



Supplier Relationship Management

An Advanced Supply Chain Management Technique

by Charles C. Poirier



EXPERIENCE. RESULTS.



As firms pursue supply chain optimization (SCO), they do so in a sequential manner. Beginning internally, with efforts aimed at reducing costs, particularly through better sourcing, improved logistics, inventory control and order management, firms progress to demand management and capacity planning, especially through components like sales and operations planning (S&OP) and advanced planning and scheduling (APS). As achievements are accomplished and documented, some firms determine the higher-level achievements come

with external help from key allies, and they enter the arena of Advanced Supply Chain Management (ASCM). Each of the previous efforts will serve as necessary precursors to taking the high ground in a market or industry – by getting the internal house in order before collaborating and applying technology in an inter-enterprise network. But now the focus moves to using the advantages gained internally to collaborate with selected allies to make similar or larger gains through a networked effort.

This higher, Level 3 and beyond supply chain effort, begins on the supply side, as the purchasing and sourcing function takes advantage of all the work that went into reducing the supply base, segmenting the suppliers in terms of importance, and beginning work with a few of those suppliers to build advanced level models, which will be beneficial to both organizations. Such an effort requires moving the firm into the realm of ASCM, with the assistance of a few strategic suppliers being an absolutely crucial ingredient to success. The vehicle for funneling that assistance into a proactive and beneficial format is Supplier Relationship Management (SRM), a keystone for constructing a successful ASCM system.

Participation in Virtual, Networked Environments Becomes the Objective

The movement to networked supply chain activity should begin on the supply side, because that is once again where the greatest opportunity for financial improvement exists, and it fits the pattern of having the house in order before approaching key customers in search of new business and further savings. The process follows a linear pattern. The firm completes its work on internal excellence and then peruses its list of key suppliers to find those willing and able to help in building a network architecture. Starting with a very few *trusted suppliers*, the idea is to work collaboratively to construct a business model containing the virtual liquidity of information transfer that will be compelling in the eyes of the targeted customers. Later, the concept can be expanded to include key customers whose help will be invaluable to complete the business model and move the focus to targeted consumer groups.

Today, many purchasing groups are testing the collaboration/ technology waters as they try to move forward with the savings they generated in the early levels of supply chain. For some, the idea of forming networks and then using the latest technology to enhance performance is simply an old trick brought up to date. What is new is the idea of collaborating across business entities and sharing information and practices so the constituents can all benefit. Another innovative feature is the concept that the purchasing function must rise in internal importance and become a vehicle for assisting the strategic intentions of the firm through inputs from key suppliers willing to help in that part of the relationship.

The advanced proposition begins with the idea that enterprises, buyers, and suppliers know how to collaborate. The problem has been that one or both parties think they must dominate the transaction that takes place. That’s an aspect of negotiation. Each party believes it has taken better advantage of the other or something has been lost. Win-lose is very much a pattern in historical buy-sell relationships. From a contemporary view, that concept loses its value as the constituents to the buying and selling seek a higher plateau and begin to focus on win-win, or how each entity can improve its position through collaboration with business partners. Working with a select group of suppliers, the advanced supply chain initiative is to find the hidden values that have eluded the buy-sell relationship, those which lead to better profits for both parties and building new revenues with targeted customers.

Through the collaboration, one key feature will be the application of technology at the right points in the jointly developed business model. Care must be taken, however, to not be premature in jumping to technology solutions. A great deal of SRM can be accomplished without software. What requires answering are these questions: Where will technology enhance the processing? What technology is



appropriate for our situation? Most importantly, why has technology implementation been so hard to achieve in a network environment? Generally, the answer to the last query is because of the lack of communications standards, common business processes recognized by all parties, and the inability to link disparate software and applications across an extended enterprise where each constituent is an expert on the one best way to communicate. It's also because of political considerations around who should dominate the relationship, who has the greatest experience, and who will compromise for the good of the alliance.

In spite of the Internet environment in which all forms of information can be shared at the click of a mouse, supply chain constituents will cling to their databases and only share what they think is inconsequential as they gather all they can to enhance their performance. The new thinking says that attitude prevents you from getting to the hidden values and savings that could come from a more open, sharing relationship. Important parts of the database that help both parties should be opened and shared through an interactive extranet designed for such a purpose. That knowledge, gained by whatever means, becomes a crucial element in SRM.

