

Consumer - Asia Pacific

Key takeaways from New Balance footwear sourcing expert call

Industry Overview

Likely need retail px hike to pass through higher cost

We hosted an expert call with Mr. Vik Saran, Director of Materials (Asia), New Balance. According to Vik, the Red Sea disruption has impacted the sportswear supply chain, notably in terms of lead time, manufacturing schedule, inventory planning, booking calendar for shipments, customers' booking and logistics costs. Freight rates have doubled to tripled over the last few weeks. New Balance's initiatives: 1) Although no immediate retail price increase was seen, Vik believes brands eventually may need to increase retail price to pass through the extra cost. 2) New Balance will diversify port entries and shipping routes to mitigate the impact of longer shipping times and higher costs, as well as the port-congestion risks. 3) New Balance is making more prebuilding and prepositioning efforts on safety stocks to mitigate the shipping risks, and so does the raw materials suppliers, instead of the usual made-to-order model.

Sourcing shifting out of China; see floor at 10-15% mix

New Balance's manufacturing scale in China is on a downtrend, according to Vik, primarily due to increasing labor costs and the overall political environment. Vik estimates currently 10-15% of manufacturing takes place in China for most global brands, trending down from 25-30% five years ago and 50% ten years ago. Some brands have entirely moved their manufacturing out of China. On the contrary, Vietnam and Indonesia are gaining shares, with 45-50% and 30-35% now, respectively. Vik believes the current 10-15% ratio should be the floor for China manufacturing even if we take Trump's likely tariff increase into consideration, as major brands are adopting China-to-China manufacturing model to supply the local market.

Weak demand outlook for China, but strong for US and EU

According to Vik, destocking continues, with heavy discounts for leading brands due to softening sell-through for their existing products inventory. At the same time, the brands are restocking with fresh products to boost sell-through without discounts, as well as to mitigate the risk of shipping disruptions. The demand outlook for China market has weakened due to the economic slowdown and the geopolitical tensions, and Vik believes domestic brands would be resilient given strong brand loyalty. Vik does not believe there will be a meaningful improvement for China market in the foreseeable future. In contrast to China softening, the US and EU outlook are strong with positive consumer sentiment.

FOB price could increase; Lead time at 52 days for shoes

In terms of COGS mix, Vik states that 60% is raw materials and 40% is labor/overhead. He believes FOB price could rise as the lower raw material costs could be neutralized by the increase in labour and overhead. He believes the shorter lead time compared to pre-COVID levels would be a new normal. Currently, 52 days is the normal lead time for footwear (from when brands place orders to when factories complete).

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