton hopes to expand its sportswear business by leveraging its sports-equipment brands. The company has been investing heavily in sportswear development, offering items in its Playlife and Killer Loop collections that are priced from premium levels to very economical in order to draw in a greater number of consumers.[7] It has concentrated management and control of sportswear production at Castrette so as to exploit as many synergies with the production of casual wear as possible.

In the sports-equipment business, Benetton is striving to consolidate the image and equity of its brands through three initiatives: investment in high-tech systems for designing sports equipment, reorganization of the production process and improvements to the retail network.

Over the past two years, Benetton has invested more than $5 million in systems for designing sports equipment. Corporate managers hope the investment will result in products that the consumer considers superior to those offered by Benetton's competitors. If consumers want them, then the large distribution chains will be forced to carry them. Research-and-development activities, which were formerly spread out all over the world, are now concentrated in Venegazzù, in Treviso county. By concentrating the R&D activities of more than 100 people in an open space of about 7,535 square feet, the company also hopes to take advantage of information sharing and knowledge sharing — and the consequent cross-fertilization of ideas. Different corporate and national cultures also mingle. Who knows what may transpire when the U.S. mentality that created Prince Sports Group and Rollerblade meets up with the Italian mind-set that created Nordica? Furthermore, with everyone under one roof, the decision-making process should become more effective and the management of common services more efficient.

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In reorganizing the production process, the two main guidelines have been to maintain and constantly expand the knowledge base, and to minimize manufacturing and transportation costs. In concrete terms, that has meant concentrating production of ski boots, skates, skis and accessories in the Trevignano plant (which is close to Treviso and similar in design to the Castrette production pole) and relocating all or part of production of some products to countries with low labor costs. Some Rollerblade components, for example, are now manufactured in Hungary and China.

With regard to improving the distribution network, Benetton has tried to develop special areas or "corners" dedicated to displaying and selling Benetton's sports equipment within the large sports shops of the distribution chains, and it has constructed a new network of Playlife retail outlets (small, independently owned shops) on the model of the consolidated casual-wear business. Moreover, Benetton is attempting to develop partnership-based commercial relations with the big specialized distribution chains that are its direct customers. And management hopes that it will eventually be able to change production from a make-to-stock approach (the pattern usually imposed by the large distribution chains) to a make-to-order approach.[8]

Innovating in the World of Communication

In 1994, Benetton's interest in new media led it to set up a center for research and development in the field of communication. The center is called Fabrica — Latin for workshop — and is seen as an incubator and catalyst for the cultural inheritance of the company. Headed by an international scientific committee that ensures the validity of the projects, Fabrica has invested in creativity and brought together young people and experimental artists from all over the world. Among Fabrica's successful projects are the film "Blackboards," which won a special award at the Cannes Film Festival in 2000, and the film "Dayereh," which won a Golden Lion at the Venice Film Festival in 2000.

More recently, Benetton has founded the company United Web. United Web's short-term goal is to integrate Benetton's brick-and-mortar businesses with the Internet, to reinforce contacts with customers, and to make the company's products and style known to an increasing number of potential customers. United Web represents not only an additional distribution channel, but also an opportunity to transform the relationships among the players on the network. Benetton's managers are currently working on e-procurement and online services for the distribution network, among other projects.

In addition, the Benetton Group has a Web site, Benetton.com, conceived not simply as a virtual shopping center, but rather as a portal through which Internet navigators can find more varied services, including such tantalizing treats as critics' reviews of the latest recording by the singer Björk, holiday offers in Thailand, opportunities to listen to the latest CDs by Ricky Martin or Britney Spears, and a summary of the spiciest gossip about VIPs in the public eye. Benetton sees the Internet as a medium that is compatible with the company's business philosophy and global image. Entering the e-business world is consistent with the company's communication strategy and with its attempt to provide consumers with a comprehensive experience, a lifestyle.

