



# The Challenges and Hidden Costs of Cross-Border Outsourcing and Supply Chain Management in Asia

*Stanford University Lecture Series:  
Cross-Border Partnering in Asia:  
Globalization Challenges for High-Tech Industries*

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please contact:

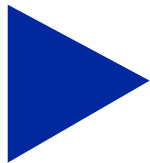
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**November 4, 2004**

**Pittiglio Rabin Todd & McGrath**

# Agenda

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**Background**

2

Outsourcing Survey Overview

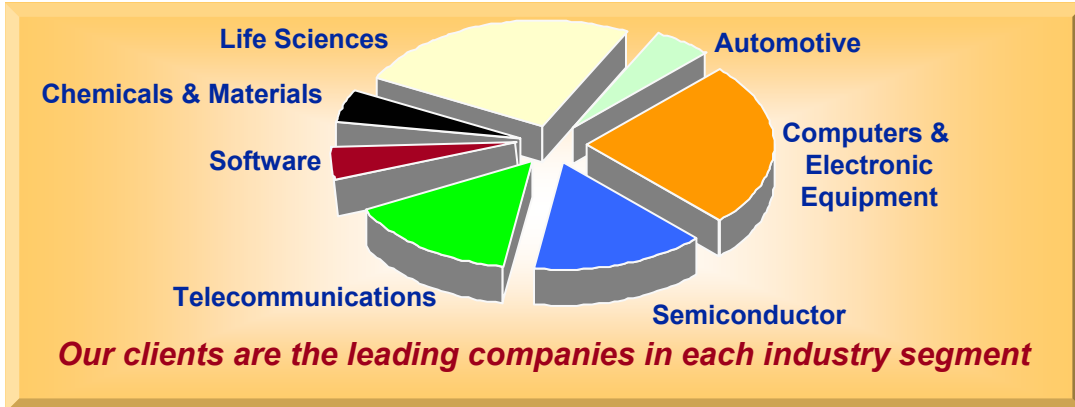
3

Outsourcing Challenges

4

Lessons Learned

# PRTM is a worldwide organization dedicated to achieving results for our clients



## Focus

**PRTM was founded in 1976 with a unique focus**

- Core business processes
- “Results, not reports”
- Technology-driven companies

## Experience

**More than 1,200 satisfied clients**

- Over 6,000 successful implementation projects
- 90% level of repeat business

## Depth

**Industry-savvy staff**

- Technical backgrounds with practical experience and MBAs from top schools
- Low staff/director ratio with significant director involvement in all projects

# PRTM brings expertise to clients both on the end-to-end supply chain and in key areas of operations



## ***Supply Chain Integration***

Supply Chain Strategy—Supply Chain Solution Design and Implementation—Supply Chain Performance Management—Make vs. Buy Analysis—New Product Introduction



## ***Supply Chain Planning***

Demand Planning—Supply Planning—Demand/Supply Balancing—Capacity Planning—Collaborative Planning



## ***Sourcing and Procurement***

Strategic Sourcing—Transaction Management—Supplier Management—Supplier Integration and Collaboration



## ***Manufacturing***

Manufacturing Strategy—Manufacturing Operations—Lean Manufacturing—Outsourcing, Divestiture, and Contract Manufacturing Management—Network Optimisation



## ***Order Fulfilment***

Order Management—Outsourcing and Third-Party/Fourth-Party Logistics Management—Network Optimisation—Warehouse and Transportation Operations

1 Background



2 **Outsourcing Survey Overview**

3 Outsourcing Challenges

4 Lessons Learned

# Data in this presentation are based on a survey conducted by PRTM and *World Trade* magazine

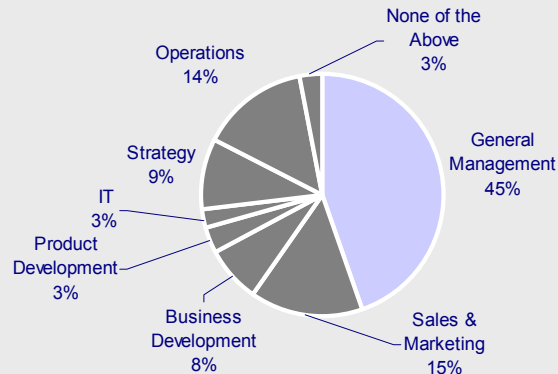
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## Scope:

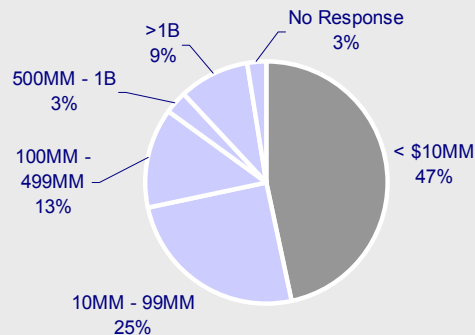
- ◆ Multiple types of offshore outsourcing—Manufacturing, IT, R&D, and Business Process Outsourcing (BPO)
- ◆ Key issues/areas explored included:
  - Reasons for offshore outsourcing
  - Major challenges
  - Satisfaction levels
  - Critical success factors

# Over 150 executives, representing a variety of industries and company sizes, responded

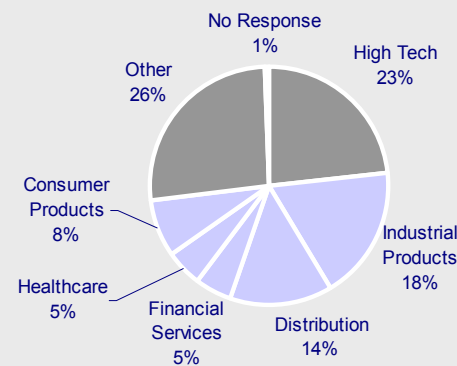
**Most respondents were executives with general management responsibilities**



**Companies of all sizes were represented in the survey population ...**

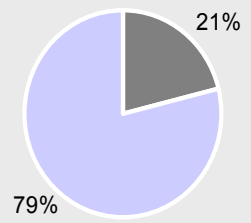


**... and industry representation was diverse**



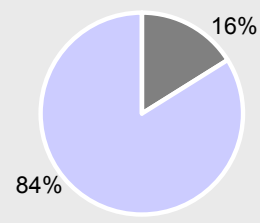
# Offshore outsourcing has entered the mainstream

## Traditional outsourcing is pervasive...



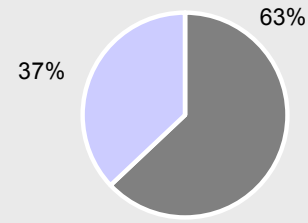
79% of respondents already use some form of outsourcing

## ...and the offshore trend is significant...



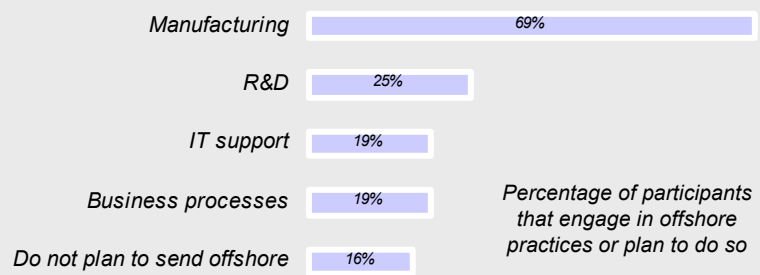
84% see themselves moving to offshore sources in the near term

## ...but companies have a selective approach



Only 37% expect to outsource more than one function offshore in the near term

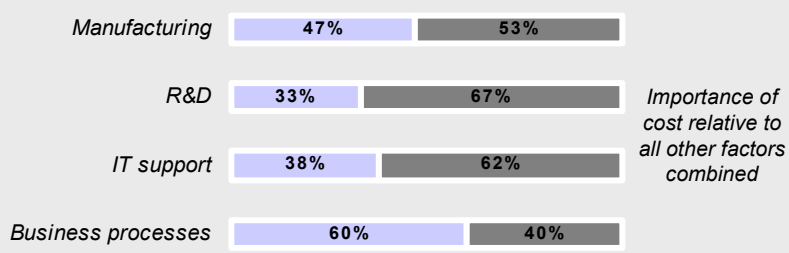
## Companies are readily sending offshore traditional core competencies...



