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Media Kit

RIMS| back to This week's issue

Supply chain management calls for close look at risks

by RODD ZOLKOS

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NEW ORLEANS-Although companies have benefited from efficient approaches, such as the use of just-in-time inventories, lurking within those supply chains are numerous critical risks that must be managed.

And, according to Craig Holmes, director of business continuity planning at Aon Risk Consultants Inc. in Southfield, Mich., it's important for risk managers to recognize that supply chains extend well beyond component flow processes, taking in other aspects of business, such as outsourcing.

Although many companies do manage the risks they face in many aspects of their supply chains, they often fail to consider the quality of risks at outsourced locations, he said.

Speaking on a panel discussing supply chain risk earlier this month at the annual conference of the Risk & Insurance Management Society Inc. in New Orleans, Mr. Holmes said, "supply chain risk management is operations risk management."

"It's like the rest of insurance," said another panelist, Steven P. Harris, vp at ABS Consulting in Oakland, Calif. "There are many factors and many perils that supply chains can be subjected to."

Mr. Holmes noted that though the degree of supply chain risk varies greatly with a company's particular situation, there are some common elements.

"I urge all risk managers to really go out and find where the single points of failure are," he said. Also, supply chain risk is "generally operational in nature, so you've got to go out and talk to the operations people," Mr. Holmes said.

Another panelist, John J. Marren, risk manager at Firmenich Inc. in Princeton, N.J., said that in the current marketplace, insurers are giving increased scrutiny to supply chain exposures.

"The insurers are also telling us there's limited reinsurance for this, so they're not able to or willing to provide us with the amount of coverage they could in the past," said Mr. Marren, who moderated the session.

Still, although it is the policyholder's responsibility to plan for contingencies and to identify contingent relationships, "what we're hearing is a lot of insureds aren't spending the time on this or even know how to tackle it to start with," Mr. Marren said.

Companies need to consider how much inventory they should maintain to continue production in the face of a supply chain interruption, the risk manager said. They also must contemplate how their customers will respond, he added.

"The bottom line is, if I don't respond to my customers' needs, my competition most likely will," he said.

"Contingency planning at suppliers is key," added Mr. Holmes. "The thing that we try to get risk managers to take a look at are risk factors associated with suppliers."

Companies should identify multiple sources for critical raw materials and equipment, Mr. Marren said, and should maintain contingency plans for obtaining needed supplies and services. They also should enter into agreements with key suppliers that provide incentives for those companies to maintain their own contingency plans.

"You need to recognize that your profitability is dependent on maintaining a high-quality, dependable supply chain," he said.

Companies also must be aware of risks associated with their customers, according to Mr. Marren, even though "as a supplier, you're kind of at your customers' mercy to manage their own risks," he said.

A company must be able to respond to a customer's needs in any situation to maintain business relationships and reputation. It also must have contingency plans to ensure that it can deliver products and should probably identify alternative sources for its product, if possible, in order to maintain the company's reputation.

Mr. Harris suggested that risk managers assessing their companies' supply chain risks start with a risk profiling process that identifies potential supply failure scenarios, their likelihood and the potential consequences. From there, a company could choose to move to more detailed quantitative risk modeling that allows a company to simulate supply chain interruptions to study their impact.

The process can offer a variety of benefits, Mr. Marren said.

"You're obviously demonstrating a commitment to your customer by going through this process," he said. "It's also important to your insurers and to your management."

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