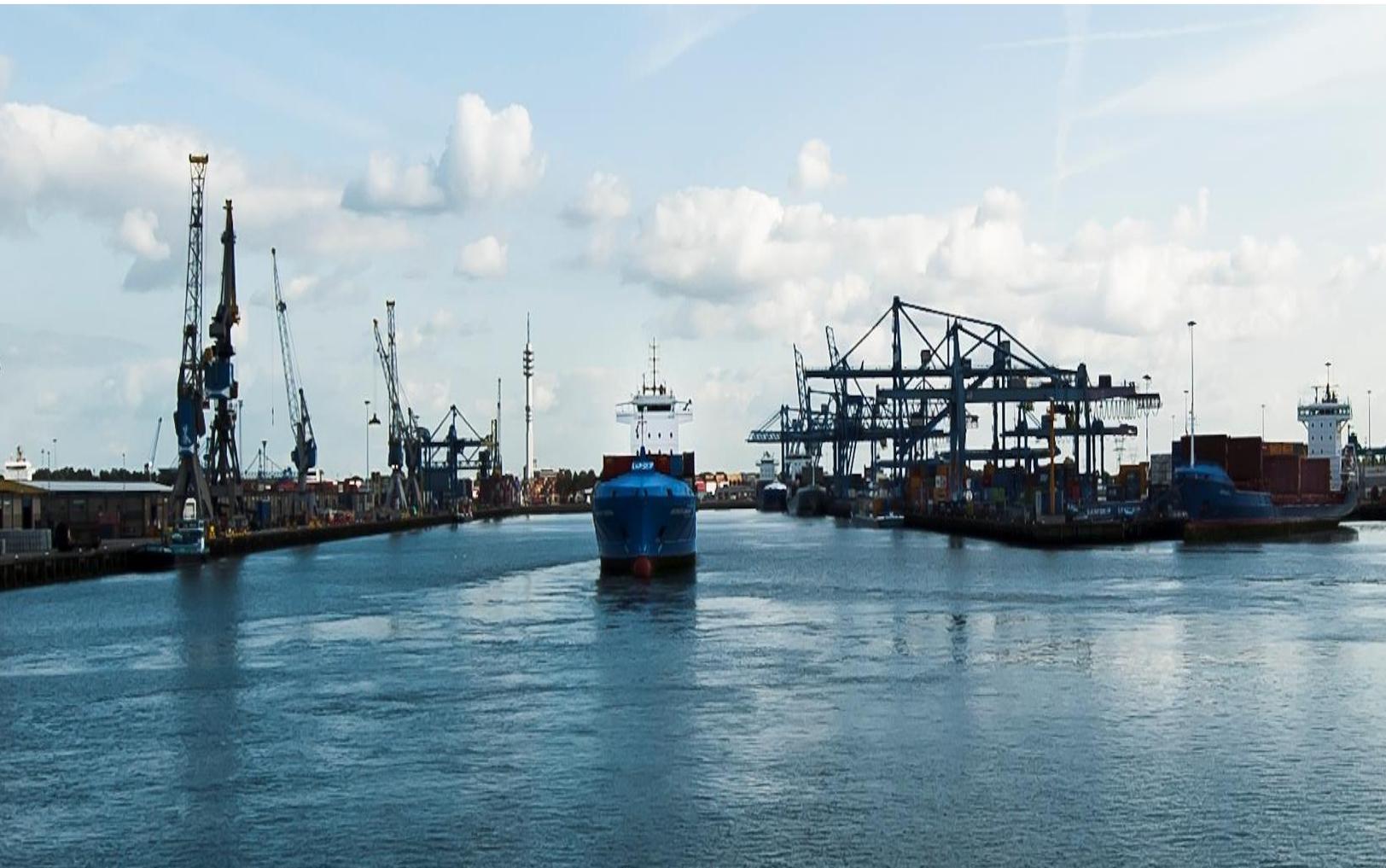


The Truth About Reshoring: Not What It's Cracked Up to be!



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If you're considering reshoring your manufacturing back to the United States, you are not alone. Over the past 2 years, the buzz has intensified in boardrooms and the headlines in the business press would lead you to believe that the move back to the United States is in full swing and only gaining momentum. However, based on new findings from A.T. Kearney's Global Strategic Operations Practice, even though manufacturing in the U.S. has clearly been on the uptake, the impact of reshoring on this turnaround is much less than the hype would indicate!