Supplier relationship management emerges from this difficult situation as companies seek the means to establish a more disciplined, honest, and strategically oriented environment around supplier relations – to assure that the network effort is harmonized to bring optimum conditions to all participants. From a purchasing perspective, this condition goes well beyond strategic sourcing, e-procurement and advanced purchasing techniques. It involves selecting a few, strategic suppliers and working diligently with them to find the optimized means of collaborating for mutual advantage. From another perspective, it also involves an alliance between the Chief Purchasing Office (CPO) and the Chief Information Officer (CIO). With this internal collaboration, their two organizations seek out those suppliers with whom they can design, test and apply the interactive communication systems needed for network cooperation.

Most importantly, SRM requires collaboration as a supplement to negotiation. As the participants to SRM move to a more disciplined and strategically focused and technically enhanced relationship, the sourcing effort moves toward using the supply side to establish a meaningful business model that supports and enhances joint business strategies. When accomplished, the distances between buyers and sellers will diminish and an integrated entity will be prepared to extend the network effort to the customer side. With the enhancements that come from the involvement of IT and the application of technology to bring features of the relationship online – to speed cycle times and connect upstream activities to the downstream necessities – the budding network only gets stronger. Then the firm goes forward toward customers knowing the network house is really in order.

SRM Becomes the Engine that Drives Collaboration

One caveat is in order before describing the models that will assist the SRM effort. To begin, there must be a solid purpose or guiding mission jointly developed and understood by all parties to the exercise. The intention of that mission cannot be to find additional values solely for the buyer. If so, the effort will fail. Too much has been extracted from supply chain efforts in Levels 1 and 2 through suppliers making concessions to maintain or grow volume. The next level of enrichment will come from collaborating on the means to find hidden values that benefit both parties, sharing the rewards, and determining how to build new revenues together. With a guiding vision capturing these thoughts, which both parties accept as meaningful, the business allies go into SRM looking for shared values. The next step is deciding on how the process should work. A definition often helps that phase of the effort.

According to Gartner Consulting, SRM is defined as “a set of methodologies and practices needed for interacting with suppliers of products and services of varied criticality to the profitability of the enterprise.” (Gartner: 2001, p.2) In view of what we just discussed, we would add to the definition that SRM is ***a means of building closer relationships with selected strategic suppliers, the purpose being to discover the added features that could enhance the relationship while improving business performance as the firms work in a network environment for mutual benefit and increase the likelihood of creating profitable new revenues together.***

How important can this relationship enhancement be? Gartner further suggests that “by 2005, enterprises will move strongly to SRM methodologies or they will see profit reductions of close to two percent.” This firm lists some of the potential benefits of SRM in Exhibit 1.

Exhibit 1 – The Benefits of SRM

- ✍ **Optimize supplier relationships** – treat different suppliers in different ways depending on the nature of the relationships and their strategic value
- ✍ **Create competitive advantage and drive revenue by jointly bringing new, better and more customer-centric solutions to market faster**
- ✍ **Lengthen and strengthen critical supplier relationships** – integrate suppliers into your business processes
- ✍ **Drive profit enhancement through reduced supply chain and operational costs while maintaining quality.**

Source: Gartner Consulting; 2001



Selecting the Right Categories Starts the Process

With mission resolved and understanding of the purpose and opportunity clear, the next step is for the company sponsoring SRM (often a large, branded nucleus firm) to group its purchases by category of importance and complexity. This step contains the implicit requirement for the firm to know all about its buy. How much of what is being bought, from whom, by which purchasing agent, at what prices, and with what results must be a part of the ante. SRM can only begin when the firm thoroughly knows its buy and has done the standardization necessary to make certain the categories of buy represent what they should contain. That means there cannot be a misunderstanding as to in which category motors or pumps belong, or confusion about whether a particular supplier is providing something that looks like a motor or pump. Standard nomenclature must be in place and the purchases made part of a specific category in the total buy.

Exhibit 2 – Purchase Categories

| | | |
|-------------|---|---|
| High | <p>Commodities</p> <ul style="list-style-type: none"> • Availability is critical • Significant leverage to influence costs • Purchase costs are high relative to administrative ones | <p>High Impact</p> <ul style="list-style-type: none"> • Availability, quality and reliability are critical • Category knowledge is essential • Purchase cost is high relative to administrative costs |
| | <p>Odds and Ends</p> <ul style="list-style-type: none"> • Mature industry products • Suppliers are differentiated by price and service • Administrative costs are high relative to purchase costs | <p>Commodities</p> <ul style="list-style-type: none"> • New industry • Unplanned usage • Supplier capabilities are important • Administrative costs are high relative to purchase costs |
| Low | Low High | |

With these requirements in mind, the firm proceeds with its SRM effort by carefully separating the buy categories into some meaningful segmentation so sourcing and pricing plans can be attached to each group. A four-segment approach is illustrated in Exhibit 2. Note that the scales vary. On the vertical axis of the matrix, the ranking moves from low spend volumes and low purchasing leverage to high positions. On the horizontal axis, the variation is from low to high product and service complexity.

