RUSSIA'S FASHION SECTOR:

INDUSTRY TRENDS, CURRENT FIGURES AND NEWS

—————

Prepared by the consultancy
firm Fashion Consulting Group, by
request of Collection Premiere Moscow.

CPM

FCG Fashion Consulting Group
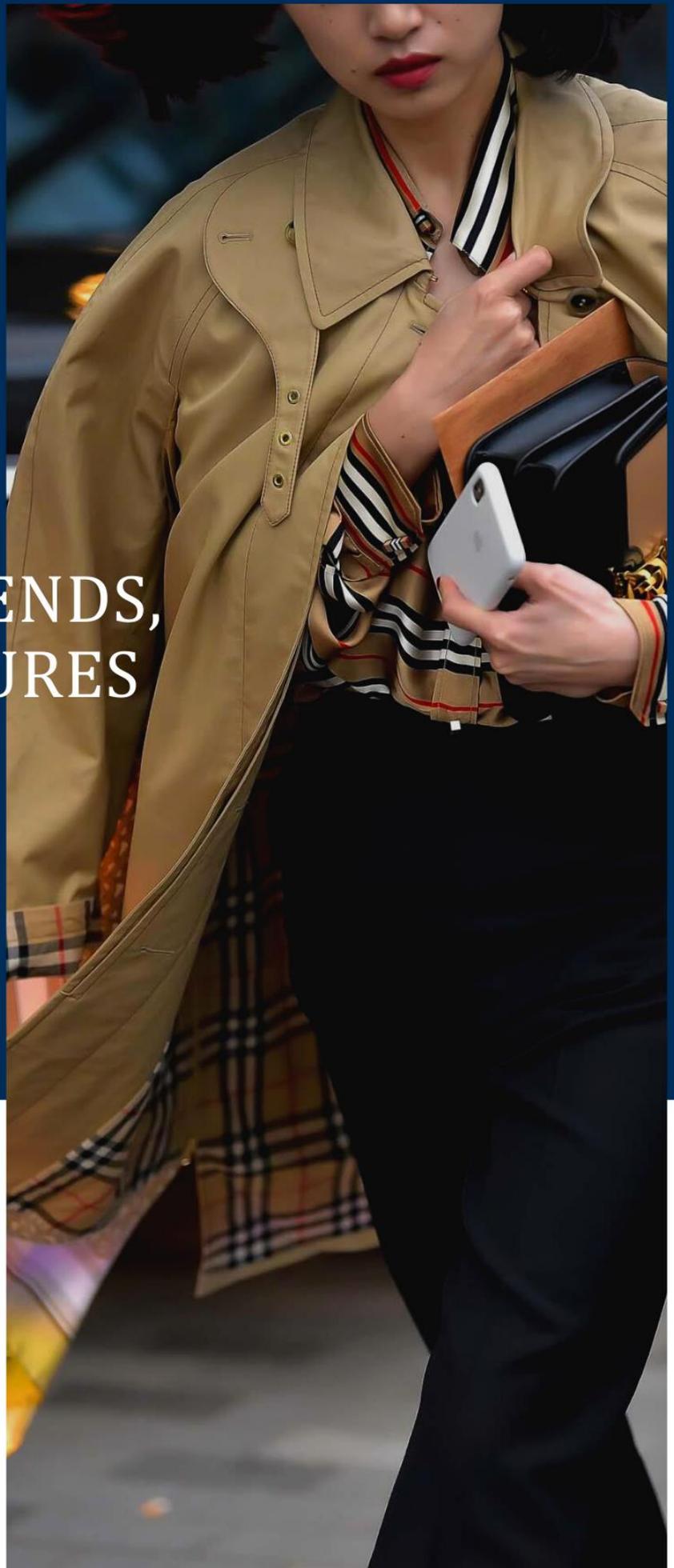
TODAY'S THEMES:

