



Creative Critters Distribution Dilemma

John Thompson is facing a situation that is limiting the potential international growth of his employer, Creative Critters. The mid-western based company only has a distribution warehouse in Kansas City, Missouri. Currently the independent franchise outlets around the world order directly from the Chinese suppliers in very small lots. The suppliers charge very high fees for the smaller orders, making it very difficult for solid profits to be made. Customer service is poor, creating an army of very unhappy franchisees demanding the director of Creative Critters supply chain operations design a more efficient and cost effective distribution operation.

In 1992, while enjoying time with her grand-daughter Briley, Rose McDonald began to think about how to create stuffed animals that reflect the preferences of children. At first, Rose made a few animals out of scrap material allowing Briley to help stuff the items to the firmness she preferred. Noticing that Briley named the "critters" as each was "stitched up", birth certificates were made by hand with the date that the specific critter was completed. Briley shared her new found friends with playmates and at school. Soon mothers, aunts and grandparents were calling Rose requesting special items for gifts based on the favorite stories or animals of a child in their life. Teachers were also requesting critters to use in the classroom for storytelling.

So by 1994, Rose found a high traffic retail location in a suburb of Kansas City to launch a store for guests to come and select a pre-made animal skin to stuff and dress as desired. A computer and printer kiosk was added to print out birth certificates for each critter on the day "it came to life". The response to the concept was overwhelming. Within months Rose had many requests for franchise options, staff was needed to assist in creating the product offering,

expand communication, creating a brand image and working with suppliers. Quantity requirements grew to the point that contract manufacturers Xian, China supplied all the clothing items and the animal exteriors to Rose's specifications. Rose got licensing agreements for major sports team clothing as well as children's movie and storybook characters. This had a major impact on market growth as more adults wanted to make and own their favorite team mascot. The average amount per sale for each store visit is \$54.

Originally, growth of the company was organic and the majority of the Creative Critters retail outlets are company-owned. Of the 638 outlets worldwide, only 86 are franchise operations (appendix B indicates criteria). These are mostly located in Africa and Asia. Approximately one third of the retail outlets are actually located outside the United States (appendix B). Revenue for 2013 was 390 million USD with franchise fees only making up 9% of the total income. Sixty percent of revenue comes from the U.S. market but that has been declining approximately 2% each year due to the rise of middle class consumers around the globe.

Additional retail franchises are currently not available until John Thompson can come up with a more cost efficient supply chain to service the current franchisees. In an effort to gather solid proposals, John has enlisted several cross-functional teams to assess and prepare strategic implementation priorities. Due to the pressure from the new management team, teams have just three weeks to develop proposals to present to various upper managers at a strategic management planning retreat. The chosen plan will be implemented by John Thompson and team members who developed it with a promise for a financial bonus.

Initially, as the first franchises began opening, the independent ordering system of licensed items appeared to be totally equitable. When entering a new market, a special critter was designed based on a country tradition, such as clothing style, to gain interest by potential customers. The suppliers did not differentiate between franchise and company orders. All items were sold FOB Nanjing, China even for the smaller volume franchisees. The terms of sale made the transactions much easier for inexperienced franchise importers. The value of economies of scale was shared by the entire network.

However with company growth, management views on purchasing became more focused on costs. Rose McDonald became more of a silent partner than a driving force in the company, so new senior managers put pressure on the main suppliers in China to reduce costs for Creative Critters main operations. Unknown to new purchasing managers, part of the costs to franchisees were absorbed with the overall prices charged to the company. With the pressure

for price to the reduction, suppliers tacked the costs on to the orders for franchisees. Now the sales terms for the smaller orders changed to EXW Xian, China requiring complicated Chinese paper work is completed by less experienced purchasers, not the Creative Critters headquarters.

So not only were franchisees hit with higher costs but also more paperwork and longer lead times. Depending on the size of the order and shipping location, the cost for the franchisee can be 20 to 35% higher than for the company. This greatly erodes the profit potential of stores. Recruiting new franchisees has become extremely difficult based on the current supply chain complications. Labeling requirements also differ per country so again franchisees had to handle the extra printing and tagging costs.

John has made an initial list of possible options to consider to overcome the current dilemma.

