Webinar: Defining and Implementing Effective Sourcing Strategies

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Defining and Implementing Effective Sourcing Strategies
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Agenda

Supply Management Changes and Trends

The Importance & Role of the Procurement Function

Strategic Sourcing
Key Themes

Key areas of focus for this session include:

- The supply function has experienced dramatic change over the last 20 years and a number of significant trends have developed.

- The procurement function fulfills a critical role in the supply chain.

- A number of key sourcing strategies exist as well as practical approaches to planning for the sourcing of critical products and services.
Agenda

Supply Management Changes and Trends

The Importance & Role of the Procurement Function

Strategic Sourcing
Supply Management Changes and Trends Over the Last 20 Years

- Purchasing has experienced dramatic change over the last 20 years.

- Once regarded as a reactive activity, capable only of neutral or negative contribution, the procurement and sourcing process at leading firms has been at the forefront of responding to, and creating, change.

- The ability of purchasing, often in collaboration with other functional groups, to affect cost, quality, time, technology, and, ultimately, customer satisfaction has been substantial.
Megatrends Affecting Business and Procurement 2020

- Socially Responsible Corporations
  - Consumers and investors will associate themselves with organizations that support their ethical ideals.
  - The two main avenues for these responsibilities are human rights and environmental performance.
  - It is business and procurement’s responsibility to manage and own these relationships with a supply base that will inevitably come under closer scrutiny over the coming decades.

- The Rise of Asia
  - The rise of Asia will change the procurement function in two key ways.
  - First - and we are already seeing signs of this today - countries such as China will move from being low-cost sourcing hubs to sources of innovation.
  - Along with this we will begin to see Asian markets rise in importance with reference to their consuming power.
Megatrends Affecting Business and Procurement 2020

Persistent Insecurity and Increased Risk
- Working across borders opens business and the procurement teams that service business up to a greater level of risk in maintaining a secure supply chain.
- These risks can relate to terrorist threats, political instability and even environmental considerations.
- The fact that we have begun to operate in more geographies means that our operations now have a greater surface area, exposed to political instability and natural disasters.

Scarcity of Natural Resources
- As the world continues on its rapid path of development and modernization, competition for natural resources will become so intense that we will move beyond straightforward inflation.
- The supply of critical resources will no longer be a question of money; securing the limited amount of natural resources available will become the key challenge.
- An early example of this megatrend is the current issue surrounding the supply of rare earth metals.
Megatrends Affecting Business and Procurement 2020

- **Diversification of Offering**
  - In order to meet evolving consumer needs, companies will provide ever more personal and customized services and products.
  - This holds particularly true when we consider the growing markets of the developing world.

- **Supplier Management & Cross-Functional Collaboration**
  - Product life cycles are getting shorter and shorter and the hunger for new and innovative features is growing further.
  - Being ahead of competition requires an intimate knowledge of all relevant technology trends and the ability to integrate them into the development of new products.
  - Companies will be able to win the race only with strong suppliers and a close collaboration with R&D and other disciplines…
Megatrends Affecting Business and Procurement 2020

Ease-of-Use
- Procurement’s role is changing from a "back-office function" to a service provider, putting customer satisfaction in the middle of the procurement score card.
- The development of future procurement systems must start with the end-user.
- Cloud-based solutions that combine latest software technologies and best practice content will allow for “faster” procurement events and start-ups.

Use of Technology
- Cloud based systems and social media are changing the face of business and how procurement meets the needs of business.
- The ability to access and use “big data” will become a critical differentiator for business and for procurement groups as they seek to understand trends and access and interpret strategic market information.
- Social media is changing the way markets react to new products and services and the way shoppers shop and will continue to play a major role in how procurement groups react to the needs of business that service markets and individuals in these markets.
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Supply Management Changes and Trends

The Importance & Role of the Procurement Function

Strategic Sourcing
In order to increase long term shareholder value every firm must increase revenue, decrease costs or both.

Procurement’s contribution should not only be focused on cost-it should also be concerned with revenue enhancement.

