

Supply Chain Solutions

Grant Thornton Consumer and Industrial Products practice Part 1 of 3

International sourcing: Offshore or near shore?



Executive summary

International sourcing is far from a new concept in the manufacturing world. Many large U.S. companies have been outsourcing to various international locations, including China, India, Mexico and other countries, for well over a decade. According to Grant Thornton's new survey, conducted in partnership with *World Trade* magazine, more than three-quarters of major U.S. companies (77%) are sourcing internationally in order to take advantage of benefits including reduced costs and increased production capacity.

The new Grant Thornton/*World Trade* survey points to a number of interesting trends in sourcing decisions. Most notably, a substantial number of those surveyed recently have made changes or have plans in the near future to bring sourcing closer to home. Even though a growing portion of respondents are spending more of their respective supply chain budgets on international sourcing, issues such as volatile fuel prices, concerns about supply reliability and shrinking product demand are leading many companies to rethink just how far afield they wish to cast their supply chain's net.

Regardless of where they are sourcing, there is a growing awareness that an effective supply chain requires not just low costs, but also flexibility, responsiveness and adaptability to changing marketplace needs and conditions. As always, cost-per-piece matters. But today there are many more – and more complex – variables entering into supply chain decisions.

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Grant Thornton LLP collaborated with *World Trade* magazine and the Institute of Supply Management on a series of three surveys concerning supply chain solutions. These surveys are intended to provide a snapshot of issues and opportunities in the supply chain industry. We hope this survey, along with targeted recommendations from Grant Thornton's supply chain experts, offers you insights to help you better evaluate your own sourcing decisions.

WorldTrade
MAGAZINE

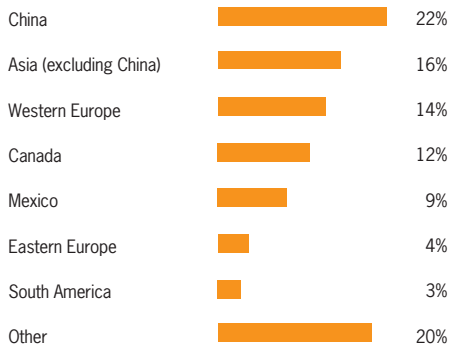
International sourcing: Offshore or near shore? (continued)

Key survey findings

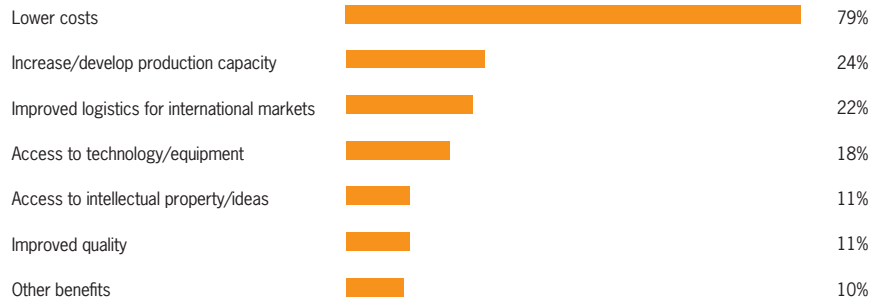
Most source internationally

The vast majority of survey respondents are sourcing internationally. More than three in four companies (77%) report spending at least some of their 2008 supply chain budgets on international sourcing, essentially the same percentage as in 2007 (76%). Among those sourcing internationally, China is the most frequent supplier country (22%), followed by other Asian countries (16%), Western Europe (14%), Canada (12%) and Mexico (9%).

International sourcing countries



Benefits of international sourcing (multiple responses allowed)



A growing proportion of supply chain budgets spent abroad

According to survey findings, more than four in 10 respondents (44%) spend between 1 and 25 percent of their supply chain budget on international sourcing, down slightly from 47 percent in 2007.

Nearly two in 10 survey respondents (19%) spend between 51 and 100 percent of their supply chain budgets internationally. This represents an increase from 2007, when 15 percent spent between 51 and 100 percent of their supply chain budgets internationally. The percentage of respondents who do not source internationally (23%) is nearly the same as last year (24%).

