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## **Operating in the UK as a strategic choice**

### **Executive Summary**

## **Background**

This summary gives the results of the thesis made by Hugues Charrat, supervised by Dr Denyse Julien and sponsored by Machan consulting Ltd. The aim of the thesis was to “explore the hypothesis that there are some manufacturers operating in the UK out of strategic choice”.

To achieve this, a literature review had been done to highlight the major themes about this topic.

Then a survey based on the literature review’s results was carried out in order to highlight the strategic drivers for operating in the UK and the strategies employed. Sixteen companies, from different industrial sectors had participated to the survey. The results were analysed and a discussion based on the results of the survey and the literature review was done.

## **Operating in the UK as a strategic choice**

In an increasingly global marketplace, the decision to offshore activities or maintain operations in the UK is a major concern for manufacturing organisations. Research carried out by Cranfield University attempts to understand the underpinning drivers for companies making the strategic decision to operate in the UK.

Since the early 1970s, offshoring of activities to low cost countries in order to reduce labour or total costs has been on the increase. But many companies only saw the reduction of direct costs and failed to recognise that offshoring can bring other hidden costs and problems, such as transport costs or cultural differences. Because of the challenges associated with offshoring, many companies are deciding to keep operations in the UK or to relocate their offshoring activities back to the UK.

“UK manufacturing is not in terminal decline, far from it. The sector still employs nearly 3 million people, generates around 60 per cent of exports and has come a long way from smokestacks, oily rags and truculent trade unions”. Sutherland (2008)

The Manufacturing Advisory Service (MAS) (Livesey, 2006) defines manufacturing as “the full cycle of activities from research, design and development, production, logistics, and service provisions to end of life management”, see Figure 1.



Figure 1 - Extended definition of Manufacturing (Adapted from: Livesey, 2006)

MAS also makes a clear distinction between production and manufacturing. Production is defined as “the physical process of making, bending, etc” and manufacturing “the over-arching process from the sourcing raw materials and converting them to goods and their associates services”.

The research carried out at Cranfield University surveyed seventeen manufacturing companies from different sectors.

Six core categories of drivers were identified from the literature on the subject:

- ✓ Customer focus drivers
- ✓ Financial drivers
- ✓ Logistic drivers
- ✓ Marketing drivers
- ✓ Political drivers
- ✓ Technical drivers

Figure 2 below summarises the key categories of drivers which underpin an organisation’s decision to operate in the UK.

