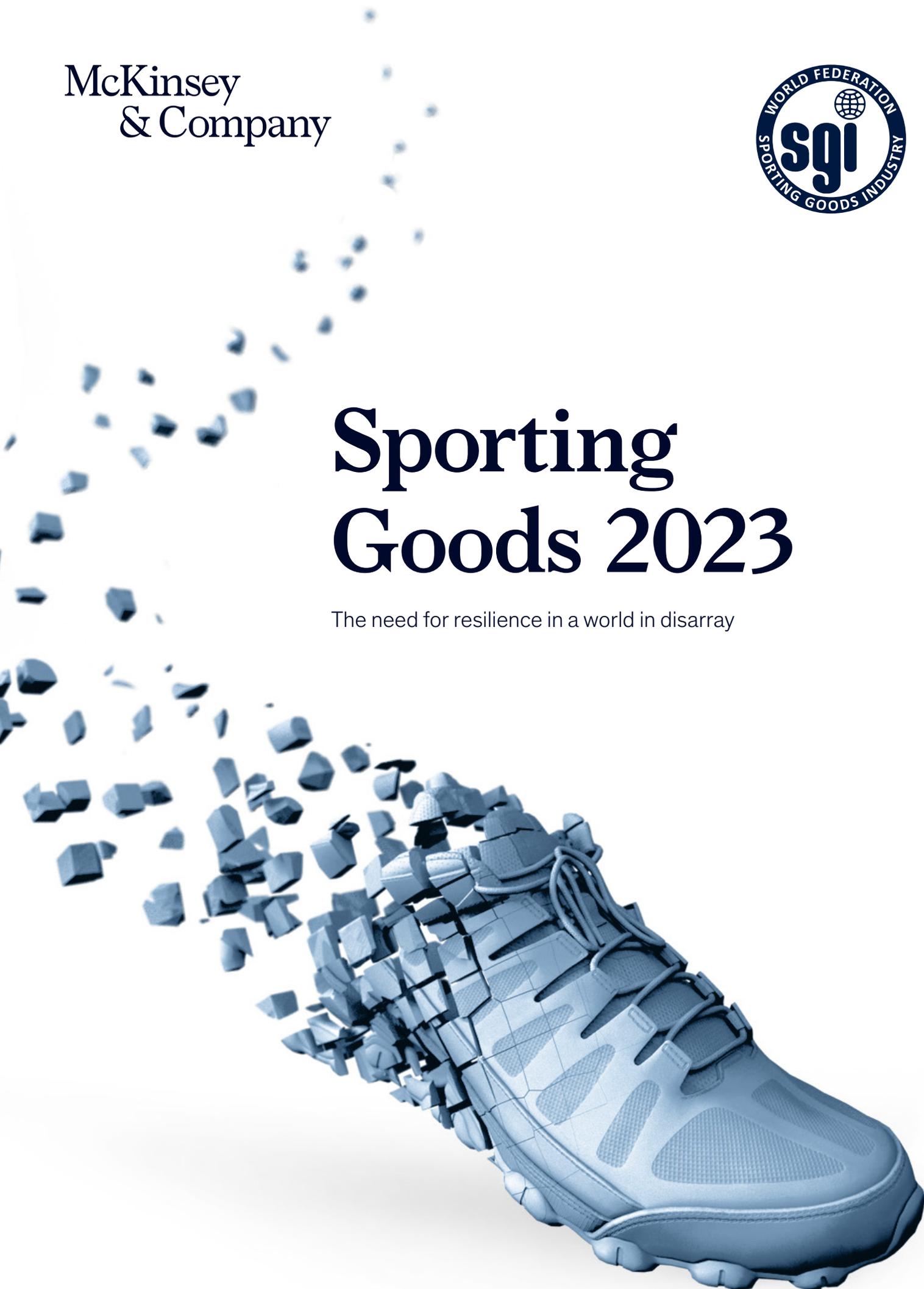


McKinsey
& Company



Sporting Goods 2023

The need for resilience in a world in disarray



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Sporting Goods 2023

The need for resilience in a world in disarray

Foreword

The World Federation of Sporting Goods Industry (WFSGI) and McKinsey & Company have teamed up once again to present our third annual Sporting Goods Industry Report – “Sporting Goods 2023 – The need for resilience in a world in disarray.”

After the industry recorded a widely positive performance in 2021, the past year has seen multiple challenges, including the threat of global recession, war in Europe, continued supply chain challenges, and rapidly rising interest rates; all contributing to a world in disarray.

This third edition of this report drills into the dynamics driving performance in the sporting goods industry. It sets out areas in which sporting goods companies have outperformed and faced challenges in the past 12 months, with deep dives into the US and China, the largest global markets. In addition, it explores how the industry can boost its resilience to the current storm. As in past editions, we focus on key trends that have impacted the industry of the past year and will shape performance in 2023 and beyond. We highlight the ever-increasing importance of branding, show how companies are responding to the sustainability imperative, and provide new insights into the nearshoring trend. We also zoom in on the value the industry is creating and how that is attracting the attention of the private investment community.

In this third edition, we dedicate even more space to our feature interviews with industry executives and experts. We are grateful for their insights into the evolution of business and for their honesty in sharing the strategies enabling them to navigate, and often thrive, in the current environment.

In many ways, the sporting goods industry is in a fortunate position. Compared to many other industries, the past two years have, in aggregate, been characterized by solid growth, equaling or outperforming pre-pandemic levels.

Looking to 2023, there are clouds on the horizon. Rising costs, the looming threat of recession, and continuing operational challenges are set to create headwinds early in the year. In response, companies are under urgent pressure to embed resilience into their operations. That will mean going beyond raising prices to boost productivity, manage cash more rigorously, and find the right balance between saving and investment.

We see this as the beginning of a time that will be more challenging to navigate, but with positive megatrends driving performance: in the mid-to-long-run, we expect a more constructive picture, building on one of the lasting effects of COVID-19, the general increase in health awareness. During the pandemic, consumer’s increased focus on health and wellbeing has been one of the key drivers of the industry’s fast recovery, primarily driven by increasing interest in sports from new customers (as shown by growing beginners’ product sales).

Nevertheless, globally, we still face significant health risks relating to higher levels of inactivity: 81 percent of adolescents and 27.5 percent of adults currently do not meet WHO’s recommended levels. In 2018, the WHO published the Global Action Plan on Physical Activity (GAPPA), which set out evidence-based recommendations for all countries to increase physical activity levels by 10 percent by 2025 and 15 percent by 2030. The WHO’s recent Global Status Report on Physical Activity 2022 showed that global implementation of the policy actions “has been slow and uneven.” The report notes that, “A consequence of this “inaction” is that already stretched health systems are burdened with preventable disease today and even more so in the future, and communities fail to benefit from the wider social, environmental, and economic benefits associated with more people being more active.” In addition, recent WHO data shows that the projected cost of inaction will add an additional \$301.8 billion to the global health budget. It is therefore clear that a lot can, and must, be done to promote sports further and close the physical activity gap. Global change on this level is beyond the capacity of the sporting goods industry alone, and multistakeholder action is critical to achieve the GAPPA goals.

One of the truisms of sporting success is that “the harder the battle, the sweeter the victory.” Over the coming 12 months, sporting goods companies have an opportunity to put this to the test, aiming to navigate the recessionary wave and emerge more robust for the medium and long terms. We hope this report will support you in making the right decisions for 2023. Thank you for reading, and we welcome your feedback and comments.

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Executive Summary

On the heels of the global pandemic, the past 12 months have seen new challenges in the form of rampant inflation, pressure on household incomes, and geopolitical tensions. The Sporting Goods 2023 report analyzes the current environment and explores how the industry can bolster its defenses. In addition, it provides an in-depth analysis of industry performance, including deep dives into the US and China, the world's biggest sporting goods markets. The report examines the key trends shaping the industry, including the enduring power of brands to create value, growing pressure to deliver on sustainability promises, the strategic case for nearshoring, and the rising attention of private investors. Through these lenses, we see an industry that is in excellent health but must work hard to build resilience in the months ahead.

Review of 2022

Two thousand and twenty-two was set to be another great year for the sporting goods industry: consumer sentiment was improving month-on-month, reflecting looser COVID-19 restrictions in most markets, companies were placing large orders, both in anticipation of demand and to avoid the supply chain challenges of 2021, and performance in the first half of the year was widely positive. In the background, however, storm clouds were gathering. Inflation was picking up due to the impacts of the war in Ukraine (especially in Europe), and higher raw material and energy costs were prompting some companies to raise prices. Meanwhile, consumer sentiment showed signs of deterioration, and discretionary spending declined. Supply chains gradually became more reliable, but the sudden increase in volumes led to widespread overstocking.

In the second half of the year, the economic outlook darkened, amid rising concern over geopolitical instability and the trajectory of interest rates—which tightened constraints on both companies and household budgets. The aggregate impact of these factors was a significant weakening in industry performance compared with 2021 (although still in advance of pre-COVID levels). The uncomfortable reality was that sporting goods companies were able to raise prices, but not enough to offset declines in units sold. That said, some categories performed better than others, leading to both risks and opportunities for individual players.

Outlook 2023

In 2023, we expect a challenging economic environment and continuing subdued consumer sentiment. This will require sporting goods companies to focus both on preserving demand and building resilience. However, companies must go beyond price adjustments and formulate a holistic response to the headwinds they face. This will mean assessing and optimizing all options that will not put demand at risk, including sourcing and supply chain, productivity, operational efficiency, and cash flows. Given the uncertain economic environment, we believe that the best predictors of future industry performance are the signals coming from the most recent retail data. In fact, for this report, we took the opportunity to collaborate with our partner NPD Group to drill down into the most recent US sales data and its implications. We hope these insights will support decision-makers as they calibrate perspectives on the critical trends in the year ahead.

Country deep dives

USA

The US sporting goods market saw a strong post-COVID recovery in 2021, in many categories surpassing 2019 performance. In 2022, the US market was exposed to the many forces shaping the global market, leading to unit sales declines of 4-8 percent in the first nine months, compared with 2021 levels, which was not offset by higher average selling prices. These unforeseen volume declines led to significant overstocking and heavy discounting in the second half. Athletic footwear and activewear saw revenue declines of 4-6 percent in the first nine months of 2022, driven by weakening consumer demand and conservative assortments. Equipment categories had a hard time beating their record years of 2020/2021. Home fitness equipment saw a 28 percent revenue decline compared with the same period in 2021. The exception was e-bikes, which continued to grow strongly.

China

In 2022, the Chinese sporting goods market saw a largely flat performance, in stark contrast to double-digit expansion over recent years. The key driver was the country's dynamic zero-COVID policy. Still, in the longer term, we see resilient fundamentals that promise a return to growth. These include government support for healthy lifestyles under the "Fitness for All" program¹, the expansion of the middle class, and rising female demand (unlike in Europe and the Americas, women spend 15-20 percent more on sports and fitness than men). In general, sports are becoming a more significant part of people's daily lives, and there is increasing interest in relatively niche areas such as skiing, surfing, and outdoor activities such as camping. Local brands such as Anta and Li-Ning are competing fiercely, for example, by offering more female-focused products—are capturing market share. Thus, there is rising pressure on international brands to raise their games.

In 2023, four themes will likely feature high on company agendas:

i. Brand relevance increasing

Building brand heat and loyalty is more relevant than ever, especially in a recessionary context, in which consumers tend to rely on trusted brands.

The consumer journey is shifting, especially when shopping for lifestyle categories. Whereas previously, consumers were motivated first by factors such as functionality, design, and price, they are now increasingly driven by brand. Notably, the industry's super-winners in terms of value creation are characterized by high levels of brand equity and loyalty.

In the lifestyle apparel category, sporting goods companies are on a similar journey to fashion companies, amid a need to build strong and trusted brands that leverage the direct-to-consumer revolution, collaboration with other brands, and community marketing.

ii. Sustainability, time to deliver on promises

Brands, retailers, and manufacturers have made bold promises of a more sustainable future, but are they up to the challenge? With self-imposed deadlines on the horizon, it is time to deliver. Two priorities should shape their agendas:

¹ For a broader perspective on global physical activity levels, please read the dedicated section in our Foreword

1) Plotting the path to net zero by setting CO₂ baselines, defining emissions abatement curves, prioritizing decarbonization levers, and planning for the challenges ahead.

2) Defining the company's role in the growing circular economy, choosing from a range of business models to scale.

Whatever they do and say, companies need to be careful to deliver against a background in which greenwashing is being targeted by both regulators and consumers.

iii. Nearshoring, a potential solution for supply chain disruptions

Supply chain disruptions, higher trade barriers, and geopolitical turmoil are putting pressure on supply chain security and leading to higher costs.

Nearshoring can unlock a range of benefits in a disruptive context: control and de-risking of the supply chain, agility and speed, cost structure competitiveness, protection against trade barriers, and a more sustainable operating model in the eyes of consumers.

Still, nearshoring does not always go to plan, evidenced by the fact that some companies have recently reversed nearshoring decisions.

Whether to nearshore or not should be decided at product level, assessing exposure to supply chain shocks, the need for shorter lead times, and the economics. It is important that the nearshore country meets requirements for raw materials and components, and offers the right capabilities and capacity. A detailed business case should take into account a holistic set of variables to determine financial impact and feasibility, as well as potential government incentives.

iv. Sporting Goods industry, a hot target for private investors

The sporting goods industry has grown strongly over the recent years and is likely to continue on that path, amid rising consumer health awareness², alongside deepening interest in outdoor lifestyles and athleisure apparel. In addition, the industry has proven to be more resilient in downturns, bouncing back faster than others. Furthermore, it comprises many smaller but well-differentiated brands, which make attractive targets for consolidation or growth plays.

These factors have fueled interest among private investors, including venture capital firms, private equity funds, and companies, with the number of annual deals doubling in the past decade. Focus areas have included outdoor categories, connected fitness equipment, athleisure/activewear, and sustainable sportswear.

In a market dominated by super-winners, private investment is challenging. We see three key priorities for investors: aspire to build a portfolio to drive synergies; elevate digital, focusing on communities and personalization; and leverage analytics at scale to harness the power of data.

To navigate the current challenging environment, we believe it is time to invest in resilience and productivity—activating levers that will not harm demand and will lay the foundations for a steep recovery. However, these actions require investment upfront, in a context in which the cost of capital is rising. This will likely mean a wider gap between super-winners and the rest once the storm is over.

² For a broader perspective on global physical activity levels, please read the dedicated section in our Foreword

Sporting Goods 2023 at a glance

The 2023 Sporting Goods report assesses the major themes driving the industry and the impacts of the current economic environment on business around the world. This year, we also present deep dives into the US and Chinese markets. As in past years, we analyze the most important trends for the coming period.

Economic environment and country deep dives

Economic environment – Navigating the recessionary wave

-40%

consumer's net intent³ to purchase sporting goods items



Sporting goods companies are seeing weakening demand, as the global economic slowdown puts consumers under pressure. The most resilient businesses will take the opportunity to reset and position for growth.

Industry performance - US – Between a rock and a hard place

4-8%

sales decline in US in Q1-Q3 2022 versus 2021 across main categories



As the post-COVID recovery fades, sporting goods companies face renewed challenges from the impacts of inflation and slowing economic growth. Tough times are ahead, with the exception of a few bright spots.

Industry Performance - China – China's long horizons

54%

of households will occupy the upper-middle income and high income brackets⁴ by 2025



Despite short-term challenges, the outlook for the sporting goods industry in China is positive, amid rising interest in well-being and a strong association between sportswear and fashion. However, competition is intensifying and the need for real differentiation is increasing.

³ % of participants who expect to spend more minus % of participants who expect to spend less

⁴ Households with >160k RMB annual income

Sporting goods trends for 2023

Brand relevance - Becoming a brand super winner

>50%

of surveyed sporting goods players expect to increase spending on branding



Sporting goods companies are among the most effective brand builders in the world. However, as consumer expectations rise and brand relevance deepens, companies should keep brand building at the top of their agendas, applying a through-the-cycle mindset.

Sustainability – Time to make it real

86%

of surveyed companies have announced or plan to announce a CO₂ reduction target



Alongside peers in many other industries, sporting goods companies face a ticking clock on sustainability. To meet their highly-aspirational targets, companies need to both accelerate decarbonization and scale circular business models. Only through a combination of these levers will they transform their businesses and reach their goals.

Nearshoring – Balancing acts

75%

of surveyed players plan to expand nearshoring by 2025



In an era of supply chain disruption, more companies are turning to nearshoring as a core element of their supply chain strategies. However, decision makers need to do their sums before taking the plunge.

Investments in the industry – Sporting routes to profitable growth in private investments

>20%

TRS (total returns to shareholders) in 2019-2021 in sportswear, compared with 4.5% among traditional apparel players



The success of sporting goods brands has attracted a wave of private investment. By focusing on a portfolio strategy of complementary brands, an elevated digital interaction with consumers, and analytics at scale, funds are most likely to maximize their portfolios' potential.

Barbara Martin Coppola, Chief Executive Officer, Decathlon



Barbara, thank you for taking the time. When you look at the sporting goods industry, where do you see the biggest challenge, the most important call to action in the years ahead?

The most important aspect is to enable everyone to have an active and healthy lifestyle. More and more people realize the benefits of sports, and the pandemic accelerated this trend. However, there are still many populations – for example, lower-income segments and kids from non-privileged backgrounds – who are not taking part. The obesity rate has risen sharply, especially among teenagers and young adults. We therefore need to collectively do more to be inclusive and ensure that sport becomes a possibility and reality for everyone, whatever their level.

What will be the most significant changes the industry needs to make to work?

An important change is the evolution of the fundamental business model which has ruled the industry for many years. We need to move away from a model purely based on first-time ownership of goods to a usage-based model. With this business model we would lower

barriers to trying sports, allow people to use seasonal products and then share them back with the community. Hopefully, this will open the possibility to more people to adopt an active lifestyle and try a wide variety of sports. I hope we will see going forward that people are not just defined by one or two sports but by many sports. People will have more flexible options to fit sport into their daily lives.

What else does the industry need to do to open the world of sports for everyone?

We must question how we all have positioned sports in our marketing and communications. Quite often, there is a focus on performance, strength, and competitiveness. This can be intimidating to many people. Instead, the positioning of sports should be as whatever you believe sport should be for you. Emphasizing health and well-being, and the connection to others. Sport is not a luxury and not a privilege of the fit, trained, and shaped. It is a way of life that needs to be accessible to everyone. Sport needs to be fully democratized. Walking around the lake is as sporty as climbing Mount Everest.

You talked about the necessity to keep up with the evolving needs of society and the emergence of a new business model. To what degree does this new business model need to be more sustainable?

It is essential that we rapidly move towards decarbonization and circularity. The sporting goods industry is already adapting significantly to decarbonize its value chain, yet there is potential for further acceleration. Sustainable products should not come at a premium, they should be accessible to everyone.

