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The top 5 mistakes companies make in managing supply chain risk effectively

Supply chains today are global – even if a company has its manufacturing in-house and on-shore, chances are, their parts or raw materials originate in 10-20 countries around the globe. In the last 15 years, companies have adopted Lean and Just in Time (JIT) practices as well as Build to Order type capabilities in a big way – this means, that globally stretched supply chains are overly optimized to operational parameters like lead times and often have low levels of buffers that would help to withstand disruptions. Business metrics focus heavily on cost reduction and inventory turns – short term incentives tied to these metrics further result in decisions at every level that erode resiliency. Traditional supply chain management practices leave vast gaps in resiliency because supply chain risk management is fundamentally different from every day operations management. When companies fail to recognize and appreciate these differences, they fail to manage risk effectively.

1

Quantify everything only by spend and not by impact

Most supply chain professionals, if asked to name critical suppliers or parts, will talk about the top 20% of parts or suppliers that constitute 80% of the total spend. All supply chain functions are prioritized by spend. Resource, time and budget allocations are all optimized to this breakdown, and it has worked well - until now. In the past 15 years, the global dynamics have changed. Suppliers are no longer where we think they are… it is so easy to setup offshore operations and outsource parts of the supply to sub-contractors. It is easy to lose sight of the long tail (80% of suppliers representing 20% of spend), esp. if there is a lot of single sourced or custom material in the low spend category. Custom paint, connectors, power supplies and other low spend items and even some kinds of labels with no alternate source can become single points of failure in the supply chain. After all, we can't ship a car without paint, or a phone or laptop missing a connector or a button. A Merck paint pigment factory impacted in the Japan earthquake caused severe shortages and lost sales at Ford, Chrysler and many other car companies for several months.

In order to ship a product, every single part needs to be present – this is the fundamental challenge for supply chain practitioners. And the biggest mistake is that in optimizing everything based on cost/spend, the impact to business is ignored. A hybrid approach also looks at revenue impact of losing a part or supplier and arriving at the "new" list which also represents single sourced, custom dependency on low spend suppliers.

2

Getting to the root cause of the problem - visibility

The fundamental challenge with risk management today is the lack of visibility into global supply chain dependencies. The answer to "what is my TRUE supply chain" is incomplete at best. There is no visibility to where parts come from or who is building them? Are my dual sourced parts truly dual sourced or are there single sourced dependencies one or two levels up the supply chain? These are far more important questions and while there is widespread acknowledgement of the problem very few have done what is needed to get visibility and enable control. The above questions need to be effectively answered and impact to business of losing a part, site or a source quantified in terms of revenue. Following this a prioritization strategy needs to be formulated which can help identify areas of the supply chain which need immediate mitigation. This will help deal with, not only with the large catastrophic events, but also many ongoing location related smaller disruptions that we supply chain practitioners encounter on an ongoing basis.

3

Consistently put risk management under immediate short term priorities

The world of supply chain management is highly dynamic. Shortages, demand upsides, excess, supplier issues, delivery delays, quality problems – the list of operational challenges that are here and now is long. Supply chain organizations are almost always under intense budget constraints. In this scenario, often organizations flit from one issue to another, always reacting, always scrambling. Key people have no time to take a step back and assess the supply chain proactively or take efforts to gain visibility and greater control. Rewards and incentives are tied to achieving short term goals around cost savings, inventory turns, time to market etc. This incentive misalignment causes indiscriminate inventory reduction and always a push to source or manufacture in areas with high supply concentration. Proactive supply chain risk management is the one activity that is at odds with targets, incentives and rewards – thus, it is the one activity that is a lot easier to deprioritize. In order to ensure that this doesn't happen, risk management/mitigation efforts have to be tied to metrics and incorporated into processes and reviews - this should be supported with regular reinforcement and incentives from top level down.