TRENDS AND FACTS

CHANGES IN PREFERENCES AND BEHAVIOUR MODEL OF CONSUMERS IN RUSSIA: EVOLUTION OF POST-CRISIS CONSUMPTION IN 2014-2019

Macroeconomic Context of Fashion Market

The macroeconomic factors do not have a beneficial effect on activity at the consumer market. Continued economic sanctions and dramatically unprecedented reduction of foreign investments in Russia accompanied by outflow of foreign capital have inevitably had a negative impact on the economy in 2019 as well. According to estimates of the Federal Service of State Statistics (Rosstat), at 2019 year-end the GDP of Russia has grown by 1.3% (in 2019 the economic growth rate has become the lowest since 2016).

The positive factors of 2019 are as follows:

- rouble stabilization – for instance, in 2019 the average exchange rate of USD was 64.7 roubles and it is higher just by 3.5% as compared to the exchange rate as of 2018 year-end (62.5 roubles),
- low inflation – at the year-end it was 3%, being the record low indicator,
- positive indicator of income growth by 0/8% at 2019 year-end (according to the data of Rosstat).

Nevertheless, the Ministry of Economic Development of the Russian Federation indicates that dynamics of consumer demand is negative. It results from several factors, such as increase in retail prices for the core consumer goods and increase in the basic VAT rate up to 20%, starting 1 January, 2019.

Through this process, the positive index of growth of salary and increase in income of the population determined by the state authorities is canceled out by increased expenses for basic needs. In spite of low inflation, prices for consumer goods keep growing (for example, according to Romir, the share of expenses for food products has grown by 6%), cost of the housing and utility services has been slowly but steadily growing (according to Sberbank of Russia, payments for the housing and utility services has grown by 4.1% in the aggregate).

Besides, the amounts of compulsory monthly payments on loans have been increasing (this indicator is twice as high than 5 years ago). The report of the All-Russia People's Front notes that the level of household debt load has grown up to 28% national average. It means that, as a rule, a household spends about 28% of the annual income for repayment of bank loans.

Reduction of the amount of savings is the indirect factor of decrease in the disposable income: in 2019, 69% of Russian nationals were not in a position to save up altogether (according to the data of the National Agency for Financial Studies, a research and analytic center). In 2018 this indicator was the minimum over the last 20 years but in 2019 it continued to decline.

So, for example, according to the research of consumer confidence by The Conference Board and Nielsen, in 2019, 56% of the Russian nationals in the survey cut down expenses for apparel which is even more than people who cut down expenses for outdoor entertainment (52%). The level of negative assessment of the future perspectives keeps becoming higher – 53% of the Russian nationals believe that the negative consequences of economic downfall in this country will be felt for a rather long time, although in post-crisis 2015, such pessimists were only 29% in number (according to GFK).

It should be noted that the climate disruption that occurred during the period of the year being the most important for Russian retailers became an additional adverse factor with respect to downturn in sales in 2019. The abnormally warm autumn was followed by the late winter that failed to come in the central region of Russia by the end of December, 2019. This factor triggered significant

RUSSIAN MARKETS CURRENT STATE: KEY FIGURES

Russia's fashion industry volume, 2012-2019F, trillon rubles

Growth dynamics of Russia's fashion market, 2012-2019F, %
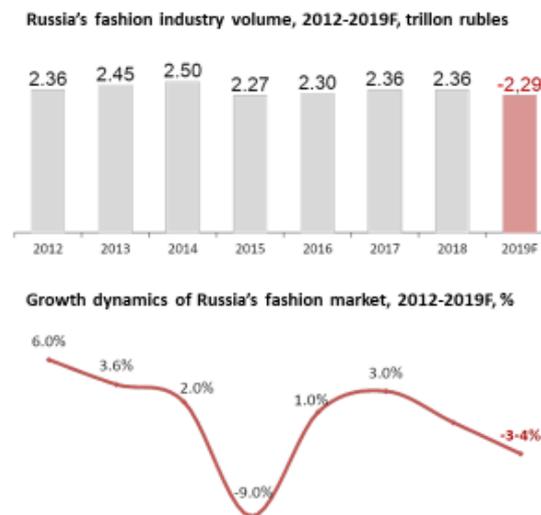
underachievement of volumes of sales of autumn/winter apparel.

