

Economic globalization and offshore sourcing management essay



In tune with increased economic globalization and offshore sourcing, global supply chain management is becoming a vital subject for many businesses and Somerset Furniture is one of the companies facing the challenges when set up its global supply chain.

The business strategy constitutes overall direction to achieve corporate objectives and goals in long term, but supply chain strategy focuses on driving down operational costs, streamlining procedures and maximizing efficiencies. However, most companies have wonderful business strategies but most of them are unlikely designed a seamless supply chain strategy which can result in great failure when doing business overseas.

In this case study, Somerset's current approach to manage its supply chain resulted in poor business performance, the visible hazards and other negative factors frustrated Somerset included poor logistics management, ineffective order system and inventory management as well as inconsistency of product quality. In adopting a value chain, Somerset must incorporate and execute a robust supply chain management strategy for " best-fit" suppliers selection, further establish on how to work with supply partners, distributors, suppliers, customers or even customers' customers as a way to remain competitive. Otherwise, the company will not survive.

As the marketplace changes rapidly and becomes very competitive, it is critical that Somerset reinforces existing relationships and work together internally and externally. That being said, a well-practiced supply chain strategy results in value creation for the whole organization. In a nutshell, supply chains have shifted from a cost focus to a customer focus, until

currently to a strategic focus, scrutinizing the success of a strategy is just as good as the company's capabilities to fully and properly execute all. A great supply chain strategic approach, connected with operational excellence, can provide success for not only the company in crisis but also its partners and customers.

1. Introduction

Somerset Furniture is an established ornate residential home wood furniture company with over 50 years history in USA, renowned for producing quality and affordable furniture with a practical range of innovative design. To cope with the fast growing U. S. market, Somerset has developed its marketing strategy by introducing new product lines every few years and successfully gained creditable reputation during the last half of the twentieth century.

The company was a pioneer in furniture manufacturing processes and in applying TQM principles to furniture manufacturing. However, Somerset soon faced with thorny problems emerging in mid-1990s, such as stiffer competition, high labour rates, diminishing profits. As a result, the company downsized the domestic manufacturing facility and labour force through outsourcing several internal furniture product lines to China manufacturers, this led to be very successful in reducing costs and increasing profits initially. By 2000, Somerset closed entire manufacturing facility in the United States and outsourced all of its manufacturing to suppliers in China and then set up global supply chain, at which a series of chain-reacting problems raised and affected business. The primary focus of this paper is to find out outsourcing solution and rectify the global supply chain strategy to be very competitive.

The evaluation of Somerset's approach on managing current supply chain both from strategic and tactical viewpoint will be addressed in Chapter 2. The subsequent Chapter 3 and 4 respectively describes the new strategic supply chain approach and then explains the transformational requirements for changing Somerset supply chain effectively and efficiently.

The conclusion will be made in Chapter 5 outlining the study points for readers.

Evaluation of Somerset Furniture Company's Approach to Managing Supply Chain from both strategic and tactical viewpoints.

Somerset's Existing Global Supply Chain Process Map

Figure 2. 1 Somerset's Global Supply Chain & Logistic Flowchart

Source: Adapted from Fawcett, Ellram and Ogden (2007, p. 218)

Foreign Competition

While Somerset formulated a good strategic marketing plan for continually launching new product lines every few years during half of the twentieth century, simultaneously, experienced the positive effects of applying the TQM in its furniture manufacturing and popularly is known as high-quality yet affordable wooden furniture provider in domestic market. However, since the mid-1990s, the company suffered from the stiffer competition, high labour rate and decreasing profits. To get out of this situation, Somerset started outsourcing several furniture product lines to China that helped benefit from cost-effective and reduced operating costs. Another strategy was reducing the manufacturing facility and labour force, to keep the low costs in line with

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the pace of outsourcing. It was very successful initially in reducing costs and increasing profits for the company.

By 2000, Somerset decided to set up global supply chain and closed entire manufacturing facility in the United States by outsourcing all of its manufacturing to suppliers in China.

