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Globalization in Uncertain Times

How leading companies are building adaptable supply chains to reap benefits and manage risk

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ARTICLE

In a period of contraction, offshoring can bring much-needed cost savings and access to new markets. But it can also lessen supply chain flexibility and, ultimately, impede competitiveness. Our survey of 300 global companies highlights the challenges companies face as they move operations offshore—and, at the same time, reveals some of the innovative supply chain practices helping them succeed. Going one step further, some companies are using these practices to develop more competitive business and operational strategies.

As the economic forecast darkens, companies are increasingly moving their operations offshore to find new sources of profitability and growth. According to PRTM's *Global Supply Chain Trends 2008–2010* report, leading global companies have relocated 42% of all manufacturing activities and 38% of final assembly to facilities offshore, with the majority of these tasks now executed in China, India, and Eastern Europe (Figure 1; for more details on the report, visit www.prtm.com/sctrendsreport2008). In addition, many companies have moved some of their product and technology development facilities to emerging markets to tap a wealth of

Sixty percent of the study participants say the lack of supply chain flexibility is a major barrier to sustainable globalization

highly skilled technical resources and to gain a better understanding of local market requirements. As a result of these trends, we anticipate that more than half of many global companies' total operations will be located outside the home country by 2010.

Expansion, however, does not guarantee success. Many companies that have enlarged their supply chain networks have reduced labor and material costs—according to our survey, this is an average cost reduction of 17% per global initiative. Yet these savings often come with a big long-term tradeoff.

Firms that rush into expanding their presence abroad without first creating solid links between their supply chain and business strategies aren't able to reap long-term benefits. That's because they lose a key capability: *flexibility*, the ability to execute efficiently while responding to the fluctuating needs of different local markets. Indeed, 60% of the study participants say the lack of supply chain flexibility is a major barrier to sustainable globalization (Figure 2).

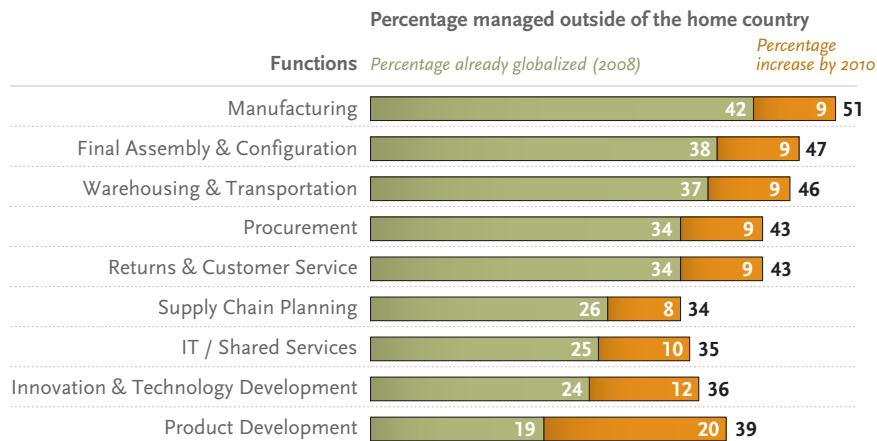
Companies that are most successful at global expansion turn the flexibility challenge into an opportunity. They develop new supply chain capabilities and then make significant changes to their business strategies on the basis of those new capabilities. Leading firms also tailor their business and operational strategies to meet the needs of different markets. Equally important, they develop the internal and external competencies needed to balance and grow all critical supply chain elements. These practices allow firms to pursue long-term globalization goals without sacrificing supply chain flexibility, cost efficiencies, or responsiveness.

Developing Innovative Supply Chain Capabilities

Moving production offshore has a major impact on many supply chain processes. Whatever issues the relocation raises—longer lead times, higher transportation costs, greater

Figure 1: Globalization Trends

More than half of manufacturing will be offshored by 2010



Source: Global Supply Chain Trends 2008–2010, PRTM

inventory costs—it is important to develop the supply chain capabilities to address them. In our experience, leading firms go one step further: They use these new capabilities to develop more competitive business strategies.

In the quest to expand the footprint as fast as possible, it's easy to overlook a simple fact: Not all markets work the same way

Logitech serves as a clear example. Founded in the early 1980s as a supplier of computer mice to PC manufacturers, Logitech initially developed supply chain practices to support mass production of a small number of products. A decade later, the company launched an ambitious growth strategy to expand into the consumer electronics retail sector and its global operations and product offerings. However, in an ultra-competitive industry where customer needs change constantly, having manufacturing facilities and suppliers in far-flung locations posed a major challenge.

