Why Supplier Management should be central to your procurement thinking

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Executive Summary

This briefing paper looks at ‘supplier management’ and explains both why the topic should be of central importance to procurement and supply chain executives, and also why this is not always the case. Procurement has gone through a number of changes of focus over the years, and the time may be right for the supplier to become the centre of procurement thinking, strategy and operations. There are very good reasons why that should be the case; not least that suppliers now account for a much higher proportion of the cost base for Upstream organizations compared to internal staff costs.

The paper then provides a definition of supplier management, and runs through the different elements that sit within it, including risk and performance management. That is put in the context of supplier lifecycle management, which seeks to look at the end to end process of managing suppliers in a structured and holistic manner.

We then suggest some of the factors that may be holding supplier management back, including the historical development of technology, which has focused on two views of the procurement task; the transactional (P2P) process and the category management / strategic sourcing process. Much procurement related technology is still designed, quite understandably, around those two core processes.

However, the paper concludes by suggesting that executives can still benefit from a more joined up and considered approach to supplier management. Even if a single, ubiquitous technology solution is unlikely in the foreseeable future, tools that address different elements of supplier management can be integrated to work together or in parallel. And effective supplier management also requires a mind shift; realizing that suppliers are vital to our organisations’ success and treating them appropriately is something that can be developed within organisations, quite independently to the technology used.
Introduction – how the procurement focus has changed

Procurement and supply chain professionals work with suppliers every day of their working lives in some sense, and yet in our view ‘supplier management’ is not as well understood as it should be by organisations and those professionals. Indeed, put ten procurement executives in a room and you will probably get ten definitions of what supplier management means!

We will come onto our attempt to clarify that definitional issue later, but it is worth first of all giving a historical overview to set the context. There is no doubt that the profession and the activities known as “procurement” have seen a number of changes in emphasis over the years.

The first procurement was probably mainly concerned with the basic supply of materials to keep the institution running successfully, or to construct physical entities – Samuel Pepys, the famous 16th century English diarist, was involved in buying both provisions for the English Navy’s operations and the construction of new ships, for example. As construction and manufacturing developed through and post industrial revolution, supplying those growing businesses became a key function - the Chicago and Northwestern Railroad’s comptroller wrote the first book exclusively about the purchasing function, *The Handling of Railway Supplies—Their Purchase and Disposition*, in 1887.

From the 1920s, the codification and growth of bureaucracy as a method of running organisations, as defined by German sociologist Max Weber, grew rapidly and the whole idea of recording and accounting for goods and services used by the organisation became more central to the procurement task. The beginnings of spend analytics can be traced back to this period.
During the early part of the 20th century, the legal contract also became more important as a focus for procurement, as the historical handshake gave way to more formal means of recording the agreement, and the legal profession and law firms grew dramatically. Then, in the 1970s and 80s, the emergence and exponential growth of computerisation led to a much stronger focus on the procurement process. We started seeing terms such as P2P (purchase to pay) and ERP (enterprise resource planning) in regular use.

Around 20 years ago, a new idea hit the procurement world and took off rapidly. Category management brought a rigorous and ‘scientific’ approach to procurement, leading to benefits for early adopters and a professionalizing of the procurement role. Organizations categorised their spending and allocated resources who would become expert in different areas; perhaps one procurement manager for software, one for a specific type of drilling equipment or service, one for transportation and so on.

Should we now be looking ahead to another change of focus? That may well be the case, and this paper will explore whether the stage is set for supplier management to move towards the heart of procurement focus, thinking and management. But a note of caution. Whilst we are clear that supplier management deserves a higher profile, it is by no means a given that it will quickly become the dominant methodology in procurement, for reasons we get into later. However, it is assuming greater importance and this trend will, we believe, continue to develop.

**Why procurement should focus on supplier management**

Suppliers sit at the heart of almost every organization’s activities and processes. As an objective illustration of that, the report published in 2013 by outsourcing firm Proxima was significant. They commissioned analysis that ended up as the report, “Corporate Virtualization - A global study of cost externalization and its implications on profitability”.