Source: according to FCG

At 2019 year-end, volume of the fashion market of Russian was estimated to have reduced by 3-4%.

Fashion Market of Russia Today: Thrift Consumption

The economic crisis and continuing economic recession have significantly emptied the market basket of consumers in Russia. The last 5 years have distanced the middle class of the Russian society from the standards inherent to the middle class in the developed countries. But, in spite of the fact that the middle class of the Russian society comprising educated professionals accounts for 38.2% of the population (according to the research work carried out in 2019: The Russian middle class in focus of various theoretical approaches: boundaries, structure and specificity), only 7% of the population comply with the international criteria for the lifestyle of the middle class.

The faltered welfare and decrease in the disposable income have generated a fundamentally new type of purchasing behaviour that have been strengthened by the global social and cultural factors: development of e-commerce and digital technologies. Nowadays people plan in advance even minor purchases, compare terms and prices. Though making purchases in the traditional outlets, customers turn to the Internet for reliable reference information.

Customers are eager to seek alternatives and wait for beginning of sales period, expecting that sooner or later outlets will offer promotional discounts. According to Ipsos Comcon, in the first quarter of 2019, the share of purchases at a discount exceeded 2/3 of the total amount of purchases of apparel (69%). And this indicator is even higher in the apparel segment – 80% of customers freely admit that they prefer to purchase apparel at a discount. Price has become the main argument for making of a

purchasing decision. Impulse-driven and light-hearted attitude has changed for reasonable, thrift and serious-minded mood.

Change in Perception of Quality Boundaries:

- Service life of durable goods has increased. For example, in the previous years, footwear was purchased for 1-2 seasons but now it is purchased for 2-3 seasons. The majority of Russian nationals (67%) purchase new winter footwear only when the footwear they use become worn, on average, once in 2-3 years.
- Quality is to a lesser extent associated with the concept of fashionable and relevant. Importance is being increasingly attached to the criteria of multipurposeness, wearability and usability.

Targeted Search of Alternative Points of Purchase Offering Low Prices:

- Discount has become the most important purchase motivator: the majority of Russian nationals (93%) are sensitive to discounts and sales events – they time their shopping to coincide with such events or pay attention to them already in the process of search (according to Deloitte).
- Various formats of clearance sales grow in popularity. The Familia chain, selling off-price collections, is the leader by the rates of growth at the market. At 2019 year-end, the proceeds of the company have increased by 20% amounting to 33.5 bln. roubles and the number of stores has increased by 19% amounting to 285.

Growth of Confidence in Local Brands:

- Growing interest in brands manufactured in Russia. According to RosBusinessConsulting, 45% of the customers in the survey are satisfied with quality of Russian-manufactured apparel (as compared to 40% in 2018).
- Increase in number of local brands in shopping centers. Over 2019, operators of shopping centers doubled the number of stores of the local designers.
- Increase in the number of local brands in the Internet (at the marketplaces). For example, over two years, Aizel doubled the number of Russian brands present at the platform up to 150.

HOT-BUTTON ISSUES FOR RETAILERS: LABELING

Main Purposes of Labeling of Light Industry Goods

Domestic products comprise only 34% of the light industry segment at the market of Russia (according to the data of the Ministry of Industry and Trade of the Russian Federation). Shadow segments continue to play an important role at the market. According to various estimates, the overall market of illegal products in Russia amount from 30% to 50% of the total volume of sales of apparel, footwear and accessories. The share of turnover of copies and replicas in the global apparel and footwear industry is estimated to range from 30 to 35%.