Furthermore, circularity needs to end its niche existence and become mainstream – recycling, refurbishing, repairing, re-selling, and renting are the future. I think we are at a tipping point of seeing solid progress on circular business models. This starts with the product's design – it needs to be focused on longevity, durability, the use of low-carbon materials, and, ultimately, recyclability. But this is not enough, the whole end-to-end lifecycle needs to be rethought. This includes modes of production, transportation, and nearshoring. Finally, it will also be critical to get the commercial aspect of this new business model right so that it increases, and not decreases, accessibility and is attractive for both consumers and brands.

How do you at Decathlon think about this sustainability transformation?

First, I strongly believe that sustainability cannot be a luxury. It needs to be affordable. This is imperative for Decathlon. Also, I firmly believe that there will be significant economic value in this transformation. Hence, the faster we evolve, the better it will be for the planet and the business.

At Decathlon, we have already made substantial progress in integrating circularity into our routines. For example, we have more than 1,800

workshops in stores which repair products like bikes. And in many stores, we are currently running tests to rent equipment instead of buying it. Of course, this is only the beginning, and I see it as our responsibility as a major global player to lead the way.

What will be required from the consumer to make this vision of a sustainable future reality?

We have been trained for a long time to act in a certain way. When you want to take up a sport as a consumer, you go and buy the necessary equipment. So, moving from a product-based to usage-based model means that we would be changing the industry and consumers' habits. There is a push and pull that needs to happen. Propositions from the industry to consumers need to evolve to rethink what and how we sell, but then consumers need to be open to this new model as well.

To get to this future you are describing and envisioning, do we need to change our common definition of corporate success?

The sporting goods industry will only exist and thrive if our playing field, the planet, is respected and protected. Hence, as the new CEO at Decathlon, I made sure that, as a critical part of our strategy, we put sustainability on the same level as revenue and profitability.

Historically, financial aspects were always the most important measures of success – sometimes the only ones that mattered. Now we are leveling up the sustainability aspects to the same height. I firmly believe that decarbonization and circularity need to be measured as rigorously as cash flow or EBIT, and must be equally

important when defining whether we are successful.

I hope we will see this across the industry and arrive at a joint aspiration on measuring sustainability and what to aim for. There is also a role to play for regulators to hold us accountable, playing by the same rules and ensuring transparency towards clients. Regulators can ensure everyone is sufficiently aspirational, in line with scientific targets regarding climate change.

Concretely, by putting sustainability goals on the same level as financial success, how do you envision this will change how managers across Decathlon will make decisions for the company in the future?

I would like everyone making decisions for Decathlon to go ahead only if both financial and sustainability goals are met. It might take longer or be a more difficult path, but it's a path that creates more value, for shareholders, society and the planet. Maybe we need to find new partners, create new alliances, rethink processes, or question long-held beliefs. I realize this is raising the bar quite a bit, but if we get it right, we will lead the way as a good corporate citizen, and we can all feel a sense of pride in doing so. And by making these decisions transparent and measurable, we will know whether we are moving in the right direction and whether we are doing it fast enough.

While the industry and Decathlon are adapting to realize a more sustainable future, there are also several acute short-term challenges. How do you prepare for the uncertain times we find ourselves in?

It is a very uncertain environment with inflation, almost unprecedented

energy prices, and geopolitical tension creating very choppy water to navigate. Therefore, building business cases and operating models around flexibility and agility is essential. Wherever there is rigidity, for example, regarding long lead times or dependencies on single factories, there is a risk. At Decathlon, we are making our entire supply chain more flexible and adaptive, leveraging the possibilities that digitalization affords us in areas like end-to-end forecasting, building in more slack where necessary, and developing new muscles. Finally, I am convinced that in uncertain times, there is an opportunity to create competitive advantage and get to a higher level.

What role – if any – does near-shoring play in your vision of a derisked supply chain for a global player like Decathlon?

What we are aiming for is right-shoring. There is definitely much effort, together with partners, to optimize assembly and production in a geographical area when we serve that same geographical area: China for China, India for India, and Europe for Europe. By doing so, we aim to create regional and local ecosystems. For us, it is about the diversification of production areas and avoidance of dependencies and monopolies. We are rethinking our entire value chain, from the material to the transportation and movement of final goods, not only to de-risk our supply chain but to optimize for sustainability – and we are doing this not alone but with our network of long-standing partners and innovative companies.

“Sport needs to be fully democratized. Walking around the lake is as sporty as climbing Mount Everest.”

Navigating the recessionary wave

Sporting goods companies are seeing weakening demand, as the global economic slowdown puts consumers under pressure. The most resilient businesses will take the opportunity to reset and position for growth.





“We observe a certain amount of downtrading but, interestingly, not so much between brands. [...] And, of course, we are seeing more customers waiting for promotions and picking up the product at a better price.”

— Holger Schwarting, Chairman of the Board, SPORT 2000 International

Across many economies, recent months have seen a “perfect storm” of cyclical, structural, and supply chain challenges, all of which are fueling inflation that is likely to persist in the medium term. To date, the impact on sporting goods companies has been muted compared with other sectors. However, all the signs point to a tough year ahead.

With inflation running in 2022 at the highest level for at least 40 years in Europe and the US, just 6 percent of sporting goods companies are confident about their resilience and performance⁵. Indeed, the three words that executives most use are challenging, uncertain, and unpredictable⁵. The biggest concerns in the second half of 2022 have been falling demand and excess inventory. Looking to the coming year, 22 percent of decision makers expect both revenues and margins to contract by more than 5 percent.

Amid rising input costs at the end of 2021 and into 2022, many sporting goods

companies reacted initially by lifting prices. Of the 60 percent of companies that did so, two-thirds lifted across the board, while a third acted based on price elasticity at product level.

Meanwhile, consumer sentiment has headed in the opposite direction, driven by factors including the war in Ukraine, higher energy prices, and rising interest rates, which have reduced household incomes and put pressure on discretionary spending (Exhibit 1). About 60 percent of consumer spending in major European economies is focused on non-discretionary categories, including food, housing, and electricity⁶. As inflation rises, a larger share of household spending will go into mandatory expenditures, reducing consumers' disposable income. At the same time, savings are shrinking, and one in three consumers is tapping into savings to cover their daily expenses⁷.

High levels of pessimism are consistent across income groups. However, younger cohorts are less pessimistic, with 27 percent of Gen Z expressing

⁵ Source: WFSGI & McKinsey Sporting goods companies survey, September 2022 (N=211)

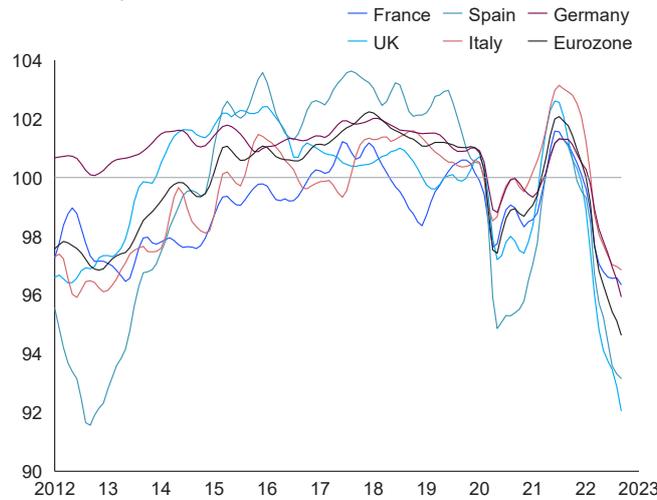
⁶ Source: Oxford Economics, retrieved on the 01.10.2022

⁷ Source: McKinsey & Company Europe Consumer Pulse Survey, 9/23–10/2/2022, n = 5,156 (France, Germany, Italy, Spain, UK), sampled to match European general population 18+ years

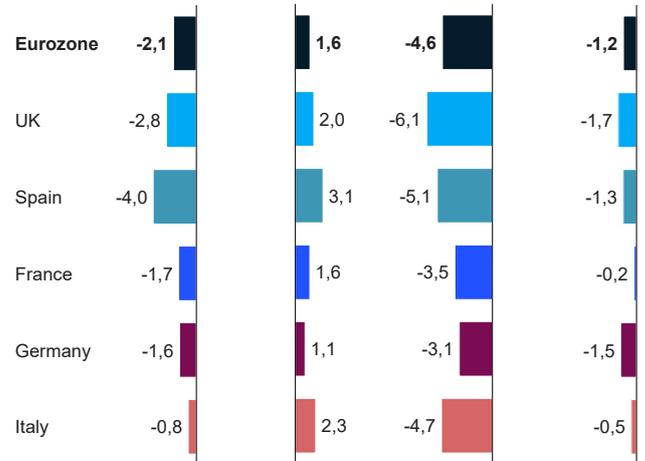
Exhibit 1

Consumer confidence continues to fall, and is below levels seen during the pandemic

Consumer confidence, Europe
Index, monthly



Change, %
Dec 19-Dec 20 **Change, %**
Dec 20-Dec 21 **Change, %**
Dec 21-Jun 22 **Change, %**
Jun 22-Sept 22



Source: OECD Consumer Confidence Index (CCI), as of 28th October 2022 (or downloaded/retrived 28th October 2022)

confidence in a post-crisis recovery, compared to an average of 14 percent across age groups⁸.

Net intent to purchase in footwear, apparel, and the sports and outdoors category has continuously fallen over the course of 2022 (Exhibit 2). Furthermore, consumers are likely to reduce their sporting goods spending over the coming period. More than 50 percent of consumers say they will buy fewer items, while about 20 percent say they will trade down to less expensive brands⁹.

Our expectation for an upcoming dip is reinforced by recent demand dynamics, which saw peaks in 2021 and the first half of 2022 (with many purchases supported by economic stimulus). After an exceptional performance during the pandemic, durable goods for individual private use, such as sports equipment, are likely to be hit hardest. Pressure on performance is expected to be unavoidable.

“When we look at spring 2023, we are concerned.”

— Rakhil Hirdaramani, Director, Hirdaramani Group

⁸ Source: McKinsey & Company Europe Consumer Pulse Survey, 9/23–10/2/2022, n = 5,156 (France, Germany, Italy, Spain, UK), sampled to match European general population 18+ years

“I think we all probably feel that volatility is persistent and change is certain.”

— Ann Miller, EVP, Chief Legal Officer, Nike

One powerful factor in the trajectory of demand will be central bank interest rates, which have impact borrowing and mortgage costs. Higher rates over the course of 2023 will further compress consumer spending on discretionary items. At the same time, sporting goods companies will see their cost of capital rising. Highly-leveraged businesses will feel the most pain and may face

difficult choices and a squeeze on investment plans.

Learning from previous crises

Previous crises have revealed strategies that have enabled some companies to be more resilient than others. Businesses in the top quartile of total return to shareholders protect revenues and margins by taking a holistic approach to managing through

adversity. That means embracing top-line and bottom-line levers, and being willing to assess a range of alternatives that do not put demand at risk. Resilient companies tend to move fast and hard on productivity, preserving their capacity to grow. They focus on cost of goods sold (COGS) reductions to boost efficiency. Moreover, they tend to deleverage heading into downturns, for example, through divestment. They then normalize their leverage ratios as the recovery accelerates, allowing them to re-invest in growth.

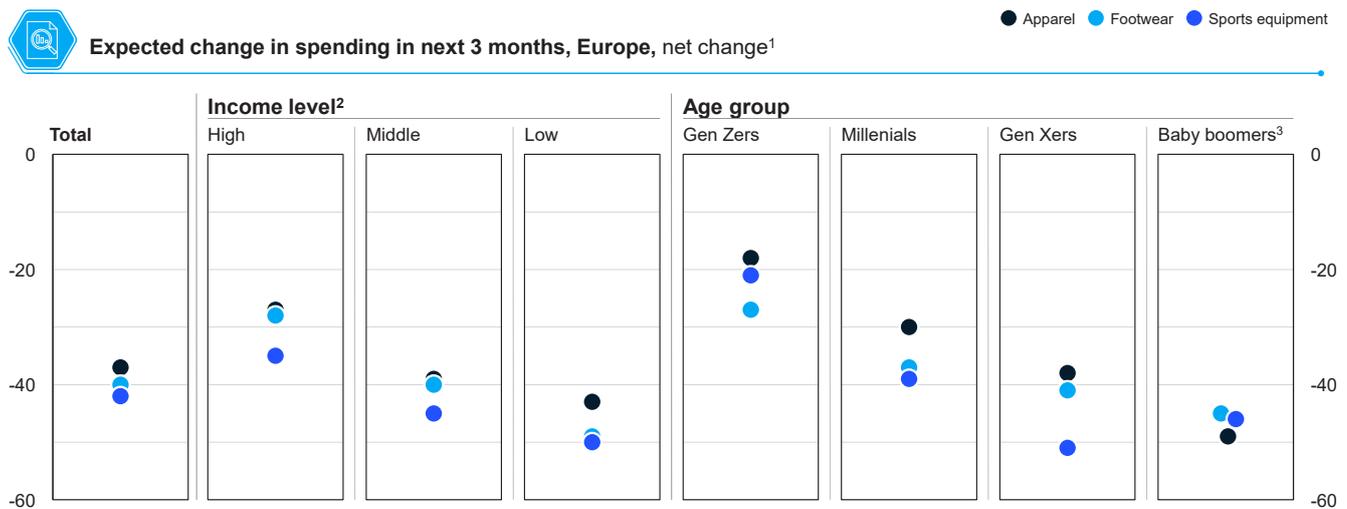
In terms of total returns to share holders, resilient companies in the ten years after the 2007-2008 financial crisis outperformed their non-resilient peers by 277 basis points⁹.

How should the industry respond?

Sporting goods companies must develop strategies to help them navigate the current economic environment. Raising prices is not an antidote to lower demand—especially given the wide availability of more affordable options. In an inflationary context, a holistic approach will encompass five key action areas:

Exhibit 2

Consumer expect to reduce spending; especially low-income groups and older generations



1. Net change is calculated by subtracting the % of respondents stating they expect to decrease spend from the % of respondents stating they expect to increase spend in the category.
 2. Low income = <25,000; middle income = 25,000–50,000; high income = >50,000. Income brackets use euros for France, Germany, Italy, Spain; for UK, the same brackets were used with pounds.
 3. Includes silent generation.
 Source: McKinsey & Company Europe Consumer Pulse Survey, 9/23–10/2/2022, n = 5,156 (France, Germany, Italy, Spain, UK), sampled to match European general population 18+ years

⁹ Source: McKinsey Analysis

Working on smart pricing and channel management: Data and analytics, for example relating to price elasticity and competitor offerings, can inform flexible pricing strategies and revenue management to protect net margins and limit the impact of volatility. Effective implementation can lead to a 5-15 percent revenue boost.

Resetting return on investment: Decision makers should conduct a top-down review of efficiency by channel and SKU to invest for growth. We estimate this could lead to a 10-20 percent saving in marketing budgets and enhanced return on investment. In a reality where cash and capital are not as available as previously, a more rigorous approach to investment prioritization and capital allocation is critical.

Strengthening brand communications: Communications should be optimized and refocused on the core value proposition. Successful implementation can lead to a 2-5 percent revenue uplift.

Building supply chain resilience: Supply chain resilience needs to be

increased through fail-safes and right-shoring. However, both are inflationary, so they need to be combined with next-generation levers to optimize the cost base.

Fostering next-generation organization productivity: An agile approach and innovations such as robotic process automation can lead to longer-term savings. Companies could review warehousing and transportation costs to unlock productivity levers, recover transportation costs as the market slows, and review facilities networks.

Optimizing finance: Companies could focus on freeing up cash and exploring divestments and acquisitions.

Through these commercial, operational, and financial levers, companies can get a grip on recessionary impacts, shape their business models, and position for a speedy return to growth. The key for decision-makers will be to manage these priorities based on their unique circumstances, while embracing a positive lens that builds competitive advantage.

“I believe it will take some time for demand and supply to right itself, especially as I suspect the economic conditions may well continue to worsen as we go into 2023, with impacts on consumer confidence.”

— Colin Browne, Interim President and Chief Executive Officer, Under Armour

US - Between a rock and a hard place

As the post-COVID recovery fades, sporting goods companies face renewed challenges from the impacts of inflation and slowing economic growth. Tough times are ahead, with the exception of a few bright spots.







Matt Powell is a Senior Sports Industry Advisor for The NPD Group and advises senior executives of athletic retailers and brands. He has 45+ years in the Retail industry and 30+ years in the Sporting Goods industry, where he worked for 20+ years as industry analyst.

Sporting goods companies are stuck on an economic rollercoaster, amid swings in performance that are creating both strategic and operational challenges. After a post-COVID recovery in which some companies surpassed pre-pandemic levels of activity, the past few months have presented renewed challenges, amid faster inflation, higher interest rates, and continuing supply chain disruption. In the US, unit sales were 4-8 percent below 2021 levels in the first nine months of 2022, and the impact on revenues was not offset by higher averaging selling prices (ASP) (Exhibit 3).

In planning for the current period, brands were blindsided by the war in Ukraine and the wave of inflation that has swept through the global economy. Many were distracted by supply chain bottlenecks, to which they responded by ramping up orders. When that stock eventually arrived, it coincided with a fall in demand, leading to widespread overstocking. While 2022 performance in aggregate remained ahead of 2019, the challenge for industry participants was to balance multiple dynamics in the context of an economy that appeared set to remain under pressure.

