

**INTERNATIONAL SUPPLY CHAIN
MANAGEMENT – BSB20123-7**

**Written Examination Stimulus Material
Case Study – IKEA**



About IKEA

Since its 1943 founding in Sweden, IKEA has offered home furnishings and accessories of good design and function at low prices so the majority of the people can afford them.

IKEA's vision is to: *"Create a better everyday life for the many people"*

Its business idea is *"To offer a wide range of well designed, functional home furnishing products at prices so low that as many people as possible will be able to afford them"*

The IKEA concept is based on their market positioning statement *"Your partner in better living. We do our part, you do yours. Together we save money"* and focuses on a commitment to product design, consumer value and clever solutions. By using inexpensive materials in a novel way and minimising production, distribution and retail costs, their customers benefit from low prices.

IKEA has more than 590 million visitors per year to its stores all over the world. In addition to the visitors in the stores, some 450 million visitors are tracked entering the IKEA website. IKEA's main marketing channel is its catalogue that is distributed world-wide as 191 million copies (in 56 different editions and 27 different languages) displaying some of IKEA's 9,500 different products.

Sales for the IKEA Group for the financial year 2009 increased by 1.4 per cent to a total of 21.5 billion Euros. At the end of the 2009 financial year, there were 267 IKEA Group stores in 25 countries stocking everything for home furnishing under one roof. In 2007 the European market constituted 82% of sales, followed by North America with 15% and Asia/Australia with 3%.

The IKEA Group has 123,000 co-workers spread across functions such as purchasing, distribution, whole-sale, range, retail, support functions and the Swedwood Group (see below for further details).

Today IKEA's product range consists of 9,500 home furnishing articles, designed to be functional and good looking but at a low price. Each item is developed by IKEA of Sweden, which is also responsible for giving each product its unique name, such as BILLY and KLIPPAN. The company designs its own furniture, which is made by about 1,220 suppliers in more than 55 countries. IKEA has 31 trading service offices in 26 countries so production can be monitored, new ideas tested, prices negotiated and quality checked while an eye is kept on social and working conditions.

Furniture is also sourced through Swedwood, an IKEA-owned manufacturer of wood-based furniture and components. However, third party suppliers provide the bulk of the company's inventory, in line with its beliefs in flexibility and its strategy of limiting investment in productive capacity.

IKEA incorporates environmentally friendly efforts into day-to-day business and continuously supports initiatives that benefit causes such as children and the environment. To cut transportation costs, IKEA uses flat packaging; customers assemble the products at home.

IKEA's supply chain has a global spread with growing sales and purchasing in all major regions of the world. What makes its supply chain really complex is that its stores are spread across many countries, that it has 1220 suppliers in 55 different countries making its furniture and that the stores are supplied from 31 central distribution centres in 16 different countries or directly from suppliers. In some cases, an IKEA store opening is a national event, with people sometimes travelling hundreds of kilometres to shop there

IKEA products are manufactured all over the world

When IKEA sources suppliers to manufacture IKEA products, the aim is to find those who can produce products of good function and design at the lowest possible price (although not at *any* price). Some of these, in the Swedish forests around the birthplace of IKEA, have been working with IKEA since its earliest days. Others have their production plants in China, Poland or Germany. But no matter where in the world its suppliers are, IKEA is always committed to long-term cooperation and does its best to cultivate close and cordial relations. IKEA buys production capacity rather than product quantities. In other words, they order 10,000 hours of production from their suppliers rather than 10,000 bookcases.

Local offices near to the suppliers

The operative purchasing work is divided up among four trading agents, supported by 31 trading service offices in 26 countries. This means that IKEA is always close to its suppliers, which is one way of creating good business relations between the companies involved. The trading service office's employees can make frequent visits to suppliers and follow the production process closely, enabling new ideas to be tested and regular quality controls to be made. They are also responsible for the important task of monitoring

working conditions, social conditions and the external environment around the factories, and for checking that these are constantly being improved in accordance with the code of conduct in The IKEA Way on Purchasing Home Furnishing Products (see Appendix 1). The suppliers, in turn, can have confidence and faith in IKEA. While IKEA know they are a demanding customer, they also feel that they are fair, professional and honest in their dealings.

