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The Incredible Shrinking Inventory

By: Brittany Glenn

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A growing problem has plagued the industry for the past couple of years: Suppliers are unable to fill orders in a timely way due to lack of inventory. This puts distributors in a tricky position with clients who expect their in-hands deadlines to be met.

What's causing these inventory shortages? Why aren't suppliers' products in stock? Moreover, how can both suppliers and distributors resolve the issues related to this problem?

As vice president of sales for Newton, Iowa-based distributor The Vernon Company (UPIC: Vernon), David Regan, CAS, is acutely aware of the lack-of-inventory problem. "This is the No. 1 issue our customer service people are dealing with right now," Regan says. "It is absolutely a critical issue for us because it's happening a lot more than it ever used to. In the last six months, it has gotten dramatically worse. It is a real issue."

Craig Nadel, CAS, CEO of Culver City, California-based distributor Jack Nadel International (UPIC: NADELINC), agrees. "There is no question it has been a problem," says Nadel. "It's been a much worse problem over the past year or so than it has in my entire tenure in the industry."

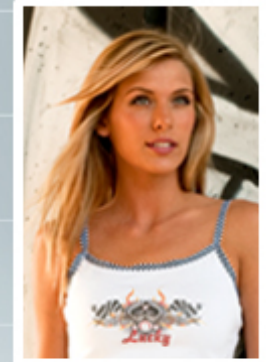
Suppliers are only too aware of the situation. "I hear a lot of distributors talking about this problem, and they are super-frustrated," says Charley Johnson, CAS, executive vice president for Salt Lake City-based supplier SnugZ USA (UPIC: SNUGZUSA). "These distributors are wasting a ton of time sourcing new vendors for these products. We have had very few out-of-stock issues since we do a lot of our stuff here in the USA."

Delays can last as long as several months, Regan says. "Sometimes things are coming in and the next thing you know, they didn't make that boat, they're coming on the next boat," he says. "Then they made that boat, but the supplier did a quality control analysis and [the products] were all rejected. This can go on for a couple of months."

Meanwhile, a distributor's relationship with his or her client often hangs in the balance. "The worst-case scenario is you let a customer down and you lose an account," Regan says. "You could also lose the order but somehow manage to keep the customer. The third scenario is you miss in-hands dates. The bottom line for us as distributors is how are we going to resolve this?"

Trouble In Paradise

The common thread among suppliers who are experiencing inventory shortages is the fact that they import products from China. American retailers have long taken advantage of China's large



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population, low labor costs and strong infrastructure. However, what was once a marriage made in heaven is now showing signs of trouble.

In recent years, American suppliers who import from China have had to contend with a host of problems, including cost increases, delayed production and shipping timelines, and shipping and container shortages. Although a divorce is not necessarily in the cards, the changes in China have required American suppliers to adjust quickly to this new reality.

"It all started with the economy downturn in 2008, which overflowed into 2009," explains Russ Rowan Mogell, CEO of West Berlin, New Jersey-based supplier Seven Sourcing (UPIC: Seven). "The downturn led to a sharp drop in demand for Chinese goods, which resulted in many factories closing their doors. Smaller factories that were already being pinched by rising costs of labor, transportation and raw materials—as well as by the appreciating RMB [Chinese yuan] and reduction in the value-added tax—are closing en masse.

"I would say more than 100,000 factories have closed in China over the past year and a half," Mogell says. "It's a scramble to find factories that can produce products and ship products on time. Furthermore, the factories that are operating are extending production times out and even turning away low-profit promotional orders for more profitable retail orders."

Caro Krissman, president of Inglewood, California, supplier Source Abroad, Inc. (UPIC: sourcea), offers further perspective into the cause of the inventory shortage. "When freight space became very tight at the beginning of the summer, many large retail players took the safe position to buy further in advance and buy more in anticipation of longer lead times so as not to be out of inventory or pressured for holiday orders. This then caused factories to be busier before the traditional peak season."

Larger suppliers have an advantage over smaller ones due to the sheer volume of their orders, Mogell says. "It's very simple that you take care of the people that take care of you," he says. "Basically it comes down to volume."

But even large industry suppliers are experiencing challenges.

"We, like everyone else, have seen some changes," says Quenton Wentworth, vice president and general manager, North America of Clearwater, Florida-based supplier Norwood/BIC Graphic North America (UPIC: BIC). "The time it takes to get the products has changed dramatically. What's also changed is the amount of information we get on where the products are in transit."

However, BIC's acquisition of Norwood Promotional Products in July 2009 translated into more purchasing power overseas for the company.

"We've consolidated our operations in Asia for both BIC and Norwood as well as for our global business," Wentworth says. "This has enabled us to speak to the manufacturers with one voice and greater buying power. While we definitely have had our issues, we've been able to offset these by the breadth of our purchasing power as we've integrated the two companies."