Beginning on the lower left side of the matrix, with the low volumes and low complexity categories quadrant dubbed “Odds and Ends,” the procurement objectives become something like:

- Ensure getting the best price and service for volume tendered
- Provide users self-service capabilities, minimizing contact time with suppliers
- Reduce administrative costs through streamlining and e-procurement techniques, where appropriate

Moving up to the area of high volume and leverage and still low complexity, we find the “Commodities” quadrant where the objectives become:

- Leverage buying power to seek the best consolidated arrangement
- Rationalize SKUs to industry standards
- Manage contracts closely to obtain negotiated benefits

In the lower right hand side, where we have high complexity and low volumes, the “Specialty” quadrant calls for these objectives:

- Gain access to cost and technology information from key suppliers
- Enable suppliers to provide value-adding features and services to internal customers
- Reduce administrative costs through improved online RFQ procedures

Finally, in the upper right, we see high product and service complexity matched with high spend volume and leverage and the category marked “High Impact”. Now the objectives become:

- Leverage buying power with limited suppliers
- Understand industry cost drivers, emerging technologies, and full capabilities of key suppliers
- Encourage supplier involvement in product development and the search for added features and values
- Involve most critical suppliers in strategy planning and customer satisfaction initiatives



A firm may care to add to the decision criteria, based on its internal needs, but it is in this last quadrant that the search for SRM candidates centers. If an effort is going to be made to find advanced relationships, where the company will share very important information, it should be with suppliers in this category. What comes out of the eventual SRM effort will establish a framework and decision rules for dealing with the other categories, but partner selection should start with the high-impact quadrant.

Selecting the Right Suppliers is Crucial to Success

With a good fix on where the action should begin, the next element in the SRM sequence is to decide on a selection criterion that makes sense to the firm, its internal partners, and the few companies selected for a collaborative effort. That means the firm needs to apply a format for picking the names of the most likely candidates for SRM activities, such as that represented in Exhibit 3.

Exhibit 3 – Supplier Relationship Attribute Model

| Supplier Category/Focus | Basic | Value Added | Preferred | Strategic |
|-------------------------|--|------------------------------------|---|--|
| Relationship | Product or service as commodity | Impacts operational efficiency | Process expertise valued | Unique advantage is valued |
| Operation Mode | Competitive bid | Performance incentive | Continuous improvement | Flexible, agile, collaborative |
| Capability | Fulfill to requirements | Deploy specific competencies | Customized expertise & skills | Ability to assist with market changes/demands |
| Information sharing | Limited – electronic | Limited – tactical | 2-way controlled dialogue | Direct linkage access to parts of company database |
| Risk Management | Contract penalties | Incentives and penalties | Incentives and information linkages | Process management, shared risk/reward |
| Planning horizon | Current deal | Ongoing, near-term | Joint planning with end point | No end point, joint strategic planning |
| Nature of trust | Confident in ability to fulfill contract | Confident of execution performance | Confident in expertise; performance agility | Shared vision, ownership of intellectual capital |
| Metrics | Compliance tracking | Service level benchmarking | Best practice relationship | Business results; shared incentives |
| Customer Interaction | None to limited | Enabler of quality | Impacts individual customers | Impacts major number of customers |

This matrix can be modified or extended to cover other characteristics that a firm believes will help segment its supply base. The idea is to move from the “basic” suppliers that a firm needs to get its work accomplished to those offering more



“value,” those adding “special values”, and those that have “strategic importance.” Most firms can make this analysis intuitively, but the matrix approach helps establish the criteria for selection and enables the firm to cope with a large number of suppliers. The focus with this technique changes in each of these categories, and again should reflect the distinctions the firm wants to bring to each segment.

Overall, the matrix should describe how a supplier moves through positions and provide a framework for selecting the key strategic suppliers with which it wants to embark on an SRM effort. Working with one major manufacturer of hand tools, we began with 3,500 suppliers. This group was reduced to 1,500 with 1,000 falling into the basic category, 250 into the value category, 150 into the preferred category and 100 emerging as strategic suppliers. The last group becomes a manageable number from which two or three are selected after matching their capabilities with the high-impact categories to begin an SRM effort.