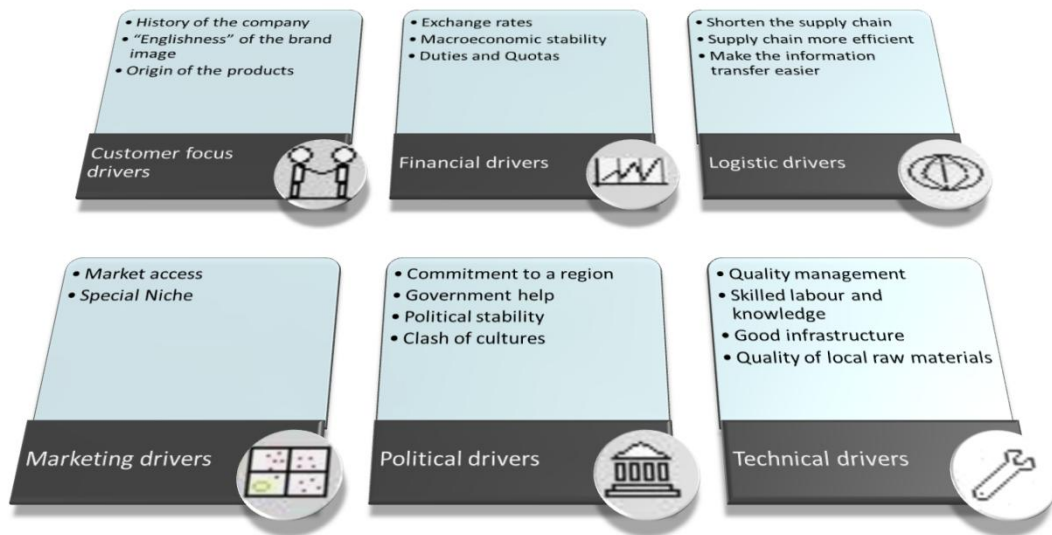


Figure 2 – List of drivers for operating in the UK

### Customer focus drivers

Every company should be focused on customer satisfaction. Some organisations will decide to keep operating in the UK to satisfy their customer expectations. The potential dangers in offshoring for these organisations include loss of customers and damage to reputation. Some organisations have adopted a strategy which involves separating their production into 'high value' and 'low value' products. The high value products are produced in the UK and targeted at customers who expect an 'English' production while the lower value products can be produced offshore, targeting the mass consumption market.

### Financial drivers

Financial drivers are an obvious concern for every company and are frequently cited as the most important. These drivers will be considered against marketing or technical drivers but will always be of great importance in deciding the final sourcing strategy.

### Logistic drivers

This is one of the most important themes because of the broad types of drivers within it. The company that chooses to operate in the UK for logistical reasons may be a foreign company that wishes to access the UK market, or a UK owned company. The need for speed to market and responsiveness to customers are often a key consideration to organisations who cite these drivers as the most important.

### Marketing drivers

Many foreign companies have clear marketing drivers to operate in the UK. Access to market and being a niche player are crucial for many UK companies deciding to keep operations in the UK.

### Political drivers

Political drivers are of significant importance for UK-owned companies, as they consider the relationship between the company and the UK government as well as with other governments. These drivers have a significant importance in sourcing strategy and are sometimes the key driver for deciding not to offshore operations.

### Technical drivers

While the technical drivers are very important they are often viewed as less critical than the financial. Some companies prefer to change their techniques and adapt their products if they can have financial or marketing benefits.

## Drivers for operating in the UK

Respondents of the survey were asked to indicate, on a scale of 1 to 6, where 6 was most important, the importance of twelve different drivers for maintaining operations in the UK. The results identified that five drivers came out as more important based on their average score (Fig 3). The five drivers ranked in descending order are:

- a. Special niche
- b. History of the company
- c. Market access
- d. Access to skilled labour and knowledge
- e. Staying close to key customers

