SWP 36/87 GLOBAL LOGISTICS FOR WORLD MARKETS

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There has been a growing realisation amongst the leaders of the major corporations of the Western World that the name of the game in the late twentieth century is global marketing. Global marketing is as different from international or multi-national marketing as chalk is from cheese. Whereas the emphasis in multi-national marketing has been to tailor products and marketing strategies to meet perceived local needs, the thrust of global marketing is to seek to satisfy common demands worldwide. There has been a belated recognition that, for all the mythology, the customer in Bogota is little different from his counterpart in Birmingham.

Companies like Coca Cola, Philip Morris and McDonalds have long since recognised the power of global marketing. So too have Boeing, Du Pont and Polaroid; but probably the winners by a long way in this high stake game are the Japanese. In product/markets as diverse as electronics, automobiles and earth moving equipment they have demonstrated that there are huge advantages in taking the global approach. Indeed many have argued that it is only by adopting a global perspective that any manufacturing business can survive at all in the long term.

The routes to success through global marketing and the strategic options available are the issues that this paper addresses.

THE SOURCES OF COMPETITIVE ADVANTAGE

Seeking a sustainable and defensible competitive advantage has become the concern of every manager who is alert to the realities of the market place. It is no longer acceptable to assume that good products will sell themselves, neither is it advisable to imagine that success today will carry forward into tomorrow.

Let us consider the bases of success in any competitive context. At its most elemental, commercial success derives either from a cost advantage or a value advantage or, ideally, both. It is as simple as that - the most profitable competitor in any industry sector tends to be the lowest cost producer or the supplier providing a product with the greatest perceived differentiated values. To be successful in the automobile industry, for example, you either have to be a Nissan or a Porsche; if you are an Austin Rover you have problems.

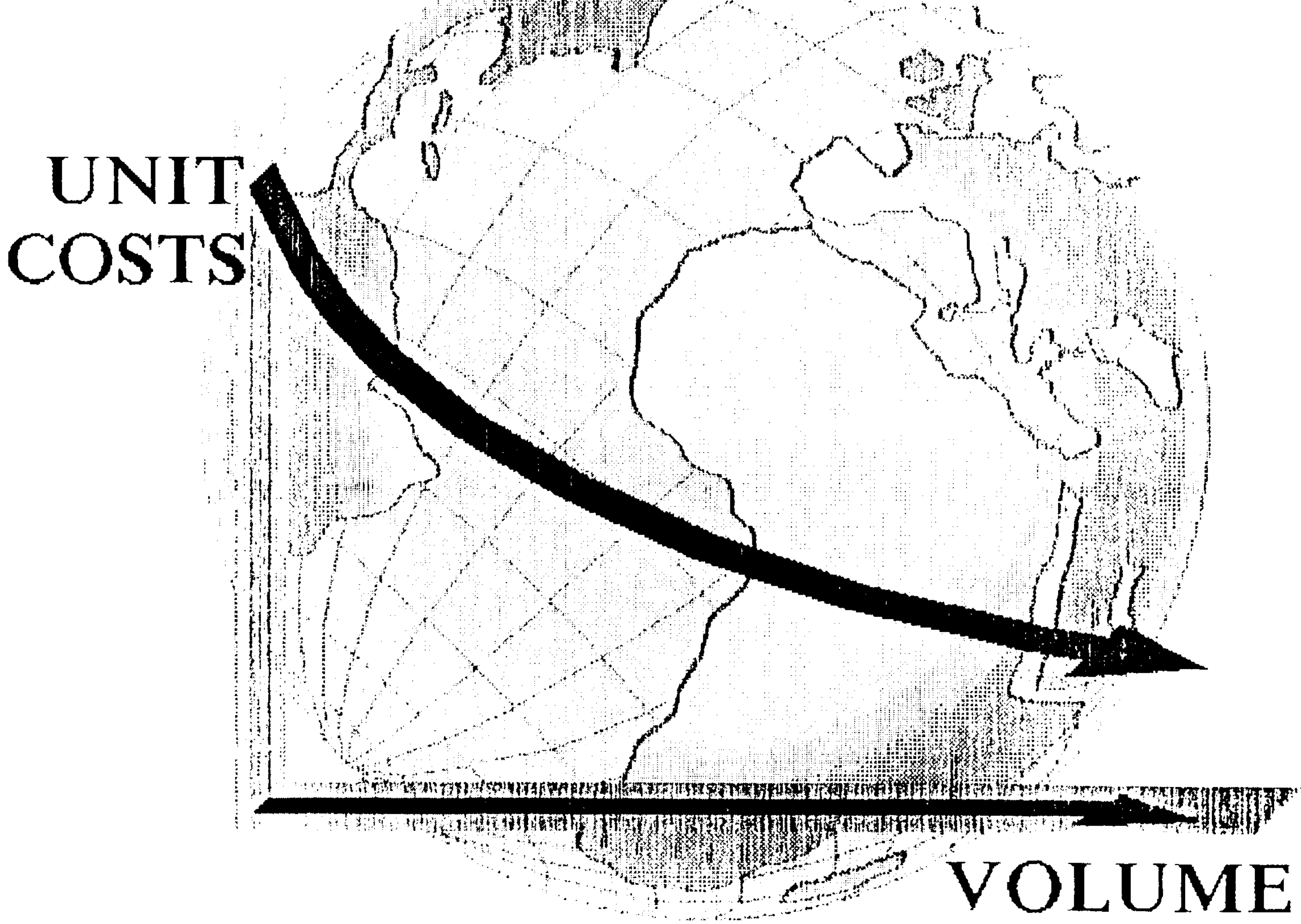
Put very simply, successful companies either have a productivity advantage or they have a 'value' advantage or a combination of the two. The productivity advantage gives a lower cost profile and the value advantage gives the product or offering a differential 'plus' over competitive offerings.

Let us briefly examine these two vectors of strategic direction.

1. Productivity Advantage

In many industries there will typically be one competitor who will be the low cost producer and, more often than not, that competitor will have the greatest sales volume in the sector. There is substantial evidence to suggest that 'big is beautiful' when it comes to cost

THE PRODUCTIVITY ADVANTAGE



advantage. This is partly due to economies of scale which enable fixed costs to be spread over a greater volume but more particularly to the impact of the 'experience curve'.

The experience curve is a phenomenon which has its roots in the earlier notion of the 'learning curve'. Researchers discovered during the last war that it was possible to identify and predict improvements in the rate of output of workers as they became more skilled in the processes and tasks on which they were working. Subsequent work by Bruce Henderson, founder of the Boston Consulting Group, extended this concept by demonstrating that all costs, not just production costs, would decline at a given rate as volume increased. In fact, to be precise, the relationship that the experience curve describes is between real unit costs and cumulative volume. Further it is generally recognised that this cost decline applies only to 'value added' i.e. costs other than bought in supplies.

