

Costco operations

Case duration (Min): **45-60**

Operations Management (OPs)

Global supply chain management**Managing quality and performance****Worldwide****Case summary:**

The first film focuses downstream on Costco - managing the supply chain to reduce costs and become more efficient thus providing a competitive advantage. The second film focuses on how this can be achieved through one supplier as an example of supply chain management.

MANAGING PRODUCTION
LOGISTICS AND THE SUPPLY CHAIN

Learning objectives:

Discuss what is meant by operations management and supply chain management
Explain the importance of operations management to business competitiveness
Identify major operations management and supply chain management activities
Evaluate how operations management contributes to business success

Case problem:

This case investigates Costco and one of its suppliers from a business operations perspective: how can value be created through cost reduction/ efficiencies and improving customer benefits.

Company
Wholesale, Other

Costco

www.Costco.com

Founded in 1983, Costco Wholesale Corporation is the largest membership (57 million members) warehouse club chain in the world, based on sales volume - Costco is only open to members and their guests. Costco operates an international chain of membership warehouses, mainly under the "Costco Wholesale" name, which carry quality, brand name merchandise at substantially lower prices than are typically found at conventional wholesale or retail sources. The warehouses are designed to help small-to-medium-sized businesses reduce costs in purchasing for resale and for everyday business use. Individuals may also purchase for their personal needs. It is the fifth largest general retailer in the United States. Revenues of over \$70 billion USD (2008) are generated through a workforce of approximately 142,000 employees. Costco focuses on selling products at low prices, often at very high volume. These goods are usually bulk-packaged and marketed primarily to large families and businesses. Additionally, Costco does not carry multiple brands or varieties where the item is essentially the same. This results in high volume of sales from single vendors, allowing further reduction in price, and reducing marketing costs. Costco also saves money by not stocking extra bags or packing materials. To carry out their goods, customers must bring their own bags or use the merchandise shipping boxes from the company's outside vendors. Costco has over 500 locations [2009] – mainly in the US but also in Mexico, the UK, Japan and other countries. According to Jim Senegal, the Company's President and Chief Executive Officer, "Costco is able to offer lower prices and better values by eliminating virtually all the frills and costs historically associated with conventional wholesalers and retailers, including salespeople, fancy buildings, delivery, billing and accounts receivable. We run a tight operation with extremely low overheads which enables us to pass on dramatic savings to our members."

First, if you are taking a taught management course then consult with your tutor and ensure that the case has not been scheduled into a teaching class or tutorial. If it has not:

1. Play/ read the media associated with the case. You may need to access the Internet and enter a URL to locate any video clips.
2. Attempt the Case study questions.

Consider attempting the case study as a group exercise; you could form a study group with fellow students.

3. Check the suggested answers - remember these are suggestions only and there are often many possible answers.

Discuss questions and answers with other students.

4. If you feel your answer(s) were weak then consider reading the relevant suggested readings again (also see the case study suggested references).

Title/ Media type

URL/ Media description

Managing Costco in a Tough Economy

http://feedroom.businessweek.com/?fr_story=5d7681157aafa9ed796cb26519a17eaa07311398&rf=bm

Film

This brief film clip provides a simple example of improving efficiency and reducing cost through operations in the supply chain. Analysis of efficiencies (pallet, container shape) for a product (in this case cashew nuts) that lead to cost savings through reduced transportation, warehousing, shelf replenishment and warehouse handling costs.

Jim Sinegal poses several important questions: how can companies better operate? How can companies work with suppliers to bring goods to market at the lowest possible price? How are cost taken out? How efficiencies built throughout the organization? These are not just challenges for Costco but also their suppliers – with whom Costco must work to meet such challenges.

Wine Entrepreneur

http://feedroom.businessweek.com/?fr_story=bfbe9e870017ebb03a89483e6afe3ae3041eca54&rf=bm

Film

In this video clip, we consider one of Costco's suppliers – a wine merchant. Cameron Hughes does not own any grapes (he is not a wine maker), but his name graces the label of tens of thousands of cases of wine. The film clip reveals how he purchases wine from Californian wine makers, filters it, creates blends, bottles and labels it, packages, stores and ships it to a major retailer--Costco.

As a business, Cameron Hughes must produce high quality wine at low price. A number of efficiency strategies are utilised to achieve this.

NOTES:

Case study questions...

