Three Key Supply Chain Management Questions for 2023

By Jonathan Powell, *Partner*
Posted February 24, 2022
kernuttstokes.com/kernutt-stokes-blog/

Manufacturers will continue to face supply chain headwinds in 2023, a cause for concern following a turbulent few years. Economic uncertainty, supply shortages, rising costs and frustrated customers threaten to impede growth.

Some supply chain industry pundits would have us believe there is little businesses can do about these disruptions, and they must be at the mercy of external factors outside of their control. Fortunately, however, manufacturers have options to mitigate the impact to their supply chains with a little clarity, discipline and direction.

To help you navigate the next 12 months, we've answered three frequently asked questions from our clients on how to optimize their supply chains amid constant uncertainty and disruption.

Question 1: Does a "China Plus One" strategy adequately diversify my supply chain?
By now, most U.S. businesses and consumers understand that far-flung global supply chains were too dependent on China. Even prior to 2020, many business leaders had already begun shifting away from China in the wake of the previous Administration's tariff challenges, IP disputes and the ensuing trade war. Factory and port shutdowns in China in the early days of the pandemic and the issues that have followed were wakeup calls for those that hadn't seriously considered alternative sources of supply. An enduring lesson of the past few years is that sole sourcing from any vendor or vendors in one location comes with a high-risk level.

Building redundancy into the supply chain at different tiers and maintaining inventory levels have become guiding principles for manufacturers. The "China Plus One" strategy has been on the radar of companies with China operations for several years but motivation to change didn't materialize until the trade war, pandemic, and subsequent disruptions. The need to diversify supply chains is now a priority, with many manufacturers actively pursuing a "China Plus One" strategy by supplementing sourcing from China with another country in Southeast Asia. However, the supply chain crisis of the past two years shows this strategy may also be failing. As long as the goods produced are an ocean away from the markets that consume them, uncertainty from various disruptive factors can lead to shortages, higher costs, lower revenues and customer dissatisfaction.

Where to focus now:
While decoupling from China is part of the equation, truly de-risking the supply chain comes down to three things: optionality, redundancy, and market proximity to your customers. Redundancies should be

intentionally created to avoid a single point of failure. And while fully onshoring production and/or sources of supply may not be operationally, economically, or logistically feasible, the supply network is less risky when it is closer to the market where it's consumed.

Consider engaging with new suppliers and contract manufacturers in the Americas to better serve the U.S. market. You should also review your supply base for any overreliance on a single source or geography, then consider options to decrease the distance between where your products are produced and where they're purchased. Insourcing, onshoring, nearshoring and acquisitions are all on the table. The approach that makes sense for your business must consider cost, capacity, quality, control and reputation, but regardless of your approach, the goal should be to improve supply chain resilience and flexibility so you can better manage the disruptions.

Question 2: Does having a backup plan mean I'm prepared for future supply chain disruption?
Maybe, if that backup plan has built-in agility and can be adapted and activated swiftly based on a variety of external factors. In the last few years, many manufacturers discovered static backup plans were not adequate to address the rapidly changing conditions across the globe. These backup strategies were not agile enough to be effective amid complex disruption. Consequently, manufacturers were challenged to get the level of service they needed from existing suppliers or quickly identify new suppliers, resulting in processes that simply were not feasible from an implementation or sustainable cost standpoint.

Backup plans have their place, but they're generally based on known risks. As global supply chains grow more intertwined and the universe of uncertainty expands, new risks and variables come into play. You can't just plan for one contingency – you need to weigh the outcomes of multiple options across different scenarios. Changes in manufacturing locations and sourcing strategies aren't the only scenarios worth evaluating, nor is resilience to disruption the only outcome worth measuring. For example, if you're considering expanding into a new market or adding to your product mix, those strategic adjustments should be factored into your supply chain model and assessed for plausibility. Tax liabilities, trade compliance risks and total cost to serve are no less critical considerations than deliverability or lead times.

The reality is you cannot prepare for every contingency, so scenario planning needs to evolve to detect signals of disruption earlier and enable greater agility in supply chain decision-making when the unexpected occurs.

Where to focus now:
Review your supply chain model to reflect current constraints and incorporate points of vulnerability and conduct a scenario planning exercise to address a specific problem or inform your next strategic move. Ideally, you should simulate multiple scenarios to pressure test the supply chain, anticipate issues and chart the best path forward when disruption hits. Scenario planning should become a regular business practice so you can quickly respond to unforeseen events.

Question 3: Is raising prices the only way to offset increases in material and transportation costs?
It's not the only way, but tradeoffs will need to be made. Higher costs are an unfortunate reality for most manufacturers in the current supply chain environment, and they're likely to persist. As cost reductions are not always easy to achieve, many companies are instead focusing on cost containment in parts of their supply chains where they have strong control.

That doesn't mean there aren't efficiencies you may be overlooking. Intercompany movements, for example, are often rife with inefficiency or seldom get the level of scrutiny they deserve. If parts and finished goods are shipped intercompany, ask why: Is there a value add, is it because your business has always done it that way, or is it an enabling factor to hedge against process inefficiencies? If your global supply chain is failing to consistently meet the needs of local markets, does the original rationale for keeping production and sources of supply at a distance still stand, or would it be beneficial to establish a near or local market capability? The use of a contract manufacturer model can be a quicker way to further evaluate whether it makes sense to establish an in-house capability.

It's also a good time to revisit lean initiatives that you may have previously dismissed or deprioritized — though be cautious of prioritizing efficiency at the expense of resilience. And beyond your own four walls, there are a few foundational measures of good supply chain hygiene that may help with cost takeout:

- Shift from transportation spot rates to contract rates to stabilize pricing.
- Ensure you have contracts with alternate suppliers; don't rely on a single source.
- Encourage your customers to optimize order volume for full truck or container loads through more rigorous enforcement of transactional service standards.

These measures may help manage costs to some degree but are unlikely to completely offset them. Instead of passing additional costs onto all your customers, consider segmenting them (we like the 80-20 method) and developing pricing strategies based on level of priority. You may not want to raise prices for your most critical customers, but there is little downside to increasing rates for your lowest-priority customers.

Where to focus now:
Analyze your customer base and product suite to understand the most profitable and least profitable segments. Consider implementing a price segmentation strategy that shifts the heaviest burden of cost increases to your least profitable (and least desirable) customers. Also take a close look at your least profitable product segments and how they line up with cost distribution. Do you have slow-moving SKUs driving a disproportionate amount of costs? It may make sense to rationalize them.