Capgemini Consulting

2012-13 Global Chief Procurement Officer Survey

Leveraging Digital Procurement and Innovation to Expand Procurement's Business Value

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2013 CPO Survey – Executive Summary

Change is a constant for all executives and those in procurement are no exception – with a seat firmly at the cost cutting table there has rarely been a greater imperative for CPOs to expand their involvement across corporate-wide initiatives such as digital transformation, innovation driven procurement, master data management, and business process outsourcing to demonstrate the value of procurement to the enterprise. As with our previous CPO publications we will explore current trends and strategies to harness these capabilities to deliver even greater bottom line impact and why now, more than ever, the CPO is an integral part of a CEO's overall corporate strategy.

In our commerce-driven world of double dip recession and Eurozone uncertainty, organizations are under increased pressure to instill confidence in their shareholders. In this study, we examine top trends that are essential to procurement leadership; many of these were nascent ideas even a year ago. Digitization, Innovation, Consumerization, Data Management, and the Cloud all offer avenues to increase and sustain value for both strategic and transactional procurement activities.

In light of global economic challenges, it is no surprise that 86% of participants said their annual savings target for 2012/13 is 10% or less. This goal represents tangible profit and loss savings (rather than cost avoidance which should be treated separately) and represents a decline from goals articulated in the past five years.

Business process outsourcing (BPO) for procurement, and the provision of sourcing and transactional (operational procurement) activities as a service provides significant savings to organizations; however, only 5% of participants suggest they are in the process of outsourcing their strategic sourcing function and approximately 60% of respondents do not use BPO services. Those organizations that do outsource operational procurement activities are approaching a point of saturation; however much opportunity still remains in procurement BPO for driving sourcing savings and committing these savings to the bottom line in more innovative arrangements; the ability to trust a BPO provider to deliver sourcing results is a proposition that many CPOs still wrestle with.

With the increasing popularity of social media, gamification and the digitization of everything we do and touch, it is no surprise that the translation of these tools from personal to professional use represents a real opportunity for organizations – but how applicable are these to procurement professionals? Our survey highlighted that 40% of procurement organizations are involved in augmenting their practices with digital tools, to:

- broaden and expedite communication with partners and suppliers and even potential competitors
- automate and integrate procurement tasks and procedures, e.g., predictive analytics and digital recognition in mobile sourcing
- enable procurement professionals to work anywhere, anytime

For those that wish to retain and those who seek to move into a position of procurement leadership, digital, mobile and social technologies must be integrated into their practices.

Further, 60% of our respondents highlighted a focus on corporate-wide master data management. From our recent client demand and experiences, we have seen this goal addressed through the drive to better manage and govern data to provide meaningful predictive analytics. This is most prevalent in the objective to ensure absolute clarity regarding what is purchased, from which vendors and whether in compliance with negotiated terms and conditions. While the ability to implement a 100% end-to-end procurement strategy inclusive of compliance, data quality and spend visibility is unlikely, it is encouraging that there is an increased focus on the joining the dots towards this goal; appropriately deployed digital tools will aid in the attainment of this goal, provide greater connectivity across the enterprise and, and of course enable greater savings.

To effectively analyze the output of the study, and highlight some of our market and industry thinking, we delineate recommended areas of focus through the following articles:

- Procurement Trends – The Evolution of the Procurement Organization
- Unleashing the Power of Digital Procurement
- Innovation Driven Procurement (IDP) - A New Frontier in Procurement Value
- Master Data Management – A Cornerstone of the New Procurement Organization
- Risk Management – As a Means to Increase Procurement Value

We trust that you will enjoy our fifth CPO Survey publication and look forward to your input and commentary. We certainly hope to hear those comments through one of our many digital mediums such as the Capgemini Procurement Transformation Blog http://www.capgemini.com/procurement-blog/

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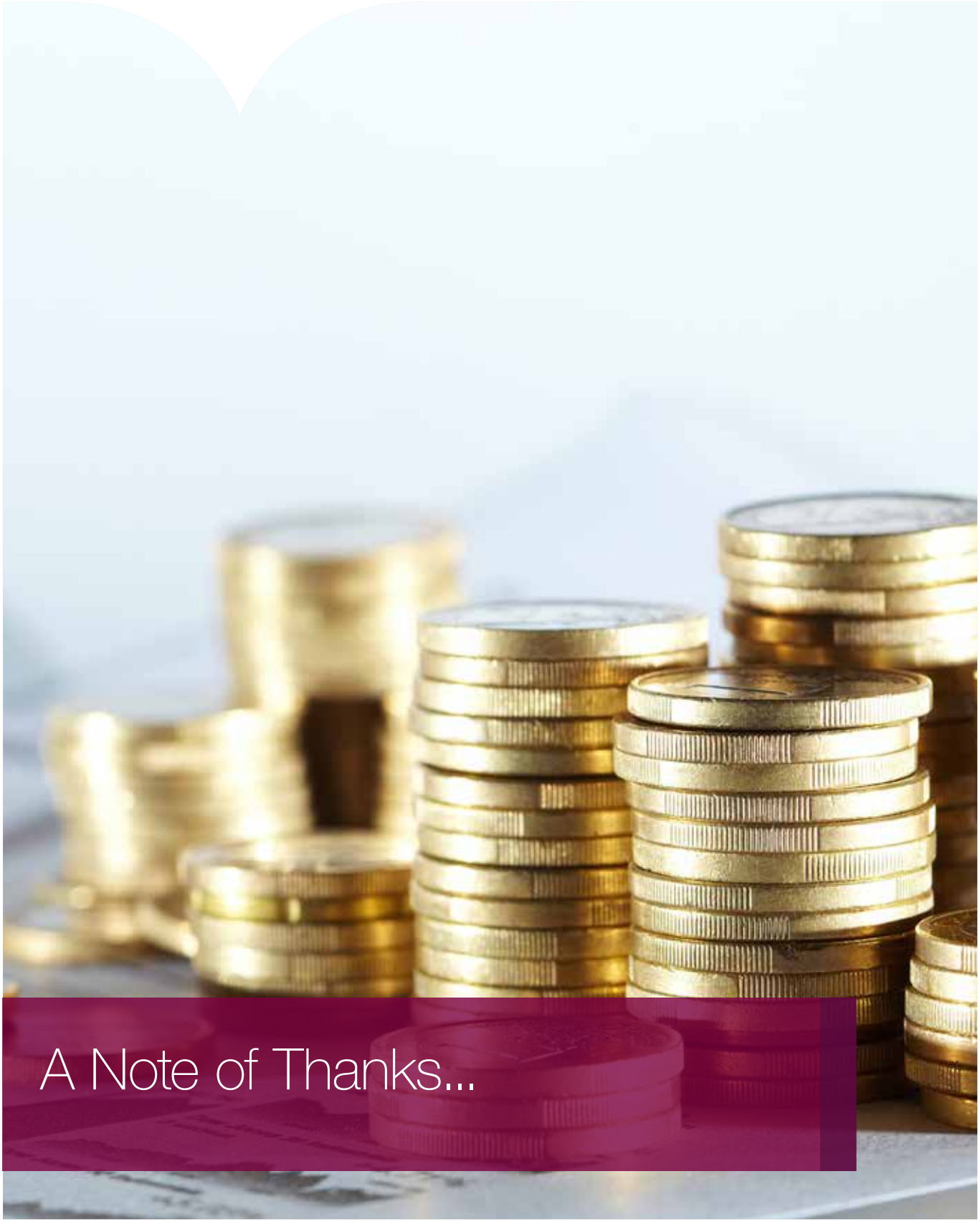

A Note of Thanks...

Capgemini Consulting extends its thanks to the senior procurement professionals who made time to participate in this Global Survey. Without their cooperation and support, this research would not be possible.

Participating Companies and Organizations

ABN AMRO Bank
Aetna
Ahlstrom
ANWB (Royal Dutch Touring Club)
APG
Arjowiggins
Atlas Copco
BAM
BD
Borealis
BOUYGUES CONSTRUCTION
Bouygues Telecom
BP
Bpost (Belgian Post Group)
Capgemini Nederland B.V.
Casino Austria AG - Österreichische Lotterien
CGGVeritas
City of Ghent
Cofely GDF Suez
Colt Technology Services Group Limited
CZ
Dairy Crest
Delta Lloyd Groep
DSM Sourcing BV
E.ON Benelux
Eandis
Federation Française de Football (French Soccer Association)
FEI
Hydro One Networks
ING Insurance
Ipsen
KONE Corporation
Kraft Foods Group
Lagardère Active
LeasePlan Supply Services AG
LSG SKY CHEFS HAVACILIK HİZMETLERİ A.Ş.
Marine Well Containment Company
Mars Food Europe
Nedtrain
Nynas AB
Océ-Technologies B.V.
Polaris
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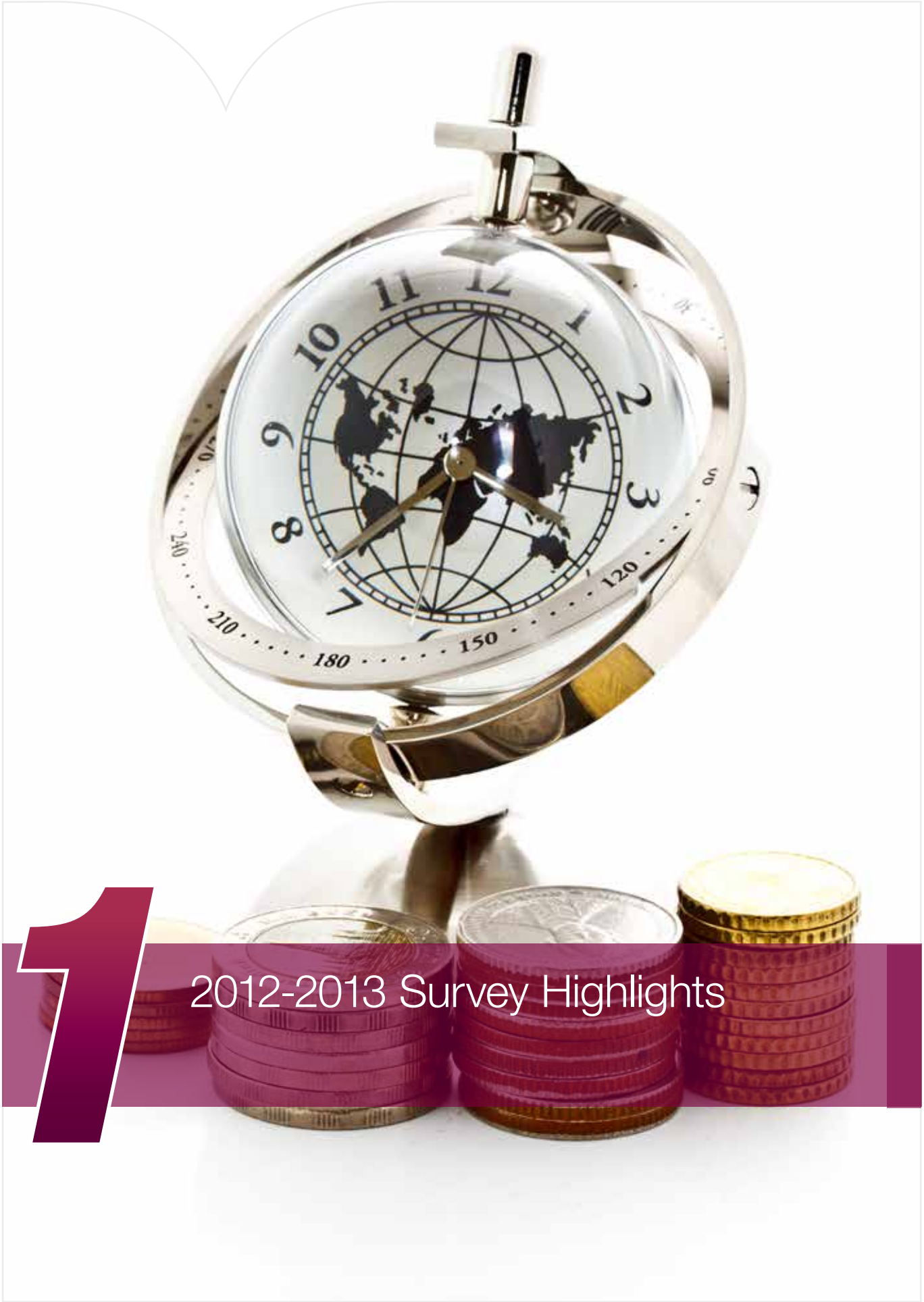
Scania
Shell Global Solutions International
Sibelga
SPIE
Sprint
Tate and Lyle
Telenet NV
Tessenderlo Chemie
Unilever Supply Chain Company AG
UWV
Vanderlande Industries
VDAB
Vodafone
ZNA
Zumtobel Lighting GmbH

