Deciding Where to Source – Local, National, Regional, or Global

Stephen C. Rogers, Director Worldwide Purchases Mastery
Procter and Gamble Company
Cincinnati, Ohio 45202 513-983-5536
Adjunct Professor, Williams College of Business, Xavier University
Rogers.SC@pg.com
armo@cinci.rr.com

Lisa L. Cooley, Associate Director, Purchases Training and Development
Procter and Gamble Company
Cincinnati, Ohio 45202 513-983-0929
Cooley.LL@pg.com

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Abstract. The choice to import or localize supply is one that requires ongoing analysis and a willingness to adjust to emerging realities in the market. To become inflexible and static is to risk being overtaken by competitors with more responsive and current systems. A recurring sourcing process must weigh the business requirement's unique drivers to local, regional or global supply with the recognition that circumstances change over time. This positions Supply Management to optimally locate its supply base. A nine step assessment thought process forces evaluation of suppliers and market change to make informed geographical choices, not just at inception, but ongoing.

The Challenge. Current business periodicals headline the shift of business overseas to the Far- East, Eastern Europe and even Canada. The range of work includes assembled items (e.g. electronics from China and Malaysia), as well as chemicals and manufactured goods (toys, furniture, pharmaceutical intermediates – you name it). However, for the first time, services are also major components of the offshore buy, especially from India, Eastern Europe and Ghana, where data entry, software, call centers and engineering research are done long distance at low cost (30-60¢ on the dollar). It sounds like a "no-brainer" to shift all sorts of things to the Far East, following the pioneers from electronics and IT.

It is not that simple. While success stories get publicity, failures and inappropriate global sourcing efforts have also occurred. Not every commodity or service is suited for the long distance buy. It is critical to understand the geographical drivers of your spend and the dynamic nature of international sourcing during the sourcing market assessment process. For domestic U.S. businesses the choices range from local to national to off shore sourcing. Major multi-national corporations face a similar set of options as well: localized (national), regionalized (a portion of the world) and globalized (worldwide) supply. They parallel the domestic company's options, just with a wider, more interdependent set of using locations. Local for a multi-national could mean a country, while it equates to a city or state for the domestic company. Similarly, the multi-national's "Region" might be Europe, while the domestic company's is "the Northeast".

	Domestic Company	Multi-National
Local	City, State	Country
Regional	Region of a Country	Region of the World
Global	Offshore, Foreign Source	Worldwide

The Drivers. For the multi-national corporation, there are circumstances that favor the localization of supply rather than importation – these drivers vary depending on the specific using location. For Procter and Gamble, a U.S. facility can see a very different set of localization drivers than a facility in Argentina or Thailand. Extremely attractive dollar cost for the U.S./customer may be unaffordable when exchanged into Reals or Baht. A global company's drivers for local sourcing include:

- Currency (particularly in weak currency countries).
- High duties, tariffs and import taxes.
- Service benefits (time, cash flow, flexibility).
- Geographic or logistical barriers (port infrastructure, mountain ranges).
- Low cost local sources (technology, labor).
- Well developed local industries with competition.
- JV considerations (inherited or partner relationships).
- Local content laws or, in the U.S., Minority and Women Owned Businesses.

The next step along the continuum is Regional sourcing, which implies the casting of a wider sourcing net (a number of geographically proximate countries – or states domestically) and the existence of several using locations across a broader geographical area. A series of factors can drive toward Regional sourcing:

- Regional leveraging opportunities (negotiating power of greater volume).
- Relatively easy and timely cross-border shipping (geographically and infrastructure).
- Regional trading agreements – low/declining duties, low freight.
- Suppliers capable of exporting (operationally and administratively).
- Technology only available Regionally, not in every country.
- Local supply monopolies that require outside competition.
- Relatively equal currency value between countries.

