

[<< Return to Main Page](#) | [Print](#)

From the pages of Purchasing Magazine Online

Supply chain success requires collaboration

By Ron Nussle, Jr. -- 9/21/2006

Over the past decade, nearly every Fortune 500 company has embarked on a supply-chain cost-reduction program. Most savings reported come from commodity-leveraged negotiations or sourcing from low-cost countries (LCCs).

The Integrated Cost Reduction process uses a broader, more fundamental approach to cost that takes into consideration such factors as engineering, supply, design, marketing, and production. Especially important to the ICR process is how it integrates the proven best-of-the-best business improvement processes: Six Sigma in quality, value analysis/value engineering in design and purchasing, Lean in production, and supply chain management and e-procurement tools in procurement, production, and logistics.

The business world goes through one fad after another trying to improve its competitiveness. Over the past few years, the following supply chain cost reduction strategies have been the most common:

Supply chain leveraged negotiations. By themselves, they are typically just "margin-transfer" with four unintended (and often painful) side effects: suppliers recover their losses during the next upturn or engineering change notice; suppliers don't give their best cost ideas up front; suppliers don't recover their losses and exit the industry.

Outsourcing. There are many benefits, but also substantial costs and risks to outsourcing. Furthermore, outsourcing is not a silver bullet and some products and job functions cannot (or should not) be outsourced. How do you balance the investment in core products and services while simultaneously investing time, resources and management in an outsourcing program? It isn't easy.

Global sourcing (to low cost countries). It has become the favorite way for CEOs to lower costs, but takes unexpectedly large investments in time and resources before break even occurs. Typically, break even takes 18-24 months after the project is initiated.

Exchanges. They have failed to materialize any real cost savings and have almost all collapsed. A few short years ago, the Big 3 automakers, major airlines, medical companies and a number of other multibillion dollar players launched exchanges with great expectations of cost reductions and many press releases.

Today, this business model has been almost entirely abandoned.

Online reverse auctions. They are really just another form of "win-lose" negotiations. One \$5 billion company experienced such a serious backlash after initiating online reverse auctions, it began missing shipments from suppliers.

While noncollaborative approaches may yield short-term savings, the above unintended side effects limit the overall benefit to cost of goods sold (COGS). One functional organization (purchasing, tooling services, etc.) may see their numbers get better while other organizations see increases in cost, or degradation in cycle time or quality.

Outsourcing: Theory vs. experience

Deloitte Consulting surveyed several companies on their experiences with outsourcing. Following are some of the results:

Outsourcing driver	Experience
Cost savings	52% said cost issues were the main risk, and 81% found hidden costs they had no visibility to in the supplier's pricing.
Best practice/quality/innovation	31% said vendors became complacent.
Flexibility/capacity/scalability	Contracts are binding. Late changes are a problem.
Focus on core/strategic functions	One in four mislabeled functions as non-strategic.
Access to high-caliber labor	One in five saw vendor-employee turnover.

Source: Deloitte Consulting Outsourcing Study, 2004



ADVERTISEMENT

More By This Author

[How to collaborate to cut costs](#)



Also, read online exclusive: ["Why Integrated Cost Reduction is superior to non-collaborative approaches?"](#) for Purchasing by Ron Nussle, Jr

Author Information

Ron Nussle, Jr. is the author of "Integrated Cost Reduction" and president of ICR Enterprises.

[<< Return to Main Page](#) | [Print](#)

© 2007, Reed Business Information, a division of Reed Elsevier Inc. All Rights Reserved.