Percentage of participants that engage in offshore practices or plan to do so

Though Manufacturing activity is most common, R&D and Business Processes offshore activities are significant

## ...in search of lower costs



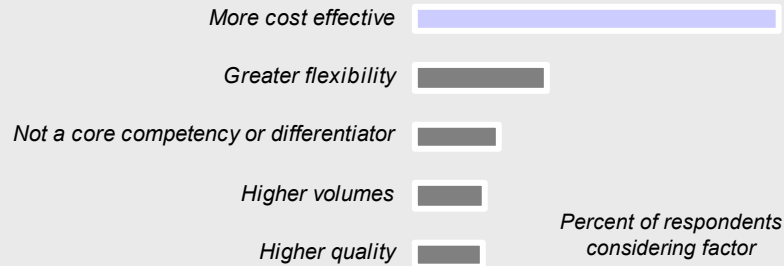
Importance of cost relative to all other factors combined

Although companies say they place importance on competency, service, time-to-market, and flexibility, in reality, **cost** is the primary decision-driver in all offshore decisions



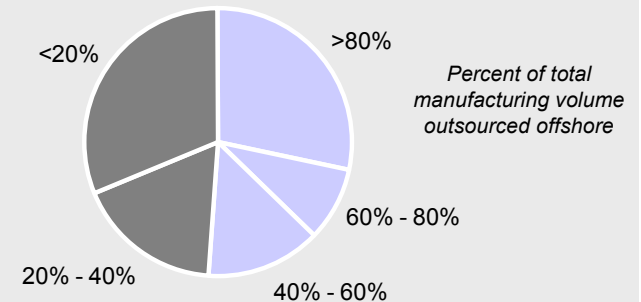
# Outsourcing manufacturing offshore is pervasive, but select, high-value activities remain domestic

As expected, cost is the primary driver in the decision to outsource manufacturing offshore...



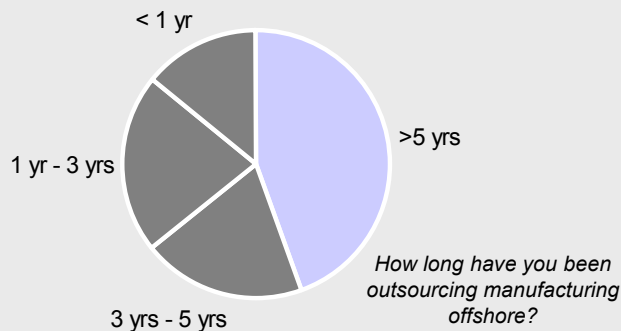
Labor-intensive processes are leading the exodus

...And, it's driven many companies to outsource the majority of their manufacturing activity



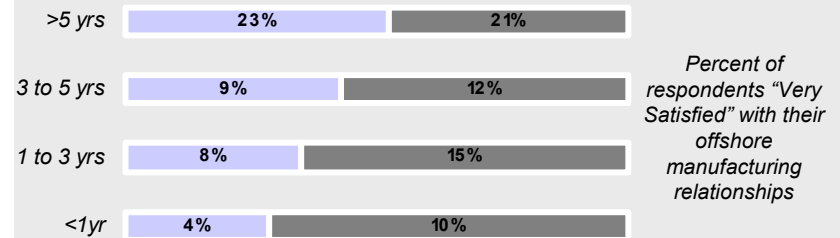
What activity remains may be more accurately called "assembly" or "final integration"

A high number of respondents have multiple years of experience with offshore relationships...



