Dynamic Supply Chain Capabilities: A Case Study in Oil and Gas Industry

Shatina Saad¹, Zulkifli Mohamed Udin², Norlena Hasnan³

¹Faculty of Business Management, Universiti Teknologi MARA
42300 Bandar Puncak Alam, Selangor, Malaysia
'shatina@salam.uitm.edu.my

²School of Technology Management and Logistics, Universiti Utara Malaysia
06010 Sintok, Kedah, Malaysia
'zulkifli@uum.edu.my

³Universiti Utara Malaysia Kuala Lumpur
41-3 Jalan Raja Muda Abdul Aziz, 50300 Kuala Lumpur, Malaysia
'norlena@uum.edu.my

Abstract— Supply chain (SC) is a dynamic process that entails a continuous flow of information, materials and funds across multiple functional areas, within and between chain members in order to meet customer’s requirements and to maximize their profit. Such dynamic process requires instantaneous acquisition and constant re-evaluation of partners, technologies and organizational structures. However, firms may encounter problems related to the dynamic process. Petroleum companies, in this globalization era are one of the dynamic supply chain entities, which require dynamic processes of capabilities, due to their high degree of uncertainties. Motivated by the complexity of uncertainty in the petroleum companies and its typical characteristic of SC, this study intends to understand the process of dynamic SC management. Using the resource-based view and organizational learning theory as the basis for developing the framework of the study, this study aimed to identify and understand the process of dynamic SC capabilities. Company in oil and gas in Malaysia will be chosen as the sample case in understanding the process of the dynamic SC capabilities and SC performance. Due to the subjectivity of the study that requires understanding process of SC, this study proposes to employ interpretive paradigm where it would guide towards rigour qualitative methodology. This study will provide rich and thick description of the dynamic of SC where the outcome will contribute to the managerial and theoretical perspective of SC management in oil and gas industry.

Keywords— dynamic supply chain, dynamic capabilities, supply chain management, case study, oil and gas

1. Introduction

Supply chain management (SCM) has received in recent years a great deal of attention by researchers and practitioners. Effective SCM will lead to a lowering of the total amount of resources required to provide the essential level of customer service to a specific segment and improving customer service through increased product availability and reduced order cycle time [1]; engage in information exchange (forecasting techniques, inventory management, delivery) and structural collaboration (just-in-time system, outsourcing, vendor-managed inventory and co-locating plants) [2, 3]; relationships with downstream supply chain partners to create end-customer value [4] and maximize benefits and minimize costs along the supply chain [5]. Thus, the nature of SCM becomes visible to participating companies with successful implementation in the ever-changing global environment of the business world. Risks abound, and it greatly affects the decision-making processes of the business management.

According to Jain, Wadhwa and Deshmukh [6], a supply chain is a dynamic process and involves the constant flow of information, materials, and funds across multiple functional areas both within and between chain members. Members in the chain need to cooperate with their business partners in order to meet customer’s needs and to maximize their profit. However, it is a very difficult task in managing the multiple collaborations in a supply chain because there are so many firms involved in the supply chain operations with its own resources and objectives. The interdependence of multistage processes also requires real-time operation and decision making across different tasks, functional areas, and organizational boundaries in order to deal with problems and uncertainties. The strategic move of focus for mass customization, quick response, and high-quality service cannot be achieved without more complex cooperation and dynamic structure of supply chains.

Teece, Pisano and Shuen [7] identified a dynamic collaboration capability should help a company access, shift and leverage supply chain resources to rapidly respond to a changing competitive environment. A dynamic process also involves the simultaneous acquisition and continuous re-evaluation of partners, technologies,
and organizational structures. Firms may encounter the same problems, but they may have different awareness and potential solutions due to differences in their engagement of stakeholders. The more flexible and open of the firms to the issues there is more likely for them to explore, create, and invest in the dynamic capabilities [8, 9]. Therefore, firms that possess a dynamic collaboration capability should be able to sustain high-performance levels over time.