And many other companies and organizations that wished to remain anonymous



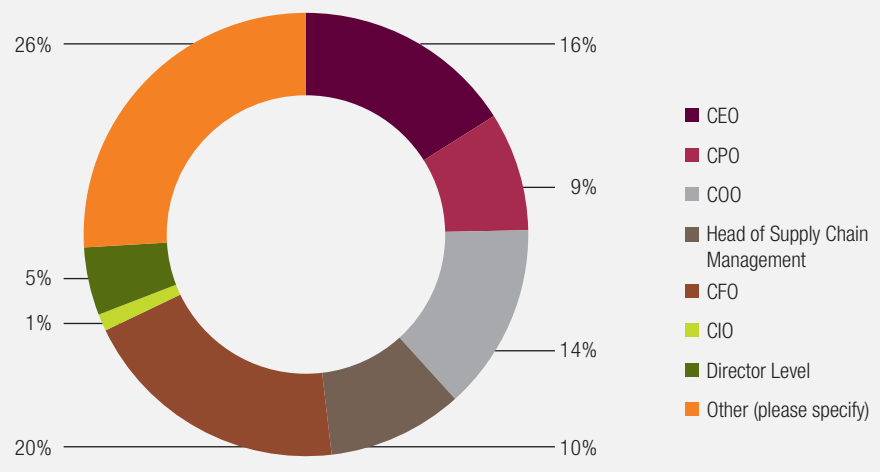
1 2012-2013 Survey Highlights

Procurement Trends: The Evolution of the Procurement Organization

Our 2010 survey highlighted the effects of the economic downturn on procurement organizations. Two years later, the organizational changes made and the mentality of "doing more with less" remain. Cost cutting continues to be the key focus of purchasing organizations, with three-quarters of respondents highlighting it as a focus area. Organizational realignment, on all levels has continued, with half of survey respondents indicating that operating model and organizational redesign is currently in process. These results underscore the trend of high-performing procurement organizations moving to a center-led or centralized model; 30% of respondents indicate that procurement innovation will be a future a focus. In addition, environmental and supplier issues remain top of mind with 33% of respondents indicating that 'green' procurement initiatives are also key initiatives.

Continued emphasis on cost cutting has resulted in an increase of both the size and stature of procurement organizations. As indicated in Figure 1, the trend of procurement functions reporting to the C-suite has continued. In 2010, 55% of respondents reported that the procurement organization reported into the CXO level. Two years later, that number has risen to 59%. Currently, 20% of respondents state that their procurement function reports into the CFO, 14% reports to the COO, and another 16% reports directly to the CEO. The percentage of procurement organizations reporting directly to the CEO has increased since 2010, when less than 1% had a direct line to the CEO. We anticipate the trend of higher reporting relationships for procurement will continue, including dotted-line relationships across operational units, as bottom-line cost cutting and organizational transformation initiatives implemented during the downturn are sustained.

Figure 1: Breakdown of reporting function in procurement organizations



In the source to contract capability, 50% of procurement leaders indicate focus on improvement of sourcing and spend analytics as shown in Figure 2. However, CPOs indicate that this will shift in coming years, with 30% reporting that supplier risk and/or relationship management will be a focus in the future. This indicates fear of a sustained downturn, thus requiring efforts to mitigate supplier risk as businesses merge or disappear.

Outsourcing continues as a component of cost cutting strategies. Organizations are moving towards BPO transactional procurement procurement arrangements to support spot buying for 'non-strategic' categories. However, this remains a small share of the market, as 87% of survey respondents indicated they do not outsource any of the Procurement functions. As noted in Figure 3, for those companies that choose to outsource, spot buying and operational procurement functions are the focus areas, with 12% of respondents each. We expect that over the next few years, procurement functions such as P2P support will be outsourced more frequently as organizations focus internal resources on strategic sourcing maturity and efforts to reduce the cost of P2P support. The data supports this trend, as 32% of CPOs identified source to contract outsourcing as a future focus area.

The other key to doing more with less in procurement organizations is increasing savings targets and cost avoidance goals on future spend as demonstrated in Figure 3A. Sustained cost savings is a key performance metric for procurement professionals. Eighty six percent of respondents are now responsible to deliver at least 10% year over year savings; however, 56% are tasked to deliver less than 5%. At the other end of the spectrum, 5% of respondents are responsible to deliver annual cost savings greater than 10%.

Figure 2: Source to Contract Focus Areas

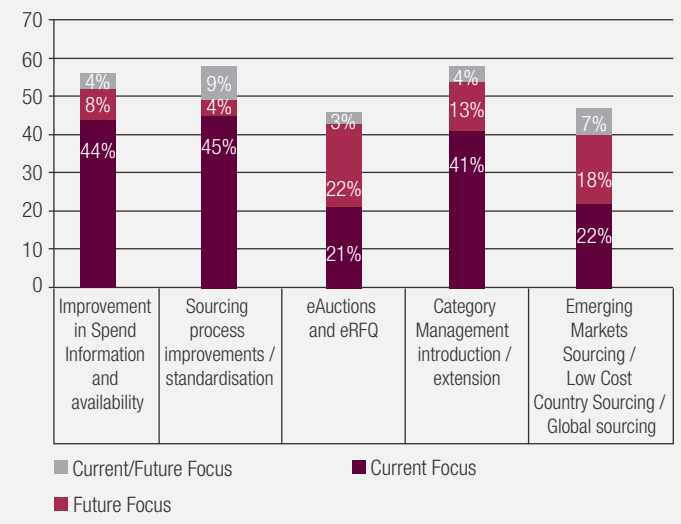


Figure 3: Components of procurement currently outsourced

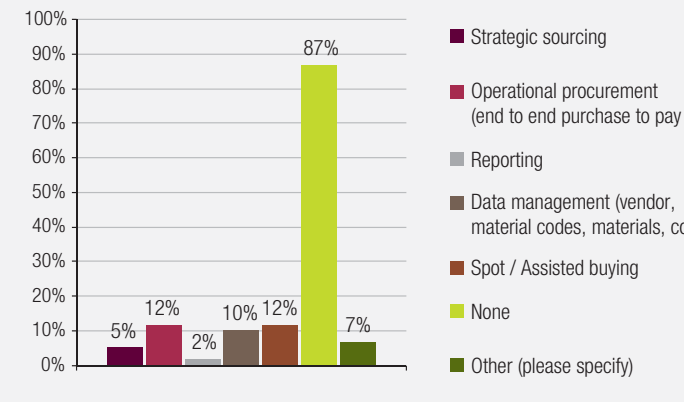
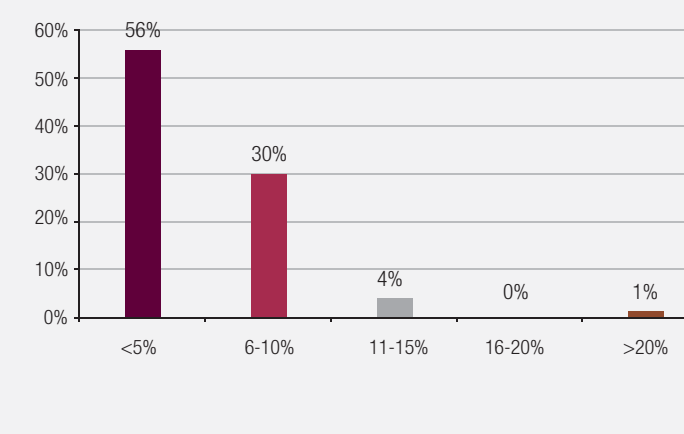


Figure 3A: Planned 2013 savings targets as a % of total spend?

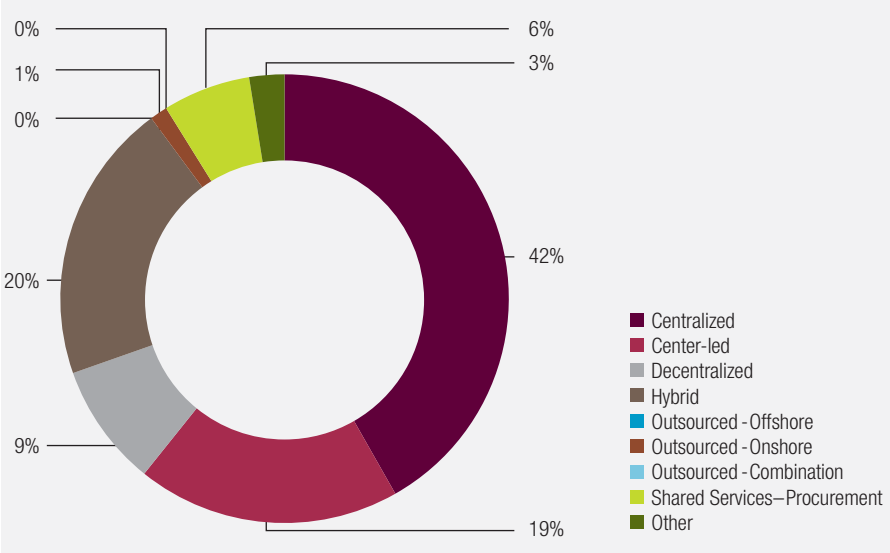


For many organizations, savings targets have remained relatively static from 2011 to 2012. This can be partially attributed to control issues, e.g., not have the visibility or processes in place to effectively identify opportunities and manage expenditures. Stagnation in savings targets may also be a by-product of an increase in procurement maturity, i.e., accessible targets with large savings opportunities have been addressed, and cost reduction now requires strategic initiatives leveraged across the organization.