Shipments of Raw Materials and Inconsistency of Product Quality

Somerset's global supply chain facilitates the wood shipments from the United States and South America to manufacturing plants in China. This shipment itinerary takes a long time to arrive China, there'll be unexpected delays for processing shipment which incurs customer complaints and orders cancellation. Despite of long shipping time, the costs of shipment to the final destination and the raw material from US and South America are apparently high that reduced the profits.

As the manufacturing plants employed Chinese workers to produce products by hand in China, it will cause discrepancies in product dimension and quality. Customers would ask for exchange or refund as the quality is not assured by hand-made.

Poor Distribution Network and Transportation Management

The finished furniture products are shipped by containers from Hong Kong or Shanghai to Norfolk, Virginia, once arrived, the containers are transported by truck to Somerset warehouses in Randolph Country, where all of retailers'

stores located and installed the furniture to prevent from damage during transport.

Ineffective Order Management

It is found that there're some critical flaws exist internally within Somerset's global supply chain on its order processing and fulfillment system. Somerset processes orders weekly and biweekly and it takes 7-14 days to developing demand forecast and 12 -25 days for processing order which amount totally 22 to 45 days for purchase order to eventually complete. It requires another 60 days to produce product by hand when going into production.

Poor Transportation Management

As required by Chinese logistics, all finished furniture items have to be transported from the manufacturing plants to Chinese ports, which can take up to several weeks depending on trucking availability and schedules. Since 9/11, random security checks of containers will delay shipment for another one to three weeks and the trip overseas to Norfolk takes 28 days.

Hence, from China to Norfolk port, it can take more than two month's delivery time. Thereafter, clearing US customs can take another one to two weeks before local workers take another 1-3 days to unload containers and transfer the furniture onto truck to Somerset's warehouse in Randolph County.

Ineffective Inventory Management

The variability of supply chain estimated is up to 40% for schedule deferment. Due to Somerset's innovative conception to introducing new

products frequently, it resulted in substantial excess inventories left over in warehouse where the obsolete furniture occupy precious space and increase high disposal and storage costs.

Somerset proudly stands behind its products and customers can get a warranty period of 1 year from the date of purchase. It brought a serious problem for parts' replacement, because China supplier is only able to provide these parts which are in production, but most of the parts are not produced anymore after 1-year guarantee period.

Poor Product Quality

Although quality auditors are employed by Chinese suppliers to perform quality audit every few weeks, Somerset still encounters several quality issues. Consequently, Somerset has to inspect every piece of furniture it receives from China due to retailers' and customers' complaints.

3. Development & Justification of New Strategic Supply Chain Approach to be used by Somerset

Foreign Competition

Owing to fierce competition, Somerset has to close its entire US manufacturing facility and outsource all of its manufacturing to China to reduce costs and increases profits for the company. Outsourcing has become a common strategy that is adopted by all US companies and managing supply chains has now become a trend due to globalisation. It is felt that Somerset should have an outsourcing strategy which will continue to evaluate alternate low-cost furniture manufacturing plants around Asia or

other regions. Depending on just low-cost China manufacturers which product its products by hand may not be a viable long term solution for its overall corporate or supply chain strategy.

3. 2 Shipment of Raw Materials & Consistency of Product Quality

Somerset's shipment of wood from the United States and South America to manufacturing plants in China is a costly and time-consuming process. Raw materials should be sourced from within China or from neighbouring countries around manufacturing facility to ensure low cost and better efficiency in materials' movement.

The China manufacturing plant produced all furniture products by hand, which is not only time-consuming, taking 60 days to finished the production, but also cause inconsistency of product's quality. It is thus recommended that China manufacturing plant be ISO9000 certified, to provide Quality Assurance and invest in partial or fully automated machine to manufacture some of these furniture products so as to cut down the production lead-time and provide better consistency in product's quality.