The research analyzed financial data for 1,954 organizations for the financial years 2009, 2010 and 2011. On average, 69.9% of those firms' revenues were spent with suppliers, against only 12.5% on staff costs. The oil and gas industry had the third highest proportion of spend with suppliers at 76.7% in 2011, behind only Retail and Automotive of the sixteen sectors Proxima considered. And the labor cost in the sector was the lowest of all, at just 4.8%.

That may not come as a surprise to those in the industry. Suppliers, supply chains (a linear arrangement of organizations) and supply networks (more complex structures)
are vital in the whole sector, which has developed an operating model that relies on large-scale outsourcing, sub-contracting and therefore the efforts of suppliers.

And of course it is far more than just the monetary spend with suppliers that is significant. The risk factors are arguably even more significant in many sectors. Supplier-related incidents or performance can have a huge impact on the customer firm's risk profile in industries such as oil and gas. That risk may be commercial, in terms of unforeseen cost implications, operational, like interruption of business, or reputational – or in the worst case, all three.

In terms of the positive side of supplier contribution, there are a number of angles too. Suppliers can play a central role in driving revenues (top-line) as well as being critical to the bottom line. For instance, putting together the best supply chain can support firms in winning tenders themselves, or being granted exploration rights in a competitive situation in an energy or mining industry context. Suppliers can provide innovation, ideas and access to new markets and technology and increased capabilities.

All these factors suggest that suppliers should sit right at the heart of procurement thinking and action. And yet suppliers are often not treated with the recognition they as a whole deserve given this critical importance. How much time do Boards and top management dedicate to considering supply and supplier related matters, as opposed to staff or sales related? Yet we have seen that 77% plays 5% comparison in the Proxima report.

So, assuming that senior procurement and supply chain executives understand the role of suppliers, then driving that appreciation with senior colleagues is a key task for those leaders within their organizations. Our first key proposition from this paper is this.

For almost every organization, the importance of suppliers means that supplier management needs to sit at the heart of procurement and supply chain strategic thinking and operational management.

Defining supplier management

When it comes to turning that desire into real actions however, matters get somewhat more complex. In our experience, every senior procurement or supply chain executive has a slightly different view of what exactly ‘supplier management’ means, which has not helped to establish an unambiguous understanding of the topic. Such understanding and useful debate is difficult without a clear, shared and accepted definition.
Thomas Kase, VP of Research at procurement analysts Spend Matters, defined it thus:

“... supplier management includes not only measuring and managing supplier relationships and performance/compliance after a contract is signed, but also managing various pre-commercial interactions such as supplier registration, supplier identification/qualification during a sourcing process, multi-dimensional supplier segmentation, and selected supplier risk management processes”.

Terms such as 'supplier relationship management' (SRM) have confused matters further, as a high profile subset of the wider supplier management picture. That process can be defined as **strategically managing the organization’s most important suppliers to generate added value beyond just contract delivery.** But the picture got more muddied some years back when SAP, the software giant, christened their procurement suite 'SRM'. (At the earliest presentations of what was then a new product, the procurement audience was confused to see a largely transactional, purchase to pay offering, and not at all relevant to what most in the room and the industry considered to be 'SRM')!

To come back to the definition and scope of supplier management, it can be considered as the totality of these five key sub-processes, as follows:

**Onboarding, vendor master data and record keeping**

The relationship with the supplier generally starts when they either start doing business with the organisation, or express a desire to do so, perhaps by applying to be on an approved supplier list or expressing interest in a particular competitive process like a tender. At this point, relevant information about the supplier needs to be obtained– a process generally known as onboarding.

Basic factual information will be obtained about the supplier that enables us to trade with them (bank details), and also potentially other general information (number of locations), capability (key service or product areas covered), regulatory (certificates or permissions to carry out particular work), or capacity (number of qualified staff). This starts to form the vendor master data record – which also plays into more strategic supplier management activities, such as spend analytics. If basic vendor master data is not collected or is incorrect or misleading, consequences can be felt further through the process.
Supplier qualification, verification and selection

Supplier information clearly forms part of the process of selecting suppliers for particular work. Verification of information provided should be considered on a risk-driven basis. If the supplier or the work they are going to do is particularly high-risk, then some verification process that goes beyond simply taking the supplier’s word may need to be considered. And of course supplier information is not static. It needs to be updated when appropriate, and that is something often better done by the supplier themselves.

