

**TELECOM SUPPLIER DIVERSITY
TASK FORCE**

**Revitalizing
the Supplier Diversity
Value Proposition through
Supply Chain Effectiveness**



Telecom Supplier Diversity Task Force Report

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FOREWORD

The recent Telecom recession revealed an important lesson about supplier diversity programs in the industry: small minority-owned, woman-owned, or service-disabled-owned businesses ("Diversity Suppliers"), even well-developed ones, have a tough time operating successfully in a poorly functioning supply chain.

SBC sponsored a Telecom Supplier Diversity Task Force in 2002 when we saw that the Telecom downturn was resulting in declining participation from Diversity Suppliers, business failures, and numerous supply chain performance problems. Comprised of some of the best industry minds on the subject, the Task Force revalidated the Telecom supplier diversity value proposition: large companies can, indeed, leverage the small business attributes of Diversity Suppliers (responsiveness, low overhead, customized services) for their competitive advantage, provided these larger companies ensure that their supply chains perform well.

The Task Force offers the industry 21 supply chain recommendations to improve supplier diversity programs. These include activities such as better sourcing, risk mitigation, process quality and control, financial management, and industry collaboration. Based on what we've learned in the last 35 years of supplier diversity programs at SBC, if these activities are performed well, all firms in the supply chain and the supply chain itself will produce more effective outcomes. To help achieve this goal, the Task Force assembled a variety of supply chain management tools and best practices (included in the appendices of the Task Force report) to support the implementation of their recommendations.

Members of the Task Force feel a great deal of optimism and excitement about the future prospects for supplier diversity programs. We see a very tangible, practical path forward that can deliver the supplier diversity participation we require as an industry. If Telecom firms act on these Task Force recommendations, the resulting supply chain improvements will increase the opportunity for Diversity Suppliers to share in the success of our industry.



Steve Welch
Senior Vice President
SBC Communications

Telecom Supplier Diversity Task Force Members

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ACKNOWLEDGMENTS

The Telecom Supplier Diversity Task Force ("TSDTF" or "Task Force") would like to acknowledge the support from SBC and The Anderson Graduate School of Management at UCLA Harold Price Center for Entrepreneurial Studies in forming, directing the efforts of and making valuable contributions to the Task Force.

The Task Force expresses its deepest appreciation for the Telecommunications ("Telecom") industry professionals who participated in this project and assisted in completing the Task Force mission. These experts provided testimony about their recent industry experiences. The individuals are from companies representing different aspects of the Telecom supply chain, including Service Providers, Original Equipment Manufacturers ("OEMs"), Electronic Manufacturing Service providers ("EMSs") and Diversity Suppliers.

The Task Force is also grateful to the many experts from other industries that provided insight from their respective industries, including: financial professionals, supply chain experts and diversity program directors.

Finally, the efforts of many were required to complete the final product, and in recognition of those efforts, the Task Force thanks the staff members of SBC and the UCLA Price Center, as well as the support staff of the other organizations represented on the Task Force.

A handwritten signature in black ink, reading "Alfred E. Osborne, Jr." with a period at the end. The signature is written in a cursive, flowing style.

Alfred E. Osborne, Jr., Ph.D. (Task Force Chair)
Director, Harold Price Center for Entrepreneurial Studies,
The Anderson Graduate School of Management at UCLA

Executive Summary

The Telecom industry has been in turmoil for the past several years. Following a period of major Telecom investment and growth in the late 1990s, several economic and regulatory factors converged to precipitously reverse that trajectory. Plunging orders and the flight of capital exacerbated a troubled Telecom supply chain that was soon choked with wildly inflated forecasts and \$160B in excess inventory. In a scramble to survive, Service Providers that were sitting on unused capacity cut capital expense budgets in half. Suppliers were left with a trickle of orders and warehouses of unused products.

Smaller suppliers with minimal capital reserves were particularly hard pressed to carry large amounts of excess inventory and cover ongoing operating costs. Cash flow shortages, over-commitments on "perceived orders," channel stuffing, a narrow focus on one technology or one customer, along with some deficits in business management capability, all contributed to the crisis faced by smaller Telecom suppliers. Many Diversity Suppliers could not endure these challenges and were forced to shut their doors. Major Telecom players also declared bankruptcy, leaving suppliers and Service Providers alike with un-collectible debts.

