Taking the First Step on Your Next Level Supply Management Journey

VFS. Hi-Def Sourcing. Next Level Supply Management. Next Practices. Value Chain Creation. The acronyms and acclamations are flying fast and furious. Even world class Supply Management organizations have to do something more to maintain their year-over-year contributions to the bottom line with the perfect Procurement storm of high demand, low supply, and high market volatility brewing off of the coast. But where does an average Supply Management organization begin?

By Michael Lamoureux
Editor, Sourcing Innovation

Contact Us
217 N. Jefferson St., Suite 400, Chicago, IL 60661
T: +1 312-373-3100
info@BravoSolution.com
www.bravosolution.com

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Supply Management Excellence

The first thing an average organization needs to understand is what it means to be world class and what will be involved in eventually getting there. Only when the organization understands what is involved in being a world class organization can it map out a transformation plan to get there and understand what will be required in the foundational first steps.

The Hackett Group, which is the leading benchmarking organization in the Supply Management space with 73% of the Fortune 100, defines a world class Procurement organization as one that is in the top quartile for both efficiency and effectiveness. Only 8% of the companies they benchmark make the cut. The rest of the companies are either above the median, and would fall into the average performer category from a traditional analyst firm's perspective, or below the median, and would fall into the laggard category from a traditional analyst firm's perspective.

If these organizations are then mapped to a 3-tier maturity model, it is usually the case that the laggard companies are at the first (or bottom) tier of organizational maturity, the average companies are at the second (or middle) tier of organizational maturity, and the world-class performers are at the third (top) tier. Exceptions will occur at the boundaries. Sometimes a company that has just finished a transformation initiative might still be below average in performance but at the 2nd tier of maturity, or still be average in performance but be at the 3rd tier of maturity. However, these companies will usually move up to the next level of performance within 12 to 24 months.

This paper defines a basic 3-tier maturity model that an organization can use to figure out where it is on the maturity curve and what it needs to focus on to advance the Supply Management function as a whole. For companies looking to advance to the next level, it defines key attributes of leading supply management organizations from a sourcing process, organization, finance, IT, product management, risk management, asset management, relationship, and metric perspective. It also discusses some specific initiatives an organization can take to advance to the next level.

It is important to note that an organization does not need to be best-in-class with respect to all of the attributes outlined in this paper to realize the value associated with advancing to the next level of supply management. A Supply Management organization only needs to be best-in-class with respect to those activities, processes, and sourcing categories that have a considerable impact on its business. For example, a services organization that leases its office space and computing equipment would not commit a lot of time or resources on asset management as it would not have many physical assets of value. However, it would need to commit a significant amount of time and resources on managing its contract labor as this would be a significant portion of its spend, and a considerable savings opportunity if managed appropriately.

Levels of Maturity

Depending upon which industry association, consulting firm, or analyst powerhouse is approached, one will typically be presented with a pyramidal or step diagram that has between 3 and 5 levels of Supply Management excellence. However, since any organization is either below average, above average but not best in class, or best in class, there is not much additional value to be gained by defining more than 3 levels of Supply Management maturity. As a result, the following levels of maturity are generally sufficient for an organization to understand where it is in its supply management journey:

Standardization & Complexity Reduction

This stage usually involves standardizing systems and processes and reducing complexity in core P2P (Procure-to-Pay) and O2C (Order-to-Cash) cycles.

Operational Excellence

In this phase, the organization moves from a focus on efficiency (faster, better) and cost (cheaper) to a focus on effectiveness and value. The focus will shift from process automation, incident response time, and optimizing Days Payable Outstanding (DPO) to optimizing settlement cost, minimizing the time to issue resolution, and optimizing working capital.

Strategic Business Enablement

In this phase, the focus shifts from doing it better to doing it different. Whereas the last two phases focused on maximizing efficiency and effectiveness of processes, organizations at this level of maturity look for entirely new processes and ways of

doing business in their quest to deliver greater value to the business. They are actively involved in NPD (New Product Development), NME (New Market Entry), M&A (Merger & Acquisition), strategic partnerships, and GBS (Global Business Services).

In simple terms, an organization at the first level of maturity in the standardization and complexity reduction phase is all about the data. What data is captured? Where is it stored? How is it accessed? How does it support standardized processes? How can it be used to calculate total landed cost? Can the largest spend categories be identified quickly and easily? Is there enough for sales analysis and demand forecasts across key SKUs? Are all supplier evaluations and customer feedback being captured and stored for analysis? Can basic performance metrics be computed on a regular basis? The organization is trying to get a grip on its data.

