International Business Development in Conditions of Global Digital Transformation: Stitch Fix Case

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Keywords: International business, Company, Strategy, Value proposition, Financial indicators and multipliers, Consumer, Investor, Sustainable competitive advantage, Digital products, Global digital transformation, SDGs, Blue Ocean strategy.

Abstract: The article discusses the practical aspects of the functioning of international business in the current conditions of global digital transformation and competition. As an object of research, it is proposed to study the case on the example of Stitch Fix. The article analyses all possible tools for the formation of the value proposition of a given company in the context of the analysis of marketing and pricing strategies. The scientific work presents an analysis of financial indicators and multipliers using the Z-score methodology. It's considered the existing and potential sources of Stitch Fix, Inc.'s sustainable competitive advantage in organisation-wide optimization, continuous product improvement and the development of new concepts.

1 INTRODUCTION

Today's global development of international companies is an important aspect of scientific research, especially in conditions of global digital transformation

In our research, we propose to consider a case on the example of a company - Stitch Fix.

The aim of the work is to assess Stitch Fix's value proposition, to analyze equity holders, developments' strategies and Stitch Fix's competitive advantages, in order to answer the questions:

- Can Stitch Fix convince its customers to keep using its service over the years?
- How equity holders would impact on the desired performance of the business?
- What strategies should Stitch Fix employ to thrive despite intense competition from the likes of Amazon?
- Does Stitch Fix have a sustainable competitive advantage?
- Does it have elements of a Blue Ocean strategy?
- How can Stitch Fix increase rate of revenue growth and keep expanding its customer base?

2 RESEARCH METHODOLOGY

As a result of a critical analysis of empirical data on the functioning of Stitch Fix in the areas of strategic management in general, HR management, marketing, and financial management, including investment design, the following elements of value proposition for the company have been identified: personalization of customer service, peer-to-peer interaction, loyal pricing and demand forecasting based on AI.

Let's dwell on the consideration of each of the presented elements in terms of theoretical basis and applied understanding within the framework of Stitch Fix, Inc. functioning, to complete the logical chain of reasoning, draw a conclusion and predict the further development of the process under study.

Consideration of either the techniques sets or methods of the customer service personalization (Hills and Singh, 2012; "Product customization:

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Theoretical basics" 2005;) makes it necessary to find a compromise between mass customization and product personalization for a large number of consumers. In other words, how avoid losing personalization process due to increasing mass customization of the product.

In 1993 Pine B.J., Victor B. and Boynton A.C. (Pine, Victor and Boynton, 1993) pointed out that mass customization is a mode of production that aims for low production cost and high-speed mass production, and provides customized personalized products and services simultaneously. McCutcheon, D.M., Raturi A.S. and Meredith J.R. (Mccutcheon, Raturi and Meredith, 1994) have shown that customer needs and enterprise capabilities should be considered during the selection of mass customization strategies by enterprises.

Smith S. (Smith et al., 2013) puts forward the purpose, configuration, integration technology, modular design technology, and flexible production system and supply chain management method as a crucial feature for mass customization.

For Stitch Fix, Inc. the personalization is the Stitch Shuffle and Style Pass services which can be understood as an applied reinterpretation of the Schumpeterian theory of innovation in which the key activity "...emphasized human action..." in the newest understanding of deep integration between stylists and specialists in AI, Big Data and Deep Learning.

If we talk about peer-to-peer or linear interaction as an element of value proposition, it should be noted that the Stitch Fix, Inc. philosophy makes each customer feel special (Wirtz et al., 2019). A theoretical rethinking and analysis of the implementation of the theoretical framework allows concluding the importance of peer-to-peer (linear) interaction for the company. It means that after getting the next Fix the client feels the result of personal interaction with the designer and this fact increases the client's self-esteem greatly and makes sense of complete satisfaction. And this in turn acts as a strong motivator not only to remain a customer of the company, but also as a stimulant to expand the customer base, especially when pregnant women are in the focus group.

The next element of a company's value proposition is loyal pricing of the services (Dibb et al., 2013). It becomes interesting the unique combination of customer-oriented pricing: where the objective is to maximize the number of customers; encourage cross-selling opportunities or to recognize different levels in the customer's ability to pay on the one hand, and on the other hand the creation of a bottle neck, getting into which the customer feels pseudo-protection - paying $20 for the stylist service (a.k.a. package) or getting 25% discount if you buy the entire Fix. In all cases, the company will maximize profits, as Stitch Fix, Inc. CEO Elizabeth Spaulding said, "In Q4 we delivered $571 million in net revenue, reflecting 29% year-over-year growth, helping us cross $2 billion in annual net revenue for the first time" (Stitch Fix, Inc. (SFIX)).