There are many implications of this relationship for the development of marketing strategy, not least in the determination of pricing strategy. However its importance in this current discussion is in the fact that if one company's relative market share is greater than its competitors' then, other things being equal, it should be further down the experience curve. In other words it will have a cost advantage.

Such a cost advantage can either be used to lower price, thus putting the squeeze on competitors, or higher margins can be earned at the same price as competitors.

2. Value Advantage

It has long been an axiom in marketing that "customers don't buy products, they buy benefits". Put another way the product is purchased not for itself but for the promise of what it will 'deliver'. These benefits may be intangible i.e. they relate not to specific product features but rather to such things as image or reputation. Alternatively the delivered offering may be seen to out-perform its rivals in some functional aspect.

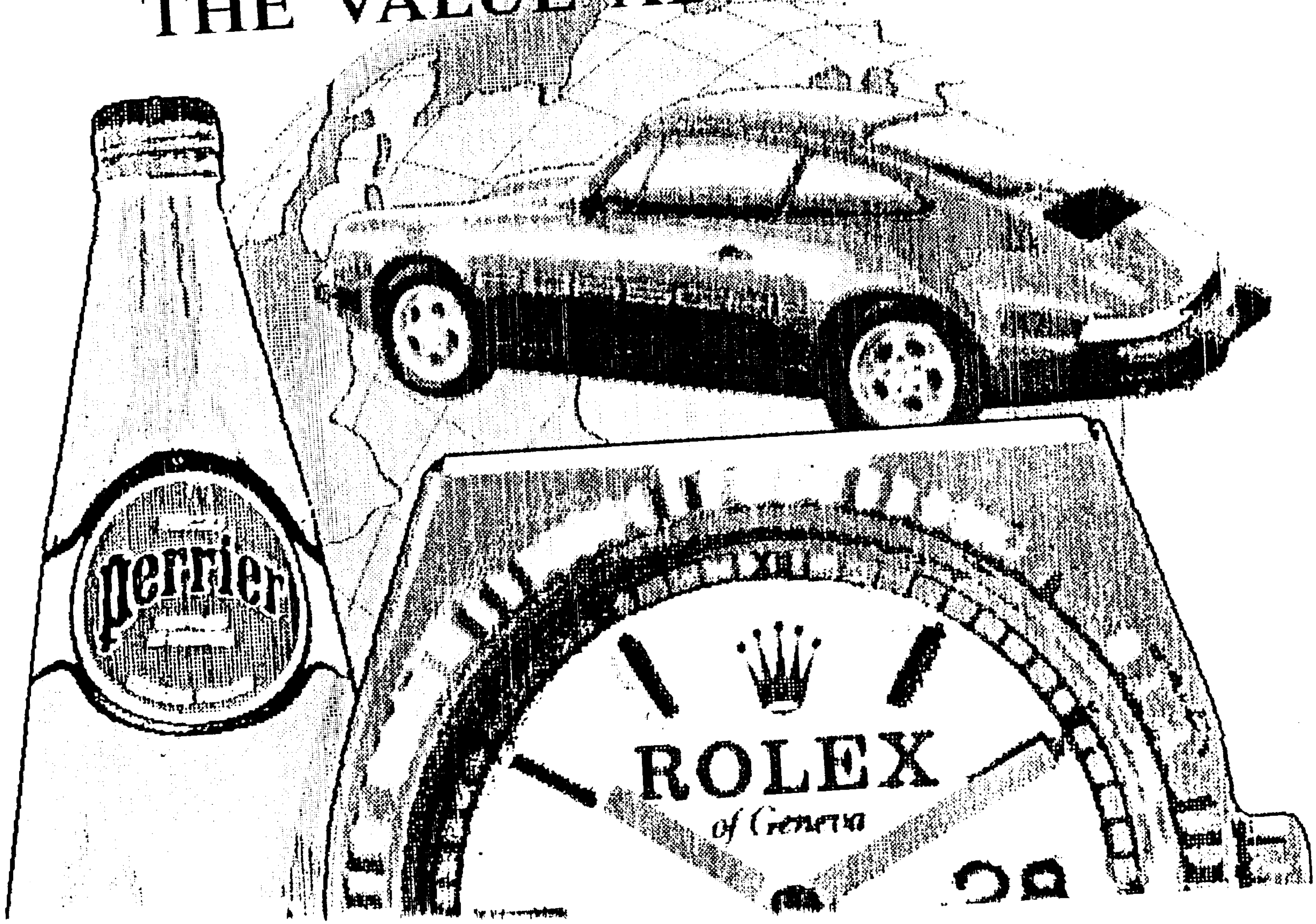
Unless the product or service we offer can be distinguished in some way from its competitors there is a strong likelihood that the market place will view it as a 'commodity' and so the sale will tend to go to the cheapest supplier. Thus the importance of seeking to add additional values to our offering to mark it out from the competition.

What are the means by which such value differentiation may be gained?

Essentially the development of a strategy based upon additional values will normally require a more segmented approach to the market. When a company scrutinises markets closely it frequently finds that there are distinct 'value segments'. In other words different groups of customers within the total market attach different importance to different benefits. The importance of such benefit segmentation lies in the fact that often there are substantial opportunities for creating differentiated appeals for specific segments. Take the motor car as an example. A model such as the Ford Sierra is not only positioned in the middle range of European cars but within that broad category specific versions are aimed at defined segments. Thus we find the basic, small engine, two door model at one end of the spectrum and the four-wheel drive, high performance version at the other extreme. In between are a whole variety of options each of which seeks to satisfy the needs of quite different 'benefit segments'. Adding value through differentiation is a powerful means of achieving a defensible advantage in the market.

Equally powerful as a means of adding value is service. Increasingly we are finding that markets are becoming more service sensitive and this of course poses particular challenges for global marketing. There is a trend in many markets towards a decline in the strength of the

THE VALUE ADVANTAGE



"brand" and a consequent move towards "commodity" market status. Quite simply this means it is becoming progressively more difficult to compete purely on the basis of brand or corporate image. Additionally there is increasingly a convergence of technology within product categories which means that it is no longer possible to compete effectively on the basis of product differences. Thus the need to seek differentiation through means other than technology. A number of companies have responded to this by focussing upon service as a means of gaining a competitive edge. Service in this context relates to the process of developing relationships with customers through the provision of an augmented offer. This augmentation can take many forms including delivery service, after-sales service, financial packages, technical support and so forth.

