Value Chain Management: The Next Evolution of Supply Chain Management

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Session Objective and Agenda

OBJECTIVE
• Discuss how value chain strategies can enhance performance and overall company competitiveness through improved customer value

TOPICS
• End-to-End Value Chain Management & Competitive Strategy
• Business Strategy & Business Models
  – Channel Management
• Customer Value Propositions & Segmentation
  – Journey Mapping
  – Customer Metrics
• Examples & Success Stories
How do you describe or define integrated supply chain?
Lack of Common Definition
- Functional Bias
- Positional Bias

These gaps can create misunderstanding and confusion in the execution of integrated value chain strategies.
Integrated Value Chain Strategy

- **Old paradigm** - Firm gained synergy as a vertically integrated firm encompassing the ownership and coordination of several value chain activities.

- **New paradigm** - Firm in a value chain focuses activities in its area of specialization and enters into voluntary and trust-based relationships with supplier and customer firms (need to consider internal and external relationships).
Integrated Value Chain Strategy

- **Supply chain management** is a way to link major business processes within and across companies into a high-performance business model that drives competitive advantage.

- **Supply chain management** integrates supply and demand management within and between companies.

- **Value chain management** puts supply chain capabilities into a societal context.
New Realities of Value Chain Management
Integrated Value Chain Strategy

Drivers Of Integrated Value Chain Management

• Reduce Total Cost
• Improve Quality
• Reduce Time-to-Market
• Increase Customer Service/Satisfaction
• Integrate Supplier Technology
• Increase Supply Chain Synergy
• Enhance Competitive Positioning
• Better Utilize Supplier/Customer Strengths, Capabilities and Resources
• Minimize New Capital Investment
Integrated Value Chain Strategy

- Historically, businesses in the value chain have operated relatively independently of one another to create value for an ultimate customer.
- Independence was maintained by buffers of material, capacity and lead times.
Integrated Value Chain Strategy

*However...*

- Market/competitive demands are compressing lead times
- Businesses are reducing inventories and excess capacity
- Linkages between businesses in the value chain must therefore become much tighter

![Integrated Value Chain Diagram](image-url)
Integrated Value Chain Strategy

Traditional Value Chains

SUPPLIERS
Other Tiers

1st Tier

Logistics Providers

FOCUS COMPANY

Sourcing

Operations

Distribution

INTERMEDIATE CUSTOMERS
Distribution Centers
Retailers

Service Institutions
Logistics Providers

FINAL CONSUMERS

Information/Demand Flows

Value Creation and Value Delivery Flows
Integrated Value Chain Strategy

Traditional Value Chains

SUPPLIERS
Other Tiers
1st Tier

Logistics Providers

FOCUS COMPANY

Inventory, Capacity and Lead-time Buffers

INTERMEDIATE CUSTOMERS
Distribution Centers
Retailers

Service Institutions
Logistics Providers

FINAL CONSUMERS
Integrated Value Chain Strategy

Integrated Value Chains

Value Delivery (Customer Order Fulfillment) Flow

Value Creation (Product/Process/Service/Development) Flow

Value Maintenance (After-Sale Service/Support) Flow

Information/Demand Flows

Sourcing

Operations

Distribution

Financial Management - Cash & Assets

SUPPLIERS

COMPANY

INTERMEDIATE CUSTOMERS

FINAL CONSUMERS
Integrated Value Chain Strategy

Integrated Value Chains

- Vision
  - Business Vision
  - Supply Chain Vision
- Enablers
  - Organization Structure
  - Culture and People
  - Information Systems/Technology
- Processes
  - New Product Development
  - Customer Order Fulfillment
  - After-Sale Service/Support
- Results
Customer Value Proposition

- *Value Proposition* is a statement summarizing the customer segment, competitors and the basic differentiation of one's products and services from the offerings of competitors.

