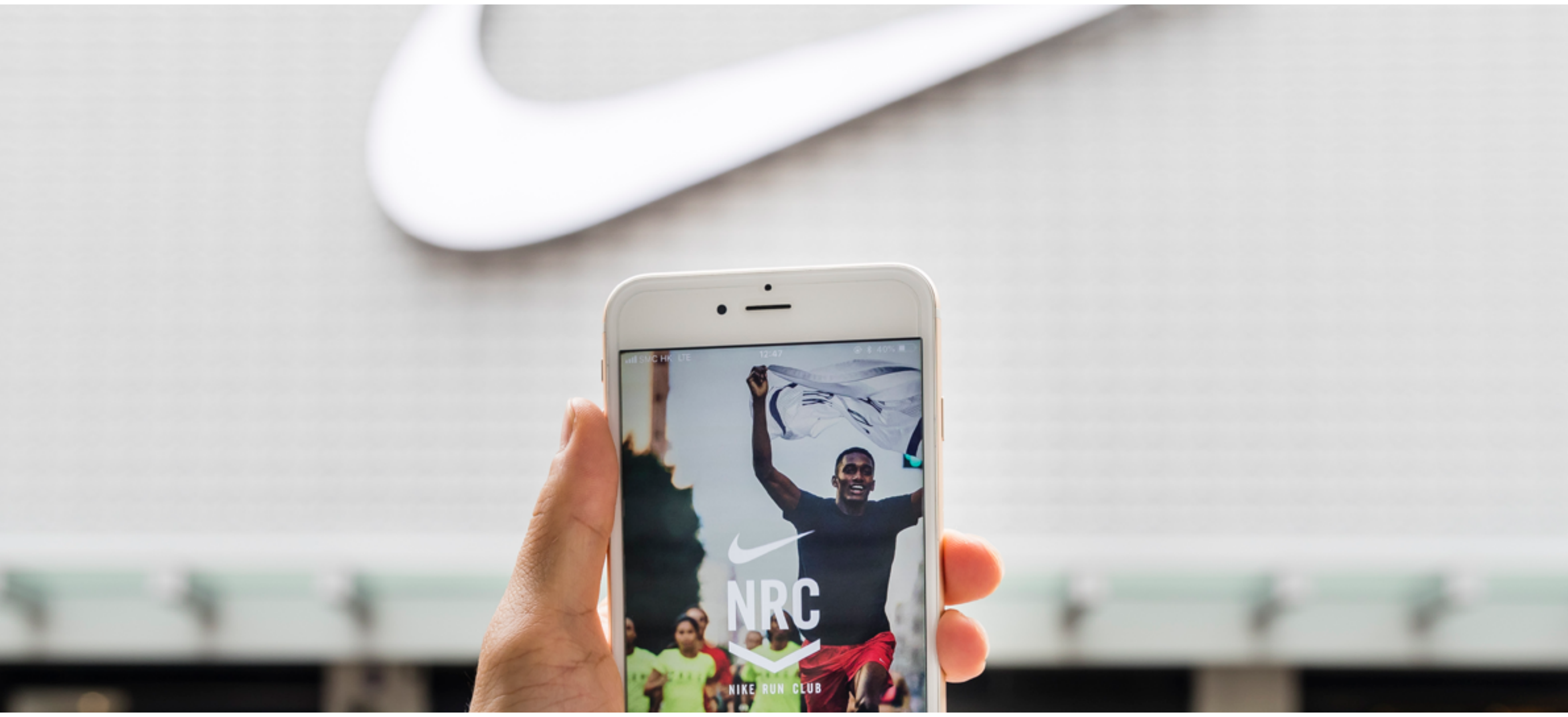
The Business of Fashion

Case Study

# Inside Nike's Radical Direct-to-Consumer Strategy

By Chantal Fernandez

How did Nike's share price hit an all-time high in the middle of a pandemic? The American sportswear giant's success is rooted in a radical direct-to-consumer strategy built around content, community and customisation, and conceived for a post-internet world where brand connections are everything.



# Executive Summary

In October 2020, in the middle of a global pandemic that had infected 188 countries, causing record sales damage across the retail sector, Nike's share price hit an all-time high.

Like other retailers, Nike had been forced to close most of its network of more than 900 stores across the world, as had its key wholesale partners like Nordstrom and Foot Locker.

But the American sportswear giant's performance during the pandemic, when its online sales spiked, signalled to many that Nike had the competency to prosper long term, in a future that will be increasingly defined by e-commerce and digital brand connections.

It was a validation of a strategy that Nike prioritised three years ago, dubbing it "Consumer Direct Offense," but the seeds of the approach go back almost a decade.

Above all, Nike is a marketing company. It doesn't just sell sneakers; it sells the brand aspiration that imbues those sneakers with meaning. But to achieve the reach required to scale its business, Nike's distribution strategy had long-relied on third-party retailers to sell its products, even if the consumer experience offered by those partners diluted its brand.

But in a future increasingly defined by e-commerce, fast-moving trends and, above all, the rising power of branding to drive consumer preference when competitors are just a click away, Nike realised that in order to thrive, it needed to take control of its distribution to better manage its brand and deepen its connection with consumers.

Such an evolution is easier said than done, especially for a business as large as Nike in a category as competitive as sportswear. But by radically cutting back on its wholesale distribution and raising the bar for brand experience with the third-party partners that remained; expanding its focus on content, community and customisation to keep customers close; investing in its data analytics and logistics capabilities; and rethinking the role of the store as a brand stage, Nike drove a veritable direct-to-consumer revolution.

When the pandemic hit, these shifts went into overdrive.

"It was definitely architecting a new retail, and a bold, retail vision for Nike," said Heidi O'Neill, Nike's president of consumer and marketplace, and one of the most prominent executives leading the brand's new strategy in recent years. "But it started with our consumer, and we knew that consumers wanted a more direct relationship with us today."

In this case study, BoF breaks down Nike's pioneering direct-to-consumer strategy and how it has worked to the brand's advantage, propelling its share price to new heights during the global crisis of 2020.

## History and Market Context

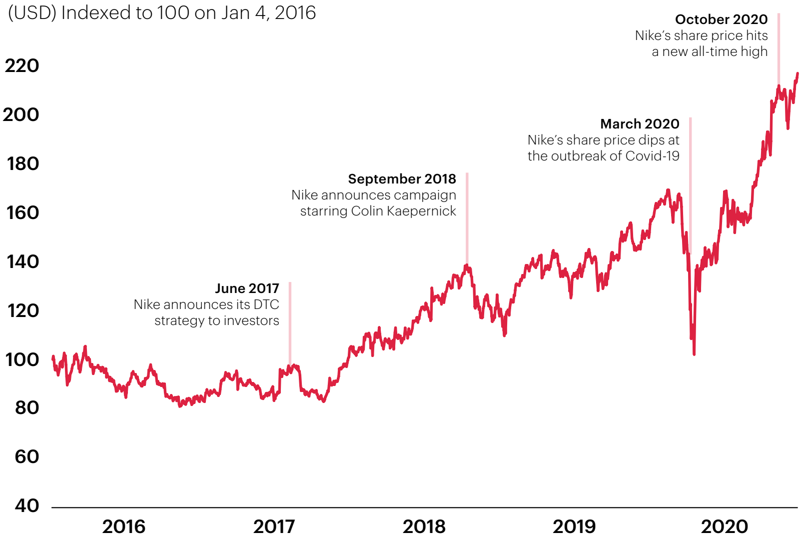
# A Tension Between Brand and Reach


A Sports Authority store, once one of Nike's largest retailers, displaying Nike merchandise. Getty Images.