A final outlier was the 1% of respondents whose annual savings targets are unusually high at greater than 20%. This savings goal suggests either 1: that these organizations have a relatively immature purchasing function (in which there are plentiful savings opportunities they are confident can be achieved), or 2: that they are undergoing significant organizational changes and have initiated drastic cost cutting efforts such as the sale of business units, merger activity, or the outsourcing of a large number of employees. Whether these types of savings would be directly attributed to procurement is a matter of debate and depends on a number of factors including the organization's benefits measurement methodology and whether savings are part of the overall corporate strategy or attributed to the functional area directly responsible.

Figure 4 shows that the trend towards center-led and/or centralized procurement continues, with only 12% of respondents indicating that their organizations were decentralized or other. Forty two percent of respondents have a centralized procurement function, and another 25% operate under a center-led or shared services model.

Figure 4: Current organization of procurement function



Even so, centralized procurement organizations have a long way to go to impact spend across the enterprise as a whole; only 7% of respondents indicated their procurement organization controlled greater than 50% of spend. From our experience and understanding of how the S2S (source to settle) ecosystem has matured in the last few years, this low percentage of controlled spend could be a result of:

- A low level of influence within organizations to ensure adherence to processes, procedures, buying channels and approved tools,
- Underutilized/under deployed/ limited capabilities of both tools and procurement professionals within the organization, and/or
- A lack of adoption within the business and therefore an inability to manage spend effectively across the user and supplier base compounded by a lack of accountability

A low level of influence may be attributed to inadequate understanding of procurement services and collaboration between with business units and procurement teams resulting in a failure to realize significant savings opportunities.

Looking forward, leading CPOs are eager to innovate and digitally transform their organizations to attain and sustain their cost cutting goals. The future is rife with opportunity for significant advances in the coming decade.

Unleashing the Power of Digital Procurement

While the exponential rate of digital commerce growth can seem exhausting, we view it as exhilarating; particularly with regard to the potential value the solutions offer to advance digital procurement. Survey responses reinforce the notion that forward-looking Chief Procurement Officers believe innovative based capabilities such as predictive analytics, mobile solutions and virtual procurement technologies will not only deliver incremental value to their organization but also are a core requirement to drive a competitive edge in a demanding business climate.

In the pursuit of improving bottom-line results, 47% of respondents are turning to advanced technologies to stay ahead of globally intensifying competition. With the emergence of innovative solutions, leading companies must do more than automate their purchasing transactions to remain competitive – they need to arm their decision makers at all levels with accessible and actionable data and insights and enable collaboration unhindered by geography. The 'Consumerization of Technology' (the trend of innovative solutions driven by consumers and end users finding its way into the enterprise) has provided predictive analytics, mobile, social and cloud solutions - key digital advances that companies must embrace to develop competitive leadership. In our review of the data, we describe how companies are leveraging digital procurement and provide reasons we believe these trends are fundamental to any procurement practice.

The Power of Predictive Analytics

Analytic software provides faster access to relevant data and trends in easier to interpret formats allowing better informed and quicker inputs to executive-level strategic planning throughout the entire source-to-pay cycle. Twenty nine percent of companies surveyed are harnessing advanced analytics to inject insights into their business operations. Many are already employing descriptive analytics in areas such as spend analysis, cost modeling, and supplier performance tracking. However, CPOs who are embracing and leading the digital market see predictive analytics as their next big move. Predictive analytics help companies evaluate commodity price volatility and therefore understand and adjust to the potential impact on their cost structure and relative profitability, e.g., modeling a number of potential scenarios to help decide a course of action. The price forecasting ability of predictive analytics also provides companies with an edge during supplier negotiations. Investment in predictive analytics will provide greater data assurance and ultimately improve cost savings by achieving a greater level of visibility and control.

Embracing Mobile, Social and Cloud Advances

Our experiences and responses highlight that the emerging trio of mobile, cloud, and social media technologies reduces the need for typical desk-bound activities and increases geographically unrestricted and 24/7 information sharing that enables companies to maximize collaboration amongst their employees and their suppliers and reduce cycle times. The time for employees to drive the business has never been greater – social media attracts this opportunity, but how organizations harness it will be paramount. Failure to respect employee innovation and interaction at all levels will be to the detriment of every CPO, CFO and CEO.

Twenty-nine percent of respondents have empowered their employees with mobile procurement capabilities, e.g. smartphones, tablets, with the ability to access key applications. Employees at these companies can approve requisitions, purchase orders, and even contracts on the go, while accessing supplier performance data from anywhere. Going forward, we expect innovative mobile technology to expand beyond existing transaction-based features that enable greater collaboration between suppliers and buyers during sourcing and negotiation to capabilities such as the ability to scan a product with a smartphone and receive three bids from preferred suppliers in less than five minutes. As the technologies advance, so too will quality and user experience expectations.

As with mobile solutions, virtual procurement capabilities remain under-utilized but are quietly gaining traction. As noted in Figure 6, twenty-six percent of respondents are boosting their virtual procurement capabilities by incorporating social media and cloud technologies with in-house resources. We anticipate significant expansion of virtual capabilities and encourage companies to leverage social media as a platform for internal project/pipeline collaboration and external collaboration with suppliers. In addition, procurement organizations should explore social media as a forum to publicly promote company credentials to recruit talent, identify new innovative suppliers and, of course, attract clients.

At the same time, companies are looking more fondly upon cloud and on-demand solutions to accelerate time to value in their procurement organizations. Software as a service (SaaS) and on-demand solution options can be deployed more quickly, are scalable, secure and help promote

common practices across the organization while saving on traditional on-premise run and license costs. We expect more companies to adopt virtual procurement capabilities – moving away from proprietary and on-premise solutions - as they strive for a lean and flexible operating model. Indeed, such a shift may need to happen rather rapidly as solution providers are moving to the cloud with their leading and most functionality-rich solutions.

By strategically merging mobile, social and virtual capabilities, companies can empower their employees and third-party partners with unprecedented collaboration and visibility to better serve their client base. Those ignoring the rise of such technologies risk lagging behind their more dynamic competitors.

The Road Ahead

The rapid pace of technological development over the past five to ten years is unprecedented and we expect this trend to continue unabated for the foreseeable future. The ability to predict coming changes is always a challenge so CPOs must ensure their organizations are nimble and well equipped to deal with the shifting scales of supply and demand. To merely remain competitive, procurement organizations will need to not only evaluate their current solution set (to ensure full utilization of existing capabilities) but also take a clear-eyed assessment of how to implement the digital capabilities reviewed herein. We have described and discussed predictive analytics, social media, mobility and cloud-based solutions separately, yet it is essential to recognize the convergence, or coming interdependence of each. That is, companies that embrace only one or two of those described do so at their peril - each uses the other as a data source and/or delivery method and collectively they reduce time to value, increase collaboration, and prove out the proposition of procurement as an innovator and differentiator across the organization.

How to Move Forward

Despite the new wave of technologies available to today's procurement organizations, the majority of companies have yet to tap into the power of digital procurement in terms of its execution and value to the wider corporate organization. Even those companies that have embraced digital solutions have more to accomplish by obtaining the most from their capabilities. To avoid falling behind in an increasingly competitive global market, companies must:

- *Develop a roadmap for digital procurement outlining how each emerging technology aligns with their company's organizational structure and enterprise goals;*
- *Deploy a thorough change management framework to address the impact of new technology on their organization and workforce, and how best to use this;*
- *Establish an innovative culture and environment for procurement – encouraging and embracing new ideas from both internal and external sources.*

Digital procurement presents a major opportunity for CPOs to enhance strategic decision making and work force efficiency, while elevating procurement's internal profile within the firm. Failure of the CPO to pay heed to the suite of opportunities this represents will only make the journey in driving value more challenging.

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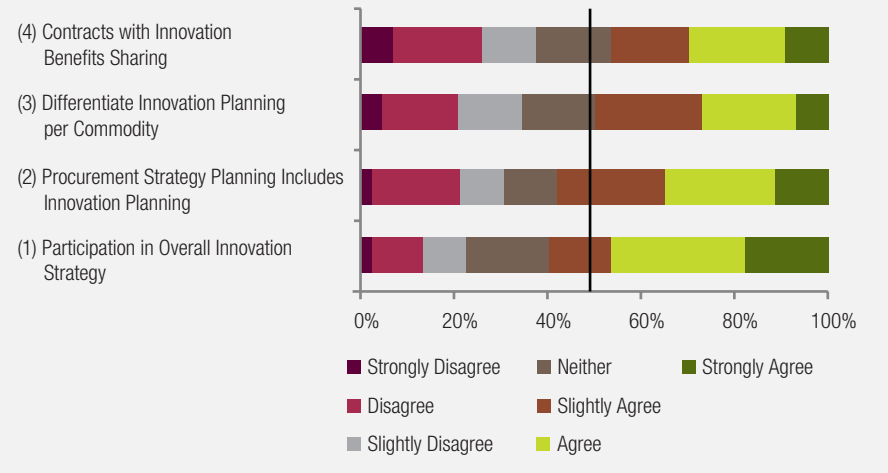
Innovation-Driven Procurement (IDP) - A New Frontier in Procurement Value

The Total Cost of Ownership (TCO) concept is nothing new. It has been preached to procurement professionals and become a cornerstone of supplier evaluation. Innovation driven procurement takes a step beyond TCO - it changes the equation. Innovation has become a new priority for CPOs as they seek to increase the value of procurement to the organization.

In the 2012-13 CPO Survey, Capgemini Consulting inquired about procurement's role in supporting innovation, innovation strategy, and product development. The results reviewed herein focus on two themes: *Measuring Procurement's Involvement in Innovation* discusses the necessity of strategic KPIs in the evolution of procurement. The *Role of the Supplier* explores how different companies engage suppliers throughout the product development cycle.

Overall, the findings show procurement's importance within the organization has increased. However, some organizations are still reluctant to involve procurement and suppliers early enough in development to maximize benefits. Altering the traditional corporate view of the procurement function might be the biggest hurdle to overcome to obtain a seat at the innovation table; to do so, procurement needs to move beyond its current role as a cost reduction function and embark on an innovative path to demonstrate its importance to the organization.

Figure 5: Internal Procurement KPIs for Innovation Success



Measuring Procurement's Involvement in Innovation

Companies surveyed in the study showed a preference for strategic IDP Key Performance Indicators (KPIs) over tactical ones. This inclination indicates procurement is still working to become an integrated part of the innovation process. Among responses, the highest emphasis was placed on "Participation in Overall Innovation Strategy". As with early procurement involvement in business planning, early involvement in innovation projects is vital to maximize benefits. Those organizations that engage procurement early in the planning process and request innovative input have begun the journey to true IDP. However, in many of our engagements, procurement is still viewed as a silo function and KPIs remain focused on tactical and cost-reduction activities – not innovation related. While Capgemini Consulting coaches procurement leaders not only to save money but also to reduce time to market, survey results indicate that these strategic opportunities are frequently missed. Embracing Innovation Driven Procurement is the key to unlocking and delivering additional value throughout the organization.