And finally, perhaps one of the most interesting, but also the most controversial elements of shaping the value proposition of the company - demand forecasting based on AI. Of course, the objective selection of a set of clothing for all segments of the consumer market using the latest digital technology tools looks very attractive and generates increased interest from potential customers («I want to test it on myself»), as well as the ability to bridge the gap in demand through their own white-label clothing (called Hybrid Designs). But let's make an assumption, that the number of sets of clothes, included in one Fix, is limited as the potential demand of buyers, and consequently it is possible to assume, that expenses for huge computing capacities, which the company uses, are not always profitable because of possibility to offer the same sets of clothes, for example, simply on the geographical feature (West and East coast or UK), the probability of coincidence of two similarly dressed people being in the same place at the same time is extremely small. Thus, it can be assumed that Stitch Fix, Inc. irrationally uses financial resources to fund unclaimed computing capacity and produce results (set of clothes) that have already taken place.

The company Stitch Fix, Inc. successfully uses all possible tools to form the value proposition, while the efficiency is maximised only in case of combination and achieving synergistic effect. The analysis of marketing and pricing strategies of the company leads to the conclusion about the emergence of preconditions for deterioration of the market position - the current efficiency of the company (ROE = 6.73%) is lower than the average for the consumer staples sector (ROE = 15.61%) (Stitch Fix, Inc. (SFIX)). To stop this threat and gain an additional competitive advantage over, for example, Amazon.com, Inc., the company needs to abandon its incremental innovation strategy and focus on breakthrough innovation (radical Innovation) (Peter F. Drucker, 2002).

3 RESEARCH RESULTS

A review of the existing theoretical framework in the field of corporate governance (Garzón Castrillón, 2021) differentiates between a stock (an equity) and a share, and also between shareholder and stakeholder, whose common denominator is dividends, in the form of earnings per share (EPS), and are typically paid out four times a year (quarterly).

An interesting empirical fact for analysis is the survey of the stock performance of Stitch Fix, Inc. with given two features - the highest level of stock price was caused by the COVID-19 pandemic, which can be considered as the most favourable factor, but still a force majeure of objectively insurmountable force, and the dividend policy - the company has never declared or paid dividend, despite the fact that the common stocks, which have been listed on the NASDAQ since November 17, 2017. This fact is the most crucial cause to analyse. The vast majority of well-known methodologies for evaluating investment performance use indicators that are based on the company's dividend policy, which in this case can be treated as a factor that prevents high-quality analysis and obtaining the reliable conclusions.

It is therefore advisable to start with the Z-score methodology (Altman, 1968) with a linear combination of four or five common business ratios, weighted by coefficients. The original Z-score formula was as follows (Formula 1):

$$Z = 1{,}2X_1 + 1{,}4X_2 + 3{,}3X_3 + 0{,}6X_4 + 1{,}0X_5 \quad (1)$$

X_1 - ratio of working capital to total assets; X_2 - ratio of retained earnings to total assets; X_3 - ratio of earnings before interest and taxes to total assets; X_4 - ratio of market value of equity to book value of total liabilities; X_5 - ratio of sales to total assets. Zones of discrimination: $Z > 2.99$ – "safe" zone; $1.81 < Z < 2.99$ – "grey" zone; $Z < 1.81$ – "distress" zone.

The Z-score ratio for Stitch Fix, Inc. is calculated according to the indicators that characterise corporate financial indicators (in USD thousands) (Table 1) (Nasdaq.com, 2022):

Table 1: Financial indicators of Stitch Fix, Inc.

Period Ending:	7/31/ 2021	8/1/ 2020	8/3/ 2019	7/28/ 2018
Total Assets	$819,2	$769,4	$616,1	$481,6
Earnings Before Tax	-$61,1	-$47,7	$30,8	$54,7
Common Stocks	$2	$2	$2	$2
Capital Surplus	$40,7	$49,6	$116,7	$79,8
Treasury Stock	$416,8	$348,8	$279,5	$235,3
Other Equity	$3,4	$2,7	-$187	-
Total Equity	$460,9	$401,0	$396,0	$315,1
Total Liabilities & Equity	$819,2	$769,4	$616,1	$481,6
Long-Term Investments	$86,089	$95,8	$53,4	-
Short-Term Investments	$101,6	$143,0	$143,3	-
Total Revenue	$2,101,3	$1,711,7	$1,577,6	$1,226,5
Gross Profit	$947,6	$754,2	$703,129	$536,0
Net Income	-$8,9	-$67,1	$36,881	$44,9

The calculated Z-score ratio for Stitch Fix, Inc. is in the following value (Formula 2), which characterises the position in the financial stability zone.

$$Z = 1{,}2 \times 1{,}43 + 1{,}4 \times (-0{,}04) + 3{,}3 \times (0) + 0{,}6 \times (0) + 1{,}0 \times (2{,}86) = 4{,}5076 \quad (2)$$

All investors as sufficient to pursue their investment interests and to shape the current situation on the NASDAQ exchange can describe current performance.