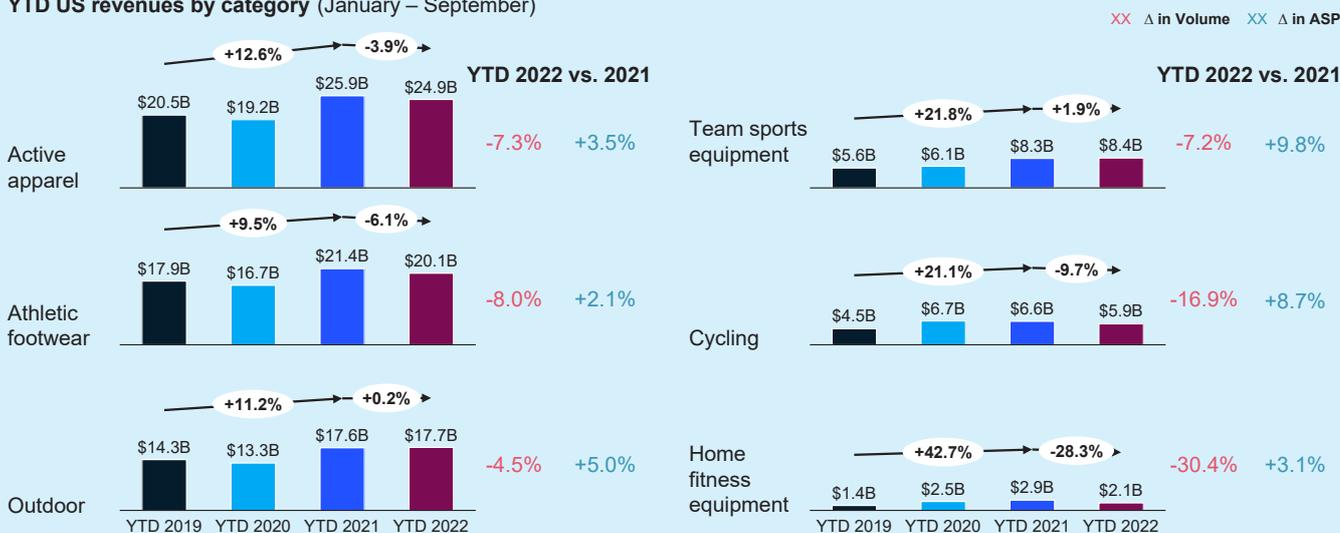
While the macro impacts of the current environment played out across segments, individual category performance varied considerably. Here we analyze the performance of various sub-categories in the US:

Athletic footwear and sportswear posted a strong performance in 2021, after seeing more than 10 percent growth (CAGR) between 2019 and 2021. However, growth stalled in 2022 as economic pressures led to declines in consumer demand. In addition, the continuing move to direct-to-consumer distribution failed to pay off for some brands. Conservative assortments, meanwhile, reflected a commercial deficit that made growth even more challenging. And to reduce stock, brands focused increasingly on promotions to support sales.

Exhibit 3

A decline in US units sold was not offset by rising average selling prices*

YTD US revenues by category (January – September)



Year-to-Date = January – September - Excludes Fashion categories. Each category leverages a different data sources of sales data
 Source: The NPD Group/Retail Tracking Service

*Note: this chart has been adjusted vs. an incorrect version in the printed copy

“After a post-COVID recovery [...] the past few months have presented renewed challenges, amid faster inflation, higher interest rates, and continuing supply chain disruption.”

- **Sportswear** brands reported an about 4 percent decline in revenues. They saw a 7.3 percent fall in unit volumes that was only partially offset by a 3.5 percent ASP rise¹⁰. Still, this was in the context of a 22 percent revenue jump compared with pre-pandemic 2019. The worst performing sub-categories were swimwear and sports bras, seeing 12 and 11 percent revenue declines respectively, while sweatshirts were strongest performing with a 7 percent revenue gain.
- **Athletic footwear** posted a 6 percent revenue decline, albeit against the background of a 13 percent rise from the pre-pandemic period. Units sold fell by 8 percent, while ASP rose by 2 percent. The best-performing sub-categories were soccer, which saw a 13 percent revenue gain versus 2021, and walking, where revenues rose 8 percent. Over the slightly longer term, price rises in some sub-categories have been significant. Men’s running shoes, for example, saw rises of 29 percent in 2022, compared with 2020.

The outdoor category bucked the negative trend, reporting 2022 revenues 0.2 percent higher than the previous year, against the background of 11 percent growth from 2019 to 2021 (Exhibit 4). Revenues were 24 percent higher in 2022 than pre-pandemic, even as units sold fell by 4.5 percent and ASP rose 5 percent. Growing sub-categories were apparel and accessories at 3 percent and 5 percent respectively, while equipment fell 4 percent and footwear declined 3 percent. The fact that consumers have been feeling safer doing activities outside has been a general boost for outdoor categories to the detriment of indoor focused sports like swimming, in some cases also linked to the closure of facilities, for example due to rising electricity costs. In the US, outdoor activities remained mainly focused on “backyard” themes, supporting categories such as camping equipment.

¹⁰ 2022 numbers in this chapter refer to first three quarters performance versus the same period in 2021, 2020, and 2019 from NPD Retail Tracking Service. The data does not include direct-to-consumer brands or vertical brands

“The 'one and done' nature of certain categories is slowing down sales after peak demand years”

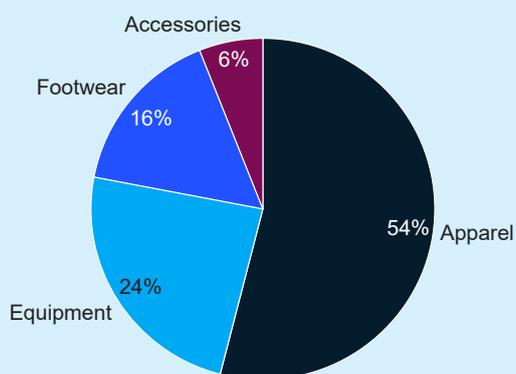
Equipment categories saw more modest gains, or declines, in 2022, after record years in 2020 and 2021. This reflected the fact that most equipment is bought for the long term (the 'one and done' phenomenon), militating against high levels of repeat business. Still, 2019-2021 growth (CAGR) was more than 20 percent, as the category expanded faster than apparel or footwear.

- **Team sports equipment** posted a slightly positive performance in 2022, with a 2 percent gain in revenues mainly driven by price increases. Units sold fell by 7 percent, while ASP rose by 10 percent. Compared with the pre-pandemic period, revenues were 15 percent higher. The best-performing sub-categories were Lacrosse, in which revenues were 27 percent higher than in 2021, racket sports, driven by Pickleball, where revenues were 13 percent higher, and soccer, where income was up 10 percent.
- **Cycling** revenues fell 10 percent compared with 2021, after 20 percent growth in 2019 to 2021. Again, however, 2022 revenues were well in advance of the pre-pandemic period, with an uplift of 32 percent. Units sold decreased by 17 percent in 2022, while ASP rose by 9 percent. The best-performing sub-categories were e-bikes, in which revenues rose 16 percent compared with 2021, amid 400 percent growth since before the pandemic (Exhibit 5). We expect strong performance in e-bikes to continue, in part because growth is coming from a long-awaited structural shift

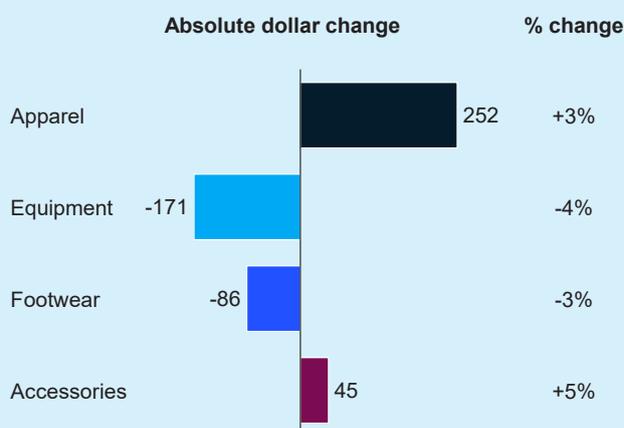
Exhibit 4

The outdoors sector performed slightly better in 2022, albeit with mixed results across sub-segments

US outdoor industry split by subcategory, % of total sales volumes

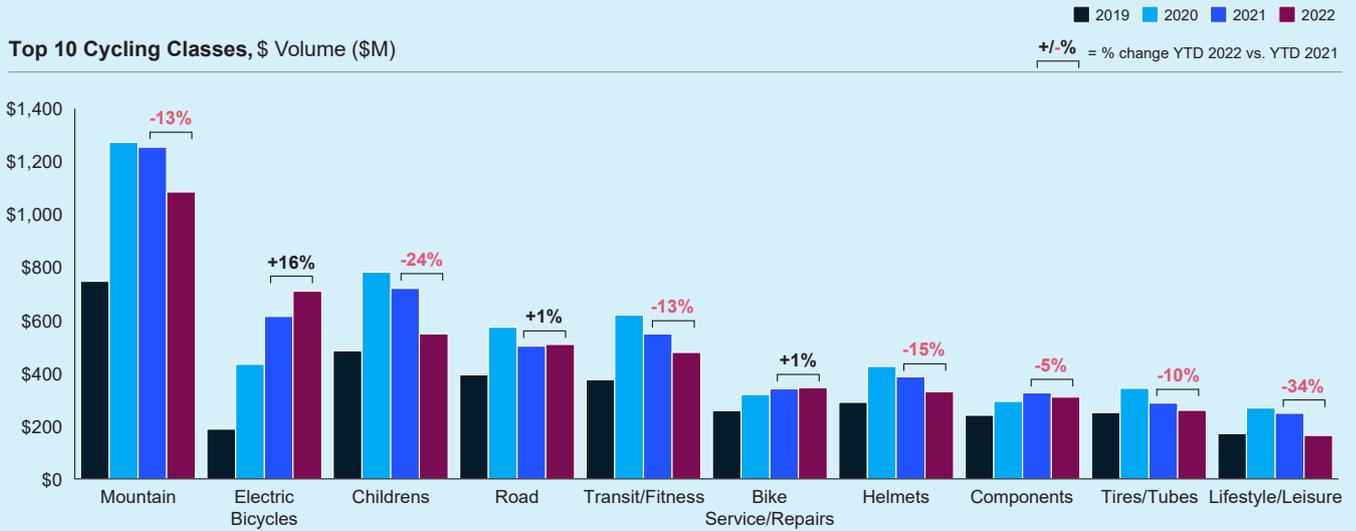


Dollar change YTD 2022 vs. YTD 2021



Year-to-Date = January – September - Excludes Fashion Categories. Each category leverages a different data sources of sales data
Source: The NPD Group/Retail Tracking Service

E-bikes were the exception to a broader cycling category decline



Year-to-Date = January – September - Excludes Fashion Categories. Each category leverages a different data sources of sales data
 Source: The NPD Group/Retail Tracking Service

(partly the result of relatively high prices that are now starting to fall) and because supply chain challenges in 2021 are yet to fully flush through the system. Indeed, supply chain bottlenecks may continue to constrain opening price performance, while ‘one and done’ may also have an impact in the medium term, offset by demand for aftersales services

- **Fitness equipment** struggled in 2022 with a 28 percent decline in revenues due to consumers returning to gyms, and due to the ‘one and done’ nature of the category. The change followed 40 percent growth in 2019-2021 category. Still, revenues were a solid 46 percent higher than in the pre-pandemic period. Units sold fell by 30 percent while ASP rose by 3 percent.

Given the mixed performance of sporting goods companies, and the likelihood of continuing challenges, the massive industry overhang will probably continue into 2023, amid an uncertain growth trajectory. On the other hand, the trend toward healthier lifestyles is well established¹¹, and the direct-to-consumer juggernaut is set to remain in place, providing cost and engagement upsides for companies that execute successfully. Moreover, e-commerce is not going anywhere, creating efficiencies and supporting data-driven business models. Finally, niche categories such as e-bikes and pickleball (paddleball) offer promise. The key for decisions makers will be to strategically assess these dynamics and selectively reset to take advantage.

¹¹ For a broader perspective on global physical activity levels, please read the dedicated section in our Foreword

NPD is a global market information company offering data, industry expertise, and prescriptive analytics to help our clients understand today’s retail landscape and prepare for the future. Over 2,000 companies worldwide rely on us to help them measure, predict, and improve performance across all channels, including brick-and-mortar, e-commerce, and B2B. We have services in 21 countries worldwide, with operations spanning the Americas, Europe, and APAC. Practice areas include apparel, appliances, automotive, beauty, books, B2B technology, consumer technology, e-commerce, fashion accessories, food consumption, foodservice, footwear, home, home improvement, juvenile products, media entertainment, mobile, office supplies, retail, sports, toys, and video games.

China's long horizons

Despite short-term challenges, the outlook for the sporting goods industry in China is positive, amid rising interest in well-being and a strong association between sportswear and fashion. However, competition is intensifying and the need for real differentiation is increasing.





Declining consumer confidence and COVID-related headwinds have put the Chinese sporting goods market under pressure in 2022, curtailing a strong run of growth. However, robust underlying demand and a deepening focus on healthy lifestyles, at least among urban populations¹², suggest companies that engage successfully will continue to perform in the years ahead.

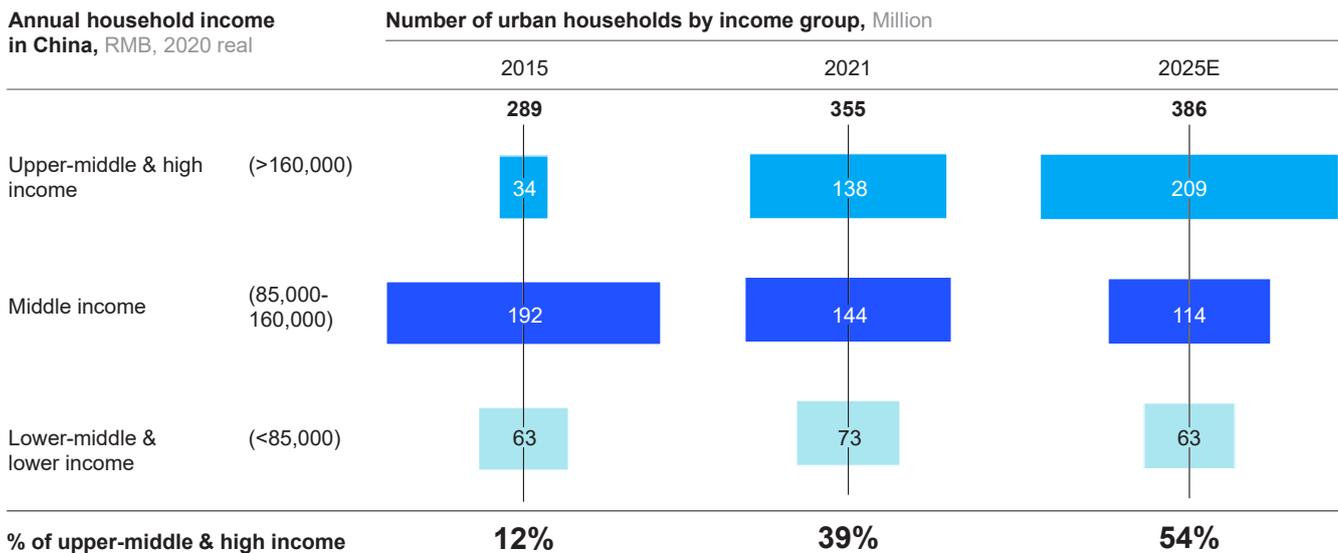
In August 2022, just 49 percent of Chinese consumers described themselves as optimistic, the lowest level since at least 2015 and far below the 67 percent reported in October 2021¹³. The key driver of the change was the COVID-19 pandemic, which continued to cause high levels of disruption under China's dynamic zero-COVID policy. As a result, the market's flat year-to-date performance in 2022 stood in stark contrast to double-digit expansion in previous years¹⁴. High-

income groups still had an appetite for spending, but to a lesser extent than in 2019, our 2023 China Consumer Report shows. Middle-income groups were feeling the pressure, with only 17 percent having increased their spending by at least 5 percent in 2022 (compared with 31 percent in 2019).

Despite these headwinds, several factors point to resilient fundamentals. The middle-class demographic continues to expand, with 39 percent of households categorized as upper-middle and high income in 2021, compared with 12 percent in 2015 (Exhibit 6)¹⁵. Indeed, in Tier 1 cities, we predict sporting goods spending will closely mirror spending in many leading western economies by 2025¹⁶. This surge in wealthier households has created millions of new consumers for sporting goods brands, fueled by a growing appetite for real sports

Exhibit 6

The growth of China's upper-middle and high income groups will fuel demand



Source: MGI Insights China macro model

¹² For a broader perspective on global physical activity levels, please read the dedicated section in our Foreword

¹³ Source: NBS, McKinsey Global Institute

¹⁴ Source: BigOne Small data, FashionScope

¹⁵ Source: McKinsey Global Institute

¹⁶ Source: FashionScope, McKinsey Global Institute

experiences, alongside sports fashion and athleisure.

By 2025, we expect 54 percent of households will occupy the upper-middle income and high income brackets. Given this trajectory, we predict single-digit expansion in the sporting goods market up to 2025.

Four fundamental trends

Aside from demographics, four fundamental trends suggest the Chinese sporting goods market is fighting fit for the longer term.

1. Government support promoting the expansion of the sports industry

There is strong government support for healthy lifestyles under the “Fitness for All” program¹⁷. This is a key element of the national agenda, which aims to create one of the world’s largest sporting industries by 2025 and a RMB5 trillion (\$700 billion) value chain¹⁸. Progress can be seen in the doubling of public sports facilities over the past five years, with “sports” now third in terms of time spent in school¹⁹, after Chinese and mathematics.

Alongside policy efforts, China has become an increasingly important hub for international sports events, including the 2022 Winter Olympics and the 2022 Hangzhou Asian Games²⁰. National competitions have also flourished. In marathons, for example, the number of both events

and participants has soared— from 22 events with 0.4 million runners in 2011 to 1,828 events with 7 million runners in 2019²¹.

2. A new generation of health seekers – especially women

A fundamental growth driver is consumer demand for a more premium lifestyle. The middle class is much more focused on health than previous generations²² and increasingly desires quality products and experiences, with greater emphasis on physical and mental health. Amid the rise of the ‘she economy’²³, women have become more body confident²⁴ and more willing to express themselves through their purchasing decisions. Women engage in fitness activities 1.25 times more frequently than men on average, and spend 15-20 percent more on sports and fitness²⁵.

3. Sport is a bigger part of people’s daily lives

Interest in sport has surged over the recent period. For example, the 2022 soccer World Cup topped search engine activity while it was being played. Early in the tournament, one match accounted for nine of 10 hot topics on Sina Weibo²⁶. In parallel, more and more people are taking part in sports such as soccer and running. Tmall²⁷ sales of small and mid-sized home fitness equipment rose by 50 percent from 2019 to 2021,

¹⁷ For a broader perspective on global physical activity levels, please read the dedicated section in our Foreword

¹⁸ Source: Fitness for all (全民健身), China national development and reform commission; Nov 5 2021

¹⁹ Per guidance from the Ministry of Education of China, starting Sep 2022, physical education is required to account for 10-11% of time (3-4 hours per week) in 9-year compulsory education (Avg. age between 7 and 16)

²⁰ Currently delayed to 2023 Sep due to COVID-19

²¹ Source: China Marathon Big Data Analytics Report 2019

²² For a broader perspective on global physical activity levels, please read the dedicated section in our Foreword

²³ A term coined by China’s education ministry in 2007, meaning the female-targeted market

²⁴ Source: China Daily ‘Women push against body shaming’ Jun 22 2021

²⁵ Source: Qianzhan Research Institute, Aurora Big Data, CBNDData, China Sporting Goods Industry Federation “2020 Fitness Behavior and Consumption Research Report”

²⁶ Source: Weibo, November 2022

²⁷ Leading B2C e-commerce platform operated by Alibaba

supported by more than 60,000 registered fitness communities in Shanghai alone^{28,29}.

