



# Supplier Management - from contribution to commitment

# Supplier Management - How do you turn chickens into pigs?

**There's an old joke. In the ham and eggs breakfast, the chicken makes a contribution but the pig makes a commitment! How do you move your suppliers from 'outsiders' – who simply contribute to your operations – to 'insiders' – directly aligned with, and measurably enabling, effective implementation of your strategy?**

## Supply chain and suppliers – the “central nervous system”

Your supply chain is the “central nervous system” of your operation. And your suppliers are key to that system. Some industries, such as automotive or industrial manufacturing, will have thousands of suppliers. Others, for example pharmaceutical, are likely to have a much smaller supplier base. These suppliers will often enjoy an alliance or partner status. But, in every case, you need to understand and manage the risks they potentially represent, while ensuring they can most effectively support your operation.

## Increasing supplier diversity

There have been various drivers that often led to a diverse supply base including:

- Cost reduction
- Flexibility
- Leveraging favourable exchange rates
- Implementation of wider outsourcing strategies
- Redundancy
- Flexible access to innovation

Pursuit of these advantages has led to supply chains that have become geographically distanced and sometimes culturally separated from the aspirations, and even the basic quality standards, of their customers.

## Cheapest is sometimes far from best

Sub-standard suppliers have had a high profile negative impact on a range of industries, from toy manufacturing to food processing to pharmaceuticals. But the damage to business and reputations is not restricted to non-compliant or even harmful products. In the aircraft industry, for example, it is not product quality but, rather, on time and in full delivery (OTIF) that has severely delayed more than one flagship project. A growing body of evidence and experience indicates that best price or lowest cost location does not always equal best supplier.

## What's the insight?

At least a decade of conventional supply chain wisdom (best price is best case) is now being challenged. There are a number of contributing factors to this situation: the global financial crisis, the constantly fluctuating price of energy, raw material and currencies, the increasing impact of risk. As a result, compliance regimes and governance grow tougher and damage to reputation becomes more difficult to sustain.

## Risk must be understood

The risk that is inherent in the supply chain – and its effective management – is now at the very least as important as issues of cost. The challenge to managers who want to migrate their suppliers from outsiders to committed contributors begins with a clear understanding of potential risks; not just product quality but ability, or otherwise, to supply on time and in full, to keep pace with changes in demand and to understand what the customer is trying to achieve.

Those suppliers who cannot offer the certainty of OTIF on an assured and flexible basis need to be identified, supported through necessary change or, if necessary, removed from the chain.

## A new approach

At the macro level, it may well be that a new approach to the whole concept of the supplier base is needed. Senior managers need to look at the relationship between potential risk, scenario planning and the economic environment.

In future, elongated and potentially vulnerable worldwide supply chains may give way to more regional sourcing, with shorter distances and more built-in redundancy. This change will mirror a manufacturing trend towards regional hubs – as opposed to single specialist global sites and the OTIF problems many of them have experienced.

## Managing the supplier base – a watershed moment

Whatever your strategic direction, a global financial crisis and its impact on everything from commodity and energy prices to market confidence is a good time to re-evaluate both the performance and the make-up of your supplier base. The encouraging news is that, while you are considering future changes, you can make a quick and positive difference to the performance of your existing suppliers.

Even a diverse supply chain need not inevitably lead to disruption, delay and disappointment. With effective management techniques, the risks of supplier diversity can be transformed into measurable advantage.

To achieve that advantage, you need management information. You need the right processes and management systems in place to enable people – your own and your suppliers’ – to do the best possible job, even when circumstances change. And you need to start with accurate and current data. You need to know exactly what is happening in your supply chain currently. This can give some surprising insights.

It may be analysis shows that a skewed Pareto principle applies. Around 10% of your existing suppliers deliver 90% of the real value. It may be that, by increasing the geographical spread of your supplier base, paradoxically the risk to your operation decreases. But whatever the case, you also need to be prepared to take action. You will almost certainly have to make changes to gain improved results.

### What are the problems?

External problems come from the physical length and complexity of the supply chain. Extreme distance can lead to confusion and operational misalignment, giving rise to quality and consistency issues, missed deliveries and slippage with the end customer. Currency fluctuations can work negatively. Rises in different regional energy costs and long transportation can erode economic advantages.

But it is also worth being aware of areas of potential improvement with your own internal operations. The supply relationship is (or should be) a two way street. The better you understand your own operational needs, the higher the probability you can accurately brief and then work with suppliers effectively to fulfil them.

## What can you achieve? (given the right approach)

The desired end point is a robust, predictable and high quality supply chain. All the links (i.e. your suppliers) are of equal standard. They take consistent approaches. And they display good alignment with the operational requirements and strategic goals that are set by you. These are based on accurate understanding of your own operational needs and clear communication with your supplier base.

