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THIS WEEK IN CONSULTING:

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SUPPLY CHAIN COLLABORATION:

Supply chain collaboration is a hot topic because companies have enjoyed dramatic reductions in inventories and costs, together with improvements in speed, service levels, and customer satisfaction.

Collaboration has to be 'win-win' for both parties.

Supplier chain collaboration itself isn't new. What's new is that it's taken on a much greater urgency and importance. **We used Supply Chain Collaboration at The Schwinn Bicycle Company in Chicago, IL during the 60s-80s before Schwinn shut down operations.**

Collaboration between companies are ***joint initiatives*** that go beyond their normal course of day-to-day business, with the aim of delivering significant improvement over the long term. With pricing under pressure from recession-scarred consumers, the temptation for retailers is to transfer the pain upstream to their suppliers by passing on price reductions and forcing them to bear an increasing share of costs.

On the supply side there is less and less room for manufacturers to absorb additional costs as volatile input prices put the squeeze on margins and the marketing investment required to differentiate branded products from private-label competitors continues to rise.

Sixty-five percent of procurement practitioners say procurement at their company is becoming more collaborative with suppliers, according to *The Future of Procurement, Making Collaboration Pay Off, by Oxford Economics.*

Why should you collaborate? Because, basically, adversarial relationships do not work effectively. Because the pace of business has increased exponentially, and businesses must be able to respond to new market demands with agility and innovation. In this climate, buyers are relying on suppliers more than ever before. And buyers aren't collaborating with suppliers merely as providers of materials and goods, but as strategic partners that can help create products that are competitive differentiators.

Supplier collaboration has always been a function of maintaining a delicate balance between demand and supply. For the most part, the primary focus of the supplier relationship is ensuring the right materials are available at the right time and location. However, sourcing managers with a narrow focus on delivery are missing out one of the greatest advantages of forging collaborative supplier partnerships: an opportunity to drive synergies that are otherwise perceived as impossible within the confines of the business.

The big challenge is when you drive those synergies with thousands, not hundreds of suppliers. Look at the Apple Store as a prime example of collaboration for the masses: Without the apps, the iPhone is just another ordinary phone!

Suppliers don't just collaborate with you to provide a critical component or service. They also work with your engineers to help ensure costs are optimized from the buyer's perspective as well as the supplier's side. They may even take over the provisioning of an entire end-to-end solution. Or co-design with your R&D team through joint research and development. ***A good tool is Value Engineering: retain the function and quality of anything, but find ways to reduce material and process costs through cross-functional team brainstorming.***

These forms of collaboration aren't new, but they are becoming more common and more critical. And they are becoming more impactful, because once you start extending any of these collaboration models to more and more suppliers, your capabilities as a business increase by orders of magnitude. If one good supplier can enable your company to build its brand, expand its reach, and establish its position as a market leader – imagine what's possible when you work collaboratively with hundreds or thousands of suppliers.

As a sourcing manager, you may need to go outside your comfort zone to think about new, innovative ways to collaborate for achieving sustainability because Collaboration comes in more than one flavor!

Supply chain collaboration has delivered some real value for participants, but overall, these initiatives are more likely to fail than to succeed. Indeed, participants in the 2010 CCM survey said that only two in 10 of their collaboration efforts delivered significant results. The remaining 80 percent represent more than just lost opportunities to add value.

If companies can't make collaborations work, they will not only fail to achieve the potential benefits that supply chain collaboration can provide, but they will also risk destroying the enthusiasm for further attempts, both inside their own organizations and with their trading partners.

Making The Right Choices

Companies can greatly improve their prospects for collaboration by taking a more thoughtful approach to the areas they select for collaboration, their choice of suppliers / partners, and the way they implement their collaboration efforts.

In this article, we will focus on key actions to ensure successful supply chain collaborations – productive collaboration and not a frustrating one; and turning supplier collaboration into a core competency.

1. Collaborate in Areas where You have a Solid Footing

Companies are often tempted to use collaboration as a way to fill gaps in their own capabilities. In practice, the most successful collaborations build on strengths rather than compensating for weaknesses. A manufacturer seeking to collaborate with a major retailer in order to improve its own forecasting performance, for example, will have little to gain from access to the retailer's point-of-sale data unless it has the in-house analytical capability to make effective use of that data.

