Far and wide
Global supply chain strategies for Consumer Products manufacturing

Supply Chain Network White Paper
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The new wide world

Over the last two decades, a wave of globalization has spread as an increasing number of U.S.-based consumer products manufacturing companies moved their operations overseas seeking — and finding — cost savings. Products manufactured overseas could be delivered to customers in the United States at a lower cost than if produced domestically.

This low-cost manufacturing model has served U.S. manufacturers well for many years. However, the shifting developments and trends across the globe are forcing manufacturers to once again rethink their outsourcing strategy in favor of one more attuned to the realities of the marketplace — one where growth and opportunity for product consumption, not just manufacturing, lie beyond United States borders. Consider these developments that are permanently altering global consumers:

- Over the next several years, middle-class populations worldwide are forecasted to grow by approximately 70 million people.[1] — an increase that equals the current population of the Western United States — from California to Washington to Montana to New Mexico and all the states in between[2]. This growth expands the market for consumer goods.
- Internet access is widespread in emerging markets. One in three people worldwide now surf the Internet — and 57 percent of these users live in developing countries. The Internet provides visibility and access to consumer trends and products from the living rooms of households worldwide.
- A popular social media tool now has more than 600 million users worldwide — that is 1 in every 13 people. Seventy percent of the user base resides outside of the United States. Many consumer product companies have set up social media pages to promote their products and connect with the consumer.
- The number of cellphone subscriptions reached 5.3 billion in 2010 — 78 percent of these subscribers live outside the United States Smartphone technology allows many of these subscribers to view, review, compare, and purchase products from anywhere.

As the world outside the United States grows more sophisticated, wealthy, and consumer-oriented, manufacturers are recognizing that they cannot afford to ignore it. No longer is the outsourcing question based on the cost to manufacture products overseas and deliver them back to the United States. Today's manufacturers are wise to deploy a supply chain strategy that considers not only the production of goods on foreign soils, but also the distribution and consumption of those products locally, where they are made.

Five steps to effectiveness in global supply chains

To help consumer products manufacturers compete effectively in the global marketplace, Deloitte professionals have identified five imperatives for avoiding common errors while entering emerging markets. These imperatives are to:

1. Align manufacturing and distribution with the corporate strategy.
2. Leverage/manage the global supply chain network.
3. Inject productivity, flexibility, and speed into manufacturing and distribution operations.
4. Deploy a global governance model to manage risk.
5. Focus on supply chain talent — people are an organization's most important asset.

1. Align manufacturing and distribution with the corporate strategy.

If there was a mantra among business advisors, it would be "align, align, align." Structuring the various organizational business units, functions, and departments to work together to support one another and the broader business strategy is key to achieving short-term objectives and realizing long-term goals. This leading supply chain practice aligns manufacturing and distribution operations with Research & Development (R&D), marketing, sales, finance, IT, and HR — a holistic approach to strategy development in order to gain alignment across the major business functions. This alignment is particularly critical to determine that the business functions — from R&D to distribution — are working together to achieve the broader business strategies and goals.

The process begins by considering the overall business unit strategy and profit targets along with analyses of retail and end consumers. This analysis also includes other market drivers, such as competition, regulatory concerns, and internal constraints. The goal is to establish a product portfolio that meets the needs of consumers, competes favorably in the marketplace, and is viable and profitable for the business to produce.

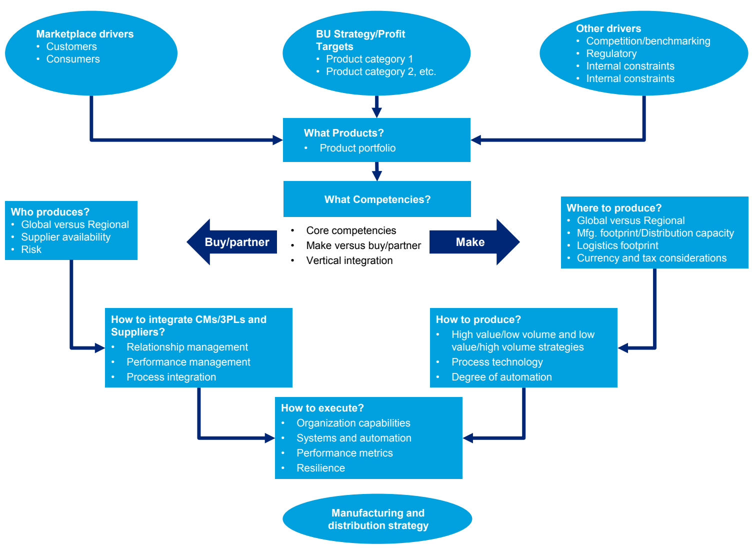
Manufacturing and distribution decisions are then made according to how well they support the business unit strategy. As Figure 1 shows, this includes:

- Identifying which manufacturing and distribution competencies will be core operations and which can be outsourced.