This step in the SRM sequence requires some cross-referencing between the lists of high-impact buy categories and the strategic suppliers. The intention is to find the small number of critical items and the small number of strategic suppliers where an advanced relationship effort will be most rewarding. That requires the firm to develop a complementary evaluation sheet that culls through the previous lists. A cross-functional team, which includes members from operations, finance, IT and logistics, in addition to purchasing and sourcing, should come together and set up decision rules around how a supplier fits into selection criteria and attains suitability to help with SRM. The team wants to make certain the selected suppliers have characteristics that relate to achieving the business strategies as well as the ability to partner in the SRM process. We suggest a simple matrix similar to that shown in exhibit 4.

Exhibit 4 – Supplier Relationship Matrix

| | | | |
|--|------|--------|-----|
| Strategic importance | High | Medium | Low |
| Ability to collaborate electronically | High | Medium | Low |
| Ability to provide resources for actions | High | Medium | Low |
| Quality of past relationships | High | Medium | Low |
| Ability to add network value | High | Medium | Low |
| Alignment of business thinking | High | Medium | Low |
| Share the same values | High | Medium | Low |
| Length of relationship | High | Medium | Low |

Once again, the matrix can be modified, but it must reflect the factors of importance to the firm, as so much will be at stake as the effort goes forward. There will be a significant commitment to time and resources and a lot of eyes will be on the progress made. Therefore, the team should take the time to make certain the first

two or three firms selected for what will become the initial SRM pilots have the highest probability of being successful.

When the names have been generated and reviewed with a cross section of senior management, a letter from the CEO inviting the selected firms to participate is prepared. This letter should include a statement outlining the opportunity to discuss the proposed vision or mission to guide the effort, the type of processing that will occur, a commitment to pursue joint benefits while using joint resources, and the preliminary list of areas of opportunity for both parties. The responding firm should also be allowed to suggest improvement ideas from its perspective.

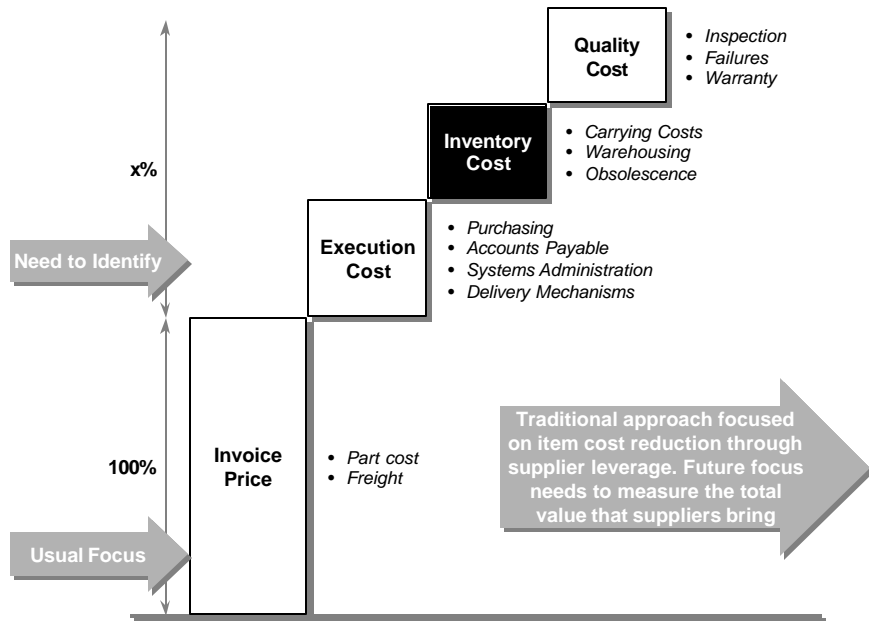
Identifying the Total Cost of Ownership Becomes a Primary Objective

When an agreement to participate is received from the invited supplier, the sponsoring firm’s team sets up the logistics. The time and place for the preliminary meetings are arranged. An agenda that will kick off the joint discussions is prepared and the specific attendees determined. Process maps, explaining how each firm believes the processing takes place between the partners, are prepared and brought to the initial meetings. This step is a crucial preliminary action. Most firms come to the first meeting with a decidedly different perception of how the products and services, information, and financial flows take place between the two companies. With flow charts showing each perception, the group has a means to get quickly into what are the actual conditions so they can then begin collaborating on a redesigned improved state.