**Exhibit 1: From Playing Catch-Up to Slam Dunk**

Nike's share price climbed to an all-time high in October as it benefitted from a series of recent strategic decisions, including a focus on direct-to-consumer channels, which boomed during the pandemic.

**Share price, market close**
(USD) Indexed to 100 on Jan 4, 2016




Source: Yahoo Finance

Starting in early 2020, the coronavirus pandemic threw the global fashion market into chaos. Brands grappled with store closures, supply chain disruption and a precipitous downturn in consumer spending.

American sportswear giant Nike was no exception. As the virus spread across the world, the brand was forced to close 75 percent of its stores in China at the beginning of the year and 90 percent of its stores in the rest of the world (except Korea) for about eight weeks in the spring. These closures left the company with 31 percent more inventory than the prior year.

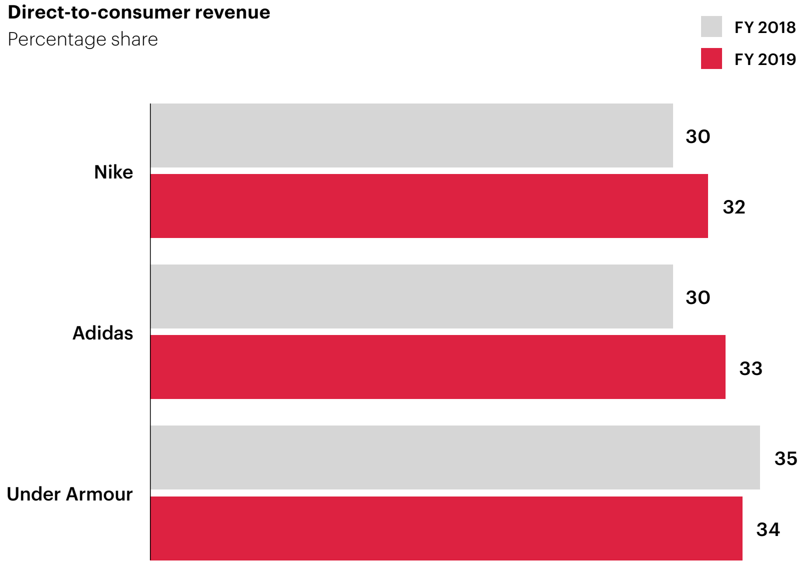
With revenue growth in the first nine months of its fiscal year, which ended May 13, Nike Inc finished the year with a total revenue decline of 4 percent. Meanwhile, the global fashion industry is expected to see a year-on-year revenue contraction of up to 30 percent in 2020, according to *The Business of Fashion* and McKinsey & Company's The State of Fashion 2021.

But five months later, Nike emerged as one of the pandemic's biggest winners when, in October, its share price, up 28 percent year-to-date, hit an all-time high.

### Exhibit 2: Rivals Shift to DTC

Nike's peers are making similar shifts to increase direct-to-consumer sales.

**Direct-to-consumer revenue**
Percentage share

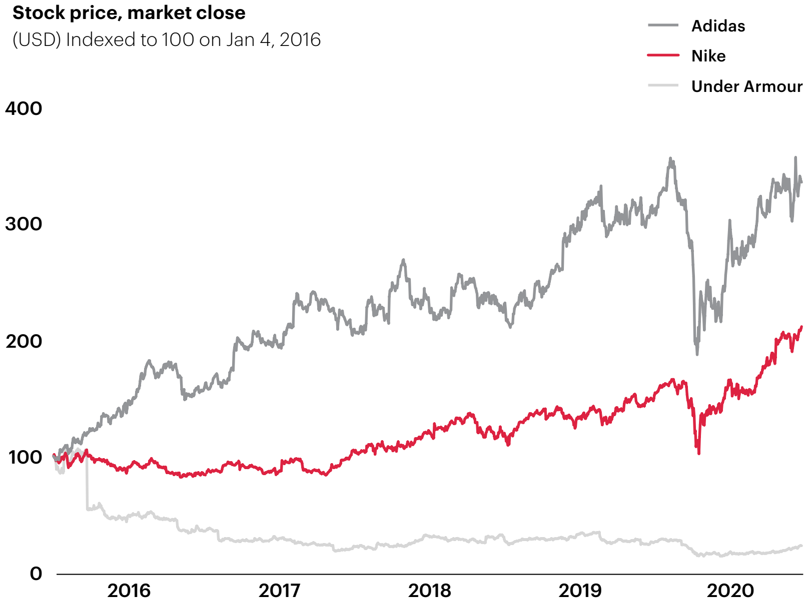



Source: Companies

### Exhibit 3: Under Pressure From Adidas

Nike's share price surge in 2020 comes after more modest growth over the last four years, during which arch-rival Adidas soared.

**Stock price, market close**
(USD) Indexed to 100 on Jan 4, 2016




Source: Yahoo Finance

Just four years ago, Nike's future as the global sportswear leader was uncertain. While the Beaverton, Oregon-based brand still dominated the market with its inspiring and provocative marketing, rooted in unleashing human potential and fronted by a heavy roster of celebrity athletes, it was losing share to fast-growing competitors — especially Adidas.

While Nike kept its marketing focus on carefully controlled collaborations with athletes, its German rival had more forcefully courted cultural influencers, not only forging a lucrative, long-term partnership with Kanye West, but "open-sourcing" its brand to a universe of lesser-known but culturally powerful partners, from musician Pharrell Williams and artist Daniel Arsham to designer Raf Simons and skate brand Palace. It was a winning strategy, as young consumers in particular flocked to sneakers less for their performance features than for their aesthetic and lifestyle attributes. In 2016, Adidas' trendy and casual Stan Smith and Superstar styles became the top-selling sneakers in the US. It became clear that Adidas was seriously threatening Nike on its home turf.

When Nike released its Cortez lifestyle sneaker the following year, with an extensive and expensive marketing push, the release fell flat with consumers. Nike's brand growth rate decreased by 4 percentage points in 2016, and was flat in 2017.

The company needed to rethink its priorities and reassert its brand. Nike is a leader in product innovation, but more than anything, the company trades on the power of its brand marketing. "They're such good storytellers and they know how to engage people better than anybody else," said Sam Poser, analyst at Susquehanna International Group. And yet, in search of scale, Nike had long-relied on a large network of third-party retailers to sell its products, even if the consumer experience offered by those partners diluted its brand.

In 1964, Phil Knight founded the company that would later become Nike as a distributor of Japanese running shoes, which were, at the time, considered the best in the world. When the brand started designing its own shoes, it needed sporting goods shops and department stores to reach customers. Less than a decade later, Knight enticed the company's biggest retailers to place larger and non-refundable product orders, which came with a discount, in a strategy he called "Futures." This approach soon represented the bulk of Nike's wholesale revenue. By the time the company went public in 1980, it sold its shoes through 8,000 retailers.

Nike's Mark Parker presenting the consumer-led transformation to investors in October 2017. Nike.

*"Everything the organisation did moving forward would now be in service of a more efficient, direct-to-consumer business."*

But nearly three decades later, the wholesale market was facing an existential challenge. More shoppers did more of their shopping online, where they could browse any number of sites and no longer relied on retailers to curate products for them. Multi-brand stores leaned more and more on discounts to keep shoppers coming back.

