



SUPPLIER COLLABORATION:

WHY IT'S VITAL TO TREAT KEY SUPPLIERS
AS AN EXTENSION OF YOUR ORGANIZATION

By 2010, more than half of all manufacturing will be outsourced, according to a recent survey of 300 firms.

EXECUTIVE SUMMARY

In the past 30 years, outsourcing has gone from a novelty to a generally accepted business practice for manufacturers in the Western world. Many enterprises now outsource most of their manufacturing to lower-cost regions, especially in electronics and high-tech.

But while outsourcing saves money on production, results have not been stupendous. One survey¹ of 300 enterprises revealed that on average, outsourcing saves at most 17%. And it can add cost to other functions, especially supply chain management during times of high fuel prices.

In the past, when most production was performed within the enterprise, managers had good visibility into production and short-term flexibility to deal with any supply chain challenges. But today, outsourcing and off-shoring have increased the number of tiers in the supply chain, greatly reducing the visibility of brand owners and making them dependent on remote suppliers for business results.

Key suppliers must be brought into the decision-making process, so that brand owners can exchange early warnings and help resolve supply chain issues. In a recent article², Tim Harden, president for supply chain and fleet operations with AT&T stated that,

“The Domain Supplier program will facilitate a more collaborative relationship with our network technology suppliers. It also enables AT&T to minimize risk to our supply chain, improve supplier performance, and increase the speed of introduction of new products and services while offering AT&T the best technologies to serve our customers.”

There can be no stronger statement of the value of a closer and more collaborative relationship with key suppliers.

OUTSOURCING IS HERE TO STAY

According to a recent study³ by Duke University and The Conference Board, an independent research association, companies continue to send work off-shore. While there has been some political pressure to reverse this trend, the recession has increased the financial pressures to outsource and off-shore.

Between 2005 and 2008, the number of American companies with an off-shoring or outsourcing strategy more than doubled, says the report, and few plan to relocate these activities back to the U.S. In fact, 60 percent of companies currently off-shoring say they have aggressive plans to expand these activities.

1. Shoshana Cohen et al, “Global Supply Chain Trends 2008-2010” PRTM, 2008, page 6. Retrieved Sept 22, 2009 from http://www.prtm.com/uploadedFiles/Strategic_Viewpoint/Articles/Article_Content/Global_Supply_Chain_Trends_Report_2008.pdf

2. “AT&T Readies Its Supply Chain for the Future” *Supply & Demand Chain Executive*, September 8, 2009. Retrieved Sept 22, 2009 from [http://www.sdcexec.com/web/online/SourcingProcurement-News/ATandT-Readies-Its-Supply-Chain-for-the-Future/27\\$11657](http://www.sdcexec.com/web/online/SourcingProcurement-News/ATandT-Readies-Its-Supply-Chain-for-the-Future/27$11657)

3. Tom Heijment, “Fifth Annual Conference Board/Duke Offshoring Research Network Survey” The Conference Board, August 3, 2009. Summary retrieved Sept 22, 2009 from http://www.conference-board.org/utilities/pressDetail.cfm?press_ID=3709

Supply chains that extend to third-party manufacturers around the world require a lot more flexibility.

For example, by 2010 more than half of all manufacturing will be outsourced by the 300 firms surveyed by management consulting firm PRTM⁴. The following table shows these numbers for four sectors.

Percentage of Manufacturing Outsourced		
Sector	2008	2010
Automotive & Industrial	33%	45%
Consumer Goods	46%	53%
Electronics & High-Tech	49%	60%
Life Sciences	39%	48%

Source: Summarized data from "Global Supply Chain Trends 2008-2010," PRTM (pages 14-21)

While Footwear & Apparel were early adopters of outsourcing and off-shoring, Electronics & High-Tech have taken this to a new level in which a global supplier like Cisco reports that 95% of its production is outsourced, giving it a massive global supply chain.⁵

Some of these companies have completely outsourced their manufacturing, while others have retained core products in-house and outsourced the non-core items. In either case, the competencies required to manage a supplier should be quite similar to those needed to manage in-house production. After all, production information needs to be shared between departments and work centers as the output of one is input into the next, to name a few:

- ▶ product changes and coordination of engineering releases;
- ▶ schedule and inventory information constantly needs to be reviewed, planned and coordinated; and
- ▶ demand changes that will impact the downstream supply chain.