The stresses in the supply chain and the unraveling of several long-term supplier diversity solutions led SBC to charter a task force of Telecom and supplier diversity experts to review the state of the industry and the established models of supplier diversity inclusion. Chaired by Dr. Alfred E. Osborne, Jr., Ph.D., Director of the Harold Price Center for Entrepreneurial Studies at The Anderson Graduate School of Management at UCLA, the Task Force sought to:

- Determine how Diversity Suppliers can continue to provide competitive advantage in the Telecom supply chain during stressful economic conditions
- Develop recommendations on how the Telecom industry can work collaboratively to revalidate and revitalize supplier diversity programs

In setting the context of their investigation, the Task Force noted that supplier diversity programs in the Telecom industry had gone through several stages of growth. Starting with awareness-building and outreach, many Telecom supplier diversity programs had graduated to proactive development of Diversity Suppliers and supplier diversity business opportunities. Some programs had also worked to leverage the competitive advantages of supplier diversity participation in the marketplace and had shown how supplier diversity delivers brand enhancement, public policy support and increased revenue generation. Overall, the Telecom industry was known for setting high supplier diversity standards, for successfully including Diversity Suppliers in the core of Telecom network business, and for working collaboratively to increase diversity participation.

However, recent and very significant changes in the Telecom environment have challenged the industry's supplier diversity success. The forces of change include: outsourcing to Electronic Manufacturing Service companies ("EMSs"), globalization of the supply chain, an increase in the number of competitors, a regulatory environment that discourages investment in the Telecom network, the flight of capital from the Telecom sector and slowed growth in the overall economy.

Telecom supply chains and procurement organizations have responded to these forces by intensifying their focus on leveraging scale and standardization to achieve lowest cost.

At the same time, differences in embedded network infrastructure, differences in the mix of competitors in local markets, differences in state regulation and differences in increasingly sophisticated customer requirements – all combined to require customized products and services.

The Task Force concluded that in its search for competitive advantage, the Telecom supply chain must find the right balance in this dynamic tension between the need for customization and the need for scale. This balance involves successfully integrating small businesses into the value-adding supply chains of the larger firms that dominate the industry in order to leverage the competitive advantage that those small businesses offer – responsiveness, customized services, and lower overhead costs.

In examining the recent performance of the Telecom supply chain, the Task Force found much room for improvement. At a time when fierce competition, lower revenues and reduced access to capital combine to put a premium on price and a seamless supply chain, supply chain disruptions have been commonplace. Some supply chain problems of a long-standing nature had been tolerated as a low priority nuisance during periods of economic growth. When the industry hit an economic trough, these disruptions became a crisis with top priority. Late payments, delayed delivery, order and invoice errors, poor project communication, and contract disputes can quickly wash out profitability when volumes are down. At a time when supply chain performance can separate the winners from the losers, a smoothly functioning supply chain becomes an imperative.

Through research, industry testimony, case studies and company site visits, the Task Force revalidated that Diversity Suppliers can play a critical role in optimizing the Telecom supply chain. They can help achieve competitive advantage with the right balance between customization and scale. Under tough economic conditions however, successful supplier diversity programs will need to be built around utilizing diversity firms to achieve supply chain effectiveness. Good outreach programs and generic supplier development initiatives will no longer be sufficient.

The Task Force reviewed five basic models of diversity participation in the Telecom supply chain: Subcontractor, Contract Manufacturer ("CM"), Prime

Supplier, Value Added Reseller ("VAR"), and Channel Partner. Each of these roles is a vital element in a successful Telecom supply chain and Diversity Suppliers can be positioned to be valuable contributors in each of these roles.

The Task Force conducted a detailed analysis of the Value Added Reseller model and revalidated that Diversity Suppliers' lower cost structure, lower return on investment hurdles, local presence, flexibility, and ability to customize provided competitive advantages to the supply chain. A VAR is well positioned to respond to the special local operating environment. Therefore, diversity VARs play an important role in optimizing local supply, reducing turnaround time on changes and modifications, consolidating orders between multiple supplier platforms, and providing flexible delivery and turn-up. Diversity VARs and small Contract Manufacturers can partner with EMSs and Original Equipment Manufacturers ("OEMs") to fulfill the need for local customization of product and customer service.