China – number one on the IKEA purchasing list

Today the majority of IKEA products (66%) are purchased from manufacturers in Europe. However, the largest single country for purchasing is China.

Top 5 purchase countries

- China 18%
- Poland 12%
- Sweden 9%
- Italy 7%
- Germany 6%

As a rule, best-selling products are manufactured by a number of different suppliers. Optimising production potential and concentrating volumes are essential in order to achieve low prices. Thanks to the fact that the IKEA range is the same all over the world, large volumes can be ordered. IKEA has developed a variety of tools to help its purchasers to find the best suppliers. Competition is a natural part of this work. But so, too, is cooperation and collaboration. IKEA also purchases raw materials and hardware in bulk, which it then sells to IKEA suppliers.

Long-term agreements give lower prices

Bigger volumes mean lower prices. And the aim is for the already low prices to become even lower still. To make this feasible, IKEA signs long-term contracts with its suppliers. This enables them to make the necessary investments and to ensure the supply of raw materials over a long period of time. In certain instances, IKEA may also support suppliers by providing financial assistance. This creates unique business opportunities, enabling IKEA to continue to offer a wide range of well-designed, functional home furnishing products at prices so low that as many people as possible are able to afford them.

Currently IKEA plans to open 10-20 new stores every year with a goal to double sales within the next five years. Considering the pace of growth in sales, the many stores and warehouses, and the fact that some business areas change up to 30% of its assortment every year, supply chain planning is a real challenge. The supply chain needs tight control and high levels of visibility to keep costs down and avoid obsolete inventory and/or stock outs.

The IKEA supply chain is mainly make-to-stock (MTS) and only a few products are made to customer orders. Consequently, the entire supply chain is heavily dependent on forecasts. The regions and the stores have traditionally had a strong power and a high degree of local freedom in terms of planning and placing replenishment requests. This has led to a fragmented supply chain planning with local optimization and a lot of manual intervention with plans throughout the supply chain. Furthermore, due to frequent shortage situations some regions have purposely overestimated demand to ensure delivery, which in turn has led to imbalance in terms of demand coverage.

Hence, some markets have suffered from stock outs during long periods, whereas other markets have ended up with obsolete inventories. Forecasting has been done on a regional level with approximately 120 users striving for different goals and using different methods. Part of the explanation for this is that IKEA has lacked a common and structured tactical planning of demand and replenishment. In terms of capacity planning, all different parts of the supply chain (stores, warehouses, regions, etc.) tried to optimize their own part of the supply chain, leading to a set of imbalanced supply plans with a low and unstable total throughput with long replenishment times for the supply chain as a whole.

To overcome the difficult situation, IKEA initiated a program (a group of projects) aiming to taking better control of its supply chain, and enhance performance in terms of delivery service and costs. A new global planning concept was developed and is currently being implemented. Its cornerstones are mutually integrated planning processes, a centralized planning organization, a focus on data quality and use of advanced software support.

Distribution

From supplier to store

For IKEA, distribution is an important part of the equation of creating home furnishing articles at prices which are as low as possible. Approximately 9,500 IKEA products are manufactured by suppliers and transported to IKEA stores around the world, often via one of the company's central warehouses and distribution centres. At IKEA, distribution is all about making the route from the manufacturer to the customer as short as possible.

In the early days of IKEA, the "warehouse" was a shed on Elmtaryd Farm in the south of Sweden where the founder of the company, Ingvar Kamprad, lived with his parents. In those days products were despatched from Elmatryd with the help of the county milk van that visited the farm each day. Things have changed a bit since then, however. Today IKEA operates 31 distribution centres in a total of 16 countries. From here IKEA products are delivered to stores around the world.

Large volumes + flat packs = low costs

IKEA works in various ways not only to rationalise and simplify distribution, but also to minimise the impact this part of the business has on the environment. The secret is to calculate as exactly as possible how many products will be needed to satisfy demand. This eliminates any unnecessary costs for production and warehousing.

The hallmarks of IKEA distribution are:

- a global distribution network
- large volumes
- flat packages
- low costs

The aim, of course, is to make sure that the right products are always available at the store when the customers wish to buy them.

