Chapter 2
Logistics Strategy

Dr. Vin Pheakdey
Ph.D. in Economics, France

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Learning Objectives

After learning this chapter, you should be able to:

- See how a logistics strategy fits into an organization’s broader decisions.
- Outline the strategic importance of logistics
- Define a logistics strategy and discuss its focus
- Discuss alternative logistics strategies
- Approach the design of a logistics strategy

1. Strategic Decisions

Decisions are classified by:

- **Strategic decisions**: the most important decisions and set the overall direction of the organization. They have effects over the long term.
- **Tactical decisions**: implementing the strategies over the medium term. They look at more detail.
- **Operational decisions**: the most detailed and concern activities over the short term.
1. Strategic Decisions

Types of Strategic Decision

- **Mission**: a statement to give the overall aims of the organization.
- **Corporate strategy**: shows how a diversified corporation will achieve its mission.
- **Business strategy**: shows how each business within a diversified corporation will contribute to the corporate strategy.
- **Functional strategies**: describe the strategic direction of each function, including logistics.
2. Logistics Strategy

- Logistics strategy consists of all the strategic decisions, policies, plans and culture relating to the management of its supply chains.
- The logistics strategy forms a link between the more abstract, higher strategies and the detailed operations of the supply chain.
- While the corporate and business strategies describe general aims, the logistics strategy concerns the actual movement of materials needed to support these aims.

2. Logistics Strategy

- The higher strategies set the context for the logistics strategy.
- Logistics managers do not simply respond to this context, they actively contribute to its formulation.
2. Logistics Strategy

Role of Logistics Managers in Strategic Decision

Focus of Logistics Strategy

- *Which factors are most important for this contribution and should be emphasized in a logistics strategy?*

- A logistics strategy is most likely to emphasize the following:
  - **Cost:** lower costs lead to higher profits for organization and lower prices for customers.
  - **Customer service:** logistics controls stock levels, delivery times, speed of response, and so on. This strategy allows organizations to get a long-term competitive advantage.
  - **Timing:** it mean rapid supply of new products, or delivering at the time specified by a customer. A common logistics strategy guarantees fast deliveries.
Focus of Logistics Strategy

- **Quality**: a common logistics strategy guarantees high-quality service to satisfy customers.
- **Product flexibility**: one logistics strategy is based on a specialized or customized service to individual specifications.
- **Volume flexibility**: it allows an organization to respond quickly to changing levels of demand.
- **Technology**: a logistics strategy can be focused on the development and use of the latest technologies for communications, tracking loads, identifying product, recording stock movements and so on.
- **Location**: one logistics strategy is to provide a service in the best possible location since customers generally want products to be delivered as close to them as possible.

In principle, organizations should do everything well, giving low cost, good customer service, fast delivery, flexibility, using high technology, and so on.

In practice, this is unrealistic. Organizations have to compromise, perhaps balancing the level of service with the cost of providing it.

Effectively they choose a specific **focus** for their logistics strategy, showing which factor they consider to be most important.
3. Strategy Option

- Michael Porter suggested two basic strategies:
  - **Cost leadership**: makes the same, or comparable, products more cheaply.
  - **Product differentiation**: makes products that customers cannot get from other suppliers.

- Example:
  - Lyons Bakeries compete by cost leadership, selling standard cakes at low prices.
  - La Patisserie Française competes by product differentiation, selling cakes that are not available anywhere else.
  - EasyJet competes by cost leadership, offering the cheapest fares.

- These two approaches are usually phrased in terms of:
  - Lean strategy
  - Agile strategy
Lean Strategies

- Lean strategy is aimed at low costs. It is to do every operation using less of each resource (people, space, stock, equipment, time, etc.).
- Therefore, lean logistics is aimed at minimizing the total cost of logistics.
- One warning is that low costs do not automatically mean lean operations.
- Lean operations maintain customer service while using fewer resources – they do not just minimize costs.