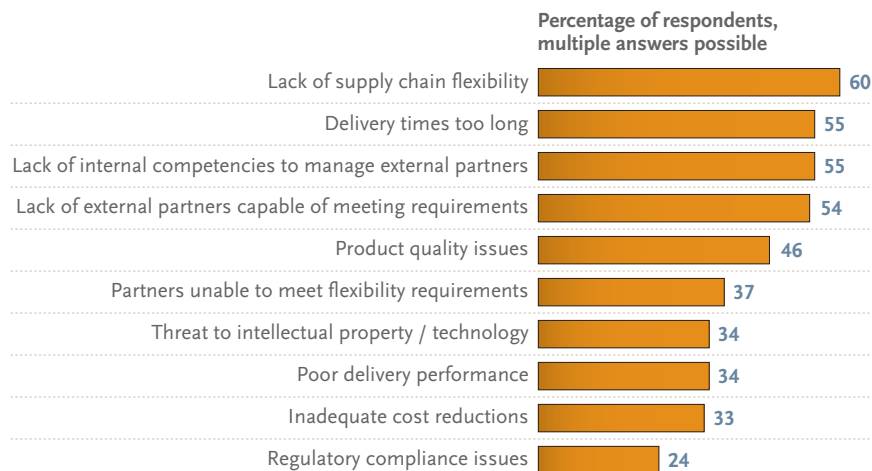
To solve this problem, Logitech found ways to make its supply chain more agile and responsive. One such innovation was the development of a new printing technology that allowed generic keyboards to be transformed into language-specific versions on demand. At the same time, Logitech developed new end-to-end supply chain planning processes. These changes introduced far more flexibility into the final stages of production. Logitech now found it much easier to respond to sudden shifts in consumer demand, regardless of where production facilities were located. And with a greater number of keyboard languages at its disposal, the company could explore a wider range of markets.

Tailoring Business and Operational Strategies for Different Markets

In the quest to expand the footprint as fast as possible, it's easy to overlook a simple fact: Not all

Figure 2: Barriers to Globalization

Sixty percent of respondents cite lack of flexibility as a key obstacle



Source: Global Supply Chain Trends 2008–2010, PRTM

In the quest to expand the footprint as fast as possible, it's easy to overlook a simple fact: Not all markets work the same way

markets work the same way. In our experience, companies often end up importing practices used with success in other markets, only to find they're not necessarily effective in the new location. Different business models—and, therefore, different operational models—are key for attracting new customers and building brand loyalty in different markets.

Consider the Bosch Group, the largest automotive supplier based in Germany. When establishing operations in India, Bosch executives realized it was not sufficient to simply replicate the product and supply chain strategies employed in Europe and North America. The company needed to develop a new supply chain strategy specifically for India, and a new business strategy in parallel.

Unlike automotive products developed for Western markets, those for the Indian market had to be able to withstand India's hot and rugged environment. To come up with product designs that met this goal, Bosch leveraged the research and development capabilities of the 250 engineers at its Car Services division in India. Working jointly with the area's five manufacturing facilities, the division created more durable products, such as specially-designed spark plugs.

Bosch also made substantive changes in its supply chain strategy. In Europe and North America, the company sold its automotive products to OEMs as well as to car dealerships and big-box automotive stores. In India, by contrast, Bosch sold these products through "mom and pop" shops, and provided technical and marketing support to many repair shop owners. Today, Bosch is a major player in the Indian

Figure 3: The COO Supply Chain Agenda

Priorities by region

Priorities	Americas	Europe	Asia Pacific
1	Increase supply chain flexibility	Increase supply chain flexibility	Increase supply chain flexibility
2	Improve delivery performance	Improve delivery performance	Reduce order fulfillment lead times
3	Accelerate globalization of supply chain; reduce order fulfillment lead times	Reduce working capital	Improve delivery performance

Source: Global Supply Chain Trends 2008–2010, PRTM

Extending the global footprint into a new region typically requires finding local suppliers—by our estimate, at least 10 to 20 new suppliers with each footprint

owner of the Mikron brand, faced similar issues when it expanded into Asia. Its higher-end, higher-performing electric discharge machines (EDM) sold in Western markets would not meet the needs of entry-market customers in Asia. So the company designed a lower line of equipment and ramped up its engineering and manufacturing facilities in China to produce it. Today, the new brand accounts for about a quarter of the entire group's sales, which exceeded US\$1 billion in 2007.

Developing Internal and External Globalization Competencies

Companies that expand in haste may lose sight of another important competence: the ability to manage suppliers effectively. Extending

market: Its products and support are available through 4,000 authorized dealers, including many that are located right along the major roadways.

