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## **Crawl, Walk and Run—The Move Offshore**

Implementing a LCCS program might sound anathema to manufacturers that have spent years developing long-term relationships with their domestic suppliers. Quality, convenience and reliability are the trademarks of these types of relationships. To further complicate matters, moving tooling or building new dies, adding buffer stocks, and establishing foreign currency hedging is enough to scare off even the boldest of companies.

So how do manufacturers make the move offshore?

Our research and experience suggest that for more complex goods, the most effective strategies often involve a phased approach over a longer time period, perhaps even years rather than moving all sourcing offshore in one step. How does this work in practice? Let's examine what a typical phased approach might look like. For example, consider a Tier 1 automotive firm who is currently purchasing steel stampings from the domestic market. As part of the relationship with its customer, the Tier 1 firm is the "steward" of the tooling, meaning though the tooling is owned by one of the Big 3 auto manufacturers, the Tier 1 firm has some say as to where the parts can be produced.

The first phase of the sourcing strategy would involve primarily domestic suppliers but also introduce a limited number of low cost country suppliers into the bidding process. During the contract awarding process, the Tier 1 firm decides to give the entire contract award (volume) to a domestic supplier. But as soon as the first order arrives, the Tier 1 firm begins to identify low cost country suppliers in SE Asia, some of which may have already been involved in the bidding process during phase one. At the same time, the Tier 1 firm receives price quotations on the costs of developing a second set of tooling. The tooling costs for dies produced in Asia are expected to be amortized and rolled into the piece part price over a two year time span as some supply begins to move offshore. In year two, after a competitive bidding event, the Asian supplier receives 25% of total spend while the domestic supplier receives 75% of total spend. In year three, both sources of supply receive 50% of the volume and the Tier 1 firm can decide in years four and five the proper mix and volumes for each supplier, depending on the Tier 1's annual "give-back" to the automotive OEM.

From a negotiation standpoint, this strategy works well when there is more than two million dollars in annual volume. At one million dollars of annual spend, the volumes are interesting to both Asian and domestic suppliers. With two or three million dollars in annual spend, the Tier 1 firm has enough volume to make the contract attractive enough to both suppliers, while still maximizing volume discounts.

Though in many situations, buying organizations would rather rationalize their supply base, reducing the number of suppliers, in this case, because of the stamping complexity and quality requirements, it actually makes better sense to fully develop two suppliers. By following such a program, the Tier 1 firm actually reduces their supply risk by developing a second source of supply while simultaneously establishing an early foothold in Asia for possible expansion in the future, either to identify future sources of supply and manufacturing or to develop emerging sales opportunities.