The Role of the Supplier

What role does the supplier play in innovation? We believe suppliers can offer more than goods and services; to drive corporate innovation, we recommend development of a stratum of supply partners. However, our IDP survey found that four out of five suppliers are engaged too late to deliver innovative ideas and products.

One explanation for the failure to involve suppliers early is that companies view ideating as steadfastly within its purview. This perspective then dictates the timing and level of involvement of suppliers. As noted in Figure 6, Capgemini Consulting has found that both procurement and suppliers tend be involved after the concept stage and many only in the prototyping stage or later. From a contribution angle, the study found that organizations do not task suppliers to provide ideas - they count on suppliers to deliver goods to market quickly.

Figure 6: Involvement in Product Development Lifecycle

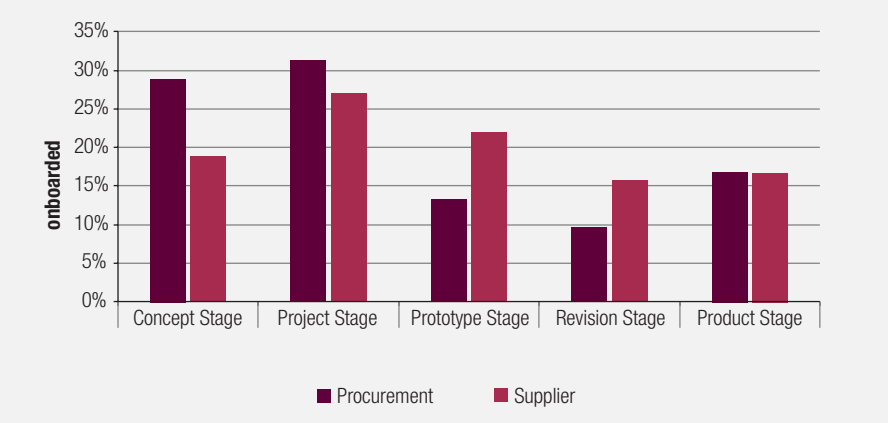


Figure 7: Supplier Value Contribution to New Product Development

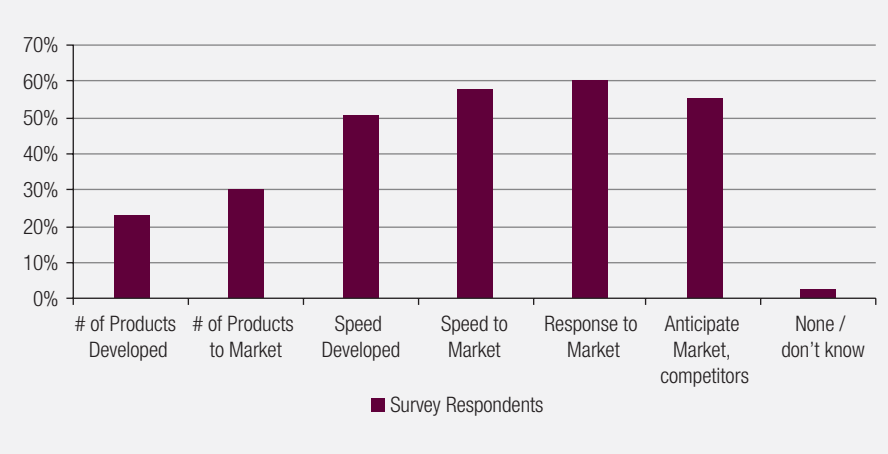


Figure 7 shows that only 20-30% of respondents view quantity of products developed and brought to market as a supplier innovation value proposition. Twice as many, 50-60%, of respondents view speed of development and agility as the true value suppliers contribute. In order to realize these benefits of IDP, earlier engagement of suppliers will allow the partnership to anticipate challenges and work together to solve them.

Companies that involve suppliers from start to finish reap the benefits of higher ROI and increased levels of project efficiency and success. While some companies involve suppliers early, the survey shows that 54% of companies on-board suppliers at or after the prototyping stage and 17% wait until the final product stage to involve the supplier.

A very small number of companies can be considered "open innovators," that is, those that engage suppliers in the early stages of innovation 90% of the time. The longer a company waits to engage its suppliers, the lower the value-add potential. Ultimately, lack of early involvement with suppliers is an opportunity cost. Innovation Driven Procurement requires early collaboration with supply partners to meet the objectives of bringing goods to the market quickly, efficiently and effectively.

In the responses, procurement fared better than suppliers; 60% are involved during the concept or project stage of a new product or service. The more integrated procurement becomes in the innovation process, the more opportunities there are for suppliers to participate and enhance the process. Therefore, it is not surprising that supplier involvement lags behind procurement's. To change this trend, procurement must articulate its value statement, broaden its relationships in the company and develop the right skills on its teams. This would usher procurement into the innovation fold and allow suppliers to follow. Unfortunately, companies remain reluctant to involve procurement and suppliers at the earliest stages of product or services development due to lack of relationships or fear of proprietary breaches.

How to Move Forward

To make a successful transition from a traditional procurement organization to an Innovative Driven Procurement organization, procurement must re-evaluate its staff, its processes and its relationships with both its internal clients and its external partners.

Organizationally, procurement must create an innovation-driven culture, starting with hiring people with the skills needed in an IDP environment, e.g., internal and external relationship building, project management experience, product knowledge and strategy, and a firm grasp of digital and mobile solutions to deliver innovation.

Operationally, the involvement of procurement in innovation-based projects is a must and the process to do so should be well-defined and broadly communicated. There needs to be a concerted effort to generate, vet and execute innovative ideas from internal and external sources.

Procurement must gain a seat at the table to influence innovation and position its organization as a preferred customer with select innovative partners. A company will not extract meaningful innovation value from suppliers that are held at arm's length (read more on this in the Further Perspectives on Procurement's Value Generation section). These two steps are foundational to drive the value of IDP throughout the organization.

In order to enable the transition, we suggest choosing a business unit and a project on which all parties (Procurement, business and supplier) collaborate to demonstrate the value of IDP. The success and savings generated by this project will then serve to encourage broader participation.

The fact that CPOs are beginning to recognize the innovation value proposition and collaborating in the product development cycle is a strategic victory for Procurement.

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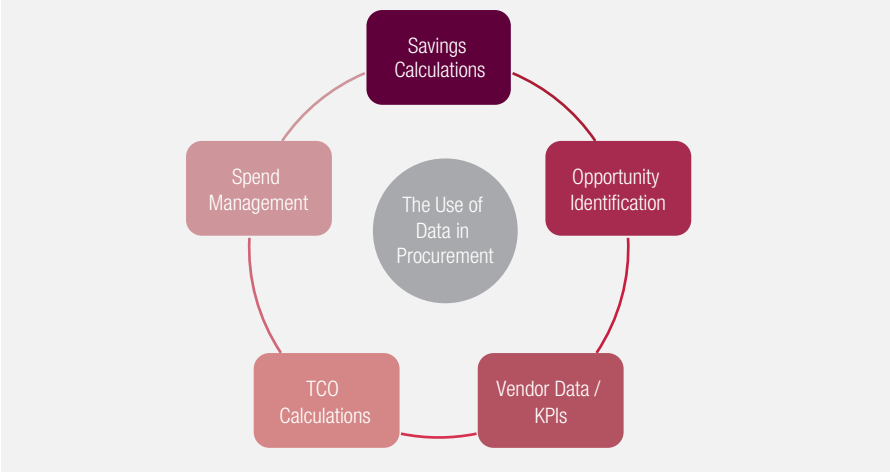
Master Data Management – A Cornerstone of the New Procurement Organization

Figure 8: Role of MDM within a Procurement business function



MDM and Procurement

The rise of "big data" (data sets which are too large to comfortably and efficiently work with common database management tools) has been a hot topic for quite some time; in the last two years, we have noticed an exponential increase in organizational implementations of data-driven decision tools relying on the collection and organization of "big data". With the inevitable growth of business intelligence and analytics, this year's CPO Survey explores the current state of Master Data Management (MDM) in leading procurement organizations and the biggest challenges to deliver the value of MDM. In addition, we propose a four-pillar, best practice framework to deliver a successful MDM strategy.

Procurement as a business function is largely driven by the use of data to recognize, sort, and execute savings initiatives. As such, its success is correlated to the effective management of the data. This inherently suggests that procurement organizations should have a comprehensive grasp of MDM. *MDM* can be defined as the unifying practice of three key functions:

- **Capturing data once**, accurately, completely and consistently thus enabling master data quality;
- **Storing and integrating data** in a way that guarantees integrity and a single place of reference; and
- **Distributing and reporting to those who need it,** whenever they need it, both internal and external.

Although MDM is useful to many business units within an organization, procurement in particular benefits from a well-governed MDM strategy due to its intense use of data in not only transactional activities but also trends analysis and opportunity identification that underpin strategic objectives.

At Capgemini Consulting, we see the effective use of MDM as a cornerstone of the new procurement organization - an organization that is capable of effective, rational and optimal decisions about major spend. MDM is best managed by keen focus on: Strategy and Vision, People and Ownership, Systems and Applications, and Processes and Procedures.

Insights from Survey

In this year's CPO survey, we tried to gain a picture of the current state of MDM in procurement organizations around the globe. To do this, we inquired as to the level which MDM is implemented at survey participants' companies and how it is organized. In addition, we asked what the biggest challenges were associated with implementing MDM.

We found that MDM is still not a primary focus for most procurement organizations. Of all the companies surveyed only 26% had a fully implemented MDM strategy. Although another 30% acknowledged that MDM was on their horizon, 36% of companies surveyed expressed no plans to incorporate MDM into their practice. Consequently, procurement organizations are, for the most part, not yet leveraging the tools available to become more effective.

To find out where organizations are lagging in their MDM strategies we asked participants to state their biggest challenges associated with MDM.

The three main challenges identified were:

- Capabilities within business functions and IT to manage data,
- Data governance and effective ownership, and
- Standard and effective maintenance process

Example: A leading insurance company was experiencing difficulties with Master Data Management as it grew. They had 14 ledger platforms and over 50 applications in place for financial reporting. As a result, the process of getting an accurate, real-time snapshot of operation was extremely challenging. By establishing an effective MDM standardization and governance process, they were able to cut their reporting process time by 50%, and significantly reduce their number of ledger platforms.

These challenges have adverse effects identified by the participants. A quarter of them stated that MDM in their companies was not well managed, while 53% replied that their companies are not yet leveraging digital capabilities. The most distressing insight, however, was that the three biggest challenges facing the participants were related to the ineffective management of MDM. These three challenges could be summed up in three words: **Master Data Mismanagement**.

Four Pillar Approach to Tackle Master Data Mismanagement

We found trends in the survey data to help identify the root cause of Master Data Mismanagement. In particular, companies did not identify a lack of expertise in data and systems as a challenge to implementing MDM. The challenges identified, however, reveal a lack of strategic alignment of MDM in organizations. Further, in many organizations the functions of MDM have not yet been clearly established and therefore data use is suboptimal.