Better efficiency means lower prices

The fact that IKEA products are sold packed flat means that they can be transported with greater efficiency. By minimising “wasted space” it is possible to transport and store more packages at a time. And by increasing what is known as “the filling rate” in containers etc (in other words, reducing the amount of wasted space), the cost of transporting each item goes down. One good example of this is HOTT kettle. Making better use of the available space by stacking some of the kettles upside down makes it possible to fit ten kettles into a box instead of just six. As a result, less packaging materials are needed and distribution costs are kept lower.

More deliveries by rail in future

Today 60 percent of all IKEA freight is transported by road, 20 percent by rail and 20 percent by sea. Less than one percent is air freighted. The aim is to constantly increase the proportion of goods transported by rail. Within the next three years 40 percent of all IKEA freight within Europe will be moved by rail.

For some years now, all the freight companies working with IKEA have been required to provide statistics for an “Environmental Performance Sheet” that details how their operations impact on the environment. This enables IKEA to keep a check on these companies’ environmental work and to monitor what measures they are introducing to reduce the use of fuel and minimise emissions.

Sustainability

Ask IKEA spokesperson Mona Liss a question about IKEA’s sustainability efforts, and the response takes a moment. It’s not because Liss doesn’t know her company inside and out, it’s because IKEA has been doing so much for so long to promote sustainability, there is an encyclopaedia worth of information on the particular details of the topic.

"We've had many of these programs in place all the way back to the 1990s," Liss said. "And even before these specific programs, it's something we've been conscious of as a company for a long time. It's not something we just decided to implement in the last few years."

It was in 1990 that IKEA decided to transform its conscious efforts into a sustainability action plan. Adopted in 1992, the Environmental Action Plan included 10 key initiatives:

1. Replace polyvinylchloride (PVC) in wallpapers, home textiles, shower curtains, lampshades, and furniture
2. Minimize the use of formaldehyde in its products, including textiles
3. Eliminate acid-curing lacquers
4. Produce a model of chair (OGLA) made from 100% pre-consumer plastic waste
5. Introduce a series of air-inflatable furniture products into the product line to reduce the use of raw materials and transportation weight and volume
6. Reduce the use of chromium for metal surface treatment
7. Limit the use of substances such as cadmium, lead, PCB, PCP, and AZO pigments
8. Use wood from responsibly managed forests that replant and maintain biological diversity
9. Use only recyclable materials for flat packaging and "pure" (non-mixed) materials for packaging to assist in recycling
10. Introduce rental bicycles with trailers for customers in Denmark

After working on these initiatives for nearly 16 years IKEA has made substantial progress and become a place where consumers can confidently buy products sourced, manufactured, packaged, shipped, and sold in an environmentally friendly way.

IWAY (Appendix 1) or the highway

For furniture makers, wood is everything. But in a world where deforestation has become a hot-button topic, it can also be a source of frustration. Where did the wood come from? Are forests in that region responsibly managed? If so, how can that be proved?

"It's difficult to do, but it's also critical," Liss said. "Our long-term goal is to source all of the wood used in our products from forests certified as responsibly managed."

To guide that effort, IKEA created the IWAY code of conduct—minimum requirements suppliers must meet in order to do business with the company. According to IWAY's environmental and forestry standards, suppliers must agree to: work to reduce waste and emissions to air, ground and water; handle chemicals in a safe way; dispose of hazardous materials in a safe manner; contribute to the recycling and reuse of products; use wood from known areas and, if possible, certified as responsibly managed.

To help spread the word and aid suppliers in meeting IWAY standards, IKEA

created a network of Trading Service Offices. The offices train, support, and monitor suppliers to ensure compliance.

“We also have our own forest specialists,” Liss said. “These staff members spread knowledge about forest management and help us trace wood back to its origins to verify our IKEA wood requirements are met throughout the entire supply chain.”

Beyond the training and monitoring, IKEA also conducts regular surveys of its suppliers and audits them on a regular basis. While its goals are lofty and standards strict, IKEA understands most suppliers won’t meet all of IWAY’s rules without a little help. That’s why the company created a four-level staircase model (Appendix 2) of its requirements that suppliers can work on over time.

Liss said the company’s goal is to have 100% of its suppliers at the minimum Level 1 requirements by 2009 and 30% at the highest requirements of Level 4 shortly after.