1 Bank of Canada, May 16, 2011
2 U.S. Census, 2010

- If products are outsourced, deciding who will be the producer and how suppliers/co-packers and contract manufacturers (CMs) and third-party logistics providers (3PLs) will be integrated effectively. This includes determining how these relationships should be managed, how performance will be tracked, and how the external manufacturing process relates to in-house operations.
- If products are manufactured in-house, deciding where they will be produced and clarifying the production strategy, including volume-value tradeoffs, process technology, and degree of automation.
- Managing execution with emphasis on talent management, governance structure, automation/IT needs, and flexibility/resilience plans.

Figure 1: Manufacturing and Distribution Strategy Framework



2. Leverage/manage the global supply chain network.

With the manufacturing and distribution strategy aligned with the broader business strategy, the focus then turns to leveraging/managing the supply chain with a global perspective. While many consumer products companies have developed detailed marketing plans for emerging markets, far fewer have developed rigorous supply chain designs — and many have suffered unintended consequences.

In some cases, foreign supply chains proved disappointing because U.S.-based managers overlooked critical local factors that would likely never occur in their domestic supply chains.

While parts of the global supply chain should be customized for local conditions, global supply chains also need to leverage economies of scale. Design is not a simple task. Nevertheless, in our experience, a rigorous supply chain design typically yields improved performance in the range of 5 percent to 15 percent.

Unlike analysis conducted in the United States, global analysis has to consider easily overlooked factors, such as utility dependability, local regulatory policies, and cultural norms. Labor and transportation cost differences can be severe, so can supplier strengths and weaknesses, infrastructure considerations, and financial concerns.

To make matters more challenging, data about locations and labor is available and comparable domestically. In emerging markets, however data is not always available. Moreover, different countries collect and report data differently, so information from emerging economies requires knowledgeable and experienced staff to make it useable and comparable. That means local knowledge and a common set of data from trusted sources become essential.

Think cross-functionally, including HR, tax, regulatory compliance and risk, and facilities

A rigorous and effective supply chain design crosses functions to include human resources, facilities, and analyses of tax and regulatory environments. While the gains from traditional supply chain initiatives are generally significant, the gains from cross-functionally designed supply chains are typically much greater.

An HR perspective typically reduces turnover and wage/benefit costs while increasing productivity. The gains from global supply chain HR efforts often exceed 10 percent.

Comparing financial/risk perspectives between potential locations in a company's supply chain network also typically achieve gains that can exceed 10 percent. Among emerging countries, tax policies and treaties with the domestic headquarters country can vary dramatically. In addition, some companies have discovered too late that they needed to look beyond income taxes and consider local taxes, customs/duties, tax incentives for locating facilities — and repatriation of earnings.

A facilities/real estate perspective often yield savings of 15 percent by rightly sizing facilities across the supply chain network, rightly locating operations, and consolidating similar operations.

Even planning for a new plant should be cross-functional. Consider a common scenario: A manager in one functional area tends to make decisions that improve the key performance indicator(s) for his or her own functional area — and overlooks important considerations for other departments. Consequently, for example, the new plant in an emerging economy has a very low cost per unit, but:

- Tax treaties, duties, and governmental fees eat up significant earnings.
- Local law prevents selling the plant's production within the country — all must be exported.
- Costs to deliver products to ports slash margins.
- Recruiting and training local labor delay start-up and can increase costs for years to come.

Cross-functional integration is critical in the leveraging/managing of a global supply chain.

3. Inject productivity, flexibility, and speed into manufacturing and distribution operations.

For many consumer products companies, distribution/logistics constitute 6 to 7 percent of sales.[3] In our experience, approximately one percentage point of these costs is wasted by inefficiencies. Consequently, many consumer product companies have the opportunity to gain a quarter- to a half-percent of sales by reducing waste across their supply chain.

