

# FROM COST TO ADVANTAGE

**Carter McNabb** looks at the evolution of supply chains, from cost centre to competitive advantage.

**O**VER THE LAST ten years in Australia, supply chain management has started to transition from the back office to the boardroom. Historically seen as a 'necessary evil' or simply part of the 'cost of doing business', supply chain was the realm of trucks, warehouses and burly men in fluorescent safety vests.

But this is changing and changing fast. Leading organisations have recognised that effective supply chain management can boost performance ratios such as return on capital employed (ROCE) by reducing operating costs, increasing asset turnover and improving customer service levels.

And this is not just the realm of familiar global examples like Dell Computer. Some local examples include the automobile parts supplier Super Cheap Auto Group and vitamins and health supplements manufacturer Blackmores.

Super Cheap Auto improved operating cash flow by \$12 million in 12 months while improving service levels by adopting leading demand planning techniques, optimising its inventories and up-skilling its planning team. The company funded growth from operating cash flow versus debt and outperformed the industry during a retail downturn. Its share price then tripled 12 months after its FY06 results were announced. As a notable point of comparison, competitor Repco was acquired by private equity and delisted from the ASX during this period.

Blackmores used its supply chain disciplines to respond swiftly and capably to the Pan Pharmaceutical recall in April 2003. It quickly locked in supply contracts, serviced key customers and increased its market share sustainably when the rest of the industry was in disarray and still trying to formulate a response.

Both examples show how effective supply

chain management can be a key competitive advantage and rapidly deliver market leading results. And these are real results.

A couple of quick facts to underscore the point. Looking at supply chain costs as a percentage of sales, did you know that 'best-in-class' performers have roughly half the costs of 'average-in-class' performers? In other words, if you're an average performer, your supply chain costs are likely twice that of the best performers. Given today's margin pressures, that's a big difference. Do you know where your organisation sits on this spectrum?

In addition, best-in-class performers have higher asset turnover because inventories are lower, often by 20-40 per cent comparatively, while customer response times are faster. In a climate of tight credit and higher capital costs, those that can generate superior cash flows and ROCE will outperform.

The view of supply chain management is shifting from a cost-driven logistics function to an end-to-end process discipline that can deliver real competitive advantages and shareholder value.

And the pressure to improve these competencies is building, because this is what the road ahead looks like:

- **Technology** – Recent advances in supply chain planning, optimisation and execution technology are remarkable. By their nature, supply chains are complex and data intensive. As a result, smart tools for supply chain design, planning and optimisation, and execution are essential. Leading organisations are employing these tools to drive sustainable cost, capital and service advantages in their business. If you are relying on spreadsheets, your ERP system or the knowledge of a few key individuals, there is significant risk and opportunity on the table.
- **Skills** – As supply chain becomes more

strategic and avails itself of these technologies, specialist skills become more important, and the market for these skills becomes more competitive. Bottom line is that it's very hard to find people in Australia with the right combination of skills. In addition, management often don't really understand the supply chain skill sets they're looking for. Organisations must identify, acquire and develop the right skills if they're to stay ahead of the curve ... or even on it.

- **The economy** – Tight credit markets, higher capital costs, a potential economic downturn, margin calls and locusts. As illustrated previously, supply chain management can have a major and rapid impact on cash flow, costs and responsiveness to change (for better or for worse). Both Super Cheap Auto and Blackmores converted disasters into successes because they understood this and had invested in the capability to respond.
- **Al Gore** – Whether you believe in climate change or not, we can all agree that energy costs are rising. We have the long, complex and global supply chains that currently exist because of cheap fuel and transportation costs. As these costs increase, and as carbon costs are factored into our decision making, supply chains will need to adapt. These changes may be very significant (eg where products are manufactured), and we may feel the impacts of this much sooner than we think.

In summary, supply chain management represents a genuine opportunity, but the landscape is changing quickly. It's an exciting time, but excitement can turn to panic rapidly if we find ourselves unprepared. ★

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