Surprisingly, not all respondents representing large companies were outsourcing offshore

...And experience breeds success



Offshore outsourcing of manufacturing rarely yields instant gratification—it takes work

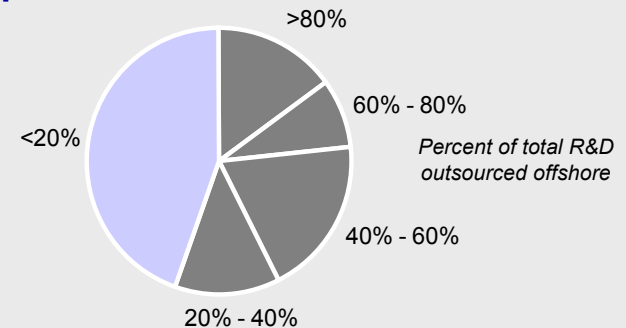
# The majority of R&D remains onshore, although cost and time-to-market are causing an offshore shift

## Cost is also the primary driver in the decision to outsource R&D offshore...



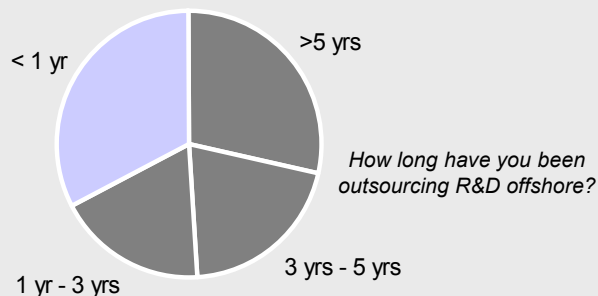
...but time-to-market and resource flexibility are becoming increasingly important criteria

## On average, companies are sending only a small portion of their R&D offshore...



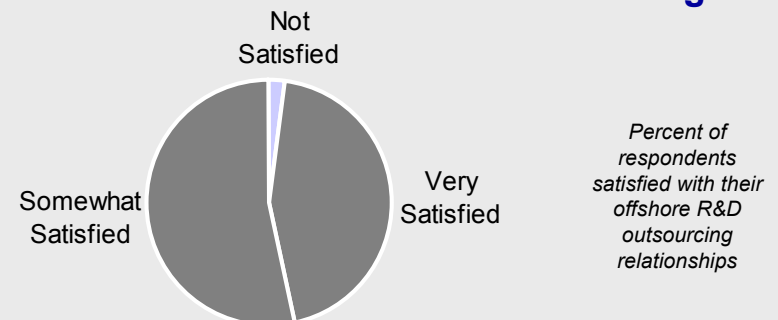
...although smaller companies (<10M in revenue) are sending more than 80% of their R&D offshore

## Most respondents are new to this type of offshore outsourcing...



...although larger companies have extensive experience in this area

## Very few respondents are dissatisfied with the results of R&D offshore outsourcing...



...primarily due to the current limited scope of R&D outsourcing and focused project management

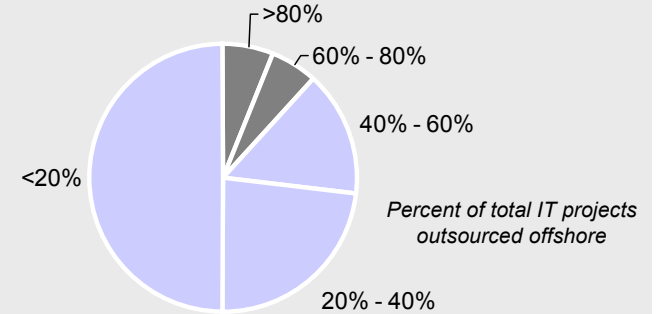
# Following the lead of large companies, medium-size companies are rapidly outsourcing IT offshore