Nike had long been able to cast a powerful brand halo over its products, even when consumers found them at third-party retailers. But over time, not even the most inspirational multi-million-dollar marketing campaign could offset the way wholesale was increasingly diluting its brand identity — and disintermediating its consumer relationships.

And even if Nike could have simply dialed up its already enormous marketing budgets, it was inefficient, especially now that the internet allowed Nike to scale distribution through its own channels in a way that would actually strengthen — and not damage — brand equity.

Moreover, as the internet put competitors a click away, removing friction from the purchasing path and making brand identity an even more powerful driver of consumer preference, Nike needed to have more agency over its relationships with shoppers.

Digital was also changing customer expectations. "They expected us to know them across our ecosystem, from app to app, from physical to digital," O'Neill told *The Business of Fashion.*

Nike was far from the only brand to realise the urgent priority to take control of its distribution channel as part of a digital transformation across the company. But with more than $32 billion in annual sales in fiscal 2017, such a fundamental shift was not going to be a simple proposition.

Though it had been laying the groundwork for a transformation for much of the past decade, Nike first presented its ambitious plan to investors in June 2017 in a strategy it dubbed "Consumer Direct Offense," which the company described as fuelled by a "Triple Double" consisting of "2X Innovation, 2X Speed and 2X Direct connections with consumers."

As part of the strategy, the company aimed to double the amount of sales through direct channels — online and off — while prioritising just 40 of its 30,000 wholesale partner relationships; cutting production timelines in half; and generating more of its sales from its more differentiated product lines, such as its "React" and "Vapormax" models.

Everything the organisation did moving forward would now be in service of a more efficient, direct-to-consumer business centred on building closer, more powerful brand connections with customers, from new store concepts to mobile apps and technology investments.

## The Challenge

# Changing Channels Amid Crises

While direct-to-consumer sales were the fastest-growing part of Nike's business in fiscal 2017, they only represented 28 percent of revenues. Competitors were making similar investments in their digital channels, while working strategically to steal market share.

How would such a giant and multi-channel brand as Nike take back control of its distribution and invest in brand connections, without shrinking or losing the support of shareholders?

"The non-digital natives of us out there are looking to see how we can thrive and be connected to consumers in a digital-first world," said O'Neill at Recode's Code Commerce event in September 2017, framing the problem Nike faced as a brand born pre-internet seeking to still dominate in a digital age.

*"Competitors were... working strategically to steal market share."*

The strategy required a significant internal reorganisation, which has led to a series of substantial staff cuts, as well as a cultural shift that came during a time of corporate crises at Nike. While these issues had minimal impact on brand perception with consumers, they caused significant internal turmoil at a time when the company couldn't afford the distraction.

In 2018, while the company was in the middle of a multi-year effort to grow its women's business, female leaders at the company started what the *The New York Times* described as a "small revolt," and more than six top male executives shortly resigned from the company, including Nike brand president Trevor Edwards, long eyed to succeed chief executive Mark Parker. The following year, the United States Anti-Doping Agency banned Nike running coach Alberto Salazar for allegedly violating rules.

"The decision had nothing to do with administering banned substances to any Oregon Project athlete," said a representative for Nike. "We support Alberto in his decision to appeal and wish him the full measure of due process that the rules require."

A few weeks later, Parker announced that he would step down as CEO in early 2020 in a long-planned transition, to be replaced by board member John Donahoe, the former top executive at eBay and the chairman of PayPal. Donahoe's selection underscored Nike's growing focus on a digital, customer-first future — one that has also come with continued internal reorganisation and leadership changes, such as the exit of the chief operating officer and the president of consumer and marketplace. Donahoe also announced a shift to organise the business around the women's, men's and children's categories, a simplification of the previous structure organised around different sports activities.

Meanwhile, outside Nike, America's "culture wars" were raging and a new generation of consumers, more polarised than ever, were turning to brands to take a stand on values with which they identified. As Nike sought to expand its footprint in athleisure, lifestyle shoes and apparel, it increasingly addressed more than sporting excellence in its marketing.

While the brand had made politically charged statements before, its 2018 campaign with American football player Colin Kaepernick, known for his Black Lives Matter activism, was a watershed, sparking controversy that was ultimately positive for brand appeal.

Nike's world headquarters campus in Beaverton, Oregon. Nike.

The Strategy

# ‘Consumer Direct Offense’

## 01 — Radical Recalibration in Wholesale

**By only focusing on 40 wholesale partners who offer a differentiated retail presence, Nike can avoid brand dilution and drive stronger connections with consumers.**

A Nordstrom x Nike sneaker boutique. Nordstrom.

When one of Nike’s largest retailers, the American multi-brand sporting goods chain Sports Authority, filed for bankruptcy in 2016, the store owed the brand a whopping $47.9 million. It was one of the first retail victims of the end of the big box era, and was ultimately forced to completely shut down. One New Jersey seller resold $200,000 worth of Nike merchandise he picked up in the liquidation, and grossed about $1 million, according to *The Wall Street Journal*. This was exactly the kind of situation Nike wanted to move to avoid as the wholesale market unraveled.

At Nike’s 2017 investor day presentation, then chief executive Mark Parker made headlines when he announced that, moving forward, the brand would prioritise only 40 of its 30,000 retail partners with marketing initiatives and special products. It marked the beginning of a culling of wholesale customers, in which the brand cut and minimised its relationship with any retailer that didn’t make extra efforts to make Nike’s brand more appealing to shoppers, a phased strategy that continues today.

Nordstrom, Foot Locker and Zalando were some of the first partners to be chosen for their special, deeper relationships, with each retailer offering Nike a specific strategic advantage — and making a commitment to present Nike in a “differentiated” way compared to competitors.

“Nike, or any other brand for that matter, should be looking at their partners and saying, ‘you know what, I can sell my stuff anywhere,’” said Poser. “So what’s in it for me as a brand, and what’s in it for them?”

Some retailers, like boutique sneaker store Concepts, gave Nike clout and authenticity in the sneaker space. Others, like Foot Locker, allowed Nike to reach a sneaker enthusiast who wants to choose from a wider selection of brands and products, or a younger customer who has not yet developed the kind of loyal relationship with Nike that could continue throughout their life. Nordstrom provided a leg up in the underpenetrated women’s market.

At Foot Locker, what Parker and other Nike executives referred to as “differentiated retail” came to life with special pop-up stores and specially trained sales associates. Then, in 2019, Foot Locker even went so far as to allow shoppers to check out in stores with the Nike mobile app, further integrating the third-party retailer into the Nike world.

> *“Some retailers... gave Nike clout and authenticity in the sneaker space. Others... allowed Nike to reach a sneaker enthusiast who wants to choose from a wider selection of brands and products.”*

That same year, Nike raised the minimum annual amount of products its retailers needed to commit to sell to keep working with the brand, according to reporting from *The Times*. It continued to cut out retailers, many of them small and independent, that did not make special accommodations for Nike.

At the other end of the scale spectrum, Nike even cut off its relationship with e-commerce juggernaut Amazon after a highly publicised test period. In 2017, after years of eschewing the "Everything Store" Nike has begun to expand its presence on Amazon with a small assortment of products. Despite Nike's official absence on the marketplace, unauthorised (and in some cases counterfeit) products made Nike the most purchased brand on the site, according to a Morgan Stanley survey in 2017, which showed Amazon offered 73,000 Nike items at the time. Competitors Adidas and Under Armour had already been selling on the marketplace as official partners for years.