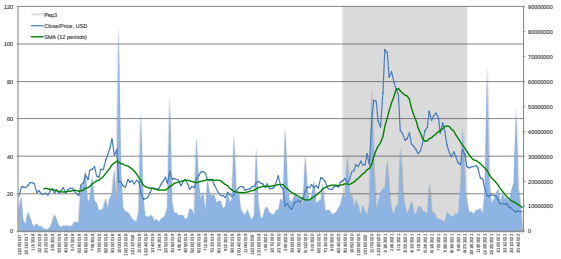

Figure 1: Stitch Fix, Inc. stock quotes (Nasdaq.com, 2022).

If we exclude the darkened area as objective positive force majeure circumstances, it can be argued with a certain degree of probability that share price, trading volumes do not exhibit significant volatility.

This to some extent defines and confirms the structure of Stitch Fix, Inc.'s core institutional investors, which are shown in Figure 2.

Analysis of the structure of the main institutional investors of Stitch Fix, Inc. shows that at December

31, 2021 it was characterised by the following parameters:

the new investors have become Norges Bank (0,9% of total shares held; $7,8 mln.) and Federated Hermes Inc. (0,8% of total shares held; $6,6 mln.);

incumbent investors such as Working Capital Advisors (UK) Ltd. increased the number of shares by 22.3%, allowing this investor to surpass 14% ($125.1 mln.) of total shares held. The second place belongs Vanguard Group Inc., which increased its portfolio on 17% up to 10% ($84.3 mln.) of total shares held;

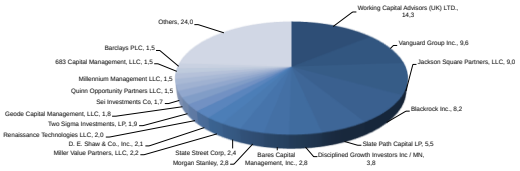

Figure 2: Stitch Fix, Inc. institutional holdings, % (Nasdaq.com, 2022).

it is worth noting the portfolio held by Morgan Stanley down to 3% ($24.8 mln.) of total shares held and investment company D.E. Shaw & Co., Inc. which reduced its holdings in Stitch Fix, Inc. by a quarter down to 2% (%18.4 mln.);

it is interesting to analyse the investment process at Stitch Fix, Inc. is the quitting out Spyglass Capital Management LLC, which held 5% of the total shares.

It should be noted that return on equity (ROE=6.73%) is low and Stitch Fix, Inc. is not efficient enough. EBITDA margin is below average for the consumer staples sector. According to the presented financial multipliers (Table 2) it is fairly valued and interesting to buy.

Table 2: Financial multipliers of Stitch Fix, Inc.

	2019	2020	2021	2022	Last t12 (LTM)	Average for consumer	Average for last 5 years	CAGR 5
P/S	1.6	4.75	0.9		0.5	2.49	1.81	-17.4
P/BV	6.4	19.45	4.3		2.39	8	7.53	-14.07
P/E	99					29.56	100.17	-15.02
EV/EBITDA		-175.02	-84.71		-346.67	4.44	-202.13	25.59
ROE, %	10.	-13.71	-2.06		-6.73	26.84	1.35	-181.38
	37							
ROA, %	6.72	-5.32	-1.12		-2.57	6.17	1.47	-176.8
ROIC, %	9.06	-12.64	-1.51		-3.26	15.15	2.1	-170.39
Z-score			5.99	4.51	4.51	4.15	5	-9.03

Earnings per share (253.57%) and EBITDA (596.21%) are both at a high level and worth looking at for a buy.

Businesses that seek to maintain a sustainable competitive advantage aim to be the leader in industry for years or decades, they don't simply try to achieve the best results in a single quarter. Sustainable competitive advantage requires continual improvement throughout the business, continuous improvement of product or service and the development of new concepts (Barringer and Ireland, 2015). Companies with phenomenal product quality, which want to achieve sustainable competitive advantage, do not just create one winning product, they keep iterating and expanding their offerings to capture more and more market share over time (Grant, 1991).