The surge in sports participation is reflected in social media activity. One sports influencer on the Douyin platform saw a 10 million rise in followers in a single day, after live-streaming a fitness course. Professional athletes such as Winter Olympic medalist Gu Ailing are increasingly among the stars of the current generation of celebrities.

4. Niche is the new mainstream.

A notable recent trend has been rising interest in niche sports such as skiing, surfing, hiking, rock climbing, and road cycling. On Tmall, the ski category saw an about 70 percent rise in GMV from 2019 to 2022³⁰. Keyword search analysis also reveals a wave of enthusiasm for activities such as frisbee and paddle board, supported by a five- to six-fold rise in publications on the RED platform.

In parallel, more consumers are discovering the joys of back-to-nature and the outdoors. Camping-related online keyword searches rose more than seven-fold in 2022, indicating surging interest in activities such as traditional camping holidays and city glamping. Tmall sales of camping equipment rose almost 30 percent annually from 2019 to 2022³⁰.

A competitive playing field

Despite solid market fundamentals, competition in the Chinese sporting goods market is intense, with rising numbers of players seeking to establish themselves and expand market share. In a highly dynamic environment, a range of distinct player types are emerging.

Probably the most resilient market participants are prominent local players such as Anta and Li-Ning. These have piggy-backed on events such as the Olympics to build market share, and have capitalized on consumer support

for local brands. Overall, market sources point to a rise in preference for local over international brands; One report found that the proportion of consumers preferring local brands rose about 1.5 times from 2016 to 2020³¹. This suggests consumers are becoming less willing to pay a premium for international brands, amid a perception that the difference in brand value is limited. Indeed, 54 percent of consumers say that local-brand sports shoes are more suitable for Chinese consumers, compared with 18 percent that say multinational brands are more suitable. In addition, 56 percent say that local sports brand apparel offers greater value for money, compared with 17 percent saying the same of multinational brand apparel (Exhibit 7).

Local brands have also shown themselves to be agile, responding more nimbly to consumers' needs and harnessing emerging trends faster than global players. Domestic players also often have an edge in navigating a dynamic digital ecosystem. In one example, local players have quickly expanded their live-streaming capabilities, responding to a rise in content-driven social commerce through platforms such as Douyin (TikTok). During the Double 11 shopping festival, both Anta and Fila hit 2022 record sales on Douyin (above RMB3 million (\$420,000) on Nov 11) through an average of four live streams per day. By contrast, some international brands' Douyin accounts do not support live streaming.

Despite signs they may be losing their edge to specialized players and local brands, multinational brands have seen strong growth in recent years, increasing their share between 2018 to 2021. Indeed, some global players have found success by tailoring their approaches to local demand. One formula has been to offer a technical assortment focused on niche sports. Companies such as lululemon, On,

²⁸ Source: BigOne Tmall data

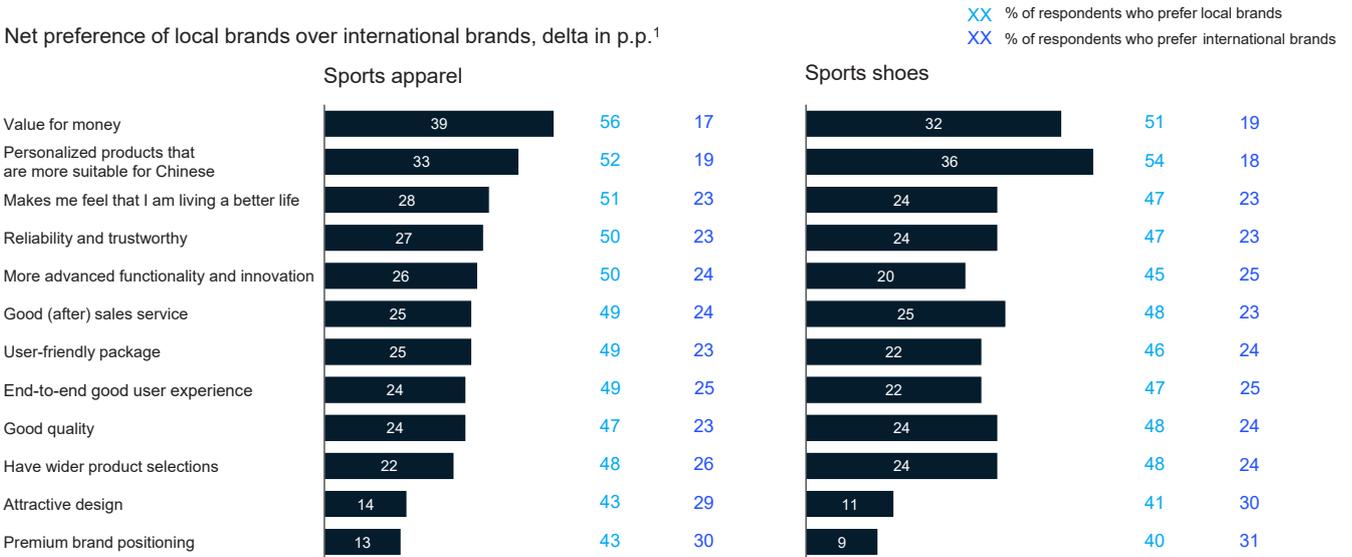
²⁹ Source: Shanghai "Fitness for all" report 2022

³⁰ Source: BigOne Tmall data

³¹ Source: Fidelity International and China Market Research Group

Exhibit 7

Local brands are preferred, amid value for money for sports apparel and personalized products for sports shoes



1. Net preference of local brands is calculated by the sum of % of responses who think local brands are extremely better/better than foreign brands, minus the sum of % of responses who think foreign brands are extremely better/better than local brands (n=1098)

Source: 2023 McKinsey China Consumer Report

and The North Face have grown through this approach, signaling that outperformance is possible through strategic prioritization, products, and demonstrable expertise.

Rising female consumption represents another opportunity, with lululemon in China among those tapping into the trend. China was one of the first markets in which lululemon debuted its new footwear brand, designed as a “women-first” proposition³².

These dynamics give sporting goods companies plenty of food for thought on how and where to play. But looking through the current economic situation, the outlook in aggregate remains positive.

In spring 2023, we will publish a comprehensive China deep dive examining the key trends shaping priorities for sporting goods brands and retailers.

³² <https://jingdaily.com/the-china-ambition-behind-lululemons-footwear-launch/> (November 2022)

Colin Browne, Interim President and Chief Executive Officer, Under Armour



Colin, thank you for taking the time. Looking back at 2022, what were some of the main trends you have observed, what changed from prior years, and what is here to stay for 2023?

It has definitely been an interesting and challenging few years, with 2022 being the culmination of them all. In 2020, we went into a full lockdown and saw significant revenue headwinds. As we came into 2021, we saw huge pent-up demand, and now in 2022, we are living with the implications of the two previous years. We are currently seeing an increasingly large amount of inventory, which has landed at the same time as softening demand, due to a broader economic environment that has started to deteriorate. I believe it will take some time for demand and supply to right itself, especially as I suspect the economic conditions may continue to worsen as we go into 2023, with impacts on consumer confidence. Beyond this dip, I do think the sports and fitness industry is going to continue to be incredibly relevant going forward. Demand for sportswear, and more broadly for the comfort and convenience that comes with

sportswear and a healthy lifestyle, will continue to be important, and I believe we at Under Armour are well positioned to navigate through the choppy waters that lie ahead.

You mentioned impacted consumer confidence and softening demand. Do you see any differences here between different types of consumers?

I think we will see some polarization: People who are financially more stable will be less concerned about continuing to buy sporting goods. But, as is common during a recession, people with lower incomes will be more challenged. We need to make sure that we are offering products that operate across the spectrum.

What measures has Under Armour already taken in light of these economic challenges?

We spent a lot of time thinking about how we ensure that we continue to drive value to our stakeholders. From a business point of view, productivity is an incredibly important metric. That doesn't just mean saving money, but also doing more with less and in more productive ways. It involves being

really thoughtful on SKU rationalization and making sure that you have a good understanding of what your product will do for each consumer.

If we look at different sports categories you play in, how have these developed over recent years and what is your expectation going forward?

On a category level, running has been immensely important in the past. And we see this trend continuing, because it is an activity that people can do without needing to go the gym. Even if we experience a recession in the next 18 months, you can always go outside and run.

We also have a smaller outdoor business, which has grown very quickly in the past couple of years, and I see no reason why it would slow down. Again, in a difficult recessionary environment, people will still have the opportunity to spend more time outside, and so I think it will continue to be an important category for us.

We also see good growth with our basketball business, where we have Stephen Curry as a core athlete. In North America, a lot of our business

“The idea of branding and being really clear on who you are, and what you stand for as a brand, will continue to be important in building meaningful, individual relationships with consumers.”

is based on American football and baseball, primarily. We are continuing to outfit team sport athletes and are really working to include them within our brand.

We have also seen major growth over the past couple of years in the golf category. Golf is one of the sports that I think is becoming younger, and more relevant, and is also opening up from a gender perspective.

Looking forward, what areas are you are planning to focus on in 2023?

We will continue to refine our offering, and make sure we are providing the right products for athletes, as well as being considerate and thoughtful in how we do that. We are also extending our engagement model with consumers, which we call “the journey to compete”. Historically, we split this journey into three different stages, which were training, competing, and recovering. Now we have added a fourth stage, which we call “live”. This builds on the idea of balance and how to include wellness into your life 24/7, as opposed to just when you exercise. That’s a pivot that I think we are going to see more broadly in society.

One last question. Looking at the macro trends in the industry in the next three to five years, what do you think are the biggest opportunities?

I think we will continue to see consumers focus on health, fitness, wellness, and sports. We are undoubtedly in a market that will continue to grow. I also think that the idea of branding and being really clear on who you are, and what you stand for as a brand, will continue to be important in building meaningful, individual relationships with consumers. In addition, sustainability and circularity are clearly going to be big drivers. We published our sustainability report last quarter, and we are incredibly excited about making a lot of progress there. On circularity, I think the industry needs to come together to figure out solutions. We have a responsibility, not only as individual brands but also as leaders.

Tim Boyle, Chief Executive Officer, Columbia Sportswear Company



Dear Tim, thank you very much for your time. How do you look at the Sporting Goods market at the moment?

Arguably, the number of sporting goods brands has reached an unsustainable level. In China alone, we have 700 branded competitors. Therefore, I think the main challenge is distinguishing your brand and offering your customers a truly unique value proposition.

There's a famous marketing executive who just recently passed away here in Portland named Dan Wieden, and he basically said, "a brand is a promise." So, when people buy your product, they expect that you fulfill a promise beyond the product's features. It's about the experience when people wear a particular brand: what it reflects and how it makes them feel.

How do you see Columbia positioned in the world of Outdoor?

We believe we're an authentic brand. We're not in the Outdoor space because the category is hot but because this is who we are. When we describe who we are in more detail, we use some keywords:

The first is "American." It's comparable to when people think about a German car

company like Mercedes. So, when we go to market, we try to continue to be known as an American company. It's actually very helpful in Europe, South America and in China and Japan, and around the world as it gives us a certain identity.

Furthermore, we obviously are "Outdoor" and think of ourselves as being in the "Active Outdoor" business. We're not making blankets to be used up. We make stuff to be used actively.

Another keyword we use is "Value." This doesn't mean inexpensive, but it means that we pride ourselves on being able to provide high-quality merchandise at reasonable prices.

So, we see ourselves as an American Active Outdoor Company with Great Value.

Columbia has significantly benefitted from a real boom in everything "Outdoor" in the last few years. How do you see this trend evolving?

I think we need to look back more than two years. It's hard to pinpoint precisely when the outdoor boom started. We've been in business since 1938 and have grown steadily. Obviously, it's grown much more rapidly in the last 18 to 24 months than it had in the previous

period, as it coincided with the onset of the pandemic, the various lockdowns around the globe, and people being more comfortable outside.

Furthermore, Outdoor is also becoming a lifestyle. As you know, the percentage of running shoes sold that are used for running is not high. And I would think the same is true for outdoor apparel. It's designed for abuse in extreme conditions, but the chances it's being worn for everyday wear are increasingly high.

How do you see outdoor growing in parts of the world where it is still a relatively new trend, like China

Indeed, historically speaking, the Outdoor business in China is relatively new – for example, if you compare it to Japan, where we have had an outdoor business for more than 40 years. When we first began doing business in China, we introduced ourselves as being in the outdoor business, and people didn't understand what that meant. People thought, "You mean you're a farmer outdoors?". Obviously, we have seen a remarkable transformation in this regard, and nowadays, Outdoor is a major category in China with fantastic growth outlooks.

At Columbia, you have a portfolio of multiple brands. How do you drive synergies in such a portfolio of sportswear companies?

The success formula for our brands is creative vision paired with a well-oiled machine.

Excellent leadership and creative vision are critical elements for each brand's success. We've been very fortunate to have genuinely distinct individuals leading the businesses that we've purchased and built who have almost a religious approach. For example, somebody like Yvon Chouinard injects his personality into his products. So, once you have one of these individuals, you have to bolt it onto a machine that delivers to make sure they can focus on what they do best, and everything is in place to make them successful.

This machine is also essential, of course. It's about branding, marketing, getting the product to market, incl. distribution and logistics, and manufacturing efficiency. But none of that will make you successful if you don't start with the first component that gives you authentic differentiation.

That may be a somewhat more simplistic description, but in a very general way is how we've approached our multifaceted business.

A topic that is top of mind for many consumers is the sustainability of their sporting goods purchases. How do you see this trend, and how do you approach it at Columbia?

There is no question that it's important and top of mind, but it is still tricky to showcase to the consumers everything

we do. We almost don't talk about it ever, primarily because there's no point of differentiation in discussing that topic. It's most outdoor companies' primary message, so how can we possibly be different if we talk about the same message as everybody else? However, that doesn't stop us from heavily investing in this area out of a feeling of responsibility. For example, we created an entire product category in rainwear that uses a fabric we developed in-house that doesn't require a PFAS application. However, explaining that to consumers is a real challenge. It's complex, and consumers don't necessarily react to complicated messaging. Maybe we all, including our retail partners, need to do a better job of making sustainability visible and experienceable at the point of purchase.

This could become a real issue for the industry. Many sporting goods companies have set ambitious CO₂ reduction targets in absolute terms. However, achieving them is not only on the industry, but it also requires pull from the consumers. Without that, a lot of companies will have trouble reaching their targets. I believe that we cannot wait for the consumer, but we need actively push decarbonization levers that we control.

Is nearshoring a lever for decarbonization that you consider relevant – maybe even a way to de-risk supply chains further?

Quite frankly, I think the whole nearshoring and logistical advantages are mostly a myth. Making the commercials work is almost impossible.

Why, Firstly, it's so easy in Asia for these commodities. So, any advantage you find in logistics has to be so dramatic that it can overcome the cost savings in Asia.

Secondly, when you're talking specifically about outerwear, a big commodity for us, it might have 30 components. The idea that you would somehow be able to marshal those 30 components, which are frankly different in every style, in a fast way, that's just not going to happen.

I would suggest that whatever efforts would have to be put forward to nearshore a complex product category would be better expended with more thought on what the product is going to be, more investigation of market acceptance, and use of the existing established processes.

“The success formula for our brands is creative vision paired with a well-oiled machine.”

Becoming a brand super winner

Sporting goods companies are among the most effective brand builders in the world. However, as consumer expectations rise and brand relevance deepens, companies should keep brand building at the top of their agendas, applying a through-the-cycle mindset.





“Consumers’ ability to influence and push brands is stronger than ever.”

— Ann Miller, EVP, Chief Legal Officer, Nike

Leading sporting goods companies are masters of brand equity building, and of encouraging their customers to engage and transact. Nike and adidas are ranked by Interbrand in the top 100 global brands³³, while 7 of the 10 most valuable apparel brands are in the sportswear category, according to Kantar BrandZ³⁴.

The strongest brands are value creators by virtue of their brands alone. As per McKinsey's State of Fashion report, this ability has catapulted them into an elite group of 20 global fashion super-winners in terms of economic profit. On that basis, Nike is the leading fashion brand in the world, while adidas, Anta Sports, lululemon, Dicks Sporting Goods, JD Sports, and Li Ning are not far behind. There were ten top 20 sporting goods super-winners in the financial years 2019-2021, compared with three in 2018³⁵.

For consumers, brand loyalty often comes down to trust, which is closely associated with willingness to purchase. Indeed, 55 percent of global consumers, and 66 percent of Asian consumers, say that trust is a make-or-break factor: without trust, they won't buy³⁶.

In the current economic environment, customer loyalty is being tested by increasing uncertainty, so trust is

more important than ever. Brands need to adapt quickly to this changing environment and make brand building a priority. Indeed, many sporting goods companies understand this and, despite pressure to cut costs, are adding to their brand building budgets (Exhibit 8). Fifty percent plan to increase spending by more than 5 percent, WFSGI & McKinsey's latest survey shows³⁷.

Consumer sentiment is also shifting. Previously, consumers were primarily driven by factors such as functionality, design, and price. Now, brand is increasingly important, or even dominant, in the purchasing decision. A typical customer looking to buy a pair of trainers, for example, in the past considered design and functionality first and brand second; nowadays, the first decision is which brand reflects and amplifies the customer's identity.

Some brands are taking brand building a step further, considering new ways to engage with consumers and influence their desire to purchase. These reassessments often catalyze bold moves to boost brand profile and create an ecosystem that will support both acquiring and retaining customers. Leading companies leverage five levers to build a strong brand:

³³ Source: Interbrand Best Global Brands 2022

³⁴ Source: Kantar BrandZ Top 10 Most Valuable Apparel Brands 2021

³⁵ Source: State of Fashion 2022, McKinsey & Co. and the Business of Fashion

³⁶ Source: Adobe study, July 2022

³⁷ Source: WFSGI & McKinsey Sporting goods companies survey, September 2022 (N=211)

1. The direct-to-consumer (DtC) revolution

As recently as a decade ago, wholesale distribution was the dominant business model. However, that is changing fast as DtC becomes increasingly relevant (Exhibit 9). For example, in 2012, just 17 percent of Nike’s sales were DtC. In 2022, it is 42 percent, and the company aims to get to 60 percent by 2025³⁸. Many other brands are following suit.

The starting point for a strong DtC model is a deep understanding of the consumer. Successful brands invest in integrated digital ecosystems to collect customer data and develop insights to inform the DtC strategy. A good example is Under Armour’s “Innovation idea house”, through which the company engages with consumers to gather ideas on topics such as products and innovations.