Supplier performance management

Once a supplier is active, there is a need to track and measure supplier performance against the contract and perhaps in terms of wider requirements. That is essential to ensure suppliers meet immediate needs and to enable performance and value improvement activities to be pursued through the course of the contractual relationship. That requires the right data of course – which must be relevant and usable.

Supplier and supply chain risk / compliance management

It could be argued that consideration of risk should run through the entire procurement process, and it is certainly central to supplier management thinking. As well as the more operational risks around supplier stability, supply interruption and so on, supplier information and management is now often related to corporate social responsibility in its widest sense. This has grown in importance greatly in recent years, and the scope of what is often needed in terms of data and information can now be extensive – see Table 1 for just some of the areas of interest for many buyers.

<table>
<thead>
<tr>
<th>Environmental</th>
<th>Social</th>
</tr>
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<tbody>
<tr>
<td>• Emissions (CO2)</td>
<td>• Labour practices</td>
</tr>
<tr>
<td>• Waste management</td>
<td>• Local employment &amp; capacity building</td>
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<tr>
<td>• Sustainable materials (e.g. hardwoods)</td>
<td>• Health and safety</td>
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<td>• Energy and water usage</td>
<td>• Conflict minerals / metals</td>
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<table>
<thead>
<tr>
<th>Quality &amp; consumer</th>
<th>Regulatory</th>
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</thead>
<tbody>
<tr>
<td>• Product failures / recalls</td>
<td>• Compliance to Government regulations and policies</td>
</tr>
<tr>
<td>• Supply chain traceability</td>
<td>• Government watch lists</td>
</tr>
<tr>
<td>• Safety and quality standards</td>
<td>• Tax issues</td>
</tr>
</tbody>
</table>

Table 1: Supplier Management - corporate social responsibility takes centre stage
Supplier relationship management and collaboration

Where a supplier holds multiple contracts with the organisation, there is a need to understand what they are doing across the entirety of the organisation – and see how they fit into the wider category, business unit or geographical landscape. And where the supplier justifies a strategic ‘supplier relationship management’ (or similar) approach, that needs to be structured and managed, with further implications for communication, activities and information management.

This categorisation is of course just one way of looking at the supplier management picture. In terms of the looking at the supplier management solutions market, Spend Matters US analysts Jason Busch and Pierre Mitchell have come up with four functional/vendor categories, describing the type of solutions available:

<table>
<thead>
<tr>
<th>Market Segment</th>
<th>Components</th>
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</thead>
<tbody>
<tr>
<td>Stand Alone “Content Focused” Solutions</td>
<td>• Financial/operational monitoring</td>
</tr>
<tr>
<td></td>
<td>• CSR, diversity, risk, health and safety</td>
</tr>
<tr>
<td></td>
<td>• Planning and remediation</td>
</tr>
<tr>
<td>Supplier Information Management Platform</td>
<td>• Process automation &amp; workflows</td>
</tr>
<tr>
<td></td>
<td>• Compliance (e.g., insurance/quality certification mgmt.)</td>
</tr>
<tr>
<td></td>
<td>• Enrichment (including risk data)</td>
</tr>
<tr>
<td>Supplier performance management</td>
<td>• Supplier auditing</td>
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<tr>
<td></td>
<td>• Supplier performance evaluation</td>
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<tr>
<td></td>
<td>• Performance monitoring</td>
</tr>
<tr>
<td></td>
<td>• Supplier development</td>
</tr>
<tr>
<td>Spend Visibility Solutions</td>
<td>• Cleansing, classification</td>
</tr>
<tr>
<td></td>
<td>• Enrichment (including new data)</td>
</tr>
<tr>
<td></td>
<td>• Analytics to slice and dice</td>
</tr>
<tr>
<td></td>
<td>• Dash-boarding/visualization</td>
</tr>
</tbody>
</table>

Table 2: Segmenting supplier management solutions
A Supplier Lifecycle approach

So it is clear that supplier management includes a number of diverse elements, adding complexity to the whole topic. But how might practitioners take a more holistic approach to the subject? If the supplier really is so vital to organizational success, how might we put the supplier at the centre not just of our thinking but of our processes and systems?

