



Supply chain disruptions and sourcing strategies

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- Since the COVID-19 pandemic, many companies have seen their supply chains disrupted and tested more than ever before.
- Recent literature has found that long-term sourcing relationships might help mitigate the impact of supply chain disruptions.
- Using the garment industry as a testing board, this study presents empirical proxies for two distinct dimensions of a buyer's sourcing strategy – namely, the extent to which buyers follow a spot versus a relational approach to sourcing and the extent to which buyers follow just-in-time (JIT) inventory systems.
- Results show that: a) the variation in both measures is mostly explained by across-buyer variation rather than product or country variation, b) the two measures are highly correlated with each other, and c) certain buyers' characteristics correlate with the type of sourcing system.

Introduction

Supply chain disruptions and their economic consequences currently play a central role in academic and policy debates. In 2021, the President of the United States emphasised the need for resilient, diverse, and secure supply chains to maintain economic prosperity and national security. Similarly, the European Union has implemented policies designed to enhance domestic capacity, diversify suppliers, and support a multilateral, rules-based trade system.

In light of these developments, this study 1) reviews existing literature on supply chain disruptions, focusing on the potential mitigating role of long-term relationships, and 2) makes progress in characterising buyers' sourcing strategies, using the garment sector as a testing board.

The study presents empirical proxies for two distinct dimensions of a buyer's sourcing strategy. The first proxy, originally introduced by Cajal-Grossi et al., (2022), measures the extent to which buyers follow a spot versus a relational approach to sourcing. The second proxy, introduced in our paper,¹ measures the extent to which buyers follow just-in-time (JIT) inventory systems. Both measures can be calculated using transaction data that includes information about the buyer and supplier, which is becoming more readily available for international and domestic transactions through customs and VAT records. The proxies can thus be used to map sourcing systems in other supply chains. We implement the two proxies in the garment sector using customs records from six different sourcing countries.

The study presents three sets of results:

- Buyer fixed effects – rather than product and country effects – account for the vast majority of variation observed in sourcing strategies.
- These two measures are highly correlated with each other. Across buyers, a JIT inventory system tends to go hand-in-hand with a relational approach to sourcing.
- Exploring the extent to which buyers' characteristics correlate with the type of sourcing system, we find that larger buyers are more likely to be relational and to use JIT, and that buyers specialised in the retail of branded garments – and thus further downstream – are also more likely to be relational and to use JIT.

¹ This policy brief is based on ongoing work, Cajal Grossi, et al., (2023).

Policy motivation for research

This project examines buyers' sourcing strategies in the garment sector and considers their role in mitigating supply chain disruptions. This is of particular importance to policymakers, who may be interested in leveraging the mix of buyers to whom exporters supply, as a margin for policy. The study is timely in its policy implications for two reasons.

First, many companies have recently seen their supply chains disrupted and tested more than ever before. As Grossman et al. (2021) simply put it, supply chain disruptions have become the new normal. For example, the 2021 Supply Chain Resilience report from BCI found that 25% of firms experienced more than ten disruptions in 2020 compared to less than 5% in 2019 (BCI, 2021). Drawing from recent experience in the garment sector during the COVID-19 pandemic, the halting of production in China in February 2020 was followed by the temporary or permanent closure of shops around the world. This led brands and retailers to cancel or postpone production orders, refusing, in many cases, to pay for clothing their supplier factories had already produced. The result has been the partial or complete shutdown of thousands of factories in producing countries.

Second, through its focus on the garment industry, the study analyses a sector that employs 60 million workers worldwide, nearly 75% of whom are women, and which has been credited for playing a critical role in the early industrialisation of many countries. This is also a labour-intensive industry, in which the pursuit of lower labour costs has shifted the sourcing of products for high-income markets to production in low- and middle-income countries – mainly China and other Asian countries, such as Bangladesh, Pakistan, and Vietnam. This turns the industry into a potentially strong engine for growth in these countries but also exposes the livelihood of millions to supply chain disruptions. In this sense, well-performing, resilient sourcing systems are critical for growth and development.

Policy impact: The project will be of interest to policymakers who are promoting the development of the apparel sector and, more generally, export and industrial development. It will inform them about whether they should be concerned about the mix of buyers to whom their exporters supply. We expect that the findings of the project will result in the formulation of appropriate policies to address the issue.

Policy recommendations

- **To whom you export matters – not just what and where**

A growing body of literature has documented how firms, even within narrowly defined industries, develop distinctive approaches to sourcing. The buyer's choice is, therefore, not only an important dimension of upgrading for exporting firms in low- and middle-income countries but also has implications for their resilience to and transmission of shocks.

- **Responsiveness and relational sourcing strategy**

Buyers specialised in the retail of branded garments are also more likely to be relational and to use JIT. As these buyers need to be more responsive to changes in fashion trends, this provides further suggestive evidence that a relational strategy might be relatively more suitable in contexts that require frequent changes and adaptation – such as the new normal.

References

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