Even so, Wentworth cites labor shortages as one of the problems with which Norwood/BIC has had to contend. "The organization that we've got over there has told us there was definitely an increase of employees who stayed home after the Chinese New Year," he says. "They've also told us that there's been an increase in salary expectations there."

Mogell agrees: "We're seeing a shift in the workforce toward more higher-end type products, which can afford higher salaries," he says.



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Jeff Lederer, executive vice president for Bridgeport, Connecticut-based supplier Prime Resources Corp. (UPIC: PRIME), also cites labor shortages as one of the problems in China that has caused production delays.

"We at Prime have spent a lot of time in China understanding the issues about longer production times," Lederer says. "Workers from factories were slow to come back after the Chinese New Year. We knew that would happen, so we beefed up on inventory and continued that throughout the year."

Krissman explains that the new labor pool gets smaller all the time as the Chinese population ages and younger workers are less inclined to work in factories.

"All of this is on top of the fact that industry suppliers are being squeezed for cash and holding lower inventory levels because they feel large orders will circumvent them," he adds. "It makes the chain challenging."

Slow Boat From China

Aside from factory production delays, another problem that suppliers who import from China are contending with is shipping and container issues.

"If China is exporting less, that means that freight and shipping lines are not shipping as frequently as they once were," Mogell explains. "So they are playing games in the sense that they're creating this faux lack of surplus as far as their shipping vessels. They actually have these vessels docked, creating the effect that they don't have the boats. But they really do have the boats."

"Suppliers are now paying 20 percent more to get their orders on containers and shipped on time," Mogell says. "Shipping vessels are also cruising at slower speeds to save on fuel, which affects delivery times by up to 10 days."

As distributors, both Nadel and Regan have received reports from importing suppliers that shipping and container issues are slowing down delivery dates. "Some of these freight companies are shipping the slow boats more often," Nadel says. "Ships used to take three or four weeks to cross the ocean. Now they're taking an extra week or two because they're saving on fuel."

"We've received e-mails from several suppliers telling us that now there aren't as many boats coming over, so they're fighting for a spot to get their stuff on the next boat coming over," Regan says. "There's more demand for less shipping space."

Even Norwood/BIC has had shipping/container difficulties. "Getting the products onto a ship and in a container can be challenging," Wentworth says. "We just got a shipment of products that have been backordered that we thought we would have had a month ago. So we're definitely experiencing delays of shipments."

Lederer says in addition to all these issues, what also slows things down is the compliance factor and product testing requirements. "We have a huge testing program in place," he says. "That is an area where we've spent considerable time and resources."

Shortage Solutions

Both distributors and suppliers have found ways to manage the inventory shortage problem.

Regan advises industry distributors to build relationships with a select group of suppliers they can trust. "If you're a distributor today, you need to try to focus your business on a smaller group of

suppliers in which you have a greater trust," he says.

"At Vernon, we have a list of 85 key supplier partners," Regan continues. "They tend to be proactive as far as telling us about stock shortages. And, if there is an outage, they tend to be very good about how they handle it. Our salespeople can sell any lines they want to sell, but we're trying to reinforce that they stick with the preferred key suppliers. This way, we reduce the chances of being affected by inventory problems."

Nadel urges distributors to call ahead before they place the order to ensure products are in stock. "Check with inventory when you can," Nadel says. "Especially when you have something that's a little unusual, check with the supplier to see if they have the inventory. Make sure that it's there."

Regan, too, says Vernon salespeople call ahead of time to ensure inventory is in stock. "However, that's not a foolproof method either because the facts change every single day," he says.

When it comes to stock shortages, Regan believes what separates the wheat from the chaff is how suppliers handle the issue when it arises. "There's a big difference between saying 'We're out of stock, sorry, we can't process your order' and being proactive and offering us some options to take to the customer," Regan says. "We have customers at stake, we have orders at stake. Suppliers have a lot at stake on how they handle the issue."

As in any relationship, open communication is the key. "To the extent that you have open communication, you can minimize the problems," Regan says. "Sometimes out of bad situations like these a distributor or a supplier can really show what they're worth with respect to offering up solutions and showing that they care. You might have a bad situation, but be empathetic about it and offer up some solutions."

Another way suppliers can be proactive in this situation, Regan says, is to show real-time inventory on their websites. "The more suppliers have real-time inventories that we can view prior to placing the order, the better off we would be," he adds.

Prime Resources is proactively addressing the situation in much the way Regan describes.

"At Prime, we have a program where if we're out of stock on something or there's a timing issue, we will try to upgrade a customer to either a similar item or one of greater value," Lederer says. "We always give distributors solutions to these situations. We, at times, have spent money on air shipments just to satisfy customers at our expense."

Prime is one of the industry suppliers that provides real-time inventory on its website. "On our website, distributors can check inventory at any time," Lederer says. "You can even search by category based on the inventory that you're looking for or price point. This is really an intuitive way to give distributors the information they're looking for."