Although it will vary from company to company, a four-pillar framework can be used to guide the optimal implementation of MDM:

- **Strategy and Vision:** The use of MDM should be driven by a clear business need. As with any major company initiative, the deployment of an MDM strategy should follow an extensive study of the functions that are impacted by data sets, e.g., 'vendors' which directly affect the procurement operation. Developing a roadmap that accounts for the needs of all primary stakeholders will facilitate the strategic planning process.
- **People and Ownership:** Unambiguous ownership and governance of master data is essential. Without question, effective control of data is achieved only if the business users own it. This requires buy-in from the top, emphasizing the importance of data as the lifeblood of the organization, and a foundation on which to build. For the procurement organization, having all the stakeholders actively participate and be knowledgeable in MDM is key.
- **Systems and Applications:** Bringing together a master data repository where data is effectively managed allows for proper control and integration of all the systems, users and processes that need to share that data. For the procurement organization, this means using state-of-the-art procurement management systems that can integrate into the company's ERP system. As with the last survey, there has been a trend for procurement organizations to become responsible for an increasing amount of a company's third party spend. In addition, a greater amount of spend is now being handled through electronic means such as P-Cards and Purchase to Pay solutions and systems. In order to handle all of this complexity, organizations should leverage the systems and applications that exist.
- **Processes and Procedures:** Embedding cross-functional processes, procedures and workflows for Master Data Management into the organization ensures that master data can properly support the core processes that rely on it. This becomes a critical step, as a quarter of the companies surveyed stated that MDM was not well managed in their company.

Moving Along in the MDM Maturity Curve

At the moment a strong MDM strategy can be a source of competitive advantage and agility; as companies realize the importance of MDM, the competitive landscape will change and maturity must increase. We employ six markers to understand a company's MDM maturity level:

- **Governance:** The management, maintenance, and uniformity of MDM inside a company.
- **Capability:** The processes in place to extract maximum value from the available data.
- **Maintenance:** The processes used to maintain and update the systems it describes.
- **Quality:** Accurate, timely, data that reflects the real world information to which it refers.
- **Nomenclature:** A consistent language to describe the data and initiatives to ensure all stakeholders share a common understanding of relevant data words and terms.
- **Tools & Systems:** Available solutions to deliver MDM. Common tools used for MDM include Infosphere (IBM), Oracle Product Hub (Oracle), Netweaver (SAP) and Informatica.

MDM Maturity Matrix

Factors	Standard	Advanced	Best in Class
Governance	MDM is a secondary initiative inside of the company. The standard processes are inconsistently used. Leadership lacks in the communication of MDM initiatives.	MDM practices are effective and secure. There is clear ownership of the initiatives. MDM is used throughout many areas consistently.	Clear leadership model with high expertise of MDM. MDM is pushed as a key company-wide initiative. Consistent processes are used and communicated to all.
Capability	Data provides enough information to make tactical decisions based on basic analytical insights.	Structured data provides a high value of insightful information that can be quickly extracted to guide important decisions.	The organization is able to maximize the value of the structured and unstructured data by using advanced analytics and data management practices. Data can be used to guide important strategic decisions quickly.
Maintenance	Data is maintained inconsistently, yet enough to provide an idea of state of current operations. The maintenance of the data is not a first priority for the stakeholders.	For the most part, the data shows an accurate idea of the real life performance. Data is updated on a consistent basis, but is not real time.	The data is up to date and accurately reflective of the real-life construct that it is based on. Stakeholders actively update and optimize the data and database architecture so that it is real-time.
Quality	Data contains inaccuracies that may affect the relevance of the data. Checking all of the data is a necessity to make decisions.	Data is accurate enough to be trusted to make decisions. Minor inaccuracies do not significantly affect the overall information presented.	Data is input accurately from the start. The data can be fully relied on to make important decisions.
Nomenclature	Language used for data is inconsistently used by stakeholders and causes minor confusion. It impacts the value the data can bring	The nomenclature is mostly consistent across most areas in the company and significantly adds value to the Master Data.	The correct language is accurately and consistently used by all stakeholders to understand, relate to, and maximize value out of the data.
Tools and Systems	MDM is limited to systems that provide basic functionality. Expertise is limited to very few individuals.	Advanced MDM solutions are in place and partially understood by the most involved stakeholders.	Best-in-class systems custom tailored for the company are used and understood by all major stakeholders.

Procurement's Role in Enterprise-Wide MDM

While MDM is fast becoming one of the variables for the procurement organization, its scope reaches far beyond this fucntion. MDM directly affects finance, marketing, operations, logistics, and almost all areas of a digitally enabled organization. For this reason, MDM roles and responsibilities must be made explicit – including those of procurement. To extract the full value of MDM, procurement organizations should advocate on two fronts:

- External: In a company-wide MDM initiative, the procurement organization should act as a change agent. As an organization that works directly with most areas in the company. Procurement is uniquely positioned to advocate the value of leading MDM strategies. This means getting involved in hiring the right firms for implementation, assuring the proper training, and of course, minimizing the TCO of the MDM initiative. The procurement function should push for a centrally owned and governed MDM team.
- Internal: To do all of the above, the procurement organization needs to set examples – it needs to lead MDM strategies to discover, implement, control, and optimize the company's major spend.

In conclusion, although MDM has yet to secure its place inside organizations, we expect to see an increase in focus on the value of MDM. Procurement organizations have much to gain with the rise of the MDM, as their processes will become much more effective and so too the value of procurement to the organization as whole. By using the four-pillar approach that takes into account Strategy, People, Systems and Processes, companies can identify and counter their primary challenges to implementing MDM. In order to better compete in the coming years, we advocate that companies move along the MDM Maturity curve by investing in the six main factors that guide best-in-class MDM. Procurement organizations should use this framework to instill leading MDM practices both internally in their organization, and externally in their company.

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Risk Management as a Means to Increase Procurement Value

Overview

Various studies have highlighted that supply chain risks are a growing concern for business leaders. Because of this, one could expect CPOs to have promoted Risk Management as a hot topic. Indeed, more than ever, respondents to this year's CPO Survey report they have instituted risk management strategies. Primary measures implemented to manage risk are: multisource strategies, continuous monitoring of supplier performance and a defined risk management process. While progress has been made, our study found that CPOs still have much to do in the area of Risk Management. Few risk indicators are being covered, risk anticipation and contingency plans are too often skipped, and too little investment has been made – for instance on risk-focused trainings or technologies – in order to say that risk management is now fully embedded in procurement's DNA.

Procurement Risk Management: CPOs no Longer Skip the Question

When thinking about risk and potential supply chain disruptions, most executives remember the devastating 2011 earthquake in Japan that severely disrupted industries ranging from steel to high-tech and automotive manufacturing (its economic impact was estimated by the World Bank to be as much as $235 billion - making it one of the most expensive natural disasters in history). While this example may be considered an anomaly, supply chain disruptions are common. According to the Supply Chain Resilience 2012 survey from the Business Continuity Institute, 73% of companies had experienced at least one disruption in the previous twelve months (with 21% reporting more than $1M in costs for a single incident). After recent times of economic uncertainty that weakened key suppliers in some industries' supply chains, we asked CPOs how they manage/mitigate procurement and supply chain risk.

In the Capgemini Consulting 2012-2013 CPO Survey, almost 70% of respondents stated they had put in place at least one strategy or action plan to assess, mitigate and manage supply/supplier risks. That is a dramatic change from the 2010 CPO Survey when 60% of respondents simply skipped the question. As a CPO stated in our survey: "The whole purchasing organization participates in exercises to proactively identify risk elements and their probability and magnitude, and puts together supplier/segment/risk specific plans to prevent the risks and make necessary preparations to handle them should they occur".

Multi-Sourcing, Supplier Performance Monitoring and Establishing a Clear Process on Risk Management are the Key Strategies Put in Place

First, as Figure 9 indicates, a decisive shift seems to be underway as companies switch from single sourcing to multi-sourcing for key commodities/ services (74% of our respondents, compared to 32% in 2010). Despite some resistance by 'traditional' category managers who may fear economic sub-optimization from such a decision, companies have moved to multi-sourcing to prevent strong dependence upon a single, or minimal supplier(s). By selecting more than one supplier to deliver their quality, price and reliability requirements, these CPOs have chosen to mitigate risks such as supplier bankruptcy or performance declines for strategic categories that are critical to business operations and client needs.

Figure 9: Strategies used to assess, mitigate and manage supply/ supplier risk compared to 2010 Survey results

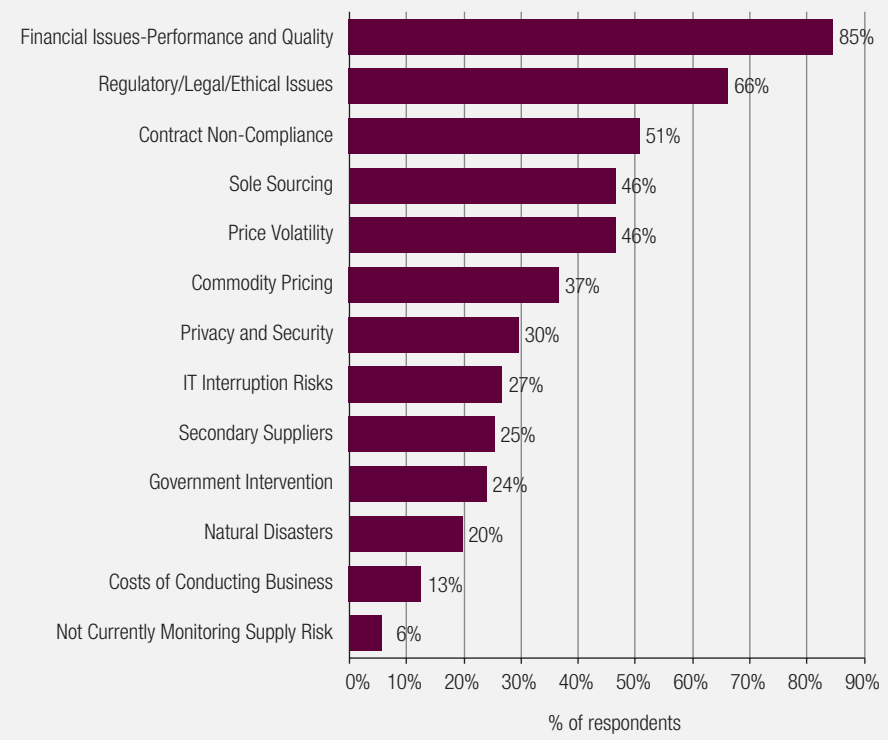
Second, As was the case in 2010, two thirds of our survey respondents declared that they continuously monitor performance of their suppliers and take action to mitigate emerging risks (e.g., quality decline). Mature organizations in procurement integrate supplier risk management into their ongoing activities: from Strategic Sourcing (e.g., during the supplier evaluation process) to supplier relationship management (various collaboration or partnerships with suppliers to detect early warnings or implementation of risk-sharing approaches). A leading practice in this area is to monitor and assess supplier risk not only for Tier 1 suppliers but also throughout the extended supply chain. Such a strategy can be effective in managing risks; according to a recent Business Continuity Institute survey, 39% of companies that reported supply disruptions in the 12 previous months identified that the issue came from Tier 2 (or lower) suppliers.