The broadest end of the continuum is global sourcing which includes two extremes – a) buying from a single country that is competitive across the world or b) buying from several suppliers across the world, creating a marketplace that spans multiple geographies depending on changing economic environments or needs. Drivers toward global sourcing include:

- Global leveraging opportunities (negotiating power from greater volume).
- Uniquely low cost supply inputs (labor, energy, raw materials) in certain parts of the world.
- Transportable commodities (services via internet/telecom, goods via water or air).
- Finished product cost structures that allow higher/longer freight considerations (durables vs. non-durables).
- Unique technologies that result in a few suppliers who export worldwide or supplier capabilities that can be successfully transplanted to a limited number of sites around the world.
- Interchangeability of supply around the world (common specs or statements of work).
- Small or absence of duty, tariff or local content laws.
- Established globally dispersed supply bases made up of export-oriented suppliers.

- Order patterns for your own finished product that allow enough leadtime for global shipment (e.g. durables).

Watch-Outs and Assessment Process. Business commerce is dynamic with constantly changing supply/demand elements. Supply Management organizations are constantly seeking to anticipate the next "low cost source". The electronics hopscotch game across Asia from Japan to Korea to Southeast Asia to China/India is just one example. Most people see it as a search for lower cost suppliers, but other changes can quickly shift sourcing from global to local or regional. Trade protectionism (anti-dumping suits, tax/tariff changes), volatile currency, emerging new suppliers and technologies, economic disruptions (inflation, deflation, terrorism, war) and regulatory shifts (e.g. European GMO good regulations, Mad Cow disease implications, SARS quarantines, etc.) can require changes in geographical sourcing scope – either sudden or gradual – depending on the situation. To put sourcing on automatic is a serious mistake. An ongoing 9-step assessment process ensures effective choices.

Assessment Process. Once a specification or statement of work is in place and volume estimates available, the nine-step assessment is as follows:

1. Is this item currently made anywhere today or could it be made with relatively small changes to existing supplier operations? (broad geographic scan, industry analysis and patent searches).
2. Is necessary quality available and, if not, can existing quality work or can a supplier make what we need? (spec understanding, cost and feasibility assessment, and supplier assessment).
3. Is capacity adequate or expandable with reasonable investment? (sensitivity analysis of volume, feedstock/labor availability, capacity investment, and industry supply/demand forecasts).
4. Where are the supplier sites located? (Local, Regional, or Global?, leveraging opportunities to fill plants, competitive opportunities between suppliers).
5. What are the delivered costs to the using locations from supplier locations? (FOB price, market price history, freight, handling, duties, taxes, feedstock/labor cost trends, currency implications, transport capabilities).
6. At each using location, are local costs or imported costs more competitive and can they be influenced via competition, capital utilization or negotiation? (sourcing strategy, supply relationships, competitive analysis, trade laws/agreements, TCO analysis, value analysis).
7. Is the logistics or delivery system capable of delivering against business needs? (leadtime assessment, inventory, cash flow analysis, country entry provisions, political situation, demand planning linkage, e-connections).
8. Which supplier(s) meet the cost/quality/availability/service needs of the business to provide value? (supply matrix and capable supplier listings, potential new supplier options, competitive supplier overlays, contracting strategy, internal using location options, competition's use of capability we uncover, make vs. buy analysis).
9. Re-evaluate to deal with/anticipate market changes. (annual assessment of usage, market, currency, trade laws, competition, supply/demand, cost structure, spec change, supplier relationship/results).

The result is not a static supply line but rather an ongoing dynamic, interactive review of the supply base to continually assess and improve supply capability and geographically locate/place suppliers where they provide best value.

<u>Organization Capability</u>. We would be remiss if we did not comment on what it takes to do this organizationally. Assuming that you are capable to move from local to imported supply and back without risk may well be a mistake. On the ground supplier knowledge about the suppliers – technical and commercial – is critical either directly or through trustworthy third parties. Strategic capabilities to change suppliers/protect supply, deal with local legal/regulatory differences and provide sensitive information safely are all capabilities that must be considered. Even “simple” tactical considerations are necessary – adequate access (computers, Web), work across time zones and languages (e.g. first language English vs. second or third language English can bring very different understanding). Think about how you will deal with these issues in terms of the skills and support systems put in place for your people.