In practice what we find is that the successful companies will often seek to achieve a position based upon both a productivity advantage and a value advantage. A useful way of examining the available options is to present them as a simple matrix.

VALUE ADVANTAGE		
HIGH	NICHE STRATEGY	COST & VALUE LEADER
LOW	COMMODITY MARKETING	COST LEADERSHIP
	LOW	HIGH

PRODUCTIVITY ADVANTAGE

Let us consider these options in turn.

For companies who find themselves in the bottom left hand corner of our matrix the world is an uncomfortable place. Their products are indistinguishable from their competitors' offerings and they have no cost advantage. These are typical 'commodity' market situations and ultimately the only strategy is either to move to the right on the matrix i.e. to cost leadership or upwards into a 'niche'. Often the cost leadership route is simply not available. This will particularly be the case in a mature market where substantial market share gains are difficult to achieve. New technology may sometimes provide a window of opportunity for cost reduction but in such situations it is often the case that the same technology is available to competitors.

Cost leadership, if it is to form the basis of a viable long term marketing strategy, should essentially be gained early in the market life cycle. This is why market share is considered to be so important in many industries. The 'experience curve' concept, briefly described earlier, demonstrates the value of early market share gains - the higher your share relative to your competitors the lower your costs should be. This cost advantage can be used strategically to assume a position of price leader and, if appropriate, to make it impossible for higher cost competitors to survive. Alternatively, price may be maintained enabling above-average profit to be earned which potentially is available to further develop the position of the product in the market.

The other way out of the 'commodity' quadrant of our matrix is to seek a 'niche' or segment where it is possible to meet the needs of customers through offering additional values. Sometimes it may not be through tangible product features that this value added is generated but also as we have noted opportunities will often exist for adding value through service. For example, a steel stockholder who finds himself in the commodity quadrant may seek to move up to the niche quadrant by offering daily deliveries from stock, by providing additional 'finishing' services for his basic products or by focussing upon the provision of a range of special steels for specific segments.

What does seem to be an established rule is that there is no middle ground between cost leadership and niche marketing. Being caught in the middle i.e. neither a cost leader or a niche-based provider of added values is generally bad news.

Finally, perhaps the most defensible position in the matrix is the top right hand corner. Companies who occupy that position have products that are distinctive in the values they offer and are also cost competitive. Many Japanese products, particularly in consumer markets, argueably have achieved this position. Clearly it is a position of some strength, occupying 'high ground' which is extremely difficult for competitors to attack.

What are the messages of all of this for global marketing?

Firstly it will be apparent that the vast economies of scale that can be provided by the sheer size of global markets means that global companies will win hands down on cost over their locally based rivals.

Secondly the concept of 'niche' marketing should not be seen in some narrow geographical sense. There is a 'niche' for Rolex watches in Norway just as there is in New Zealand.

To secure the greatest position of defensible superiority on a global scale means that markets must be pursued not only because they offer volume but also because they are responsive to differentiation. This need not be a contradiction of terms, witness the success of Sony or Seiko. Many Western companies are also learning this lesson. For example, it is probably not coincidental that ICI's greatly improved profitability has paralleled its concerted focus on international markets for speciality or "effect" chemicals.

CHARACTERISTICS OF GLOBAL COMPETITION

A number of commentators have recently examined the global market place in depth and have reached some important conclusions concerning its characteristics:

(i) **Standardized yet customized**

Firstly, and very much related to our foregoing comments it would seem that products that win in world markets are standardized yet capable of being "customized" where appropriate! Thus products that can be adopted to local regulations or requirements e.g. motor cars and TV sets but yet make use of standarized technology will fare best in a global setting. Similarly when national rules require a proportion of local content in the finished product the same principles of standardized yet customized must apply.

(ii) **Shortening life cycles**

The life of products in the market place is getting shorter. This applies to high technology products perhaps even more than to low technology products. It is now by no means uncommon to see life cycles of less than a year. Computer printers and disk drives provide examples of shortening life cycles but the same is happening in home audio as one technology replaces another and as competition intensifies. At the same time it would appear that the time taken to get the product from the drawing board to the market place has actually lengthened!

(iii) **Out-sourcing and off-shore manufacturing**

There is a marked trend in the United States, and one that is also visable in Western Europe, for an increasing proportion of the content of manufactured goods to be sourced overseas and indeed for their assembly to take place off-shore too. Singer sewing machines take their body shells from the USA, their motors from Brazil, their drive shafts from Italy and the whole thing is put together in Taiwan. The finished product might be bought in Sydney, Australia or Cologne, West Germany.

(iv) **The convergence between marketing and manufacturing strategy**

There was a time when marketing and manufacturing were separate worlds, indeed were not even in the some universe, in most companies. However it is increasingly recognised in the global corporations that these old labels are meaningless, indeed dangerous. To compete successfully in today's marketplace requires total co-operation and co-ordination between marketing and manufacturing. It is no longer possible for manufacturing to work in isolation from the market place and vice versa. The speed with which new products must reach the market place demands a team-based approach. The new technology of manufacturing itself is providing an impetus for this changed approach. The true potential of FMS for example can only be realised if the conduit to the market place is direct and open.