1. Warehousing
 - a. Stay with one U.S. location
 - b. Add additional warehouses in U.S. or abroad
 - c. Ideal location(s)
 - d. Services provided to franchisees
2. Shipping and ordering
 - a. Continue requiring direct orders to licensed suppliers from franchisees
 - b. All orders processed by CC Headquarters
3. Possible change of suppliers
 - a. Less complicated country regulations
 - b. Lower costs
 - c. Located closer to international outlets
4. Tagging requirements
 - a. CC Headquarters handle
 - b. Franchisees continue responsibility
 - c. Suppliers provide stock already tagged
5. Costs
 - a. Inventory holding
 - b. Order processing
 - c. Handling
 - d. Shipping

Teams should consider these various items but are encouraged to be creative in developing a solution and a plan of action. While short-term success is essential for current franchisees and company stores, consider this proposal as a foundation for future franchise growth.

APPENDIX A- Franchise requirements

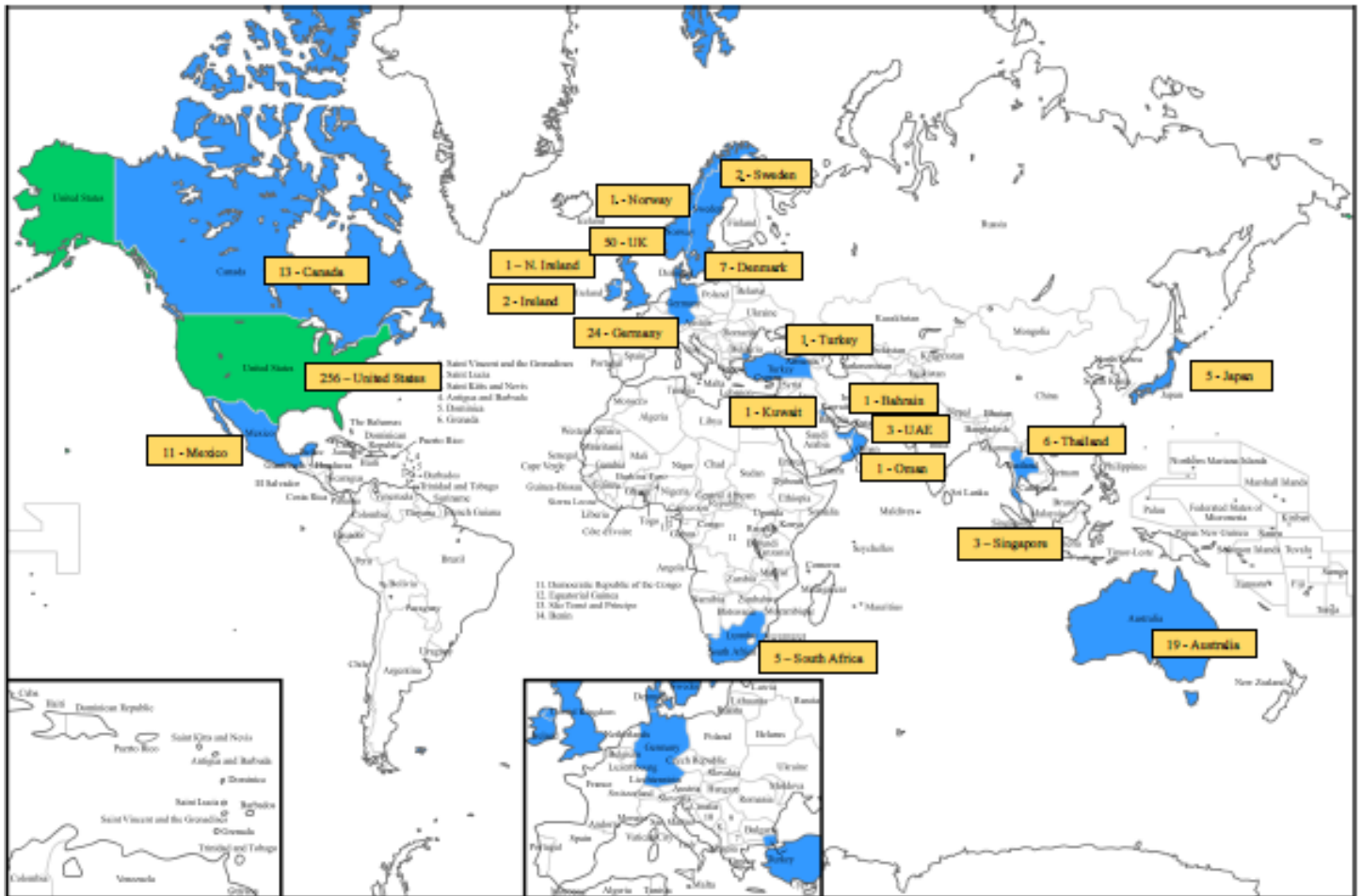
Ideal Franchisee:

- Strong background in retail or franchise operations,
- Extensive knowledge of local real estate market,
- Commitment to develop the Creative Critter operations for the entire country or region being contracted,
- Ability to support at least 15 stores,
- Must reside in the territory of franchise territory
- Minimum capital net worth.

