

SUPPLIER RELATIONSHIP MANAGEMENT – THE ROLE IN EFFICIENCY FOR AN ORGANISATION

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ABSTRACT

Nearly all professional procurement organisations have a stated intent and commitment to do more in the area of supplier relationship management and save cost. The need and process of a supplier relationship management are complex. A robust process would ensure that the capabilities and composition of the procurement team would need to change along with the team's orientation. It requires the management of the organisation to spend more time with the suppliers than with the procurement team. It would require to identify relationship with suppliers to be business-centric relationship.

Simply put, being able to negotiate a deal does not mean a buyer is able to manage a relationship, nor is it possible to ensure premium access to suppliers in a contract. A study was conducted to gain a better understanding of Supplier Relationship management and to advise our clients on this topic.

A study was conducted by conducting interviews of academicians and industry professionals to identify the objectives, challenges and benefits of supplier relationship management in organisations. The study also identified the critical success factors and the competencies required for success of a supplier relationship management program.

Introduction

The role of the procurement function is drastically changing in today's challenging world. In the past, procurement was expected to ensure the timely availability of products and services while also being responsible for accurately processing transactions. Economic developments during the 1990s and later prompted companies to recognise the potential contribution of procurement to meeting cost-out targets. Through the implementation of category management and running strategic sourcing initiatives, procurement was able to rationalise the supply base and consolidate volumes, resulting in price reductions. Global sourcing and outsourcing of non-core activities became popular as well.

However, the procurement function was still functionally organised, with little collaboration and alignment with other business functions, which kept the price orientation alive.

During the advent of the Total Cost of Ownership (TCO) concept, organisations started to realise that a change from a functional orientation towards processes optimisation was required, with cross functional collaboration. As a result, procurement became the responsibility of cross-functional teams while its strategic importance and recognition increased. The procurement function not only contributed to price reductions, but also played a crucial role in optimising total lifecycle costs. The next step towards procurement excellence is to adopt a value-driven orientation with external/supplier collaboration as a key cornerstone.

As stated previously, ensuring the best prices through strategic sourcing is no longer perceived as a strategic capability of the procurement function. As a result of further outsourcing of non-core competencies, the procurement costs as a percentage of total cost is 50-80% for companies that develop, manufacture, trade and/or distribute goods. Besides this financial impact, organisations are starting to realise that they have become more reliant on suppliers in terms of innovative power, security of supply, corporate social responsibility, and delivering on-going cost savings. Together with sustainability, strategic partnering is at

the top of the corporate agenda of many global organisations and is seen as one of few remaining procurement topics that can still make a significant difference.

Literature review

Companies are now aware that they must integrate and collaborate with suppliers to remain competitive and take the next step towards procurement excellence. Supplier management is not a new topic, but it has always been the 'stepchild' of the procurement function. KPIs like spend reduction were an important culprit here. Companies became rather proficient and mature in running strategic sourcing initiatives and created "money on the table". After realising the contracted savings, category teams and buyers jumped on the following sourcing initiative while neglecting the implementation and management of contracts. Delivering "money in the pocket" reflected as savings in the P&L appeared to be another story. Research indicates that there is an average of 25% contract value leakage ("money in the air"). Formalising contract management and delivering "performance to contract" is a challenge for many organisations.

Not every supplier is qualified as a partner: supplier segmentation is necessary to differentiate supplier strategies. If a supplier is qualified as strategic, an organisation can decide to initiate a partnership.

In our definition, Supplier relationship management is a systematic approach for developing and managing partnerships. It is focused on joint growth and value creation with a limited number of key suppliers based on trust, open communication, empathy and a win-win orientation. Non-partnerships are managed by means of other measures like contract administration, contract management and vendor rating. In our opinion, Monczka e.a. (CAPS Research, 2011) had the Supplier Relationship Management objectives and benefits very concisely:

1. Become 'customer of choice': preferential treatment regarding availability, costs, access to technology, innovation and risk reduction
2. Focus on value: increased market competitiveness through consideration of all relevant elements that determine stakeholder value
3. Leverage on supplier capabilities: advantageous position through early involvement in the innovation and product & process development processes
4. Share growth, profits, risks and investments: joint objectives, efforts and resource commitments resulting in a healthy culture for continuous growth.

