

Rules change in the global marketplace

As flexibility, short production runs and responsiveness to market demands become the survival factors for 2010, can global supply chains deliver performance as well as price? By **Nick Allen**.

How a company behaves in one part of the world can have huge ramifications for the way its reputation and brand are perceived in another.

This year China is set to overtake Japan as the world's second largest economy based on gross domestic product. Its continued growth throughout the global recession reflects the gathering strength of its own domestic demand and the West's dependence on goods manufactured in China.

But with Western companies set on outsourcing manufacturing to this booming economy, how well are corporate supply chains aligned to the task? Are these lengthy chains robust enough? How do you gain visibility of activity across your supply chain – and how do you determine the true costs of global sourcing?

There are many considerations to take into account when companies choose to outsource to distant shores, complexity that goes beyond a pure cost-per-piece calculation.

Procurement professionals need to fully understand the dynamics of supply chain performance over such long distances and the impact this will have on inventory holdings, capital requirements, transport costs, responsiveness to market changes and the heightened exposure to supply chain risks.

For instance, Western brands are susceptible to corporate social responsibility (CSR) risk in emerging economies and it's not just fashion brands that are at risk.

So, just what procurement practices and strategies are being used to mitigate the supply chain risks associated with extended, and in many instances brittle, supply chains? One significant development that has occurred over recent months is the move by shipping lines to mothball fast but fuel-hungry container vessels – built for rushing Chinese goods to the US – using instead slower moving, larger and more economic container ships.

The net result is an extra few days on the lead-time for goods arriving from the Far East. This may not sound a great deal, but holding inventory for even a few days more can add to costs and impact responsiveness. In uncertain times procurement professionals want greater flexibility, not longer lead-times.

There is rising anecdotal evidence of companies reconsidering their sourcing strategies, with some

moving manufacturing back closer to Western markets.

"Buyers are looking for shorter production runs and they are looking for flexibility," says Stephen Rinsler of Bisham Consulting.

"The problem with long supply chains is that they are not flexible. A retailer of electrical units may have one technology in store, another on the water and yet another technology in production – what happens if the first technology doesn't sell too well?"

According to Rinsler, there is some evidence that a growing number "may be doing their first production run a long way from home, but their top-up runs much closer to home – mainly in Eastern Europe. There are a lot of issues around demand planning, production planning, timing of acceptance of stock, getting it into the store and selling it through.

"There are signs that some companies have found that the costs of getting it wrong are too high and they are starting to outweigh the benefits of lower manufacturing costs. If you want smaller quantities – because you want to change your stores much more frequently – you need to be much closer to home. Only then are you able to cope with the change in design, pattern, colour, and specifications needed for fast changing markets, such as with technology goods," says Rinsler.

Distant

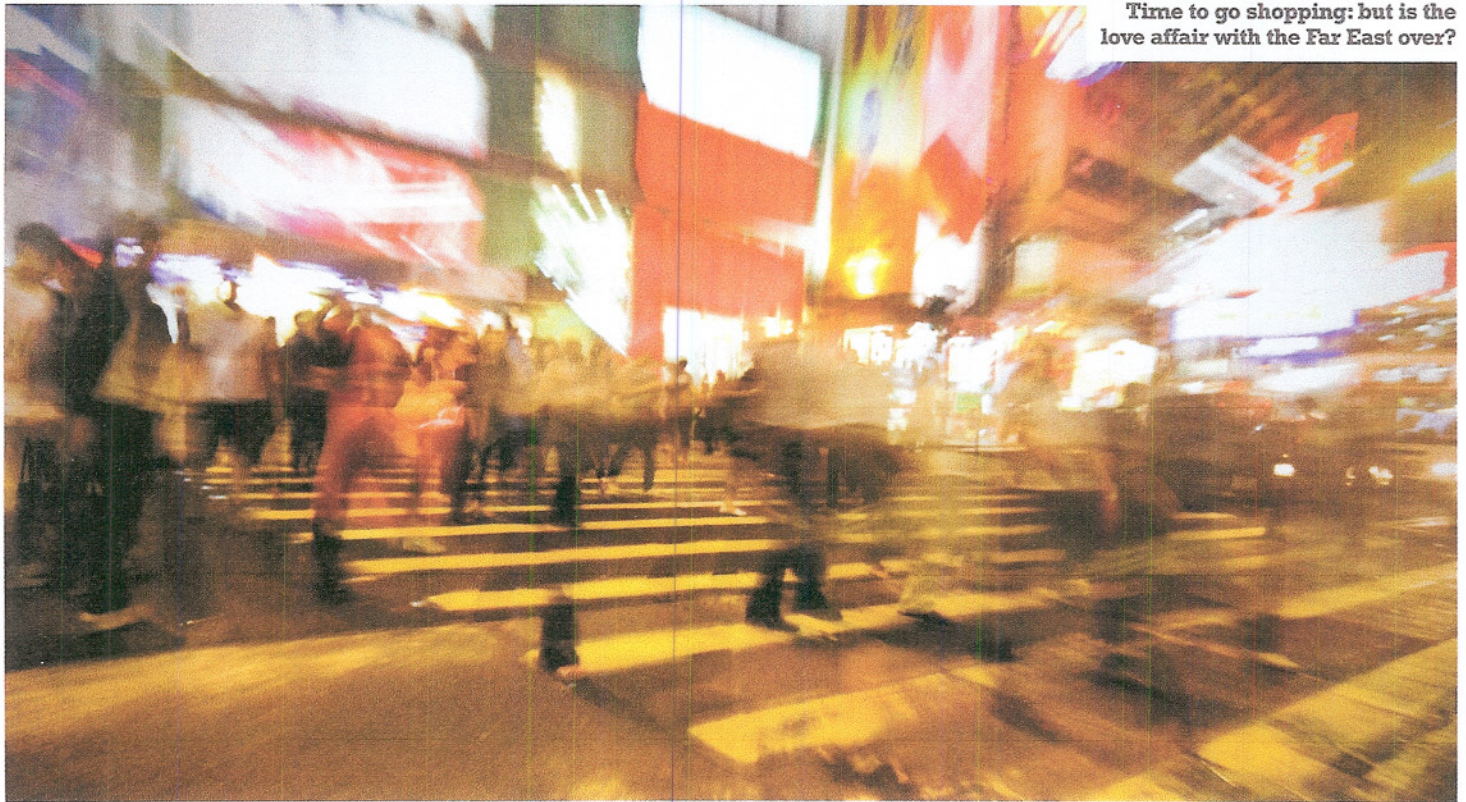
However, if distant sourcing is the considered way forward, Andrea Harris of Davies & Robson has some advice. "Contingency planning, in particular, is critical as inexperience in the mechanics of long-distance supply chains is often to blame when new outsource solutions stumble. The true cost of contingency and associated time delays can be grossly underestimated. Dealing with distant suppliers exposes businesses significantly more to risk than dealing with a 'mate' down the road who, with a bit of friendly persuasion, will do a short production run in a quick turnaround."