Thoughts for the Future

For more than a decade, the network has been considered the most flexible organizational model, the one that ensures the highest degree of both differentiation and integration.[9] Network organizations have developed especially in labor-intensive, mature industries, such as textiles and apparel. Even in those industries, however, the acceleration of the industry "clockspeed" (to borrow from Charles H. Fine's 1998 book of the same name) has sharpened competition and changed the power structure across the supply chain. Large retailers shape global production networks and are capable of operating on a global scale, offering high-quality products to sophisticated, multiethnic customers.

In that context, the Benetton case illustrates how a company can design and manage its supply chain innovatively. It seems that in some segments of the supply chain, only exclusive ownership of assets (such as brand equity, knowledge of consumers' behavior, process innovation in fabric and garment design, and technology for logistics) can lead to improved performance. By bringing those assets in-house, fully integrating the production cycle and introducing new e-business tools, Benetton is transforming its organizational model into a New Economy business network. Today, designing the boundaries of innovative business networks requires more attention to ways of dividing up knowledge — not merely tasks — among producers, suppliers and retailers. That can have long-term effects not only on the performance and survival of companies, but also on the future of the industrial bases of whole nations.

Benetton's choices represent a major break with its past, and, to some extent, a significant divergence from industry practice. Benetton's old network model was flexible but had become, because of globalization, increasingly fragile. On the whole, the company's transformation represents a possible trajectory for making other network organizations more robust.[10] Paradoxically, higher external flexibility is made possible by a more rigid organizational structure, tighter control of the supply chain and full exploitation of size effects. Benetton is betting on the idea that advantages from scale economies and quick response capabilities will compensate for risk and investment. Only time will tell us if the company is right.

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2. Our study is based on original fieldwork. We conducted research at Benetton headquarters from March 2000 to September 2000, adopting a quasi-ethnographic approach. We had two research assistants working full-time at Benetton for three months. The research was carried out in three stages. Phase 1 (March 2000 to May 2000): database construction and off-site research and data gathering. Phase 2 (May 2000 to September 2000): direct observation and interviews with managers (approximately 200 hours). Phase 3 (September-December 2000): data analysis and elaboration, case-study writing and discussion with Benetton managers.

3. Other industries that are trying a similar strategy include branded food products and eyewear. Luxottica is a particularly interesting case. Based in northeastern Italy, it is the world leader in eyewear (it recently bought Ray-Ban, LensCrafters, managed-vision-care company First American Health Concepts and Sunglass Hut). It is fully vertically integrated, it produces in-house and in Italy almost all of its product, and its U.S. distribution and sales flow through its own large retail network.

4. V. Ranadivé and S. McNealy, "The Power of Now: How Winning Companies Sense and Respond to Change Using Real-Time Technology" (New York: McGraw Hill, 1999).

5. Flash collections are introduced several times during each retailing season to update the articles offered to customers and to help the company respond better to fast-changing market trends. Benetton expects flash collections eventually to comprise 35% to 40% of its total products.

6. At the moment, the foreign contribution to Benetton's production is limited to 30%, but it is expected to increase.

7. Playlife is Benetton's general-purpose brand for sportswear collections; the Killer Loop brand targets a young, extrovert market.

8. Benetton has come close to the make-to-order ideal with its Blade Express Formula, which makes it unnecessary to produce on the basis of forecasts anymore and avoids the need for warehousing.

9. Two works that discuss that assumption are W.W. Powell, "Neither Market Nor Hierarchy: Network Forms of Organization," in "Research in Organizational Behavior" (New York: JAI Press, 1990), 295-336; and M. Van Alstyne, "The State of Network Organization: A Survey in Three Frameworks," Journal of Organizational Computing and Electronic Commerce 7 (spring and summer 1997): 83-151.

10. For more thoughts on the subject, see V. Perrone, "The Co-Evolution of Contexts and Forms: The N-Form," in "Advances in Organizational Behaviour: A Festschrift To Honor Derek Pugh," ed. P. Clark (Aldershot, United Kingdom: Ashgate, 1998).

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