The third risk management strategy highlighted by 60% of our respondents is to put in place a clear process to continuously assess, mitigate and manage supply risks in general (e.g. risks related to disruption of supply, inventory and schedule, incoming delays, etc.). This is reassuring news when compared to our previous survey results in which only 46% of CPOs stated that they were taking action. It seems that a growing number of companies have realized they cannot rely only on a case-by-case approach to risk management, and have decided to define and implement a more rigorous approach to the issue. Our question is whether these processes are relevant and holistic to effectively address procurement risks.

Financial Performance as the Number One Risk Measure: Is It Enough?

Asked about the types of sources monitored, our respondents stated financial issues, regulatory/legal/ethical issues, contract non-compliance, single sourcing and price volatility. As noted in Figure 10, the most watched risk category is financial according to 85% of respondents.

Figure 10: Sources of supply risks currently being monitored



Such a focus on financial performance indicators is not surprising; this is a valid and long-standing indicator; however, the risk is that the monitoring of a few "past performance indicators" (generally on financials, quality and service delivery) provides a limited view. A look at recent natural disasters and political turmoil, one could question whether financial issues are the most pressing ones to be monitored. We suggest procurement organizations take a more balanced approach and consider a scorecard that focuses on a combination of several factors. One example is a consistent review of commodity price fluctuations. A category manager could turn volatility into opportunity precisely by monitoring commodity volatility and either mitigate financial risks or take advantage of low price opportunities.

Few CPOs have invested in strong Risk Management capabilities

Our findings also raised questions about whether CPOs have set up specific capabilities to manage risk as part of ongoing procurement activities. According to our survey, less than one third trained their teams in advanced supply risk management techniques or implemented technology related to supply risk management.

Further, only 38% of respondents have established processes to perform proactive risk analysis and have contingency plans in place. Even though we noticed slight progress on this topic compared to 2010, it seems that CPOs have not considered (or perhaps have not received financial support from top management) investing/expanding their risk management capabilities.

While supply risk management is a growing concern for business leaders (more than 90% of those surveyed by the World Economic Forum in 2011 indicated that supply chain and transport risk management has become a greater priority in their organization over the last five years), a limited number of CPOs have translated this concern into strong risk management capabilities within their procurement organizations. Concern on this front is heightened when reviewing the impact of supply disruptions on companies. In a study of 800 supply disruptions, Hendricks and Singhal revealed that impacted companies suffered from 33%-40% lower stock returns, 107% drop in operating incomes and 11% increase in costs. Risk is a constant and our recommendation is that CPOs define and deploy a diverse risk management program.

Taking the lead on Procurement Risk Management

At Capgemini Consulting, we believe that risk management should be part of the procurement capabilities inclusive of formal risk management processes, dedicated and trained resources, and relevant technology support. CPOs wishing to make a difference in this realm should consider:

- How is risk management embedded into their Strategic Sourcing processes (e.g. supply market analysis, supplier audits, etc.)? To what extent do companies ask their key suppliers about their continuity plans?
- How often do Category Managers leverage external data to review and assess risks in their supplier portfolio (e.g. financial data, commodity price indices, etc.)?
- How often do companies actively take steps to ensure risk-sharing with suppliers (through regular negotiations, clauses, etc.)?
- How can procurement take the lead and establish a formalized role/group in the company responsible for anticipating and monitoring risk, e.g. a risk management committee led by procurement, but inclusive of legal, broader supply chain, and corporate audit?

Final reflection

By embedding Risk Management into procurement activities and processes, CPOs will expand procurement's value beyond traditional cost savings. What a great way to increase perceived value from their procurement department and become a strategic interlocutor for other internal departments and business partners.

Sources

- 4th Annual Survey – Supply Chain Resilience 2012, November 2012, The Business Continuity Institute
- Supply Chain and Transport Risk Survey 2011, World Economic Forum
- The Effect of Supply Chain Disruptions on Long-term Shareholder Value, Profitability, and Share Price Volatility, June 2005, Kevin Hendricks and Vinod R. Singhal

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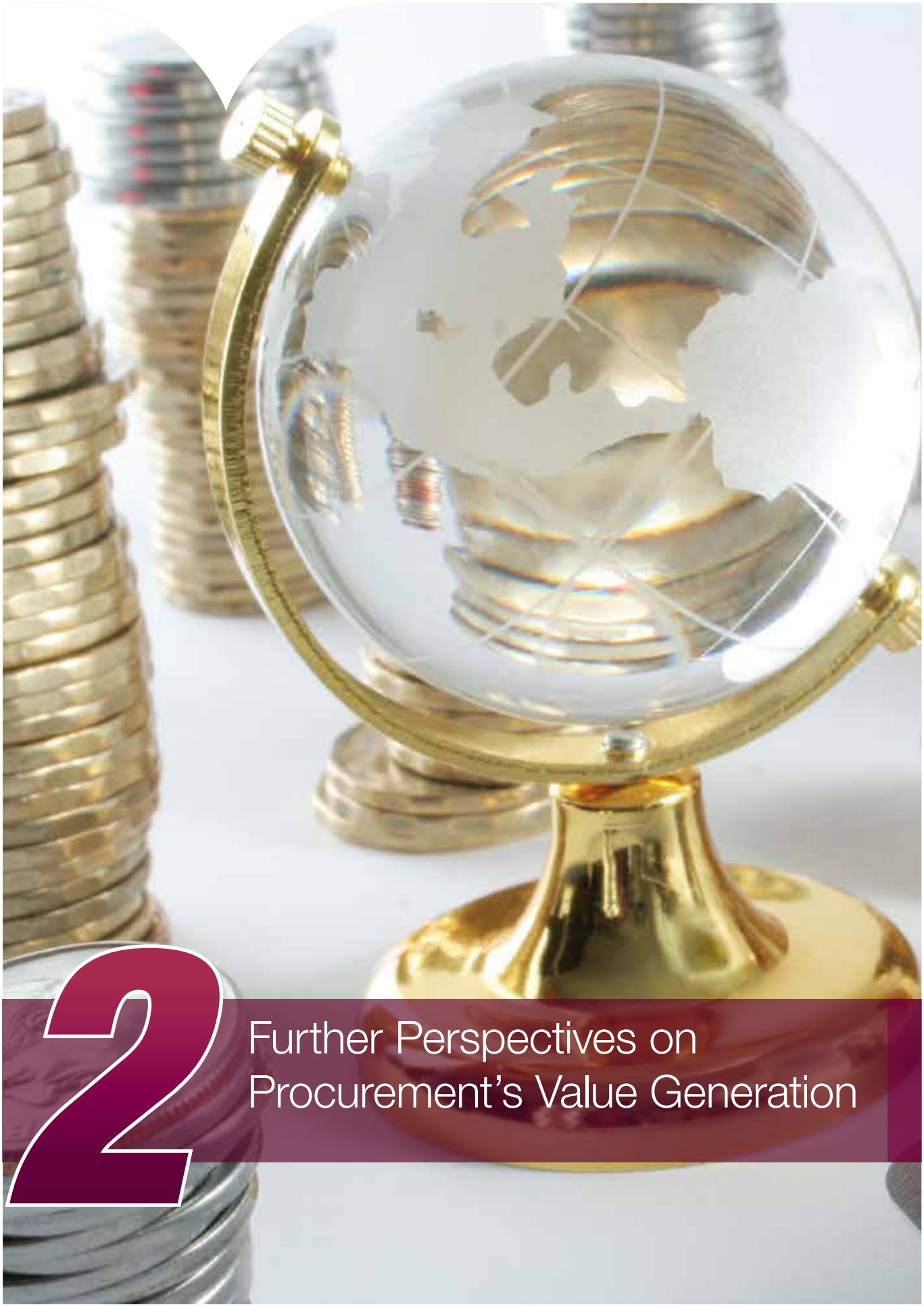


2 Further Perspectives on Procurement's Value Generation

Digital Procurement

One of the evolving megatrends of our decade, besides new forms of mobility, urbanization and the ongoing globalization, is the growing digitization. With *digitization*, we mean the *conversion of real-world content into binary numeric form*. We even believe that digitization has the potential to become the driver of the third industrial revolution, after the steam engine and electricity in the past. Needless to say this new driver will impact all entrepreneurial areas. In this section we analyze the impact it will have on the procurement function in detail. In order to fully understand the resulting effects and tools, we first start with an overview of the underlying trends.

Current Trends in Digitization

I. Cloud computing

The cloud enables a real-time access to a corporate database from multiple devices (see figure 11). By outsourcing the operation of the cloud to external service providers, the use of IT services can be adapted and scaled to the actual fluctuating demand.

II. Mobile devices

Along with the increasing globalization and mobility, mobile devices have become the preferred mode of communication for both private and business travelers. In developing countries with lack of fixed ICT infrastructure (e.g. India) the growth in ICT mainly depends on mobile devices. This comes along with a steady drop in equipment prices.