## Cost remains the primary factor driving offshore IT outsourcing decisions...



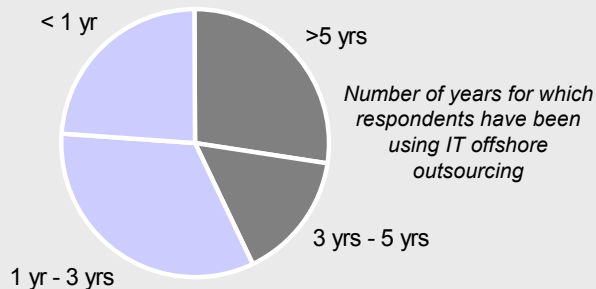
*Greater flexibility of resources and faster time-to-deployment are other key factors*

## ...But, most companies have outsourced less than 20% of their IT projects



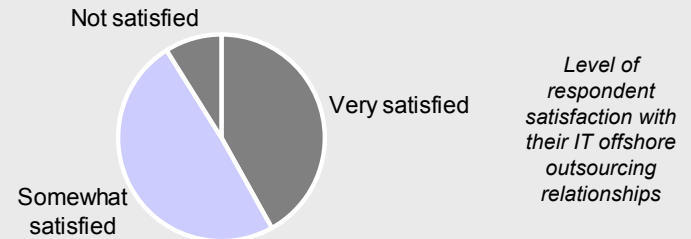
*Companies typically begin with projects related to the maintenance and enhancement of legacy applications*

## Within the last three years, there has been a big push in favor of IT offshore outsourcing...



*The early adopters (> 5 yrs) proved the concept's worth and the other companies are following their lead*

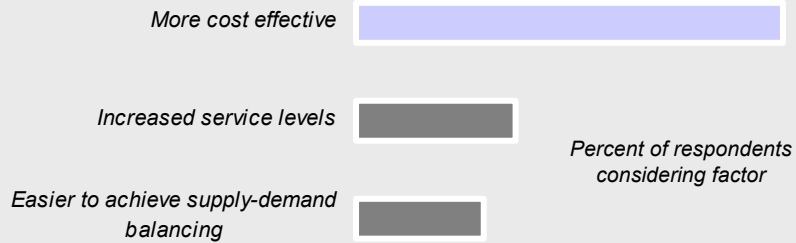
## ...And overall satisfaction runs high, but companies recognize the need for improvement



*Companies have yet to realize the full value of their IT offshore outsourcing relationships*

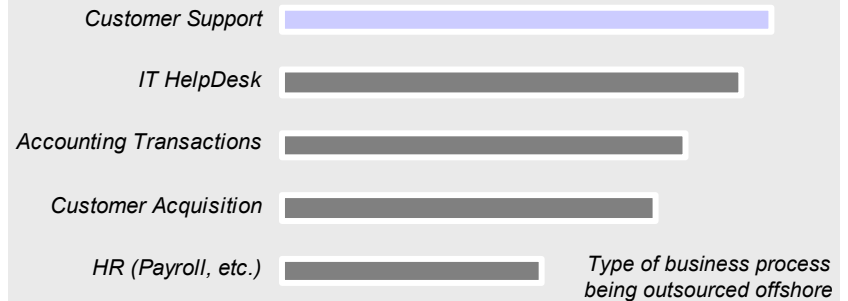
# Offshore Business Process Outsourcing (BPO) is also experiencing an upward trend

## Again, cost reduction is the primary driver ...



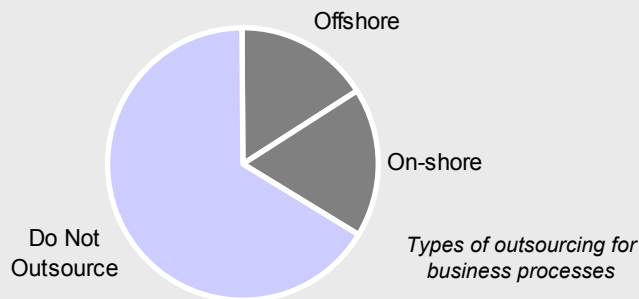
*...and these lower costs often bring improved service levels due to better scale and the ability to specialize the work force*