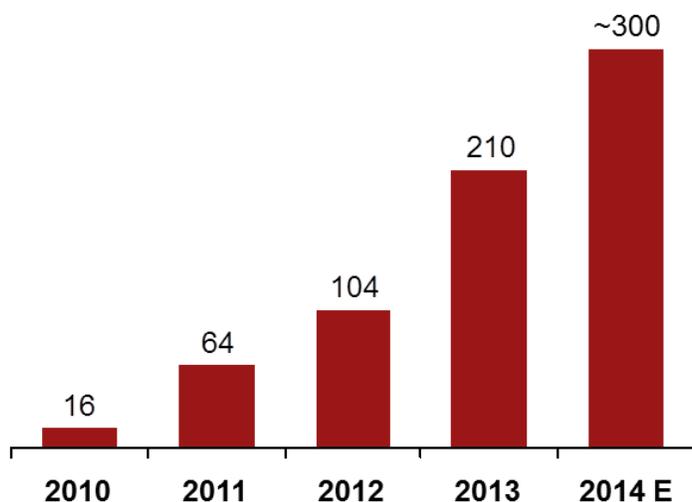
How much manufacturing has actually been reshored? And which categories are experiencing the largest shifts? Thus far, the evidence has been largely anecdotal: typically a few expert quotes, a couple of case studies, references to Walmart's pledge at the beginning of 2013 to increase spend with United States domestic suppliers by \$50 billion over the next five years, and some well-articulated opinions. Even the best research on the subject has relied heavily on prognostication, with insufficient measurement and tracking of the actual results.

Given that closing down or scaling back operations and suppliers in, for example, China and moving them back to the United States is a significant undertaking for any company, A.T. Kearney decided to leverage its wealth of practical experience in helping our clients identify, negotiate, and implement the right supply chain decisions, to go beyond the hype and determine what's really going on. Both from a micro level (in our Reshoring Database detailing around 700 U.S. reshoring cases since 2010) and a macro level (through our innovative Reshoring Index), we have actively been tracking the evolving reshoring trends. What is our objective? Discern the facts based on hard data, separate the hype from reality, and provide our clients with sound advice on the matter.

Slow to ramp up

A.T. Kearney has analyzed 700+ reshoring cases that have been announced in the past five years. In the latest update of A.T. Kearney's Reshoring Database at the end of July 2014, there were 116 recorded reshoring cases already this year. Though this number was actually slightly below the 2013 full-year pace of 210, we still expect the total number of cases to be around 300 by the end of 2014. The number of published reshoring cases is of course only one metric to gauge the degree and intensity of reshoring impact on the U.S. economy, as the economic value of the cases may be different year to year. A database of documented reshoring cases is, however, useful in developing an understanding of the changes in rationale and the shifts across industries of the re-shoring cases. (see Figure 1)

Figure 1
Reshoring cases over years 2010 – 2014



The documented reshoring activity has been observed across several sectors, including some where reshoring was expected: computers and electronics, appliances and electrical equipment, primary metals, machinery, furniture, plastics and rubber, paper, and fabricated metals. But reshoring is also happening in sectors that most thought would never return, such as apparel and textiles. The table (Figure 2) below shows the top reshoring industries documented in A.T. Kearney’s Reshoring Database.

Figure 2

	% Cases
Electrical Equipment, Appliance, & Component Manufacturing	15%
Transportation Equipment Manufacturing	15%
Apparel Manufacturing	12%
Computer & Electronic Product Manufacturing	10%
Miscellaneous Manufacturing	7%
Plastics & Rubber Products Manufacturing	7%
Machinery Manufacturing	5%
Fabricated Metal Product Manufacturing	5%
Primary Metal Manufacturing	3%
Furniture & Related Product Manufacturing	3%
Chemical Manufacturing	2%
Other Manufacturing	8%
Other non-manufacturing	8%

Over the past five years appliances and electrical equipment and transportation equipment were the top reshoring industries, followed by computers and electronics. But over the past 24 months, reshoring cases from the apparel industry have been increasing, making the sector the third in our ranking. This micro trend that can be spotted in our Reshoring Database is also present at the macro level. To understand the forces driving reshoring in apparel please refer to the sidebar titled “The Unexpected Case of Apparel.”

Individual companies, however, have different reasons to reshore and different approaches to make it happen. We also see diversity in the products that are reshored, with some relatively low cost products being brought back as well as more premium goods being reshored (no surprise, we’re seeing an uptick on the latter).

As for the reasons for reshoring, companies, not surprisingly, quote delivery quality and cost as their main drivers. However, and this is surprising, brand/image is becoming increasingly important. The table below shows the top reasons documented in A.T. Kearney’s Reshoring Database. (see Figure 3)

Figure 3

	Mentions
Delivery time improvement	30%
Quality improvement	29%
Image/Brand (prefer U.S.)	20%
Freight Cost Improvement	20%
Wage Cost Improvement	20%
Total Cost of ownership	17%
Energy Cost Improvement	14%
Government Incentives	14%
Innovation/Product Differentiation improvement	13%
Higher productivity	13%

Customers expecting shorter lead times and everyone getting more worried about supply chain disruptions are certainly forcing companies to rethink their supply chain. There are also capability issues that are forcing companies to consider coming back, which is why you see quality and, to a lesser extent innovation, featured in the top 10 reasons. Another cluster of companies are bringing back manufacturing for the same reason that they off-shored their operations in the first place: cost! Interestingly, “Made in USA” is becoming a big deal and moving up in the ranking, especially in the past two years, even though many companies admit that it’s still to be seen if U.S. customers are willing to pay the extra cost it still takes for most products to carry the Made in USA label.

