

PART ONE

The Process

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An Introduction to Strategic Sourcing

MANY BOOKS HAVE ALREADY BEEN WRITTEN on the subjects of strategic sourcing and supply chain management. Each describes a sourcing process that generally includes five to seven steps, and overall the primary differences between these books are the ways those steps are defined and segmented. The process we describe in this book does include six steps, starting with the inception of the initiative (project kickoff) and concluding with final monitoring of the implemented program (continuous improvement). However, our process applies strategic sourcing techniques specifically to indirect spend categories and offers insights and strategies that have been used successfully in real-world practice. Our process is not based on theory; the techniques described have been refined based on years of experience working with many types of companies to reduce their costs for indirect goods and services. As you will discover as you progress through the book, the process itself serves primarily as a project management tool. The use of creative strategies and the ability to adapt to ever-changing conditions are the key elements that make your sourcing initiative truly strategic.

Many companies still do not apply strategic sourcing techniques to indirect spend categories. Instead, indirect spend is treated as a series of one-off purchases, or is sourced with a simple three-bid strategy with no efforts

beyond reviewing the supplier price responses. Typically, with indirect spend, per-item prices are relatively low, the product or service is not crucial to the business, and the overall costs are rarely examined because of the difficulty entailed in gathering meaningful spend and market data. Strategic sourcing allows companies to shift away from thinking about indirect spend in this ad hoc manner, and provides spend visibility, objective decision making, and a project management tool to ensure efficient use of the sourcing team's time and efforts.



VISIBILITY

Strategic sourcing provides visibility into business processes, operational issues, and spend details that may not have been clearly available to management and stakeholders in the past. The process of strategic sourcing provides a road map for collecting and analyzing this information to determine how the purchase of a particular product or service truly fits into the overall business operations of an organization, from the identification of the need to the use of the product or service and (if necessary) its disposal. This includes identifying:

- Who buys the product
- How it is ordered
- How it is received
- How it is paid for
- Where the payment information resides in your systems
- What the payment reconciliation processes are
- Where the product is stored
- When it is used
- Why it is needed
- Who the suppliers are
- What value-adds or services are provided
- What happens to the product after its useful life is over

As we discuss throughout the book, all of this information is necessary to properly perform strategic sourcing, to ensure the most efficient processes and tools are utilized, and ultimately to implement and maintain the final program developed as a result of the process.



OBJECTIVITY

Strategic sourcing allows companies to shift the management of indirect spend from a series of one-off purchases to a more coordinated effort with checks, balances, and objectivity that justifies costs and requirements. Historically, indirect purchases and spend for most companies were managed by one or many individuals, with little oversight from management and no requirement to justify their selection of suppliers. Strategic sourcing provides a process to identify the true requirements of the organization (rather than those of the individual managing the spend) and to identify suppliers and price points that appropriately meet those requirements. The process is performed in such a way that requirements are identified well ahead of supplier identification, and stakeholders agree to those requirements before alternatives to the existing arrangement are presented.



PROJECT MANAGEMENT TOOL

Finally, a well-designed strategic sourcing process becomes a project management tool that ensures the engagement will not end in failure due to scope creep or lack of a clear path forward, and that those working on the project make the most efficient use of their time. Attempting to reduce costs without a formalized strategic sourcing process can easily end in frustration, as roles are not clearly laid out between team members, steps are not identified, and timelines are not set. As we discuss throughout the book, the strategic sourcing process includes many challenges, and teams can easily get bogged down in noncritical details or fail to come to consensus on next steps. The process in itself includes steps that can be integrated into a comprehensive project plan that avoids convoluted outcomes.

The six basic steps of the strategic sourcing process are:

1. Data collection and spend analysis
2. Research
3. The RFX process (requesting information, quotes, and proposals from suppliers)
4. Negotiations
5. Contracting
6. Implementation and continuous improvement

Our goal is to help you navigate through specific activities that most sourcing books fail to cover—dealing with and effectively utilizing internal constituents, motivating the supplier marketplace, and gathering the information required to make informed decisions during each step of the process.