Of course, much of this outsourcing flows to low-cost regions such as China, India, and Eastern Europe. Manufacturers are keen to benefit from dramatically lower labor costs in these destinations, even if they are halfway around the world.

BUT BETTER RESULTS ARE ELUSIVE

But has off-shore outsourcing paid off for manufacturers? Is the transition from "make" to "buy" as smooth as it needs to be for flawless execution and solid ROI?

Not according to the PRTM survey⁴, whose respondents are achieving only 17% cost saving from outsourcing. While labor costs are reduced by 26% and material costs by 18%, management and overhead costs are being trimmed only slightly, which reduces the overall savings.

4. Shoshana Cohen et al, "Global Supply Chain Trends 2008-2010" PRTM, 2008, page 4. Retrieved September 22, 2009 from http://www.prtm.com/uploadedFiles/Strategic_Viewpoint/Articles/Article_Content/Global_Supply_Chain_Trends_Report_2008.pdf

5. Kevin Harrington and John O'Connor, "How Cisco succeeds at global risk management," *Supply Chain Management Review*, July 1, 2009. Retrieved September 22, 2009 from www.scmr.com/article/CA6672233.html

Simply off shoring
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“A gap does remain between aggressive plans to ‘go global’ and actual realization of the anticipated payback,” says the report. “Many companies claim that potential benefits are lost due to lack of efficient processes and supply chain coordination.”

It turns out that managing supply chains that extend to third-party manufacturing partners around the world requires a lot more flexibility. In fact, “limited supply chain flexibility” is cited by 60% of the PRTM respondents as a major barrier to ongoing globalization.⁶

LOW-LEVEL DATA EXCHANGE IS NOT ENOUGH

“Simply off-shoring more functions isn’t the solution,” says Arie Lewin, professor of strategy and international business at Duke University, and director of the Center for International Business Education and Research. “To achieve real savings, companies need to get the process right.”⁷

Manufacturers traditionally have a double standard when it comes to communicating and collaborating with suppliers versus internal operations. Perhaps it is because operations are often and appropriately looked upon by the supply chain organization as the customer. While this is true, the internal operations is also a supplier of materials and information and they require the same inputs that any supplier needs to execute flawlessly.

Even within mature supply chain organizations the supplier is treated with an arms-length relationship, information being provided on a “need to know” basis. While this may have been sufficient in the past, competitive pressures and the economy have demanded more and more flexibility from a company’s Supply Chain. Once again, in PRTM’s report⁶, they highlighted a number of barriers to globalizatoin, including a number that are of particular importance to supplier collaboration, including

- ▶ lack of supply chain flexibility,
- ▶ lack of internal competencies to manage external partners, and
- ▶ partners unable to meet flexibility requirements.

One could argue most of the barriers cited are influenced by the quality of the collaboration process when it comes to communicating changes in demand, supply, process requirements, quality requirements, cost targets, etc. How these factors are managed will determine the level of flexibility or agility of your extended supply chain.

Certainly there has been good progress in initial collaborative tools of the tactical nature; with sending electronic MRP forecasts, purchase orders, expedite notices and ship signals. From the tactical perspective, the state of supplier collaboration is in good order. Trading partners have been able to exchange office-style documents like spreadsheets and reports since the start of the outsourcing boom. For years, EDI systems have sent transaction notices up and down the supply chain, provided the partners have the required technology infrastructure. Today, most supply chain managers can send and receive electronic documents quickly, such as MRP forecasts, POs, expedite notices, and ship signals.

6. Shoshana Cohen et al, “Global Supply Chain Trends 2008-2010” PRTM, 2008, page 9. Retrieved September 22, 2009 from http://www.prtm.com/uploadedFiles/Strategic_Viewpoint/Articles/Article_Content/Global_Supply_Chain_Trends_Report_2008.pdf

7. “Fifth Annual Conference Board/Duke Offshoring Research Network Survey” The Conference Board, August 3, 2009. Summary retrieved September 22, 2009 from www.conference-board.org/utilities/pressDetail.cfm?press_ID=3709

Then why are there still issues? Can't solid decisions be made quickly by sifting through a pile of transaction notices? Can't tradeoffs be balanced, issues resolved, and business results delivered by wading through massive spreadsheets? Are these tactical tools not enough?