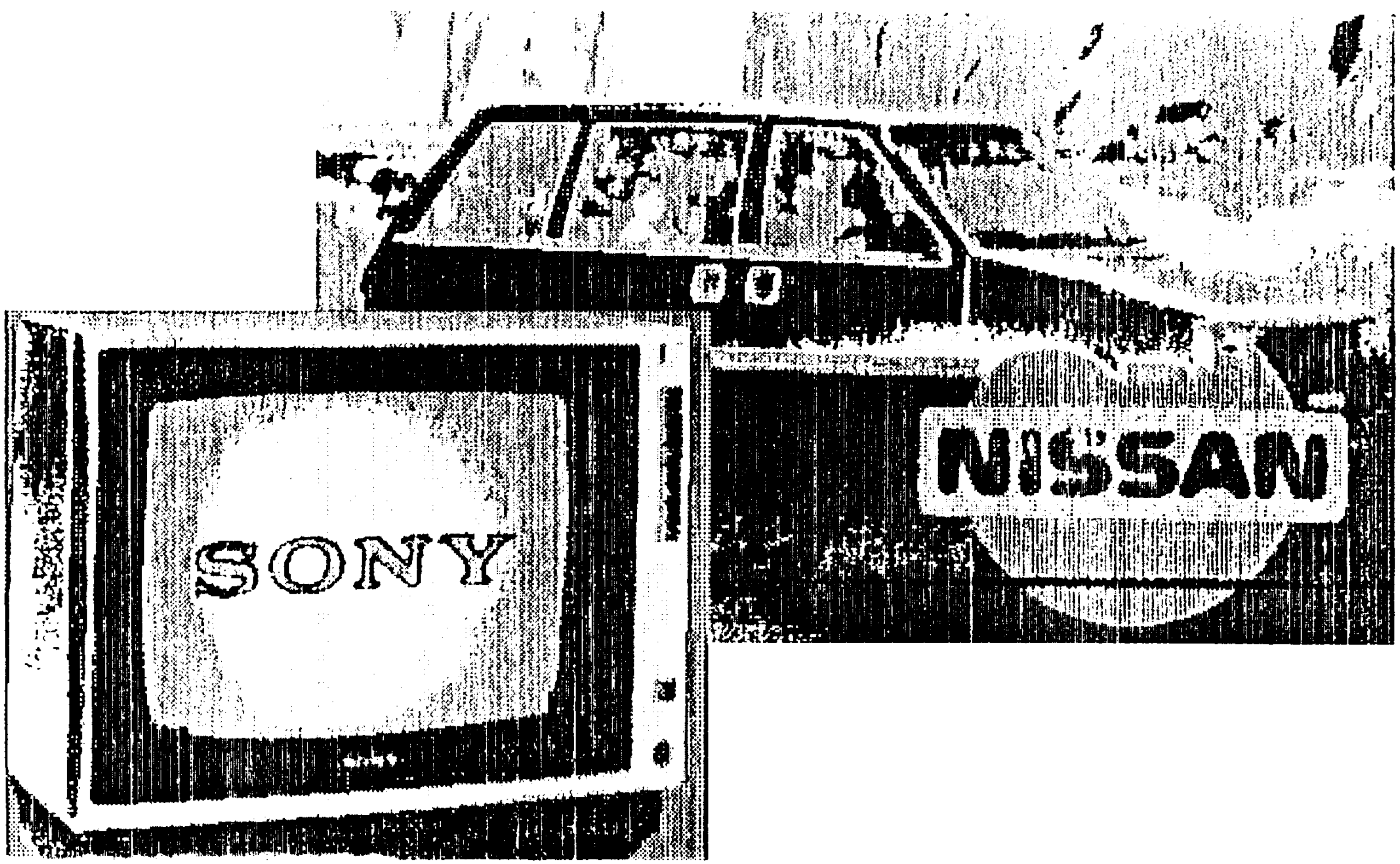
All of these factors have combined to produce an environmental context that is uniquely different for business in just about every industry. What then should be the response?

Clearly there are many requirements to succeed in such a market place, not the least being innovation in technology and marketing, but over-riding all of this is a need for co-ordination. Michael Porter, of Harvard Business School, has summed it up aptly:

> "Co-ordination of complex global networks of company activities is becoming a prime source of competitive advantage. Today's game of global strategy seems to be increasingly a game of co-ordination - getting dispersed production facilities, R&D laboratories and market facilities really to work together".