Data Collection and Spend Analysis

Once you identify the need for strategic sourcing, the next step is collecting and analyzing spend data. The purpose is twofold. First, the data is needed to determine where you should focus your efforts. Your resources are more than likely limited, and it will not be possible to immediately reduce costs across all areas where your company spends money. Areas of opportunity need to be identified and a project road map created to provide context and timelines for your efforts.

Second, data is needed to determine both quantitative and qualitative requirements associated with a spend category. When we discuss the quantitative aspects, we are referring to current price points, discounts, payment and freight terms, and other costs associated with a particular area of spend or supplier. Qualitative requirements refer to the quality and services tied to these costs. The current suppliers were more than likely chosen based not just on price, but other value-added considerations as well, and these factors need to be understood and considered. The quantitative baseline and qualitative requirements become the launching pad for the rest of the engagement, which makes it critical not just to identify them, but also to make sure they are agreed on by other interested parties within your organization before moving to the next step.

Research

The research phase provides context to the categories you are sourcing. The purpose of research is to develop or refine your sourcing strategy by determining what competition exists in the marketplace; what alternative products, services, or processes are available; and whether or not current market conditions make it a good or bad time to go to market. We will define market intelligence in greater detail and discuss its importance as it relates to your ability to drive savings in a spend category.

The RFx Process (Requesting Information, Quotes, and Proposals from Suppliers)

During the RFx phase you will execute the sourcing strategy developed during the data collection and research phases. In all likelihood this will include

requesting proposals or quotes from alternate suppliers or performing a reverse auction. However, depending on market conditions, the competitive landscape, and how the product or service purchased fits into your overall business strategy, it could also mean focusing on other cost reduction strategies that do not involve bidding out the business. We outline some of these strategies and point to a couple of case studies where bypassing the request for proposal (RFP) was a successful strategy. During the RFX stage of strategic sourcing you will also evaluate the proposals and other information submitted by suppliers to determine both the quantitative (cost savings) and the qualitative (service/value-add) benefits through the objective process of scorecarding or grading.

Negotiations

Once initial proposals are received, refined, and analyzed, you will move into the negotiation phase of strategic sourcing. At this stage you will develop target price points for the products or services you buy, identify preferred suppliers (incumbents or alternates), and request that suppliers meet the established targets in order to win your business. Chapter 6 provides strategies to help you identify how to come to your price targets and how you can leverage multiple bids against each other.

As we discuss in detail in Chapter 6, considering negotiations as a separate step in the sourcing process is slightly misleading, and separating it from the rest of the process can be detrimental to the overall results of the project. Some form of negotiation should be taking place with the supplier community throughout the strategic sourcing process.

Contracting

Once the final supplier or suppliers are selected, your next step is to award the business. The contracting phase converts the business terms agreed to during the sourcing phase into a legally binding document detailing the rules of engagement between the customer and supplier. The contracting phase does not necessarily end in a signed contract between two organizations; it could result in a pricing agreement with agreed-to terms or a simple purchase order.

Implementation and Continuous Improvement

Often overlooked or considered outside the scope of strategic sourcing, implementation and continuous improvement ensure that the work performed during the sourcing process is properly utilized and taken advantage of by your

organization for years to come. Simply entering into an agreement with a preferred vendor does not result in cost savings. End users and stakeholders need to make purchases under the terms of the agreement, as maverick buying is often the primary reason savings are not achieved. Savings need to be tracked to ensure that the supplier is upholding its end of the bargain (price) and your organization is holding up your end (volume). This means rolling the agreement out internally, reviewing invoiced pricing as well as other internal documentation to ensure internal customers are not buying off-contract, and requesting credits for improper billings.



IN SUMMARY

Part One of this book covers each of the steps in the strategic sourcing process in great detail. While some of the challenges discussed may not apply to your organization, we have taken care to use examples we find in many of the companies we work with, regardless of size, industry, or type of project.

While the strategic sourcing process on its own can produce cost savings, working to optimize your results requires you to think about the steps in the process and determine the best way to customize those steps for your organization. Developing cost-savings strategies, delving into market research, and negotiating with internal stakeholders and external suppliers requires a highly creative approach—it is not all analytics. Applying strategic sourcing techniques to indirect spend categories can be a challenging endeavor; however, for companies looking to cut costs or enhance profitability, these spend areas can provide a wealth of untapped savings opportunities.