Similarly, an organization at the second level of maturity (the Operational Excellence phase) is all about the information. Now that the data is centralized, current, and easily accessed, the Supply Management organization is focused on extracting useful information from that data that can support the business strategy, not just day-to-day tactical operations. The focus shifts from total landed cost calculations to extracting the true costs required to populate deep total cost of ownership (TCO) models. With true TCO models, an organization is able to understand the total cost of a product or service. Sourcing shifts from commodity-based projects to category management where each buy, on one or more commodities, is part of the overall long-term strategic plan for the category. Category strategic plans are generated through a careful analysis of historical and projected buys in the category. Organizational trends are identified in products and services through multi-year data analysis and analyzed against current megatrends to determine if current sourcing strategies may need to change. The organization is asking how the data can be analyzed to produce information that will allow it to make better sourcing decisions.

Finally, an organization at the third level of maturity (the Strategic Business Enablement phase) is all about knowledge. Now that the organization has TCO under control, the focus shifts from controlling costs to finding new sources of value. The organization will attempt to make sense of all of the information it has available to it while considering the forthcoming needs of its internal customers. Maybe the current supplier of semiconductors is the most cost effective, but if demand signals point to increased demand and supply shortages in the market,

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217 N. Jefferson St., Suite 400, Chicago, IL 60661
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info@BravoSolution.com
www.bravosolution.com

The following are the strategies and activities that an organization in each phase of maturity will likely focus on:

Activity Group	Standardization & Complexity Reduction	Operational Excellence	Strategic Business Enablement
Sourcing Process	procurement process standardization *adoption of standard n-step sourcing methodology* tactical vs. strategic segmentation *cost focus* landed cost *starter team (sourcing manager, contract specialist, negotiation expert)* identification of largest cost reduction opportunities *freight optimization* current trend focus *data management*	lean procurement & waste reduction *deep cost modelling* category sourcing *outcome focus* TCO *extended cross-functional team with operations and finance representation* maverick spend reduction and automatic spend capture *network optimization* megatrend alignment *information management*	quality function deployment (QFD) and customer specific methodologies (e.g. CMM) *source for value* category management *result focus* TVM supplier and customer representation on the sourcing team *maximization of spend under management* cross-docking and end-to-end transportation management *minitrend exploitation* knowledge management
Organization	process-based restructuring *centralized*	geographic focal points *center-led*	global supply management operation *adaptive hybrid model*
Finance	discount management *index tracking*	working capital management *hedging techniques*	balance sheet improvement *proactive cost control*
Information Technology	centralized system of record	system of record augmented with best of breed for sourcing, contract management, and analysis	applications for demand management, NPD, and innovation management
Product Management & Marketing	sales analysis / demand forecasts *cost reduction focus* market optimization	demand visibility & reduction *quality improvement focus* market expansion	demand creation & shaping *(joint) innovation focus* new market entry
Risk Management	identification	mitigation	avoidance
Asset Management	divestments	utilization maximization	increase rate of return
Relationships	implement SRM/VMI *customer satisfaction tracking*	collaboration in product development *customer account management*	vendor development initiatives *end customer focus*
Metrics	intermediate cost of capital, quality, transportation, and disposal metrics	intermediate cost of capital, quality, transportation, and disposal metrics	advanced ROI, ROIC, EBITDA, EV, EVA, NPV, TTM, and TTV metrics

then the right strategy might be to choose a more expensive supplier who can guarantee sufficient supply and to work with the supplier to lower costs over time. However, the organization will only be able to figure this out if it has in-depth knowledge about current and future needs and market trends. It has to weave a thread of relevance through the information available to it to arrive at the knowledge required for a deep market understanding. And it will start this process by collaborating with all affected parties to identify the right information, the right connections to make, and the right conclusions to draw to transform the information into knowledge that it can use to make better sourcing decisions that will lower cost while increasing value.

The Yellow Brick Road

Elton John may have bid adieu to the Yellow Brick Road back in 1973, but it is still within the reach of an aggressive and progressive Supply Management organization willing to go the extra mile and risk the tornado. However, for a Supply Management organization still at the first stage of Supply Management maturity, it is a long journey that could easily take up to 8 years to achieve (in the case of a Global Multi-National that does over 10 billion in revenue a year).

So where does the organization start? If it is in the first stage of maturity, it usually starts with standardization and automation. If it is in the second stage of maturity, it often starts with strategic initiatives that often involve upgrading the platform with a best-of-breed bolt-on (since, in the first phase, it will likely have standardized on an ERP that is very effective as a transaction store but poor at advanced data analysis). If it is in the third stage of maturity, the supply management team starts with those activities that will align with mega-trends and mini-trends and ultimately lead to the most profitability for the company as a whole. The particular activities will be dependent on the company in question and the current market state, but the first set of activities will often be aligned to the next generation sourcing, finance, product management, and risk management activities identified in the last section.