That takes us into the Supplier Lifecycle Management approach, which has gained adherents over the last few years. Instead of looking at what could be defined as the 'traditional' procurement processes (category management / strategic sourcing being one, and the transactional purchase to pay cycle the other), we can look at a Supplier Lifecycle process as an alternative world-view. Fig. 2 shows a representation of a supplier-centric view of the end to end procurement process; many of the steps were discussed in the last section.

The supplier lifecycle based view of the world starts with identifying, qualifying and evaluating suppliers. Risk aspects may well be considered for the first time at this stage, with checks on the supplier, and the potential for more detailed data capture. However, arguably risk does not fit neatly into the cycle visualization; it is really something that needs to be considered throughout the entire supplier management cycle.

Supplier onboarding, as described earlier, can be carried out before or after the selection and contracting process, and there are pros and cons for each option. We may want to obtain onboarding information in order to support the supplier selection process itself, helping to decide whether we should choose this supplier. Or (and this is what often happens in practice), a certain amount of information is gathered to feed into the supplier selection process, then a full, detailed onboarding process takes place if and when the buyer decides to start trading with the supplier.

Once we move into the delivery phase of contracts, performance management is likely to be central to our efforts; ensuring that the supplier delivers what we require, measuring performance, and the continuous process of risk management of course. The cycle then shows development and relationship management, which can range from simple contractual change and variation management through to strategic relationship programs and the like.

Finally, the lifecycle shows spend analysis and potential supplier rationalization – which feeds back into the start of the process, as suppliers are re-qualified and perhaps evaluated for further contracts and business.
This is certainly a somewhat different way of looking at procurement process compared to traditional purchase to pay or category management cycles. And whilst we would not suggest for a moment disregarding those processes, considering activities on a supplier management lifecycle basis is a good discipline. It can certainly be a powerful way to identify strengths and weaknesses in the way suppliers are managed within an organization.

**Why supplier management doesn’t always get the focus it deserves**

Despite what seems like the compelling logic we have outlined for putting supplier management at the heart of procurement efforts, it certainly does not happen in many organisations. Why is that?

One major stumbling block, in our opinion, is that the two ‘standard’ procurement cycles, transactional (P2P) and sourcing, don’t align with the broader supplier management perspective. Not only do most procurement functions look at these processes quite separately, but the solution provider industry has developed along similar lines.

There has been a separation between the ‘eProcurement’ systems and tools and ‘eSourcing’ for instance, and the dominant solution providers have tended to focus
on one or the other. Fundamentally, the solutions landscape, principally software products and platforms, are not yet aligned to a 'supplier management' model. That brings us to another key proposition.

| Achieving a stronger supplier management focus is in part an attitude and educational issue; but the tools available still do not fully support the holistic supplier management approach. |

That is beginning to change, to some extent at least. There has been growth in the last two or three years in providers offering 'source to pay' suites and systems. Those tend to cover the sourcing process, contract management and the ability to take the contract straight through into transactional activities i.e. cataloguing what has been sourced, placing orders and handling payments related to the contract.

But even here, there are key elements of that wider supplier management picture missing. Onboarding may well be covered, but still areas around deep supplier information and risk management tend to be provided by stand alone or more specialized firms. So whether it is Dun & Bradstreet providing deep financial data, or Achilles (a strong presence in the oil and gas industry in some geographies) providing information about supplier capability, qualifications and capacity, they address one important subset of supplier lifecycle management rather than the whole picture.

Equally, at the performance and quality monitoring end of the process, the broader software products tend to be weaker, and other specialists come into play. The good news however is that we are seeing innovative tools emerging, ranging from mapping technologies that enable visualization of the supply chain, to risk and performance platforms that help buyers pick up relevant external information about key suppliers. They can even make relative comparisons – how the supplier's performance for your organization compares to their wider performance in the market, for instance.