As a result, the supplier moves, over time, from responding to an order to making a commitment for the success of your operations.

## How do you do it?

Senior managers need to rapidly examine the existing supplier base. Speed, accuracy and effectiveness are essential. An audit of suppliers and analysis of the data it yields will give a clear picture of what is good and what is weak.

Historical data will provide answers to questions such as who has performed well on price, or OTIF, or quality and other key measures. It will also reveal who has been deficient. But the historical view is only part of the picture. Apply future scenarios to existing supplier performance. See who among your suppliers is most, and least, prepared to support you through the impacts the global economic downturn may have on your operations.

## What if?

This is a good opportunity to ask 'what if'? What if currency and interest rates develop unfavourably for you or your suppliers? What if you need to reduce production rapidly? Or increase it? What if you decide to manufacture closer to home? Or if you need to pass on price reductions to your suppliers? Or if there is a major change to your product portfolio through innovation or tougher compliance regimes? And what if you want to migrate more of your current internal processes to suppliers?

Any and all changes can have an impact on your suppliers. To minimise future risk, you must have a clear picture not just of how you can improve their performance today, but of how you can help them prepare to support you tomorrow.

## What now?

It is vital not just to gather performance data from suppliers. You should be able to read and interpret it, so that you can create a dashboard of management information that supports future supply chain decisions.

If necessary, draw on external advice to help you identify a set of Key Performance Indicators (KPIs) that show the stability of your suppliers to weather an economic storm and provide up-to-date information how well or poorly they are supporting you in your key areas.

In addition, plug the supplier base KPI data into some scenario planning to predict the likely impact of change. You can go a long way towards effectively managing future risk by understanding which suppliers are likely to be weak or strong, where the potential weakness lies and what, if anything, can be done to address it.

### **What can you do to make a complex supply chain contain lower risk while delivering higher value?**

Effective supplier management is a contact sport. As the customer, you need to be prepared to roll up sleeves and get involved. This may mean detailed liaison with suppliers, perhaps through regular visits to their premises, or even an extended presence.

It may mean involving supplier development experts to work with suppliers, their people and process, to make lasting changes. These will enable the supplier to deliver to your agenda rather than their own. It may even mean parting company with some suppliers and sourcing new ones.

There are three key phases in the creation of a risk-managed, future-proofed and flexible supplier base. They are: **Recognition**, **Measurement** and **Action**.

- **Recognition**

Recognise that there are many actions you can take to drive better value out of your supplier base.

- **Measurement**

Fact-based analysis, carried out if necessary at the suppliers' sites, will yield the detailed knowledge you need to identify gaps and plan measurable improvements.

- How does the supply chain support the operating strategy of your organisation?
- What are the total landed costs per item or category sourced?
- How much is poor supplier performance really costing you?
- What are the risks inherent in the supply chain? What mitigation strategies are in place, and what actions do you have in place ready to act on if and when required?

- **Action**

Interpret the data from supplier audits. Decide which suppliers you need to develop and which you need to remove. Work with the best and most viable suppliers. Communicate your current requirements and, where appropriate, your future needs. Install the practices and safeguards that will reduce, and then, over time, remove the causes of non-delivery and other disruptive outcomes.

## Results

Transforming suppliers into low risk, involved and responsive contributors to productivity and profit brings measurable results in key areas of the business. Across the supply chain you will see improvements ranging from reduced inventory levels to increased delivery plan attainment to an OTIF situation you can rely on.

And, even more importantly for the future, you will see suppliers who can rise to the challenge of changes in your production requirements without delaying your operation, disrupting your output and letting you and your customers down.

How you achieve this in practical terms is the subject of our more detailed companion paper: **Transforming your supplier base – an operational guide**



## About the Author

### Martin Laub

Martin Laub is a Senior Project Manager with Celerant, and also leader of Celerant's Integrated Supply Chain Capability for our German business. With over a decade's experience in consulting, Martin's work with clients has spanned a number of industries (predominantly in Manufacturing), addressing a number of key business issues, specialising in the domains of Supply Chain Management, Supply Chain Performance Management, Sourcing & Procurement, Supplier Management, Operational Strategy and Business Management Systems and associated business processes. His work has results in considerable benefit realisation for his clients, and several of the projects he worked on won industry awards.

Martin has spoken at numerous conferences, and has published articles focusing on the themes of Integrated Strategic Sourcing and Supply Chain Intelligence.

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Erik is a seasoned Six Sigma Master Black Belt, has driven multi-million \$ productivity improvements in the Netherlands, Belgium, Germany, France, Italy, UK, USA, Japan and has been applying Process Excellence and business improvement principles for over a decade. Erik has a Business Administration degree from the University of Groningen.

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