Swiss industrial equipment maker GF AgieCharmilles, part of the Swiss Georg Fischer Group and

the global footprint into a new region typically requires finding local suppliers—by our estimate, at least 10 to 20 new suppliers with each footprint expansion. But often companies looking to grow operations quickly end up making these selection decisions based purely on cost. As a result, suppliers lack the competencies—robust planning tools and just-in-time or just-in-sequence capabilities—needed to provide components quickly and on time. Many challenges companies experience with product quality or safety are actually due to inferior supplier performance.

All of this explains why more than half of the survey participants stated that two major barriers to globalization were the lack of capable suppliers and the lack of internal competencies to adequately manage international partners.

Leading companies deal with these challenges in a few ways. First, they invest in internal training so their staff can learn how to best manage across a globally distributed value chain. Employees not only need to learn how to work with a common set of supply chain processes. They also need to develop greater familiarity with different languages and cultures to facilitate effective interaction with business partners worldwide.

The 10 Major Global Supply Chain Trends

Our recent survey found 10 major trends influencing cross-industry innovations in supply chain design and configuration.

- 1. *Shifting organizational focus.*** Rapid globalization has led to large structural shifts for the supply chain organization and presents new challenges for effectively managing supply chain performance. In particular, globalization initiatives previously focused on manufacturing and assembly are starting to shift to product and technology development.
- 2. *Underlining growth priorities.*** The pressure to reduce costs continues to be a key reason for the acceleration of globalization. At the same time, however, access to local markets has also become a primary objective.
- 3. *Closing gaps between planned and actual savings.*** Despite average cost reductions of 17% per globalization initiative, many companies struggle to realize savings in management costs. The inability to manage internal processes as well as external partners is a key reason for the shortfall between planned and actual savings.
- 4. *Evaluating geographic strengths.*** While China and India continue to be the key destinations for globalization efforts, Eastern Europe is catching up because of its proximity to Western Europe and its attractive skill/cost mix.
- 5. *Mitigating risk.*** Product quality and safety, as well as supply chain delivery and security, are the most critical concerns for companies expanding their supply chains globally. Companies are employing various strategies to minimize these risks, such as frequent on-site audits and more extensive training of suppliers.
- 6. *Breaking barriers.*** Limited supply chain flexibility and an internal lack of competency to manage partners are two of the greatest barriers to globalization. Better visibility and management across the supply chain may help overcome these hurdles.
- 7. *Factoring in environmental sustainability.*** Although environmental sustainability is not a primary driver of supply chain strategies today, it will increase in importance in the future.
- 8. *Gauging supply chain maturity.*** Supply chain maturity, which measures how companies apply strategic, organizational, collaborative, and performance management practices to the management of their supply chains, differs significantly across geographies and industries.
- 9. *Increasing need for more flexibility.*** By 2010, the need for greater supply chain flexibility will surpass product quality and customer services as the most important reason for improving supply chain strategy. The great majority of companies surveyed are focusing on improving delivery performance to achieve that flexibility.
- 10. *Setting a new COO agenda.*** COOs worldwide share the same priorities: increasing supply chain flexibility, improving delivery performance, and accelerating the globalization of the supply chain.

We've found that top companies also provide training for their key suppliers. Since many suppliers from emerging markets are less experienced in the supply chain practices common to global companies, they may not be familiar with the way a larger company does business. According to our survey, the more successful companies make a point of spending time teaching their suppliers how to perform. They also set up quality control systems at the manufacturing sites of key suppliers to ensure that a high proportion of products pass quality tests the first time around. Regular audits and improvement sessions help to ensure that suppliers develop the competencies needed to be part of a global and flexible supply chain.

For the foreseeable future, globalization will be a major force driving the supply chain agenda of leading COOs around the globe (Figure 3). The challenge will be to continue the internationalization of a company's operations footprint while improving supply chain flexibility, on-time delivery, and cost savings.

While going global is still a good way to realize cost savings, it provides other substantial advantages as well. As leading firms have demonstrated, expanding abroad opens up access to novel technologies, untapped R&D resources, and whole new markets. In a downturn, these are benefits no company can afford to ignore.

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SURVEY METHODOLOGY

More than 300 global manufacturing and service companies participated in the Sixth Annual PRTM Global Supply Chain Trends 2008–2010 Survey. Data was collected between December 2007 and March 2008. Participation was geographically balanced, with approximately 42% of respondents from Europe, 37% from North America, and 21% from Asia. The survey population comprised organizations from a diverse set of industries, with a strong representation of industrial and automotive, consumer goods, electronics and semiconductors, and life sciences companies. Participants represented various management levels, regions, and industries. About 16% of those surveyed were CXOs, 52% were directors or vice presidents, and 32% were managers.

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