Similarly, there is little point in entering collaborations to boost sales if any increase in demand is likely to run into manufacturing-capacity constraints.

Understand your category like never before so that your organization can realize the full potential of its supplier investments while delivering products that are consistent and of high quality. How? By leveraging the wisdom of your suppliers. To be blunt: they know more than you do.

Tap into that knowledge to gain a solid understanding of the product, market category, suppliers' capabilities, and shifting dynamics in the industry, If a buyer does not understand these areas deeply, no amount of collaboration will empower a supplier to help your company innovate as well as optimize costs and resources.

Potential collaborators should also be sure they have the right supporting infrastructure in place in advance of any collaborative effort. Is top management committed to the collaboration process and ready to offer support over the long term? Are in-house information technology (IT) systems robust enough to facilitate real-time data sharing if required?

2. Turn Win-Lose situations into Win-Win Opportunities with the Right Benefit-sharing Model

Some collaborations promise equal benefits for both parties. If, for example, a manufacturer and a retailer collaborate to optimize product mix, both could expect to benefit from the resulting increase in sales. In other cases, however, the collaboration might create as much value overall but the benefit could fall more to one partner than to the other.

Here's one real-life example: a retailer and a manufacturer were able to reduce overall logistics costs between factory and store by cutting out the manufacturer's distribution centers and treating the retailer's distribution network as one integrated supply chain, from manufacturing plant to store shelf. However, the retailer's supply chain executives struggled to gain acceptance for the idea from their leadership because it resulted in the retailer carrying a far larger fraction of the logistics cost.

Rather than shying away from such asymmetric collaborations, smart companies can make them work by agreeing on more sophisticated benefit-sharing models. These can come in the form of discounts or price increases to more fairly share increased margins or cost reductions, or they can involve compensation in other parts of the relationship.

For example, when one retailer collaborated with a manufacturer on a co-branded product line, the manufacturer agreed to absorb the upfront product-development costs in return for an expanded share of the retailer's product offerings across a wider set of categories.

Benefit sharing can help to overcome differences in strategic priorities, too. One growth-focused manufacturer was persuaded to join a supply chain waste-reduction collaboration with a retailer by establishing an agreement to deposit part of the savings both companies achieved into a joint pool, which would then be invested in efforts to generate additional sales.

The two companies established a joint benefits pool and agreed to use a percentage of the savings to fund future cost-reduction efforts and a sales-improvement program.

Why not seize the opportunity to raise your and your supplier's brand profile in the marketplace?

Take Intel, for example. The laptop you're working on right now may very well have an "Intel inside" sticker on it. That's co-marketing at work. Consistently ranked as one of the world's top 100 most valuable brands by Millward Brown Optimor, this largest supplier of microprocessors is world-renowned for its technology and innovation. For many companies that buy supplies from Intel, the decision to co-market is a strategic approach to convey that the product is reliable and provides real value for their computing needs.

3. Select Suppliers / Partners based on Capability, Strategic Goals, and Value Potential

The biggest potential partner might not be the best one. Many companies aim to collaborate with their largest suppliers or customers because they assume that the greatest value is to be found there. In many cases, however, this turns out not to be true.

Collaboration may be of more interest to a smaller partner, which might invest more time and effort in the program than a very large one that is already juggling dozens of similar initiatives.

A better approach is one that assesses current customers or suppliers across three key dimensions.

First, is there enough potential value in collaborating with this partner to merit the effort? Both partners in a prospective collaboration need to be sure that it will deliver a sufficient return to justify the upfront investment.

Second, do both partners have sufficiently common strategic interests to support the collaboration? A retailer that has prioritized growth in a particular region or segment will have more to gain from collaborating with a manufacturer that has a strong offering in the same area.

Third, does the partner have the right infrastructure and processes in place to provide a basis for the collaboration? Collaborating to improve forecasting and demand planning is likely to be frustrating if one partner's existing planning processes, systems, or performance are inadequate.

4. Invest in the Right Infrastructure and People

Lack of dedicated resources as one of the top three reasons for the failure of collaboration efforts. Companies frequently underestimate the resources required to make collaborations work, assuming that they can leave it up to staff in various functions to do what's required in addition to their other responsibilities.

In practice, even relatively simple collaborative tasks will be more difficult than equivalent activities conducted within the walls of the organization. That's because staff must overcome differences in culture, organization, and terminology, not to mention the basic challenge of finding the right contact within the partner organization with whom to liaise.