4

No one person accountable for risk management

A Procurement Strategy Council research report indicates that the vast majority of CxOs hold the Chief Procurement Officer responsible for supply chain disruption response. However, it is not at all clear as to who is the person that the CPO holds accountable in his/her organization. Most companies don't have this responsibility assigned to a person or group within the supply chain or procurement organization – someone who can take leadership at an operational level. This means, when there is a crisis, there is a large amount of confusion and lack of coordination as extraordinary response actions fall outside the normal scope of responsibilities. Every crisis needs a leader for effective response coordination and recovery, but what doesn't work is that every crisis looks for someone to take the leadership mantle. A May 2011 study by W P Carey reveals that leadership is as critical as effective systems for crisis response. Rudy Guiliani proved in his handling of the Sept 11 attacks that an effective leader who is accountable and who wears the mantle with responsibility can make all the difference. On the other hand, FEMA's handling of the Hurricane Katrina disaster reveals how an unprepared and inexperienced leader can create immense amount of angst and chaos. A strong leader, appointed in advance, trained and equipped with information, tools and crisis response infrastructure can help the CPO appear to be in control, rather than at the mercy of the event. Lack of a coordinated response does have its downside – Michael Brown had to step down in the aftermath of Katrina amidst a lot of questions about his leadership – the PSC report cites a 62% likelihood of a job loss. But more importantly, the upside of demonstrated leadership excellence in crisis response is high – Guiliani went on to a Presidential run largely on the basis of his leadership during the 9/11 crisis.

5

Subconsciously endorsing the diving catch approach

A crisis, even a small one with low to no impact, is an opportunity to learn. However, this critical point is not sufficiently appreciated – often we think we got lucky when we are not impacted or are able to recover quickly. A crisis war room is perceived to be the place where people get exposure to top executives – visibility! If product gets to the customer by paying 20x premium and 10x freight expedites, the execution team has "saved the day"… while necessary in extraordinary times, the fact is that this type of a diving catch approach for every situation has a huge impact on profitability. In the aftermath of Japan factory shutdowns, Toyota's profitability took a 75% hit and they lost their number 1 position; Cannon's profits dropped 29% and they missed Mother and Fathers' day sales. A post crisis assessment with Finance would reveal the cost to the business of such an approach. A post crisis assessment is very important as it helps develop key insights into what went wrong, and where investment and attention is needed in order to ensure that next time, we are better informed, more in control, more coordinated and less impacted. Smaller disruptions have to be perceived as drills and training for when the big one strikes. Rewards have to be in place for crisis aversion rather than crisis response – this is the best way to ensure that proactive risk management becomes embedded in an organization's culture.

To conclude, supply chain risk management has to be thought of as a strategic investment and viewed in the context of long term gains. Limited duration consulting projects for risk management don't address the core issues and in a highly dynamic world, are outdated before the report hits the executive desk. Risk management needs a fundamentally different approach from traditional supply chain management. As long as these differences go underappreciated, companies are not focusing efforts where they are truly required, nor are they solving the visibility related problems that are at the root cause of the problem. They are not empowering nor encouraging people to make resilient choices proactively… which means we will be in a reactive mode in every disruption – scrambling and trying to catch up. Given the widespread globalization of supply chain and the extreme impact of disruptions on corporate results, supply chain risk management is on the fast track to become a corporate governance issue that requires the attention of not only the CPO, but also of the CEO and eventually the board. Corporations would do well to start preparing for this new level of scrutiny. The reality of the new globalized world is that we are going to face disruptions from one corner of the globe after another. So it is time to invest resources and budget into tools, processes and leaders to ensure that we have a well-oiled and trained machine for swift, coordinated crisis response every time we are faced with a disruption.

About Resilinc

Resilinc offers an end to end cloud-based solution for proactive supply chain risk management deployed with large and mid-sized High Tech companies. Delivered on the Force.com platform, their highly scalable supply chain mapping solution helps capture global locations where parts originate and quantify revenue impact of losing a supplier, part, site or region as well as risk scores. Their crisis solution involves crisis preparedness tools, disruption monitoring and response capabilities, as well as enterprise social networking to capture the collaborative elements of a truly effective risk management platform.

About ALOM

ALOM is a Fremont, California-based supply chain management provider.
Our award-winning services are designed to provide world-class global management and execution of corporations' product supply chain as well as marketing operations supply chain. Services include materials and inventory management, print management, logistics, assembly, light manufacturing, fulfillment, and reverse logistics from 14 locations across North America, Asia and Europe. ALOM caters to the technology, medical, automotive, energy and clean-tech, as well as the government market. More information is available at www.alom.com

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