Figure 11: Enterprise-wide connectivity with the cloud

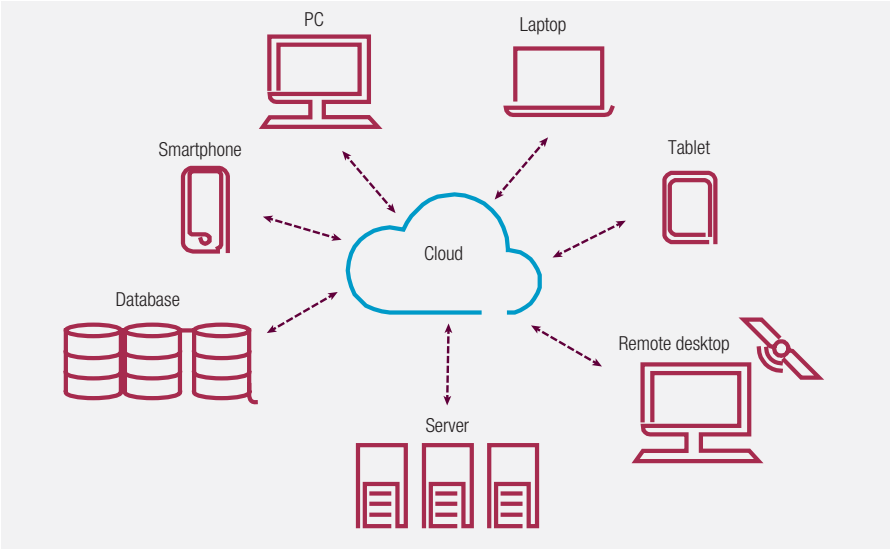


Figure 12: Development of mobile devices

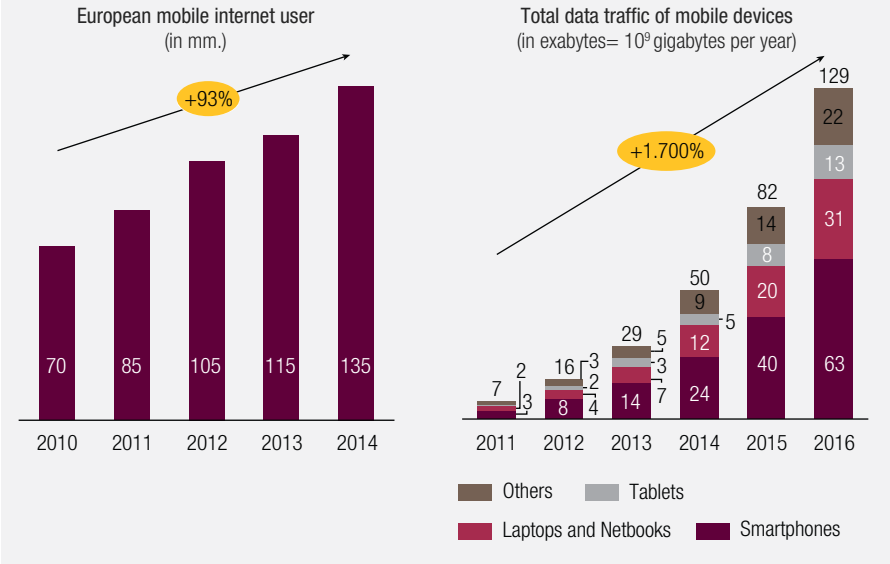


Figure 13: Amount and costs of data storage

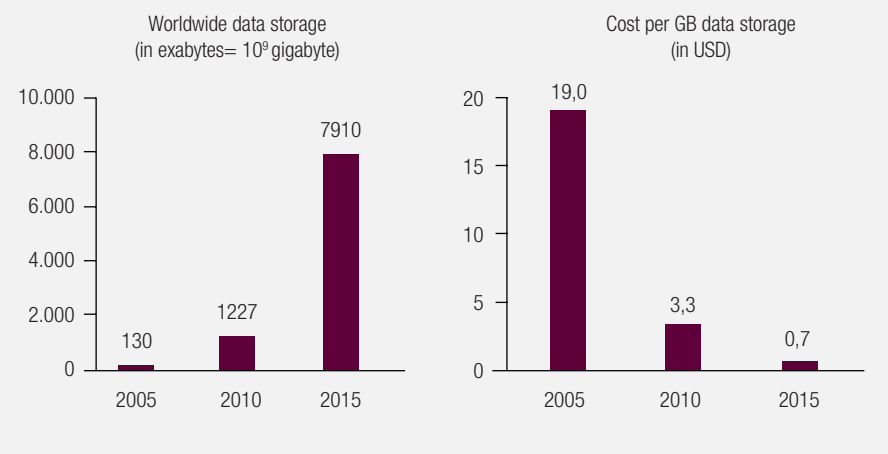


Figure 14: Examples of social media

III. Business intelligence

The amount of worldwide data storage has increased dramatically within the last decade, as prices for data storage have almost dropped to zero (see Figure 13).

IV. Social media

Social Media has fundamentally changed the way we communicate. We no longer call people, but instead blog and twitter. Whereas companies use the new media mainly for marketing purposes, private persons use it as the preferred mode of communication with friends.

Benefits of Digital Procurement

Digital Procurement means the use of digital technologies to radically improve the performance and capabilities of the procurement function. We believe that Digital Procurement has the potential not only to increase efficiency of the procurement function but also to transform its operating model.

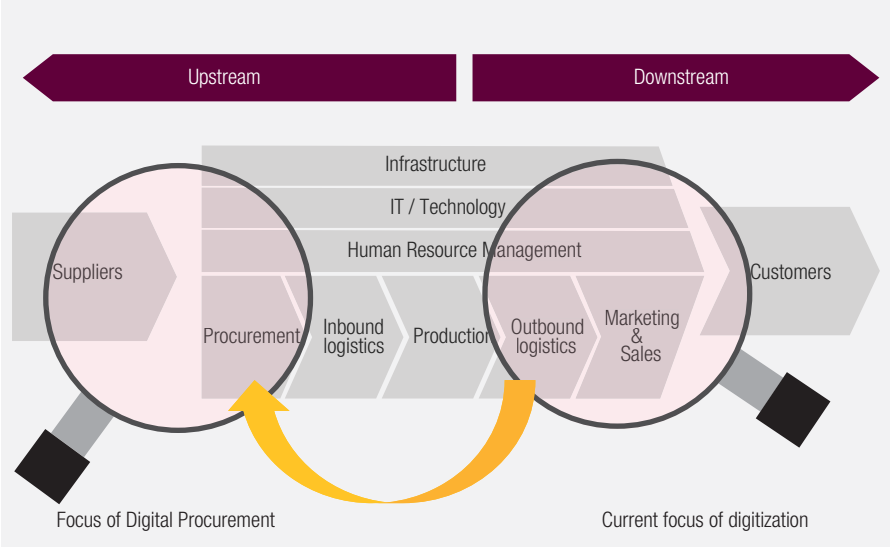
Currently, digitization within enterprises is mainly deployed in the interaction with customers. In the marketing function, we can observe a lot of effort being made in order to derive as many conclusions about customers' needs as possible (e.g. dedicated rewards programs to gain understanding of buying patterns, online-platforms for product customization etc.). However, when we take a closer look at procurement, we will find a different situation. The results of this year's CPO survey show that only 47% of the participants stated that they leverage digital capabilities in their procurement function, whereas the majority have not made any efforts so far.

This result reveals that most of the companies simply give away great optimization potentials, as the following paragraphs demonstrate. By shifting the focus of digitization from the downstream towards the upstream of the enterprise (see Figure 15), companies could leverage new ways of streamlining their organization.

Social media for example also has the potential to breakup intra-organizational knowledge silos. Via enterprise-comprehensive wikis and blogs, knowledge can be shared and utilized for procurement purposes (e.g. identification of technological improvements by certain suppliers that might justify increased prices as they lead to higher quality). For larger procurement functions, commodity-specific knowledge and sourcing communities are a simple way to capture intrinsic knowledge and make it available for a broader community. Even reactive training and qualification measures can be enriched by proactive sharing of current market trends via online communities. Another example is the emergence of digital supplier networks. These are not only ways to identify and get in touch with a larger number of suppliers but also to easily route electronic purchase orders.

Business intelligence allows a completely new approach within procurement. Whereas years ago procurement was only able to reactively satisfy the demand triggered by requisitions, now it is able to act proactively by forecasting the demand based on identified patterns. This provides traditional purchasing with a new scope of action (e.g. to prepare and negotiate more appropriate framework contracts). Another benefit is a more detailed understanding of the performance of suppliers. This can be used to weigh strengths and weaknesses of the allocation of certain suppliers to certain key products. It can be achieved by detailed root-cause-analysis based on e.g. ordering, delivery and quality data. Furthermore, these analyses enable a development away from normal spend analysis towards determination of the right costs for goods and services.

Figure 15: Focus of Digital Procurement



As cloud computing is not a front-end technology, it might not be recognized as a main driver. However, it is the enabler of a variety of tools. Cloud computing allows real-time access to the corporate database (e.g. for procurement data such as contracts, PO's, price lists…). Centralized supply chain portals enable a synchronized link of suppliers to the companies' ERP systems. This clears the way for a harmonized demand planning and fosters stock reduction. Via this common access, cloud computing fosters the standardization of tools & templates (e.g. requisition, RFx, PO's). The access is also independent of the actual location of the procurement department, which permits a new geographical distribution of the procurement function (e.g. outsourcing to shared procurement centers).

Finally, mobile devices unify the benefits of the mentioned drivers. By accessing real-time supplier performance data stored and analyzed on the corporate database, procurement managers have unforeseen possibilities during negotiations at the supplier site. Furthermore, customizable KPI-dashboards enable more precise conclusions on strengths and weaknesses and can be easily shared with the supplier. Requisitions as well as purchase orders can be reviewed and approved by procurement managers while they are on their way to the next negotiation. Lastly, the enhanced traceability of goods via mobile devices helps to achieve a more timely provision of goods.

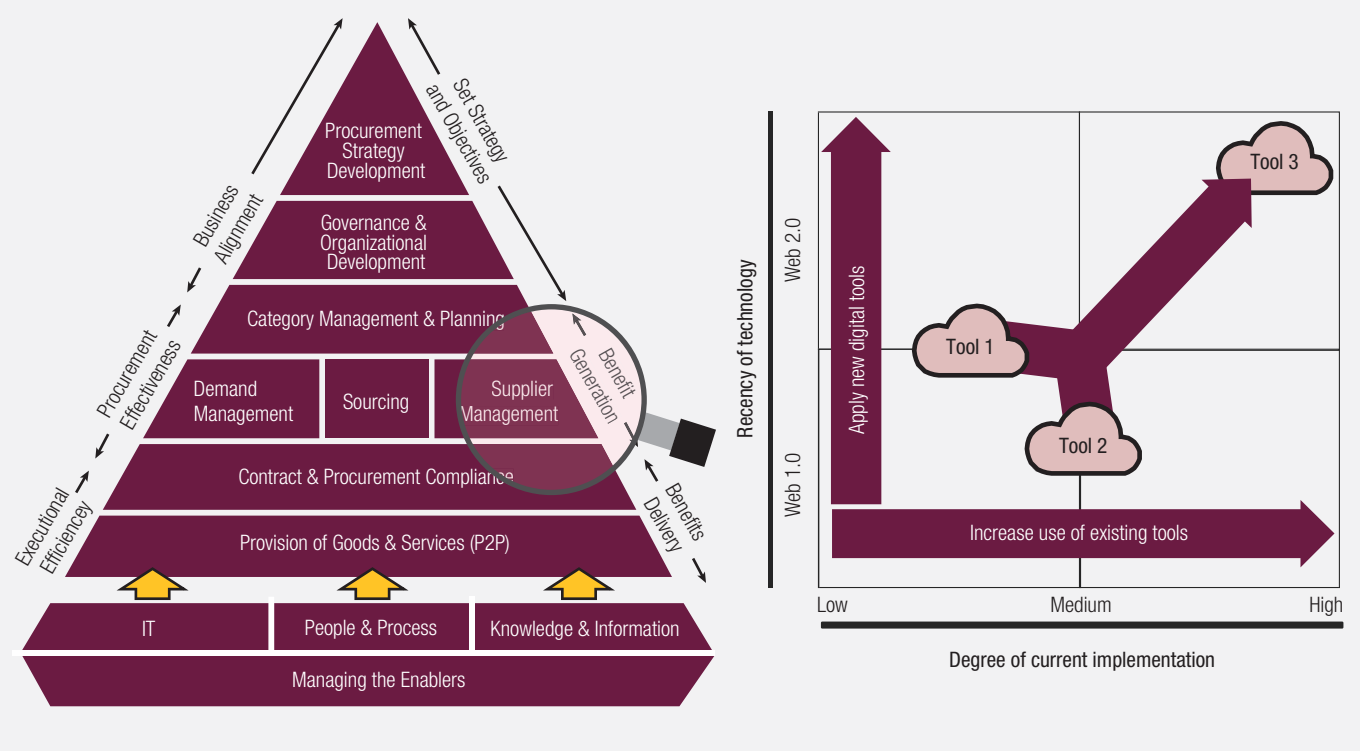
All these digital tools have the potential to revolutionize the procurement function. As mentioned before, their current use however is limited. Capgemini Consulting with its *Digital Procurement Assessment*, proven methods and best practice approaches can help to leverage the full potential of Digital Procurement by evaluating the progress made regarding the digitization within the procurement function.