- A value proposition should answer the question:

  “Why should a customer buy *this* product or service?”
Customer Value Proposition

- Customer journey maps
  - The analysis of the customer buying process
- Business process maps
  - The analysis of business processes used to satisfy customers
Customer Value Proposition

- Efficiency
- Relevancy
- Value Creation
- Effectiveness
- Sustainability
- Value
- Creation
- Efficiency
- Relevancy
- Sustainability
Value Chain Principles

• Service segmentation
  – “One size does not fit all”
• Analytics
  – “Manage with data”
• Efficient versus responsive value chains
  – “Match processes with performance requirements”
• Operational consistency
  – “Variability destroys value chain performance and customer value”
• Risk management
  – “What is the risk appetite of the organization?”
Service Segmentation - 3 Levels of Customer Focus

Basic Service

Achieve internal standards (e.g., specified performance cycle of fill rate)

Satisfaction

Meet customer expectations (e.g., arrive on time with right product as measured by the customer)

Success

Customers of choice achieve their objectives (e.g., logistics operation can provide product and service in a manner that ensures long term customer viability)
Customers Have Different Objectives, Requirements and Expectations

When considering value chains, do you appropriately segment requirements and delivery approaches?
Analytics – Manage with Data

• Providing “predictive analytics” by…
  – Keeping a finger on the pulse of critical requirements needed for the customer to succeed and advising on the proactive steps the customer can take to stay competitive

• Providing “assurance analytics” by…
  – Helping demonstrate that products, services or solutions assure customers of minimum cost, least time spent, and the best quality

When considering value chains, do you use data to build and support the business case?
## Functional vs. Innovative Products – Differences in Demand

<table>
<thead>
<tr>
<th>Aspects of Demand</th>
<th>Functional (Predictable Demand)</th>
<th>Innovative (Unpredictable Demand)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Product life cycle</td>
<td>&gt; 2 yrs</td>
<td>&lt; 1 yr</td>
</tr>
<tr>
<td>Contribution margin</td>
<td>5 – 20 %</td>
<td>20 – 60 %</td>
</tr>
<tr>
<td>Product variety</td>
<td>Low (10 – 20 variants per category)</td>
<td>High (large number of variants per category)</td>
</tr>
<tr>
<td>Average forecast error</td>
<td>10%</td>
<td>40 – 100%</td>
</tr>
<tr>
<td>Average stockout rate</td>
<td>1 – 2%</td>
<td>10 – 40%</td>
</tr>
<tr>
<td>Average end-of-season markdown</td>
<td>0%</td>
<td>10-25%</td>
</tr>
<tr>
<td>Leadtime for MTO products</td>
<td>6 – 12 months</td>
<td>1 – 2 days</td>
</tr>
</tbody>
</table>
### Physically Efficient vs. Market Responsive Value Chains

<table>
<thead>
<tr>
<th></th>
<th>Physically Efficient Process</th>
<th>Market-Responsive Process</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Primary purpose</strong></td>
<td>Supply predictable demand efficiently</td>
<td>Respond quickly to unpredictable demand to maximize service</td>
</tr>
<tr>
<td><strong>Manufacturing focus</strong></td>
<td>Maintain high average utilization rate</td>
<td>Deploy excess buffer capacity</td>
</tr>
<tr>
<td><strong>Inventory strategy</strong></td>
<td>Generate high turns and minimize inventory</td>
<td>Deploy significant buffer stocks</td>
</tr>
<tr>
<td><strong>Lead-time focus</strong></td>
<td>Shorten leadtime while not increasing cost</td>
<td>Invest in ways to reduce leadtime</td>
</tr>
<tr>
<td><strong>Approach to choosing suppliers</strong></td>
<td>Select primarily for cost and quality</td>
<td>Select primarily for speed, flexibility and quality</td>
</tr>
<tr>
<td><strong>Product-design strategy</strong></td>
<td>Maximize performance and minimize cost</td>
<td>Use modular design to postpone differentiation</td>
</tr>
</tbody>
</table>
### Matching Value Chains with Products