In the meantime, the leader should take action of outsourcing another manufacturer in China to replace the current one, because the current plant may not have enough capital to purchase all necessary expensive equipment. Furthermore, the conversion from undeveloped factory to a qualified lean manufacturing facility cannot take place in one day since it is viewed as a long term transformation. Therefore, Somerset should outsource

the production base to other China furniture manufacturing facilities, which comprise the following competencies:

- Lean manufacturing system implementation

Lean manufacturing results in significant cost savings over a two to three year period. Specifically, manufacturing companies report significant reduction in raw materials, in-process inventories, setup costs, throughput times, direct labor costs, indirect labor costs, staff, overdue orders, tooling costs, quality costs, and the cost of bringing new designs on line (Swamidass 2002)

- ISO9000 certification

- Flexibility (refers to modification, design, machine, production lines and time flexibilities)

- Capacity (in terms of space, labor, equipment, IT and materials)

3. 3 Better Distribution Network & Transportation Management

According to Chopra & Meindl (2010), with regards to movement of products from factory to customer, there are six distinct distribution network designs for company to select one of them, as shown below:

Manufacturer storage with direct shipping

Manufacturer storage with direct shipping and in-transit merge

Distributor storage with package carrier delivery

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Distributor storage with last-mile delivery

Manufacturer/distributor storage with customer pickup

Retail storage with customer pickup

Somerset can select one of above distribution network to help in improving its distribution network.

Choosing the manufacturer storage with direct shipping will help to eliminate the movement of furniture from Somerset warehouse to retail stores. This will have the advantages of better customer's experience and lower inventory costs. Installation of hardware can therefore also be done at customer's house instead of at retail stores. However, it has the disadvantages of higher transportation costs (because of increased distance and disaggregate shipping) and requiring investment in information infrastructure to integrate manufacturer and retailer.

Another improvement in transportation is to eliminate export of raw materials from US to China by sourcing these materials from China or its neighbouring countries. This not only saves transportation time but also costs of materials. Purchasing department of Somerset will thus have the task to source for these new raw materials around Asia.

3. 4 Effective Order Management

The order processing and fulfillment system in Somerset's global supply chain is too long and it is suspected that Somerset and Chinese manufacturing plant may not have the necessary information technology to

enable the rapid sharing of demand and supply data. Per Harrison & Hoek (2002), they mention that integration of demand and supply data so that an increasingly accurate picture is obtained about the nature of business processes, markets and consumers, can provide increasing competitive advantage.

Figure 3. 1 shows a conceptual model of how supply chain processes (supply, source, make, distribute and sell) are integrated together in order to meet end customer demand (cited by Harrison & Hoek 2002, p. 14):

Figure 3. 1 Integrating demand and supply chains

Source: Harrison & Hoek (2002, p. 14)

Another solution is to ensure that Somerset utilizes software for order processing which will automatically route for approval and issue purchase order in an efficient manner. There should also be policy in place to ensure that the approval routes are short and approving manager does not take too long to approve it.

3. 5 Better Transportation Management

Apparently, the Chinese logistics' arrangement, depending on trucking availability and containers, causes wide time's variability in shipment of finished furniture items from China ports to Norfolk. It is really critical for Somerset to have a good logistics/transportation manager to understand the root causes, select work with the Chinese suppliers to reduce this time and wide-variability to avoid delay shipment to customers.

Langley et al. (2009) recommends proactive management approach to identify and solve transportation problems by reducing the number of carriers, negotiating with carriers, establishing carrier contracts with prescribed service levels, and modifying loading procedures. Hence, Somerset can negotiate and establish new contracts with Chinese suppliers or carriers to ensure that the finished products can depart China ports consistently at a shorter lead-time. In fact, Somerset should establish contracts with all transportation modes to ensure the required transportation service level and lead-time's predictability. Other means of improvement and cost-effectiveness can be done through consolidating shipments and monitoring transportation service quality.