From Standardization to Excellence

If the organization is below average in supply management competency, then it is still at the first stage of organizational development and needs to first progress to the operational excellence stage before it can become a world class Supply Management organization. The first thing it will need to do is get its sourcing process under control. For an average organization, this will require moving from a basic landed cost focus to a more holistic outcome focus that revolves around TCO for high-value strategic categories. The organization will also need to modify the generic sourcing process for key categories, focus on should-cost models and not best quote, include operations and finance on sourcing teams, and optimize the network as a whole, not just the freight costs.

If the organization is centralized, it will need to shift to a center-led model with geographic focus points, and if the organization is still running off of a basic ERP (or other system of record), it will involve the incorporation of best-of-breed systems. With respect to product, the organization will shift from after-the-fact sales analysis to immediate demand visibility, shift demand to more profitable products, and focus on moving into other profitable markets. SRM (Supplier Relationship Management) efforts will be extended and suppliers will be included in NPD (New Product Design). In addition, the Supply Management group will actively identify and implement mitigations for any risks that are likely to occur or that would be too costly to recover from.

It is important to note that the organization will have to start by classifying its purchases into categories and then classify those categories by value and strategic importance. It is a waste of time and resources to do a deep sourcing effort on a low-value non-strategic category like office supplies when an automated reverse auction will capture most of the savings available to the organization. However, for key raw materials, like chicken in Food & Beverage, steel in Construction, and semiconductors in Electronics, the organization will want to apply all of the knowledge and technology it has at its disposal. Saving an extra 2% on a 50M strategic buy while improving quality is much more valuable than saving 8% on a 5M buy.

With respect to strategic sourcing, the organization needs to effectively “change the curve”. In an average supply management organization that has reached operational excellence, there are typically a large number of projects on small to medium spends of low or moderate complexity. This is the case for two reasons. First, the organization has learned that it can find savings in every category upon the initial application of strategic sourcing to the category. Second, the organization is comfortable running projects of moderate size and moderate complexity. However, to find the real treasure trove of value, the organization has to move out of its comfort zone and tackle the large, complex categories which can provide the organization with considerable value and automate the small to medium spend categories of low to moderate complexity. Maybe it needs to tackle the complex transportation spend category which requires a detailed analysis of hundreds of lanes, or maybe it has to tackle categories globally, and not just locally. It has to change the curve from a large number of low-to-moderate complexity projects to a smaller number of high complexity projects where the most value will be found.

For example, some multi-nationals will source print on a regional basis. However, if the multinational is essentially distributing the same catalog around the world, with the only difference between printed catalogs is that some will be in different languages, maybe it should be analyzing the spend on a global basis. For example, essentially the same catalog could be created for Canada, New Zealand, Australia, the UK, and the US. Not only could Canada and the US be treated identically, as should Australia and New Zealand, as they are geographically close, but maybe they should be printed in Mexico and shipped North and maybe the company that handles Australia and New Zealand should also handle Indonesia, Malaysia, the Philippines, and Papua New Guinea because they are all in the same geographic region. Complex projects often yield unexpected savings under sophisticated analysis, like the kind that generally occurs in sourcing events where a cross-functional team comes together in a collaborative manner for the benefit of the company and the end customer.

Let's examine the changes required from a sourcing perspective and look at how better processes and technology can help. For starters, now that processes have been standardized, they can be broken down into strategic and tactical components. Tactical components, such as cutting purchase orders, reviewing and approving invoices, and reconciling invoices with goods receipts can be outsourced to a tactical support unit, allowing supply

management professionals to spend more time on category management, strategy development, and innovation. Best of breed suites allow sourcing professionals to start with templated projects for categories of low or moderate complexity and to almost fully automate events for routine purchases like office supplies, desktop replacements, and janitorial labor contract renewals. This frees up the supply management personnel to spend considerably more time on the more complex categories like resins, customized bio-degradable and reusable packaging, and global transportation.

In addition, the focus on lifetime total cost of ownership instead of just landed cost will save the organization considerably in complex categories. As an example, consider the situation where a company is buying widgets and sprockets direct from suppliers who are handling shipping, because quotes on the individual lanes from the 3PL (Third Party Logistics) were higher (on average) than letting the supplier manage freight. Let's assume that the organization is able to group widgets and sprockets into a single category, can combine shipments from suppliers in the same geographic area, and can also model warranty and return costs by supplier.