Environmental uncertainties in oil and gas industry lead to a need for higher reliability and flexibility within the production systems and the planning and control systems in the supply chain. Reducing these uncertainties will be achieved by understanding the root causes and how they interact with each other. Change in markets, products, technology, and competitors are occurring at an increasingly rapid pace [4, 10]. As a result, managers must acquire decisions on shorter notice, with less information, and with higher penalty costs. Therefore, a reliable yet a flexible system are fundamentally needed to assist the management in making decisions that might prove to be the make-or-break decision for their companies [11, 12].

O&G industry can be seen from several perspective namely personal, business and environmental issues. From a personal perspective, O&G provides the world's 6.9 billion people with 60 percent of their daily energy needs. As fuels and as petrochemical feedstock, O&G is the raw materials used to manufacture fertilizers, fabrics, synthetic rubber and the plastics that go into almost everything people use these days, from toys to personal and household items to heavy industrial goods [13].

Meanwhile, O&G also represents global trade on a massive scale in business perspective. Over 200 countries have invited companies to negotiate for the right to explore their lands or territorial waters, hoping that they will find and produce O&G, create local jobs and provide billions of dollars in national revenues [13].

Finally, from a health, safety and environmental perspective, there is a continuous concern for safety in O&G operations, the impact that new projects have on surface environments, the possibility of oil spills and the effect of pollutants such as CO2 (carbon dioxide) on global climate change and air quality. The O&G business is clearly a comprehensive, global industry that impacts all aspects of one’s lives.

Supply chain in the O&G industry for quite some time was not taken seriously by players in an industry where technical advancement and time were the core values aiming only for fast exploration and high production of O&G. Mohammad [14] stated that it was initially considered a “soft issue” in the industry until players beginning to realize that 80% of all operating expenses were spent on the supply chain system. They also noticed that the successful of project depends if careful attention and precautions on the procurement or supply chain system are taken seriously.

It was therefore, not surprising that few articles are published on a dynamic supply chain, specifically in an O&G industry to the related journals. Many of the articles found in the supply chain in journals or other publications prior to this have done research on the dynamic supply chains referring to the manufacturing, retailing and using modeling techniques as a method in deliberating the decision [2, 15-17].

Based on the literature survey of studies conducted in Malaysia, several studies on the supply chain issues include: value changes and multicultural complexity [14]; collaborative supply chain [18]; outsourcing [3] sustainability and environmental control [19]. Although there are many new technological breakthroughs in exploration and production [12, 20, 21], there has been insufficient development in dynamic supply chain strategies and methods. Many ideas have simply been taken on those used in other sectors or industry rather than considering the specific need of the O&G industry. Thus, this study will be focusing on exploring the dynamic supply chain capabilities on the O&G companies in Malaysia.

1.1 Research Objectives

Generally, the research objective is to examine and understand the dynamic supply chain in the organizations, specifically for O&G industry in Malaysia's environment. The focus will be at the internal and external firm’s capabilities of dynamic supply chain capabilities and controls by the environmental uncertainty of the O&G industry.

The research specific objectives are as follows: 1) to identify any association of internal firm’s capabilities and dynamic supply chain capabilities in O&G industry in Malaysia; 2) to identify any association of external firm’s capabilities and dynamic supply chain capabilities in O&G industry in Malaysia.

1.2 Significance of Research

From the theoretical perspectives, this study utilizes dynamic capabilities, industrial system, resource-based view and organizational learning theory. These theories discuss the importance of information and materials as unique resources in SCM for the competitive advantage. It will represent an exploratory study on dynamic supply chain capabilities of the O&G industry in Malaysia. Furthermore, it will provide information to develop a better understanding of dynamic supply chain
capabilities towards strategies and decision made in the internal and external firm’s capabilities.

From the managerial point of view, this study will benefit them in several ways. The results of this study will be expected to show the performance of a dynamic supply chain on O&G industry. This will help the players in the industry to understand the progress and future actions that could improve the SCM competitiveness in of Malaysia.