## Customer Support is the top candidate for outsourcing to an offshore location



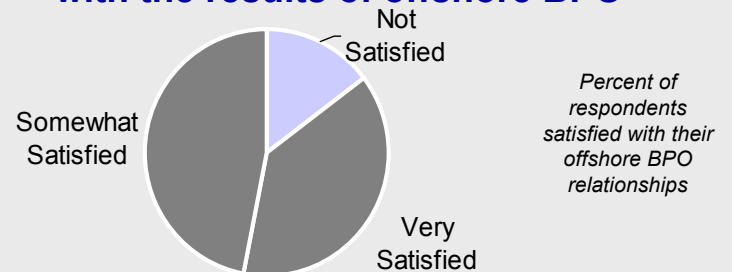
*Sending the IT Help Desk offshore is becoming increasingly common*

## Although most respondents do not outsource business processes...



*...both on-shore and offshore BPOs are already quite common among the larger companies (>1B in revenue)*

## Relative to the other types of offshore outsourcing, respondents are less satisfied with the results of offshore BPO



*Treating BPOs as divestitures rather than mergers often creates the dissatisfaction*

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3 **Outsourcing Challenges**

4 Lessons Learned

# The cost of outsourcing manufacturing and supply chain management to Asia is sometimes underestimated

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A “high-touch” model is required

Better management skills are needed

Suppliers can be hard to find

Labor rates are rising rapidly

# Asian business and cultural norms can be different than those practiced by American companies

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Relationships and reciprocal obligations (“guanxi”) are important

Metrics may be resisted

Intellectual property laws are not consistently enforced

Business practices considered unacceptable in the U.S. are used

# Managing a supply chain 7000 miles away is challenging!

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Complexity increases  
with distance

Multiple time zones  
make problem resolution  
difficult and time  
consuming

Language barriers make  
collaboration, training,  
and troubleshooting  
more difficult

Asian companies are  
developing their own  
supplier networks



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4 **Lessons Learned**

# Lesson 1: Offshore outsourcing is a holistic decision

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## Offshore-related decisions are not point solutions to reduce costs in a functional area

- ◆ Don't allow functional managers to make offshore-related decisions in isolation
- ◆ Have planned offshore transfers—either outsourced or insourced—reviewed by the entire senior team

# Lesson 2: Consider all costs

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## Take all potential costs into account

- ◆ Consider the internal resources and skill sets required to ensure success
- ◆ Also consider the costs of travel, training, system integration and collaboration

## **Lesson 3: If it's broken, don't send it outside**

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**Ensure any process being outsourced is stable and operates at a competitive performance level prior to initiating the transition**

- ◆ Well-defined roles and responsibilities are critical to success

## **Lesson 4: Make sure products are suitable for outsourcing**

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**Products that have complex manufacturing or troubleshooting processes are much more difficult to outsource**

**Ensure that development capabilities will not be hampered by transferring the manufacturing process**

## **Lesson 5: Don't rely on a partner's sales pitch**

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**Visit sites, talk to the managers at those sites, and talk with other customers to ensure you understand the strengths and weaknesses of the partner and the sites**

# Lesson 6: Maintain control over key suppliers and technology

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## Consider and minimize the risk of losing intellectual property

- ◆ Make sure your partner knows that you consider intellectual property protection of critical importance

# Lesson 7: Learn from others

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## Leverage what others have learned and experienced to reduce your own risk and costs

- ◆ Use frameworks and approaches that have proven successful for others



# Lesson 8: Use a structured approach

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We have developed a rapid, yet effective, approach for evaluating and implementing offshore outsourcing



*Relative importance and duration of each step is dependent on project specifics and complexity*

# **Outsource partners in Asia are working hard to resolve issues and strengthen capabilities**

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**Partners are eager to learn and anxious to get into long-term relationships**

**Be patient, and willing to invest the time and effort to teach and train partners**


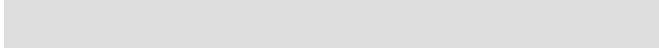
**Asian cultures are generally open to outsiders providing education and training**

**Partners know that being good at supply chain management is a selling point so they are working to improve their expertise in this area**

# Thank you

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Should you wish to discuss this topic  
in more detail, please contact:



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