Q&A: The New Global Supply Chain

Q&A with Barry Jaruzelski, Partner, Booz & Company

IMPO: How is the supply chain changing in 2011?

Jaruzelski: It's a bit of a good news/bad news scenario. Obviously, the good news is that we've turned the corner on the recession. Production is back up, which means there is more demand throughout the supply chain.

The "to be determined" news is that in response (to the recession), people cranked down their inventory levels, and increased the amount of slack they had in the system. We will see whether people overshot on the downturn, and whether they will have supply constraints as things come back, particularly if they were fortunate enough to have a particularly hot product. I think we're going to increasingly see stories about shortages and outages because of the conservatism that people now build into their supply chain.

The poster child for these issues is the suspension — or interruption — of rare earth supplies from China, whether it was meeting internal demand, geopolitical decisions, or a combination of both. Coming out of this recession, I think that two things are going to be happening simultaneously as people are looking at their supply chain. One, is that there's different levels of political risk in having suppliers or parts of your supply chain in different countries.

Another issue is that the relative economic and currency position of different

countries has changed. The fact is that we all know what the trend is. The trend is all going to be one-way on those debates, and the issue is the velocity at which it gets there. A lot of people are going to be wondering why they picked certain suppliers, and why they decided to locate production facilities in certain locations. It was based on a set of assumptions. The relative currency and relative demand in a many of those cases is different. A lot of folks are going be revisiting why they did that, where it's likely to move, and they'll start to layer on that second-level question: How much can I rely on that being a safe supply?

I wouldn't say that people are going to be running for the hills—that would be sophomoric. A different lens is going to be put on both the relative currency advantage, the relative cost advantage, and the geopolitical risk assessment of being in certain countries as a source of supply and a source of production.

IMPO: You mention looking through a different "lens" at the situation of having an overseas supply chain. Could these same issues arise in the future with any other country?

Jaruzelski: It gets to the need for a diversified supply base. You want alternatives. There can be geopolitical decisions, or, for example, there was the earthquake in Taiwan, which had a massive impact on flat-panel computer screens for notebook computers. That was purely a natural disaster, but that impacted availability. It comes down to the same issue: being overly-concentrated in only one locale.

IMPO: What else can manufacturers do to prevent supply chain incidents in the future?

Jaruzelski: One option is looking toward alternative sources that are trending away from being volatile. Secondly, are there options that are closer to home? It's not just the cost of the material in China, for example. What's the cost of transportation? What does it cost to have this component or material sitting on your loading dock? If oil prices continue to rise, that will ripple into the cost of transportation, particularly by ship. And you have the cost of the component, the cost of what it takes to get here, the vulnerability, and that you have to "own" the item for however many weeks or months while it's in transit. Obviously, that lengthens the ellapsed amount of time in your supply chain.

The other thing — and this is more of a strategic question — is how you feel about the intellectual property dimensions, if you have a more engineered product. That has been a long-going concern, particularly in certain arenas of particularly advanced goods, electronics, and industrial products. Can you really strategically risk having a product made there? And we're starting to see companies who are making decisions where the more commodity-based dimensions of their product are being made in China, but with the highly-proprietary portion — where they're concerned about losing the process knowledge — components are maybe made in Mexico. You don't actually let the "secret sauce" pieces of the final product be in places where you're concerned about protecting intellectual property.

IMPO: Will that account for more production being moved back to the U.S.,

or will these companies simply shift their work from one low-cost country to another?

Jaruzelski: Realistically, the beneficiaries are unlikely to be U.S. manufacturers. For highly-engineered goods — think power turbines, or commercial aircraft — we're not competing with the Chinese. We're competing usually with the Japanese or the Europeans. Our exchange rate between us and them is much more to the point. For the things that might make the Chinese less competitive — textiles, or consumer electronics — the beneficiaries of that loss of competitiveness will be Vietnam, or India, or the Philippines, not the United States.

The idea that it's going to have a marked impact beyond just potentially just reducing imports, because everything becomes more expensive, is probably wishful thinking.

IMPO: I've noticed that among *IMPO* readers, there is a slight distrust of consultants. What's Booz & Company's "pitch" as to why consultants can bring new ideas to the table.

Jaruzelski: [Consultants] are an impartial advisor. Particularly for large strategic questions, there's a lot vested (in the situation), which makes it difficult for there to be an honest dialogue. Sometimes an outsider, who doesn't have a vested interest in the outcome, will actually be able to analyze the data — present the pro's and con's — and make a recommendation. Ultimately, a consultant is just a consultant. Management has to make a decision based on the merits of the case, but an independent, impartial third party can help.

Clearly, any effective consulting situation needs to be collaborative, because management will always know the day-to-day situation better. But consultants, having seen similar challenges — sometimes once-in-a-lifetime challenges for a particular company — can bring the context of what other people might have experienced when confronted with that situation. Call it "best practice." They can provide that context of how others have dealt with analogous challenges.

Booz & Company has 61 offices around the world. Having that global footprint, and that global access and perspective, is part of what we bring to the table.

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