It is equally important in these initial meetings to have a cross section of functions in the meeting room. In addition to buyers and sellers, there should be representatives from logistics, IT, operations, finance, planning, engineering (where appropriate), and so forth. The idea is to give exposure to the functions that can benefit from an improved relationship the chance to discuss, first hand with key suppliers, what these improvements might be and how they would impact each organization.



Exhibit 5 – Total Cost of Ownership Model



moved upstream and onto the books of the suppliers. The new thinking is to match demand with supply and have a flow that covers demand without excess safety stocks.

The highest block is called quality costs and represents the costs of inspection, failures and warranty. Now the partners want to look at making certain there are no hidden costs in assuring the right goods at the right time and place do not have to be returned or discarded. There is generally plenty of historical information to identify these costs, but they lay buried in databases and must be rooted out and assembled in a meaningful manner, so the inventories can be reduced or eliminated, often through joint action team initiatives. As the partners unearth this information and begin using it, the supplier should be given a chance to add any elements to the total cost of ownership, which it believes are also of importance.

Referring to Exhibit 5, we can see a model that will help initiate the preliminary conversations with the selected suppliers – the total cost of ownership. The usual focus with any buy-sell share session is placed on the invoice price and how it can be improved. Freight is separated from the part or supply cost so a focus can be placed on both of these elements. In SRM, the focus moves higher to measure the total value that suppliers provide. Above the usual base line, we find a category marked “execution costs.” Here attention is brought to the costs associated with making the purchases, handling the accounts payable, systems administration, and the delivery mechanisms.

Moving even higher on the chart, we encounter the inventory cost, a most elusive supply chain cost. The elements are clear enough - they contain the value of the inventory as it resides in working capital on the balance sheet, the carrying cost of holding the inventory, the warehousing costs and the cost of any obsolescence. This is a very serious part of the effort as the joint intention must be to reduce the amount of network inventory needed, through visibility and just-in-time delivery techniques, without jeopardizing manufacturing plans. Traditionally, inventories are simply



Exhibit 6 – Uncovering the Hidden Costs of Procurement

| | Acquisition | Reception | Possession | Utilization | Elimination |
|-----------------------|--|--|--|--|---|
| Supplier Level | Cash | | | | |
| | /// Total purchase discounts | | | | |
| | Non-Cash | | | | |
| | /// Supplier vetting costs /// RFP costs /// Contract administration costs /// Supplier follow-up costs (feedback) /// Supplier change costs | /// Litigation costs for breach of contract | | /// Engineering costs /// Personnel training costs /// System adaptation costs | |
| | | | | | |
| Order Level | Cash | | | | |
| | /// Payment-delay savings or costs | /// External transportation costs | | | |
| | Non-Cash | | | | |
| | /// Ordering costs | /// Receiving costs /// Invoice and payment processing costs /// Quantity testing costs /// Quality testing costs /// Litigation costs for problems with quality | /// Internal transportation costs | /// Quality control costs /// Production delay costs | /// Waste collection |
| Unit Level | Cash | | | | |
| | /// Price /// Production discounts | | | /// Intrinsic efficiency /// Replacement costs | /// Recycling costs of revenues /// Disposal fees or revenues |
| | Non-Cash | | | | |
| | /// Service costs for installation and assembly /// Testing costs | | /// Inventory holding costs /// Order picking costs | /// Production failure costs /// Product failure costs /// Maintenance costs /// Installation costs | /// Costs of removing obsolete materials /// Disposal management costs |



As the team looks at this total cost of ownership from the latter perspective, there is another format that will prove helpful, supplied by Zeger Degraeve and Filip Roodhooft in their Harvard Business Review article. These authors point out that a systematic exploration of all costs involved in the relationships with suppliers will help the firm “make intelligent decisions about trade-offs using mathematical optimization models.” (Degraeve: 2001, p. 22) They offer the framework illustrated in Exhibit 6 as a means for the team to identify opportunity areas by focusing across various levels – unit, order, and supplier – and across activities – acquisition, reception, possession, utilization, and elimination. In the appropriate sectors, they call attention to costs that can be investigated to see if they can be improved.