Before formulating proposals to strengthen existing and create new instruments of sustainable competitive advantage for Stitch Fix, Inc. in the intense competition from the Amazon.com, Inc., it is appropriate to formulate basic conceptual statements about Amazon's value proposition. An analysis of the main sources of available information (Galloway, 2018) shows that Amazon.com, Inc. is successfully implementing a profit maximisation strategy through a phased alternation of cost-minimising means in the digital sphere and the physical world.

In other words, if we trace the financial and technological history of Amazon.com, Inc., we'll see that physical and digital technologies have been complementing each other: e-commerce and shopping web page successfully coexisting with Amazon cashier-less grocery store using "Just Walk Out" technology that also powered 25 Amazon Go stores, successful traditional logistics services for themselves or for third parties are complemented with pioneering developments in autonomous driving - Amazon.com, Inc. acquired Zoox, a California-based start-up that develops autonomous driving technology in a deal estimated to be worth over $1.3 billion and has invested in one of the top autonomous driving start-ups Aurora, and it has tested self-driving trucks powered by self-driving freight start-up

Embark. Such similarities can be identified in almost all areas of Amazon.com, Inc.'s revenue generation. This allows forming a sustainable competitive advantage for Amazon.com, Inc.

4 DISCUSSION OF RESULTS

Let's now consider the existing and potential sources of Stitch Fix, Inc.'s sustainable competitive advantage in organisation-wide optimization, continuous product improvement and the development of new concepts. In the area of organisation-wide optimization, Stitch Fix, Inc. recruited Walmart.com COO Mike Smith as well as Netflix's VP of Algorithms Eric Colson and Julie Bornstein, the former Head of Marketing and Digital initiatives at Sephora are still part of the company's leadership team. This will have a positive impact on generating new ideas aimed at increasing competitive advantage in the long-term period through continuous product improvement, starting with expanding the company's own range of clothing offerings (Hybrid Designs).

As a recommendation, giving the consideration to providing a discount on a future Fix (and/or Style Pass) for the return of self-made garments that have been purchased but not used (brand new) or have been purchased and used within six months/year can be suggested. The tool presented will increase customer lifetime value and sale per customer that reached $518, up 18% in 2021 over 2020. In addition, Stitch Fix, Inc. will be able to increase reputational benefits as an eco-friendly corporation that operates under the recycling philosophy of the SDGs, also known as the Global Goals, that were adopted by the United Nations in 2015 (The 17 goals, 2022).

Blue Ocean strategy is about creating and capturing uncontested market space, thereby making the competition irrelevant. It is based on the view that market boundaries and industry structure are not a given and can be reconstructed by the actions and beliefs of industry players (Chan and Mauborgne, 2005; Blue Ocean Strategy & shift: Create New Market space and make the competition irrelevant, 2021).

One of the main building blocks of Stitch Fix, Inc.'s business model is the processing of large amounts of data. It is the personal information about customers, including height, waist size, chest size and other anthropometric characteristics. Based on this data a garment selection process takes place. It is logical to suggest that these parameters should not only be used, but that they should also be tried out by app-based means to correct body shapes through a suggested set of physical or sport activities with a personalised trajectory, as well as the composition of a nutritional kit, which should help to achieve the target parameters more effectively (Figure 3).

As a motivational incentive (prize), Stitch Fix, Inc. may offer a free Fix for significant results or an increased discount on premium clothing brands. It should be noted that there would be an opportunity to sell S and XS sizes, which are usually not in high demand position and lead to increased storage level, which is an extremely negative factor for economic efficiency in general.

But the most important feature of the offered combination is the possibility to concentrate in one place a large amount of personal data. The safety and protection of this information are the important factors in consumer preferences.

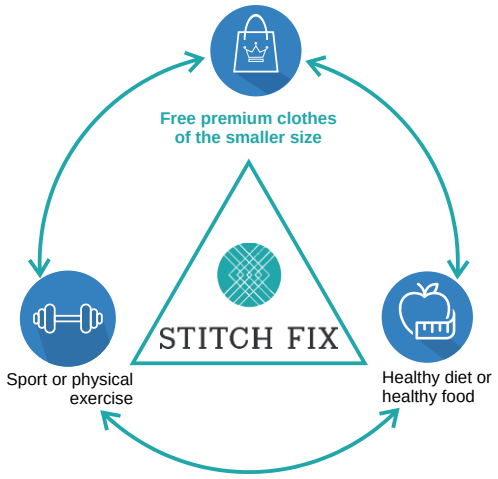

Figure 3: Stitch Fix, Inc. Blue Ocean strategy recommendation.