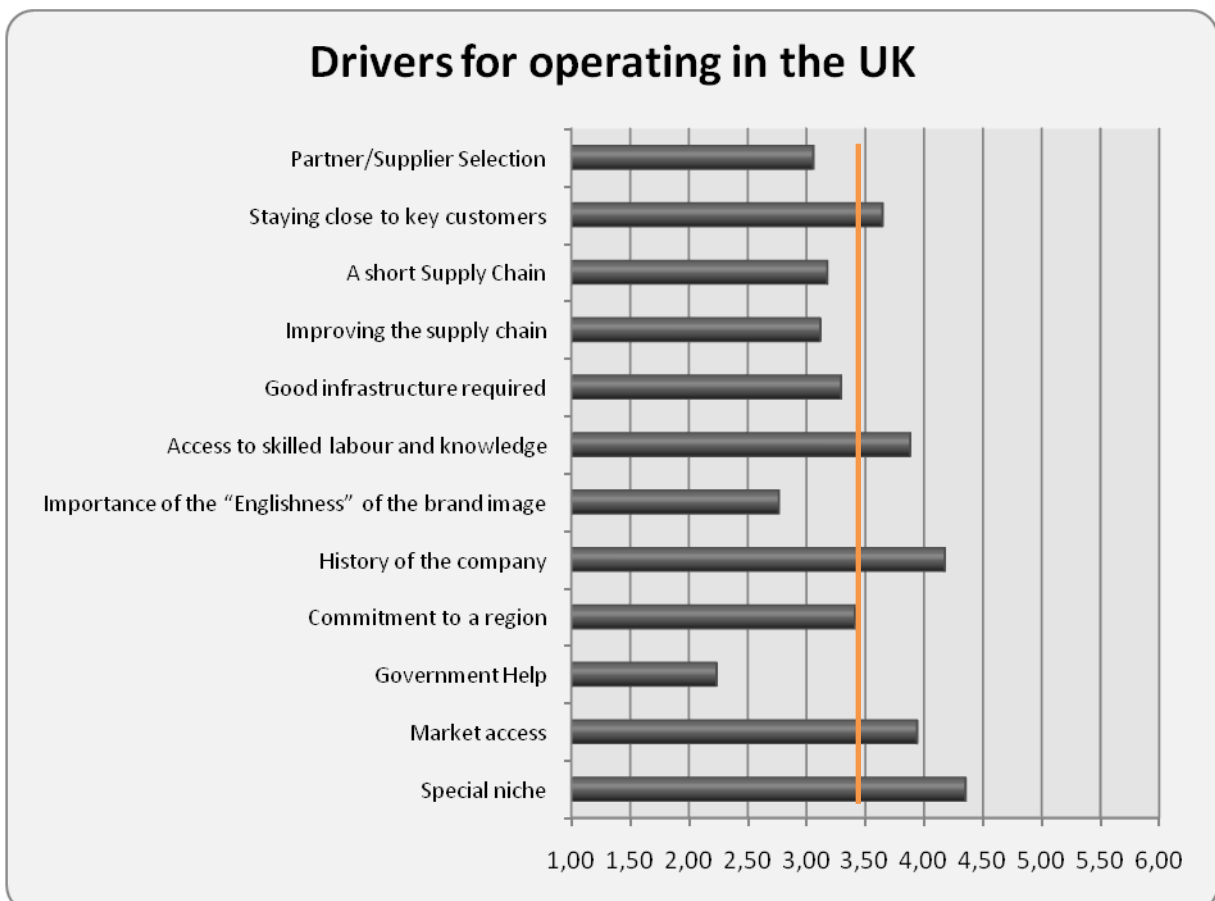


Figure 3 – Most important drivers

A common theme for these five key drivers was defined as ‘Customer Relationship Focus’. This observation underlies the importance of aligning the company’s strategy with the needs of their key customers and understanding the core differentiators of their business. It is also interesting to compare this with earlier studies looking at drivers in favour of offshoring (Bacon, 2007) where the primary driver for offshoring was found to be cost reduction. For companies choosing to maintain operations in the UK the emphasis appears to be more on customer relationships and position in the market.

Belonging to a special niche market often requires the company not to offshore for different reasons. A special niche may imply a low volume of production and consequently it may be better to produce locally than offshore where additional costs associated with offshoring can be kept to a minimum. It could also require the operation to take place in a specific area if the product is geographically positioned. The second most important factor was the ‘history of the company’; ten of the seventeen respondents rated this factor as very important in the sourcing strategy decision.

## Barriers to offshoring

Another interesting output from the survey was the companies’ opinions on the barriers they see to moving operations offshore (Fig 4). Seven factors out of a possible 18 emerged as more relevant than the rest, and are ranked below in descending order of importance:

- f.** Risk of the loss of knowledge (intellectual property etc)
- g.** Would have increase the response time to the customers
- h.** Product quality required could not be achieved
- i.** Skills and knowledge not found overseas
- j.** Customer’s expectation about the “Englishness” of the brand image
- k.** Transfer of knowledge too difficult
- l.** Problem in resolving problems overseas