Exhibit 7 – A Total Value Weighting Process

| Weight | Element | Measurement | Weight |
|--------|-------------|--------------------------------------|--------|
| 25% | Quality | /// Quality Performance | 30% |
| | | /// Receiving Inspection | 20% |
| | | /// Line Performance | 20% |
| | | /// Reliability Performance | 20% |
| | | /// Field Retrofits Required | 10% |
| 25% | Delivery | /// On-Time Committed Receipt Date | 30% |
| | | /// On-Time Requested Receipt Date | 10% |
| | | /// Standard Interval Performance | 30% |
| | | /// Delivery Error Performance | 20% |
| | | /// Flexibility and Lead Time | 10% |
| 25% | Technology | /// Access to Obsolete Technology | 15% |
| | | /// Process Technology | 25% |
| | | /// Early Design Involvement | 20% |
| | | /// Long-Range Plans | 20% |
| | | /// Technology Roadmap Match | 20% |
| 15% | Service | /// Purchasing/Materials Support | 60% |
| | | /// EDI Capability Support | 20% |
| | | /// Leading-Edge Procurement Support | 20% |
| 10% | Environment | /// Environment Policy | 30% |
| | | /// Regulatory Compliance | 50% |
| | | /// Conservation Program | 20% |

As the total cost of ownership becomes clear, the firm will also want to establish a system to assign weights to the elements pinpointed for improvement. This step involves identifying the improvement areas and weighing the importance of each area. Next, the team identifies what data will be used to measure the improvements accomplished and how this data will be obtained. Then they focus on how the data will be used, obtaining the supplier commitment to help, and making supplier responsibilities part of the SRM effort. Exhibit 7 outlines a typical weighting process.

Formal Steps Extend the SRM Activity

With the potential value improvement opportunities identified and the selected suppliers committing to provide resources for the selected SRM activities, joint teams are now dispatched to review the opportunities in a formal manner. The opportunity list should be divided so teams can be assembled with the expertise to tackle each major area. These sub-team meetings are arranged and comprehensive review formats established to monitor progress. Executive reviews should be overlaid on these meetings so participants can recap past achievements, report on progress status, and identify new opportunities discovered in the team interactions. These reviews should be structured to be as comprehensive as possible and to achieve a consistent and total category and supplier evaluation. Exhibit 8 depicts an example form that could be used so the opportunities are classified and progress rated versus the initial plans developed and the projected completion dates.



Exhibit 8 – Supplier Relationship Management Review Example

Category: _____ **Period** _____ **Purchases** _____
 (\$M): _____

Review _____ **Year-to-Date** _____ **Purchases** _____
Period: _____ **(\$M):** _____

Key Organ. _____ **Total Year Forecast** _____
Contact: _____ **(\$M):** _____

Phone/Fax #s _____ **Prior Year** _____
 (\$M) _____

Key “Supplier” _____ **Phone/Fax #s** _____
Contact _____

Organ. Site(s) Represented

Review of Previously Identified Key Action Items

| Action Item | Current Status | Remaining Required | Action |
|-------------|----------------|--------------------|--------|
| _____ | _____ | _____ | _____ |
| _____ | _____ | _____ | _____ |
| _____ | _____ | _____ | _____ |

Quality Performance (25 Possible Score: _____ Points)

| |
|-------------------------------|
| Accomplishments |
| _____ _____ _____ |
| Issues |
| _____ _____ _____ |
| Actions |
| _____ _____ _____ |
| Total SRM Score: _____ |

A Behaviors Model to Guide Joint Actions Establishes Agreement

As the teams progress with their research to discover the hidden opportunities in their firms’ relationships, evaluations and recommendations will emerge and a pattern will develop describing the enhanced relationship. For the product flow, new logistics systems will be found that take advantage of joint assets – warehouse space, distribution facilities, and trucks. Substitute materials will be recommended or the supply of larger sub-assemblies. Features of supply that enhance the machine set-up times and quality, the changeover process between orders, and manufacturing run capabilities will be discovered. The information flow will show new ways to bring visibility to the critical information – to better match actual demand with supply capacity and reduce the need for safety stocks. Algorithms and software will be selected to greatly improve the accuracy of forecasts and match demand planning with supply capacity. Cycle times will also shrink as non-value-adding steps are eliminated. In the financial flow, schemes will be introduced to speed payments and eliminate any errors and reconciliation. In short, the results of SRM show the teams generally come back with a laundry list of surprising means to add benefits for both firms.

