

Don't be the weakest link

Buyers will never crack low-cost country sourcing until they understand the importance of inventory and logistics, Peter O'Brien tells Emma Clarke

Purchasers still have a lot to learn about low-cost country sourcing, according to Peter O'Brien, senior vice-president for supply chain management at logistics firm DHL and managing director of a new integrated supply chain company. He says he has worked with buyers who lack understanding of how Asia operates and are naive about the risks and costs involved.

For companies to become more successful and truly reap the benefits that low-cost country sourcing can bring to the bottom line, he believes purchasers must build smarter partnerships and think about an integrated end-to-end supply chain.

"Procurement professionals need to think beyond procurement. Not just about the cost or quality of a product but also where it is warehoused and how it is delivered, as well as inventory financing." Only by considering the full supply chain will they continue to reduce total cost, guarantee quality and supply and reduce management complexity.

End-to-end concept

O'Brien first became aware of the demand for integrated supply chains - bringing together companies with expertise in sourcing, logistics and inventory financing - six years ago, when he was in charge of building DHL's global procurement operations.

One of his responsibilities was to set up the procurement of uniforms for DHL's drivers and staff who operated from more than 200 countries. With staff in different locations, his objective was to get the right items, in the right materials, with the right features for the best price, but also

to ensure all products were delivered to staff, wherever they were in the world. "If we are sourcing out of one supply market and then delivering to a complex number of others, we need a fully integrated supply chain."

He also wanted the right technology to assist with sourcing and logistics and to find if there were ways of holding stock in Asia to keep costs down.

He recognised that purchasing needed to have a greater understanding and control over "inventory financing" - in this case, which company owns the risk at which point while the goods are in transit. "If you are buying a product from Guangzhou in southern China it will take 60 days to ship it home. There is a significant issue around ownership of inventory during that period and the associated risks."

But he found there was a lack of understanding or partnership between the different elements of the supply chain. Logistics firms such as DHL were at arm's-length from the sourcing companies, which in turn were far removed from the inventory financing providers such as General Electric.

How many purchasers, asks O'Brien, understand the impact of inventory being on a company's balance sheet as opposed to off it? Very few, he believes.

"And neither do buyers have a proper grasp of logistics. They choose a freight forwarder for each product, but managing this support service is not usually their skill." And the logistics providers know this, he warns, which means they are in the perfect position to take advantage.

Conversely, he has also noticed that logistics experts are soon out of their comfort zone when considering issues revolving around currency or quality risks of working with suppliers in China or India: "These are all diverse industries that need to be brought together." And to enable this, the skill set and knowledge of procurement professionals has to develop dramatically.

Chief procurement officers need to start developing the skills of their staff. In addition, and perhaps more importantly, they will need to look outside the function to see who has the skills they do not have in-house and build relationships with these providers.

A new business model

"There is an evolution going on in supply chains and the business model of the future will be in finding ways to collaborate with partners in logistics and inventory financing."

He expects this way of working to be a threat to the traditional purchaser who prefers to control everything in-house. "But this is about keeping control while at the same time recognising there are providers out there that you can work with to find a better solution."

For larger companies this may mean building direct relationships with logistics and finance companies, but for others, and for certain spend areas, it could involve outsourcing to an integrated supply chain service provider.

Triscol is the DHL-owned but independent operation recently set up by O'Brien which brings together expertise on low-cost country sourcing, logistics and inventory

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financing. Based in Singapore, it has built partnerships with companies that can manage and deliver the end-to-end solution from design, manufacture and sourcing through to quality control, fulfilment and delivery. Initially this will focus on four spend areas: corporatewear, printed materials, promotional items and maintenance, repairs and operations (MRO).

The service is aimed at Western firms who want to access low-cost country sources in the Far East but don't know how, or have that knowledge but would rather focus efforts on spend areas core to their business. Currently their clients include a European telecommunications company, a European postal company and an Australian airline.

Triscol is managing sourcing and delivery for two spend areas - uniform and MRO - for the telecoms company. While these are not core to the business, they represent over €12 million each, every year. "We help them design products, find suppliers in China, build their new supply chain capability, warehouse the stock in Asia, set up warehouses in Europe and look after the inventory risk to the point it is delivered."

Expert partners

To do this, Triscol has collaborated with a number of partners, including Asian Sourcing Network, an IT and consulting service that will plan its low-cost country sourcing.

For logistics it is partnering with two providers, one of which is DHL. "We will only use DHL when it is the most competitive. In this case it was the best for one spend area, but not the other."

Triscol is working with two inventory financing companies in the US and Europe who will share the risk for the inventory. This aspect of the programme will come into operation in the second phase later this year.

By switching to a low-cost country source, they have saved the firm 50 per cent on costs and, by passing responsibility to Triscol, procurement staff could refocus on other core spend areas.

Considering what O'Brien believes to be the procurement sector's continued lack of understanding of the complexities of sourcing in Asia, he thinks many firms could benefit from partnerships with integrated solution providers. "Asia is a completely different market. The drivers are varied, it has diverse cultures and a level of growth that we have never seen before."

Despite the wealth of material about the subject and the number of years that companies have been sourcing from the Far East, he feels there is still a lot of naivety and fear about the risks involved. "The only way that this fear can be overcome is, first, getting buyers to appreciate the differences in Asia, and second, understanding the skills and partners they require to deal with suppliers there." Where firms have gone wrong in the past, he says, is in sending people from the West to establish and manage their operations in the Far East. "The only people that can deal with the locals are the locals."

And it's more than just the language. It is understanding how business is done and grasping the relationships. "Western companies send out a few executives for a couple of weeks and expect them to turn around a strategy on

who to partner with. But Chinese companies have taken 50 years to set up their operations."

Before tackling low-cost country sourcing, buyers need to understand who the capability providers are and who has knowledge in Asia and build trust with these partners.

Learning from successes

O'Brien also believes purchasers should look beyond their own sector for partners or inspiration on how to tackle sourcing. "Consider different industries that have been successful in setting up offices in Asia."

Leading in this area are the retailers and automotive companies that were first to source direct materials from Asia. He says: "Some of these have been very successful in setting up sourcing offices in China." Perhaps this is unsurprising considering the money they were able to invest as a result of the volumes they were trading in and the strategic importance of the products to their businesses.

But he believes indirect spend deserves the same attention. "Indirect spend has not been as successful because the volumes have not been there. We spent €25 million a year on corporatewear at DHL. Compared with the €4 billion a year spent on transport in Europe, it wasn't even on the radar."

Because of this lack of focus, buyers were happy to rely on agents and importers to buy their indirect materials from Asia. These local European importers went through agents in China and, at every step in the supply chain, each player took their margin. "It is time to cut these players out and source indirect material directly from China but through a

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fully integrated solution. Whether you are a logistics provider, a technology provider or a buyer, everyone talks about supply chain. But all things considered, a full supply chain can only be from end to end."