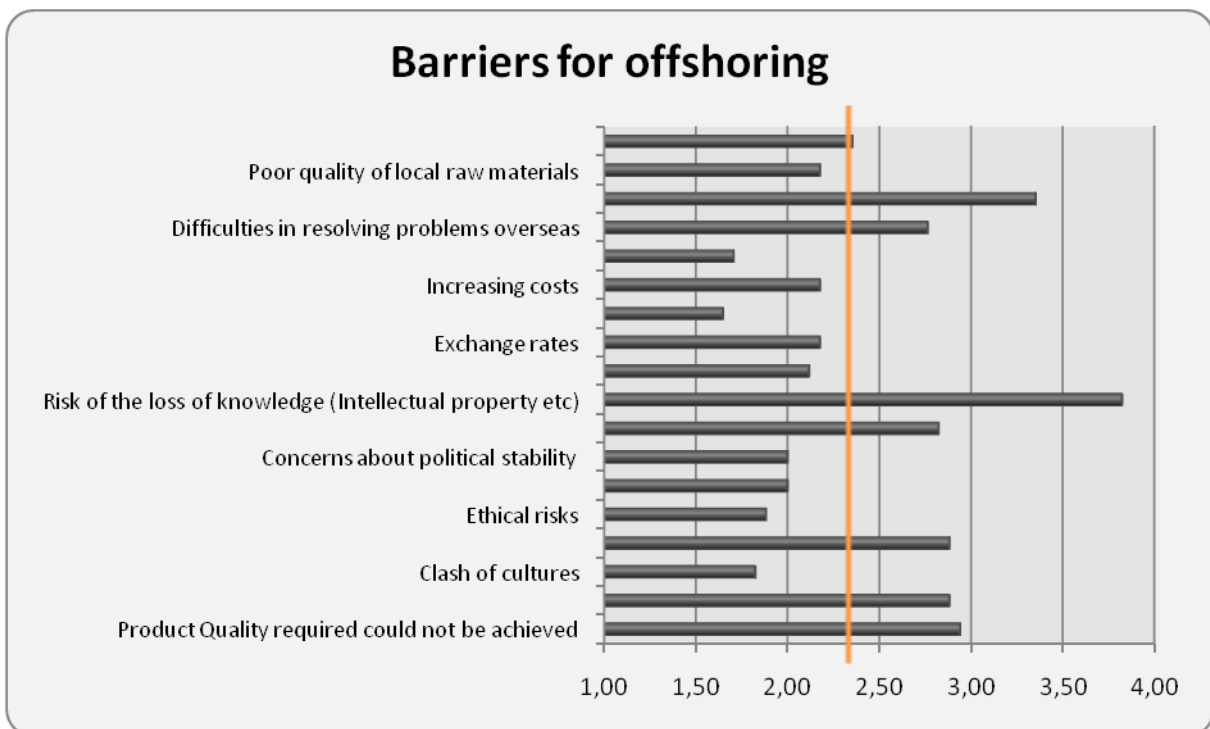


Figure 4 – Barriers to offshoring

The seven factors can be grouped into three main themes; knowledge management, customer relationship management and technical management. The biggest individual concern for the companies surveyed was the potential

loss of intellectual property. Some companies try to mitigate the risk of the decision to offshore to gain cost reductions through keeping the production in-house, even if offshore.

Once a company has decided to operate in the UK, it needs to adopt an effective strategy to meet competition from companies based in low cost countries. To achieve this, companies will need to undertake a detailed evaluation of activities that can remain in the UK, including operations that should be kept in-house, and those which can be outsourced offshore.

Many companies follow a mapping process to determine activities that are, or are not, appropriate for outsourcing. Figure 5 provides an example from one UK Company where all their components from a single business unit were mapped onto the matrix of core vs. competitiveness to help the management assess the potential components for outsourcing which fall into the ‘Buy’ quadrant.