The complexity of the supplier management picture and the wealth of data that is already available (and will only increase) mean that we may never see a single software tool or platform that supports every aspect of supplier management. However, it is already clear that technology integration is becoming easier and more feasible. So we can see a future in which different tools and platforms work together, with much of the look and feel of a single integrated solution to the user / supplier manager.
Conclusions - practical steps for procurement leaders and practitioners

So what does all this mean for the procurement strategist in industries like upstream oil and gas, where suppliers undoubtedly play key roles in defining their customers' success?

![Behavioural shift in view of suppliers](Image)

**Fig 3: A high-level approach**

It's not hard to convince procurement and supply chain professionals of the importance of suppliers to the business. Equally, colleagues who work alongside suppliers in many operational business areas intuitively understand that. But the actions of organizations and executives don't always reflect this. Whatever technology solutions and tools that are used to support supplier management, and however we define that discipline, suppliers should certainly be at the forefront of thinking – strategic and operational – for procurement.

Whilst many professionals do understand how important suppliers are, we have seen that we are not yet at a point where software tools fully support an integrated 'supplier lifecycle management' approach. So smart organizations are using 'best of breed' solutions to address different key needs (risk management, onboarding, etc) and looking to integrate them where appropriate and possible to increase usability.
So we would suggest three key steps for procurement and supply chain professionals.

1. The first is encouraging a behavioral shift in their organizations in order to promote the view amongst all executives in the organization that suppliers are central to success and deserve to be treated as such. Suppliers are not a ‘necessary evil’; they are fundamental part of delivering the business and the future success of the firm.

2. The second recommendation is to look carefully at each key element within the supplier management picture. We have seen the importance of aspects such as onboarding suppliers, risk and performance management – is each one managed properly at the moment? If not, how can that be addressed? There may be a need to prioritize in terms of improvement opportunities, and if so, each organization needs to consider its own situation. But in our experience, the most pressing need within that wider supplier management picture is often in the fundamental areas of risk and performance management.

3. As well as ensuring each element is addressed, a more holistic, supplier lifecycle approach to supplier management should be considered. For instance, rather than looking for the perfect technology solution, which doesn’t exist, look for tools that can help in different areas and then consider how they can be integrated or linked to add value where appropriate.

Managing suppliers effectively, however it is achieved and whatever terminology is used to describe it, is absolutely critical in most industries. That is certainly true in upstream oil and gas, where third party costs are such a large proportion of the total cost base, and where supplier related risk is so critical. So taking a supplier-centric view of procurement and supply chain strategy makes sense, with the simple goal of driving greater supplier contribution, which ultimately must improve the organization’s own performance.
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Peter has over 25 years experience in procurement and supply chain as a manager, procurement director, consultant, analyst and writer. He edits Spend Matters UK / Europe, and with Jason Busch, the founder of Spend Matters in the US, has developed it into a leading web-based resource for procurement and industry professionals. Peter worked as Procurement Director for the NatWest Group, the Department of Social Security (the DSS), and the Dun & Bradstreet Corporation, and held senior positions in the Mars Group during his management career. He has an MA in Mathematics from Cambridge University, is a Fellow and was 2003 President of the Chartered Institute of Purchasing and Supply, and his first (co-authored) book, “Buying Professional Services”, was published by the Economist Books in June 2010. Further information on this topic and others can be found at the website www.spendmatters.co.uk, or he can be contacted at psmith@spendmatters.com. Reproduction of this publication in any form without prior written permission is forbidden.

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OFS Portal is a group of diverse, worldwide suppliers working together with a non-profit objective to facilitate e-Commerce by guiding trading partners in best practices and to provide standardized electronic price sheets to B2B trading partners. OFS Portal works with global standards organizations and trading partners to develop and improve open and royalty free e-Commerce data and business process standards in order to reduce costs to all participants in a technologically neutral manner. For more information, please contact:

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