Help from my friends

Going it alone is never easy, and in working with wood suppliers around the world to promote sustainable forestry, IKEA has had more than a little help from its friends.

Through partnerships with organizations including the World Wildlife Foundation (WWF) and the Rainforest Alliance, the company has armed itself to better tackle problems like illegal logging and lack of Forest Stewardship Council (FSC) certification. Projects are currently underway in Laos, Cambodia, Vietnam, Russia, China, Romania, Bulgaria, Ukraine, Latvia, and Lithuania, and to date, more than 5,000 individuals have been trained in topics related to sustainable forest management and certification. In China alone, more than 1.8 million acres of forest have become FSC certified under IKEA’s program.

“One of the most encouraging stats we’ve seen is in the number of wood supply chain audits we conducted last year,” Liss said. “That number decreased from 90 audits to 50 audits. It’s a good thing because it means more suppliers are meeting our documentation requirements and proving their wood comes from the right places.”

Beyond the trees

IKEA’s aggressive effort to use sustainable, responsible materials in its products is just the first step in a long line of green initiatives.

From the initial design stage through the product’s life cycle, IKEA designers, product developers, and technicians consider all safety, quality, and environmental aspects. As a result, all of the company’s home furnishing products are comprised of 71% renewable material and include as much recyclable material as possible.

When these environmentally friendly products are produced, IKEA works with its manufacturers to ensure safety, efficiency, and sustainability are top goals. Those products are then shipped using IKEA's well-known flat pack strategy. The "assembly required" products are shipped in smaller and fewer containers, allowing the company to get more boxes in vehicles, thus reducing trips, energy use, and emissions. IKEA takes it a step further by making sure optimal loading techniques are used, vehicles run on cleaner fuels, and more fuel-efficient driving practices are followed. To top it all off, only recyclable materials are used for flat packaging.

The result of IKEA's supply chain initiatives is end products consumers can confidently label as "green." It's impressive when you consider supply chain is just one piece of the company's comprehensive environmental strategy, just ask Mona Liss.

"We do so much, it's hard to keep track of it all," she said with a laugh. "But it's well worth the effort, and it allows us to deliver the brand message that we truly are a green company."

SOURCES:

The material contained in this case study has been taken either directly or indirectly from the following sources, with the overall document edited and collated by Stephen Kelly (March 2010).

Bartlett, C., Dessain, V. & Sjoman, A. (2006), *IKEA's Global Sourcing Challenge: Indian Rugs and Child Labor (B)*. Harvard Business School Publishing.

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This document is intended as a stimulus for discussion and not to illustrate either effective or ineffective handling of a business situation.

Appendix 1 – THE IKEA WAY ON PURCHASING HOME FURNISHING PRODUCTS

1. Our Code of Conduct

This document “The IKEA Way on Purchasing Home Furnishing Products” is our *Code of Conduct* in our relation with suppliers of products for the IKEA range. The *Code of Conduct* is our minimum requirements on Social & Working conditions and Environment.

It has been established in order to make the IKEA position clear to suppliers and their co-workers, as well as any other parties.

It is based on the eight core conventions defined in the Fundamental Principles of Rights at Work, ILO declaration June 1998 and the Rio Declaration on Sustainable Development 1992.

Further IKEA recognises the Fundamental Principles of Human Rights, laid down by the “Universal Declaration of Human Rights” (United Nations 1948).

We believe that our daily business has an impact on Environmental and Human Right issues, in particular, in relation to people's working and living conditions.

A complete specification of our minimum requirements is stated in the IWAY Standard document.

2. The IKEA Concept in a Nutshell

Our Vision

To create a better everyday life for the many people.

Our Business idea

We shall offer a wide range of well-designed, functional home furnishing products at prices so low that as many people as possible will be able to afford them.

This shall be achieved through a rational product range development and by adapting product design to production conditions.

A rational distribution idea in combination with a caring meeting with the many people.

A strict cost-consciousness in all areas.

3. Customers and Suppliers in Focus

We have decided once and for all to side with the many. This is an objective that carries obligations.

We want to offer our customers low prices for well-designed and functional home furnishing products of good quality, manufactured under acceptable working conditions by suppliers that care for the environment.