The remainder of this paper is organized as follows. Section 2 reviews the related literature, and Section 3 describes the research methodology. Section 4 reports the results of the case study, whilst Section 5 presents the conclusions and suggests directions for future research.

2. Literature Review

The petroleum industry can be characterized as a typical supply chain where all levels of decisions (strategic, tactical, and operational) may arise in it. Management of the petroleum supply chain is a complex task due to the large size of the physical supply network which dispersed over vast geography, complex refinery production operations, and inherent uncertainty. Shah et al. [12] stated that uncertainty arises in realistic decision making processes and has a huge impact on the refinery planning activities. Three major uncertainties that should be considered in refinery production planning include: market demand for products; prices of crude oil and the saleable products; and product or production yields of crude oil from chemical reactions in the primary crude distillation unit.

The dynamic capability viewpoint has had a significant impact on strategic management research in general and in research regarding organizations and the natural situation in particular. It offers the potential to extend and complement the Resource-based view (RBV) to create a more thorough understanding of the process by which firms undertake sustainable development strategies. The dynamic capabilities perspective, with its emphasis on variation within uncertain and dynamic markets, is particularly well suited to the study of supply chain management strategies. This is because the perspective in which firms develop capabilities to deal with these issues is highly complex and unclear [9].

As already emphasized [22], trust plays a crucial role in the development of any long-term relationship and is especially important in strategic partner relationships. In general, trust is an accumulated product of repeated past interactions among parties through which they come to understand themselves and develop a common knowledge of mutual commitments. In the supply chain network context specifically, the effectiveness of collaboration is dependent on a firm’s initiatives to build and foster trust with its partners [23], which can improve responsiveness even when suppliers have more power than buyers in the supply chain.

2.1 Oil and Gas Supply Chain Management

Petroleum companies, also known as Oil and Gas (O&G) companies have formed a key part of the global economy for the last decade since petroleum or crude oil has become the main fuel source. By 2020, Malaysia will have a more diversified oil, gas and energy sector that remains vital to the nation development, and that builds on the nation’s competitive advantages. A key thrust not only to intensify exploration and enhance production from domestic reserves but also to develop a strong regional oilfield services and equipment hub and a stronger presence in the regional midstream logistics and downstream markets [24]. Malaysia’s national O&G Company, Petroleam Nasional Berhad (Petronas), holds exclusive ownership rights to all O&G exploration and production project in Malaysia. As Malaysia’s oil fields are maturing, the government is focused on enhancing output from existing fields and from new offshore developments of both O&G, which are expected to increase aggregate production capacity in the near-to midterm [25]. Among other major players in Malaysia O&G industry are Esso Malaysia Berhad and Shell Malaysia Limited.

Shah, Li, and Ierapetritou [12] stated that a typical petroleum industry supply chain is composed of an exploration phase at the wellhead, crude procurement and storage logistics, transportation to the oil refineries, refinery operations, and distribution and transportation of the final products. The upstream activities (exploration, development and production of crude oil or natural gas) and downstream activities (tankers, pipelines, retailers and consumers) are two important activities in the petroleum industry [19]. SCM in O&G industry requires the company to integrate its decisions with those made within its chain of customers and suppliers. This process involves relationship management of the company to their customers and suppliers. A firm can create long-term strategic relationships with their suppliers and in most cases there is a collaborative process between the oil and gas company with its suppliers [5]. Generally, O&G companies view their supply chain configuration and coordination systems as worthy of improvement. Making necessary improvements over time allows the firm to gain competitive advantages in the marketplace.

Furthermore, in the oil refinery industry, the supply-chain network is composed of shipping via vessel, oil tankers, and pipelines that may run
across multiple countries. This network is used to transport crude from wellhead to refinery for processing, to transport intermediates between multi-site refining facilities, and to transport finished products from product storage tanks to distribution centers and finally to the customers. Any disruptions arising in the global supply chain can have tremendous adverse effects in achieving operational efficiency, maintaining quality, profitability, and customer satisfaction. The adverse events may happen due to uncertainty in supply of crude, demand, transportation, market volatility, and political climate. Hence, Shah et al. [12] identify that to effectively model a supply-chain design problem, the dynamics of the supply chain ought to be considered and data aggregation techniques for the extensive data set should be employed.