In response to the challenges distributors currently face finding available inventory, Norwood/BIC recently introduced its Always In Stock program, which features 180 popular products that are always in stock—because they're manufactured in the U.S.

"We can guarantee inventory on 90 of our BIC pens because we manufacture them right here in the United States," Wentworth says. "And we can guarantee 90 calendars in stock until December 31, 2010. So any issues we have with sourcing products from Asia don't affect those 180 products we make here in the United States.

"We're uniquely positioned in that we manufacture both our BIC pens and our Norwood calendars

in the United States," Wentworth adds. "This gives us a competitive advantage because people are having issues supplying products that they source from Asia. Being made in America gives us a quality advantage and gives us an advantage of being in stock."

Krissman, who manages the importing process as an overseas partner for industry distributors, is also realistic about the challenges. "Importing has more hurdles than before. Planning, staying ahead of the curve and having staff in China who are working with factories to keep production space available are more important than ever," he adds.

American Advantage

Mel Ellis, president of Portland, Oregon-based supplier Humphrey Line (UPIC: HUMPHREY), also believes his company is uniquely positioned in the industry because Humphrey Line makes all of its products in the U.S.

"We make our products in a factory in Kentucky," Ellis says. "It's called onshoring. It's a new word. We have injection molding and blow molding and all kinds of decorating capabilities. We make our own labels. We are a very integrated manufacturer in a tightly defined set of products."

In 2009, while many industry suppliers were struggling to stay in business due to the downturn, Ellis reports that business was booming. "Last year was a record year for us, out of all our years in business," he says. "That was because when the swine flu came through, we were able to make and ship all the hand sanitizer that the market needed. But the importers ran out of product two weeks into it. So all we had to do was increase capacity, which we were happy to do."

Humphrey Line has shipped more than 99 percent of its orders complete and on time for the last 16 years, Ellis says. "See, if you control your schedule then it's not that complicated," Ellis says. "But if you don't control your schedule you're reduced to guessing five months out what it is you're going to sell and how many of them."

What about the cost of labor in the U.S. as compared to China? "We have micro-processor-controlled equipment that we can use in lieu of labor." Ellis explains. So where you can make the product with capital equipment versus labor in some manufacturing processes you can match the Chinese cost level."

Ellis says domestic suppliers have two advantages over importers. "One is we never run out of inventory," he says. "The other one is if your raw materials are domestically made, then you know what's in them with regard to compliance and testing."

Ellis believes relying on offshore suppliers opens importers to exogenous risks related to materials, lead times, currency fluctuations, political instability, strikes and more.

"Being a domestic manufacturer competing against importers gives us an unfair advantage these days," Ellis says. "It's a great time to be an American manufacturer."

Brittany Glenn writes about current issues, trends and the economy for consumer and business-to-business magazines. She is a former associate editor of PPB magazine.

Inventory Innovators

The following suppliers are just some of those which have created online systems that allow distributors to check inventory before placing an order. Check with your suppliers to see if such systems are available on their websites.

Bodek and Rhodes (UPIC: ULTRACLB), www.bodekandrhodes.com

Gemline (UPIC: GEMLINE), www.gemline.com

Leed's (UPIC: LEEDS), www.leedsworld.com

Logomark (UPIC: logomark), www.logomark.com

Prime Resources Corp. (UPIC: PRIME), www.primeline.com

Sourcing Options

The most obvious solution to inventory shortage problems is for suppliers to take their manufacturing business to countries other than China. This is exactly what some suppliers ought to think about doing, says Russ Rowan Mogell, CEO of West Berlin, New Jersey-based supplier Seven Sourcing (UPIC: Seven).

"Suppliers are looking at other countries—Mexico, Vietnam, Sri Lanka—some manufacturing is now shifting to those countries," Mogell says. "I think it's smart to always look at alternate sources just in case there are issues in the primary country that you're working with. India is another market suppliers should be looking at as well as a good portion of Southeast Asia.

"I think it's important to keep your options open as far as product sourcing," Mogell says. "Loyalty is important, but I think you also need to protect your business. As prices go up and as production times go out, you need options. You can't fight the labor shortages—you really don't have any say in that. And you're pretty much forced to do what the shipping lines want."

However, this is easier said than done. "To create an infrastructure like China has created takes so many years," says Jeff Lederer, executive vice president for Bridgeport, Connecticut-based supplier Prime Resources Corp. (UPIC: PRIME). "To create an infrastructure with shipping ports and the testing knowledge and the manufacturing, it's not insignificant. Vietnam is trying a bit, and also Malaysia. But China is a major hub for manufacturing, and that's not going to change anytime soon. They have the infrastructure required to deal with any type of manufacturing en masse."

Even Mogell admits he doesn't see much business shifting away from China in the near future. "China's infrastructure is much better than say Pakistan or even Sri Lanka," he adds. "China is very streamlined. They know what they're doing. There's no government unrest. I won't work with any country that's unstable."

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