3. 6 Effective Inventory Management

It is highly recommended that Somerset adopts Just-In-Time (JIT) and Lean thinking concepts, as discussed by Harrison & Hoek (2002), that can reduce delay, waste and inventory costs. Long-standing approaches to material control, such as reorder point stock control (ROP), economic order quantities (EOQ) and material requirements planning (MRP) can be made far more responsive by the application of JIT principle whereas lean thinking seeks perfection by gradually reducing waste from each of below four areas:

Specifying value from the customer perspective

Identifying the value stream (through time-based mapping)

Making the product flow through the supply network (by applying JIT principles)

Letting the customer pull (through pull scheduling)

Somerset may also adopt vendor-managed inventory (VMI) where it takes responsibility for monitoring sales and inventory in the retailer's process. This information is used to trigger replenishment orders. As VMI is facilitated by willingness to share data, the use of integrated systems, and standard procedures, it is made more difficult by such factors as long replenishment lead times, inaccurate data, and unwillingness by either party to invest in systems support.

Murphy & Wood (2008) highlights tracking technology, radio-frequency identification (RFID) to keep track of inventory, which can further improve the efficiency in the supply chain network.

3. 7 Better Product Quality

The fact that Somerset has to inspect every piece of furniture it receives from China proves that China manufacturing plant must be ISO9000 certified and implement Quality Assurance System in-house. In addition, this will avoid the need to get quality auditors who are employed by Chinese suppliers to perform quality audit. A Quality Improvement Team should be formed in the China manufacturing plant and be trained so as to improve quality on a continual-basis.

Somerset can also assist in the implementation of lean manufacturing for its outsourced China manufacturing plant or introduce Lean Six Sigma methodology to effectively control the process for better consistency in product's quality. The requirements for the successful implementation of

lean manufacturing, as per Swamidass (2002), are:

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All levels in the plant, from the production worker to the president must be educated in lean production philosophy and concepts.

Top management must be totally committed to this venture and provide necessary leadership. Everyone must be involved in the change, and the internal customer must be empowered to play a vital role in this evolutionary process.

Everyone in the plant must understand that cost, not price, determines profit. The customer determines price, the plant determines the cost.

Everyone must be committed to the elimination of waste. This is fundamental for becoming lean.

The concept of standardization must be taught to everyone and applied to documentation, methods, processes as well as system metrics.

4. Evaluation & Transformation Required

In order to change the Somerset's Supply Chain Philosophy from its traditionally position of functional independence to an integrated single entity, top management of Somerset has to ensure that conflicting functional objectives along the supply chain are reconciled and balanced. According to Barnes (2001), supply chain management requires a new approach to systems: integration is the key.

Somerset must better manage its supply chain effectively through adapting the six building blocks for effective supply chain management (Harrison & Hoek 2002) as follows:

Develop a supply chain strategy

Elements to be incorporated are:

Customer service requirements

Plant and distribution centre network design

Inventory management

Outsourcing and third-party logistics relationships

Business processes

Organizational design and training requirements

Performance metrics and goals

Gather supply chain information

Enterprise resource planning (ERP) systems to facilitate the flow of information across their organization

Develop effective partnerships and alliances

Collaborative approach with key suppliers and customers for better decisions in procurement, production, inventory and fulfillment.

Pilot new supply chain solutions

Piloting initiatives on a small scale reduces risk and can encourage buy-in from others within the organization or supply chain. Elements to be included in any pilot projects are:

Involvement of key stakeholders, suppliers, customers and employees.

Selection of scope and environment

Identification of critical success factors

Organise for supply chain performance

Organisational change for cross-functional instead of functionally based structures.

Develop measurement system for supply chain performance

Cross-supply chain instead of function focused measures:

On time in full, outbound

On time in full, inbound

Internal defect rates

New product introduction rate

Cost reduction

Order to delivery lead time

Fiscal flexibility

Somerset can also consider the proposal by Heinrich & Betts (2003) to transform company's supply chain into adaptive business network. This new business model joins companies as partners, into an adaptable and flexible set of business relationships such that each company is able to respond more swiftly into changing market conditions and leverage the network's cumulative ability to:

Plan and anticipate demand and supply.

Execute plans efficiently and effectively.

Sense events that affect the plans as those events occur, and analyze them for impact.

Respond to and learn from ever-changing business conditions.