In December, 2017, the Government adopted a decision on implementation of the Integrated System for Labeling and Traceability of Goods hosted and supported by the Center for Development of Advanced Technologies by 2024 for the purpose of obtaining of the latest and reliable information about flows of goods.

In fact, it means assignment of electronic passports to each item of goods that enable to determine their origin and the actual characteristics, i.e., name of the manufacturer, place/date/time of manufacturing or sale, product ID, etc.

Labeling is the most efficient technique for protection against counterfeit. It is expected that through implementation of the labeling system, the legitimate business will obtain protection against all the types of illegal products: counterfeit, forgery, illegal trafficking, etc. Besides, electronic format simplifies the system for accounting and finding of facts of infringement of rights of the right holders.

List of Labelled Goods and Implementation Time Lines (Examples)

The list of goods that are subject to mandatory labeling is supplemented in a step-by-stem manner. At the moment it is mandatory to label fur coats, tobacco products and some pharmaceuticals; pilot projects for labeling of dairy products and wheelchair are under implementation. From December, 2019, the list has been supplemented by 10 more categories: perfumes and toilet water, knitwear blouses, coats and short coats, rainwear, cloaks and jackets, wind jackets and windbreaker jackets, bed cloths, table clothing, bath and toilet cloths and kitchen linen, photo cameras and flash tubes, tyres and

Labeling

Tobacco	Fur	Footwear	Medication	Cameras and flashbulbs	Tyres	Garment industry	Pefumes

Experiments

Diary	Wheelchairs	Bicycles
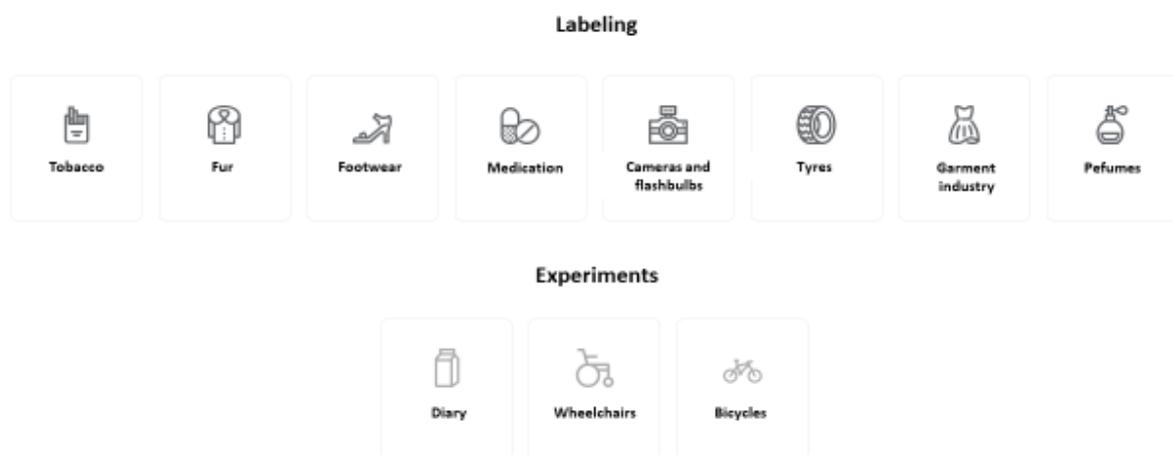
pneumatic tyre covers.

Source: Chestny Znak, National Track & Trace Digital System

- *Labeling of fur products.* The regulation on mandatory labeling came into effect on 12 August, 2016. As of 1 June, 2019, the information system for labeling of fur products was integrated with Chestny Znak, the integrated national system for labeling and traceability of goods.

- *Labeling of footwear.* Mandatory labeling of footwear was introduced on 1 July, 2019. From then onward, economic agents shall have commenced the phase-by-phase switching over. Manufacturing, import of footwear, wholesale and retail sale of unidentified footwear are prohibited, beginning from 1 March, 2020. Labeling of the remainder footwear manufactured or purchased prior to 1 March, 2020, is allowed till 1 May, 2020, only if the documents confirming the date of purchase thereof are available (Regulation of the Government of the Russian Federation No. 860 dated of 5 July, 2019).