Lean Strategies

- Five main principles:
  1. **Value**: designing a product that has value from a customer’s perspective.
  2. **Value stream**: designing the best process to make the product.
  3. **Value flow**: managing the flow of materials through the supply chain – getting an efficient flow of materials, eliminating waste, interruptions, waiting and detours.
  4. **Pull**: only making products when there is customer demand
  5. **Aim of perfection**: looking for continuous improvements to get closer to the aim of perfect operations.
**Agile Strategy**

- The aim of an agile strategy is to give a high customer service by responding quickly to different or changing circumstances.

- Two aspects of agility:
  - There is the speed of reaction; agile organizations keep a close check on customer demands and react quickly to changes.
  - It is the ability to tailor logistics to demands from individual customers.

- Organizations that put a lot of emphasis on customer satisfaction are said to have a **customer focus**.

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**Lean versus Agile**

<table>
<thead>
<tr>
<th>Factor</th>
<th>Lean logistics</th>
<th>Agile logistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Objective</td>
<td>Efficient operations</td>
<td>Flexibility to meet demands</td>
</tr>
<tr>
<td>Method</td>
<td>Remove all waste</td>
<td>Customer satisfaction</td>
</tr>
<tr>
<td>Constraint</td>
<td>Customer service</td>
<td>Cost</td>
</tr>
<tr>
<td>Rate of change</td>
<td>Long-term stability</td>
<td>Fast reaction to changing circumstances</td>
</tr>
<tr>
<td>Measures of</td>
<td>Productivity, utilisation</td>
<td>Lead time, service level</td>
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<tr>
<td>performance</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Work</td>
<td>Uniform, standardised</td>
<td>Variable, more local control</td>
</tr>
<tr>
<td>Control</td>
<td>Formal planning cycles</td>
<td>Less structured by empowered staff</td>
</tr>
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</table>
Strategic Alliances

- The purpose of this strategy is to get efficient supply chains, with all members working together and sharing the benefits of long-term cooperation.
- A strategy of forming partnerships allow for better customer service, increased flexibility, reduced costs, avoidance of investment in facilities, and lack of expertise within the organization.
- Some common areas for partnerships is transport, warehousing, import/export services, materials storage, and so on.

Other Strategies

- **Time-based strategies**: aim for a guaranteed faster delivery of products. Benefits include:
  - Lower costs by having less stock in the supply chain
  - Improved cash flow by not having to wait so long for payment
  - Less risk by reducing changes to orders, obsolete stock,…
  - Simpler operations by eliminating delays and unnecessary stores.
- But faster logistics may reduce the quality.
Other Strategies

- **Environmental protection strategies:** A small, but increasing, number of organizations are developing strategies based around environmental protection.
- The principles in logistics are to use reusable containers and recycling of materials.
- Most organizations assume that “going green” raises costs.
- In reality, many programs for environmental protection reduce costs. Ex: insulation of warehouses, regular maintenance of road vehicles…

Other Strategies

- **Increased productivity strategies:** Aim for using available resources as fully as possible.
- Ex: facilities (e.g. warehouses) have high fixed costs and using them at full capacity spreads these costs over more units. Imagine a facility that is working at 60% of capacity. Obviously, there is spare capacity that is raising unit costs.
  - The lean approach would look for ways of removing the 40% spare capacity – and then continue looking for further reductions over time.
  - A high productivity strategy is more likely to accept the present capacity, and starts looking for alternative uses for the excess. An office or warehouse might rent out space.
Other Strategies

- **Valued-added strategies**: aim for adding as much value as possible to final products.

- Organizations can add value by adding time and place utility, or doing more work on the product.

- Ex: a company delivers washing machines to customers’ houses. It adds value by delivering to the place and at the time preferred by customers, or by doing more work such as installing the machines, testing them, giving instructions on their use, removing old machines, offering service contracts, and so on.

Other Strategies

- **Diversification or specialization strategies**: look at the range of services offered by logistics.

  - Some organizations have strategies of diversification, offering the widest range of services and satisfying as many customers as possible. Ex: a department store which sells every product; some transport companies move every kind of load from letters through to oversize loads.

  - Other organizations have a strategy of specializing in a very narrow range of services, but being the best provider in their chosen area. Ex: some transport companies move only small packages with high security.
Other Strategies

- **Growth strategies**: aim for getting economies of scale – larger operations can give both lower costs and better service.