Along our *Procurement Transformation Pyramid* we support our clients in assessing the required actions in the different procurement areas (see Figure 15). For each area, the existing digital tools will be evaluated. It may be the case that important tools have already been introduced, however employee adoption has not reached the required level. In this case, the tool usage needs to be fostered by applying the right change management techniques. On the other hand, important new tools may not have been identified and implemented for some procurement functions yet, or form a standalone system. In this case, appropriate tools need to be introduced and/or linked to already existing ones.

Such a transformation project must not be restricted to the tools and IT perspective, but also consider the change triggered in the business and people perspective in order to fully integrate the proposed solution into the company.

By increasing the use of the right Digital Procurement tools, organizations can start today to prepare for the upcoming competitive challenges of tomorrow.

Figure 16: Approach of Digital Procurement



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Innovation-Driven Procurement Performance Monitoring

Introduction

For years companies have focused their supply base performance measurement primarily on spend and cost management metrics. Most have implemented systems to assess and monitor procurement activities such as category spend, savings rates and on-time delivery (OTD). These measurement systems provide "facts". Of course, these 'facts' remain relevant but we see a new trend emerging – the measurement of "soft" facts or behaviors – particularly in the area of innovation. While traditional supplier performance assessment is associated with metrics and goals to achieve desired outcomes, companies infrequently monitor concomitant innovation metrics.

Innovation Performance

Innovation metrics are based on:

- The success of an innovative sourcing program
- The contribution to overall innovation performance

Innovation performance measurements help speed innovation from suppliers. They enable communication of firm-level innovation strategies, objectives and priorities to business units, R&D, supply management, other functional areas and suppliers. Metrics enable management to assess business units and suppliers performance and to provide executives and managers with valid, auditable measurement of innovation's contribution to organizational success. Another objective of innovation metrics is to influence and guide behavior – both internally and with suppliers – that leads to successful collaboration with as well as innovation from suppliers.

One important distinction to consider when discussing innovation metrics is the difference between major innovations that can add significantly to firm revenue and continuous improvements that simply reduce costs. Most companies separate continuous improvement innovation from stand-alone initiatives and they take different approaches to manage each. It is also apparent that companies struggle to construct valid and reliable innovation metrics.

Innovation metrics should be applied to all organizational constructs such as revenue generated by new products, number of new projects entering the NPD (New Product Development) cycle, number of preferred suppliers assessed on innovation capacity, and number of new ideas presented by suppliers, to name a few.

Supplier Innovation Metrics

Especially in the industrial sector, suppliers are important contributors to innovation success, as the purchased component often comprises a substantial portion of the final product. In this context, there are fundamental questions that need to be answered:

- What is the supplier's overall capacity to innovate?
- What is the supplier's contribution to innovation success?

Companies are more likely to measure actual supplier innovation performance rather than supplier potential for innovation. However, we suggest that both need to be measured.

Some metrics for supplier innovation potential:

- Technology leadership
- Number of design engineers/design centers
- R&D spend
- Investment in new capital
- Co-design capability
- Past innovation record
- Program management capability
- NPD process contributions

Some metrics for supplier innovation on NPD programs:

- Number of innovations brought to client
- Number of supplier designs incorporated into new products
- Proactive communication of supplier strategy and roadmaps
- Costs, performance, delivery achievements vs. objectives in later NPD stages
- Total Cost of Ownership (TCO) achievements vs. objectives
- Responsiveness to client needs in the NPD program

Beyond these metrics, it is important to consider supplier contributions to the overall innovation progress of the firm. Supply managers and procurement are often prominent players late in the NPD cycle and are focused primarily on commercial aspects of interactions with the suppliers. Supply management cannot be separated from the overall effort and it is therefore worth measuring and monitoring this. Finally, though the supply base is still primarily evaluated on traditional metrics such as costs, quality and delivery, there are metrics companies can use besides these to direct the efforts of supply management and highlight its contribution to innovation success:

- Number of buyers assigned to NPD processes
- Number of projects in which NPD buyers are actively involved
- Satisfaction of innovation NPD team with procurement
- Number of qualified suppliers available for innovation NPD projects
- Contribution of procurement to risk mitigation within NPD projects

Continuous Improvement Innovation

In addition to innovation that leads to NPD for the buying firm, suppliers should be a source of continuous improvement innovations that contribute to production and TCO reduction. Setting a cost reduction objective in the NPD process can help to define a continuous improvement plan that will maintain margins in a competitive environment.

Such projects can lead to manufacturing cost reductions, cycle time reductions, quality improvements, parts rationalization, design changes, etc. in order to reduce TCO. Methods such as value analysis, design or redesign to cost, Kaizen, and Lean can be implemented for these purposes.

Metrics of this type of are rarely associated with NPD processes but they are related to the success of continuous improvement projects. Some could be:

- Number of projects
- Resources devoted to projects (client and supplier)
- Savings
- Quality improvements
- Cycle time improvements
- SKU reduction

Innovation-Driven Procurement Planning

Supplier involvement from the early stages of the NPD process is the best way to maximize innovation success for both the supplier and the organization. Despite metrics deployed all along the NPD process, management of the supplier is needed in order to:

- Develop transparency and trust among teams
- Manage objectives vs. tollgates
- Validate innovations
- Mitigate risks
- Manage profit/gains sharing

Client cross-functional teams manage the whole NPD process and suppliers should be part of it. Program reviews are still the governance means to validate tollgates and suppliers need to be fully involved from preparation to debriefing. Procurement functions, and commodity buyers in particular, need to oversee supplier performance and to validate compliance to commodity strategies. To do so, procurement should organize regular contract reviews and define joint action plans to improve collaboration efficiency and ensure global innovation success.

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Leverage Your Supplier Capabilities by Becoming the Preferred Customer

While the sales side has and continues to segment and classify its customers, few procurement organizations are aware of how they are perceived and classified from their suppliers' perspective. More than that, very few organizations actively work to become their suppliers' preferred customer. The reason for this dichotomy is that few understand the value of being a supplier's preferred customer.

Becoming the preferred customer is a cornerstone to advancing successful procurement – supplier relationships. To become a preferred customer is one of the more important strategies to derive the full value of a long-term customer/supplier relationship. The role of preferred customer positions procurement departments to drive continuous improvements and innovations with its key suppliers, and generate value that is passed to the company and to its customers.

A Foundation to Build Upon

Before you focus on the preferred customer concept, here are some key areas to address:

Attractive Volume

Without offering suppliers attractive volumes, it will be a challenge to attain the position of preferred customer. Some companies target small and medium size suppliers because it increases their likelihood to be a primary customer and its chance to influence outcomes. In this case, it is important to balance the risk of becoming too dependent on a single supplier. One way to mitigate this risk is to set an overall purchasing target to avoid constituting more than, for example, 20% of the supplier turnover.

Long-Term Perspective

If the supplier does not know that a long-term business relationship with your company is desired, you will never be ranked number one. Therefore, it is important to communicate to the supplier that it can attain a preferred position and the necessary conditions. It is crucial to be clear and transparent in your communication and reinforce words with actions; share relevant information and have a clear development strategy for each supplier. In this scenario, the full value of mutually preferred status may be attained.

Fair Profitability

A long-term perspective and a predictable sales volume will increase your attractiveness to suppliers but without offering the supplier a fair profitability over time; you are unlikely to move the partnership further. Even if a supplier is more expensive than its competitors at the outset of the relationship, evaluate the effort to attain an advantageous ranking as well as the full potential return.

Leverage Your Opportunities to Reach Top Ranking

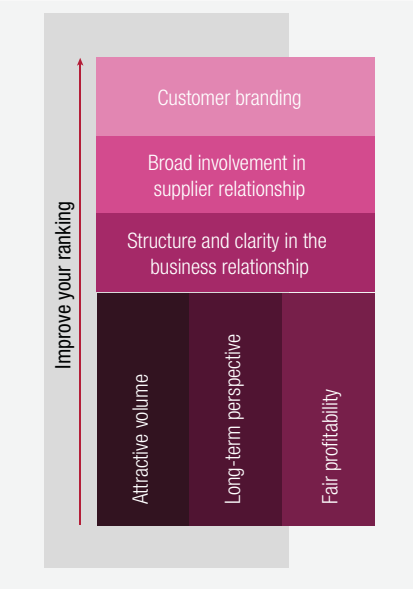
Your organization's ability to collaborate and its approach to the relationship are ways to boost your chances to attain preferred customer status.

Broad Involvement in the Supplier Relationship

To leverage your supplier relationship, and increase your chances to be a preferred customer, the relationships should be established at multiple levels - from owners and CEO to quality managers, production managers and in some cases key line staff. Connecting with supplier top management gives you the opportunity to sell your organization and the flexibility to potentially bypass the KAM (Key Account Management) when necessary. Multiple levels of alliance increase communication channels and the potential to benefit from improvements and innovations. As important as it is to build relations with multiple stakeholders at the supplier, it is equally important to reciprocate - the supplier should have access to key stakeholders in your organization.

Clearly, your behavior will influence the supplier's perception of your company. This includes not only procurement interactions but also everyone who

Figure 17: Important elements to consider in becoming the preferred customer



interfaces directly with the supplier, e.g., engineering departments, material planning and quality engineering. Many companies have core values to be applied within and outside the company; apply these same values in your dealings with suppliers.

A tried-and-true way to build rewarding relationships in the automotive industry is to invite key individuals from the supplier to assemble their parts in your production facility with you. This concept can of course be applied in other industries. It demonstrates your positive intentions for the relationship, and contributes to increased product knowledge and understanding of the entire value chain. Both act as enablers for suppliers to identify and share improvements and innovations with your organization.

Structure and Clarity in the Business Relationship

Cooperation with the supplier needs to be structured in a way that allows them to stay updated on current initiatives, plans and supplier performance KPIs. The rewards of exemplary performance and consequences of poor performance should be clear to both parties while keeping in mind that a coin has two sides. It is not uncommon that quality and delivery issues initially attributed to suppliers can be traced to poor or unclear specifications and renderings.

Having a mutual commitment to success and a structured method of working together will save time and money for both organizations; indeed, it is often cited as one of the positive customer characteristics that contribute to the goal of becoming a preferred customer.

Customer Branding

Your company brand is not only important to your end customers but also to your suppliers - in particular when dealing with small and medium sized suppliers. If your company is prominent, it will be easier to reach the top customer ranking, as suppliers will use you as a quality stamp in their sales pursuits. Naturally, this parameter is less easy to control but is important to bear in mind throughout the relationship.

Face the Facts

There are no shortcuts to becoming a preferred customer. In the end, suppliers require business volume, a fair profit and a long-term relationship. Remember, it might not always be the short-term, lowest cost supplier that brings your customers the most value. It will bring more value to your organization and your supply partners if you execute a shared vision to increase your competitiveness develop improvements and drive innovation.

If you succeed, you can move beyond capturing marginal value through negotiation – you and your suppliers will have a platform to deliver on total cost reduction throughout the development cycle.

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