Amazon reportedly promised to cut down on the sale of unauthorised Nike products. But even after the company developed an official relationship with Amazon, these unauthorised sales continued and Nike pulled out two years later, citing its focus on "direct, personal relationships." The experiment was a failure, and the pressure was on for Nike to work harder to lure more fans of the brand through its own sales channels.

"As part of Nike's focus on elevating consumers' experiences through more direct, personal relationships, we have made the decision to complete our current pilot with Amazon Retail," said a representative for Nike.

Meanwhile, Nike continued to edit its wholesale network. In 2020, Nike cut relationships with multi-brand retailers including Belk, Dillard's, Zappos, Boscov's, Bob's Stores, Fred Meyer, EbLens, VIM and City Blue, according to a report from Susquehanna's Poser. It even cut its relationship with small family businesses like Frank's Sport Shop in the Bronx, New York, which had carried Nike products for more than 50 years.

"We continually evaluate our distribution approach based on our strategy," said a representative for Nike. "As part of this evaluation, from time to time, Nike chooses to conclude distribution with certain retailers."

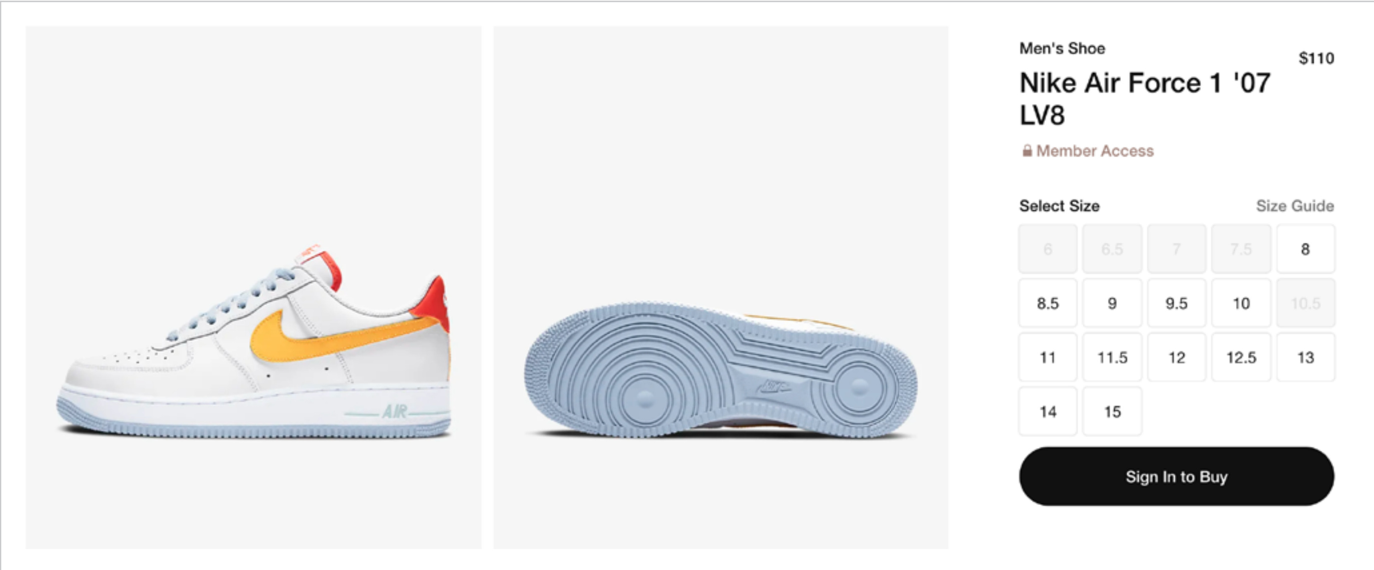
Meanwhile, the company expanded its business in recent years with the "digital high street," including European apparel e-tailer Zalando, and Alibaba's Tmall.

"We'll continue on our path to differentiated retail — to fewer, better partners, who work with us in a more connected experience," said O'Neill, "so that the consumer can be recognised as a Nike member, throughout all of their shopping journeys."


Nike merchandise on display at a Foot Locker store. Getty Images.

## 02 — Pivot to Direct E-Commerce

**As Nike cuts back on wholesale, its investments in direct e-commerce allow the company to drive reach in a way that does not dilute, but instead boosts its brand.**




Nike Air Force 1s on their direct e-commerce channel. Nike.com.

Meanwhile, Nike invested in technology and distribution upgrades to support growth in its direct e-commerce business.

In 2018, Nike acquired American customer data analytics company Zodiac, which uses predictive tools to forecast the lifetime value of a customer and increase revenue with personalised marketing and recommendations. The following year, it also acquired retail predictive analytics and demand-sensing firm Celect, which helps predict consumer demand.

*"Nike invested in technology and distribution upgrades to support growth in its direct e-commerce business."*

Nike's tech investments escalated in fiscal 2019, when it invested over $1 billion in new data and analytics capabilities, expanding Nike's suite of apps and digital-friendly store features.

Nike also opened new distribution centres to deal with the increased volume of product it was shipping directly to consumers. In fiscal 2018, it expanded seven of its distribution centres, including one in the US specifically dedicated to processing returns. Ahead of the 2020 holiday season, Nike also opened a new warehouse near Los Angeles to deal with additional e-commerce demand, which uses more than 600 robots to pick global products.

Nike plans to generate 50 percent of sales from online channels, including retail partners, but hasn't yet indicated how much of its total business it aims to generate from its own channels. Poser, who estimated that Nike will seek to generate 30 percent of the online segment via its own channels, said it was unlikely the company would ever abandon key wholesale battlegrounds. "That's how they gain share," he said. "If they're not hammering their competition there, they know they're not going to sell a lot online anyway."

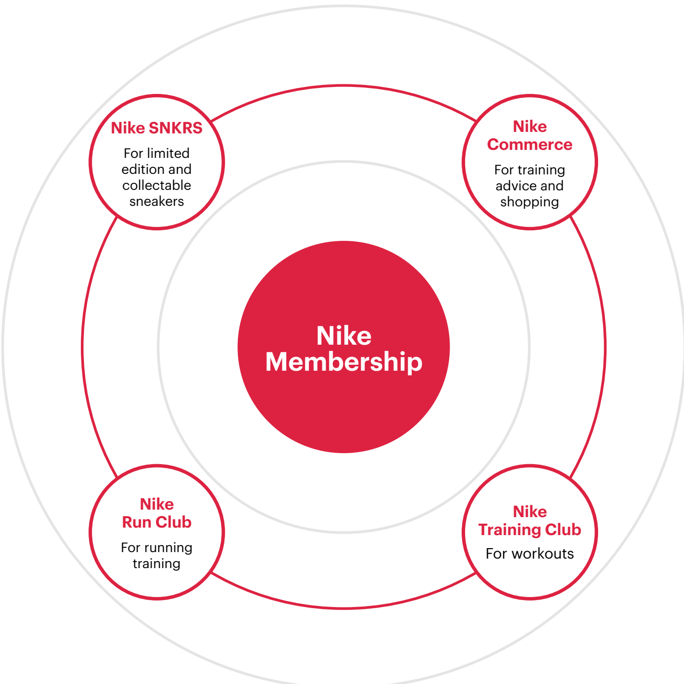
## 03 — Content, Community, Customisation to Drive Brand Connection

**With a universe of digital content, community and customisation experiences, Nike keeps its customers close, creates powerful organic marketing that boosts engagement and customer lifetime value, and gleans data that can inform future products and experiences.**

A customisation station at Nike's House of Innovation in New York (left). Members of the Nike Training Club community (right). Nike.