A significant consideration for buying organisations sourcing from suppliers in distant locations is the potential for exposure to risks related to corporate social responsibility. Damage to corporate reputation and brand are central concerns for businesses operating in a global market. How a company behaves in one part of the world can have huge ramifications for the way its reputation and brand are perceived in another.

And nowhere is this more important than in how an enterprise sources its products and services.

According to Colin Maund, chief executive of supplier management services provider, Achilles Group: "Being absolutely certain that suppliers, wherever they may be in the world, are compliant and responsive to a buying organisation's corporate social responsibility policies is critical to protecting the brand. The risk to brand value from a supplier, or a sub-contractor to the supplier, using child labour, for instance, is immense."

However, he believes many companies perceive this risk as one primarily affecting the retail sector, following coverage in the press of incidents with suppliers to



Time to go shopping: but is the love affair with the Far East over?

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Primark and Gap, for example.

"Few outside of retail consider the damage that may ensue from, say, the discovery that a boiler suit used by a major oil company was produced using child labour, or that a hose component sourced by an engineering company was manufactured under appalling working conditions," says Maund. "No company can divorce itself from the errant policies and practices of its suppliers."

As those in the retail sector have determined, ethical audits of suppliers are necessary for reducing exposure to this potentially highly damaging source of risk.

"It is important that other sectors too recognise the importance of monitoring suppliers in this way," he says.

Undertaking a proper ethical and social audit is a highly skilled activity requiring knowledge of the process, of CSR issues and of good auditing priorities. In particular, many suppliers will be adept at presenting only that which they wish to be seen. Maund points out that there have been cases where several sets of books have been kept, giving very different perspectives.

"Sending a buying team in to a supplier with no particular training in this area could be more damaging than not sending one in at all," he says. "At least by not sending a team in you are not under the impression that you are protected."

In recent weeks an important collaborative initiative from within the electronics sector seems set to have an influence on the way many industrial sectors will monitor suppliers with regards to CSR risk.

At the beginning of March, Achilles and the Global e-Sustainability Initiative (GeSI) signed a memorandum of understanding to set a new three-year strategic plan to drive forward the Electronics Tool for Accountable Supply Chains (E-TASC).

Subscribers enter details on how their supply facilities manage and reduce their labour, social and ethical, environmental, and health and safety risks and share the information, through the online tool, with their customers. In this way they drive continuous improvement in the supply chain.

Although E-TASC has been used extensively by the

electronics industry since 2007, with over 1,000 supply facilities on the system and over 50 global brands now subscribing to it, the new agreement puts it in a strong position to be adopted by other industries for managing CSR compliance globally.

Much of the focus within organisations over the past 18 months has been on containing costs and in particular, on improving efficiencies within procurement and purchasing departments. It's easy to understand as a small percentage saved on each item purchased can deliver a huge improvement to your profit margin.

Andrew Spence, supply chain business development director at Oracle, sees one of the biggest challenges facing many organisations – particularly those that have been through an acquisition – is in getting a single view of spend across individual category areas and with a single supplier. Often a supplier can be represented in different ways across different systems.

Disparate

Consolidating this information from across disparate systems using master data management tools helps identify situations where supplier "A" in one business unit may be known as supplier "B" in another.

He says by feeding this consolidated information into an analytics process a clearer view of spend can be achieved across the enterprise. Then there is spend classification, which is the ability to apply automated classification rules to your purchase orders.

"Most procurement managers will recognise that when they view an analysis of their spend an awful lot comes up as miscellaneous. What spend classification tools do is go through the data, and using certain rules, relate an invoice, say, to an order," says Spence.

The application of analytic tools to this consolidated data enables procurement departments to see exactly what they are spending across categories with each supplier. Spence points out: "If, for example, you were able to procure this item at the lowest price we have seen you buy it at over the last year, we reckon you would save this amount of money."