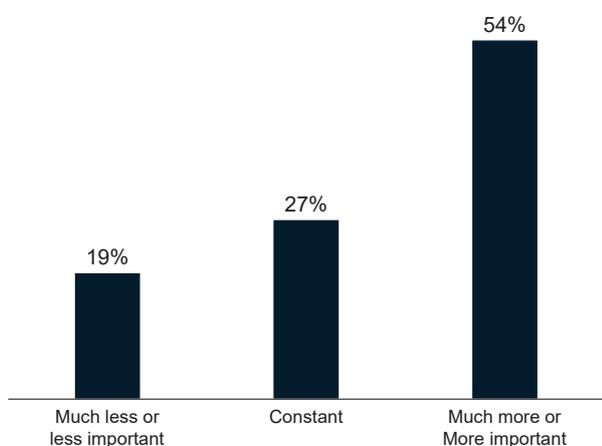
2. Collaborations with high-end fashion brands

Several highly-technical brands have joined forces with fashion businesses to broaden their appeal and tap into new audiences whose willingness to pay is often high. Tie ups between On and Loewe, Arc'teryx and Jil Sander, and The North Face and Gucci have forged winning combinations of design and craftsmanship. One impact has been to expand customer bases. Online searches for On rose 42 percent after the tie-up with Loewe was announced, and were up more than 114 percent in the first four months of 2022, according to online fashion platform Lyst³⁹. Another example is the Fjällräven-Specialized partnership, which developed a collection of functional clothing and equipment linked to cycling activities.

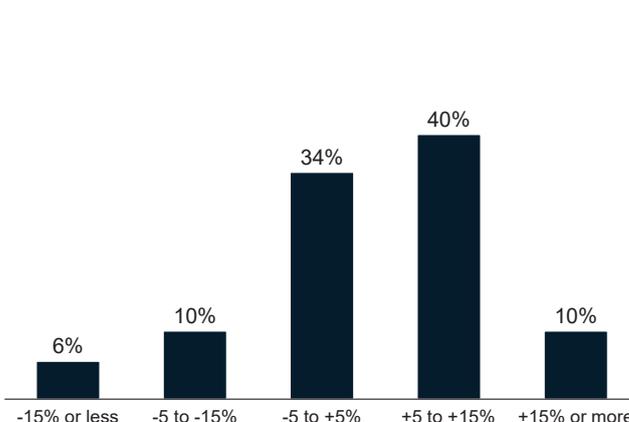
Exhibit 8

Sporting goods companies are focusing and investing more on brand

Evolution of brand relevance, % of respondents



Expected change in brand investment, % of respondents



Source: WFSGI & McKinsey Sporting good companies survey, September 2022 (N=211); In your opinion, how is the relevance of having a strong and trusted brand evolving? (n=163); How are your company’s investments on brand building evolving? (n=88)

³⁸ Source: Company reports

³⁹ Source: Company website, press releases, fashion search engine Lyst

3. The power of community

Sporting goods brands are rewriting the digital marketing playbook to create a much more prominent role for communities. With the same aim, companies are also investing in social media, affiliates, search, apps, platforms, and media networks. They are backing this up with purposeful brand stories, hero products, and personalization, alongside multiple micro-campaigns throughout the year— including across non-commercial touchpoints. Indeed, the top sports-focused digital communities, including Strava, Freeletics, and Relive, are developing customer relationships that extend far beyond the transactional.

Nike, lululemon, and Gymshark are among the brands to have been successful in fostering communities, and this has enabled them to reduce their traditional media spend. Lululemon has said that community building is core to its marketing strategy, including initiatives such as an ambassador program founded by local fitness and yoga coaches.

Finally, digital communities (“there is an app for that”) have enabled active people to be part of a group while taking part in sports that are otherwise more solitary, including hiking, cycling, and running.

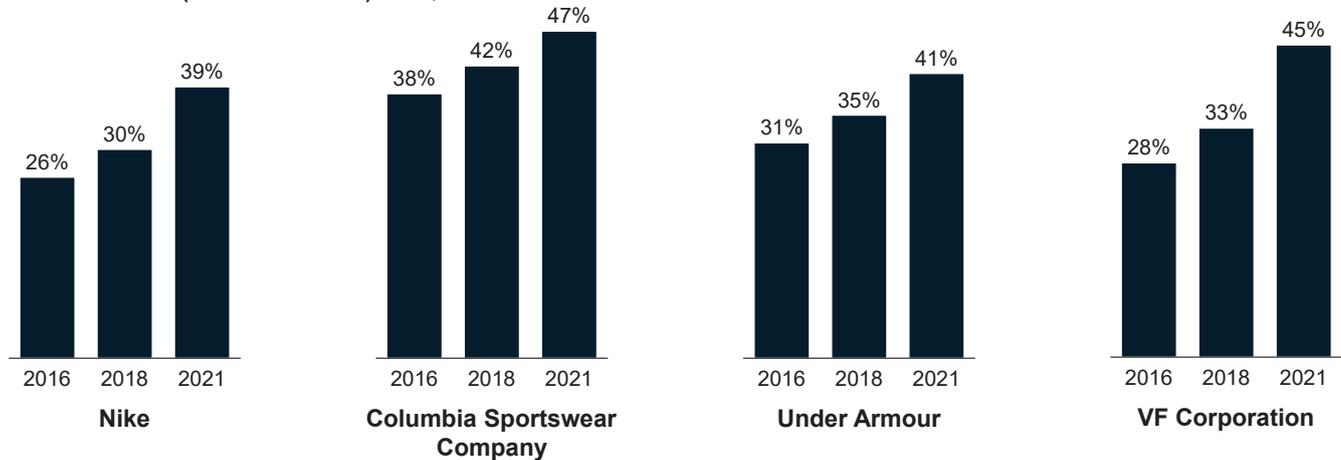
4. From celebrity endorsement to influencer marketing

Celebrity endorsement has traditionally played a significant role in sporting goods marketing, with sports stars an obvious choice to lead campaigns. And athletes are still the most trusted people when it comes to the technicalities of sportswear and equipment.

Influencer marketing plays an increasingly important role in building brand awareness and loyalty. Brands are using social media channels to boost their most significant sponsorships, often reaching new audiences through the human faces of micro-athletes. Adidas is working with 50,000 US college athlete brand ambassadors and with individual influencers such as Adriene Mishler in the yoga space, promoting an

Exhibit 9
Sporting goods players have moved to DtC in recent years

Evolution of DtC (online and offline) sales, % of total revenues



1. 2018 data for VF Corporation not available due to transitions in reporting; in 2017 DTC sales were 32%, and in 2019 33%
Source: Companies annual reports

“Leisure and lifestyle are about image and identity – finding a brand you identify with.”

– Holger Schwarting, Chairman of the Board, SPORT 2000 International

aspirational and authentic brand voice. Alo has launched a Yoga Pro program, offering discounts to instructors and building a network, while Gymshark has signed deals with influencers such as LICK and Nikki Blackketter, backed by a range of pop-up stores, world tours, and fitness meets. The company almost doubled its revenues in 2021.

Not surprisingly, the most amenable demographic to influencer marketing is Gen Z, 58 percent of which believes that influencers expose them to new products and services, compared with 23 percent of Baby boomers. McKinsey's consumer research shows that Gen Z and Millennials are influenced by social media up to 20 percent more than the general population⁴⁰.

5. Working with wholesalers and retailers

Some companies are working directly with partners to build brand equity, and many retailers now present assortments by brand rather than product category. Meanwhile, brands are seeking to expand customer loyalty in collaboration with strategic retailers. For instance, Nike signed a partnership with JD sports, Dick's,

and Zalando, by which customers purchasing Nike at the retailers enter Nike's direct customer loyalty program. In exchange, the customer experience is enhanced through new community-building events and access to exclusive products. The closer collaboration between brands and retailers represents a win-win opportunity for both sides, enabling more sophisticated and extended consumer engagement.

By transacting directly with consumers, focusing on fashion industry collaboration, and developing communities – both digital and traditional companies are developing a new vision of brand building that is tailored to the demands of the modern economy. They are backing this up with digitally-native influencer marketing and recalibrated distributor relationships. These initiatives show that brands understand that customer loyalty in a digital world is fragile, and the customer's voice is powerful. In response, the most successful brands will continuously refresh and innovate their brand strategies to ensure they remain on point.

⁴⁰ Source: McKinsey & company COVID-19 Consumer Pulse Survey, 2/25-3/1/2022, n=2160

Ann Miller, EVP, Chief Legal Officer, Nike



Dear Ann, thank you for your time. Looking back at a tumultuous 2022, what trends or events would you highlight as particularly relevant?

I think we all probably feel that volatility is persistent and change is certain. But more particularly to the sporting goods industry, we are seeing an expanded definition of sport, which is really exciting. We are seeing a trend towards wellness and mental health, and these present great opportunities to engage with consumers on new levels and help people to discover their full potential.

The role of leading brands like Nike in engaging with consumers has always been vital in this industry, but how do you see this evolving?

We have seen consumer expectations for brands going through the roof. Consumers expect you to have

a commitment to sustainability. Consumers expect you to speak out on specific issues. Consumers expect you to live your values. Consumers expect you to be relevant in their communities and committed to Diversity, Equity & Inclusion.

Some might say there are more pressures on brands. I would say there are more opportunities for brands to step up, play a more significant role, and make a difference.

Are you saying consumers have an expectation that brands deliver more than just great products?

Yes. Absolutely. At least at Nike, we do not believe consumers are just buying a product. They are buying a value proposition and our mission. When they make a purchase, they are essentially

endorsing us as a brand. And we take that very seriously. If we were merely a commodity, you would not give that type of significance to a purchase.

The pandemic has heightened those expectations because we have become much more reliant on digital and social media. So, consumers have many more opportunities to express themselves, and they have a more prominent voice. Consumers' ability to influence and push brands is stronger than ever.

And we say bring it on! We should be pushed. It should be a two-way street for us all to try to get better. In fact, if you think about Nike's mission, it is not just to offer consumers good products. Our mission is to innovate and inspire. Consumers get behind that and therefore expect it of us.

“At Nike, we do not believe consumers are just buying a product. They are buying a value proposition and our mission.”

“I think if you are issuing a press release every time a social issue emerges, your voice is not going to be differentiated. In trying to stand for everything, you stand for nothing. I believe that having discipline and really knowing who you are should guide when you choose to speak out.”

What is the right recipe for engaging with consumers, being meaningful for them, and increasing your brand relevance?

First, really know yourself. Know your brand. Know when it makes sense to step in and have a voice. But equally, know when you are not the right brand to engage. We come back to our mission and our purpose, and that always guides when, where, and how we engage in a conversation.

The danger is trying to be everything to everyone when you don't have authenticity, credibility, or a differentiated point of view. Contrast that with really knowing who you are and taking those opportunities when they are aligned with your values, aligned with your mission, aligned with your purpose. That is when you can be credible. That is when you can be authentic. And that is when consumers believe you, trust you, and will go with you on the journey.

Taking a stand also means opening yourself up to potential criticism, no?

The larger risk is that you speak out about something where you are not credible or authentic. Your consumers

are sophisticated and will call you out. They know if you are saying something that isn't true to who you are.

I think if you are issuing a press release every time a social issue emerges, your voice is not going to be differentiated. In trying to stand for everything, you stand for nothing. I believe that having discipline and really knowing who you are should guide when you choose to speak out.

If there is no unique proposition and no differentiated impact, then I urge caution. Because I think you dilute your impact, and I think you can harm your brand unintentionally by not really picking and choosing moments where you can really drive impact for consumers and communities and employees.

And the last thing I would say is knowing when not to be quiet. Knowing when you actually have a role to play, and it is unique. If you don't speak in those moments, it can do just as much harm.

This might seem complex but, in the end, it comes down to being true to yourself, and acting with both confidence and also humility.

Holger Schwarting, Chairman of the Board, SPORT 2000 International



Dear Mr. Schwarting, thank you for taking the time. As one of Europe's most prominent sports retailers, what are your biggest challenges today?

Reviewing the past couple of years, the sporting goods industry underwent major transformations but also experienced a lot of positive impacts, driven by growing sports participation and the blending of health and sports in people's minds, as well as of private life and business life.

However, we are still dealing with supply chain disruptions. We are still not getting all the orders we place with brands, either in the correct quantity or delivery time. The most significant risk for me in this regard is the Zero-COVID policy China is sticking to. It can result in lockdowns, factory closures, and quarantine regulations for business travel from one day to the next.

Of course, because of different expectations, most sports retailers are dealing with higher-than-usual inventory levels. Some retailers are even canceling specific orders to manage that higher stock level. What is counterbalancing that challenge is that prices are going up, and we ordered

at lower prices. If we cancel the order, we will then have a 10 percent higher price on the next order. So, sometimes it even makes sense to keep the orders. Overall, inventory is a challenge we can deal with.

The second major challenge is inflation and the insecurity it causes among consumers. We observe a certain amount of downtrading but, interestingly, not so much between brands. For example, instead of buying a pair of trainers that used to cost €160 but have gone up to €180, consumers look for another pair of that same brand that costs €140. They are taking a slightly lower-value product from their brand of choice. And, of course, we are seeing more customers waiting for promotions and picking up the product at a better price.

You mentioned the transformation of the industry during the past few years. Could you talk about the most important shifts for you and how you are perceiving their stickiness now that it seems we have moved out of the pandemic state with all its implications?

We saw, especially during the lockdowns, how quickly even people

who had never purchased online suddenly did so naturally. For a retail group with many retailers who were not very digitally savvy, it was a challenge to put up a system as soon as possible that made our retail offering digitally available. We managed to do it but had we failed, we would have faced grave consequences.

Since the shops reopened, the incredible ecommerce growth has slowed down. Instead, we saw a revival of brick and mortar shops. It is evident that many people like to go back to shops. They want to hold the products in their hands before buying them, and they value expertise on the sales floor.

We are seeing a new normal with a mix of digital and bricks-and-mortar. The same consumer prefers to buy a couple of tennis balls quickly online but visits the store to buy an innovative new racket. The bottom line is that we must play in both worlds and blend them into a unified customer experience. Even though we have some online pure-players in our group, our task is mainly to evolve our brick-and-mortar offerings with seamlessly integrated digital elements.

You mention that you observe consumers reducing spending but staying loyal to their chosen brands. What drives this brand loyalty – especially in these uncertain times?

Let's distinguish between sport leisure and lifestyle categories on the one hand and sports performance on the other. If people buy primarily for sports leisure, they are very brand driven. The large global brands are at a clear advantage here. They have the highest direct-to-consumer percentage and can fuel their brand heat through marketing, investments into digital touchpoints, well-known ambassadors, and even collaborations with high-end fashion brands. Leisure and lifestyle are about image and identity—finding a brand you identify with.

On the other hand, we have the more technically driven sports performance segments. Here, people buy for a specific activity, which allows small specialist brands to gain traction. Brand trust in this segment is less defined by image and identity than by the brand delivering what is needed in terms of technical features and attributes.

What will the midterm effects on the sporting goods retail landscape be? What kind of players will benefit?

I think we'll see increasing polarization. On the one hand, we will have price-driven and low-priced products that are standardized and primarily purchased online. On the other end, we will have innovative, higher-value, brick-and-mortar retailers offering the kind of expertise and experience that make a physical store visit worthwhile. I think we will see winners on both ends of this spectrum. Whoever remains in the middle will be struggling. This is true for Europe and beyond.

At SPORT 2000, we have always focused on specialization in critical categories like outdoors or running. This category expertise, in combination with strategic relationships with key brands, allows us to cater to customers who are not only driven by the lowest price.

Finally, as you and other sports retailers aim to stay ahead of the curve of consumer trends and offer that premium experience, what is the next big thing you need to master?

I think a trustworthy and impactful offering around sustainability. Sustainability has become table stakes for many consumers, as you wrote in your last report, and we need to deliver on it. And not only that; we are excited to do our part for a livable future.

At SPORT 2000, we started many years ago with an initiative called Green&Fair, where we engaged with brands on topics like fairness in production and sustainable materials. However, we were a bit ahead of the curve. At that time, not many brands had a strategy regarding these topics. This has changed in the past two or three years, and we see brands doing a lot. However, it is our job as a retailer to bring this across to consumers at the point of sale. One of our essential functions is working with brands and explaining sustainability strategies and products. Consumers today want to make sustainable choices but are faced with a vast offering of products with different and sometimes cryptic sustainability claims. The brands have a big challenge here, but at the end of the day, we are the ones who need to bring this across in a transparent way on the shop floor.

What about circular business models? Where do you, as a retailer, see the most significant potential?

Rental is where I see the highest potential for retailers like us. For example, ski rental allows reuse of a ski 30 to 40 times in the season. In Europe, 60 to 70 percent of ski sales go into rental. We've substituted sales with rental income. Of course, that is difficult for brands since their volumes have decreased, but it is a much more sustainable model.

The second area with potential is repair and service. We have much experience with that in the bicycle market. The bicycle market is a relatively high-value product, so people don't want to throw it away after two years. They

want to come back to have it serviced. However, I see this as a general trend. Products, at least by the brands we work with, are increasingly built for longer lifetimes but will also require servicing or repair to reach their longevity potential. This goes beyond equipment, by the way, and includes performance apparel.

Furthermore, in recycling, we are happy to play a collection role and can assist in shipping it back to the brands. A closed-loop recycling system for brands will not work without the stores as critical collection points, and we are glad to take on this responsibility.

Sustainability - Time to make it real





Alongside peers in many other industries, sporting goods companies face a ticking clock on sustainability. To meet their highly-aspirational targets, companies need to both accelerate decarbonization and scale circular business models. Only through a combination of these levers will they transform their businesses and reach their goals.

Across the sporting goods industry, the sustainability bandwagon is in full swing. Almost every brand has made a commitment to reduce emissions, tackle destructive environmental practices, and embrace circular business models. Most sporting goods companies are driving initiatives that go beyond CO₂ reduction, tackling dimensions across the environmental, social, and governance (ESG) challenge. Companies have published targets, made promises, and reported on their progress. However, many are still seeing rising absolute emissions, despite reducing CO₂ intensity per unit of revenue. As they plan to meet their 2030 targets, the next two to three years will be critical (Exhibit 10). To get there, many will require a strategic pivot, and a commitment to put decarbonization and circularity at the top of their agendas.

About 45 percent of sporting goods companies have announced targets to reduce greenhouse gas emissions, on

average by 50 percent. Another 40 percent plan to announce targets soon, according to WFSGI & McKinsey's latest industry survey⁴¹. Many have aligned their approaches with standards published by the Science Based Targets Initiative, meaning they are referencing pathways specified by the Paris Agreement on climate change. However, most expect absolute emissions to continue to rise until 2023/24, ahead of a rapid turnaround. There are, however, exceptions to the rule. For example, Patagonia saw its emissions fall by 39 percent between 2018 and 2021⁴².