2.2 Scope and Limitation of Research

This study will be focusing on exploring issues on dynamic supply chain capabilities on O&G industry only, thus the generalization cannot be done in other organizations and industry throughout Malaysia. The assumption of this study is that the major players in the O&G industry are doing the similar practices in managing their supply chain. In the exploration and production sectors of the oil and gas industry, the product is exactly the same for all competing firms with very narrow product differentiation. Thus, exploration and production companies can only differentiate themselves based on the ability to economically find and produce O&G more efficiently than their competitors. Even though exploration and production companies are unique in many fields, a differentiating factor can lie in the ability to adapt an SCM agenda.

3. Research Methodology

This study is an exploratory since not much is known about the situation of dynamic supply chain capabilities in oil and gas industry in Malaysia environment. An in-depth study are undertaken to better comprehend the nature of the problem, since very few studies have been conducted in the dynamic supply chain capabilities [26-28].

In addition, when the phenomenon of interest is new, dynamic or complex, relevant variables are not easily identified and extant theories are not available to explain the phenomena. In this situation, a qualitative approach is often preferred in order to build understanding grounded in a detailed description of the phenomenon generated by collecting field data. It provides researchers with access to a deeper level of understanding of new or complex phenomena by yielding a high level of details [29, 30].

Yin [31] and Eisenhardt [30] give useful insights into the case study as a research strategy, but leave most of the design decisions for further discussion for both the strengths and the weaknesses. The strength of case study is tailoring the design and data collection procedures to the research questions. On the other hand, this approach has resulted in many poor case studies, leaving it open to criticism, especially from the quantitative field of research. The fact that the case study is a rather loose design implies that there are a number of choices that need to be addressed in a principled way [32].

3.1 Research Sample

The concept purposive sampling is employed for the study because the researcher selects individuals and sites for the study. The decision need to be made about who and what will be sampled, what form the sampling will take and how many people or sites need to be sampled [27, 29, 33]. Since this study is conducted in the O&G industry, gaining an in-depth insight into advanced practices which later set the ground for the generation of proposition [34]. The snowball or chain case selection technique is employed with the procurement and supply chain function in the organization as the unit of analysis [29].

3.2 Case Study

This study employs the case study protocol suggested [35] as in Figure 1. The first step in the case methodology is to define the research questions. As stated before, the research objectives of this exploratory phase were: (1) To identify any association of internal firm’s capabilities and dynamic supply chain capabilities in O&G industry in Malaysia, (2) To identify any association of external firm’s capabilities and dynamic supply chain capabilities in O&G industry in Malaysia.

The following steps refer to the process of determining the unit of analysis. As supply chain management involves the integration along the supply chain, the most appropriate approach in the study would have been considering all elements in those chains such as retailers, third party logistics providers, refiners, purchasing centers, etc. But, due to the need of limiting the scope of the study, the study will focus on the upstream and downstream from the oil and gas industry in Malaysia. The most appropriate approach to analyzing these relationships will be to analyze particular upstream – focal – downstream organizations triad, but this approach was not possible due to the discretion of the interviewees to identify the supply chain partner they were talking about.
In order to increase the reliability of the case study, an interview protocol and a case study database are developed. With respect to how to link the data to the research questions, a chain of evidence will be established in order to allow any external observer to follow the derivation of any evidence from initial research questions to ultimate case study conclusions.

After establishing the interview protocol and how to link the data to the research questions, interviews with companies will be conducted. Companies among the leaders in different product categories, and selected upstream and downstream companies will be selected among the top supply chain in O&G industry.

Data collected will be introduced in the case database, which will be analyzed to obtain the conclusions. Other sources of evidence such as newspaper clippings and articles also will be used to corroborate and augment evidence.