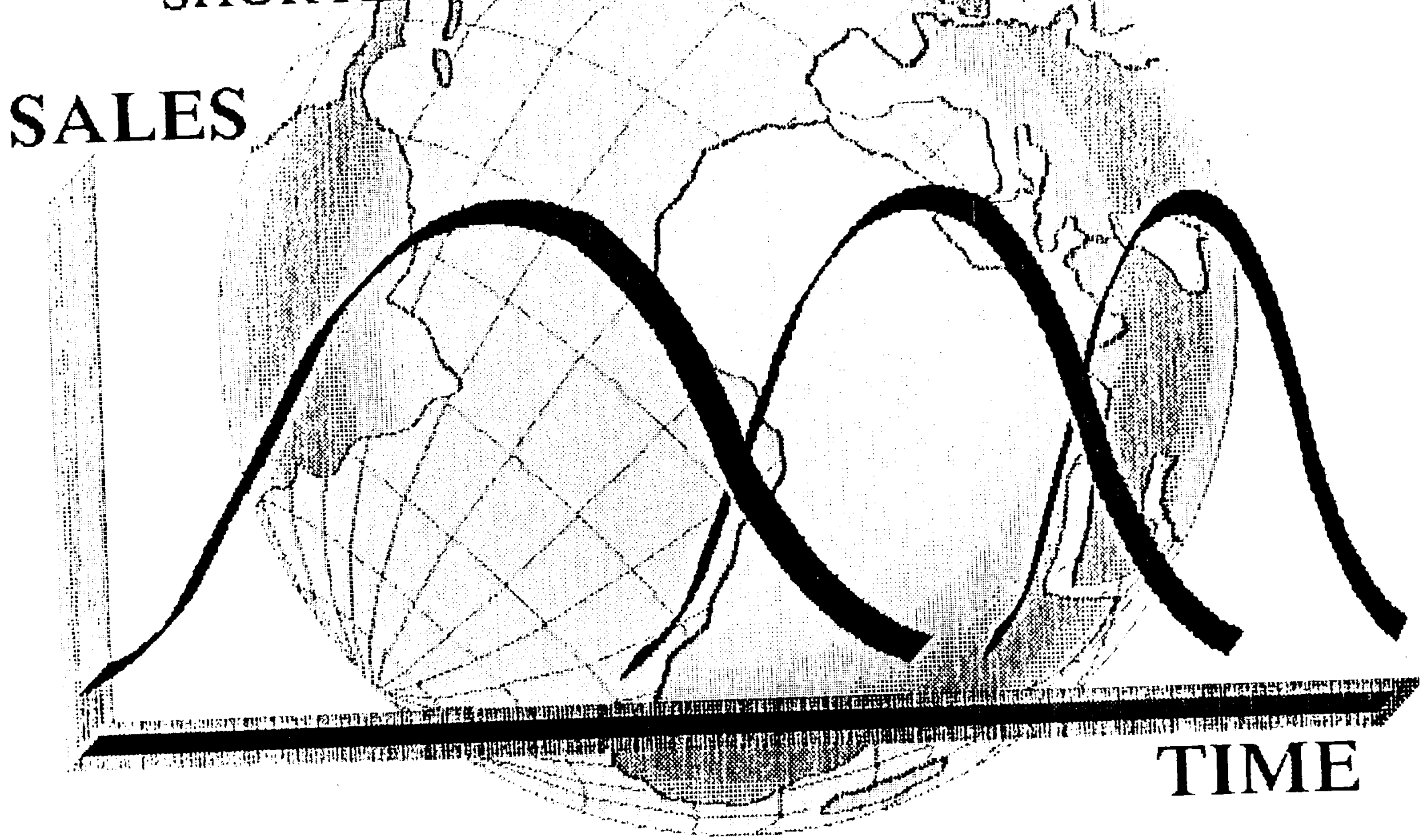
CHARACTERISTICS OF GLOBAL COMPETITION

STANDARDISED YET CUSTOMISED



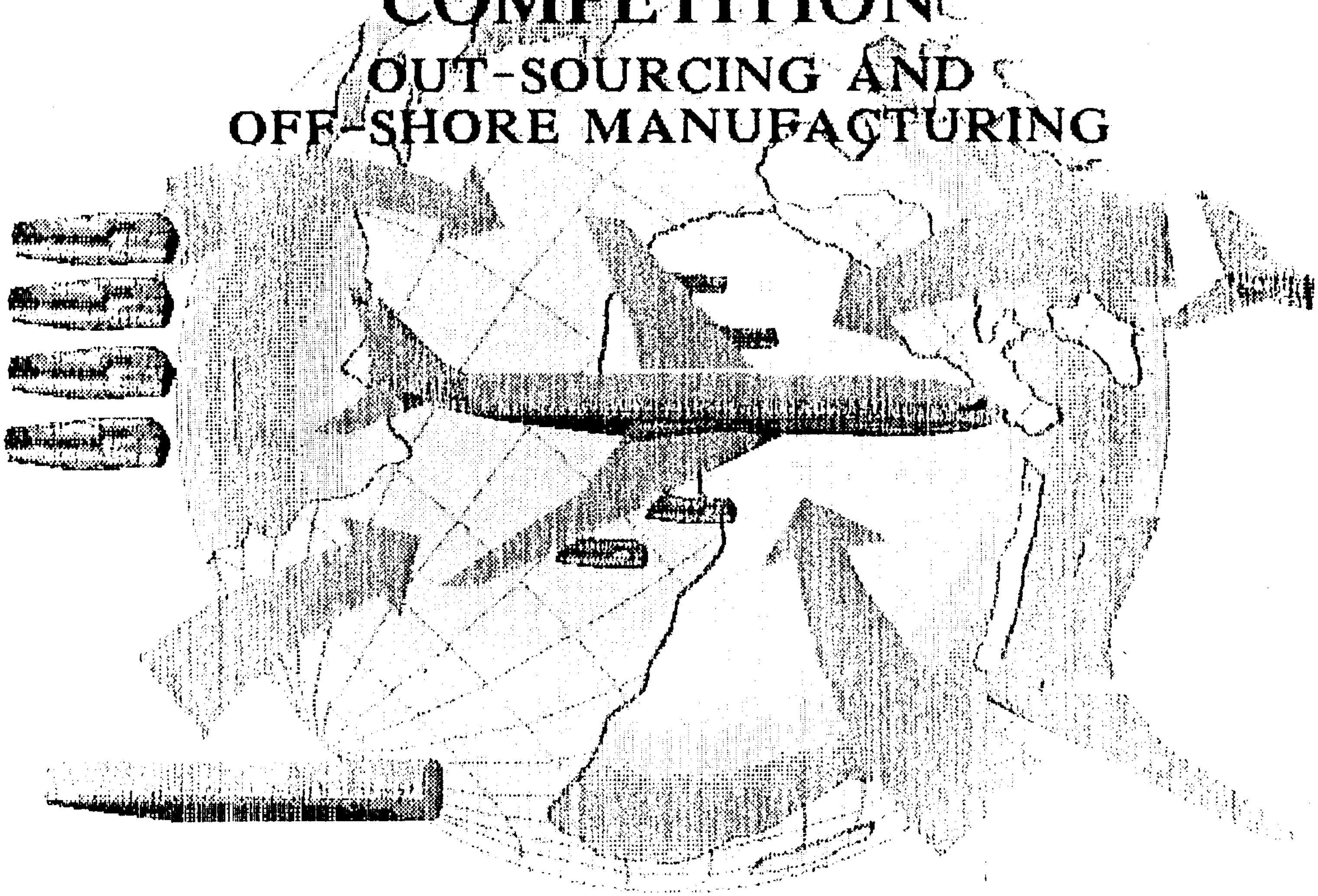
CHARACTERISTICS OF GLOBAL COMPETITION

SHORTENING PRODUCT LIFE CYCLES



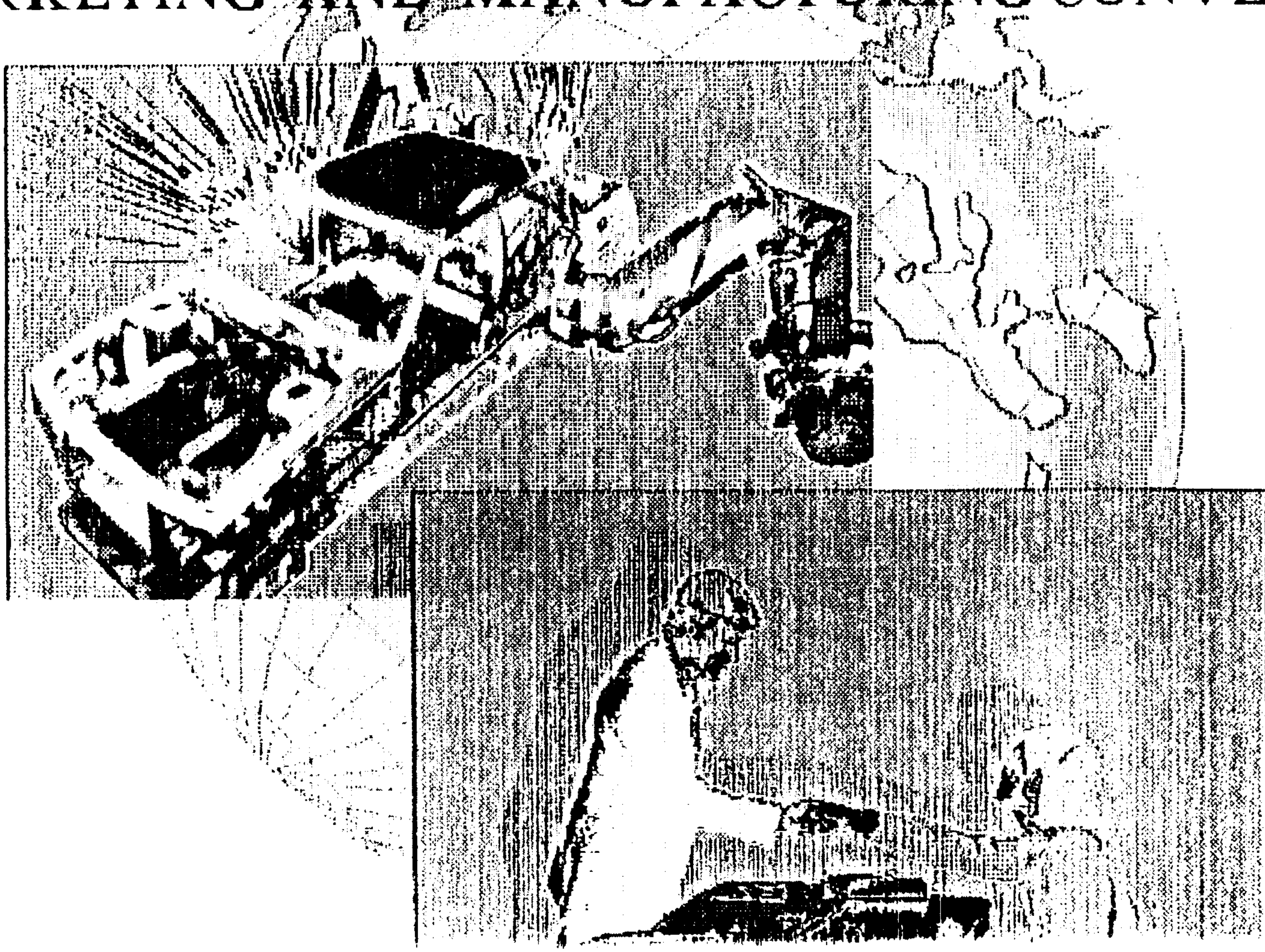
CHARACTERISTICS OF GLOBAL COMPETITION

OUT-SOURCING AND OFF-SHORE MANUFACTURING



CHARACTERISTICS OF GLOBAL COMPETITION

MARKETING AND MANUFACTURING CONVERGE



This need for co-ordination extends from the decisions on sources of supply of raw materials and components, through manufacturing and assembly, to the end user. In essence this is what global competition is all about - the logistics of linking manufacturing to the market place.

THE ROLE OF LOGISTICS MANAGEMENT

One of the most significant trends of the last decade has been the emergence of logistics as an integrative concept spanning the entire supply chain from raw material through to the point of consumption. The underlying philosophy behind the logistics concept is that of planning and co-ordinating the materials flow from source to user as an integrated system rather than, as is so often the case, managing the goods flow as a series of independent activities. Thus under a logistics management regime the goal is to link the market place, the distribution network, the manufacturing process and the procurement activity, in such a way that customers are serviced at higher levels and yet at lower cost. In other words to achieve the goal of competitive advantage through both cost reduction and service enhancement.

Can such a situation really be achieved in practice?