Many of these cases in the A.T. Kearney Reshoring Database are still in the early stages of implementation and have yet to translate into real economic impact. So the benefits to the U.S. manufacturing sector have not been fully realized. But the fact that the number of reported reshoring cases appears to be no longer growing as fast as it did over the past three years is a first interesting observation that appears to contradict the hype. However, to fully understand the economic impact of reshoring, a macroeconomic view is needed.

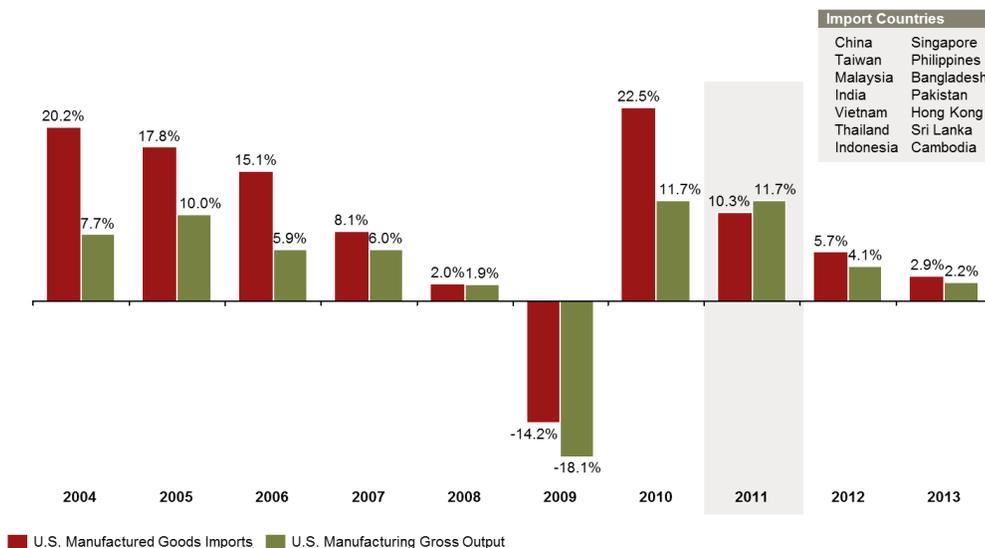
Reshoring Index

From a macro perspective, the recent reshoring trend has definitely helped lift U.S. manufacturing, which is already in its fifth straight year of expansion after the low point of 2009, despite a slight drop off in recent months. Between 2009 and 2013, domestic manufacturing gross output grew by an average compound rate of nearly 6 percent, and by 2011 gross output was already ahead of its 2008 pre-recession levels on a nominal basis. The recovery has been particularly strong in the automotive and metals, and chemical industries, spurred by increasing global competitiveness and domestic demand. Reshoring was far from the leading factor driving U.S. manufacturing's output growth, but its impact should not be overlooked.

Interestingly, imports of offshored manufactured goods into the U.S. have increased at an even faster rate. By offshored we refer specifically to products that are being imported from the Asian low-cost countries to which American companies moved their manufacturing operations over the past 15 years with the intent to produce (partly) for the U.S. market. Of course, the most important of these trading partners is China, from which the U.S. imported more than \$428 billion of manufactured goods in 2013. But we are also including 13 other offshore countries in our analysis, including Taiwan, Malaysia, India, Vietnam, Thailand, Indonesia, Singapore, Philippines, Bangladesh, Pakistan, Hong Kong (reported separately from China in the United States International Trade Commission import data), Sri Lanka, and Cambodia. For the purpose of the reshoring discussion, these 14 offshore countries are the most relevant. Note that we are excluding certain countries from which the U.S. imports sizeable amounts of manufactured goods (measured in dollar value), most notably the two largest "nearshore" trading partners Canada and Mexico, as well as other high-cost countries such as Germany and Japan, since the reshoring debate is about the return of manufacturing from mostly Asian, so-called low cost countries. (see Figure 4)

Figure 4

United States Manufactured Goods Imports and Domestic Gross Output
Year-over-Year Nominal Growth—2004-2013



Source: United States International Trade Commission; United States Department of Commerce Bureau of Economic Analysis