From an IT perspective, some of the typical traits that come from SRM efforts and help drive success include:

- Joint capability to resolve issues around disparate information systems and use an open Internet-based architecture for communication of vital data
- Agreement on translation engines that permit information sharing between heterogeneous systems and applications
- Online visibility of product, information and financial flows across the full supply chain
- Ability to provide online collaborative support in the search for continuous improvement with further process steps across the supply chain



In some of the more advanced SRM efforts, the results from the effort with the selected supplier participants will lead to a larger understanding and set of decision rules, which can be applied by the sponsoring firm across its supply base. A “Behaviors Model” appears that summarizes the new actions and benefits while describing the intended rewards for both organizations. Exhibit 9 is an abbreviated version of such a model that has been extended to list the behaviors, not just for the strategic suppliers, but each of the previous categories listed in earlier matrices.



Exhibit 9 – SRM Behaviors Model

| | Rewards/ Value | Basic | Value-Added | Preferred | Strategic |
|---------------------------|-------------------|---|--|--|---|
| Value and Compensation | Supplier | <ul style="list-style-type: none"> ///Supplier provides exactly to the contract agreement ///Agreements are short-term transactions | <ul style="list-style-type: none"> ///Offer improvement suggestions ///Provide no special expertise; electronic purchasing | <ul style="list-style-type: none"> ///Commit to cost improvements ///E-Procurement ///Non-traditional pricing | <ul style="list-style-type: none"> ///Value added through expertise ///Metrics-based agreement |
| | Buyer | <ul style="list-style-type: none"> ///Paid according to agreement and conditions ///Short-term transactions | <ul style="list-style-type: none"> ///Negotiate early payment options ///Process orders electronically | <ul style="list-style-type: none"> ///Direct entry of invoices ///2- to 5-year contracts for multiple transactions | <ul style="list-style-type: none"> ///Bonus incentives ///Open-ended contracts |
| Pricing/Volume | Supplier | <ul style="list-style-type: none"> ///Commit to competitive pricing ///Supply not guaranteed | <ul style="list-style-type: none"> ///Contract with fixed term and option to extend ///Audit rights to buyer | <ul style="list-style-type: none"> ///Multi-year options with price guarantees ///Audit rights to buyer | <ul style="list-style-type: none"> ///Most favored customer commitment ///Supplier shares pricing model to establish profit margin |
| | Buyer | <ul style="list-style-type: none"> ///Commits to volume spend ///Uses competitive bid for awards | <ul style="list-style-type: none"> ///Awards business as back up to preferred supplier ///Alternate sources may be tested | <ul style="list-style-type: none"> ///RFP not required ///Always in bid process ///Evergreen contract | <ul style="list-style-type: none"> ///Allows fair margins ///Collaborates on requirements ///Offers right of first refusal |
| Risk Sharing | Supplier | <ul style="list-style-type: none"> ///Accepts minimal risk based on contract | <ul style="list-style-type: none"> ///Accept modest risk with allowed incentives and penalties | <ul style="list-style-type: none"> ///Accept moderate risk with allowed significant incentives | <ul style="list-style-type: none"> ///Compensation tied to buying firm's successes; makes joint investments |
| | Buyer | <ul style="list-style-type: none"> ///Accepts minimal risk based on contract | <ul style="list-style-type: none"> ///Accepts modest risk with incentives and penalties | <ul style="list-style-type: none"> ///Accepts moderate risk balanced with incentives for enhancements | <ul style="list-style-type: none"> ///Shares documented successes; makes joint investments |
| Information Sharing | Supplier | <ul style="list-style-type: none"> ///Shares data as defined by contract | <ul style="list-style-type: none"> ///Shares limited tactical data to better enable completed tasks | <ul style="list-style-type: none"> ///Shares product strategy and best business process practices | <ul style="list-style-type: none"> ///Shares business strategy and direction; facilitates sharing of improvement ideas |
| | Buyer | <ul style="list-style-type: none"> ///Shares data defined by contract | <ul style="list-style-type: none"> ///Shares operational data to help planning | <ul style="list-style-type: none"> ///Significant tactical data and some strategy to aid supplier | <ul style="list-style-type: none"> ///Allows supplier to participate in strategy development and add value servicing |



Buying Engines can be Applied to Facilitate Lower Purchase Categories

As the firm builds its SRM relationships, it will find here are some ancillary benefits. When most firms progress with internal supply chain improvement, they invariably begin to consider e-procurement systems to simplify, control and automate the purchase of goods and services from multiple sources. Software offerings are considered and used to aggregate needs, choose sources, and reduce the transaction time and cost. Marketplaces and auctions are employed to find opportunistic savings. Buying portals are set up for sharing requests-for-quotations and facilitate the bidding process with selected suppliers. Order placement, tracking and payment can be handled with such portals. Many companies are now extending these cyber-based techniques from what was initially an attempt to reduce indirect costs to more direct buying categories.