**Exhibit 4: A Universe of Apps to Keep Consumers Close**

Nike has developed a suite of apps that keep customers engaged with content and community features, while gathering consumer data to inform its strategy.




To support its pivot to direct channels, Nike sought to track and engage with consumers more closely than it ever could when its partners controlled the relationship with shoppers at point of sale.

Throughout the 2010s, Nike reallocated advertising dollars to digital. Though the brand had never been short on social-media friendly content, digital media allowed the company to go beyond traditional "push" messaging and forge tighter customer relationships, improve targeting and, ultimately, create a community it could analyse to inform its overall strategy.

Nike's constellation of mobile apps were key to this element of the strategy, as was its membership programme, which, like an AppleID or Amazon Prime account, tracked customer behaviour and allowed the brand to see how its customers interact with its products, stores and content.

Nike's apps have evolved and served different functions since they first launched a decade ago. Nike set up a "Digital Sport" division in 2010 dedicated to creating wearable tech products and the software that would support them. The Nike+ FuelBand launched in 2012, and tracked a user's activities, steps and other fitness related goals and synced them with the apps and a users' Nike account.

**Exhibit 5: Bridging the Tech Gap**

Over the last four years, Nike has acquired technology start-ups with expertise in various fields, from content creation to data analysis.

**August 2016**
**Virgin Mega**
An American digital design studio that develops mobile technology

**March 2018**
**Zodiac**
An American customer data analytics company

**April 2018**
**Invertex**
An Israeli 3D technology firm that scans and measures shoe sizes

**August 2019**
**Celect**
An AI retail predictive analytics and demand-sensing firm

**October 2019**
**Trace Me**
An American content app start-up for "superfans"

Despite initial interest in the product and its updates, Nike felt it couldn't compete with the likes of Apple and Google in technology hardware and discontinued most of its wearables in 2014, favouring a strategy rooted in integrating with products like the iPhone and, later, the Apple Watch.

The software, however, remained, and would continue to gain importance within the company, as Nike recognised that more of its customers were spending more time online and specifically on their phones.

Nike's membership programme actually predated the iPhone era, launching in 2006 in a collaboration with the Apple iPod that tracked running workouts through a small transmitter embedded in Nike shoes. Three years later, Nike introduced its first ever iPhone app, dedicated to providing training workouts for women, and was followed up shortly with the first running app, which tracked the user's steps through GPS instead of wearable tech.

Over the next five years, before Nike cut the wearable tech category, the brand rolled out a series of different software for different devices, designed to sync with different workout machines and regimes. The apps gained their own followings, offering workouts from Nike trainers as well as running tips and tracking. But the apps were fragmented in their approach.

"Nike had some really strong consumer apps and stores, but we didn't build out a connected consumer experience," said O'Neill, describing much of her work around "breaking down the walls" between retail, digital product and engineering teams. "We weren't offering members personalised journeys through those experiences."

Then, in 2016, Nike began to connect the dots, re-releasing most of its apps to reinforce the underlying membership, with the Nike commerce app (for training advice and to showcase and shop products), the Nike Training Club (with more workouts for men and women) and the Nike Run Club. Membership grew from around over 100 million at the end of 2017 to 185 million by the end of 2019.

The apps also play an increasingly central role in Nike's retail strategy. With Run Club and Training Club focused on fitness tools and instruction, the Nike commerce app became a tool for enhancing Nike's physical retail strategy, which has expanded with new retail concepts since 2018. After surveying more than 500 consumers, the brand rolled out new features on the app that allowed customers to scan products in a store to summon the item from salespeople, as well as check stock information. Shoppers could also reserve products before entering a store, get access to special discounts and pay for their in-store purchase in the app.

Nike's SNKRS app is another key consumer relationship builder, one that has grown into a $1 billion annual revenue channel. Originally developed in 2015 and then later expanded to focus on selling its limited edition and most collectable sneakers, Nike opened the app to 22 new countries in 2017, in addition to the US, as the app's popularity skyrocketed. It grew from generating $70 million in revenue in fiscal 2016 to over $750 million in fiscal 2019.

> *"Someone may only buy footwear and apparel a few times a year, but engaging with us each week [through the Nike Training App]... brings Nike into their lives."*
>
> — John Donahoe

Nike poured investment into the app, making it more resilient against bots that tried to game the release process to profit on the resale market, and introducing different features to "gamify" the sneakerhead shopping experience.

Four years ago, Nike bought Virgin Mega, a start-up branded with Richard Branson's Virgin that developed technology to incorporate games into mobile shopping, and quickly integrated it into SNKRS. Sneakerheads could "queue" for products digitally as part of Nike's efforts to cut off shopping bots that snap up in-demand limited edition sneakers, such as collaborations with Virgil Abloh or Travis Scott, in large quantities to resell for high markups.

SNKRS had offline potential, too. In 2017, for example, the release of limited edition PSNY x Air Jordan 12s shoes drew shoppers to Washington Square Park on a summer's afternoon, in a kind of scavenger hunt for the geo-tagged location where they would be able to unlock the option to purchase the shoes.

These investments have paid off. The SNKRS app has "acquired more new members than any other digital channel for Nike," Parker told investors in 2019.

When the pandemic hit in 2020, all of Nike's apps suddenly took on more importance as shoppers were stuck at home and looking for streamable workouts. Many returned to the apps frequently, making them increasingly valuable organic marketing channels.

"Someone may only buy footwear and apparel a few times a year, but engaging with us each week [through the Nike Training App], maybe even each day, brings Nike into their lives," Donahoe told analysts in June.

In March, Nike had made its Training Club app, previously $14.99 a month for full access, free to all users, which resulted in a surge in memberships. It became clear that Nike's apps had become one of its most effective customer acquisition tools. Nike expanded the number of workouts available on the training app, totalling more than 150, including yoga and stretching.

The strategy was especially important in China (where the app is integrated with WeChat ID and users can pay with Alipay and WeChat) and 13 markets in EMEA, where Nike's app had only launched in November.

Since the pandemic began, Nike's apps have streamed over 375 million workouts, helping increase Nike's membership by 50 million over the same period. The more members Nike amasses, the more data it collects on its customers and their preferences and habits. The more data it collects, the better the brand can design and deploy its products to shoppers.