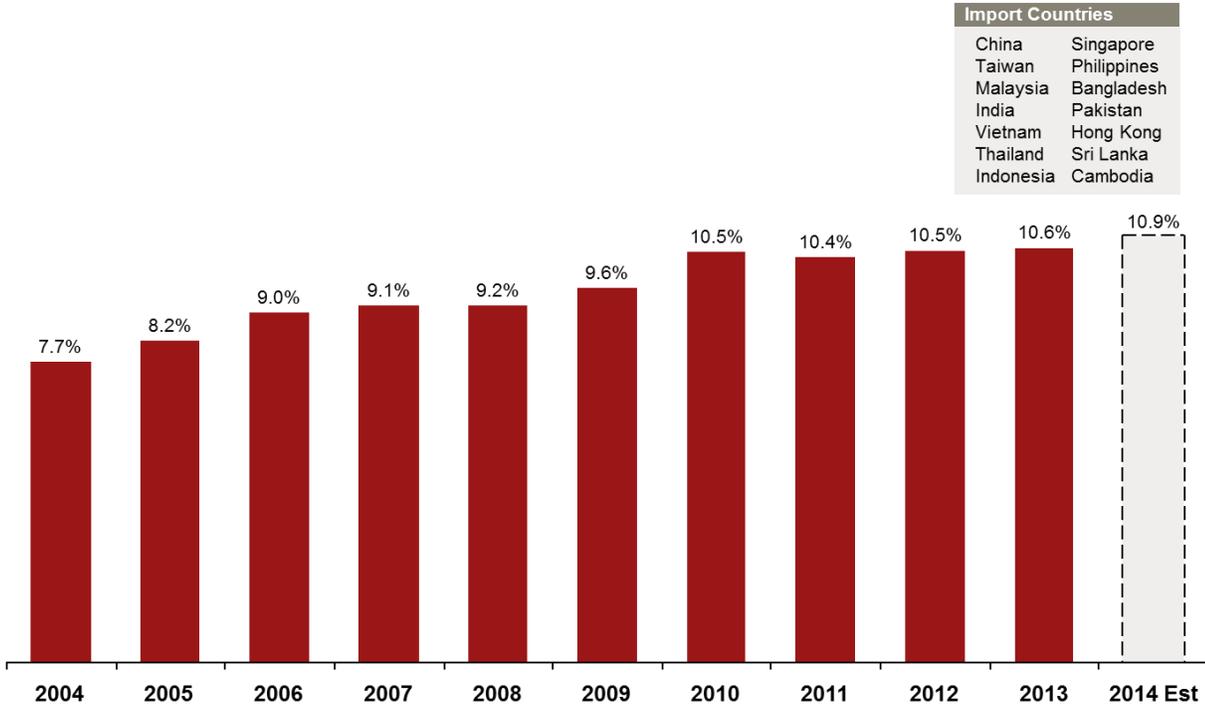
Between 2009 and 2013, manufactured goods import value into the U.S. from those 14 offshore trading partners grew by an average rate of 8 percent. In fact, nominal U.S. manufactured goods offshore import growth has exceeded domestic manufacturing gross output growth in nine of the past 10 years. The only exception was 2011, when U.S. manufacturing gross output expanded by nearly 12 percent compared with just over 10 percent growth in the value of offshore manufactured goods imports. We need to be careful simply comparing these two numbers, as U.S. manufacturing gross output and offshore manufactured goods imports, by definition, are not mutually exclusive. Gross output includes intermediary manufactured goods import value and some manufactured goods imports include U.S. intermediary manufactured goods exports (included in the gross output number). However, given the trend toward importing “finished” goods (from the 14 offshore countries) and exporting intermediary raw materials and finished manufactured goods rather than intermediary manufactured goods (to the 14 offshore countries), the comparison is conservative and the result is that much more compelling.

How are U.S. manufacturing gross output and offshore manufactured good import values meaningful to the reshoring debate? Detailed review and comparison of the two datasets provides a powerful indicator of where manufacturing of goods for the United States market is happening. Rather than showing the datasets side by side, A.T. Kearney has aggregated the data into a single Reshoring Index. The Reshoring Index starts with a simple ratio of annual offshore manufactured good import values to the U.S. manufacturing gross output, based on the nominal United States dollar value and summarized as the Manufacturing Import Ratio (MIR). From 2004 through 2010, the MIR grew by almost 300 basis points, from 7.7 percent in 2004 to 10.5 percent in 2010, reflecting a significant amount of offshoring of production for the U.S. market over that time period (Figure 5). However, that pace has slowed down and has been hovering around 10.5 percent over the past three years. This would suggest that the U.S. manufacturing gross output has been growing at a faster pace than the growth in manufactured goods imports. One could argue that this can be attributed, at least in part, to reshoring. That is the good news. But the MIR for full-year 2014 (based on 2014 latest available data) is on pace to reach 11 percent or higher. If this is indeed how 2014 will conclude, then it could be argued that the year-over-year growth in the U.S. manufacturing gross output is slowing down. This could be an indication that the impact of the reshoring wave is waning.