Offshoring: The good and bad

There is a strong consensus regarding the primary benefit of international sourcing: cost savings. The vast majority of respondents (79%) report that they benefit from lower costs. Other reasons for international sourcing include increased production capacity (24%); improved logistics for accessing international markets (22%); access to technology or equipment (18%); access to intellectual property and ideas (11%); and improved quality (11%).

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International sourcing: Offshore or near shore? (continued)

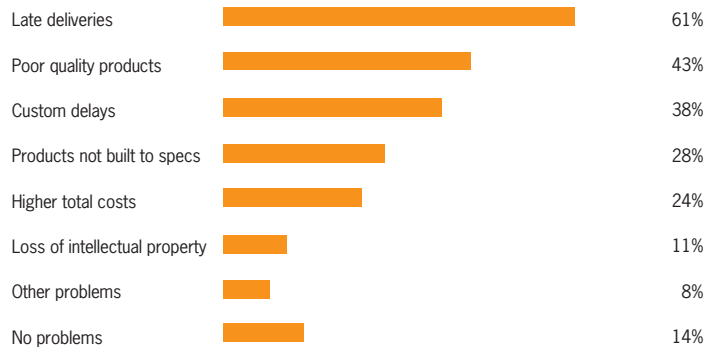
The issues respondents cite as problematic are more varied than the benefits. Although more than six in 10 respondents (61%) indicate the prevailing problem with international sourcing is late product delivery, other frequently cited concerns are poor quality products (43%); customs delays (38%); and products not built to specifications (28%). Nearly one-quarter (24%) complain of higher overall costs. More than one in 10 (11%) note problems with the loss of intellectual property.

Is it profitable? Mixed feelings

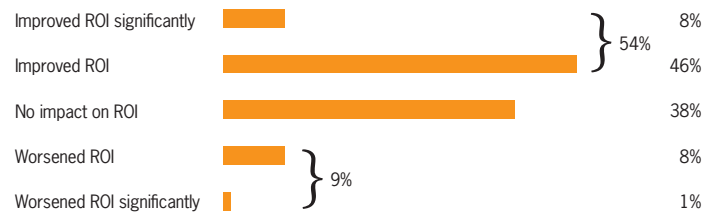
Most respondents report that the return on investment (ROI) from offshoring has been positive. More than half (54%) indicate that international sourcing has increased their ROI. At the same time, nearly four in 10 (38%) say that there has been no impact on ROI due to international sourcing. An additional 9 percent say that international sourcing has worsened their ROI. Considered together, the finding is striking: Nearly half of respondents (47%) see offshoring as neutral or detrimental to their ROI.

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Problems with international sourcing (multiple responses allowed)



Impact on ROI



A one-size solution does not fit all. You need to look at each of your suppliers on a case-by-case basis and determine what makes sense for your company.

International sourcing: Offshore or near shore? (continued)

Sourcing closer to home

Did you bring sourcing closer to the U.S. in the past 12 months?

- Yes 28%
- No 72%



Plans for the future: Moving sourcing closer to home?

While the largest percentage of survey respondents that source internationally relies on China (22%), this trend may be changing. In the coming year, many respondents are considering or actively planning to bring their operations closer to home, relocating sourcing to Mexico, Canada and, in some instances, the U.S. Nearly three in 10 respondents (28%) report that they brought sourcing closer to the U.S. during the past 12 months. More than four in 10 (45%) say they plan to bring sourcing closer to home during the next 12 months.

Do you plan to bring sourcing closer to the U.S. in the next 12 months?

- Yes 45%
- No 55%



Grant Thornton recommendations

Based on the survey findings and our ongoing work helping clients make informed sourcing decisions, Grant Thornton supply chain experts recommend the following:

1. **Look closely at the financial health of your supply base.** “It’s absolutely essential to examine your supply base and make sure it will still be there six months and a year from now,” explains Don Bailey, Grant Thornton Advisory Services principal and regional practice leader. “You want to have as much financial information as possible about your supply base, both domestically and internationally, and you need to be prepared to react to any signs of financial distress.”