From a global warming perspective, these trajectories are concerning. If science-based targets are missed, warming will continue on its current unsustainable path, leading to unpredictable damage to economies, societies, and ecosystems. Thus, the onus is on sporting goods companies to step up to the challenge.

To play their part, companies could prioritize action through two steps. A first priority should be to cement their decarbonization plans. This would require them to set a baseline, define an abatement curve based on the cost per ton of CO₂ and CO₂ reduction impact, and prioritize levers for decarbonization⁴³. It would then mean executing effectively on those plans.

Along the way, companies will face inevitable barriers. Low collection rates will limit the supply of recycled fibers, breakthroughs in material technology will take time, and restructuring of supply chains will be costly. Hence, companies also need to rethink business models that revolve around selling new products. That will mean ramping up efforts to encourage more resale, reuse, and recycling. Through extending product lives, they can reduce raw material use and lessen the damaging impacts of mass production.

Exhibit 10

Although the industry has started to set bold ambitions, more needs to be done to achieve GHG reduction targets

Scope 3, as of Dec. 2022, outside in

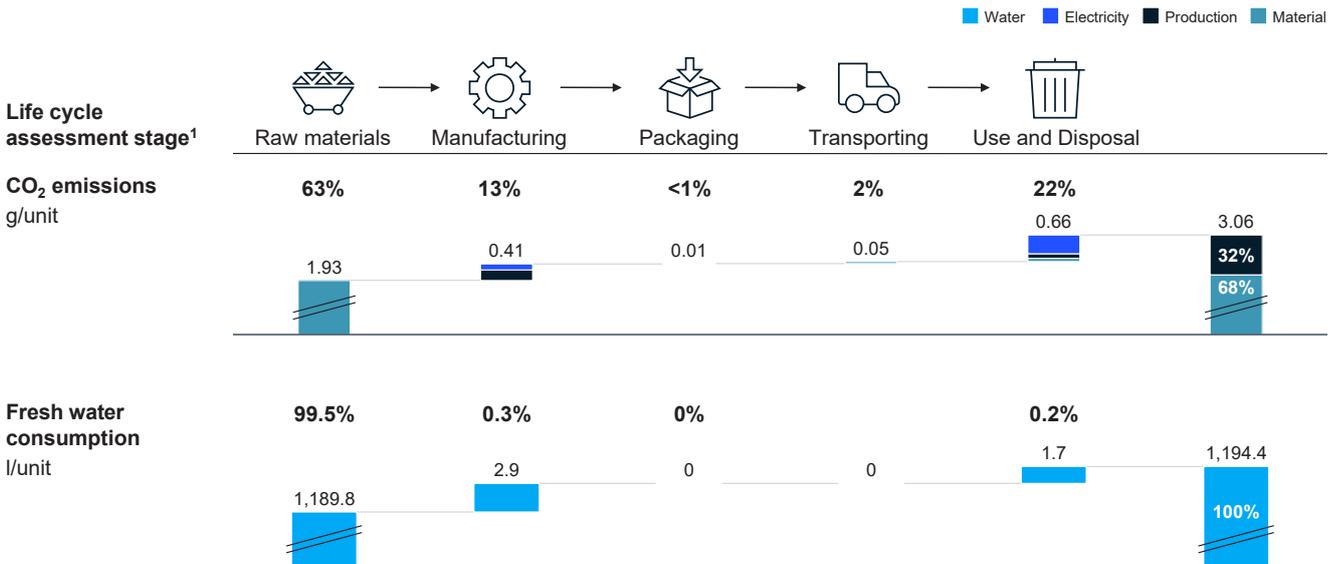


1. Absolute targets converted to relative targets for comparability; Intensity targets established
 2. CAGR since baseline year
 3. Future reduction in emissions required to reach 2030 target; future revenues calculated based on Apparel industry growth rate estimates (~3% in 2022-2030)
 4. Scope 3 considered to cover 15 different categories, from Purchased Goods to Investments
 5. 1.5°C aligned qualification for Scope 1 & 2 target (Scope 3 rating not available)

Source: Company sustainability reports, SBTi website and CDP climate change reports

⁴¹ Source: WFSGI & McKinsey Sporting goods companies survey, September 2022 (N=211)
⁴² Patagonia did not publish Scope 3 emissions prior to FY 2018. The significant decrease in emissions from FY20 to FY21 is largely due to a decrease in product inventory and the operational shutdowns due to COVID.
⁴³ A marginal abatement cost curve presents the costs or savings expected from different opportunities, alongside the potential volume of emissions that could be reduced if implemented

CO₂ emissions and water consumption are concentrated in raw-materials



1. Example for a knit cotton T-Shirt produced in China and distributed in Central Europe
Source: McKinsey Resource Cleansheet, expert interviews, GaBi Database for CO₂ emissions

Conceptually, these two steps are quite easy to define. However, as companies are seeing, they are difficult to implement. In response, more investment and commitment are required, alongside a strategic approach that will deliver results and create competitive advantage.

Step 1: The road to decarbonization

One of the biggest challenges for sporting goods companies lies in data, particularly around sourcing activities (Scope 3), where the majority of emissions reside. To get a grip on the task, the first step should be to ascertain an emissions baseline. That means obtaining as much transparency as possible on emissions in the supply chain – not easy due to the difficulties suppliers (especially tier 2, 3, and 4 suppliers) have in identifying and measuring their emissions. Still, companies should strive to get as far as they can given available resources.

The second step is to define an abatement curve. This will set out the ways in which the company can decarbonize and the associated

costs. Many levers will precipitate savings, including lower e-commerce returns rates, energy efficiency in retail operations, and using more sea transport. Conversely, other initiatives will incur new costs. These include increasing the use of recycled polyester or adding organic cotton. Renewable energy is also more expensive in some countries.

Once levers are categorized based on CO₂ abatement potential and costs, decision-makers can identify quick wins

“The sporting goods industry will only exist and thrive if our playing field, the planet, is respected and protected.”

– Barbara Martin Coppola, Chief Executive Officer, Decathlon

and no-regret moves. In addition, they need to define how much CO₂ they want to abate based on their targets, and therefore which of the levers they should implement first, and the costs. Once lever selection is complete, companies can translate them into concrete initiatives, including plans to address challenges along the way.

The industry’s decarbonization should be addressed with an end-to-end perspective on the value chain. In fact, the industry’s biggest contribution

to CO₂ emissions comes from raw materials, followed by use and disposal, and manufacturing (Exhibit 11). The scarcity of green raw materials will be a challenge. It is therefore important for companies to act urgently and carefully consider potential implications for production and product quality. This is particularly relevant when it comes to sportswear, which often requires technical garments that are designed to withstand challenging conditions. For example, many companies commonly use elastane, which is made from fossil fuels through a highly synthetic process. Of course, there are many sustainable fibers now entering the market, but few are produced at scale.

Another challenge is that demand for sustainable and recycled materials is rising fast. Consumer goods companies, for example, require large volumes of recycled polyester for packaging. In many cases, these closed-loop systems trump fashion applications, which are not infinitely recyclable. The industry expects a shortage of rPET up to 2025, when current investment in mechanical

and chemical recycling will start to pay off. Still, sporting companies are moving forward. Lululemon, for example, has committed to at least 75 percent recycled polyester by 2025, which would reduce its CO₂ emissions by 30 percent.

Step 2: Defining the company’s role in the circular economy

According to the Ellen MacArthur Foundation, the average number of times a piece of clothing is worn fell by 36 percent between 2000 and 2015. Over the same period, clothing production doubled. Both trends highlight the imperative to move away from a linear take-make-waste system and toward a circular model, in which the valuable lives of products are extended and waste is minimized.

The circular economy is defined as a model of production and consumption that involves sharing, leasing, reusing, repairing, refurbishing, and recycling materials and products. However, it is not simple to be bold on circularity, which may require a redefinition

of the business model, creates cannibalization risks, and is complex from a business case and logistics perspectives. There is also the chance of strategic dissonance, in that brands that have made a virtue of newness are suddenly building hype around extending life; a tricky combination to pull off.

Right now, more than 70 percent of companies generate less than 5 percent of revenue from circular business models⁴⁴. However, the industry’s ambitions are growing. By 2030, about 75 percent of companies plan to generate more than 5 percent of revenues from circular business models, half of which have a target of above 10 percent.

One reason for changing attitudes is the rising impact of regulation. The EU Circular Economy Action plan is among initiatives to set specific targets, for example, to ensure that textiles are collected separately in all member states by 2025. In addition, circularity presents a business opportunity.

Exhibit 12

Sporting good companies need to consider different criteria when selecting where to play in circularity



Source: McKinsey, Expert interviews

⁴⁴ Source: WFSGL & McKinsey Sporting goods companies survey, September 2022 (N=211)

“It starts with the design and raw material selection. [...] The next stage is how we build the product. We need to develop products that are easy to recycle [...], and we need the brands to collaborate and drive this.”

— Rakhil Hirdaramani, Director, Hirdaramani Group

According to a McKinsey analysis, the European sports circular market is expected to grow 20-25 percent a year, reaching €30-50 billion by 2030⁴⁵. Key drivers will be apparel and footwear. In the sports equipment category, the refurbished, resold, and rental segments will see the strongest growth, rather than recycling.

Companies have a range of circularity business models to choose from, based on factors such as the size of their markets, margin, and intensity of competition, as well as the right to win based on product and price point. More than 75 percent of surveyed companies are focused on recycling, repairing, and refurbishing, with second-hand – consumer-to-consumer or consumer-to-business-to-consumer – and other business models seen as lower priorities. Companies should consider a range of criteria when selecting an approach, including market size, competitive intensity, and abatement potential (Exhibit 12).

A growing trend is competition from new entrants. Picture is a French sports apparel and equipment brand that enables consumers to rent products. The company also makes recycled,

sustainably-produced products, and offers repair services. Its newest collection is 100% circular, made solely from recycled materials from the industry. Houdini is an outdoor company based in Stockholm that offers lifetime guarantees, repair services, resale options, and recycling. As these kinds of propositions are rolled out, incumbents face a potential innovators dilemma that could, over time, threaten their leadership positions.

Often motivated and inspired by new entrants, some leading brands are making progress. Decathlon has launched a “Second Life” scheme, in which its teams of technicians repair products, including bikes, fitness equipment, and kayaks. Stores have their own Second Life floor spaces. North Face has launched Renewed, a collection of refurbished products that confirms the growing consumer interest in outdoor lifestyles. When it comes to sporting equipment, brand intermediation is key, reflecting that technical performance and safety are often at stake.

Incumbent (and new) brands can also play a role by adjusting their design processes. Recyclable materials and

less mixing of fibers can unlock the recyclability of millions of garments.

As new entrants and incumbents compete, a potential red flag is greenwashing. A report published by the European Commission in March 2022 warns that terms like “eco-friendly” or “good for the environment” need to be underpinned by “recognized excellence in environmental performance”. Indeed, government enforcement actions and civil suits are on the rise, through rules that include securities regulations, consumer protection laws, fraud and misrepresentation statutes, and advertising standards. In July 2022, the UK Competition and Markets Authority, for example, announced the launch of an investigation into how three fashion brands market their products as environmentally friendly.

The sporting goods industry is no stranger to this challenge, and decision-makers must ensure they come to market with clean hands. The prize for those that find the right approach will be increased competitiveness and a leading position in the race for a more sustainable future.

⁴⁵ Source: McKinsey analysis

Rakhil Hirdaramani,

Director, Hirdaramani Group



Dear Rakhil, thank you for taking the time. Looking at the recent evolution of the sporting goods industry, how would you summarize the last 18 months?

It has been a rough two years. We went into lockdown in Sri Lanka before Europe and North America. For six weeks, our factories could not run, but demand was still high. Six weeks later, as we opened, the rest of the world went into lockdown. We saw some of our customers canceling orders, causing a double-whammy for us. This was an absolute disaster not just for us but for most manufacturers in 2020 and parts of 2021.

It was only in July 2021 that we started to see light at the end of the tunnel. We saw a significant increase in orders for 2022 and supply side of manufacturing capacity couldn't cope with demand. There was a global shortage of capacity, so prices began to go up. This wasn't limited to manufacturers, but extended into Raw Materials and even Logistics as we all saw.

What are your expectations for 2023 – particularly regarding supply chain disruptions and disarray?

When we look at spring 2023, we are concerned. With supply-side

inflation kicking in from cotton, utilities, logistics, and the cost of labor, demand is also much lower, especially considering the demand that we saw in 2022. Our spring numbers are not looking as high as they used to be from big brands. Many manufacturers are seeing this as the potential start of a recessionary cycle.

When you look at Supply Chain, we have learned a lot from COVID-19. The whole supply chain is fractured. We as an industry need to look at it in its entirety: it's an ecosystem. We are seeing so many opportunities right now with some of our brands who have understood there needs to be a change. They are moving toward more strategic partnerships with manufacturers. They are looking to work with more prominent players that have a presence in multiple countries to avoid a reliance on a single country. It is the first time in history that we have seen Brands truly engage in Strategic Planning to this extent. It's exciting to see the level of partnership coming to the table.

We manufacturers also realize we need to work more collaboratively with our extended suppliers. We are having three-way conversations

with brands, manufacturers, and our valued partners; we have to extend the conversations beyond Tier 2. If we are strategic partners to brands, they share our problems, and we work out solutions together.

You are emphasizing how relevant collaboration is. How has that impacted your potential to innovate?

Massively. If only we could collaborate more closely with brands and other players in the supply chain, our work would be totally different.

The biggest challenge that will never be accomplished without collaboration is sustainability. It is an industry problem, especially in sporting goods. When you consider that the majority are synthetic, and contain lycra/spandex or elastane – the drive to circularity remains a problem that needs to be solved. We've seen in the press and know that synthetics release high levels of pollutants (that can then be leached into waterways). Yet, we are avoiding the subject.

Yes, we are seeing significant innovation with biological agents and natural fabrics, but none have the performance of polyester or nylon that are also affordable. Some of the technical and merino wool innovations have worked well in premium apparel and footwear, but it is still minimal.

We also have a waste problem. We have offcuts that shift into landfills that are significant. We are trying to recycle, leveraging innovations like machinery that can dissolve polyester and cotton blends, but the cost is high. And the bigger question is if the end customer is willing to pay? That is the age-old question for the brands and retailers, right? Are you ready to raise the cost of your products when you know that everything else has also gone up? Even if it is the right thing to do.

In a previous interview, you stated, "We want to be the more sustainable manufacturer in the world." How are you tracking against this inspirational aspiration

We have been driving an ambitious sustainability agenda since 2008, when started by building Asia's first green facility. We just celebrated our 10th anniversary of this year. In Sri Lanka we were certified Net-Zero across our footprint in 2019. We have 16 LEED Gold/Platinum rated facilities across our geographies and have also reduced water and electricity consumption 35.5% and 12.2% respectively.

Our Team built a sustainability roadmap until 2025 called Future First. In this we've come up with some big commitments. This is not about an end state: it is about the journey and constantly improving. We realize many of our activities can inspire and create an impact, even for our competition and other factories that may not have the resources.

How do you think manufacturers can generally shape the industry toward a more sustainable one?

We need to focus on people, the planet, and performance. We started with greening our facilities, expanded into organic, fair-trade and recycled products, bought and investing in renewable power. And let's not forget about people. The sporting goods industry has been perfect because large brands realized that excellent working practices were the cornerstone of sustainability.

The question is, how do we continue to make things faster and cheaper while doing the right thing?

Here, automation has been a big driver. We are trying to automate as much as possible: machines or digital skills. It is not about replacing people with machines but about reallocating people to value-added activities. We like the term Augmenting Human Potential. This involves having a program to reskill our people.

Do you think the industry needs to reduce the volume or revenue to become more sustainable?

I don't think so. We have a growing global population which just crossed 8 billion. We need to cater to them. I believe there is so much waste in our systems today. We can still work on reducing our greenhouse and CO₂ emissions while growing. It is about moving to more sustainable practices. For instance, our laundry: At one of our laundry facilities, we moved to recycling 70% of our water with a reverse osmosis plant. There are a lot of simple activities that can happen, but we need innovation and collaboration.

If we talk specifically about circularity as an aspect of a sustainability roadmap that many brands advocate, what role can a large manufacturer like you play?

We haven't taken the collective effort as a supply chain. We need all stakeholders around the table to dissect the whole bill of materials, to say, "Hey, how do we make this better? Can it be worn longer, and can it be recycled?" It starts with the design and raw material selection. Manufacturers can share insight from our historic knowledge in manufacture to share how we can improve the makeup. Brands ultimately have to drive circularity as a critical KPI in design.

The next stage is how we build the product. We need to develop products that are easy to recycle. If you look at denim jeans, we have all these rivets and metal on them. How do we take it off? The thread we use is often polyester and therefore needs to be removed. So, many of those decisions need to be made at the inception or creation phase, and we need the brands to collaborate and drive this.

If we talk about refurbishing models, how do you believe they will impact the industry from a manufacturing perspective?

I see it as a massive opportunity: it needs to be serviced near to market to upgrade that product. The opportunity is to see smaller, agile players operating

in this area, sometimes even in store. Some manufacturers may choose to put in mini-tailoring shops in neighborhoods or regions. I think it could be an exciting game-changer.

However, I think there will always be a need for manufacturing as we enjoy the fashionability and uniqueness of product.

Are you optimistic about the future in terms of the progress of the industry in sustainability?

I am excited about the future. I think some great technology is coming out that would allow us to do much of the work. I don't think it is ready yet. If you look at wastage in the apparel industry, the average cut-to-ship ratio is about 97 percent for the industry. So, from the fabric we receive, we only ship 97 percent. Now, if you want to get technical and start looking at markers where we cut the panels of the fabric, your average efficiency is 85 percent on a marker. So, when you start doing the numbers, the industry wastes so much. And I think this is where newer machines are coming in, with 3D knitting. We are starting to see that innovation. It is too new and expensive at the moment because it hasn't gone into mass production, but it is coming. I believe we will see some real innovation in the next five years.

Also, when you look at Gen Z and their views, responsible purchasing practices are here to stay. Gen Z gravitate towards Brands with Purpose and that walk the talk. I think we're already seeing a boom in the resale market. We will see a contraction in volume per style, but I don't believe that is necessarily bad. We need to be more flexible, agile and ensure that we continue to improve production. It is inspiring and exciting because I think those who commit to the journey will win in the long run, both Brands & Manufacturers alike.

Sandra Wolf, Chief Executive Officer, Riese & Müller



Sandra, thank you for taking the time. If we look at the industry and the consumer trends for e-bikes over the past two years, what are your biggest takeaways, and where do you see the industry heading?