The supply function continues to evolve as technology and the worldwide competitive environment require innovative approaches.
The Importance & Role of the Procurement Function

- Negotiation is replacing competitive bidding (where appropriate), longer term contracts are replacing short term buying techniques.

- “E” commerce tools permit faster and lower cost solutions not only on the transaction side but for management decision support (e.g. spend data analysis).

- All of these trends are a logical outcome of increased managerial concern with the value and increasing procurement aggressiveness to meet specific supply objectives of quality, quantity, price, service, continuity of supply and continuous improvement.
Effective procurement contributes significantly to organizational success.

Today the emphasis is on the supply management process in the context of organizational goals and management of supply chains.

The rapidly changing supply environment with cycles of abundance and shortages, varying prices, lead times and availability, global sources of supply, etc., provides continuing challenges to procurement professionals.

In addition environmental, security and financial regulatory requirements have added considerable complexity to the procurement professionals task of ensuring that supply and suppliers are used to provide competitive advantage.
There is a shift from predominantly defensive strategies resulting from the need to remain competitive to more aggressive strategies in which firms take an imaginative approach to achieving supply objectives.

This now includes an emphasis on processes and improvement thereof, the understanding of the competitive and other forces driving market prices, knowledge of supply chain (including global supply chain) implications for supply total costs, etc.
The Importance & Role of the Procurement Function

- The financial impact that the procurement function can have on the financial well being of an organization is significant.

- The financial impact of the corporate spend can be illustrated by the profit leverage effect and the return on assets effect.

- The profit leverage effect is measured by the increase in profit obtained by a decrease in purchase spend.
The Importance & Role of the Procurement Function

Typical “cost reduction” initiatives focus on workforce reduction or discretionary operating expense across the company.

A small reduction in external spend will significantly improve bottom-line profits

A strategic approach to the total cost management of external spend provides a greater opportunity.
Agenda

Supply Management
Changes and Trends

The Importance & Role of the Procurement Function

Strategic Sourcing
Let’s Position Our Thinking...

**Quantify and Categorize Total Spend**
- What do we spend across our purchase categories and business units?

**Recognize a Supply Need Exists**

**Tender management**

**Evaluate and Select Suppliers**
- Which suppliers will receive purchase contracts? What are our supply strategies?

**Manage Suppliers**
- What must we do to manage the supply base effectively and efficiently, including performance measurement?

**Develop and Improve Supplier Capabilities**
- What efforts should we put forth to develop and improve supply base performance?
Strategic Sourcing

- is an institutional procurement process that continuously improves and re-evaluates the purchasing activities of a company
- is a systematic and fact-based approach for optimizing an organization's supply base and improving the overall value proposition
- is an organized and collaborative approach to leveraging targeted spend across locations with select suppliers that are best suited to create knowledge and value in the customer-supplier interface
- is an approach to supply chain management that formalizes the way information is gathered and used so that an organization can leverage its consolidated purchasing power to find the best possible values in the marketplace
- is a method of managing procurement processes for an organization in which the procedure, methods, and sources are constantly re-evaluated to optimize value to the organization
How About This Approach?

**Strategic**: Decisions or plans designed to impact favorably the key factors on which the desired outcome of an organization, game, system, venture, or war, depends.

**Sourcing**: The process of finding suppliers of goods or services

From: www.businessdictionary.com
Defining Strategy

The strategy of an organization, or of a subunit of a larger organization, is a conceptualization of:
- long-term objectives and purposes of the organization
- broad constraints and policies that restrict activities
- current set of action plans and near-term goals expected to help achieve an organization’s objectives

An effective supply strategy consists of a number of parts—objectives, constraints, plans, and goals

This material is adapted from Richard Vancil, *Strategy Formulation in Complex Organizations*, Harvard University
Supply Management’s Contribution

Discussion Question

What can supply management contribute within an integrated strategy formulation process?
Sample Strategy Development Process

Step 1: **Identify Sourcing and Supply Opportunities**
An executive steering committee, working with functional managers, identifies supply strategy development opportunities offering the best return.

Step 2: **Establish Strategy Development Teams**
The executive steering committee charters cross-functional teams with members from worldwide locations participating. The committee provides resources as required.