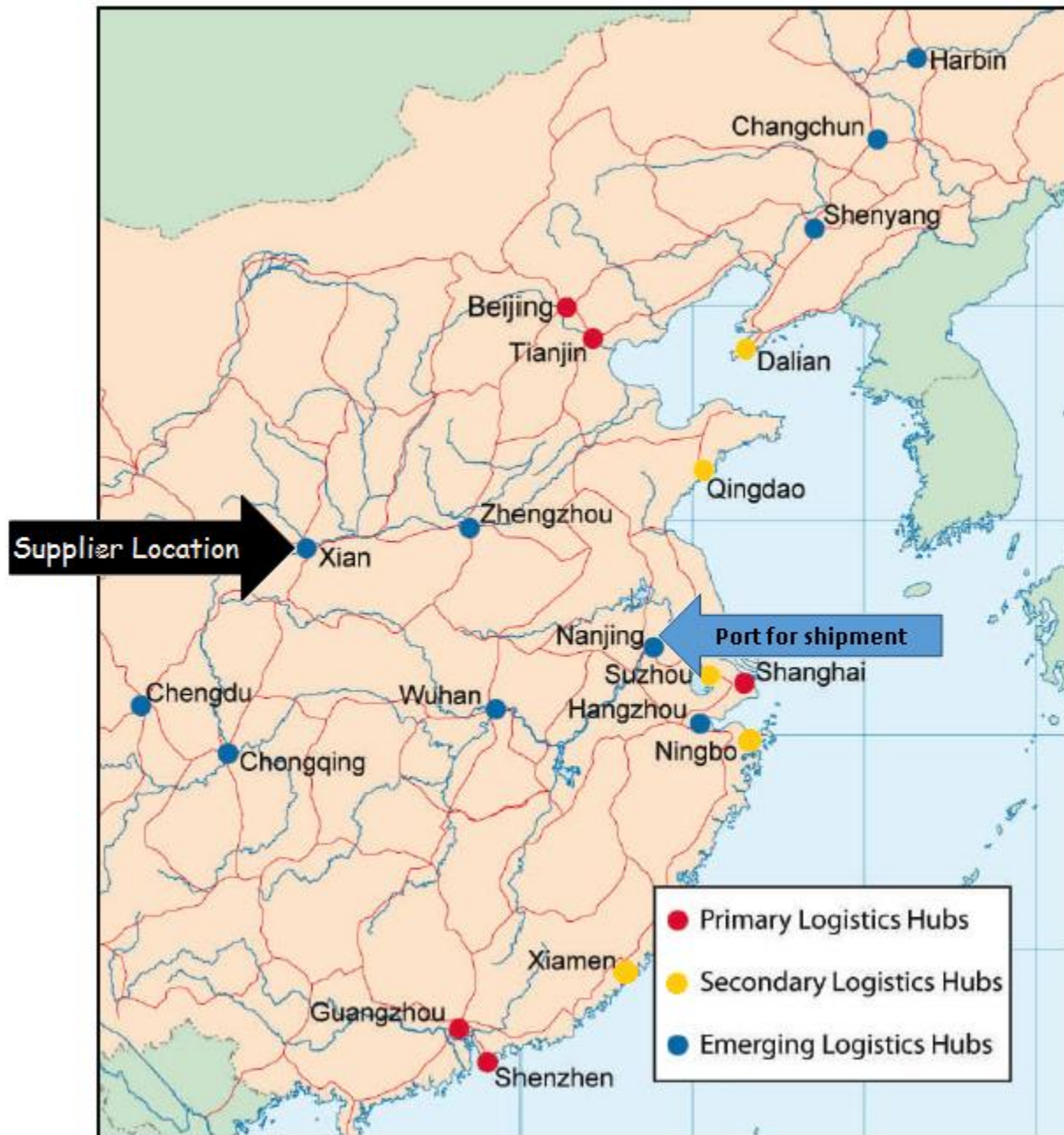
Depending on the economic environment of a country or territory, between 5 and 12 million USD may be required for start-up of the franchise.

Franchise contracts are set at a minimum of 5 years with renewal decisions made on overall performance of the franchisee.

APPENDIX B- Store locations



APPENDIX C- Current Supplier location



Map courtesy of Transport Intelligence.

The suppliers were chosen when a group of business professionals came to Kansas City from the Chinese sister city of Xian early in the company's development. Rose supported the sister city concept and felt it important to do business within the established economic and political relationship.