Since Riese & Müller was founded in 1993, we have focused on daily mobility. And between 2017 and 2019, e-bikes for commuting saw a boom in southern European countries such as France, Italy, and Spain, where previously bikes tended to be used for sport. Now, a big community of people sees the advantages of using bicycles in the city instead of cars. In 2020 and 2021, we grew exponentially. People started seeing e-bikes as a safe and healthy mobility option, and as they couldn't spend their money on traveling or other pleasures, they began buying e-bikes.

We are unsure how the current economic outlook will affect our sales in the coming years. We are definitely seeing consumption slowing down and dealers who are more reluctant to invest than before. Nevertheless, I'm confident that things won't be harmful for e-bike players in the midterm, especially for daily commuting, as people will increasingly choose more sustainable mobility options.

I really think that quality e-bikes, and especially cargo bikes, have an essential role to play in the future of cities.

When it comes to sustainable urban mobility, what advantages do e-bikes have over other forms of transport?

In the cities, you have a wide variety of mobility opportunities. However, commuting on an e-bike offers many advantages over any other form of transportation. The benefit for the rider is definitely the fresh air, the exercise, and the convenience of moving to the inner city without parking problems and traffic jams. This will also help cities and smaller businesses within city centers to continue operating—thanks to the higher daily traffic enabled by bikes, which brings consumers to spend time and shop. Cities with lots of bikes are often in better shape than where bikes play no major role.

What advice would you give to cities that want to become more bike friendly? What are the most important things to enable this form of mobility?

First, cities should not plan for a particular vehicle, cars, or bikes, but rather for humans. Where can we be

more human-centric as a city, and where do humans need more space? Then, cities need to differentiate between the different uses of bikes, for example, daily commuting or cargo bikes for business. We cannot just have roads for cars and lanes for bicycles. We must differentiate based on who is doing what and who needs what. Third, a mobility transformation can only happen if we can work with more data. Infrastructure planning needs to be data-driven, so data collection becomes crucial: how are people moving through the city, where, at what speed, and which means of transportation are they using?

How is the sharing segment growing for bikes?

We are already involved in numerous high quality sharing programs. We have partnerships with neighborhood sharing programs and, more recently, with companies that provide their employees with bikes to move around, as well as hotel chains. Bike-sharing programs in cities have grown exponentially. A particularly great thing about them is that they are tapping into a younger audience and showing them the advantages of e-bikes.

How would you currently describe and maybe segment the e-bikes market?

When e-bikes arrived, let's say eight to ten years ago, we only talked about city e-bikes, and there was more or less one type of bike that wasn't for sports. What we now have is all types of e-bikes so from any category, be it mountain bikes, road racing bikes, or bikes for cities.

What I see, which is also new to the bike business, is that new players have come in that had nothing to do with bikes and bike manufacturing. Be it car manufacturers interested in new mobility or companies that come from the digital side developing software for e-bikes. This is something completely new, in my opinion.

With the growth of e-bikes, there was also scarcity. What is your reflection on the supply chain situation?

The entire industry had some trouble over the past two years in terms of the supply chain. First, there were lockdowns in Asia, where many suppliers are located. Then, we had super-high demand but no availability. I think there was and still is a vast supply chain disruption, which has prompted us to rethink where we are, where we came from, and where we want to go. At Riese & Müller, we try to have many of our suppliers in Europe, not only for risk mitigation but also for sustainability reasons. Our competitors now also try to source from Europe to be less dependent on markets whose circumstances we cannot predict.

Regarding sustainability, can you please share your perspective on what role it has in your industry and how it is evolving?

I am a person who pushes sustainability in the industry because I think it's super important that our product helps our customers live a sustainable lifestyle and production. We have a lot of worldwide suppliers, making building a fully sustainable and transparent supply chain difficult and complex, but we are moving in the right direction.

As an industry, I think we are waking up. We are a small number of players collaborating in working groups to really

bring this forward. Still, I'm not sure if the whole industry has seen sustainability's importance and potential.

What are the most demanding challenges when it comes to making that happen?

The biggest challenge is the supply chain and how to get all the information to make it transparent, as well as the risks in terms of sustainability. I personally thought this would be easier, but in the end, you depend on your suppliers, sub-suppliers, and sub-sub-suppliers. Getting to the very start of a product, it's a very long journey that you have to take.

Where do you see the e-bike industry going if we speak about circularity?

I think circularity is very important, and I think it will be even more critical in the future because most e-bikes are still in their first life cycle. It is not an old product, and many people are still riding their first e-bike. We have to really think more deeply about the second life cycle. For example, the more sharing we have, and the more companies we have financing and leasing bikes, the quicker bikes will come back, and the more programs we will have to refurbish them and start a second life cycle. And, of course, one other big topic is battery recycling, which we already have. At least in some European countries, there is quite a good program. It is essential because the bike lasts longer than the battery.

Nearshoring - Balancing acts

In an era of supply chain disruption, more companies are turning to nearshoring as a core element of their supply chain strategies. However, decision makers need to do their sums before taking the plunge.



Persistent supply chain disruption, geopolitical considerations, and rising Asia labor costs are prompting many sporting goods companies to consider moving production closer to home. So-called nearshoring, which offers potentially faster time to market, has become a common topic of C-Suite discussions. However, as early movers have discovered, decision-making requires careful balancing of potential challenges and rewards.

With global trade continuing to struggle from the impacts of COVID-19 and trade tensions creating uncertainty, companies are increasingly concerned about supply chain reliability. For many, nearshoring presents a potential solution, as well as a positive sustainability story (though the jury is still out on that).

factory—in the process avoiding import duties. Meanwhile, New Balance, as part of its strategy to proudly produce in the US, has committed to five factories in Maine and Massachusetts, the last one opening in March 2022. Evidence of increasing nearshored production is also found in an analysis of footwear manufacturing in the Euro-Mediterranean region, which is expected to see a more than tripling of production within five years (Exhibit 13).

In addition to being an important diversification and risk mitigation strategy, nearshoring becomes more attractive as sourcing costs from low-cost hubs rise. In the US, the discussion is also informed by restrictions on imports of cotton and growth of tariffs on Chinese imports. These themes are reflected in executive cost

“I believe you need to start with a merchandising and assortment plan. Which portion of my assortment is predicated on speed, cost premium, and full-price sell-through? Which part is instead based more on scale and volume, which I prefer to source from the global network?”

— Hoa Ly, Senior Vice President for Global Sourcing, adidas

As a result of these dynamics, about 75 percent of sporting goods companies plan to expand their nearshoring activities by 2025, according to WFSGI & McKinsey’s latest executive survey⁴⁶. Eight percent are already doing so. Among examples, Ski specialist Salomon in 2021 opened its Advanced Shoe Factory 4.0 in France, while Decathlon invested about €30 million in Romania to build Europe’s largest bike

expectations. Already in 2021, half of executives in one survey expected cost increases of more than 4 percent, while 20 percent expected rises of more than 6 percent⁴⁷.

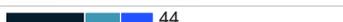
Not simple

Despite the cosmetic allure of localized production, nearshoring is not a simple proposition. Indeed, there are multiple operational and strategic challenges in making the transition. US importers

⁴⁶ Source: WFSGI & McKinsey Sporting goods companies survey, September 2022 (N=111)

⁴⁷ Source: McKinsey Apparel CPO Survey 2021.

Footwear manufacturing in the Euro-Mediterranean region is growing

		■ Fabric Upper ■ Leather Upper ■ Rubber / plastics Upper	
Top Euromed footwear exporters ¹ , in M pairs exported in 2021		CAGR trend, 2017-2021	Labor cost 2022 ² , in €
Turkey		12%	1.06
Italy		21%	18.25
Spain		-1%	15.01
Poland		13%	5.27
France		n/a	18.32
Greece		39%	7.59
Portugal		0%	10.57
Slovakia		-4%	5.27
Cech Rep.		-4%	4.85
Hungary		5%	4.85
Austria		2%	25.13
Romania		-10%	3.58
Bosnia		-2%	n/a
Ukraine		0%	n/a
Serbia		-3%	n/a
Slovenia		n/a	11.99

1.5 Bn footwear manufactured in Europe (estimation)

From 11Mp To 34 Mp in 2026

1. Custom codes include Footwear with Rubber or plastics soles and Fabric, Leather or Rubber upper
2. Based on average base labor for unskilled worker

Source: ITC data, McKinsey analysis

shifting their sourcing to Mexico and Latin America report finding it tough to locate suppliers with the right raw materials, production quality, and networks⁴⁸. In switching production, companies may take years to match the labor capacity and supplier depth they have in Asia, experts say. In addition, there are potential challenges around culture.

Another potential headwind is that automation expectations are often not fully met in the nearshored environment, or are too expensive to implement. These issues have prompted several manufacturers to reconsider their plans to focus on US-based factories and instead form partnerships with facilities in Asia.

Data-driven approaches

To reduce the risk inherent in nearshoring, sporting goods companies should analyze a variety of factors at both product and country levels:

The product perspective.

Nearshoring needs to be considered around four key metrics.

- Lead times:** Lead times should be considered on a product basis. For example, a never-out-of-stock product may see unpredictable demand and therefore benefit more than others from in-season replenishment.
- Risk exposure:** To what extent is the product exposed to supply shocks, trade disputes, COVID-19 policies, or other risks to the normal conduct of business, and how dependent is it on Asian manufacturing?
- The parameters of success:** Most brands see speed and flexibility as supportive of nearshoring initiatives. Leading companies thus analyze labor costs and skills requirements, and how they may evolve.

- Sustainability and greenhouse gas footprint:** Our modeling shows that partially shifting production to nearby locations with cleaner energy can cut CO₂ emissions per unit by 11-14 percent. Reduced transportation needs are also a factor. Where companies are using large volumes of high-CO₂ materials, such as polyester, these calculations become even more relevant.

Often companies will need to assess trade-offs between metrics. For example, it may be that regional nearshoring boosts costs by up to 20 percent for a t-shirt, driven by labor and energy (Exhibit 14), but reduces lead times by as much as 20 days. The offsetting factors in relation to the latter include faster time to market, with the potential to reduce overstocking, wastage, and the need for promotions. The exact parameters of these judgments will depend on the products involved and relevant economics.

⁴⁸ Source: U.S. Companies Face Hurdles in Moving Production Closer to Home, WSJ, April 2022

“Wherever there is rigidity, there is risk. [...] At Decathlon, we are making our entire supply chain more flexible and adaptive”

— Barbara Martin Coppola, Chief Executive Officer, Decathlon

The nearshoring equation may play out differently depending on product characteristics. For example, a simple t-shirt may benefit from nearshoring because of its relatively low labor cost and the ability to quickly adapt to shifts in demand. However, a more complex, less automatable product would see fewer benefits because the adaptations may not be possible, and the high labor cost would make nearshoring more expensive.

Based on this analysis, companies must make nuanced decisions product-by-product on whether the nearshoring equation makes sense:

The country perspective

Companies should again consider four key variables:

1. **Capacity:** Capacity is a function of the relative cost of production and availability of productive resources and labor (or ability to acquire them). Companies need to compare the total landed cost of production in different countries, including manufacturing and transportation of finished goods and raw materials. This will enable them to assess the potential additional cost of nearshoring and compare it with quantified benefits such as greater availability and the impact of sustainability.
2. **Capability.** When it comes to labor, many nearshore countries do not have the same capacities and capabilities as Asian countries. Individual nearshore locations need to be analyzed to determine whether capabilities are sufficient.

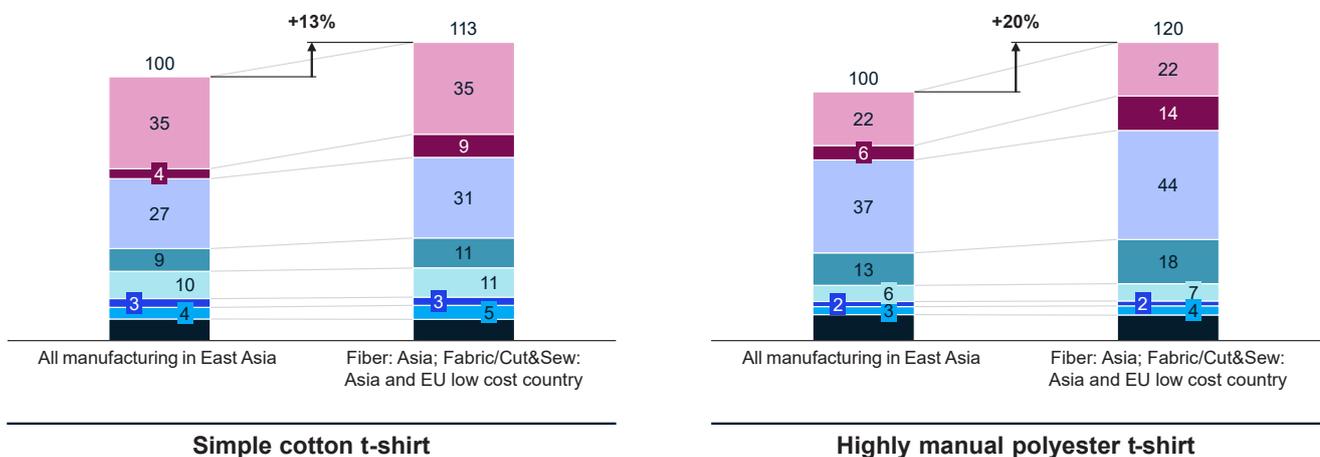
Exhibit 14

Regional nearshoring of t-shirts could increase costs by 13-20% depending on the labor and energy intensity

Illustrative – simulation

Material Labor Utilities OPEX non-labor¹ CAPEX depreciation Duties Transportation CO₂

COGS breakdown 2030, indexed to current global network



1. Includes R&D, SG&A, and Profit by suppliers

Source: McKinsey & Co. CPG Apparel network model and analysis (June 2022)

3. **Raw materials.** Companies should ask whether raw materials are available in the nearshore location or if they need to be imported. Right now, raw materials are mainly sourced in Asia, so transportation costs and lead times need to be considered. If raw materials continue to be sourced from Asia, the lead time benefit of nearshored production will be reduced.
4. **Regulation:** Finally, companies should review the regulatory situation and any grants or incentives that may be applicable. These could have a big impact on costs. Additionally, it is crucial to consider the trade environment. Protectionism has increased since COVID, and companies need to carefully consider the rules when assessing sourcing options.

All of these variables should be taken into account as business leaders assess whether to nearshore or not—as well as for which products and to which country. Inevitably, it will make sense to take tradeoffs into account. Does it make sense to de-risk the supply chain by switching to multi-country production rather than nearshoring, or

would it be better to cut lead times by nearshoring, which would also enable more accurate demand responsiveness and more streamlined operations? Companies that effectively balance these factors will be best placed to make nearshoring decisions for the right reasons and aligned with their strategic objectives.

Finally, nearshoring should never be an end in itself. Rather it should be seen as a mechanism to achieve a specific goal, such as shorter replenishment lead time for new products where demand is uncertain. Through this focused perspective, set against a broader supply chain strategy, companies are most likely to make the right decisions first time.

75%

plan to increase **nearshoring** by 2025



8%

of surveyed companies are already pursuing a transition plan to increase **nearshoring**

“At Riese & Müller, we try to have many of our suppliers in Europe, not only for risk mitigation but also for sustainability reasons. Our competitors now also try to source from Europe to be less dependent on markets whose circumstances we cannot predict.”

— Sandra Wolf, Chief Executive Officer, Riese & Müller

Hoa Ly, Senior Vice President for Global Sourcing, adidas



Dear Hoa, thanks for taking the time. Thinking about the sourcing world, what are the key trends you see and what is your perspective on nearshoring?

The three major trends in the sourcing world that I see are:

1. **Agility** as a key capability now and in future. Our industry is highly exposed to potential disruptions in its value chain. Supply chain volatility requires companies to build a diversified and flexible network of suppliers, not only on the manufacturing side, but also raw material infrastructure. This is crucial to allow them to quickly pivot and adapt to any possible scenario or situation.
2. **Manufacturing efficiency** is key to protect the profitability of the brand and supplier partners. This requires continuous improvement in design/creation for manufacturability and business process simplification.
3. **Sustainability** is both an opportunity and a threat for the industry. Opportunity-wise, the industry can positively influence its carbon emission by driving

conscious choices on **what goes into the product and how the product is manufactured**. The threat is the reliance of the industry on growth in consumption, and we all know the challenge with fast fashion and its impact.

With the COVID situation, geopolitics, and fear of deglobalization, nearshoring has almost become a buzzword in the past three years. Almost every company out there is talking about it. I think nearshoring is an important element of a good sourcing strategy, but it will not be the one and only headline. In my opinion, a robust sourcing strategy requires a balance of capability, quality, sustainability, and cost competitiveness. In fact, when we talk about nearshoring, raw material infrastructure and cost competitiveness become big topics.

What role do you expect nearshoring to have in the future?

I believe many companies will seek to increase the share of their business nearshored, while not massively overhauling the scaled and reliable global supply network, which balances cost, capability, sustainability, and

quality. Nearshoring will have a role to play, but I think it needs to be a part of a company's operating model.

Certain fast fashion pure direct-to-consumer brand/retailers have successfully leveraged nearshoring. A proportion of products are being developed and manufactured in nearshore locations, with a significant cost premium. The business model is founded on a belief that fashion is fleeting and that the biggest risk to profit comes from discounts. In their case, nearshoring works because it is demand-led, starting from clear enterprise-level strategic direction and segmentation of products the consumer is willing to pay a premium for. Speed of nearshored products (albeit at a price premium) allowed fast fashion retailers to bring products to market at full price sell thru and the controlled inventories (at times scarcity of products by design) significantly reduced markdowns.

The sporting goods industry, on the other hand, with its mix of largely wholesale and DTC, first needs to transform the operating model internally, including assortment

planning, product design, planning, and supply chain infrastructure (especially upstream inputs from T2 and beyond), to scale nearshoring in a sustainable and value-adding way.

What are the internal complexities you see to be able to take full advantage of nearshoring?

I believe you need to start with a merchandising and assortment plan. Which portion of my assortment is predicated on speed, cost premium, and full-price sell-through? Which part is instead based more on scale and volume, which I prefer to source from the global network?

Today, most companies start out with a big range of wholesale and D2C together, and then we go through a process to select what to nearshore. Immediately, you run into a cost competitiveness challenge.

To take full advantage of nearshoring, it is fundamental to use data and a demand-led approach to drive allocation. I mean, many companies make a mistake in thinking that nearshoring should be led by the sourcing organization. I would argue with that it needs to be the other way around. You need to start first with a business model in mind: What is the business case, what is the benefit, how do I segment my assortment, how do I improve internal demand planning and measure the end-to-end benefit of nearshoring holistically? And then you build a sourcing capability to cater to that.

What is your experience with nearshoring and what learnings could you share?