Figure 5

U.S. Manufacturing Import Ratio (MIR) = Total Manufactured Goods Imports as a % of Domestic Manufacturing Gross Output

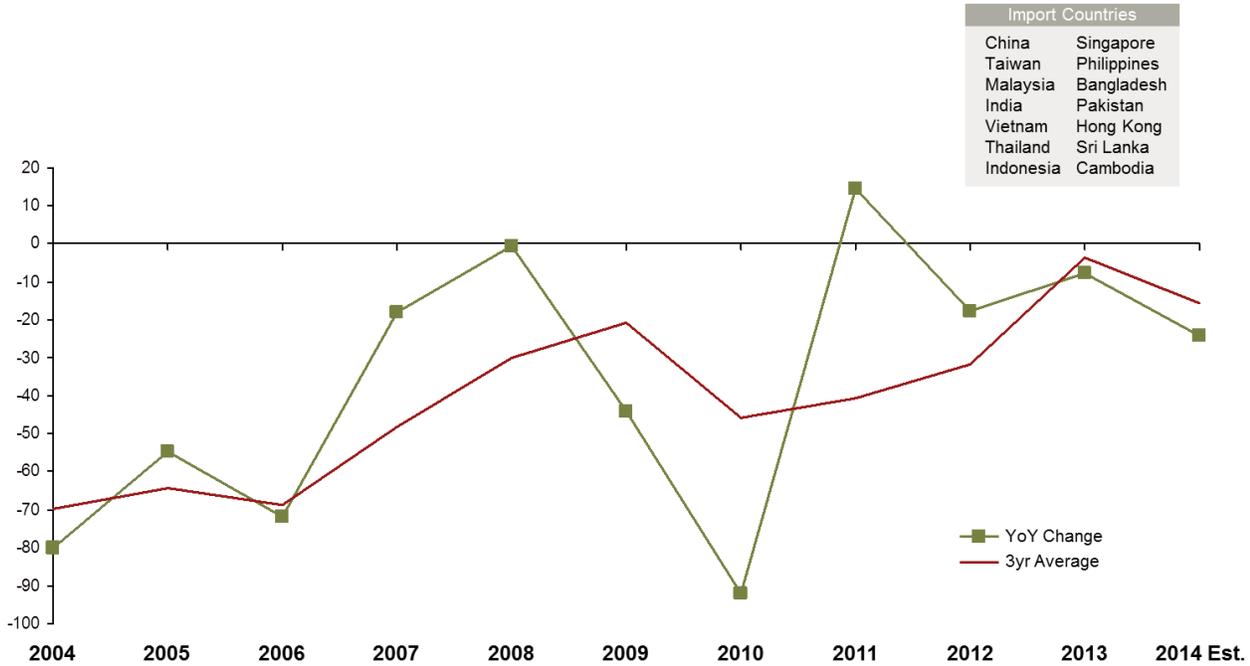
(%, 1997 – 2014 Est)



Source: United States International Trade Commission; United States Department of Commerce Bureau of Economic Analysis

The Reshoring Index, then, tracks the year-over-year spread in the MIR—measured in basis points. Positive values demonstrate a net reshoring, while negative values show net offshoring. Looking at the evolution of the Reshoring Index over time leads to three interesting observations: (1) The U.S. has experienced wide swings in reshoring over the time horizon of the Reshoring Index; (2) Even in the past five years, the period in which reshoring has garnered the most media attention, the Reshoring Index turned positive only once, in 2011; (3) Instead of building on the momentum of 2011, the Reshoring Index flipped back negative in 2012 and appears to be tapering down based on the latest economic data as of the end of 2014. The growth of offshore manufactured goods imports has leveled off recently, but the growth of U.S. manufacturing gross output has slowed even more.

Figure 6
A.T. Kearney Reshoring Index
Year-over-Year Change in the U.S. Manufacturing Import Ratio
 (Basis Points, 2004 – 2014 Est.)



Import Countries	
China	Singapore
Taiwan	Philippines
Malaysia	Bangladesh
India	Pakistan
Vietnam	Hong Kong
Thailand	Sri Lanka
Indonesia	Cambodia

Source: United States International Trade Commission; United States Department of Commerce Bureau of Economic Analysis
 Note: 2014 data are not yet available beyond Q2, so the full year YoY change is estimated based on 2013 Q1-Q2 vs. 2014 Q1-Q2 change

In addition to reviewing the aggregate level macro data, we also evaluate the Reshoring Index at an industry level. The U.S. Bureau of Economic Analysis is less timely in its reporting of industry-level manufacturing gross output data as compared to its reporting of aggregate data (for example, the data are only available up until 2012), but comparisons across and within industries can still be instructive. As Figure 7 depicts, our primary focus is on the 12 industries that have been most significantly impacted by offshoring, based on the relative MIRs by industry: apparel, leather, textile mill, electronics, furniture, miscellaneous manufacturing, appliances, textile products, plastics and rubber, machinery, mineral products, and fabricated metals. For instance, in the apparel industry, the 2012 MIR was 468 percent—meaning that there is \$4.68 of apparel imports (from the 14 offshore countries) for every \$1.00 of domestic manufacturing gross output. On the other end of the spectrum, the 2012 MIR in the beverage industry was 0.2 percent—or two-tenths of a penny of imports for every dollar of U.S. gross output. Neither of those are necessarily a surprise, but that changes if you look at the Reshoring Index.

