

## Reaching Sourcing Excellence, Part 2: Going From Good to Excellent

Mickey North Rizza

Sourcing teams vary in their focus and alignment to the business, business processes, and performance. Regardless of positioning, all have an opportunity to improve. In this segment of our sourcing landscape, we identify the sourcing organization's maturity levels and provide a self-assessment tool.

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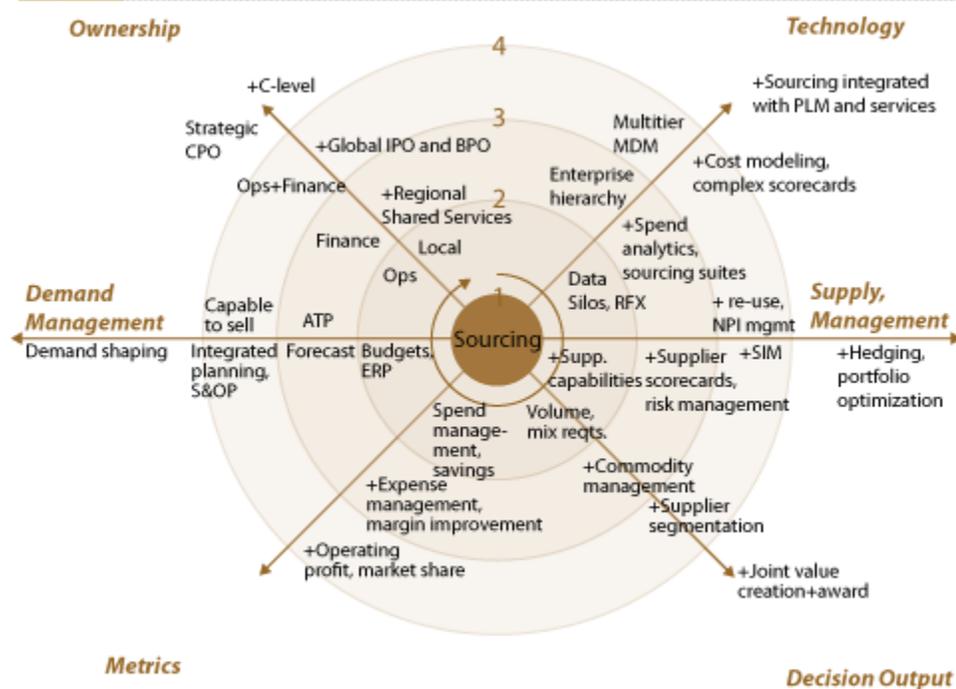
For every dollar sourced, there's an opportunity to use trading partner contributions of innovation and excellence, improve revenue, reduce costs, and streamline workflows (as we discussed in Part 1 of our sourcing landscape). Creating this value, however, requires an honest assessment of your company's sourcing organization.

Based on 78 interviews AMR Research conducted with global sourcing organizations, we have created a maturity model and self-assessment tool to help you establish your sourcing organization's maturity.

### Knowing what good looks like

Recognizing where your company sits in the maturity model is one half of the battle to understanding what good looks like (see Figure 1). The path to achieving sourcing excellence represents a multi-year journey for most organizations. Fortunately, dramatic returns come even at the earliest stages of progression. Increasingly, smart C-level executives insist on dramatic returns as they begin their quest for sourcing excellence.

**Figure 1:** Sourcing four-stage maturity model



Source: AMR Research, 2009

The other half of the battle is recognizing what's missing in your organization. With our self-assessment guide, you can fill in the gaps (see Figure 2).

**Figure 2:** Sourcing self-assessment



Source: AMR Research, 2009

We've outlined a series of questions to ask yourself and your organization as a way to identify any sourcing organizational gaps so you can advance along the maturity curve. Each step has a series of questions to help you identify the stage where your sourcing organization currently resides. A look forward to the next step will show you what's required to continuously improve.

There are eight segments across the four steps, with transformational elements for you to consider (see Table 1). The missing transformational elements of most sourcing organizations are typically culture, organization, measurement, business process, technology, savings, and supplier relationships. Elements within each become your key areas for improvement. They'll require different approaches based on your company's business strategy, culture, processes, and systems.