To prevent these problems, best-practice companies devote extra resources to their collaborations, particularly in the early stages of a new relationship. Appropriate infrastructure for a successful collaboration begins at the top of the organization, with a steering committee of senior leaders who can set the defining vision for the collaborative effort and allocate resources to support it.

The detailed design of the collaboration program is then completed by a team comprising members of all relevant functions from both partners in the collaboration. The team for a demand-planning effort, for example, should include members from sales, finance, and supply chain for the manufacturer, and from purchasing, merchandising, and store operations for the retailer. This team will also be responsible for the day-to-day monitoring of the effort once it is up and running.

Execution of the collaboration should take place within the line organization and will ultimately form part of the everyday responsibility of the staff assigned to it. The best companies avoid forcing their front-line staff to "reinvent the wheel" by providing strong support when establishing each new collaboration. They may, for example, leverage experience gained in previous collaborations by setting up teams to support their colleagues during the initial phase of subsequent efforts.

5. Establish a Joint Performance-Management System

An effective performance-management system helps a company to ensure that any long-term project is on track and delivering the results it should. In supply chain collaboration efforts, both participants should use the same performance-management system. By building common metrics and targets and jointly monitoring progress – companies avoid the misaligned incentives that damage so many collaboration efforts.

Picking the right metrics can be challenging, however, and it will inevitably involve trade-offs. In a collaboration to reduce logistics costs, for example, the partners may have to choose between a pallet configuration that's optimized to suit a retailer's restocking processes, which will reduce in-store labor costs, and one that optimizes truck fill, which will reduce transportation costs from distribution center to retail store.

How to overcome these potential conflicts? The trick is to keep things simple by picking the smallest possible number of metrics required to give a picture of the collaboration's overall performance, and then to manage those metrics closely, with regular joint reviews and problem-solving sessions to address trade-offs.

The real power of any performance-management system comes from this frequent, robust dialogue between partners, yet this is also the element most commonly ignored or underemphasized by collaborating companies.

6. Collaborate For the Long Term

The final vital ingredient of a successful collaboration is stamina. It may take time and effort to overcome the initial hurdles and make a new collaboration work. Both parties need to recognize this and build an appropriately long-term perspective into their goals and expectations for the collaboration.

This means including metrics that review performance beyond the first year, as well as conducting some joint, long-term planning so both partners can gain an understanding of each other's longer-term objectives and identify a roadmap of initiatives they can work on together over time. Such planning helps companies to break out of the short-term-project mentality that can limit the beneficial impact of collaborative efforts.

Nevertheless, partners must also take care to ensure that they are doing everything they can to capture any available quick wins, so the collaboration starts delivering value as rapidly as possible.

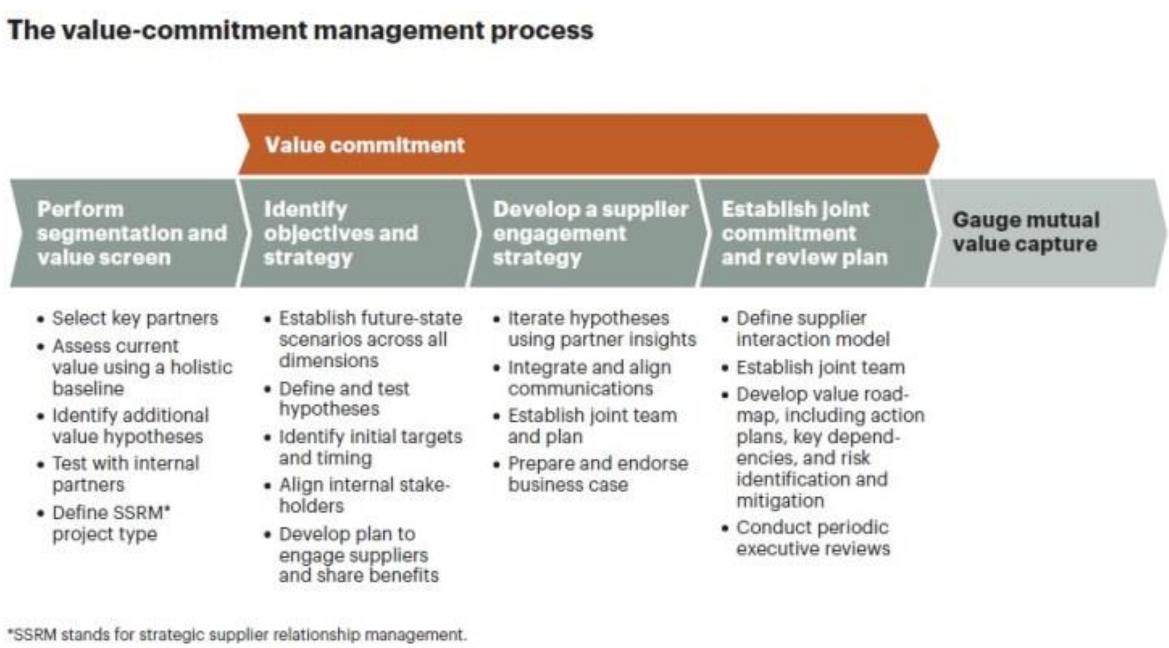
When companies take a long-term perspective, their collaborative efforts can become a virtuous circle: a greater understanding of each other's capabilities, knowledge, and costs will often reveal new potential sources of value, while the experience of working closely together means that later initiatives will take less time and be easier to execute than early ones.