A recent report stated that car industry experts are suggesting that each car made by Nissan's new Tyneside plant will be produced for about £600 less than it costs a British manufacturer to make. The report went on to state that the reason for this Japanese cost advantage is no longer primarily cheaper labour costs but is due to superior logistics management. Nissan will be managing the total material flow, from component source to final car, as an entity. As a result their inventory of materials, work in progress, goods in transit and finished goods will be kept to a minimum; throughput times will be reduced; transport costs will be lower - yet their ability to service the end market will not be diminished.

We have already commented that product life-cycles are getting shorter. What we have witnessed in many markets is the effect of changes in technology and consumer demand combining to produce more volatile markets where a product can be obsolete almost as soon as it reaches the market. There are many current examples of shortening life-cycles but perhaps the personal computer symbolises them all. In this particular case we have seen rapid developments in technology which have firstly created markets where none existed before and then almost as quickly have rendered themselves obsolete as the next generation of product is announced.

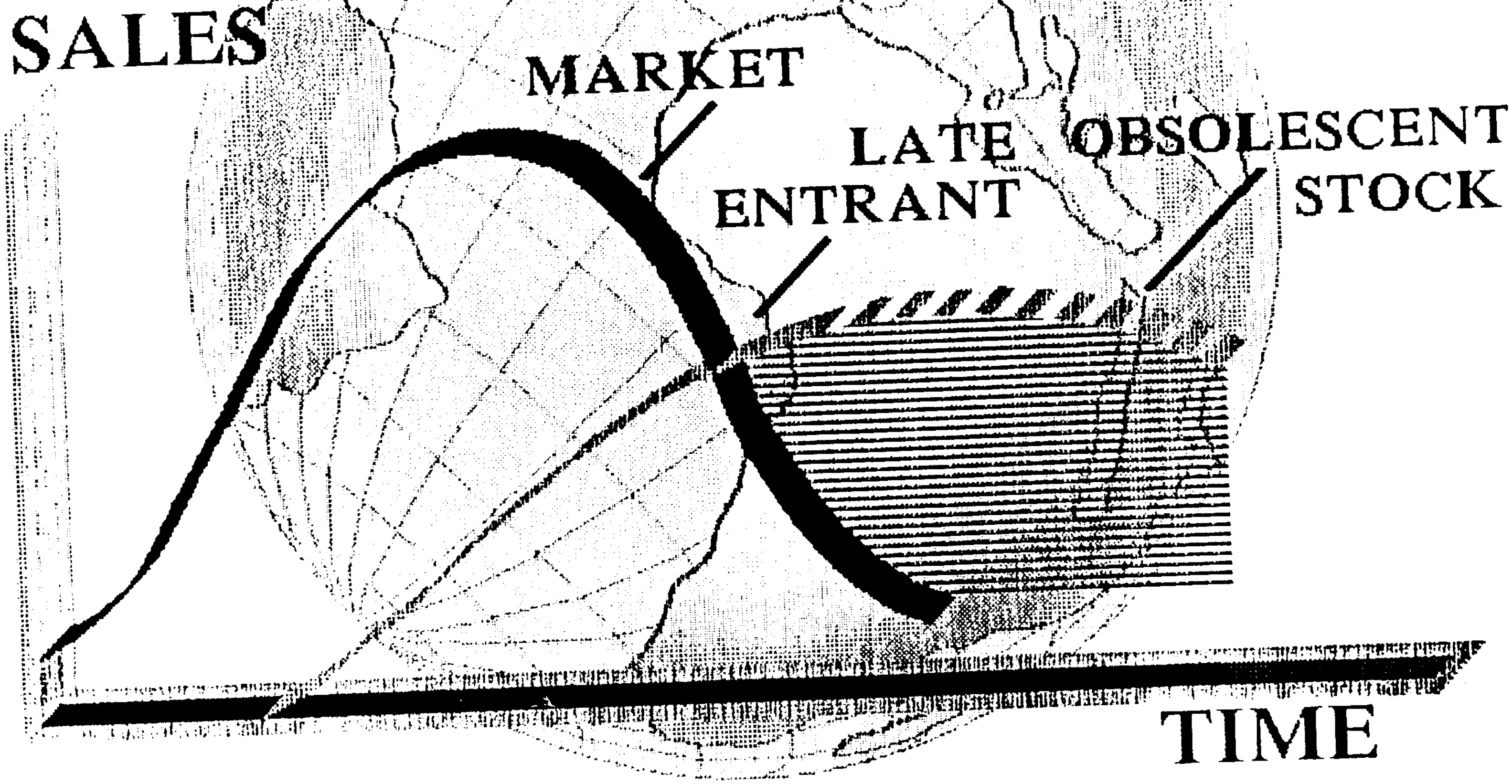
Such shortening life-cycles create substantial problems for global logistics management. In particular shorter life-cycles demand shorter lead-times - indeed our definition of lead-time may well need to change. Lead-times are traditionally defined as the elapsed period from receipt of customer order to delivery. However, in today's global environment there is a wider perspective that needs to be taken. The real lead-time is the time taken from the drawing board, through procurement, manufacture and assembly to the end market. This is the concept of <u>strategic lead-time</u> and the management of this time span is the key to success in managing global operations.