- *Labeling of other light industry goods.* From 27 June to 30 November, 2019, an experiment was carried out with respect to labeling of light industry goods. Switching over to the labeling system is also implemented in a phase-by-phase manner. Mandatory labeling of some items of apparel and bed cloths came into effect in Russia on 1 December, 2019 (items of apparel, inclusive of workwear, made of real or blended leather, blouses, coats, short coats, rainwear, cloaks and jackets, inclusive of ski coats, wind jackets as well as bed cloths, table clothing, bath and toilet cloths and kitchen linen). In compliance with Regulation of the Government of the Russian Federation No. 1956, turnover of unidentified goods will be prohibited, beginning from 1 January, 2021; till 1 February, 2021, all the economic agents shall label the leftover stock unsold before 1 January, 2021.

Impact of Implementation of Labeling on Business Processes

Implementation of labeling means not only significant effort but also significant time expenditures. In effect, it is switching over not only to piece count of products but also to detailed formalization of a large set of parameters for each item. These are fundamental changes.

That is why all the preparatory works shall be commenced in advance. Prior to beginning of the negotiation process with contractors and vendors (for example, all the contractors shall switch over to electronic document management), it is required to form and train an internal work team, to appoint persons in charge and to be registered with the labeling system.

Introduction of labeling requires changes in business processes for all the companies, especially, with respect to the accounting and planning system. It is a complicated work on introduction and practical approval of new rules.

The economic agents involved in turnover of labelled goods include:

- Manufacturers,
- Importers,
- Wholesalers,
- Retail stores,
- Commission merchants (for example, Wildberries, Lamoda, Butik.ru and others).

Switching over to new business processes requires additional funds and additional experts having new skills and qualifications in all the above listed industry sectors. New equipment will be required for the entire life of products. For example, with due account for the fact that each label is unique, special-purpose printers and scanners for such labels shall be available both at the warehouses and in stores.

- Automation process is a rather costly and time-consuming procedure. For instance, updating of software will be necessary for cash handling units that are in operation at the present time. Moreover, adjustment of electronic document management systems (EDMS) will be required.

- It is more than likely that not all the factories will be able instantaneously to ensure the statutorily required reliability and authenticity of labeling. One collection may be created at a number of factories and be delivered via various routes, while the threat of failure of the supply chain is the challenge of every vendor. It means that it is required to add the service for relabeling of products at the warehouses to the supply chains.

If at the phase of transformation, foreign vendors are reluctant to bear the expenses for labeling, these tasks and expenses shall be solved and borne by their local distributors in Russia. In any case, at the first phase they will have to pour cash into labeling of the leftover stock that have already been delivered to Russia and are at the warehouses. The entry fee amounts to 3 thousand roubles upon registration with the GS1 Russia system (it is required, in the first place, for manufacturers and importers); 50 kopecks shall be paid for each label (tag) to the operators of the Center for Development of Advanced Technologies Center for Development of Advanced Technologies and all the expenses for implementation of business processes shall be self-funded, inclusive of expenses for obtaining of the enhanced qualified digital signature, equipment for printing of adhesive labels, consumables, training and salaries of employees.

Example of Indirect Costs for Implementation of Labeling:

Non-recurring expenditures:
- Obtaining of the enhanced qualified digital signature – starting at under 3 000 roubles;
- Connection to the EDMS – free of charge for receiving but on a paid basis for sending of documents (up to 10 roubles for each way-bill);
- Updating of firmware for online cash registers and of point-of-sale software – up to 2 000 roubles;
- Procurement and adjustment of 2D-scanner (it is required for each cashier to read codes) – starting at under 4 500 roubles;
- Procurement of thermal transfer printer or commercial printer to print labels – starting at under 10 000 roubles;
- Registration with the GS1 Russia system and annual membership – 3 000 roubles upon registration and from then on – 3 000 roubles per year.