A successful Diversity Supplier must understand the challenges it will face within the Telecom supply chain. The competitive Telecom environment requires that Diversity Suppliers diversify their value proposition beyond low margin, basic distribution service offerings; make improvements in governance; and develop strategies that focus on long-term profitability, growth and diversification of the revenue base either through new customer acquisition, new service offerings, or by penetrating new industries. Finally, Diversity Suppliers must develop a core management team with strong Information Technology ("IT") and e-enablement skills, expertise in financial management, quality process management, and solid Telecom industry experience. Diversity Suppliers are often small businesses, and Web-enabled tools provide accurate, timely information on inventory levels, delivery status, and other performance measures that can help mitigate the risks of using smaller suppliers in a very large supply chain.

Financial capability, which can be seen in a strong balance sheet and positive, growing cash flow, is essential to business success in the Telecom supply chain. Those suppliers with financial resources are better situated to manage the variability in revenue streams that occur over the business cycle. The Task Force found that Diversity Suppliers in the Telecom supply chain are often operating with slim margins in the 2%-10% range and tend to be undercapitalized and cash poor. Careful financial management is a vital factor for these entrepreneurs.

The Task Force determined that timely action is needed to address the challenges facing the Telecom supply chain and Diversity Suppliers in that supply chain. To facilitate such action, the Task Force developed a set of specific recommendations under each of five identified critical success factors. The action-focused recommendations are further supplemented with a set of appendices that include specific examples and tools that can be utilized in carrying out the recommendations. These tools and examples are illustrative and are offered to stimulate the sharing of best practices and practical ideas among

companies interested in achieving supplier diversity and supply chain optimization.

Since the work of the Task Force is only a beginning effort that calls for continued collaboration within Telecom and across other industries as well, the Task Force recommends the establishment of a few strategic, Web-based supplier diversity resources sites. The Institute of Supply Chain Management ("ISM"), the QuEST Forum, and the National Minority Supplier Development Council ("NMSDC") have all shown interest in supporting resource sites of this kind. These sites could serve as the focal point for collecting and disseminating a wide variety of best practices and tools; a vehicle to enable timely discussion of issues and ideas along with benchmarking; and the launch pad for further collaboration in the ongoing work of revitalizing the supplier diversity value proposition in the Telecom industry.

The Task Force launched its efforts with significant concern about the challenges facing Diversity Suppliers in the Telecom supply chain. The Task Force concluded its work with a solid belief that Diversity Suppliers have an important role to play in optimizing a supply chain that is struggling to regain performance excellence and maintain the proper balance between scale and customization. If the industry collaborates to implement more effective strategic sourcing, improved risk mitigation measures, better quality process management and enhanced access to capital and financial management skills, our supply chains and Diversity Suppliers will be positioned to accelerate the Telecom recovery.

Summary of Recommendations

The Task Force identified five critical focus areas necessary to leverage the participation of Diversity Suppliers through improved supply chain performance:

- I. Implement Effective Sourcing for Supplier Diversity***
- II. Enhance Risk Mitigation Activities in Supply Chain Management Practices***
- III. Deploy Process Quality and Control***
- IV. Improve Access to Capital and Financial Management***
- V. Accelerate Supplier Diversity Participation Through Industry Collaboration***

Under these five critical themes, the Task Force developed twenty-one recommendations (see Section G of this report) for revitalizing supplier diversity participation and supply chain management. The very initiatives and practices that will strengthen the contributions for Diversity Suppliers will also strengthen the performance of the overall Telecom supply chain.

I. Implement Effective Sourcing for Supplier Diversity

The Task Force recommended that Procurement contracting should develop more effective sourcing practices for supplier diversity. Supplier diversity planning should be integrated into the supply chain sourcing process. This includes requiring bidders to file a detailed and specific supplier diversity plan as part of the RFP process, explicitly defining supplier diversity program requirements as part of final contracts and ensuring that suppliers report their level of diversity participation one level up in the supply chain (e.g., channel partners in sales and distribution) and two levels down (prime supplier and subcontractors). Telecom companies should also map the functions and participants in their supply chain to verify the small business value proposition as measured by cost, performance and schedule terms, delivery, customer satisfaction, and total cost of ownership.