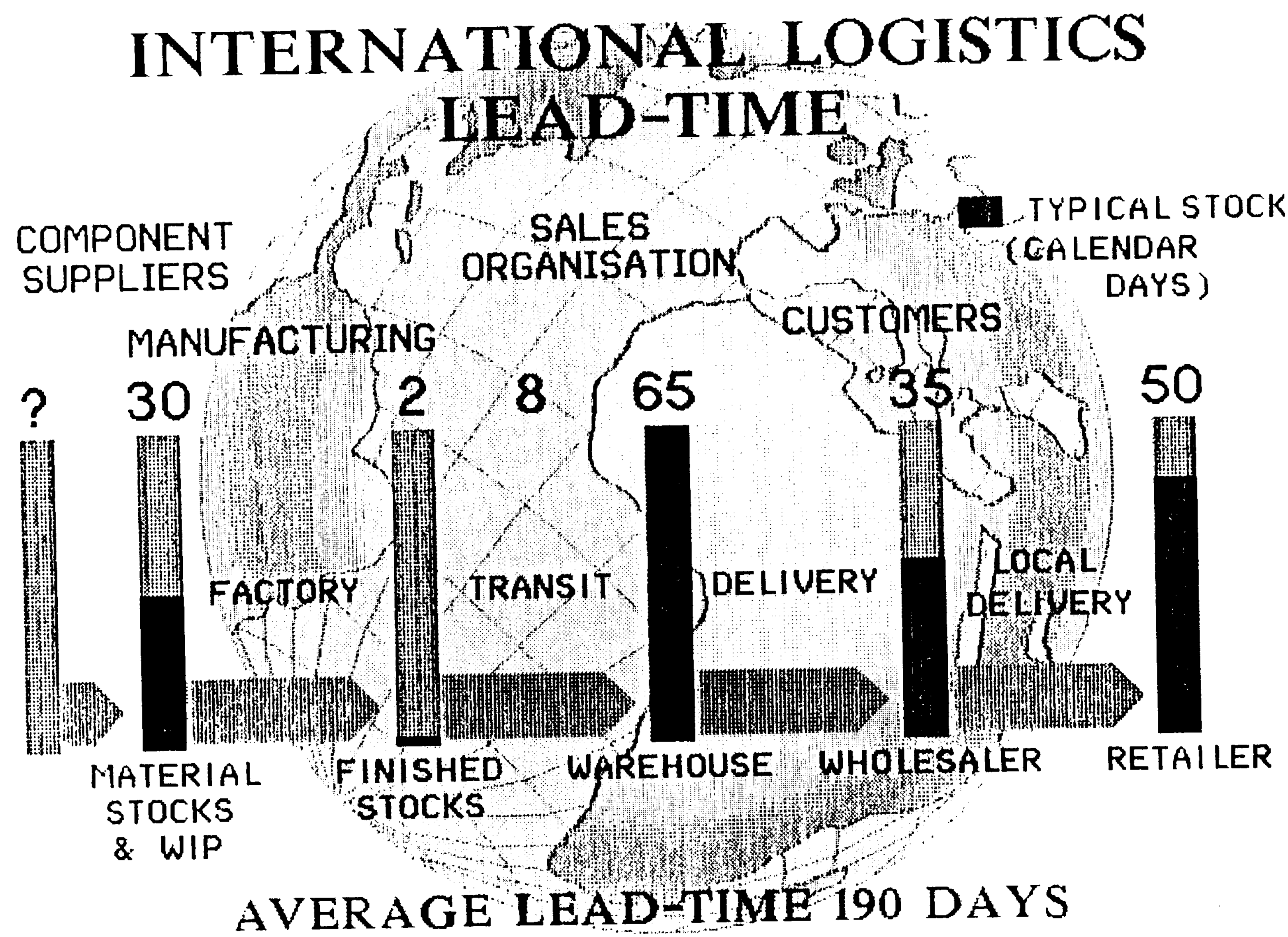
There are already situations arising where the life-cycle is shorter than the strategic lead-time. In other words the life of a product on the market is less than the time it takes to design, procure, manufacture and distribute that same product! The implications of this are considerable both for planning and operations. In a global context the problem is exacerbated by the longer transportation times involved.

Ultimately, therefore, the means of achieving success in such markets is to accelerate movement through the supply chain and to make the entire logistics system far more flexible and thus responsive to these fast-changing markets.