Achieving cost savings requires defining the supply chain to include:

- Inbound and outbound logistics globally
- Make versus outsource analysis
- Networks of suppliers, manufacturing, distribution centers, and customers globally
- Demand management
- Procurement
- Manufacturing
- Returns
- Links with product development/launch

Relentlessly seek plant and distribution center improvement

In our experience, virtually every supply chain has significant opportunities for savings. However, finding them requires a rigorous, disciplined, and imaginative look at operating differently.

For example, few companies regularly analyze the true profitability of their product categories. In many cases, the great majority of profit is earned by a minority of categories, and it may be more effective to collaborate with other players or outsource some categories.

Continuously monitoring Operating Equipment Effectiveness (OEE) can indicate areas for improvement. OEE measures uptime, speed of operations, and quality of production. Many leading batch manufacturing companies achieve OEE greater than 80 percent. In contrast, our experience shows that in many companies, OEE hovers in the range of 60 to 70 percent.

Better integrate the supply chain with product development and launch

In many cases, differences in culture, taste, price sensitivity, and regulations among emerging markets likely require developing new products. However, unless supply chain is involved in the new product development/launch process from early stages, product win rates, speed-to-market, and margins can suffer. Without early supply chain involvement, unfavorable consequences could become likely.

Supply chain participation is needed to ascertain production and delivery costs — and to develop a network of reliable suppliers and transportation providers. Supply chain involvement is also needed to avoid delayed launches, soaring warrantee costs, intellectual property losses, product safety lapses, and regulatory compliance failures. Since the globalization of supply chains adds complexity and time, the involvement of supply chain in new product development needs to occur sooner than it did in the past.

Moreover, collaboration with suppliers in emerging economies can help develop and improve new products. While many consumer products companies need to manage their global supply chains to leverage economies of scale and scope, many should also personalize marketing, sales, and product development to the local market as much as possible.

3 *Supply Chain Benchmark Study for Consumer Products* by Deloitte Global Benchmarking 2009. This study evaluates supply chain performance within consumer products companies across the strategy/plan/source/make/deliver process taxonomy and offers insights across the three key drivers of shareholder value: revenue growth, operating margin, and asset efficiency.

Supply chain's role in relationship management with suppliers means its role in the product innovation process has become more important. For example, a shampoo manufacturer could avoid costly mistake by ensuring that a local supplier makes packaging changes because as consumers in emerging market preferred single-use packets over bottles.

Changing product development from a fully in-house process to a collaborative one often entails changing internal culture. It requires that staff learn new skills and gain an understanding of different cultures.

Customize supply chain services and pricing by customer

Never forget the customer — each customer. Supply chain costs and processes differ dramatically between retail customers. Many companies customize supply chain services to meet customer demands, but do not charge for it or change product pricing accordingly. This presents a substantial opportunity that is often overlooked.

Effectiveness in pricing by customer entails a rigorous analysis of business processes and customers, including order-to-cash, freight, distribution, store-level picking and packing, mixed versus full pallets, truckload versus less than truckload, chargeback policies, delivery wait times, shelf space/planograms trends, and more. Each of these factors can add to or subtract from supply chain costs significantly.

4. Deploy a global governance model to manage risk.

As a company grows globally, suppliers and service providers can/may become distant — physically and culturally. In many cases, they also become more important, providing greater breadth and depth of service than a typical supplier relationship domestically.

However, many companies have naturally treated outsourcing manufacturers and logistics providers as just another local supplier: provide specifications, negotiate a price, and await delivery. That is often a mistake.

In these circumstances, supply chain governance requires a higher level of visibility and oversight to effectively manage the risks of a distant supply chain.

Establish a formal governance program

Many experienced global manufacturers have established a formal program to qualify, certify, and manage outsource partners, such as contract manufacturers and component suppliers. These programs establish standard operating procedures that govern the relationship and help achieve product consistency (price, performance, quality, etc.) by focusing on:

- Governance structure
- Product specifications
- Certification requirements
- Performance requirements
- Contractual and legal terms
- Corporate values and culture

Gain visibility into remote operations

The second critical imperative for managing global operations is visibility. Many global manufacturers have come to recognize the value of "boots on the ground" to monitor foreign operations. These foreign offices are a valuable tool for monitoring the performance of remote operations. They can also be structured in a way that they become a legal entity within the country, providing savings in taxes and duties.