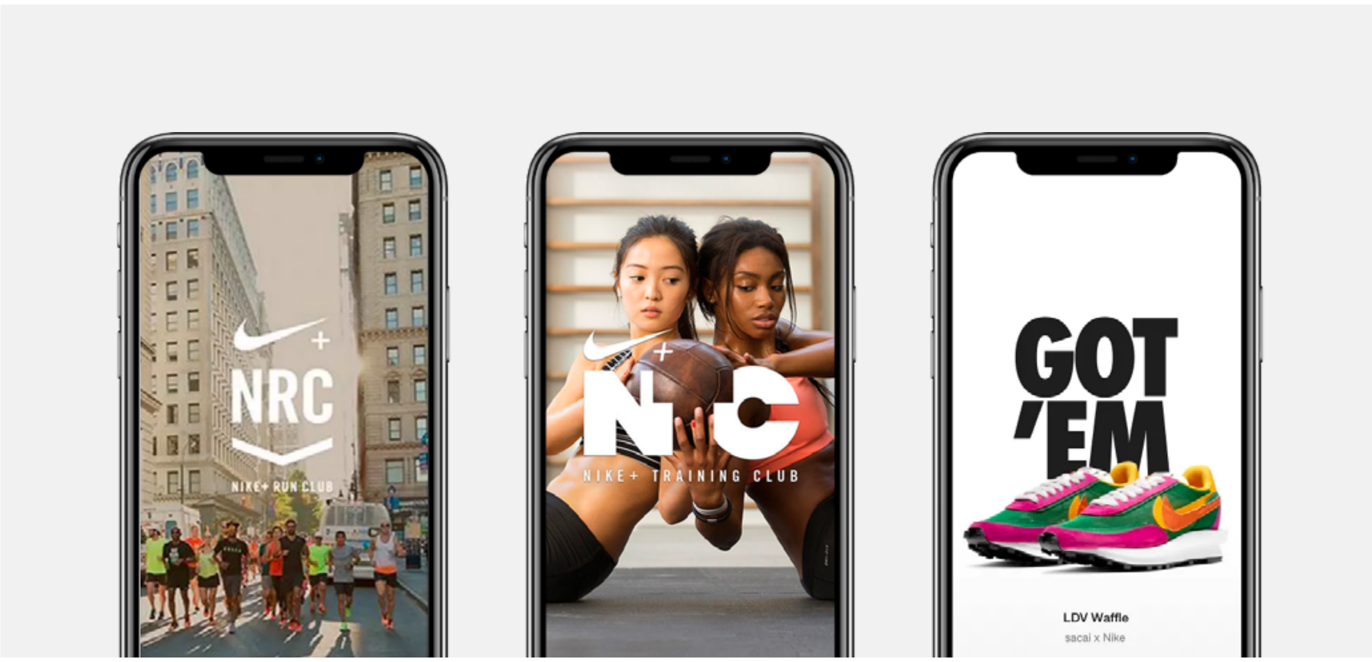
"Behaviour on the app is as important as what they tell us," said O'Neill at the 2017 Code Commerce event.

In an interview with BoF, O'Neill cited people who run at night as an example. "With digital, we can serve underserved segments [where] there just might not have been that distribution channel," she said. The brand recognised night runners among its members through the app and is designing more apparel with reflective fabrics.

In recent years, Nike has also invested in product customisation experiences, which also tie consumers closer to the brand. In 2018, Nike acquired Invertex, an Israeli firm that uses 3D technology to, among other functions, scan and measure feet for shoe sizes. A year after that acquisition, the brand introduced the same scanning technology in its Nike app for footwear shoppers. It also later brought the scanning technology to its stores, where shoppers could be virtually measured for sports bras.

And in April 2019, Nike relaunched its shoe customisation project, formerly known as NikeID and renamed Nike by You, with more design options and collaborations with designers like Heron Preston. The brand has continued to draw attention to the customisation feature with other micro-collaborations with athletes and influencers.

In order to support customisation with faster speed-to-market, Nike has built "express lanes" of products in recent years, by storing materials at factories. The strategy cut down production from months to weeks on some products, and grew to represent 10 percent of all revenue in the third quarter of 2019, with a focus on custom shoe designs as well as limited-edition collections.




Nike Run Club, Nike Training Club and Nike SNKRS. Nike.

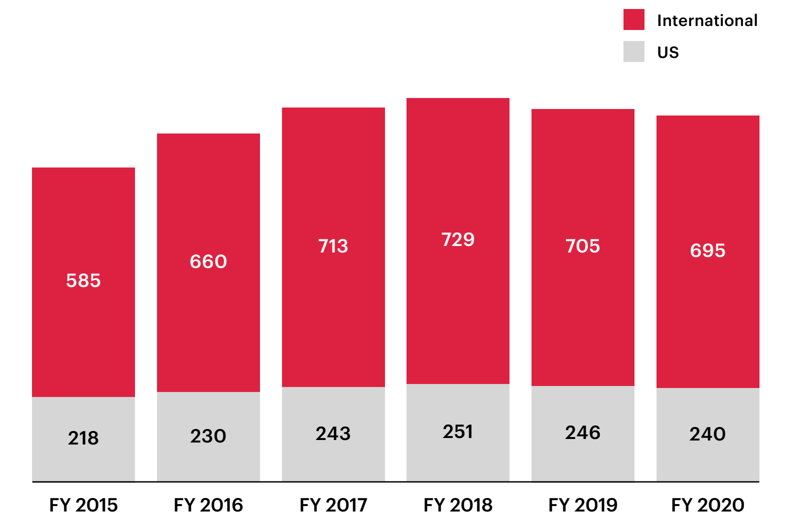
## 04 – Stores as Brand Theatre

**Nike's stores are becoming stages for brand experience where the company can deepen connections with consumers, remind shoppers how its products are different and underscore why its logo has cultural meaning, regardless of where they ultimately make their purchase.**


The digitally-enabled "Center Court" at Nike's House of Innovation in Shanghai. Nike.

**Exhibit 6: Rethinking the Physical Store Network**

Nike did not rely on opening more stores to grow direct sales. Instead, the company trimmed back its retail network but invested in experiential flagships.




Source: Nike

Building brand connections wasn't just about digital activations. A new approach to physical retail was a critical part of Nike's strategy.

When O'Neill was named president of Nike's new direct-to-consumer division in 2016, one of the top priorities was rethinking the ways that Nike's different segments worked together. The following year, as part of a reorganisation that saw the brand cut 2 percent of its workforce, Nike's digital product team merged with its retail commercial one, meaning O'Neill began working much more closely with Adam Sussman, then chief digital officer, breaking down walls between their groups.

"I see the role of the store as an extension of the mobile experience," O'Neill said in an interview with Fortune in 2019.

That strategy came to life in a series of new retail "House of Innovation" flagships that first opened in Shanghai in October 2018. The multi-level store was a kind of theme park for the Nike brand, and the kind of place where shoppers could come and spend the day, participating in different workshops and events or customising shoes and shopping with personal stylists.

Many elements of these new large-format store concepts were digitally enabled and designed to be supported by the app, which shoppers could use to scan and pay for products and participate in special events or offerings. The brand also set up members-only floors, where sales associates offer personal styling and fitness advice.

The brand followed the Shanghai opening with similar new locations in New York and Paris. The format was a model for the future, and the brand saw that shoppers who visited the locations spent 30 percent more than the average Nike customer with the brand over the following months.

Meanwhile, the brand developed another large-format store design it called "Nike Rise," which opened in Guangzhou, China in July 2020 with a focus on running, basketball and football.

*"It's about making the experience, physically or digitally, [a] richer, more dimensionalised experience for consumers."*

— Mark Parker

Nike is also investing in a network of smaller-format stores designed to cater to a specific area. "Nike Live" first opened in Melrose, Los Angles in 2019 and tapped users' data to inform the kind of inventory stocked in the store which, in the Melrose location, meant more running gear and brighter colours and patterns. And "Nike Unite," another locally targeted small-store format focused on sports and community, has rolled out in five locations in the US, UK and Korea, with plans for additional locations in the US and China.

To support these investments, Nike acquired Boston-based artificial intelligence firm Celect in 2019. The company predicts browsing and buying patterns both online and in stores, in real time, and helps brands plan what products they need to have available in stores or distribution centres at any given time.

"Ultimately, it's about making the experience, physically or digitally, [a] richer, more dimensionalised experience for consumers," Parker told investors in June 2019, explaining that the brand was experimenting and testing different formats. "We are seeing where we have those digital connections through like Nike app at retail, we're seeing the engagement from consumers rise significantly. And the actual spend per consumer in those cases actually jumps up dramatically."

