Voice of the CSCO

Evaluating supplier financial health and weighing repatriation

KPMG convened chief supply chain officers (CSCO) from a cross-section of industries for a discussion on the topics of supplier engagement, supplier financial health, supply chain re-patriation, and vertical integration. Rob Barrett, U.S. Supply Chain Advisory leader hosted the session. Joining him were Brian Higgins, U.S. Supply Chain Operations leader, and Mary Rollman, principal, U.S. Supply Chain Operations.

Key takeaways

- **Interconnectedness with Trading Partners**—Companies need connectivity with their trading partners to manage the processes of their supply chain. The key is focusing on the business problem that the collaboration resolves and the purpose of the connectivity
- **Evaluating supplier financial health**—Companies need to take steps to determine when a supplier is suffering from financial distress—or worse case, going bankrupt—which can cause major supply chain disruptions.
- **Repatriation**—Exposure to long lead times from Asia and potential tension with China have caused many companies to consider moving their sources or manufacturing operations closer to or back within the United States. But that process can present some challenges.

Supply chain visibility remains a concern for CSCOs.

Peter R. Hantman, chief operating officer at **E2open,** spoke to share forum participants about how companies could improve the connectivity with their trading partners to better manage the processes of their supply chains.

He noted that research shows that most companies have very high levels of visibility and collaboration with their tier-one suppliers, but only a few companies have that same level collaboration and visibility with their end-tier suppliers.

These statistics suggest that the concept of collaboration across multiple tiers is well understood, but the process of collaboration can be intimidating, and many companies fall short of the mark.

Hantman stressed that successful engagement with suppliers begins with being clear about the issues that you want to solve and how you and the supplier can collaborate around the business process that can solve it. For example, it can be gathering data around child labor or conflict minerals. Typically, the easiest tier and suppliers to connect with are those with which you have a direct contract relationship with.

One CSCO participant noted that a persistent issue hampering collaboration is obtaining proprietary information from suppliers. There is a perception that if the supplier gives up information, they will be more vulnerable to the purchaser's replacing them or vertically integrating—or just using the information to drive prices down. However, Hantman noted that there are ways around this issue, and companies often underestimate their negotiating power. Suppliers will be more willing to share it they know that they will get something in return or are told how the information will be used.

Evaluating supplier financial health

A supplier suffering from financial distress—or worse case, going bankrupt—can cause major supply chain disruptions.

CSCOS wanted to know how they can assess the financial health of suppliers so their business isn't interrupted. For example, a financial health check could be done on a semiannual basis. If the supplier is found to be in financial distress, the company could try to support them. Or, if they're past the point of no return, find the best way to pivot away from them to ensure there's no disruption.

One participant suggested the "big net, big holes; small net, small holes" approach. The first step is to use a credit risk monitor that can give a broad-brush view of your vendors. If any company falls through that screening, they can be examined closer with a second-tier monitor. This approach offers an efficient and cost-effective option, since applying a high level of scrutiny to all suppliers would simply take too much time, effort, and money.

Another CSCO suggested looking for trends around suppliers' financial health. A supplier with an average, but consistent financial risk metric, may not be a concern. But if a vendor's rating suddenly falls several points, that may be a call for more due diligence.

Of course, evaluating the financial health is more difficult with private companies than public one where the financial information is more readily available. For private companies, it may require an offline discussion between the finance teams of the company and the vendor.

Repatriation

Exposure to long lead times from Asia and potential tension with China have caused many companies to consider moving their sources or manufacturing operations closer to or back within the United States.

> There are multiple strategies. One size doesn't fit all, but the intent is to try to be less reliant on these materials coming out of China and in India, although many companies can't totally eliminate them from supply chain.
>
> *– Participant*

A number of CSCO participants indicated that they have taken some steps toward repatriation of sourcing or manufacturing. But that process can present complex challenges, and every industry and every company has its own difficulties when it comes to finding the right mix of global, regional, and local for their supply chain. CSCO participants agreed that an over-reliance on any one source of supply is risky under any circumstances but is even more critical in the current political climate. It is an issue that has made its way to the Board of Directors and is of strategic importance for the company as a whole.

A number of steps can be taken to mitigate risk while the broader strategic decisions are being. One is to place teams on site at key suppliers to micromanage the operations, however this approach may not work with all suppliers. Another tactic mentioned is to build an inventory of critical starting materials in certain manufacturing locations around the world or working with a vendor or supplier to expand into another one of its facilities outside of China—in other words, keeping the business with the company but derisking the supply. Still another participant said that their company worked to find other alternatives for their raw materials, whether it's changing the country of origin or changing the raw material itself. Finding an alternative would naturally require partnering with research and development.

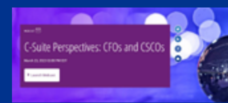
> It's really working cross-functionally in the organization to find all the alternatives, whether it's changing the raw material country of origin, changing the raw material itself, the way that we manufacture, or where we manufacture to address the overall risk.
>
> *– Participant*

Another CSCO said his company was looking to move manufacturing to places like Mexico and the U.S., as well as diversifying the supply base and being very transparent with the manufacturers about where they need to be so they both can come to a win-win financial solution.

Additional insights

[Stop flying blind: Wide-ranging supply chain visibility improves overall resiliency]

[Q4, 2022 Global Supply Chain Stability Index Report Discussion]



[C-Suite Perspectives: CFOs and CSCOs]

[Procurement transformation on display in full color]

Connect with us

Rob Barrett
U.S. Supply Chain Advisory Leader
KPMG LLP
T: 650-814-0347
E: rhbarrett@kpmg.com

Brian Higgins
U.S. Customer and Operations Leader
KPMG LLP
T: 773-619-1253
E: bhiggins@kpmg.com

Mary Rollman
Partner, U.S. Customer and Operations
KPMG LLP
T: 312-618-9863
E: maryrollman@kpmg.com

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