When the SRM effort is underway with a few strategic suppliers, the sponsoring firm can take a step back and apply the information developed during the selection and action processes to help its buyers with the lower echelon buy categories from the lower segmented suppliers by taking advantage of these e-commerce techniques. As the firm looks at its “odds and ends” and “commodities” categories, for example, and how they are sourced from “basic” suppliers, an automated mechanism could make good sense. The question becomes how do we choose from among the many options available?

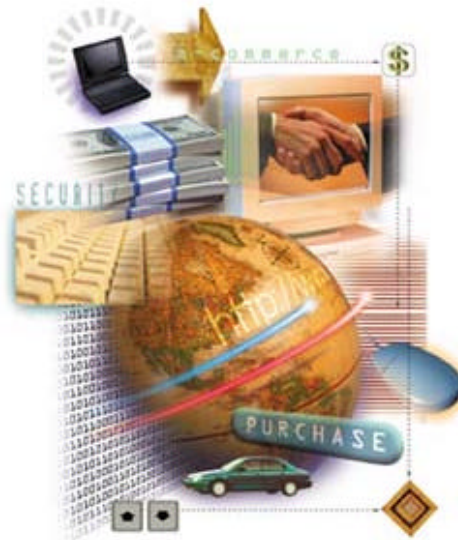
One answer lies in the application of a software comparison grid. That means the firm lists the various software providers it is considering and develops a grid that shows the strategic focus of the offering, the maturity state of that offering, the positive and negative aspects of using the offering, and information on any installations in a similar industry that might be available for each company. The idea is to have the spending categories drive the assisting technology choices and apply a spend/supply analysis for prioritizing how the sourcing tools are selected and applied.

There is one complication. There are so many buying engines and software solutions being offered, it is often difficult to match the appropriate software with the appropriate category. In fact, the landscape has become almost littered with choices and, as much as we would like to offer help and advice, it is somewhat risky to list the current conditions as acquisitions and mergers are changing the landscape. A recent listing of principal vendors, including those performing auction services,

would contain: Agile, Ariba, Clarus, Commerce One, Diligent, Emptoris, Freemarkets, Healy Hudson, iPlanet, i2Technologies, MindFlow, MRO Software, Oracle, PeopleSoft, Peregrine Systems, PurchasePro, SAP, and Verticalnet. The recommendation is that these sources, or the shorter list of viable candidates selected by the buying firm, be placed on the comparison grid and the buyers match the capabilities of the various suppliers with the needs of the lower position categories in view of the engines capability to automate and improve some or most of those categories.

While there is no definitive data available to determine exactly how much of the total buy these software engines have absorbed, reasonable estimates place e-procurement at about 15 percent. So, for most firms employing such techniques, it has become a significant part of the buying process. Such electronic buying has significantly progressed beyond the use of auctions and now includes an entire field of e-sourcing tools: spend analysis and planning, sourcing directories, direct materials sourcing, RFQ workflow, collaboration, bidding events, bidding analysis, negotiation, contract development/management, trading exchanges, and supplier performance management.

In short, there are a plethora of offerings and the firm is well advised to sort out those options against the needs of the categories for which they will be applied. According to experts at *Information Week*, the “key goal is to find the best deal, the right products, sufficient product availability, and acceptable prices.” “Businesses need, moreover,” they explain, “to evaluate not only prices, but also attributes such as supplier responsiveness, service levels, delivery history, and customer satisfaction ratings.” (Foust: 2002, p 1) These authors present a very good analysis of some major e-procurement suppliers that could be very useful as a firm builds its comparison grid. (Foust: 2002, pp 4 – 6) Similar information is available through Boston-based AMR Research.





Improvements Can Be Significant

Results from SRM efforts and the fall-off events that aid lower echelon buying systems will vary by firms, partners selected, industry and market conditions. Case studies are limited as the technique is new and still evolving. An example, however, points out the potential. One firm studied purchased 22,000 products from thousands of suppliers. Following a strategy that began with SRM efforts with the more limited group of strategic suppliers, and extended to “webifying” the lower buy categories through the application of some form of e-procurement, the firm documented the following improvements:

- Inventory turns went from 11 to 24
- Procurement costs improved by 17 percent
- Purchase order cycle time was reduced by 50 percent
- Automation of purchase orders went to 70 % of the total
- Inventories identified as “excess” were eliminated
- Suppliers rated the effort as good to excellent, particularly in view of the shared savings

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About the Author

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