**Table 1:** What does good sourcing look like? Continuous improvement

	Stage 1 Reacting	Stage 2 Anticipating	Stage 2 Anticipating	Stage 3 Collaborating	Stage 3 Collaborating	Stage 4 Orchestrating
	Stage 1 to 2 Transformational Elements		Stage 2 to 3 Transformational Elements		Stage 3 to 4 Transformational Elements	
<b>Business Process</b>	Standardize and automate processes Sourcing becomes part of design phase		Integrated lean business processes across key stakeholders and with supply partners. Flexible supply contracts		Sourcing involved in customer account planning Sourcing orchestrates the innovation process and architects products and services to combine partner expertise	
<b>Organization</b>	Global Sourcing Organization Global commodity/category managers Shared Service Centers for Indirect and Services spend Spend Under Management		Integrated back and front office. Cost effective and efficient organization: Shared Service, BPO, and Commodity Partners VP of Supply Management or CPO is leader under CFO or COO.		Focus shifts to demand translation for value creation and profitable ecosystem. COO is overall leader. CPO becomes a voice on sourcing business strategy, alignment and results.	
<b>Measurement</b>	Global standardized metrics Internal focused metrics for stakeholder awareness Annualized Savings by Spend Type Forecasted Savings vs. Realized Savings		Align inside out metrics Supplier metrics of Finance, risk, service level, compliance, responsiveness, innovation.		Shifts to outside in metrics aligned to business needs.	
<b>Continuous improvement</b>	Total Cost Management Cost Differentials Analytics provide rationalization and data points for improvement		Supplier leveraged for expertise in design, commodity, or manufacturing. Should cost models, designs for re-use, and green requirements.		Open supplier innovation is encouraged. Suppliers are part of end user requirements meetings and design for success.	
<b>Technology</b>	Move from pure Microsoft applications and ERP to Best of Breed point solutions of Spend Analytics, Sourcing and Contract Management.		Supply visibility and collaboration enabled by technology.		Technology enables business processes globally, including multi-tier supply visibility and collaboration.	
<b>Culture</b>	Employees require technology training. Certification programs are outlined around technology training.		Employees focus on meeting business strategy and objectives. Culture of change and risk taking is encouraged and rewarded.		Employees align with business needs. Financial statements drive sourcing success across the enterprise. Strategy, finance, negotiation, analytics, collaboration are key sourcing criteria.	
<b>Supplier Relationships</b>	Move from adversarial to cooperative. Suppliers recognize sourcing in process. Sourcing selects best suppliers for business requirements		Sourcing recognized as leaders and facilitators of supplier relationships across the enterprise. Suppliers are segmented by business need, relationship, and products.		Enterprise and integrated supply partners have largest global and multi directional visibility.	
<b>Savings</b>	Move to 20-40% savings with optimization technologies but not sustainable. Supply chain savings typically 7-12% based on demand, innovation, and alternate materials. Savings based on varied processes of demand, sourcing technology, and face to face negotiations.		Savings based on all spend types rationalized. Focus on design for supply. Margin improvements of at least 2%.		Margin improvements tied to product expectations based on demand and market share. Savings may be shared with suppliers. Demand and expense management are practiced by all stakeholders.	

Source: AMR Research, 2009

The questions in Figure 2 and the transformational elements found in Table 1 can serve as a framework for your sourcing organization.

**The stages of maturity**

Consider the following four stages: reacting, anticipating, collaborating, and orchestrating.

*Stage 1: Reacting*

Reactive sourcing organizations are unconsciously incompetent because they don't know how to do anything to solve the sourcing excellence requirements other than react to a given demand. Source identification, supplier capability assessment, and supplier selection are usually done prior to the sourcing organization's involvement. Once these three are completed, sourcing is

then asked to complete the process. The remaining sourcing process is then completed in a typical fashion, with negotiation technologies such as RFX and reverse auctions.

In this scenario, negotiation of savings justifies its existence. Sourcing skills are focused only on securing the most savings, often at the supplier's expense. Without negotiation technology, category-specific savings are typically 5% to 10%. With the negotiation technology, they're 10% to 20%.

Sourcing value in reactive organizations is based on the savings negotiated, contracts awarded, and the closure of events. Integrated supplier relationships, lower cost supply strategies for new and current products, and embedded capital and expense management strategies are only a vision or idea in reacting sourcing organizations.

#### *Stage 1 case study: Don't leave money on the table*

A \$5B discrete manufacturer with a decentralized sourcing organization that focused on localized, one-time negotiated savings invested in RFX and negotiations sourcing technologies. With the formation of a few commodity councils and negotiation technology deployment and training, the company found savings on average of 17% across all categories.

However, the supply chain suppliers focused their attention on the forecasted demand from the product line managers and didn't recognize sourcing importance until the business award, which came after the product qualification was complete. Sourcing was not an integral part of the product plans and supplier communications, which, according to the vice president of sourcing's estimation, left an average eight cents of the purchased supply chain dollar with the supplier.

#### *Stage 2: Anticipating*

Anticipating organizations are consciously incompetent: While the sourcing organization is anticipating and meeting many needs, employees aren't aligned to business requirements.

These sourcing organizations are much leaner, are involved earlier in the design phase, and have global commodity management and shared services organizations. They use sourcing negotiation tools and work toward a lower total cost of ownership (TCO). Anticipating sourcing organizations look for more spend under management using negotiation, optimization, spend analytics, and contract management applications.

#### *Stage 2 case study: \$21M in savings, anyone?*

A \$4B high-tech company has an anticipating sourcing organization that's focused on controls, efficiencies, and working toward all spending under management. It used spend analytics tools to put more spend under management as well as segment its supply base into enterprise, collaborative, and transactional types. As a result, it found additional savings of 7% per category.