Recurrent expenditures:

- Services of the Fiscal Data Operator (communication of fiscal data to the Federal Tax Service) – starting at under 1 000 roubles;
- Ordering of labeling codes, one code is worth 50 kopecks (VAT exclusive);
- Application of labeling codes on new goods by manufacturers, labeling of the leftover stock. If relabeling is required or loss of labels occurs, ordering of new code and application on packing/packaging, etc.

At the current phase of implementation of labeling, while many processes have not been adjusted yet, technological challenges have not been solved and errors have not been eliminated, the economic agents involved in turnover of labelled goods shall address all the arising questions to the government authorities (the Center for Development of Advanced Technologies, the Ministry of Industry and Trade of the Russian Federation, the Federal Customs Service, the Federal Tax Service, the Russian Federal Service for Surveillance on Consumer Rights Protection and Human Wellbeing, etc.) and refer to the Regulations of the Government of the Russian Federation, the Executive Orders of the Government of the Russian Federation, the federal laws and to other regulatory documents currently in effect.

SOCIAL TREND: DIGITAL FASHION – NEW TECHNOLOGIES AND FASHION

There are 2 main approaches to the concept of digital economy. The first approach means that the digital economy is classified as a separate environment and branch of economy that is based on digital technologies. In this sense, it is related only to electronic goods and services, that is, to virtual goods and services. The second approach implies a broader understanding of the digital economy – as digitalization of the economy as a whole – that is, it is economic activity using digital technologies. All the transformations that take place in the fashion industry are the illustrative indicator of changes towards digitalization of the economy.

All the trends can be generalized as 4 major vectors of technological development that are evolving in the process of such transformation and essentially change the fashion industry:

1. Remote simulation and management of business processes (the Internet of things, digital manufacturing and 3D printing of objects);

2. Development of systems that enable to create virtual copy of the outworld (AR/VR - Augmented reality and Virtual reality);

3. Acquisition, structuring and analysis of unlimited volumes of data, training of systems for self-development, self-improvement and autonomous decision making (Big Data and artificial intelligence, integration of IT systems and cybersecurity);

4. Change of all the processes for digital formats that previously required creation and disposal of tangible products as well as various forms of power management for the purpose of maintaining of the environmental balance (reducing of disposables and expendables, inclusive of paper, etc.)

These 4 vectors of development have impact on all the segments of the fashion industry: production of raw materials, manufacturing of finished goods, disposal and recycling of finished goods; distribution of products has been essentially changing.
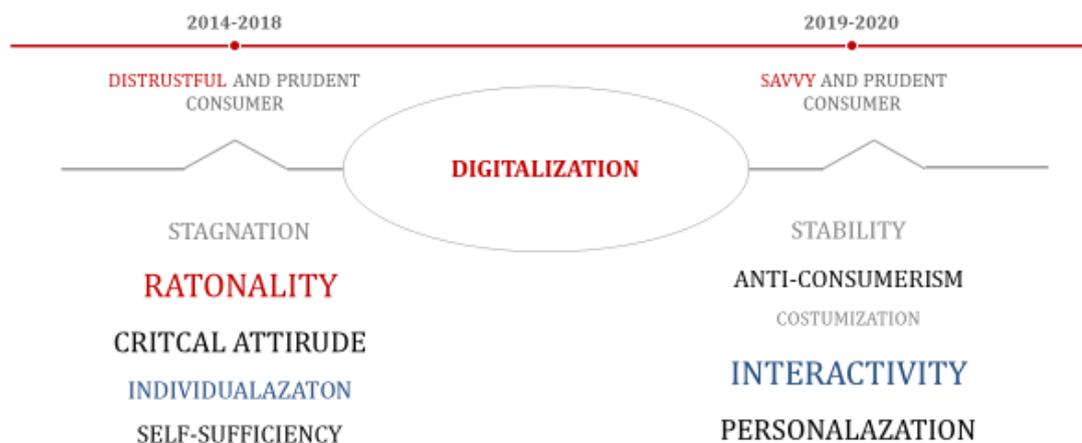
Source: according to FCG