Figure 7

2012 U.S. Manufacturing Import Ratio (MIR) = Total Manufactured Goods Imports as a % of Domestic Manufacturing Gross Output

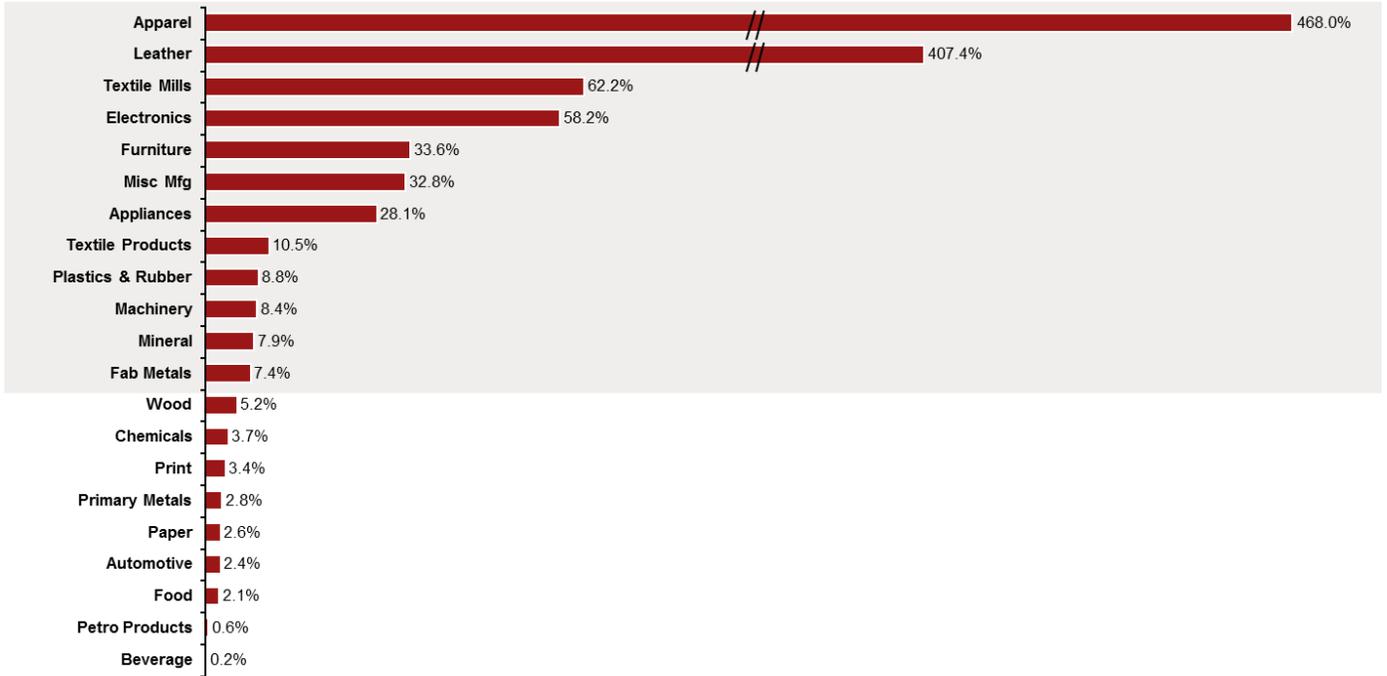
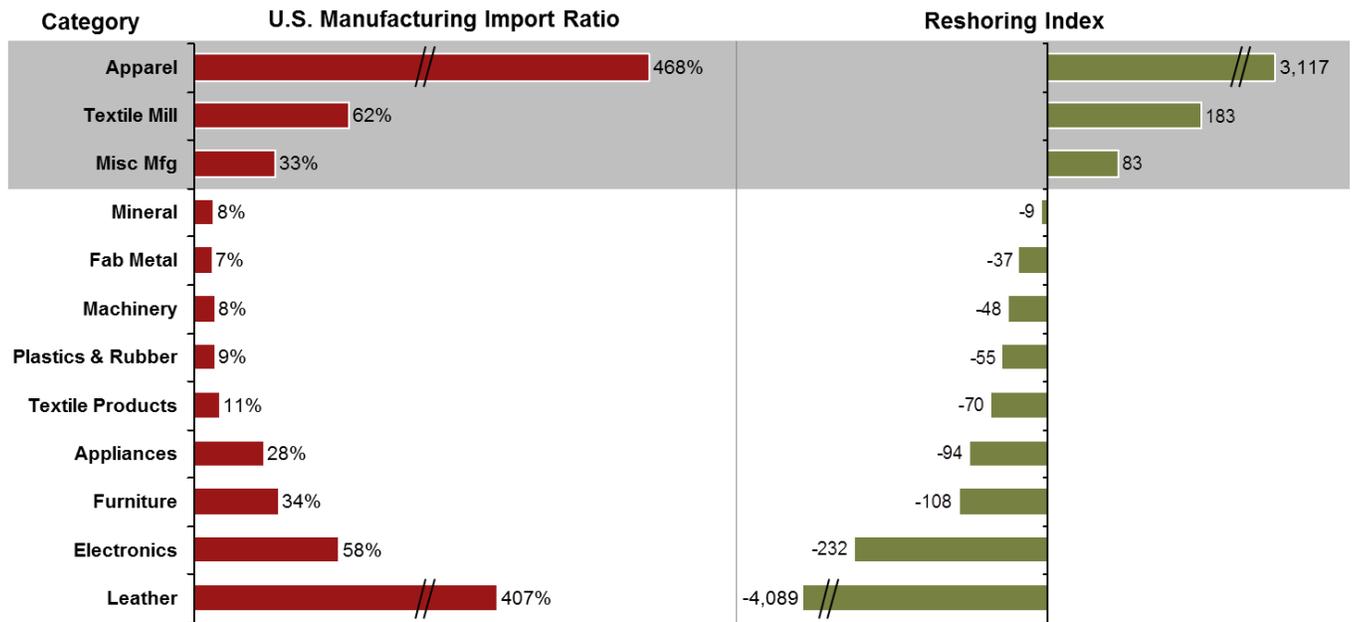