Action	Pre/During/After class
1 EXPLAIN THE CONCEPT OF OPERATIONS MANAGEMENT Explain the concept of operations management - in groups create a definition of operations management	During
2 VALUE CHAIN Draft a description (and diagram) for the value chain (see Porter) at Cameron Hughes	During
3 EXPLAIN THE CONCEPT OF VALUE AND HOW IT IS INCREASED BY WINE MERCHANT CAMERON HUGHES Explain the concept of value and how it is increased by wine merchant Cameron Hughes	During
4 SUPPLY CHAIN AT CAMERON HUGHES Describe the supply chain at Cameron Hughes and how it differs from the value chain	During
5 DISCUSS KEY VALUE CHAIN AND SUPPLY CHAIN OPERATIONAL DECISIONS Discuss key value chain and supply chain decisions: where might value be added in terms of customer benefits/ quality and cost reduction (efficiencies)?	During
6 STRATEGY Discuss how the value chain and supply chain decisions contribute to strategy	During

Answers...

OPERATIONAL EFFICIENCY

helps improve supply chain performance.

OPERATIONAL EFFECTIVENESS

performing similar activities better than rivals perform them

SUPPLY CHAIN

All of the activities related to the acceptance of an order from a customer and fulfilling it. In its extended format, it also includes connections with suppliers, customers, and other business partners.

SUPPLY CHAIN MANAGEMENT

An attempt to coordinate processes involved in producing, shipping and distributing products, generally performed only by large corporations with large suppliers. Private Trading Exchanges can extend Supply Chain Management to all trading partners regardless of size because they provide a central location to integrate information from all supply chain participants. (See Exchange.)

GLOBAL SOURCING

Global sourcing: purchasing services and components from the most appropriate suppliers around the world regardless of their location

OPERATIONS

The core activities of a business

ECONOMIES OF SCALE

A decrease in the per unit cost of production as a result of producing large numbers of the good

INVENTORY MANAGEMENT

controlling stock levels within the physical distribution function to balance the need for product availability against the need for minimising stock holding and handling costs

Question/ Answer

1 Explain the concept of operations management

Explain the concept of operations management - in groups create a definition of operations management

See definitions of terms associated with this handout

2 Value chain

Draft a description (and diagram) for the value chain (see Porter) at Cameron Hughes

Tankers of ready made wine arrive as inbound raw materials.

Operations involves filtering, blending, bottling and labelling the wine.

Outbound logistics includes palletising for Costco, storage as outbound inventory in a warehouse, then shipment to Costco

3 Explain the concept of value and how it is increased by wine merchant Cameron Hughes

Explain the concept of value and how it is increased by wine merchant Cameron Hughes

Value is about benefits (quality) and price (cost)

Value can be increased by adding benefits and or reducing cost/price

Cameron Hughes creates benefits through the unique nature of his blends and process

Costs are reduced through scale benefits, disintermediation (removal of the distributor), the operations processes, bulk purchasing of inputs, renting equipment rather than owning it - operating as a virtual company, the use of a single 'factory',

4 Supply chain at Cameron Hughes

Describe the supply chain at Cameron Hughes and how it differs from the value chain

The value chain plus

1. upstream show the suppliers as wine makers in California

2. downstream show the retailer (Costco) and sales to consumers

5 Discuss key value chain and supply chain operational decisions

Discuss key value chain and supply chain decisions: where might value be added in terms of customer benefits/ quality and cost reduction (efficiencies)?

Students should use the value and supply chain analysis/ frameworks to focus upon where value might be added and efficiency gains made. Key questions include:

Outsourcing - what should be done in house and why?

Backward integration - should Cameron Hughes acquire wine makers?

Forward integration - should Cameron Hughes develop their own retail/ ecommerce capabilities?

Productivity and the utilisation of resources

Quality - whether and how to make the blends better - understand what customers and Costco want

Assess where technological improvements might be made; where information systems might help

Analyse the business processes for continuous improvement

6 Strategy

Discuss how the value chain and supply chain decisions contribute to strategy

Discuss generic strategies such as cost, differentiation and focus

PRODUCTION

Activities involved in creating a product

PRODUCTION PROCESS

the way that businesses create products and services

PROCESS

A set of logically related tasks or activities performed to achieve a defined business outcome.

VALUE CHAIN

Viewing a firm as a series or chain of basic activities that add value to its products and services and thus add a margin of value to the firm.

LOT SIZE

the number of units of product or item to be manufactured at each set up

VALUE CONFIGURATIONS

Describes how value is created in a company for its customers

Case study references

Cole, G A. and Kelly, P P. (2011) 'Management Theory and Practice', Ed. 7. Cengage EMEA.

Collier, D. and Evans, J. (2009) 'OM', Ed. 1. Cengage Learning.

Kelly, P P. (2009) 'International Business and Management', Cengage Learning EMEA.

Porter, M E. and Millar, V E. (1985) 'How information gives you a competitive advantage.', Harvard Business Review, July-August 63, p. 149 - 174.