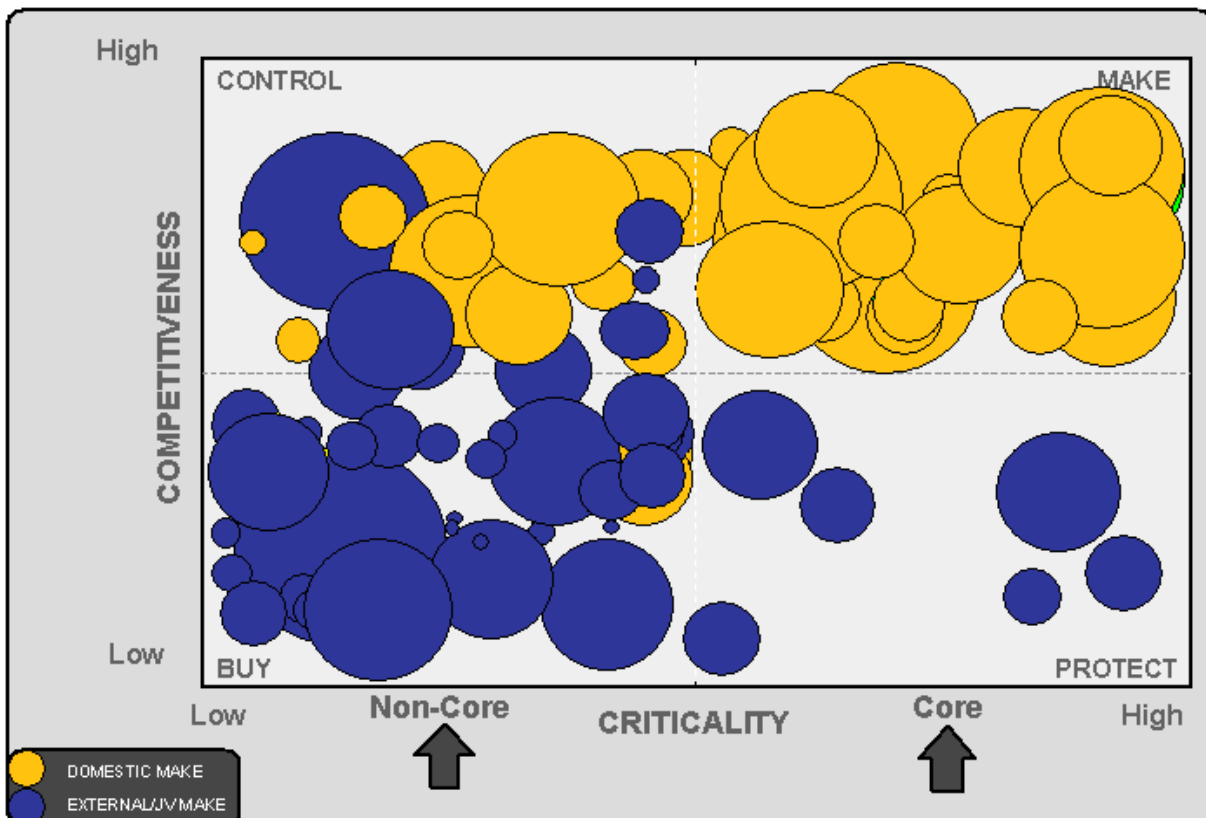


Figure 5 – Make vs. Buy matrix

UK based respondents to the survey were also asked about the type of activities that they would keep in the UK (Fig 6).

Unsurprisingly, core operations emerge as the main activities that are kept in the UK. The core competencies of the company are those which differentiate an organisation from its competition and are key to their long-term survival. Keeping the core competencies in the UK limits the risk of the potential loss of intellectual property rights while helping to maintain the ‘Englishness’ of the organisations’ brand image. Companies will often offshore the production of low value products or the components of their final product and retain the most value adding operations in the UK. This approach is often linked to the decoupling point in the company’s supply chain where they hold strategic stock which allows the company to maintain a high level of customer responsiveness, whilst still managing to gain benefits from a lean upstream supply chain.