Examples of the most in-demand technologies by segments of the fashion industry are given below:

RAW MATERIALS:

− raw materials for 3D printing of apparel and footwear,

− fabrics with added functions, integrated conductive fibers. Examples of digitalization of raw materials: smart jacket by Google and Levi's, Paqsule innovation-based smart bag, Nike Adapt BB smart self-lacing running shoes and others.

MANUFACTURING, RECYCLING AND DISPOSAL:

− design with the aid of AI – Google and Project Muze, Fast fashion by Amazon, Tommy Hilfiger in cooperation with IBM and Fashion Institute of Technology and others,

− automation and robotics technology: digital manufacturing without a lot of personnel (Sewbots fitted with robot-assisted tubes, vacuum grippers and special-purpose micromanipulators by SoftWear Automation, water-soluble solutions for stiffness of fabrics by Sewbo),

− technologies that change the traditional manufacturing cycle, for example, technologies for welding of fabrics – threadless manufacturing (fusing, ultrasonic, hot gas welding, etc.), Pili-bio renewable colors, liquified gas for cleaning of fabrics by Tersus and others.

DISTRIBUTION (inclusive of online and offline retail services):

− IoT and labeling – QR and RFID tags,

− Big Data and customization – system for recognition of faces/images for customization of offers, chat bots and virtual stylists (Echo Look by Amazon, chat bots by Prada and Levi's and others), 3D-scanning (smart leggings by LikeAGlove),

− AR/VR technologies for sales of apparel and footwear: interactive mirrors and virtual try-on rooms, smart shelves, scanners of apparel and footwear sizes, holographic 3D displays and others,

− Automation and robotic automation: stores without cashier desks and personnel, electronic shopping assistant, mobile POS-terminals and others.

MARKETING AND COMMUNICATION:

− Big Data and digital marketing: content marketing, inbound marketing, event marketing, affiliate marketing, influencer marketing, performance marketing, gamification, etc.

ANNEX. RELEVANT NEWS

NEW TECHNOLOGIES AND SERVICES:

- Доставку одежды и обуви можно будет оформить через голосового помощника "Олега" 09.12.2019
- «Обувь России» запустит онлайн-платформу для работы с поставщиками 26.11.2019
- «Яндекс.Еда» добавила в приложение «временные» онлайн-магазины с коллекциями от российских дизайнеров 25.11.2019
- Butik внедрил цифровые примерочные 25.11.2019
- Молодые дизайнеры и IT-специалисты МИДИС совместно с "Юничел" разработают модель обуви будущего 22.11.2019
- Дмитрий Шишкин открывает первую в России цифровую швейную фабрику 15.11.2019
- «Яндекс» запустил AR-приложение Sloy с распознаванием одежды из видео 15.10.2019
- Основатель Sela выступил инвестором стартапа GardeRobo AI - это сервис рекомендаций, который подстраивается под покупателя интернет-магазина и позволяет подобрать наиболее подходящую ему одежду 09.10.2019
- В Санкт-Петербурге представили конструктор для умной одежды 22.08.2019
- На Lamoda появилась виртуальная примерочная обуви 16.08.2019
- Российская текстильная фабрика «Чайковский текстиль» создала огнестойкую ткань с защитой от нефти, не имеющую аналогов на отечественном рынке 31.07.2019
- Компания «Линдстрем» запускает в России сервис по аренде рубашек 26.02.2019
- O'stin обзавелся онлайн-помощником по подбору одежды 22.02.2019
- Российские специалисты из Шахт создали одежду с микроклиматом для прогулок на инвалидной коляске 24.01.2019