A MORE COLLABORATIVE RELATIONSHIP IS NEEDED

The concept of a "maturity model" has been applied in various ways to supply chain management. The following table shows the PRTM Supply Chain Maturity Model, with four phases of maturity in how companies manage their supply chains, particularly the level of collaboration with supply chain partners.

With more mature business relationships, you can achieve better long-term results.

Stage 4	Stage 3	Stage 2	Stage 1
Cross-Enterprise Collaboration	External Integration	Internal Integration	Functional Focus
Work is done with customers and suppliers to define a mutually beneficial strategy and cross-enterprise processes are enabled by information technology	Practices are extended to interface with strategic customers and suppliers; associated information needs are identified	Division or company-wide processes are defined	Planning and optimization is conducted within functions and / or departments
Real-time performance targets are set with both customers and suppliers	Corrective actions are taken when performance falls below expectations	Cross-functional metrics are defined	Processes that cut across multiple functions are not well understood
Leaders	Challengers	Followers	

Source: "Global Supply Chain Trends 2008-2010," PRTM (page 22)

Working from right to left, an enterprise becomes more mature, graduating from being a "Follower" to a "Challenger" and ultimately a "Leader." At each level, there is more meaningful sharing and collaboration with supply chain partners.

How well you communicate any changes in demand, supply, process requirements, quality requirements, cost targets, and so on will determine the flexibility of your supply chain... and perhaps the profitability of your enterprise.

By sharing more high-level information and working more collaboratively with key remote suppliers, you can make faster, better decisions. With a more complete view of the facts, you can resolve issues faster. And with more mature business relationships, you can achieve better long-term results.

Colleen Crum with Oliver Wight Americas writes about the difficulties in achieving flexibility while maintaining control in her blog posting⁸ "Advances in communicating information across a supply chain aid in better decision making and collaboration." She states that,

"Supply chains, both fully integrated within one company and multi-enterprise networks, need to return to the fundamentals (well designed processes that utilize best practices and are operated by knowledgeable people). They also need to leverage

8. Retrieved September 22, 2009 from: <http://blog.kinaxis.com/2009/06/colleen-coco-crum-advances-in-communicating-information-across-a-supply-chain-aid-in-better-decision-making-and-collaboration/>

the advances of information technology in communicating information across a supply chain to aid in better decision making and collaboration.

Inefficiencies, poor customer service, and other waste in a supply chain are inevitably the result of: 1) poor decisions made by people, and 2) poorly designed processes that lack integration (although many people incorrectly blame the information technology)."

Yet many manufacturers are still guarded when communicating with remote suppliers, providing them with minimal information on a strictly "need to know" basis, using technology that is both difficult to implement and modify, and does not provide a mechanism for joint or collaborative decision making. While treating suppliers at arm's length may have been good enough in the past, the competitive pressures of today's economy demand more flexibility.

Key suppliers must be brought into the decision-making process, so that brand owners can exchange early warnings and help resolve supply chain issues.

SUPPLIER SEGMENTATION IS KEY

The level of collaboration and integration with suppliers advocated in this whitepaper is best performed with a few key suppliers. There may be many commodity components that can be bought from several suppliers for which this level of process and technology sophistication is not required.

Instead your company needs to focus on the few key suppliers that,

- ▶ represent the majority of the spend on components;
- ▶ supply components to products which represent a major portion of your company's revenue; and
- ▶ supply long lead time components for which there is a potential for excess and/or obsolete inventory.

CONCLUSION: SUPPLIER COLLABORATION IS VITAL

To be truly effective, collaboration with suppliers needs to go far beyond tactical exchange of data. It's vital to develop more mature and trusting relationships with long-term suppliers. It's time for sharing business strategies, mutually investigating risks and threats, jointly looking at opportunities, developing and linking plans and targets ... and treating key supplier as an extension of the business. This is the best way to squeeze better results out of today's complex, outsourced supply chains.



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