Of course, the coronavirus pandemic has hampered Nike's brick-and-mortar retail strategy, as the brand was forced to close most stores globally for an average of eight weeks. But it also puts more focus on the types of stores it continues to invest in for the future. Covid-19 has raised the bar on store formats: because of safety concerns, shoppers need more compelling reasons to enter physical retail.

"The way the consumer shops is changing," said Poser. "And if they're going to go to a retail store when the dust settles with all this, you better have a really good story to tell."

**Exhibit 7: Nike's Formula for its 'Consumer Direct Offense'**

The company's multi-pronged DTC strategy goes beyond its sales channels.

| Nike's Approach | How It Works |
|---|---|
| Recalibrate Wholesale | Discontinue retailer relationships that don't make extra efforts to make Nike's brand more appealing to shoppers, and invest in those that do. |
| Pivot to E-Commerce | Expand direct e-commerce by developing data and analytics capabilities and mobile apps to drive reach. |
| Content, Community, Customisation | Nurture a community of consumers through unique experiences and content that attracts new fans and builds loyalty. |
| Stores as Brand Theatre | Upgrade the store as a branding exercise or hyper-localised boutique to deepen customer connections. |

## The Results

# DTC Scorecard

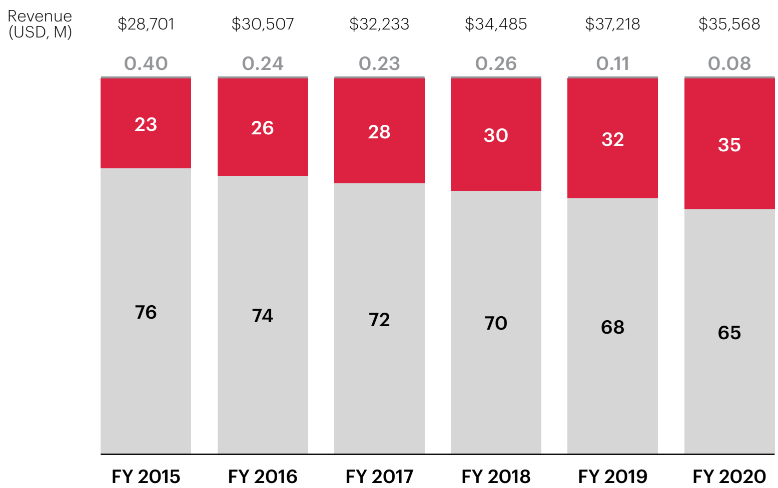

Nike's "Mission Control" wall in its House of Innovation in Paris. Nike.

### Exhibit 8: Direct Sales Double

The company's direct-to-consumer revenue has nearly doubled in five years.

**Nike revenue by category (2015-2020)**
Percent

Global Brand Divisions
DTC
Wholesale




| Revenue (USD, M) | | | | | | |
|---|---|---|---|---|---|---|
| Global Brand Divisions | 115 | 73 | 73 | 88 | 42 | 30 |
| DTC | 6,634 | 7,857 | 9,082 | 10,428 | 11,753 | 12,382 |
| Wholesale | 21,952 | 22,577 | 23,078 | 23,969 | 25,423 | 23,156 |

Source: Nike

As Nike cut back on wholesale and invested in its own distribution channels and brand experiences over the last five years, direct sales have grown consistently, representing 35 percent of sales in fiscal 2020, up from 23 percent in 2015. Then came the coronavirus pandemic, which proved Nike's investments had come just at the right time.

*"Sales through the Nike app grew by 'triple digits' and generated 30 percent of North America online sales."*

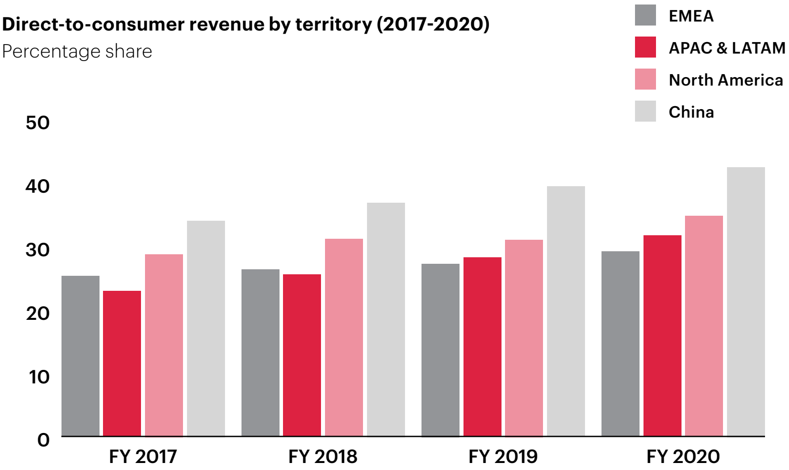
Twenty-five million people signed up for the Nike membership in the fourth quarter ending May 31, 2020, up over 100 percent year-over-year, half driven by Nike's running and training apps, which saw active new member growth exceed 200 percent in the quarter. During the same period, the Nike app was downloaded more than eight million times, three times more downloads than the previous year. And in the year ending May 31, the SNKRS app generated $1 billion in revenue for the first time.

Nike brand's e-commerce sales grew by 79 percent, with digital sales representing 30 percent of total revenue in the quarter, up 80 percent year-over-year. Direct-to-consumer brand sales grew 5 percent

### Exhibit 9: DTC Grows Globally

The DTC strategy has paid off in all markets, with Asia Pacific and Latin America seeing the highest growth.

**Direct-to-consumer revenue by territory (2017-2020)**
Percentage share

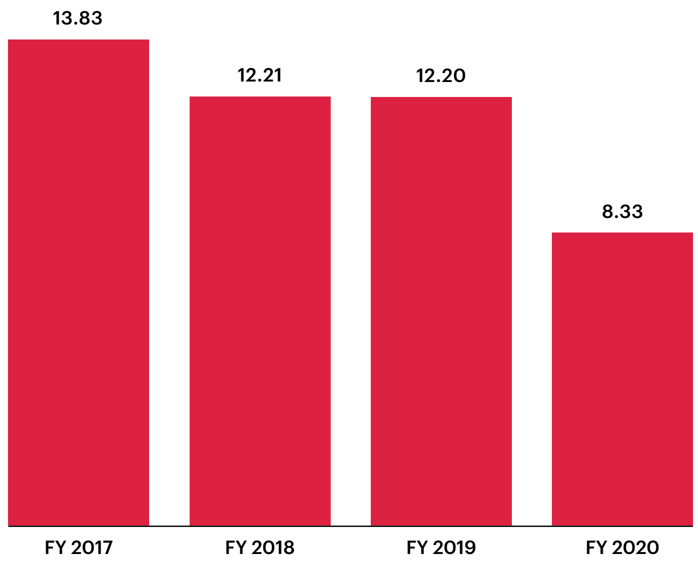



Source: Nike

### Exhibit 10: Squeezed Margins

Nike's investments have resulted in a drop in profitability.

**Nike Inc operating margin (2017-2020)**
Percent




Source: Yahoo Finance

while wholesale revenue dropped by 9 percent year-over-year. Sales through the Nike app grew by "triple digits" and generated 30 percent of North America online sales.

To be sure, the pandemic was an exceptionally difficult time for the company, which forced it to close stores across the world and disrupted some of its key investments, especially its marketing plans around the Tokyo Olympics. Nike Inc. saw sales decrease 38 percent in the quarter ending May 31, 2020, and inventory increase 31 percent in the same period. Meanwhile, Nike Inc.'s operating margin suffered, decreasing to 8.3 percent in fiscal 2020 from 12.2 percent the prior year.