Somerset can then move to an adaptive business network in four steps, as in Figure 4. 1:

Figure 4. 1 The Four Steps of an Adaptive Business Network

Step 1 – Visibility:

Sharing of information with partner companies.

Many routine business processes with partners standardized.

Information posted for common view on portal.

Greater insight into business process and data accuracy problems.

Step 2 – Community:

Moving day-to-day transactions to the portal.

Establishment of minimum and maximum control thresholds.

Reduction of inventory.

Time savings via mechanizing transactions.

Step 3 – Collaboration:

Sharing of customer demand data with members.

Targeted replenishment of supplies.

Responsibility transferred to supply replenishment vendors.

Ability to reallocate inventory to fulfill maximum number of orders.

Step 4 – Adaptability:

Time required for many tasks greatly decreased.

Many tasks completely eliminated.

Inventory and working capital dramatically reduced.

New alliances, products, and revenue opportunities possible.

Source: Heinrich & Betts (2003, p. 80)

Harrison & Hoek (2002) illustrates a number of transitional forces that need to be harnessed to give momentum to the change project, as structured in Figure 4. 2 below:

Figure 4. 2 Transition forces

Source: Harrison & Hoek (2002, p. 267)

These 5 forces are described briefly as follows:

Viability of current performance level

Consider in light of market changes such as:

Demographics

Time-stressed customers

One-to-one marketing

The marketplace becomes the marketspace

Perceived pay-off benefits from targeted performance

Reap the potential benefits of e-business and benchmarking of improvement projects to quantify the potential benefits of making a change.

Belief and enthusiasm

Ability of project manager to communicate belief in the change process with enthusiasm.

Ability to manage change

Ability to plan the change, organizing the resources needed to make the change and managing the application of those resources in order to achieve the necessary outcome.

Ability to operate in the new environment

People in the organization must have the right skills, tools and techniques to operate the new process. The management of the new process will require a new set of performance measures to be in place so that its efficiency and effectiveness can be assessed.

Specifically, there are several action items that are required to progressively (from Stage 1 to 3) change Somerset's supply chain network to be effective and efficient, as illustrated in Table 4. 1 below:

Table 4. 1 Action Items Required To Change Somerset's Supply Chain Network

Item

Action Item

Action To Be Taken

Remarks

1

Foreign Competition

Outsourced to China manufacturing plants –

Re-evaluate its capabilitynacity

Done

2

Shipment of Raw Materials from US

Source raw materials in neighbouring countries of China

Stage 1

3

Poor Distribution Network

Manufacturer storage with direct shipping to customers

Stage 3

4

Ineffective Order Management

Integrating demand and supply data using technology

Stage 2

5

Poor Transportation Management

Re-negotiate new contracts with all transportation modes

Stage 2

6

Ineffective Inventory Management

Implement JIT approach and pull system scheduling

Stage 3

7

Poor Product Quality

Get China manufacturing plant ISO9000 certified

Stage 1

However, the implementation of change in business is often frustrating and difficult, particularly in supply chains as it has to be undertaken in a coordinated manner across and between several organizations. It is therefore important to gain agreement from the top level of all companies involved before wide-scale changes can be made.

5. Conclusion

In this case study, Somerset's approach to manage its supply chain resulted in poor business performance. The visible hazards and other negative factors frustrated Somerset included poor logistics management, ineffective order system and inventory management as well as inconsistency of product

quality. In adopting a value chain, Somerset must incorporate and execute a robust supply chain management strategy for “ best-fit” suppliers selection, further establish on how to work with supply partners, distributors, suppliers, customers or even customers’ customers as a way to remain competitive. Otherwise, the company will not survive.

In addition, top management of Somerset has to lead and motivate not only all internal functional teams, but also external suppliers and partners, to work as an integrated entity in the new strategic supply chain network, so as to achieve the overall corporate objectives.

In a nutshell, supply chains have shifted from a cost focus to a customer focus, until currently to a strategic focus, scrutinizing the success of a strategy is just as good as the company’s capabilities to fully and properly execute all. A great supply chain strategic approach, connected with operational excellence, can provide success for not only the company in crisis but also its partners and customers.