Step 3: **Evaluate Sourcing Opportunities and Propose Strategies**
Teams validate the assumptions underlying the project, verify current volumes and expected savings, determine if qualified suppliers exist, evaluate the current set of specifications between design centers, and propose preliminary supply strategies. The executive committee reviews the recommendations developed by the strategy development teams.

Step 4: **Identify Requirements for Supplier Proposals**
Strategy development teams, working with other internal participants, pre-qualify suppliers and develop the request for proposal that suppliers receive.

Step 5: **Forward Proposals to Pre-Qualified Suppliers**
On average, teams forward proposal requests to six suppliers with responses expected within six weeks.
Sample Strategy Development Process

Step 6: Evaluate the Technical and Commercial Viability of Proposals
The team performs a commercial and technical evaluation of supplier proposals and conducts supplier site visits as required.

Step 7: Negotiate with the Most Qualified Suppliers
A smaller team negotiates with suppliers at the buying company’s U.S. headquarter. Negotiations, which last up to three days, lengthen if the buying company does not achieve its previously established improvement goals.

Step 8: Award Final Contract(s) to Winning Supplier(s)
Information concerning the awarded contract is communicated throughout the company. The steering committee reports expected savings to executive management and finance.

Step 9: Manage Transition to New Contracts and/or New Suppliers
Agreements are loaded into the appropriate corporate and contract management systems. The sourcing team manages the transition if the supplier and/or part numbers change from previous agreements or designs.

Step 10: Monitor Supplier Performance and Review Expiring Contracts
Performance measurement systems assess supplier performance and validate savings. The contract repository system notifies supply managers of expiring agreements six months prior to expiration.
Portfolio Matrix Analysis

A Tool for Developing Supply Strategies!
Portfolio Matrix Analysis

✓ This approach assumes that different kinds of strategies support different kinds of needs
✓ The portfolio matrix is a positioning tool
✓ Sometimes we position the good or service, sometimes the market positions the good or service
✓ This use of this tool helps prescribe...
  • The kind of supply strategy or approach to develop
  • The type of supplier relationship to pursue
  • Whether to practice cost or price analysis
  • Whether to engage in win-win or win-lose negotiation
  • How best to create value for your organization
  • How best to measure supply performance
What does **Win-Lose** mean?

What does **Win-Win** mean?

Let’s discuss…supply chain power and the economic continuum of markets
Segmenting Supplier Relationships and Approaches

Critical Items
- Collaborative relationships
- Cost focus
- Win/win approaches

Leverage Items
- Cooperative relationships
- Cost focus
- Usually win/win approaches

Transaction Items
- Transactional relationships
- Transaction cost focus
- Win/lose approaches

Market Items
- Competitive relationships
- Price focus
- Win/lose approaches

Value
- High
- Low

Items = purchased goods and services
## Segmenting Supplier Relationships

<table>
<thead>
<tr>
<th>Counter Productive</th>
<th>Competitive</th>
<th>Cooperative</th>
<th>Collaborative</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Also called antagonistic relationships</td>
<td>• Also called adversarial relationships</td>
<td>• Parties work together and share information</td>
<td>• Congruence of goals exists</td>
</tr>
<tr>
<td>• Parties work actively against the needs of each other</td>
<td>• Parties engage in competitive struggle over fixed value</td>
<td>• Closer relationships are a result of mutual goals</td>
<td>• Parties work together to create new business opportunities</td>
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<tr>
<td>• Neither party takes responsibility for what happens in the relationship</td>
<td>• Parties attempt to maximize value for their side</td>
<td>• Supplier and customer involvement increases</td>
<td>• Parties work jointly to identify creative solutions to problems</td>
</tr>
<tr>
<td>• Destructive conflict occurs</td>
<td>• Minimal sharing of information</td>
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### Outcomes

- **Lose/Lose**
- **Win/Lose**
- **Win/Win**
Strategic Supplier & Category Management

- **Strategic supplier management is:**
  - A supply strategy based upon joint opportunities, mutual trust, respect and open & honest communication between the customer and the supplier

- **Category management is:**
  - A structured process to maximize value from an organization's total supplier spend covering:
    - Category Planning
    - Subcategory Sourcing
    - Strategic Supplier Management
Why are Strategic Supplier Relationships More Important Now Than Ever?