<table>
<thead>
<tr>
<th></th>
<th>Functional Products</th>
<th>Innovative Products</th>
</tr>
</thead>
<tbody>
<tr>
<td>Efficient Value Chain</td>
<td>Match</td>
<td>Mismatch</td>
</tr>
<tr>
<td>Responsive Value Chain</td>
<td>Mismatch</td>
<td>Match</td>
</tr>
</tbody>
</table>

**When considering value chains, do you appropriately match value chains with products?**
Operational Consistency – Performance Cycles

- Material source
- Lead supplier (tier 1)
- Manufacturing plant
- Distributors
- Customer

Purchasing cycle

Manufacturing support cycle

Customer accommodation cycle

Input and output requirements are not illustrated

Node

Transportation links
Communication links
Operational Consistency – Variability

When considering value chains, do you focus on eliminating variation through standard processes?
Risk Management

- Quality and availability
- Supply
- Access to data and visibility
- Cost
- Compliance
Risk Management – Value Chain Dimensions

<table>
<thead>
<tr>
<th>COMPLIANCE</th>
<th>COUNTRY EVENTS</th>
<th>FINANCIAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Supplier code of conduct</td>
<td>• Natural disasters</td>
<td>• Public companies</td>
</tr>
<tr>
<td>• Supplier high risk audits</td>
<td>• Labor relations</td>
<td>• Private companies</td>
</tr>
<tr>
<td></td>
<td>• Geopolitical risks</td>
<td>• Payment changes</td>
</tr>
<tr>
<td></td>
<td>• Trade barriers</td>
<td>• Bankruptcy</td>
</tr>
<tr>
<td></td>
<td>• Duties and tariffs</td>
<td>• Ownership changes</td>
</tr>
<tr>
<td></td>
<td>• Pandemic</td>
<td>• Public press releases</td>
</tr>
<tr>
<td></td>
<td>• Terrorism</td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>PERFORMANCE</th>
<th></th>
<th>MARKET SEGMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Achieving excellence</td>
<td></td>
<td>• Expertise</td>
</tr>
<tr>
<td>• Delivery</td>
<td></td>
<td>• Certification</td>
</tr>
<tr>
<td>• Quality</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Audit results</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Capacity constraints</td>
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</tr>
</tbody>
</table>

When considering value chains, do you think about risk profiles and the potential business impact?
Putting the Pieces Together – Business Models

Value Proposition

Value

Key Customer

Capabilities
Value Drivers & Relationships

- Evolving Performance Focus
- Value Drivers
  - Revenue
  - Cost
  - Assets
- Strategic Profit Model
Does the customer talk about value, but use metrics that are price-based or cost-based to hold suppliers accountable?
Value Drivers

When considering value chains, how do we appropriately leverage capabilities to achieve organizational value outcomes?
Value Drivers

Revenue (+)
- Product/service development time
- Technology access
- Product/service quality
- Market knowledge/responsiveness

Cost (-)
- Direct labor costs
- Transaction costs
- Operating costs
- Overhead

Assets (-)
- Fixed asset base (in/outsourcing)
- Efficient use of assets
Strategic Profit Model

ROA = \frac{Net\ Income}{Total\ Assets}

Net\ Income = Revenue - Total\ Expenses

Revenue = Price \times Quantity

Total\ Expenses = COGS + Other\ Expenses

COGS = Materials + Overhead + Labor

Accounts\ Receivable = Current\ Assets + Inventory + Cash

Current\ Assets = Fixed\ Assets
Strategic Profit Model – Two Fundamental Ways To Improve Return On Assets

• Manage net profit margin improvements
  - **Net profit margin** is net profit divided by net sales
  - Measures portion of each sales dollar that is kept by the firm

• Manage asset turnover improvements
  - **Asset turnover** is ratio of total sales divided by total assets
  - Measures efficiency of management utilization of assets
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QUESTIONS