Thus, this recommendation, which is based on well-known and widespread digital products, consists of a new combination of them and gives Stitch Fix, Inc. a possibility to open up or even create a niche in the market where there will not be any competition for some time, which is a key characteristic of the Blue Ocean strategy.

Perhaps this slowdown is short term in nature due to two factors. Firstly, users were confused with how the company led them between its Fix service, which involves curated batches of apparel, and its "freestyle" offering that is more like traditional e-commerce shopping.

Top-line revenue grew 3% year over year to $517 million in Q2 of 2022 financial year which ended January 29, 2022, along with gross margins of 45.1% and $10 million in adjusted EBITDA, that was previously have withdrawn our full year ratio. Net

revenue per active client reached a new record high of $549 in the second quarter and freestyle revenue grew at nearly 30% year over year. Stitch Fix ended the Q2 of 2022 year serving approximately 4 million active clients, an increase of 4% from a year ago, but active clients declined 4% quarter over quarter.

The main reason is largely impacted gross adds - conversion of new visitors for fix and freestyle is not where it was prognosed previously and mentioned above. Q2 gross margin was 45.1%, representing growth of 214 basis points from a year ago, primarily driven by leverage in shipping costs due to higher average order values and improved product margins (Stitchfix.com, 2022).

Net actives of Stitch Fix, Inc. were also impacted by iOS 14 privacy changes that limited ability to target and measure advertising, as well as higher dormancies due to lapping the high dollar referral program for new customers in the first half of 2021.

In an effort to launch and promote freestyle, Stitch Fix, Inc. chose to direct visitors coming to stitchfix.com toward the freestyle experience. It is important to note that stitchfix.com is the primary landing page for customers interested in ordering a fix. Therefore, in leading clients to the freestyle experience first, Stitch Fix, Inc. inadvertently created friction for those seeking a fix. In an effort to mitigate this friction, Stitch Fix, Inc. is beginning to direct stitchfix.com traffic to a clear and easy fix onboarding path.

It should be noted that the launch of Stitch Fix, Inc. freestyle has made it much more difficult to buy men's clothing, i.e. the lack of possibility to buy them as a one-off online as it can be done for women clothes. In addition, female clients can't get to mens brands through their own account.

The main conclusion about the problematic situation at Stitch Fix, Inc. can be described as a lack of a clear understanding about the nature and quality of customers, i.e. there is no answer to the question of what is better to achieve performance growth: to maintain the number of higher-quality customers or to increase the customer base by attracting lower-quality customers through available and developed omni-channel methods.

Despite these negativities faced by Stitch Fix, Inc., it should be noted that the significant institutional investors such as Vanguard Group Inc. and Blackrock Inc. increased their investments by 10% and 8% respectively. They are also the same significant institutional investors for Amazon.com Inc. This builds strong confidence in future positive developments because of possible insider information that is not publicly available.

So fixes were about flat in terms of reactivations, but freestyle was a whole new channel of being able to reactivate clients. And I think part of that is signing up the right way to reach and meet the attention of those clients as there were expanding Stitch Fix ecosystem. This opportunity related to Freestyle offering, including that Freestyle will unlock a much larger total addressable market and is an engine for growth and that is why Freestyle will provide leverage in overall margin.

We've learned that Freestyle First clients are coming primarily through product listing ads and other marketing channels that were not available to us prior to launching freestyle. Stitch Fix should continue to test, learn, and iterate on how best to use these new marketing channels. Improving the freestyle client experience and converting more visitors to active clients and make freestyle the growth engine. Freestyle revenue grew 29% year over year, and penetration from our fix business is steadily improving with over 32% of Stitch Fix women's fix clients purchasing via freestyle today. In this case, we suggest making a change to the pricing and filling of one Fix: to offer another set of 3 items instead of 5 and the stylist fee is $10 instead of $20, taking into account the traditional 3 days for trying on clothes. To compensate for the cash flow, the services of an earlier suggested set of physical/sport activity and heath nutrition as part of an existing subscription can be offered or offer a new one with 25% discount.

At the same time, in Stitch Fix kids and U.K. businesses, where were 19% and 73% growth, respectively, on a year-over-year basis it is advisable to propose expanding the number of brands for men firstly and to think about targeting geographical areas of supply, for example to EU countries.

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