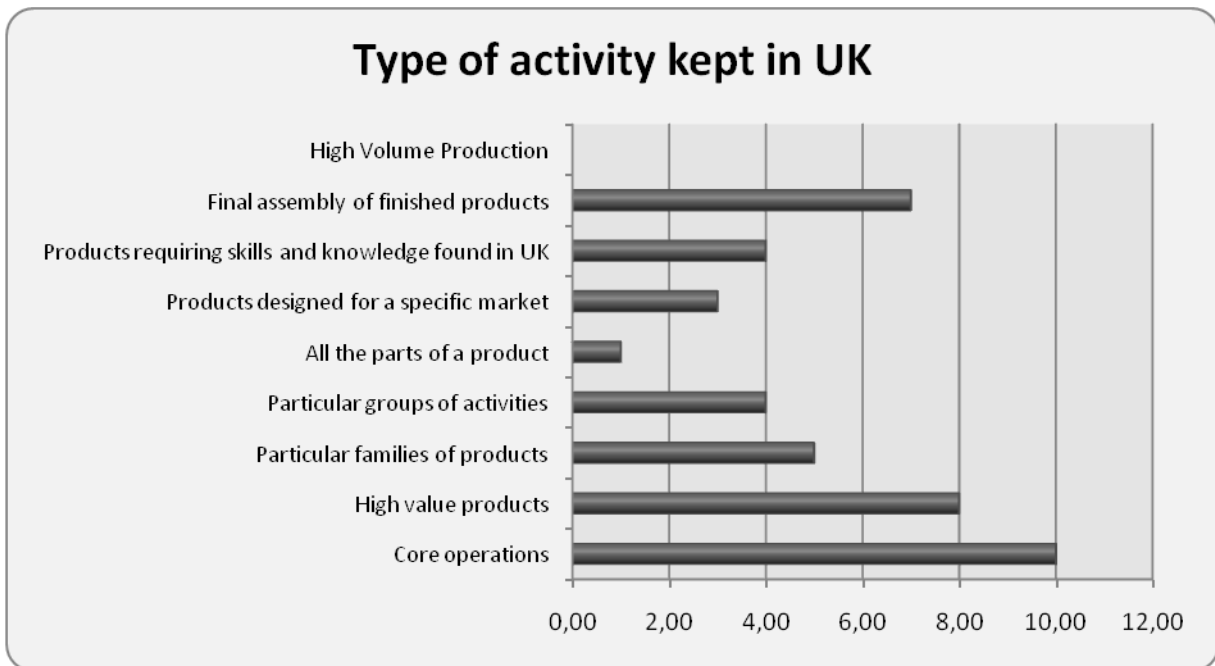


Figure 6 – Core activities to keep in the UK

Based on the survey results, UK based companies are clearly focused on developing strong customer relationships and leveraging their special skills and knowledge base. This is reflected in the other two main activities kept in the

UK: high value products and final assembly of finished products. Companies are directing their strategy towards customer satisfaction by offering high quality products with a high customisation level to satisfy their customers' needs. There is also a strong emphasis on increasing their responsiveness and bundling more services with the products as part of their shift up the value chain.

## **Adoption strategy**

One of the main challenges for a company deciding to operate in the UK is the need to face the harsh competition from companies based in low cost countries which are eroding UK based companies' market share. However, despite being a 'high cost' country, companies operating in the UK are successful and very competitive. This demonstrates that cost reduction is not the only driver for success and that operating in the UK presents other benefits.

In response to these challenges UK companies must find ways to integrate and align themselves with their customers needs to make substitution of the product or service more difficult. UK companies are working on increasing production efficiency, improving quality, maintaining high customer responsiveness and offering highly customised products with a range of services bundled in with the product tailored to the customer needs. Companies need to effectively analyse and understand what drives cost for their products, their current and future market, their process and supply chain and their competitive advantages.

Another challenge faced by UK manufacturing companies comes from the economy itself. The UK has a long and successful industrial history with competitive, creative and successful companies. This history has given companies today a strong knowledge base on which to grow. Today many UK manufacturing companies have been bought by foreign companies and the sourcing decision is often no longer influenced by a local regional commitment. If these foreign-owned companies continue to move their core activities out of the UK then the impact on the UK skill base will be significant and eventually limit the evolution of skilled labour in the UK.

'Access to skilled labour and knowledge' was highlighted in the survey as one of the main drivers for operating in the UK. Certainly skilled labour will demand higher wages but the benefits derived in terms of productivity and higher quality could justify the higher price.

Another advantage to keeping core operations in the UK is that supply chains are less complex and the management of the information flow and management of problems is simpler. Improving the efficiency of the supply chain has also been found as one of the key concerns of the surveyed

companies. An efficient supply chain will help improve the responsiveness of the company, limit its costs and increase the quality of the products. Furthermore, an efficient supply chain will be able to offer greater and better services to its customers. This strategy supports the trend of bundling services with the product resulting in a unique offering in the marketplace. This strategy is well illustrated by the Rolls-Royce Totalcare® strategy which focuses less on selling an engine but rather the time in service by the engine, which Rolls-Royce manages for the customer.

The results of this research demonstrated that operating in the UK brings significant advantages to companies in terms of economic and political stability, supply chain and management efficiency and finally access to skilled labour and knowledge. One of the most common drivers for choosing to operate in the UK is related to a focus on customer satisfaction. Thus a company will decide not to offshore those core activities which provide it with the capability to be more responsive to its customers and to offer better services in the marketplace.

## References

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