Using a TCO model and a shared services structure, the company utilized its spend analytics, e-sourcing negotiation, and optimization applications as well as face-to-face negotiations to yield \$21M, or 31%, in savings in five of its larger categories. Because this sourcing strategy brought such significant results, a technology training program was deployed, which improved its technology adoption and led to a sourcing education and certification program.

#### *Stage 3: Collaborating*

Collaborative organizations are consciously competent because they're meeting business objectives, measuring and meeting stakeholder requirements, and riding the track of continuous improvement. They're adept at using technology to enable their business processes, including spend analysis, business intelligence (BI), sourcing, contracts, EDI/XML, supplier portals, and supplier risk and performance technologies. These organizations have integrated lean sourcing

processes, and they've also segmented their supply bases, considering their supply partners integral to organizational success.

Collaborating sourcing teams use should-be cost modeling and baseline indicators to gauge success, with a focus on supplier management, including metrics based on financials, risk sharing, service level, compliance, responsiveness, and innovation. Collaborating sourcing organizations represent a culture of change, where taking risks is encouraged and rewarded.

#### *Stage 3 case study: Lift and shift and tech training to the rescue*

A large consumer products CPO, upon reviewing his business strategy and objectives, discovered that despite the continuous cost savings driven by cross-functional business teams and should-cost models, the product margins were dwindling in the face of rising commodity costs. Aligning business strategy and sourcing collaboration across business functions are two critical parameters of collaborative sourcing organizations.

Taking a calculated risk, but staying tied to his business strategy (which is another key indicator of a collaborating sourcing organization), the CPO moved several of his best supply chain sourcing and commodity experts to indirect goods and services categories. Using **Ariba** augmented with **SAP**, this calculated, collaborative sourcing strategy saved his company \$10M in 12 months through expense reductions. It now operates more efficiently and uses technology as an enabler to deliver results. The sourcing organization's effectiveness has grown tenfold because of this employee lift-and-shift program.

However, the CPO also needed to address the supply chain products. With the recent purchase of a supply-chain-oriented sourcing tool with more advanced capabilities in optimization, supply intelligence, and categorization, the CPO took advantage of the technology and training. With this training complete, the supply chain sourcing teams, coupled with should-be cost modeling techniques, and the design-for-supply teams attacked the company's margin erosion with gusto.

This collaborative sourcing approach brought in great results, including a reversal of margin erosion in the near term and targeted margin improvements for the future. By applying a more complex tool, a greater understanding of the supplier economics, better capacity management, and complete optimization analysis, this sourcing team is heading in the right direction.

#### *Stage 4: Orchestrating*

Orchestrating organizations are consciously excellent because they run seamlessly across their enterprises, conduct customer account planning, manage the innovation process, and architect products and services that combine supply partner expertise.

Orchestrating sourcing is focused on demand translation into joint value creation and a profitable ecosystem. Sourcing leadership lies ultimately with the COO, with the CPO part of the business strategy development and alignment, finally achieving a voice and a seat at the executive table.

Orchestrating sourcing organizations' cost savings are shared with ecosystem-integrated supply partners for co-prosperity. The suppliers are given greater freedom, understand end-user needs, and creatively solve issues. Advanced use of technologies provides global, multi-tier, bidirectional collaboration.

Employees are aligned with business strategies and are highly skilled in finance, analytics, and collaboration. Their focus is on integrated enterprise and partner teams. Orchestrating sourcing organizations with direct material supply chains orchestrate similarly to many in the [AMR Research Supply Chain Top 25](#) .

#### *Stage 4 case study: Offshoring brought the greatest cost reductions*

A \$14B hard goods retailers aligned itself with its consumers by understanding innovation and trend requirements. The alignment, along with sales and operations planning (S&OP), ensured the company's product success as it tied its sourcing strategy to margin requirements.

Offshore and nearshore supply strategies were implemented based on time-to-market requirements by market and region. Nearshore strategies were utilized for market trials and product opportunity assessment. Once the products were cemented in a particular market, offshore providers were pursued.

Offshore partners provided the greatest cost reductions while meeting financial, risk, and innovation and trend requirements. The offshore strategy improved margins 18% to 26% and ensured a successful sourcing strategy for the lifespan of the specified products. The sourcing organization's focus on demand translation across the ecosystem also enabled profitability improvements of an average 8%, including savings to the ecosystem partners.

The voice of the customer and supply intelligence are driving this retailer's orchestrating sourcing decisions. A sourcing suite, business intelligence (BI), and supply chain technologies provide multiple levels of collaboration and measurement of ecosystem success.

### **Next steps**

Once you have identified your maturity level and found your gaps, you will need to ponder key considerations to establish the right transformational strategy and business plan, and then execute for success. The right resources are also critical elements in the sourcing transformation journey. Stay tuned for upcoming research that can help you and your organization on both fronts.

I welcome your comments and questions at [mnorthrizza@amrresearch.com](mailto:mnorthrizza@amrresearch.com).