According to Bailey, monitoring supplier health means staying in communication with your key vendors to address business issues and ensure you stay in tune with any supply chain risks. By opening the lines of communication, your organization and its vendors can work more effectively during these difficult times. Discuss creative solutions to minimize supply chain costs, while maintaining high-quality service.

Don’t wait until you hear about supplier problems, because by then it may be too late to line up a viable replacement, cautions Bailey. Ensure you have more than one supplier for any product that is critical to your operations. If no alternative sources exist, ask yourself these questions: Are you prepared to offer programs and incentives to maintain the flow of products and services from key suppliers? Should you consider vertically integrating or making an acquisition to ensure your ongoing supply?

2. Monitor the evolving marketplace and respond as quickly as possible to changing opportunities.

Last summer, high fuel and transportation costs were driving many supply decisions. Today, with the substantial drop in demand for products – 40 percent from a year ago – overhead costs are a growing concern. Many companies are consolidating operations, closing factories and laying off employees.

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International sourcing: Offshore or near shore? (continued)

“There is a recognition among supply chain leaders that the market is constantly changing,” says Steve Lyman, Grant Thornton Advisory Services partner. “Companies need to be ready to react to a range of shifting conditions.” For example, when the economy recovers, which it inevitably will, companies will need to position themselves to react quickly to that demand.

“The more nimble the supply chain, the quicker you can react to changes in customer demand – or changes in the supply market. Companies certainly do not want to lose opportunities for sales because of long transit times. The potential advantages of locating manufacturing facilities close to distribution centers, such as shorter, more reliable delivery times and lower shipping costs, are certainly worth factoring in to your decision,” comments Lyman.

3. Consider a broad range of variables – not just per-piece costs.

In making the decision whether to move offshore, bring operations home or maintain the status quo, you need to consider factors beyond labor costs. Moreover, these factors can change frequently.

“You want a supplier who can provide what you need at a high quality, when you need it. Factor in not only cost of goods, but also the cost of late deliveries, the cost of getting the product to distributors and customers, and intellectual property issues, as well as warranty and service costs,” says Lyman.

Making the right decisions requires a sophisticated understanding of many variables, concurs Tim Dumond, principal with Grant Thornton’s Corporate Advisory and Restructuring Services.

“Whereas it used to make sense to build an entire product in China, now decision-makers are looking at the full cost structure and where it makes sense to take advantage of different competencies,” he explains.

“For example, protection of intellectual property can be a concern in China. As a result, a number of companies are using China as a low-cost source for basic technology components and then adding the higher-value elements here in the U.S.,” Dumond notes.

Growing complexity in supply chain decision-making

“A one-size solution does not fit all. You need to look at each of your suppliers on a case-by-case basis and determine what makes sense for your company. At the same time, you’ve got to become more flexible to respond to changes in the market. It’s a completely dynamic process that requires greater expertise and knowledge of all the factors that can affect your global supply chain,” concludes Dumond.

For some companies and under certain conditions, the best way to streamline their supply chains will be to bring sourcing and manufacturing closer to home. For others, this may not be the best decision. At the end of the day, a broad range of factors related to each company’s specific situation will dictate those needs. But every company can benefit from developing a flexible, sophisticated and adaptive supply chain that is poised to take advantage of opportunities as they emerge. •

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About the survey

Grant Thornton partnered with Clear Seas Research, a subsidiary of BNP Media, to produce this original research about current and planned sourcing strategies. A total of 442 responses by readers of *World Trade* magazine and members of the Institute of Supply Management were gathered from Nov. 3 to Dec. 22, 2008.

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About *World Trade* magazine

World Trade Magazine is business-to-business logistics journal delivering news and information to U.S. subscribers active in domestic and international trade. *World Trade* covers every aspect of the global supply chain from the movement of products across the U.S. to the procurement from and delivery to international markets.

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