

Operations Practice

# Excellence in Supply Chain Management



# Foreword

As the global business landscape continues to evolve, so do its challenges. New competitors are entering the market. Product life cycles are getting shorter. Customers are more demanding, and their expectations now extend beyond cost and service to include ethical, environmental, and sustainability concerns. This complex and fast-changing environment puts new demands on supply chains, as companies seek ways not just to manage the change, but also to use their supply chains as a source of competitive advantage. Those that succeed are thinking far beyond their organizational boundaries. They are optimizing their supply chains from end to end, and are finding new ways to collaborate with both suppliers and customers.

No longer can companies afford to focus only on their established markets. The consuming class in emerging markets is expected to grow from 2.4 billion people to 4.2 billion between 2010 and 2025, resulting in a 150 percent increase in consumption to \$18 trillion. Building efficient and effective supply chains to compete in these markets will be critical for any player looking to win the global game. Global supply chains are inherently risky, however, and managing risk and volatility in the supply chain has become an everyday necessity. Our analysis suggests that dramatically improved agility will be the next key driver for logistics and network design.

McKinsey & Company's mission is to be a thought partner to senior leaders around the globe and to help them solve their most difficult and important challenges. By continually bringing the latest research to our clients and maintaining a top management perspective, we have become the leading advisor on supply-chain-related topics to companies around the globe. Our fundamental belief is that supply chain strategy must support an organization's overarching corporate strategy, and that improvements in the end-to-end supply chain can help generate value and bottom-line impact.

We hope that the articles we have selected for this compendium will provide food for thought as you seek to evolve your own supply chain to enhance competitive advantage and accelerate your journey to global excellence. We welcome the opportunity to discuss these and other relevant topics as you move forward.

Best regards,

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Principal



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# Supply chain as a source of competitive advantage



# Supply chain management on the CEO agenda

Christoph Glatzel and Johannes Röhren

*“In this battle for customers, our supply chain and distribution network gives us a key advantage.”*

– Meg Whitman, CEO of HP

In recent decades, companies in sectors from automotive and high tech to retail and consumer packaged goods (CPG) have come to realize that their supply chain is much more than the cost of getting products into customers' hands. These companies understand that it is the supply chain that translates corporate strategy into day-to-day interactions both within and beyond the organization. Ultimately, it is the supply chain that satisfies or disappoints their customers. These companies also use a broader definition of the supply chain, including planning, information sharing, and value-adding activities, from raw material to final distribution, rather than just logistics.

Leading companies have made strategic investments in their supply chain capabilities and set up efficient and effective organizations that overcome cross-functional silos. By outperforming the overall level of maturity in their sectors, they have been able to disrupt them, as Amazon has done in retail, for example. These companies have redefined their customers' expectations of service and their ability to bring innovation to the market, turning their excellence in supply chain execution into a powerful source of competitive advantage.

Critically, the very best companies continue to evolve and reinvent their supply chains, even if they have already achieved a leading position in their industry. By doing so, they are able to manage risks, respond to changes in the economic, technological, and competitive environment and exploit new opportunities more effectively than their competitors.

## Supply chain as CEO priority

In a recent survey, leading global CEOs indicated that the supply chain is the topic

that has risen most in their attention over the last years. Supply chain excellence is getting harder, however. Production and distribution networks are increasingly complex and global, and their effective operation is vital for profitability and resilience. At the same time, risks across the supply chain have increased, and improved transparency is critical to the coordination of effective responses. Making those supply chains work at their best requires tight cross-functional coordination and the right decisions and trade-offs across the organization. More importantly, however, the right supply chain capabilities are playing a critical role in allowing companies to exploit emerging opportunities to boost growth and improve profitability.

Three examples illustrate the difference supply chain excellence can make:

One leading CPG company uses its supply chain to manage input price volatility. It has created multiple recipes and supply chains for a core brand of cleaning products. Depending on the current prices of ingredients, it switches between these recipes and supply chains, allowing it to hedge against increasingly volatile raw material prices.

A major cosmetics company has created a dedicated high-speed supply chain for new products. This supply chain, incentivized only on time to market and product launch excellence, allows it to get the latest trends into the hands of consumers before its competitors, while its “conventional” supply chain segment controls costs for products with steadier demand.

Or take the fast-growing online retail market that is transforming consumer expectations of delivery time and product availability. In China, the online retail market for consumer electronics provides an example. Companies such as Suning and Gome, the two leading players, deliver to consumers in the larger cities within two or three hours. Such speed has become

a competitive necessity, since consumers increasingly order the same item at several retailers, take the one that is delivered first, and reject the later arrivals.

### *Three powerful interventions*

If these examples demonstrate anything, it is the variety of ways that supply chain execution can drive business performance. In our work helping companies to transform their supply chain performance, however, we have identified three specific actions that senior leaders can take to maximize the potential of their own organizations' supply chains.

#### **1. Differentiate your supply chain and corporate strategies**

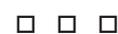
Whether the strategy of your business is superior service, product innovation, or cost leadership, ensure your supply chain is helping to deliver the key points of that strategy. Bring together leaders from across your business to define the supply chain that will work for you—and ensure they provide the data your organization needs to deliver. Marketing needs to tell you what your customers value most from your service, how those needs vary between customers, and what will differentiate you from your competitors. Your commercial functions have to identify which customers justify the cost of the highest service and which would be better served using a more standardized approach. Together, your supply chain and product development functions can find ways to create innovative products that suit the needs of all those different customer groups, while keeping overall costs under control.

#### **2. Create a modern, end-to-end supply chain organization**

The times of managing the supply chain in separated tiers is over. Sophisticated data analysis enables companies to manage supply chains end to end and, in industries like retail, almost in real time. Appoint a single leader with responsibility for end-to-end performance and for delivering improvement projects across tiers and traditional functions such as marketing, manufacturing, and procurement. Make sure your supply chain organization combines operational excellence with strong analytical capabilities and data-driven, cross-functional decision making. Create analytical teams to support decision making and to identify hidden risks and opportunities in unstructured data. Ensure your IT function is supporting them with nimble applications and platforms that enable collaboration and analytical decision making.

#### **3. Set the performance standards for the entire organization**

Incentivize your supply chain organization to work in ways that deliver the most value for your business, while protecting against its biggest risks. That means using more than the traditional metrics of cost, service, and capital. The right KPIs depend strongly on the needs of the business, the product, and the market segment: cost of production for value players; stability of supply for staples and critical products like spare parts or medical devices; agility in volatile markets with fluctuating demand; or launch excellence for new products are key. If a metric doesn't matter in your business, don't misdirect the organization by using it.



The best companies have transformed their supply chains with time, investment, and sustained top management attention.

What are you doing to turn your supply chain into a powerful source of competitive advantage?

### Questions a CEO should ask about the supply chain

Check your current understanding of your organization's supply chain needs and capabilities. Can you answer these questions?

- What is your customers' experience of your supply chain? How does it stand out from your competitors?
- What is your supply chain strategy, and how does it support your business strategy? For which customers, products, and segments does your supply chain target the best performance? Where does it optimize for cost rather than for service?
- Do you have clear supply chain performance and cost targets? Which KPIs do you use to measure these?
- Who is ultimately responsible to deliver against these performance targets? How do you ensure every function in your business supports those efforts?
- How quickly can you ramp up production of a new product or a new sales region? Is your supply chain agile enough to flexibly respond to external changes?

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