Nearshoring has been a part of global sourcing strategy since the early 2010s, driven then by trade barriers and the deglobalization trend. For example, for many years, we have maintained nearshoring and/or local sourcing capabilities, such as China sourcing for the China market, Latin American sourcing for Latam, India for India, Turkey/EMEA sourcing for Europe, and Central Americas sourcing for North America. Our experience

has been that when the commercial function in the market plays an active role in demand planning and is actively accountable for the nearshoring/local supply base, it generates win-win benefits.

On the other hand, the speed factory concept was not successful. We learned that we did not have a strong unique selling point to justify the premium price, and we were very narrowly focused on a specific product construction, which limited the ability to scale and expand.

So, I think the lesson learned, again, is that you need to start out with the demand, the assortment plan, and what works well for the market and sourcing model. I think when you have that, you can build the sourcing plan.

Do you think that the recent economic and geopolitical situation, and potentially more trade barriers, have increased the relevance of nearshoring?

Yes and no. With the recent COVID and logistical disruption, we have seen an acceleration of nearshoring, because the massive surge in transportation costs had made the cost premium of nearshoring product more digestible. However, this trend is only sustainable if companies can successfully leverage shorter transportation lead-times from nearshoring sourcing regions to drive full-price sell-through, and reduce mark-downs and inventories. This is easier said than done as we have seen in our industry.

The geopolitical situation and more trade barriers do not necessarily increase nearshoring. They rather block consumers' access to competitive, technical, and innovative products available from a globally dispersed sourcing network.

Are there any industry-specific considerations to make when it comes to nearshoring in the sporting goods industry compared with other industries?

What we have to consider is how technical a product is and how labor-intensive its manufacturing is. Apparel

products that are more fashion oriented are easier to nearshore because the supply chain or sourcing infrastructure in a nearshore location is more developed. Nearshoring footwear can be a much bigger challenge. The capital investment and the cost of entry to build up an extensive raw material infrastructure and know-how is significant. So, I think there is a big difference there. I think when we talk about nearshoring, the bigger opportunity for us is in the fashion garment industry, rather than footwear.

One more question. How do you see the role of sustainability in this topic of nearshoring and in the supply chain as a whole?

Pretty big. The commitment to achieve carbon neutrality is a great responsibility. I think nearshoring has a role to play there, but the commitment requires each actor in the value chain to step up and play its part, from raw material suppliers, to manufacturers, to brands and beyond.

To reduce our carbon footprint, we cannot just optimize the manufacturing process. We also need to control the inputs; we need to start from a radical approach to design sustainably and use of new materials. For example, the adidas x Allbirds collaboration managed to create a performance running shoe with less than three kilograms of carbon footprint, when on average a pair of shoes across the industry generates maybe 15 or 17 kilograms. This is just an example, but it shows there is still much as an industry we can do.

Sporting routes to profitable growth in private investments



The success of sporting goods brands has attracted a wave of private investment. By focusing on a portfolio strategy of complementary brands, an elevated digital interaction with consumers, and analytics at scale, funds are most likely to maximize their portfolios' potential.





89
CB

78 PAC	74 DRI
63 SHO	92 DEF
75 PAS	88 PHY

91
RW

91 PAC	94 DRI
89 SHO	34 DEF
90 PAS	64 PHY

The global sporting goods and sports apparel markets have seen impressive growth in recent years, and, despite current industry and economic challenges, a longer-run positive trajectory is expected. The segment's stellar performance has attracted the attention of investors and fuelled a wave of venture capital (VC) and private equity (PE) deals, as well as a spike in M&A activity. In 2021, there have been 233 deals, over a 100 more than 10 years previously⁴⁹. VC accounted for the majority of growth. Still, with the industry remaining dominated by large brands, many investors face a challenge in establishing winning propositions. Astute portfolio management is required to achieve maximum returns.

Sportswear brands and retailers have thrived in recent years, amid growth of about 13.9 percent (CAGR) from 2019

to 2020, driven by a boom in athleisure. Investors have also fared well, with upward of 20.3 percent in total return to shareholders from 2019 to 2021, compared with 4.5 percent among traditional apparel players⁵⁰. Moreover, sportswear brands have proven to be more resilient to downturns than traditional apparel players (Exhibit 15). In the 2007-2009 financial crisis, the global market for sports apparel saw a stable performance, before rebounding fast, amid growth of between 4 percent and 10 percent across categories from 2009 to 2011⁵¹.

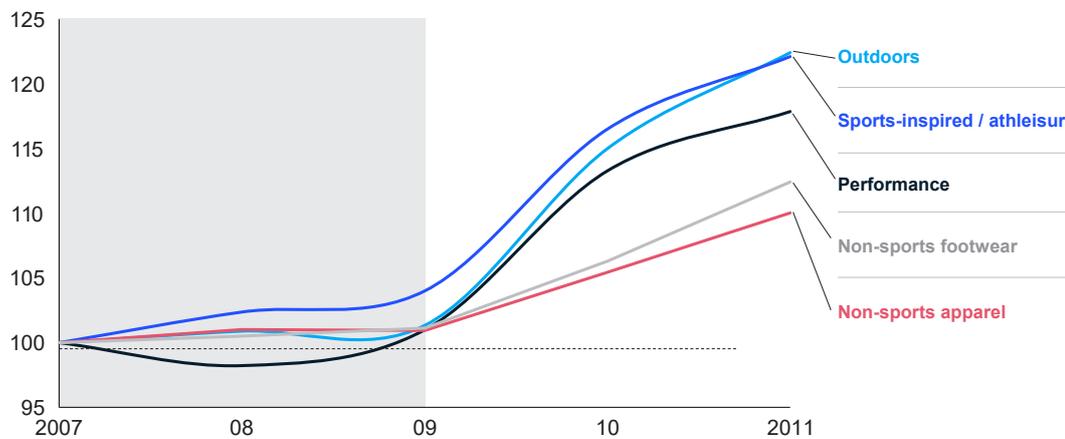
During the COVID pandemic, many smaller sporting goods companies grew exponentially as consumers shifted to work-from-home wardrobes and focused more on health and wellness⁵². In 2022, most sporting goods companies are expected to exceed pre-pandemic levels of

Exhibit 15

Sporting goods companies were resilient during the 2008 crises, and bounced back strongly after

Global market for sports apparel and footwear

Retail sales in EUR M indexed to 2007 as 100



Global Financial Crisis

CAGR

	'07-'09	'09-'11
Outdoors	1%	10%
Sports-inspired / athleisure	2%	8%
Performance	0%	8%
Non-sports footwear	0%	4%
Non-sports apparel	1%	5%

Source: Euromonitor data as of September 2022

⁴⁹ Source: McKinsey analysis

⁵⁰ Source: Capital IQ, McKinsey corporate performance analytics. McKinsey analysis

⁵¹ Source: Euromonitor International, McKinsey analysis

⁵² For a broader perspective on global physical activity levels, please read the dedicated section in our Foreword

“If you are constantly buying businesses, pumping them up, and selling them after five years, are you going to make investments in those key areas of sustainability that a longer-term holder would?”

—Andy Rubin, Deputy Chair, Pentland Group

performance, reflecting a positive trajectory that has been in place for a decade.

The industry’s growth is reflected in deal sizes, which in some investment areas have quadrupled since 2011. VC deal values averaged \$22 million in 2021, compared with \$5 million 10 years previously, while corporate deals averaged \$202 million, compared with \$54 million previously. Conversely, PE deal sizes fell from an average of \$247 million in 2011 to \$126 million in 2021⁵³.

The most active investment category from 2016 to 2021 was outdoor gear, which saw 161 deals (Exhibit 16). Prominent buyouts include those for Amer Sports, Bass Pro Shops, and Jack Wolfskin. Connected fitness equipment has also been active, with 85 deals, while athleisure recorded

58 transactions, including for Sweaty Betty and Campus Activewear. Notably, there were 26 deals for sustainable sportswear brands, compared with 53 for performance sportswear⁵³.

A strong trend across the industry has been an increasing focus on lifestyle and health⁵⁴. North Castle Partners in the US has invested in companies including Barry’s and Echelon, while Sweden’s Caddie Ventures focuses on scalable, community-driven sports and lifestyle companies. Pentland Group in the UK has built a portfolio of small/ mid-sized sportswear companies.

Challenges ahead

In a segment dominated by a few super-winners, a significant challenge facing private investors is to optimize the performance of mid-sized companies valued between \$100 and \$300 million, as well as effectively manage a

⁵³ Source: PitchBook Data, Inc.; Data has not been reviewed by PitchBook analysts, McKinsey analysis

⁵⁴ For a broader perspective on global physical activity levels, please read the dedicated section in our Foreword

long tail of smaller enterprises. Before putting their money to work, investors need a clear idea of how they will promote growth based on a strategy aligned with their investment horizons.

Based on our work with mid-size companies in both sport and fashion, we see three key areas where productive investment should focus:

Building a portfolio of complementary brands

Smaller players that create a portfolio of complementary brands can both reduce risk and compete more effectively with super-brands. Synergetic frameworks can boost negotiating power with suppliers and logistics partners, increase the company's allure with retailers, and attract top talent. In addition, there is an opportunity to centralize operations,

and there has been a shift to more centralized product design and development. In another example, Columbia Sportswear Company has achieved steady revenue growth across its four brands after centralizing control but keeping operations flexible across brands.

Elevate digital through tailored content for each community

Online interactions reveal the truth about people's behaviors, priorities, and interests. In parallel, surveys can help companies identify the key drivers of online behavior. However, few players leverage this rich seam of information to build a comprehensive picture of their target customers.

To step up engagement, a phased approach is recommended. As a first step, companies should drill down into

“I think there are different business models that you can employ in how you create value. In our brand division, we create value by buying brands and then adding them to our platform.”

—Andy Rubin, Deputy Chair, Pentland Group

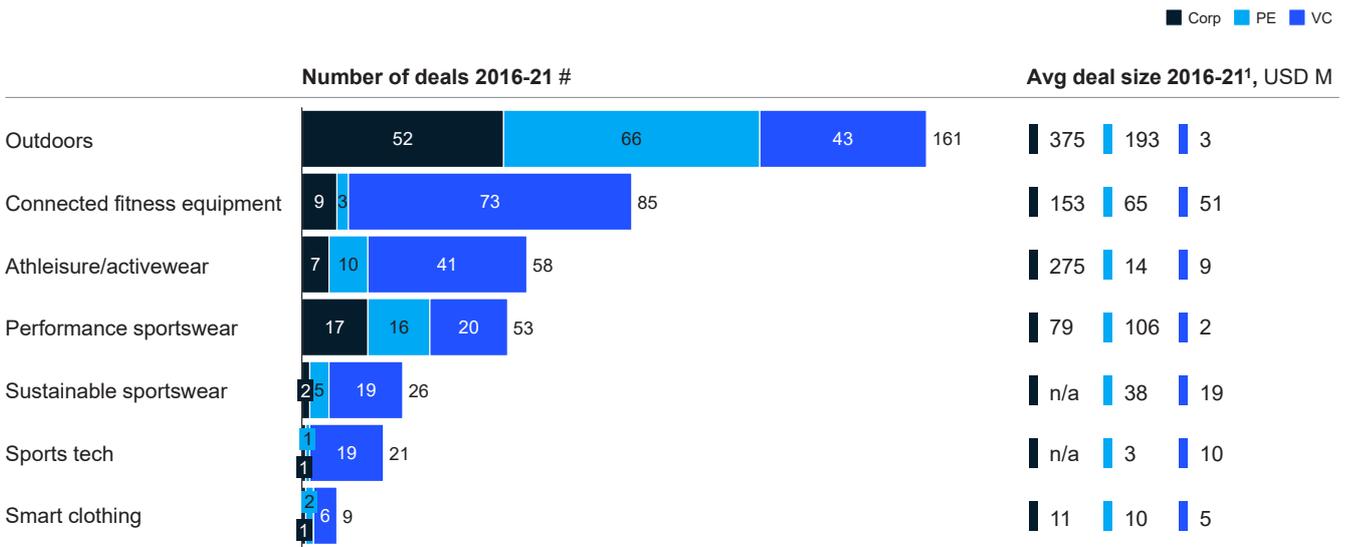
sourcing, and e-commerce, while retaining brand autonomy in aspects of operations. The potential efficiencies are particularly compelling when the portfolio is focused on a limited number of categories.

Among synergistic success stories, Johnson Outdoors is a portfolio of eight brands across diving, camping, fishing, and wearables. The portfolio has achieved strong revenue and margin growth after centralizing strategic decision-making and marketing, as well as taking an integrated approach to e-commerce and digital. Sales are managed on a category basis,

transaction and online data to identify cohesive customer segments, based on parameters such as interests, belief systems, brand loyalty, and channel usage. Several off-the-shelf tools are available to support this analysis.

Based on the analysis, brands can produce focused communications that appeal to specific personalities and points of view. Typical archetypes might be self-motivators, go-getters, or daredevils. Brands can create content and highlight hero products tailored to these groups, backed by credible stories that reflect values and behaviors. Finally, to create a sense

Outdoors and connected fitness are the leading investment categories



1. Includes only deals with publicly available data

Source: PitchBook Data, Inc.; Data has not been reviewed by PitchBook analysts

of community, brands should back their stories with engaging content, both online and across ecosystems of non-commercial touchpoints, such as community initiatives.

Leverage analytics at scale to harness the power of data

Across industries, companies are starting to use analytics to derive actionable insights. However, small- and medium-sized brands often lack the capabilities and infrastructure to optimize outputs. In response, they require a more strategic mindset and a steely focus on execution. Progress is likely to be predicated on sufficient budget and resources, but the prize can be an up to 30-40 percent uplift in EBITDA.

Common data and analytics use cases are focused on assortments, pricing and promotions, and demand forecasting. In assortment management, brands can use analytics to deliver real-time optimization. SHEIN is among the companies to have mastered the skill, operating a “test and chase” process to respond quickly to demand trends, backed by dedicated

content and monitored through KPIs. Where a first small batch gets a positive reaction, new production is triggered and distributed directly through vendor systems. A weak response, meanwhile, is met with immediate scale down.

Pricing and promotions are equally amenable to real-time analysis, enabling brands to respond flexibly to demand and events as they happen.

Through these three key levers, investors in sporting goods brands can create portfolio dynamics and elevated levels of performance that support revenue growth and long-term margins. Just as importantly, in a hyper-competitive market, they can help them establish profiles that compete more effectively with some of the most powerful brands on the planet.

Andy Rubin, Deputy Chair, Pentland Group



Andy, thank you for taking the time. Looking back at the year 2022, what are your key takeaways? How do you feel about your business but also about the industry as a whole?

I think the past couple of years have been very unusual for the industry. Obviously, the impact of COVID and the lockdowns around the world have been significant, and we're still feeling that. Upfront, it was about the consumer impact that the lockdown had, but also about sporting activities as well. Team sports in many parts of the world had to shut down, and swimming pools were closed. On the other hand, the outdoor industry and cycling saw a boom because people were still able to get outside. And then, we went through supply chain challenges, with factories being shut down in many parts of Asia because of the lockdowns and shipping containers being in the wrong places, as well as shipping prices rising. And now the war in the Ukraine has obviously impacted energy prices considerably. So, we have had this very interesting intersection of consumer challenges and consumer preferences changing, while we have had to balance working through supply chains, which have been dramatically affected by

macroeconomic and geopolitical events.

What do you think the lasting changes are?

I hope that there has been a realization through COVID and the lockdowns about how much personal health matters. I think there has been a big wake-up call to people around the world in terms of the importance of being healthy. I also hope that people have discovered activities for the first time that they will stick to – be it the ability to go out for a walk or to get on a bike.

Coming to the subject of private equity in sporting goods, how do you see this space evolving?

We as Pentland Brands have built our business over the past 30 years through acquisitions, and the market has changed considerably because of the amount of money available to investors. This has definitely impacted valuations and the way businesses are run. And what has changed is that you have a lot of PE firms that are buying brands or retailers in the industry, building them up, and then, after five to seven years, looking to exit. And the next PE fund comes in and buys it, and they do the same thing again. So

as an industry player, it can make it a lot harder to invest in assets that we think we can add value to, because the valuations are frequently overinflated.

PE firms usually just buy individual assets, which means you lose out on the opportunity for synergy and scale that you would get through a portfolio of sports businesses. What is your perception? Are synergies a nice-to-have or a must-have to be successful going forward?

I think there are different business models that you can employ in how you create value. In our brand division, we create value by buying brands and then adding them to our platform. We can then give them access to our sourcing and distribution network around the world, adding our expertise in consumer behavior, product innovation, marketing, and communication. Private equity firms think less about synergies and more about growth in revenues and margins over the next five years. Both are viable models, but they are very different.

Is it possible to combine the two approaches? And why do PE firms not also buy a couple of brands in the sector to leverage synergies and scale?

Yes absolutely. Independent brands are looking to create value by accelerating growth, but we do it for the long term; let's say on a 10–15-year time frame. This is very different than if you were looking to pump something up and make sure that you are maximizing the value at exit in five to seven years. So, it is a different way of working. The second point is, yes, a PE could group together brands in a sector and try to generate synergy. However, this is not easy, and it is much easier to sell firms on an individual basis than combined.

Do you think there are types of businesses that are more open to the idea of being bought by a PE player than others?

I believe there are sellers that are interested in what happens to their company after it is sold, particularly if they retain an equity stake, and there are sellers that are not. We have had a couple of businesses that we have invested in because the seller wanted to sell to an owner that was thinking long term, that cared for its people, and that was going to invest in its future. So, I think there are certain advantages to sell to a strategic buyer that operates for the long term, but it might mean that some value will be lost in the transaction compared when you sell to other players, particularly PE.

Given the rising interest from PE funds and investors in the industry and their short-term views, do you think this has influenced the evolution of the industry and shaped certain trends?

I'm sure the answer must be yes. If you are constantly buying businesses, pumping them up, and selling them after five years, are you going to make investments in those key areas of sustainability that a longer-term holder would? The answer is probably no. Thus, there's probably a detrimental effect to the industry of short-term owners of assets.

Now, looking at the long-term macro trends in the industry in the next three to five years, what do you think are the biggest opportunities?

For the sporting goods industry, I think there is a significant opportunity to grow our businesses in very interesting ways. There are interesting developments to tap into. For example, we've seen people starting to casualize what they wear. And what we must do as a sporting goods industry is to innovate and create products specifically for activities or sports and then separately for people to wear casually. The second key theme is how we can minimize the impact on our planet, so sustainability has

become critical and should be on the top of every leader's agenda. The third key theme is inspiring people to move more, to be healthy and to try to combat the problem of obesity. Lastly, there's the inequality issue – how can we help more people to have access to facilities, to coaching, to sport kits, and to be able to participate wherever they are in the world.

“We as Pentland Brands have built our business over the last 30 years through acquisitions, and the market has changed considerably because of the amount of money available to investors. [...] valuations are frequently overinflated.”

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