- Several ways to achieving growth:
  - Expanding the geographical area covered
  - Diversifying into more logistics activities by moving different types of materials.

4. Designing a Logistics Strategy

- There are three factors to consider when designing a logistics strategy:
  - the higher strategies
  - the business environment
  - the organization’s distinctive competence
4. Designing a Logistics Strategy

Factors in the Design of a Logistics Strategy

- Higher strategies set the organization’s goals and the context for all logistics decisions.
- The mission sets the overall aims, and the corporate and business strategies show how these aims will be achieved.
- The logistics strategy must support these higher strategies. If, for example, the business strategy calls for high customer service, the logistics strategy must show how logistics will achieve this.
Business Environment

- The business environment consists of the factors that affect logistics, but over which it has no control. These include:
  - *customers* – their expectations, attitudes, demographics
  - *market conditions* – size, location, stability
  - *technology* – current availability, likely developments, rate of innovation
  - *economic climate* – gross domestic product, growth rate, inflation
  - *legal restraints* – trade restrictions, liability and employment laws

Business Environment

- *competitors* – number, ease of entry to the market, strengths
- *shareholders* – their target return on investments, objectives, profit needed
- *interest groups* – their objectives, strengths, amount of support
- *social conditions* – customers’ lifestyles, changing demands
- *political conditions* – stability, amount of governmental control, external relations.
Organization’s Distinctive Competence

- A distinctive competence stems from an organization’s assets, which include:
  - *customers* – their demands, loyalty, relationships
  - *employees* – skills, expertise, loyalty
  - *finances* – capital, debt, cash flow
  - *organization* – structure, relationships, flexibility
  - *products* – quality, reputation, innovations
  - *facilities* – capacity, age, reliability
  - *technology* – currently used, plans, special types
  - *processes* – structures, technology used, flexibility
  - *marketing* – experience, reputation
  - *suppliers* – service, flexibility, partnerships
  - *other assets* – knowledge, innovation, patents.
4. Designing a Logistics Strategy

- In short:
  - the business environment and distinctive competence show where an organization is now.
  - the higher strategies show where it wants to be in the future.
  - the logistics strategy shows how to move from one to the other.

Logistics Audit

- The purpose of a logistics audit is to collect relevant information about existing practices and performance of logistics.
- We have details of current performance from the audit.
Logistics Audit

- Two main parts to a logistics audit:
  - **Getting information about business environment (external audit):** the nature of customers, types of demand, accepted service levels, competitors and their operations, benchmarks and comparisons, economic conditions, geographical and political constraints, and other relevant external information.
  - **Getting information about distinctive competence of organization (internal audit):** the structure of the supply chain, warehouse locations and size, stock holdings, lead times, order processing, damage, productivity, and other relevant internal information.

- This approach is similar in principle to a **SWOT analysis**, which lists an organization’s **strengths, weaknesses, opportunities, threats**.
- We know where we want to go from a logistics **mission**, and where we are at the moment from the logistics **audit**.
- The next stage is to identify gaps between these two and show how to bridge the gaps.
Developing the Strategy

- **There are eight steps for designing a strategy:**

  1. The external audit gives an analysis of the business environment and then shows the factors that lead to success in this environment.

  2. The internal audit analyses higher strategies from a logistics viewpoint, giving the context and overall aims for logistics, its strategic focus and perhaps includes a logistics mission.

3. Design the general features of supply chains that can best deliver the desired services. This includes the design of the network, location of facilities, capacity, technology used, and so on.

4. Set specific goals to show what each logistics activity must achieve. The internal audit shows how well the current logistics achieve these goals, and identifies areas that need improving.

5. Design the best organizational structure, controls and systems to support the logistics network.
Developing the Strategy

6. Benchmark logistics, looking at the performance of leading organizations, defining measures to compare actual performance with planned, optimal and competitors’ performances.

7. Implement the strategy, setting the conditions for lower levels of logistics decisions.

8. Monitor actual performance, continually look for improvements, keep the strategies up to date, and give feedback.

End