- **Volatile Markets**
  - Price-focused sourcing strategies don’t work in periods of increasing commodity prices
  - More sophisticated relationship-based approaches are required to meet cost reduction targets
  - Based on recent increases in raw material, especially fuel, traditional unit based savings will not generate substantial savings, suppliers must be willing to provide creative solutions to remove costs from how they service or re-engineer the procured materials

- **Merger & Acquisition Trends**
  - Larger, national/global presences of many firms require more strategic supplier relationships to support growth and cost synergy targets

- **Expansion of Supplier Value-Added Services**
  - Suppliers continue to expand their value-added services offerings, increasing the value of strategic supplier relationships
  - Outsourcing
Strategic Relationship Characteristics

- **Types of Goods & Services**
  - High $ Spend
  - Critical business implications
  - Custom engineered
  - Limited availability or alternatives

- **Buying Considerations**
  - Trust is a major issue
  - Cross-functional involvement
  - Highly resource intensive
  - Long range planning required

- **Supplier Relations**
  - Longer Term Agreements
  - Total interaction
  - Close working relationship
  - Aligned objectives and philosophy
Strategic Relationship Criteria

- Potential for impact
- Common values
- Aligned goals
- Proper environment
Positioning Global Sourcing in a Strategic Procurement Framework

Executive Leadership + Guiding Philosophies + Procurement Strategies and Processes = Competitive Advantage

Corporate Executive
Business Unit Management
Functional Management

Strategy Enablers

Organization, including the use of cross-functional commodity and sourcing teams
Measurement and evaluation, including total cost and benchmarking
Information systems technology development and application
Human resource development and application

Guiding Philosophies

- Total Quality Management
- Internal/External Teaming
- Total Cost Management
- Supply Chain Integration
- Globalization

Procurement Strategies and Processes

- Insourcing/Outsourcing
- Early supplier involvement
- Supplier evaluation and selection approaches
- Supplier management and development approaches
- Strategic cost management
- Global sourcing
- Longer-term contracting
- Strategic alliances and relationships
- Supplier quality management systems

Competitive Advantage

- Total quality
- Lowest price
- Lowest total cost
- Technology advantages
- Shorter cycle times
- Customer responsiveness
- Superior delivery and service
- Product differentiation
- Improved profits, ROI, cash flow
- Breakthrough and continuous improvements
Supplier Collaboration

- Supplier collaboration involves sharing of information, competencies, skills, intelligence, and risks, and making appropriate commitments in terms of actions and business decisions.

Supplier Relationship Management

- SRM is the discipline of strategically planning for, and managing all interactions with third party organisations that supply goods and/or services to an organisation in order to maximise the value of those interactions.
Strategic Supplier & Category Management

- **Strategic Implications**
  - Adopt a business—not cost—driven focus
  - Balance long-term vision and planning with short-term agility
  - Separate strategic processes from tactical processes
  - Recognize supplier segmentation as a foundation for category management
  - Engage procurement in the full value chain with a specific focus on customer needs and values

- **Resource Commitment and Talent Management**
  - Empower visible, focused category management teams with diverse membership
  - Provide opportunities for career progression and skills acquisition through clearly articulated and differentiated requirements across the procurement organization.
  - Seek to incorporate procurement and sourcing early in the new product development process
Strategic Supplier & Category Management

Category-Specific Processes and Tools
- Create a standardized category approach to enable working and resourcing across categories and the ability to decide how much to invest by category
- Implement category risk management to monitor external market risks at the market or category level
- Conduct supplier risk assessments as part of the strategic sourcing process and on an ongoing basis
- Maintain an Intranet portal to provide one source for information that all relevant employees can access

Extending Supplier Relationships
- Invest in building strong suppliers
- Give suppliers tools to succeed and create a symbiotic relationship
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http://www.youtube.com/gtscl