In June, Donahoe announced that Nike would enter a new phase in its transformation strategy, with the goal of generating half of all sales through e-commerce (both Nike and select partners), and would increase its investments in technology including "demand sensing, insight gathering [and] inventory management."

He said the brand would focus more energy on its membership programme, reaching nearly 250 million members as of September 2020, and also open more small-scale Nike stores to target specific communities, like women.

Donahoe also announced an internal reorganisation that would shift from a focus on activity groups, like basketball and running, to a focus on consumer groups, with new departments around men, women and children. These changes will reportedly result in about 700 job cuts at Nike's Oregon headquarters.

"We believe this digital acceleration is more indicative of a strategic shift towards a new future marketplace, rather than being a reflection of temporary challenges to the mostly physical marketplace of the past," Donahoe told analysts in June.

# Looking Ahead

"We have so far [that] we could go, we're [just] scratching the surface, but we've come a long way in terms of breaking down the walls and siloes in our teams," said O'Neill, acknowledging the work that still lies ahead for Nike. "The first and most important pillar of our marketplace strategy is to continue to invest in both our tech infrastructure and our digital ecosystem."

Amid the pandemic, the brand signed on millions of new members, who started to engage with the brand's new digital ecosystem for the first time. The pressure is now on the brand to bring those relationships down the purchasing funnel and turn them into commercial transactions. As shoppers continue to stay home, the apps will continue to play an outsized role in how shoppers meet and engage with Nike, but it's also a market in which the brand faces new types of competition from other fitness content providers, from giants with cult followings of their own, like Peloton, to influencer trainers with popular YouTube followings.

"How are we going to inspire [customers]?" asked O'Neill. "How are we going to encourage them to train and how are we going to hear them out? So that's got to be a big focus for us."

O'Neill highlighted Nike's renewed focus on better targeting the women's category and apparel, as part of the athleisure movement, which Donahoe pegged as the company's strategic priorities over the summer. The more Nike understands about consumers who are interested in those categories, through the data it collects about where, how and why they shop, the better it can convert them into shoppers.

"We talk a lot about knowing to serve from a digital perspective," said O'Neill. "But thinking about bringing that insight all the way up to innovation and product creation and what we can do there — our product teams are just psyched for the potential for better serving consumers from a data perspective."

Nike is in the process of renovating two of its New York City stores into new "Nike Live" stores focused on women and apparel. It's part of an expansion of the small-store format that will see 10 to 15 new openings this fiscal year, and an additional 150 to 200 openings in the next several years. Here, a challenge for Nike will be nailing its retail mix during a time when shoppers are being more cautious about stepping into physical stores, behaviour that will likely linger in some form after pandemic-related health concerns have passed.

Another challenge lies in Nike's supply chain. When Nike announced its DTC strategy in 2017, "2X Speed," or investments in "new capabilities and analytics to deliver personalised products in real time," as Parker explained to investors that October, were key to the strategy.

Two years earlier, Nike inked an ambitious partnership with Silicon Valley manufacturing company Flex to "nearshore" production of footwear closer to its largest market, the US, in Mexico. The goal was to accelerate deliveries through automation to allow the brand to be more responsive to product demand.

It marked a new era for the brand, which for decades worked with the same group of footwear suppliers across China, including large-scale factories like Fengtai in Yunlin, Taiwan that dedicated all of their output to the market leader's products.

The priority was keeping costs as low as possible, though long lead-times were more of a liability for the brand. For decades, Nike mitigated the risk of betting on the wrong product by sharing some of that risk with wholesale partners, who placed orders for products six months in advance through its "futures" model.

But in a future where direct-to-consumer would represent most of Nike's sales, the brand would need to build more flexibility and speed into its supply chain to more efficiently adapt to consumer trends and preferences, which were evolving at a faster and faster rate.

Yet only a few months after the 2017 investor presentation, Nike shut down the project and disbanded the partnership, with millions reportedly lost by both Flex and Nike. It was reported the project failed to make sense for Nike on a cost basis.

Competitor Adidas faced similar challenges when it invested in its first automated factories in Ansbach, Germany and Atlanta, Georgia in 2015. The location made the facilities and labour still too expensive to be worth the savings on shipping and shorter production times from the brand's perspective.

For Nike, the question remains how the company plans to double its direct-to-consumer revenue without making substantial changes in its supply chain. Leadership in that area has also transitioned under Donahoe: the executive who oversaw supply chain projects in recent years, longtime chief operating officer Eric Sprunk, was one of the senior leaders who left the company in February.

"Can you double the business, can you get where they want to go on the same supply base in Asia? The answer is, no, you can't," said John Thorbeck, chairman of supply chain analytics firm Chainge Capital LLC. "The company is not very productive from an inventory standpoint, and nowhere near best in class."

Nike has recently been focused more on expanding its RFID technology, or "radio-frequency identification" smart tags, to its products for greater visibility of its inventory in different sales channels and locations. This technology would allow Nike to reallocate inventory across channels, from online to a partner retailer, depending on need and, using predictive technology acquired last year with Boston firm Celect, ahead of demand.

But Nike has a growing margins problem, made worse by the pandemic. Gross margins decreased by 90 basis points in the quarter ending August 31, 2020, executives said, as the brand dealt with holding and selling excess inventory and discounting. Even before the pandemic, Nike's margins were lower than its shareholders hoped, as the investments of the last several years are yet to pay off on the bottom line.

The company should look to Apple's "asset-light" manufacturing as a model, Thorbeck said, cautioning that Nike still judges its supply chain primarily on cost, not on risk. The brand will need to expand the "Express Lanes" in its supply chain or find other ways to work with more flexibility with suppliers as it continues to transform from a giant of the analogue era into a leader in the post-pandemic digital age.

# Further Reading

- The Business of Fashion, The Radical Strategy That Drove Nike's Pandemic Success
- Highsnobiety, Community? Nike doesn't care about your family-run store
- The Financial Times, Online sales surge sends Nike shares to record high
- Bloomberg, Nike Job Cuts Will Cost Up to $250 Million
- The Financial Times, Nike ecommerce gains fail to make up for pandemic fallout
- The Business of Fashion, How Are Sports Brands Marketing Without Sports?
- The Business of Fashion, In Brands We Trust: Why Companies Are the New Communities
- Bloomberg, Nike to Stop Selling Products on Amazon Site
- The New York Times, Doping Scandal Includes a Direct Link to Nike's C.E.O.
- The Business of Fashion, Can Foot Locker Be Cool?
- The Business of Fashion, Despite Setbacks, Nike Is Scoring with Direct-to-Consumer 'Offense'
- The Business of Fashion, Why Brands Are Launching Secret Apps for Superfans
- The New York Times, Nike Nearly Dropped Colin Kaepernick Before Embracing Him
- The New York Times, At Nike, Revolt Led by Women Leads to Exodus of Male Executives
- Bloomberg, Nike's Failed Attempt to Challenge the Old-School Adidas Cool
- Bloomberg, Nike Stocks Falls as Competition for Sportswear Intensifies
- The Business of Fashion, How Adidas Converted the Cool Kids

Design by Lucinda Scholey
Edited by Vikram Alexei Kansara and Hannah Crump

Front cover image: Getty Images

Discover our complete online courses and learning resources at: businessoffashion.com/education

info@businessofashion.com