Figure 8

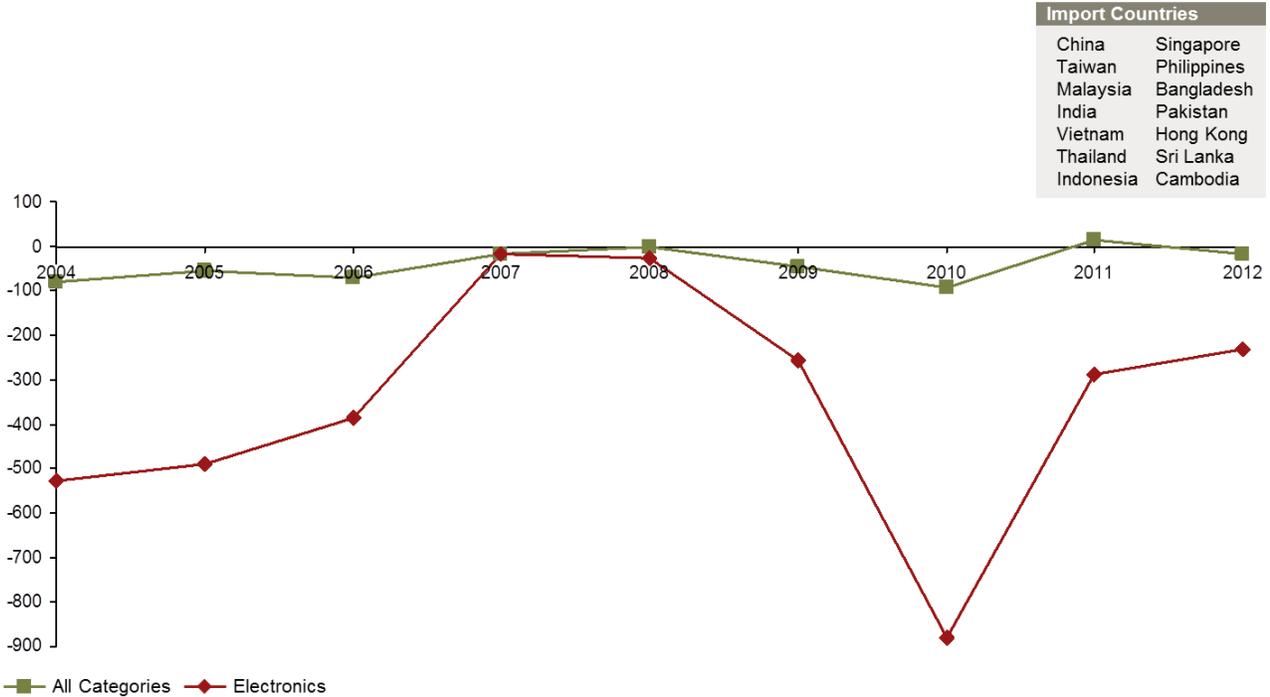
2012 U.S. Manufacturing Import Ratio (%) and 2011-2012 Reshoring Index (bp)



Source: United States International Trade Commission; United States Department of Commerce Bureau of Economic Analysis