Technology also plays a critical role in monitoring remote operations. Real-time data collection and transmittal can occur at the critical steps of manufacturing. Many companies are deploying technology that allows them real-time visibility into manufacturing operations that are occurring in facilities around the world. This visibility allows these companies to respond to quality or productivity issues as they are occurring, rather than weeks or months later, when resolution of the issue is more costly to the company or the consumer.

5. Focus on supply chain talent people are an organization's most important asset.

As consumer goods supply chains have globalized, become increasingly integrated with other functional areas, and been outsourced to other countries, the need for highly skilled supply chain talent has multiplied. Supply chain processes now need to operate with tight integration and be continuously improved using a holistic perspective — and that requires people with specialized knowledge and experience.

That is why some leading consumer products companies are instituting talent management in their supply chains. They assess the skill needs they expect to have with global growth, then proactively develop, recruit, and retain talent accordingly. In our experience, companies with top-performing supply chains:

- Recognize that turnover and motivations differ regionally and by age group
- Assess current talent against current and future needs globally
- Develop their brand as an employer
- Focus training on priorities

Learn the motivational differences by age and region

Many companies underuse nonfinancial retention incentives and mistakenly apply the same motivations globally, even though different motivators work better for different ages and regions. Today's "Generation Y" employees have different professional incentives than their "baby boomer" colleagues: GenY cites additional compensation as their primary motivator while baby boomers favor strong leadership above other motivators. Motivations also vary by region. For example, 34 percent of employees surveyed in the Americas and Asia-Pacific region chose "lack of compensation increases" as one of the three most significant factors that could cause them to look for new employment today, while only 13 percent of employees surveyed in Europe/Middle East/Africa made the same choice. Understanding and adapting employee retention programs to meet the needs of diverse perspectives is crucial.

While salary increases and bonuses/financial incentives are normally the top two motivators, the next four top motivators, as rated by employees in a recent Deloitte report,[4] are nonfinancial:

1. Strong leadership
2. Job advancement guidelines/expectations
3. Support and recognition from supervisors
4. Flexible work arrangements

Leadership development and customized career planning are two powerful motivators of particular importance to supply chain managers. In the same Deloitte report, supply chain professionals surveyed in North America indicated that they wanted to advance in supply chain, but would likely join another company because they did not believe their current company could provide a pathway to senior management through the supply chain function.

Reduce voluntary turnover

With so many companies realizing their need for supply chain talent with expanded skills, a competition for high-quality supply chain managers has sprung up. Retaining talent has become a priority. Here are some steps to take that can/may help you retain the leading people:

- Focus attention on high performers, since they drive the company's performance and have a higher risk of leaving because they have more options.
- Show leadership commitment to the company and to employees, which helps to earn employees' respect and dedication, making them less likely to leave.
- Incent managers to make retention and the management of people as important as "making their numbers." Consider tying managers' bonuses and rewards to their department's turnover numbers.
- Communicate honestly and openly to build trust, which can reduce turnover intentions and may help keep employees supportive of their organization, even when corporate decisions are personally unfavorable.
- Capture and apply institutional knowledge about what has been successful in managing and retaining people in the past.
- Maintain social budgets. By keeping social events, you are helping to create a stronger internal social network, which helps reduce the likelihood that your employees will leave.
- Build your brand as an employer to make your company known as a desirable place to work.

Conclusion: Change is challenging but necessary

The enormous growth potential in emerging markets is an opportunity that consumer products manufacturers cannot afford to mismanage. Effectively tapping into these markets requires first aligning the supply chain with broader business goals and then systematically redesigning it to address the challenges inherent in "going global." Supply chain leaders need to focus on driving out inefficiencies and building closer collaboration with the internal product development function as well as with external suppliers and providers, including the governance processes to control the risks of a distant supply chain. Product mix and pricing should be adjusted to reflect the customer, regulatory, tax, and other realities of the global market. Finally, companies should make acquiring and retaining the talent needed to manage intricate global endeavor an ongoing priority.

The task is not an easy one, but foregoing it in favor of business as usual is not an option for companies that want to stay market competitive and grow. Just as the demand for consumer goods has changed, those who supply those goods must change as well.

4 Managing talent in a turbulent economy: Keeping your team intact, September 2009, Deloitte.

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