- Recommendation #1 – Integrate supplier diversity planning into the sourcing process
- Recommendation #2 – Require Supplier Diversity Plan in RFPs
- Recommendation #3 – Require Supplier Diversity Plan in contracts
- Recommendation #4 – Require Supplier Diversity participation reporting in contracts
- Recommendation #5 – Design and verify Supplier Diversity business value propositions

- Recommendation #6 – Develop contracts that mitigate risks to small businesses
- Recommendation #7 – Assess the supply chain value of Diversity Suppliers by including total cost of ownership calculations and the potential marketing and revenue generation value of the relationship in addition to first cost. Utilize a best overall value assessment, rather than a first cost assessment alone when calculating the relative value of competing supply chain solutions.

II. Enhance Risk Mitigation Activities in Supply Chain Management Practices

The Task Force recommended that a Readiness Assessment be conducted with supplier diversity partners before implementing a new supply chain arrangement. This would include assessing operations, in addition to other areas such as IT capabilities and financial viability. This proactive assessment of supplier capabilities will help reduce future process problems related to functions such as ordering, invoicing and inventory management. The Task Force also proposed that a Supplier Health Check dashboard be created to keep Telecom OEMs and Service Providers updated on the stability and sustainability of their diversity small business partners. Additionally, it was concluded that Web-enabled performance tracking capability, and enhanced IT capabilities for smaller business would help reduce risk.

- Recommendation #8 – Conduct Readiness Assessments
- Recommendation #9 – Maintain Supplier Health Check dashboards
- Recommendation #10 – Utilize Web-enabled performance tracking
- Recommendation #11 – Promote information systems capabilities for small businesses

III. Deploy Process Quality and Control

The Task Force recommended improving quality and control of the supplier diversity process by creating cross-functional teams made up of Diversity Suppliers, OEMs and/or Service Providers. These teams would ensure that new supply chains are properly constructed with all of the necessary performance measures, Web-based surveillance reports, and issue resolution capability to ensure high performance.

- Recommendation #12 – Create cross-functional implementation teams with Diversity Supplier, OEM and/or Service Provider members jointly focused on utilizing quality process management to guide the implementation of new or significant supply chain arrangements

- Recommendation #13 – Implement Value Added Reseller/Channel Partner Best Practices to effectively integrate Diversity Suppliers into the Telecom supply chain
- Recommendation #14 – Develop clear strategies and quality-focused processes for integrating supplier diversity planning into the marketing and sales process

IV. Improve Access to Capital and Financial Management

The Task Force recommended that the industry consider additional funding sources for Diversity Suppliers. The idea of creating a source of funds from the industry's largest companies is still under consideration, particularly, as it has been modeled in the automotive industry. The Task Force also felt that progress could be made to reduce financial risk and improve cash flow management through better contracting terms and conditions which protect small business cash flow (for example, late payments from Service Providers and better inventory return procedures from VARs to OEMs). Greater emphasis on financial management capability and working capital planning skills should be emphasized in the industry's university programs.

- Recommendation #15 – Improve access to both long- and short-term capital
- Recommendation #16 – Enhance university management programs for diversity entrepreneurs to place greater emphasis on financial management capability and working capital planning skills

V. Accelerate Supplier Diversity Participation Through Industry Collaboration

The Task Force recommended several tools for promoting ongoing collaboration within the Telecom industry, including Web-based diversity resource sites, university-sponsored Joint Venture Success Labs which would bring together Diversity Suppliers, manufacturers and Service Providers and business school academia, and an annual "State of the Union" report on the Telecom supply chain. The Task Force also proposed that the Telecom industry continues working on standardizing metrics and reporting methodologies for supplier participation in diversity programs. The increasing role of EMSs in Telecom calls for their full collaboration in supplier diversity programs and processes.

- Recommendation #17 – Establish Web-based supplier diversity resource sites
- Recommendation #18 – Leverage the resources of existing university diversity management training programs to establish multi-disciplinary Joint Venture Success Labs

- Recommendation #19 – Propose a Telecom supply chain “State of the Union” report
- Recommendation #20 – Standardize supplier diversity participation metrics and reporting methodologies
- Recommendation #21 – Encourage large scale EMSs to adopt the supplier diversity goals and best practices of their Telecom industry customers, establish supplier diversity programs and launch initiatives that will integrate Diversity Suppliers into the EMS supply chain as CMs, VARs, direct suppliers and subcontractors

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