IKEA is a production-oriented retailing company. We strive to build long-term relationships with suppliers that share our commitment to promote good practices, and who want to grow and develop together with IKEA.

Suppliers can expect from IKEA:

- to be reliable,
- to adapt our products to production,
- to contribute to efficient production,
- to care for the environment,
- to support material- and energy saving techniques,
- to take a clear standpoint on working conditions,
- to respect different cultures,
- to have clear and mutually agreed commercial terms.

4. Producing for IKEA Includes the Following Requirements

Legal Requirements

Suppliers *must* comply with national laws and regulations and with international conventions concerning Social & Working Conditions, Child Labour and the protection of the Environment.

Social & Working Conditions

IKEA expects its suppliers to respect fundamental human rights, to treat their workforce fairly and with respect.

Suppliers must:

- provide a healthy and safe working environment,
- pay at least the minimum legal wage and compensate for overtime,
- if housing facilities are provided, ensure reasonable privacy, quietness and personal hygiene.

Suppliers must not:

- make use of child labour,
- make use of forced or bonded labour,
- discriminate,
- use illegal overtime,
- prevent workers from associating freely with any workers' association or group of their choosing or collective bargaining,
- accept any form of mental or physical disciplinary action, including harassment.

Environment and Forestry

At IKEA, we shall always strive to minimise any possible damaging effects to the environment, which may result as a consequence of our activities.

Therefore, IKEA and its suppliers shall continuously reduce the environmental impacts of operations.

Suppliers must:

- work to reduce waste and emissions to air, ground and water,
- handle chemicals in an environmentally safe way
- handle, store and dispose of hazardous waste in an environmentally safe manner,
- contribute to the recycling and reuse of materials and products,
- use wood from known areas and, if possible, from sources that are well managed and preferably independently certified as such.

Suppliers must not:

- use or exceed the use of substances forbidden or restricted in the IKEA list of “Chemical Compounds and Substances”,
- use wood originating from national parks, nature reserves, intact natural forests or any areas with officially declared high conservation values, unless certified.

5. Implementation

The supplier shall effectively communicate to all its sub-suppliers, as well as to its own co-workers, the content of the “The IKEA Way on Purchasing Home Furnishing Products”, and ensure that all measures required are implemented accordingly. Via a network of Trading Service Offices, IKEA supports their suppliers to improve their operations. Believing in long-term relationships, IKEA does not break off relations due to non-compliance only, as long as there is a willingness to improve in the right direction with an agreed plan of action to comply with the IKEA requirements within an acceptable time frame. Repeated violations of IKEA’s requirements will result in the termination of the co-operation.

6. Support and Monitoring

The IKEA Trading Service Offices has the direct responsibility to support and monitor the suppliers. To ensure compliance with the requirements, IKEA has also formed a global compliance and monitoring group in order to support and follow up developments on a global basis. IKEA always reserves the right to check suppliers with the help of independent organisations.

Appendix 2 - IKEA’S STAIRCASE MODEL REQUIREMENTS FOR WOOD SUPPLIERS

Level 1 – Start-up Conditions

Basic requirements that wood product suppliers must fulfil before doing business with IKEA.

- Origin of the wood must be known and supplier must be able to state from which region within a country the wood originates
- Wood must not originate from intact natural forests or high conservation value forests
- High value tropical tree species must be certified according to the Forest Stewardship Council (FSC)

Level 2 – Minimum Requirements

The first step up in IKEA's model includes a number of minimum requirements.

- Wood must be produced in accordance with national and regional forest legislation and other applicable laws
- Wood must not originate from protected areas
- Wood must not originate from plantations in the tropical and sub-tropical regions established after November 1994 by replacing intact natural forests

Level 3 – 4Wood to Ease Transition

4Wood is the standard developed for suppliers by IKEA in 2005 to ease the transition from Level 2 to Level 4. The 4Wood standard emphasizes the use of wood-tracking procedures and other routines to better control wood from procurement through production.

Level 4 – Forests certified or responsibly managed

The expectation at Level 4 is that forest management and chain of custody standards must be produced in a balanced co-operation between social, environmental, and economic stakeholders and verified by an independent third party. Currently, FSC is the only Level 4 certification recognized by IKEA.