Compare apparel (see also panel on “The Unexpected Case of Apparel”) to electronics, the single largest category of imported manufactured goods. For various reasons, electronics is often on the list of industries on the “tipping point” of reshoring, and there are many individual case studies among electronics manufacturers. But the value of electronics offshore imports (\$226 billion in 2013, more than three times larger than the next largest category apparel), as well as the growth rate, has been so high that U.S. manufacturing has been hard pressed to keep up. With few exceptions, the Reshoring Index for electronics has historically been significantly lower than the overall Reshoring Index. Consider what has happened to computers and peripheral equipment, one of the largest sub-categories under the electronics industry. Between 2009 and 2012, the value of offshore imports into the U.S. for computers and peripheral equipment increased by \$23 billion, at the same time that domestic gross output decreased by \$23 billion. With year-over-year offshore import value growth slowing for electronics to a relatively modest 1.9 percent in 2013, are we now at the tipping point? We will leave that for the time being to the prognosticators, but at least we now have a robust Reshoring Index to indicate the inflection, as and when it is reached. (see Figure 9)

Figure 9
A.T. Kearney Reshoring Index—Electronics vs. All Categories
Year-over-Year Change in the U.S. Manufacturing Import Ratio
 (Basis Points, 1999 – 2012)



Import Countries	
China	Singapore
Taiwan	Philippines
Malaysia	Bangladesh
India	Pakistan
Vietnam	Hong Kong
Thailand	Sri Lanka
Indonesia	Cambodia

Source: United States International Trade Commission; United States Department of Commerce Bureau of Economic Analysis

The Unexpected Case of Apparel

When you think of which industries might be interested in reshoring, apparel, with its labor-intensive operations well-established in low-cost countries, is usually not at the top of your list. However, as identified in both A.T. Kearney's Reshoring Database and A.T. Kearney's Reshoring Index, apparel has been a top reshoring industry for the past two years.

When seen from a macroeconomic perspective, the apparel industry had the highest Reshoring Index value of any industry in 2012. The numbers bear it out: between 2011 and 2012, the value of offshore apparel imports decreased by \$845 million, while U.S. manufacturing gross output for apparel increased by \$640 million. Admittedly, these are not large numbers in the scope of the U.S. economy—or even the broad sweep of cut and sew offshoring—but they are a clear demonstration of the tangible results of reshoring in that industry. So, what is driving this?

A segment of apparel companies, usually premium and brand-/image-driven, are reshoring for the following reasons:

- Responsiveness to meet changing “fast fashion” trends and volatile consumer demand
- Closeness of product innovation, manufacture, and point of sale provides a competitive edge
- Leaner and shorter inventory pipeline to mitigate the rising cost of retail discounting
- Reliability of supply and elimination of oversight functions especially for low-volume, high-quality boutique companies
- Brand value (ethical reputation or able to capture premium for Made in America)
- Manufacturing costs are not relevant given the high margins of premium products

Many of these apparel manufacturers rightly argue that smaller runs of high-quality garments that sell at full-price are far better than volume runs of garments that have to be sold at discount. The need to continuously shrink and optimize the supply chain will remain in the foreseeable future.

But other companies also bank on the Made in America brand as a way to differentiate and compete. In a recent market test, Karen Kane dresses, blouses, and jackets promoted with Made-in-USA posters at Dillard's department store posted 15 percent higher sales than similar non-promoted clothing.

What makes the A.T. Kearney Reshoring Index so powerful? Three key reasons:

- It represents the choice that U.S. executives are making between domestic production and offshore production to meet U.S. and export demand. What is most important to the U.S. economy (and to figure out whether reshoring is truly happening on a big scale) is changes in share, not absolute values, between domestic and offshore manufacturing.
- It normalizes changes in market demand. For example, an increase in U.S. manufacturing to meet demand does not necessarily point to an increasing trend of reshoring if offshore manufactured goods imports have increased at a faster rate.
- It depicts flows of domestic and offshore trade, not shifts in physical assets or employment levels. If a U.S. company idles its China manufacturing plant during a downturn in order to keep its domestic operation running, that scenario still counts as reshoring in our Index (as it should)—even if the tooling was not returned from China or the domestic employment levels did not change.

Conclusion

With both our comprehensive Reshoring Database and our Reshoring Index, A.T. Kearney is hoping to shed more light on the subject and cut through the hype to get to a clear, fact-based view of what is really happening and at what scale. Are we able to project exactly what the future holds for reshoring? No, but that was not the objective of this study. However, we now have two powerful indicators of actual reshoring activity, as the reshoring trend continues to evolve and take shape.

As to the question of whether or not to reshore your operation, for many industries and a number of product categories, the answer may indeed be “Yes.” But a follow-the-herd mentality is misplaced since, as it turns out, there’s probably less of a herd than the hype may have led you to believe and for most industries, the answer is much more nuanced and dependent on the particular characteristics of each industry as well as your company’s individual situation. Instead, prepare for an exhaustive review (see A.T. Kearney’s white paper “Solving the Reshoring Dilemma”) and keep tracking the A.T. Kearney Reshoring Index to uncover the real reshoring trends in your industry.

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