4. Findings

Some case studies can be found in the literature on how a fully integrated supply chain practices program can be used by an oil and gas company to improve operational efficiency, resulting to lower cost per well. The contribution of oil in Malaysia energy mix was once up to 87.9% before the Four-Fuel Diversification Strategy was implemented in 1981. After the international oil crisis in 1973 and 1979, the government had called for the diversification of energy resources to prevent over-dependency on oil. Malaysia has proven oil reserves of 5.46 billion barrels as of January 2008. The majority of the country’s reserves is located off the east coast of Peninsular Malaysia and tends to be of high quality.

Several new oil production projects have come online during the last few years, although Malaysia’s oil output declined somewhat in 2006. Average production for 2006 stood at 798,000 barrels/day (bbl/d), down 7% from 2005 levels. In 2006, Malaysia consumed an estimated 515,000 bbl/d of oil, with net exports 283,000 bbl/d. According to Oil and Gas Journal, Malaysia had about 545,000 bbl/d of refining capacity at six facilities as of January 2007. Malaysia’s state-owned national oil company, Petroleam Nasional Berhad (PETRONAS), dominates upstream and downstream activities in the country’s oil sector. PETRONAS operates three refineries (259,000 bbl/d total capacity), while Shell operates two plants (200,000 bbl/d), and ExxonMobil one (86,000 bbl/d) [36].

Malaysia total investment approved in 2012 is RM162.4 billion including the services (72.4%), manufacturing (25.3%) and primary (2.3%). During the first half of 2013, totaled of the RM16.8 billions has been invested in the primary sector as compared to the RM2.6 billions in 2012. Those investments extremely from upstream oil and gas activity's projects with investments of the RM16.6 billion [37, 38].

Malaysia has invested heavily in refining activities during the last two decades, and is now able to meet the country’s demand for petroleum products domestically, after relying on the refining industry in Singapore for many years. Despite growth in exploration activities and few new projects that are set to come on-stream in the next number of years, Malaysia’s proven oil reserves have declined in recent years, and the oil production fell 13% from 2008. Provided that the production rate is consistent at average of 700,000 bbl/d, Malaysia’s oil reserves will be worn out in around 20 years.

Malaysia Petroleum Resources Corporation identifies that 90% of annual turnover in O&G industries are coming from domestic projects. These domestic projects comprise from the local suppliers in Malaysia. These domestic suppliers involve 84% as services providers and 16% in products' supplies. The services' providers are mainly in 63% and 32% coming from production and development phases respectively and majorities are in minor fabrication, maintenance and manpower services. Furthermore, many companies needed for technologies to support the O&G industry in Malaysia. Furthermore, there are more than 4,200 domestic product supplies for O&G industry in Malaysia. These are mainly in
mechanical, electrical and instrumentation, chemicals and safety system and also the highest are for the office supplies.

Supply chain network is made up of individual firms collaborating to serve end customers; therefore, its effectiveness is greatly dependent on trust between the network partners. In fact, trust plays a crucial role in the development of any long-term relationship. Trust also tends to improve the average cycle time and in-time order fulfilment rate and supply chain financial performance [39].

5. Conclusion

As a summary, studies on dynamic supply chain capabilities of O&G industry identified in several elements such as internal firm’s capabilities, external firm’s capabilities and environmental uncertainty. As previous studies looked at the variables independently few attempts were made to link between dynamic supply chain capabilities and dynamic supply chain performance. This study also integrates the internal firm’s and external firm’s capabilities as they are considered crucial in ensuring the dynamic supply chain capabilities are well practiced. Trust and supplier’s relationship plays a major role as the internal firm’s and external firm’s capabilities. Having the environmental uncertainty as control to build dynamic supply chain capabilities as it will modify dynamic supply chain performance and helps in any competitive advantage in the O&G industry in Malaysia.

Acknowledgments

The authors would like to thank gratefully Ministry of Higher Education of Malaysia for funding this research under the IPTA Academic Training Scheme (SLAI).

References