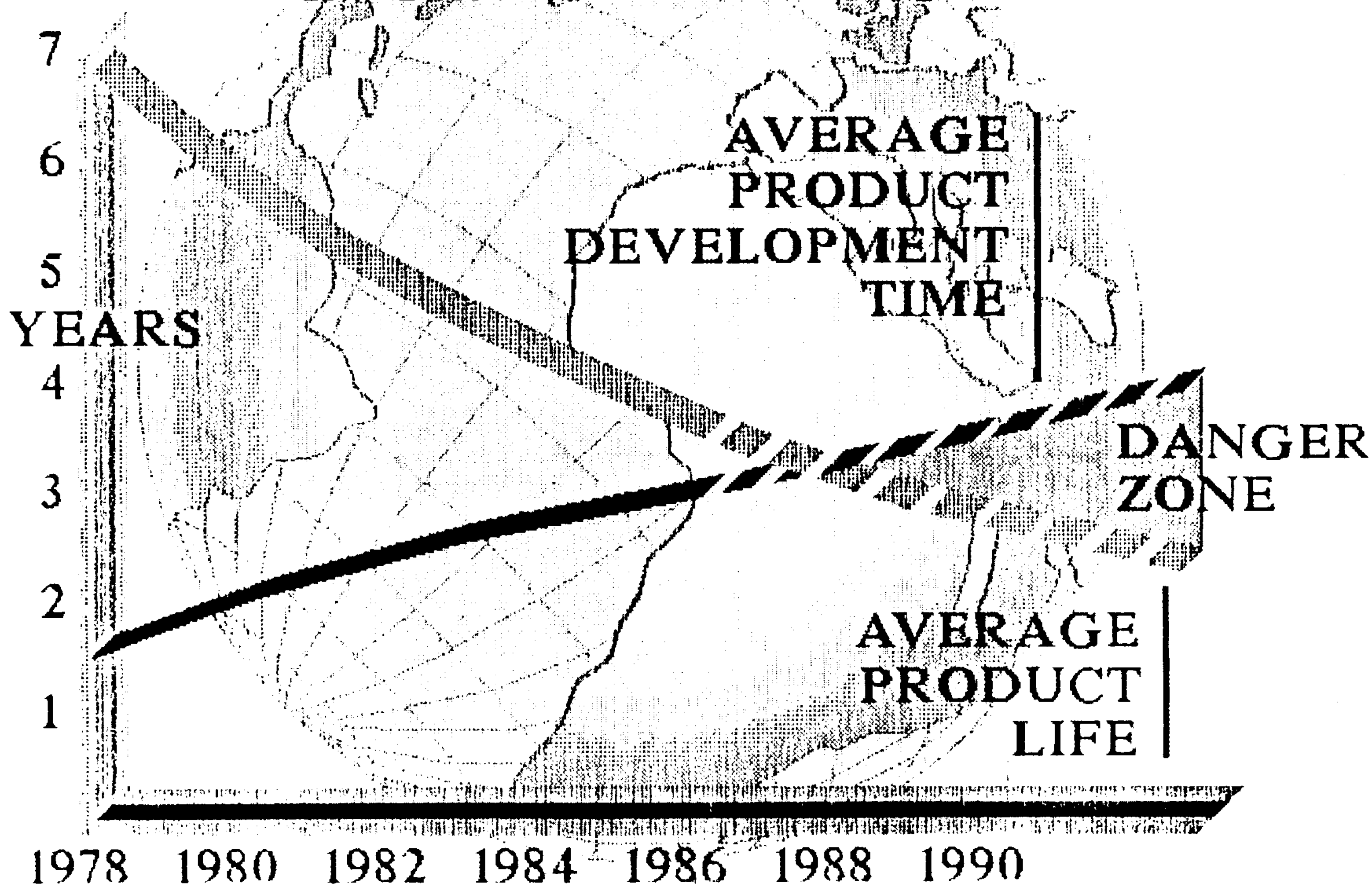
SHORTER LIFE CYCLES MAKE TIMING CRUCIAL

- LESS TIME TO MAKE PROFIT
- HIGHER RISK OF OBSOLESCENCE




INTERNATIONAL LOGISTICS
LEAD-TIME
COMPONENT SUPPLIERS
MANUFACTURING
SALES ORGANISATION
CUSTOMERS
TYPICAL STOCK (CALENDAR DAYS)
?
30
2
8
65
35
50
FACTORY
TRANSIT
DELIVERY
LOCAL DELIVERY
MATERIAL STOCKS & WIP
FINISHED STOCKS
WAREHOUSE
WHOLESALER
RETAILER
AVERAGE LEAD-TIME 190 DAYS

COMPLEX PRODUCTS ARE TAKING LONGER TO DESIGN, BUT NOT LASTING AS LONG IN THE MARKETPLACE



How might this be achieved?

(i) **Cutting short the pipeline**

Many companies have not paid proper attention to the length of the pipeline from suppliers through to customers, particularly with regard to transit times and intermediate stock holding. The presence of inventory in the supply chain, whether components, sub-assemblies, work-in-progress or finished goods inevitably adds to the total pipeline length. In the past the case for this inventory has been based upon the principle of "protection", i.e. the desire to protect production, distribution or marketing against upstream or downstream fluctuations in supply or demand. Such a motivation however should be considered unwise since it only serves to reduce flexibility. Instead the emphasis must be upon the adoption of "just-in-time" principles in delivery and manufacture to "fast track" products to the market place. Similarly closer co-operation with suppliers, who also will be substantially fewer in number as a result of a move towards increased single-sourcing, must be the norm. Treating suppliers as partners rather than adversaries means that even greater responsiveness to changed market needs can be achieved.

(ii) **Improve pipeline visibility**

Poor co-ordination in the supply chain will result in a lack of visibility in the pipeline. Traditional functional divisions in the orgainisation ensure that all we ever see is our own particular section of that pipeline. Bottlenecks and excess inventories are not easily identified and thus smooth and efficient movement through the pipeline is impeded.

The priority here has to be the removal of the organisational barriers that lie at the root of the problem. Typically the companies that lack pipeline visibility, and thus control over what happens in the pipeline, are also those that have conventional, functionally oriented organisation structures. "Territory" is jealously guarded and little information is shared. On the other hand the pace-setting global corporations have discarded these organisational strait-jackets for structures which are market-focussed. They are also characterized by the quality of their information systems - they can identify, in a real-time setting, the current status of each stage in the supply chain.

(iii) **Manage logistics as a system**

Because the global corporation tends by its very nature to operate in a context of an extended supply chain, it has been forced to confront the issue of international logistics management. In this scenario the needs of the market place must be matched with the organisation's production capability, against the over-riding objective of meeting local service requirements whilst keeping costs to a minimum. The achievement of this complex balancing act can only come about through a process of management which recognises the inter-relationships and the inter-connections of the chain of events that link the supply market with the customer. This is the challenge of logistics management in the global context.

In a sense the globalization of industry has brought the logistics management concept to centre stage. The essence of logistics is that it seeks to manage the materials flow from source to user. Logistics management demands that all those activities which link the supply market to the demand market be viewed as an inter-connected system - the point being that a decision taken in one part of that system will impact throughout the entire system. Now the emphasis has switched from a narrow functional orientation to the wider view of the value chain, in other words management has come to recognise that the primary purpose of business is to serve markets by adding value. The management of that added value, it is argued, is best accomplished by focussing upon the materials flow rather than upon traditional notions of functional or departmental efficiency.

To conclude, the pressures and imperatives of doing business on a global scale in the late twentieth century are inevitably leading to a recognition of the central role of logistics. Our definition of logistics has been broad, but in essence it reflects a concern with the need to gain a competitive advantage in markets that are subject to rapid change. The prizes in today's markets go only to those companies which are capable of providing added value in ever-shortening time scales. The paradox is that manufacturing technology has already developed to the point where it can achieve such a requirement - what we still lack is the means to deliver.


THE GOAL
SUPERIOR COMPETITIVE
ADVANTAGE