Turning Supplier Collaboration into a Core Competency

Turning supplier collaboration into a core competency will not be easy. But when properly structured as an initiative to develop a key capability, it will not be insurmountable (no more so than developing strategic sourcing capabilities was 20 years ago). There are tried-and-true ways to establish this competency, requiring consideration of three core elements:

1) Form value creation teams

Value creation teams follow a flexible but repeatable “value commitment management process” for creating mutual opportunities to create value (see figure). Each team, comprising the appropriate internal stakeholders, begins with a value segmentation and screening of potential partners, followed by defining objectives and strategy, including development of a plan for engaging suppliers and sharing the benefits. The next step is engaging suppliers, seeking deeper insights through more integrated work, followed by a joint commitment, in which a joint team develops a roadmap and business case, with periodic executive reviews.



2) Establish foundational processes

These processes guide the value-creation teams so they can devote their creativity to the work, rather than the procedures to accomplish it. These processes should include cross-enterprise governance models (to encourage supplier interaction), organizational redesign (making necessary changes), and protocols for measuring and sharing value.

3) Manage the transformation

Transformation management ensures that the investment in various capabilities pays dividends. Goals include talent management (because the skill sets for collaboration differ from those needed in sourcing), knowledge transfer, performance measurement, communications management, and an active transformation management office.

Benefits of Supply Chain Collaboration

In the case of supply chain collaboration, ***sharing of information leads to enhanced knowledge across the chain that allows you to achieve:***

You can use a <u>Service Level Agreement (SLA)</u> as a collaborative win-win "living" document that you discuss together and set key metrics. This SLA can be reviewed in detail monthly so you both see if you are meeting metrics you both set, like:

- Lower inventory levels and higher inventory turns
- Lower transportation and warehousing costs
- Lower out-of-stock levels
- Shorter lead times
- Improved customer service metrics
- Visibility into customer demand and supplier performance
- Earlier and quicker decision-making
- Incremental revenue growth
- Mitigate potential supply disruptions and the potential risks become opportunities to gain advantage over competitors.
- A sustainable competitive advantage such as cost, agility, responsiveness and scalability

Conclusion: <u>Potentially Huge Payback</u>

It should be clear by now that successful supply chain collaboration is neither quick nor simple. But is it worthwhile? The answer is <u>"YES."</u>

In my experience, successful Supply Chain Collaborations that involve two or three separate initiatives in a category boost margins by 5% in the affected category, through a combination of increased sales and reduced costs.

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Mr. Charles (Chuck) Intrieri is a highly experienced and credentialed Supply Chain professional and is a recognized thought leader and innovator, primarily in the areas of Supply Chain Optimization, Third Party Logistics (3PL) International Purchasing/Importing, Requests for Quotation (RFQ) generation, Inventory Management and Logistics, Warehousing, strategic sourcing, supplier management, contract negotiations, truckling: TL/LTL/TMS/pooling/consolidation and reviews, and Purchasing operations. He is a motivational team builder with a history of conducting c organizational transformation and achieving important operational successes at the local, regional and global level.

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