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Consider the following quotes:

Company/Product	V	W	X	Y
widget	11.0	10.0	10.5	11.5
shipping	1.0 (12.0)	1.5 (11.5)	2.0 (12.5)	1.5 (13.0)
warranty	(12.0) 1.0 (13.0)	(12.5) 2.5 (14.0)	12.5) 2.0 (14.5)	12.5) 1.0 (14.0)
sprocket	16.0	15.5	15.0	17.0
shipping	2.0 (18.0)	1.5 (17.0)	1.0 (16.0)	1.5 (18.5)
warranty	(17.5) 1.5 (19.5)	(17.0) 1.5 (18.5)	(18.0) 3.0 (19.0)	(18.0) 1.0 (19.5)

Shipper/Per Unit	B	C	D
widget	1.25	1.75	1.75
sprocket	1.75	1.50	1.25
Over 1M Units			
widget	1.00	1.00	1.50
sprocket	1.25	1.00	1.00
avg	1.13	1.00	1.25

Using a simple landed cost analysis, the company would choose suppliers W and X at a total cost of 33M (once warranty and return costs are taken into account) if the demand for each was 1,000,000 units. However, if warranty and return costs are factored into the model and the shipments grouped, the company would now choose suppliers V and W and ship using 3PL C at a total cost of 31M, for a savings of 6%. This is just one of the many ways that a company would reduce and avoid costs by advancing supply management to a state of operational excellence.

From Excellence to Enablement

If the organization is above average in supply management competency, then it is likely still at the operational excellence stage of organizational development and needs to implement next generation supply management concepts and techniques before it can become a world class Supply Management organization that strategically enables the business. The first thing the organization will likely need to do is shift its focus from supply management outcomes to balance sheet results that maximize the bottom line of the business and not just Supply

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info@BravoSolution.com
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Management. This will typically involve a shift to a profit and end state value focus from the current cost optimization focus and a move to TVM (Total Value Management) from the current TCO focus. Advancement will also typically involve the inclusion of supplier and customer representation on the category management teams, the adoption of cross-docking and other advanced end-to-end transportation management techniques, the identification of mini-trends on the leading edge to maximize the gains from mega-trend efforts, and the emergence of truly collaborative sourcing teams that include suppliers and customers on strategic projects.

The organization, which will typically be center-led, will need to transform into a true Global Supply Management organization with an adaptive hybrid model that reacts to markets. Cost control will need to become proactive and forward looking. Product Management involvement will start day one, focus on innovative ways to reduce costs, and identify new markets early to allow Supply Management to help create and shape demand. Risk Management will move from a mitigation focus to the identification of the supply strategies with the least risk to begin with, and Supplier Relationship Management will expand its focus to develop key suppliers to allow for better performance overall.

The organization will want to invest the time and effort to get to the next level of maturity because the payoff will be substantial. It will go beyond just a cost reduction of 5%, 10%, or 15% and positively impact the supply chain for years to come. For example, identifying a petroleum-free bio-degradable plastic or resin, which can be made entirely from plants, while more expensive in the short term, will guarantee long term supply at prices guaranteed to decrease as time goes on (and production technology gets better and cheaper). In comparison, it's a given that oil prices will continue to rise as oil becomes a scarcer resource. A 5% cost increase now could translate into year-over-year cost reductions of 5% in the future, and no shortages of supply that could restrict sales and profit.

However, the transition will require a considerable investment of time and resources as well as a significant shift in mindset.

Whereas Excellence focused on total cost, Enablement focuses on total value, especially in non-traditional and complex categories. In the sourcing of legal services, Supply Management will be helping internal counsel to identify the best law firm to defend a case, not just the cheapest firm, since losing a lawsuit could result in millions of dollars of damages. From a risk management perspective, spending a few extra hundred thousands to reduce the chance of a multi-million dollar judgement that could bankrupt the company is a smart move. In the sourcing of precious metals, instead of trying to guarantee a supply of tantalum given the piracy off of the Somali coast and the political instability of the region, maybe the organization institutes a new recycling and recovery program that also allows it to reclaim the precious metal from used devices that consumers will happily return for a small credit off of the new model. It's all about identifying value to the internal stakeholders and the organization and pursuing that above cost reductions. In the end, it's all about profit and organizational growth, and that's a balance between reducing costs across the board over the long term and insuring that the organization can sell the optimal amount of goods and services at all times.

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About BravoSolution

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Every company's strategic objectives are different. Supply management executives are uniquely positioned in their organization to provide a deep understanding of what drives their business' success. To harness this perspective and contribute to these distinctive objectives, sourcing executives need an exceptional solution to maximize their company's competitive advantage.

With over 40,000 procurement professionals in 60 different countries using BravoSolution's technology and services, BravoSolution offers leading software, practice innovation and expertise to ensure that supply management is aligned with their company's strategic objectives to drive business growth. Top analysts have found that the right blend of skills, process, and technology improves a company's financial performance by 30 cents on every dollar spent. BravoSolution works with supply management to address each business's unique processes, stakeholders and goals to deliver tailored solutions across the entire supply management cycle.

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