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Supply Chain News: More Evidence the Tide is Turning a Bit in the Offshoring Tsunami

First, it was Logistics Costs; Now, Other Factors; Overcoming a $2.50 Increase Per Unit for a Hair Iron

SCDigest Editorial Staff

Over the past decade, Western manufacturers have in many cases raced to outsource production, especially to China, lured by promises of dramatically lower costs and less capital tied up in assets.

Of late, some of the bloom has come off that rose. First, logistics costs, especially for heavy, low value-to-weight ratio products, started to soar with the tremendous spike in fuel prices in 2007-08, and the corresponding rise in ocean shipping rates tied to the explosion in offshoring.

Then, even as those logistics costs came back down, many, such as Boston Consulting Group's **George Stalk**, argued that the cost of inventory miscues often made domestic or at least "near shore" manufacturing the more advantaged strategy versus Asia. (See **The True Costs of Offshoring**.)

In June, GE CEO **Jeff Immelt** brought up the need to rethink the role of manufacturing in the overall economic health of the US.

"Many bought into the idea that America could go from a technology-based, export-oriented powerhouse to a services-led, consumption-based economy – and somehow still expect to prosper," Immelt said in a Detroit speech. "We must make a serious commitment to manufacturing and exports. This is a national imperative. We all know that the American consumer cannot lead our recovery. This economy must be driven by business investment and exports."

He added: "We should set a national goal to create high value added jobs and have manufacturing jobs be no less than 20 percent of total employment, about twice what it is today. And we should commit ourselves to compete and win with American exports."

The key issues driving the move: inventory management, being closer to the majority of its customers, quality management, and fighting counterfeit products .

Small Appliance Maker Moves Back to Texas

This week, Farouk Systems Inc., a $1 billion maker of hair irons, announced it was moving all of its production back to a giant factory near Houston, dramatically expanding what had been a small manufacturing facility there.

The key issues driving the move: inventory management, being closer to the majority of its customers, quality management, and fighting counterfeit products that have been coming to market in Asia.

"We'll make more money this way -- because we'll have better quality and a better image," the company's founder, **Farouk Shami**, is quoted as saying regarding the change in supply chain strategy this week in the Wall Street Journal.

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For example, the company currently spends about half a million dollars a month fighting counterfeit products made in China. Moving design and production thousands of miles away may thwart much of that counterfeiting, Shami believes.

In China, counterfeiters may source parts from the same suppliers that sell to the real brand owner, for example. Changing that dynamic may make it harder to knock off branded goods.

NCR, GE, Emerson Electric, and other high profile companies have recently announced strategies that would bring at least some production back to the US. NCR, for example, recently announced plans for a major new electronics facility near Atlanta.

Of course, labor costs in the US and Western companies are simply much higher than in China and other developing economies. That means in general more automation must be used in the US to reduce labor content – a strategy Farouk is pursuing, along with changes in product design to reduce manufacturing labor and costs. Still, the company is estimating the raw per unit manufacturing cost will increase by $2.50 – a number it hopes will be made up in inventory savings and faster response to market.

It is also important to note that the Farouk hair irons, called "Chi's," live at the very high end of the market, retailing for around $150.00 due to their unique design that minimizes damage to hair from their use. That is several times higher than standard irons.

But that is exactly the type of product that US manufacturers should look at for possible return of production to the US, or changes of plans to outsource to China, BCG's Stalk told us, where margins are high and demand is hard to forecast – making the cost of inventory overstocks and understocks quite high.

"You have to be willing to pay more money in some supply chain steps to reduce total supply chain costs, and of course that's where it breaks down in many companies, because some functions have to absorb those costs," Stalk told SCDigest. "It often really takes CEO leadership to cut through all that, and many CEOs of course don't understand it."

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