Supplier Relationship Management maturity level

Maturity models help organisations to define the current state of affairs and provide the opportunity to facilitate a discussion on the ambition level. Academic literature identifies four different levels:

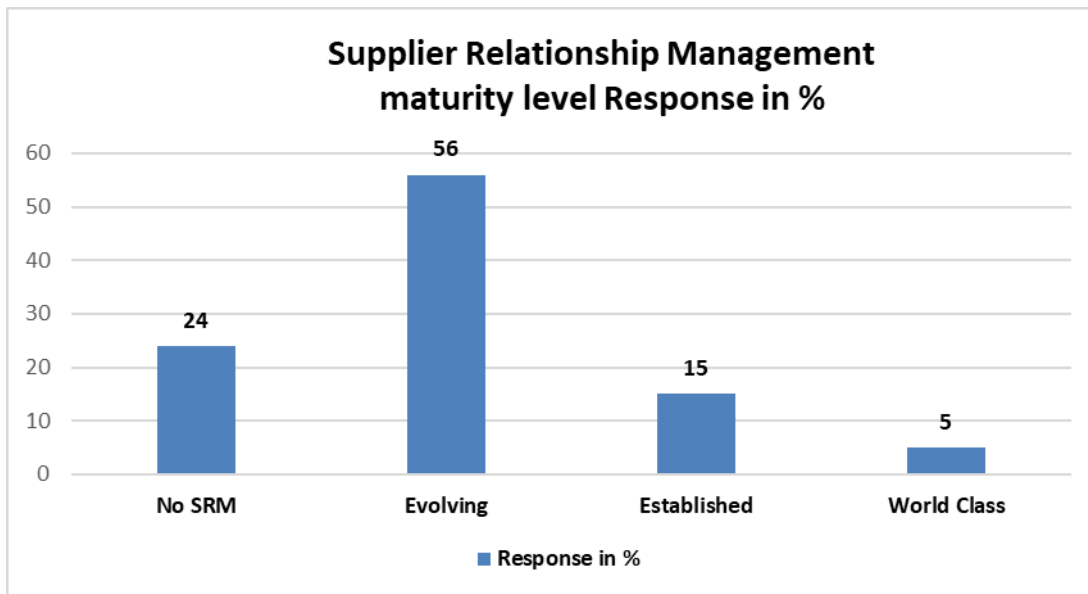
1. No Supplier Relationship Management: the organisation manages all suppliers by means of contracts without any differentiation in supplier strategies. The objective is to realise 'performance to contract'. Performance management is one directional and rather directive. Collaborative improvement initiatives are rather unstructured.
2. Evolving - the organisation recognises the value potential of key suppliers and initiates a limited number of pilot projects to build trust, experience and credibility. Joint initiatives now go beyond cost reduction and are organised in a more structured way, but are still rather operational/tactical by nature.
3. Established: Supplier Relationship Management is a mature business process and fully integrated in the operating model. All key suppliers are covered by the Supplier Relationship Management programme and financial benefits are delivered while risk exposure is significantly reduced. Supplier Relationship Management starts to deliver top-line improvements as well and is seen as a strong contributor to competitive advantage. Joint improvement initiatives are formalised with a clear governance structure.
4. World-class: Supplier Relationship Management is at the heart of the business and fully incorporated in the corporate strategy. The organisation is "customer of choice" for a selected number of strategic suppliers

with which it is fully integrated. The organisation shows double-digit improvement percentages year-on-year and, as a result, stays ahead of its competitors. Collaboration between both partners is a way of working: procedures are no longer necessary.

The responses in the maturity are given in the flowing figure, which clearly indicates that the current maturity level of Supplier Relationship Management is still relatively low. Almost a quarter of all respondents (23%) indicate they have no Supplier Relationship Management programme at all.

Collaboration with strategic suppliers is unstructured, as are joint improvement initiatives. Most organisations are at the ‘exploring’ stage (64%).

They initiated a Supplier Relationship Management programme and are developing toolkits & templates, but only for a limited number of partners. A minority of the respondents have fully “established” Supplier Relationship Management programmes (13%) while none of the respondents has a ‘world-class’ Supplier Relationship Management programme in place.



Source – Survey results

Research objectives and Methodology

With more than 500 sourcing & procurement practitioners worldwide, commercial department have broad and deep expertise to support organisations in solving supply-related issues. It is seen that many organisations encounter difficulties in initiating, developing and managing supplier partnerships. It was decided to conduct personal interview with academicians and also industry professionals and conduct a survey of the procurement professionals.

A survey of 30 (thirty) procurement professions was conducted to get a better understanding of the typical challenges and to determine how supplier capabilities drive competitive advantage.

Our respondents were drawn from private companies in the areas of manufacturing, trading and academicians in the field of supply chain management. The companies based in Pune were taken for the survey. The instrument used were personal interviews. The sampling was purposive sampling.

The focus to understand the following areas of supplier relationship management,

- a) What are the objectives of supplier relationship management structure in India
- b) What are the key challenges in building strategic partnerships with suppliers
- c) What are the best practices to be adopted to achieve world-class Supplier relationship management
- d) Which supplier capabilities contribute to competitive advantage
- e) How to successfully implement Supplier Relationship Management.
- f)

Findings

Objectives of Supplier Relationship Management

Developments in the business environment have become much more difficult to anticipate due to the globalisation of demand and supply markets, more demanding customers and consumers, shorter product lifecycles, continuous pressure on costs and cash, and societal pressure regarding corporate social responsibility. As a result of outsourcing, procurement and supplier management have become more important and strategic.

The key three objectives from as identified by respondents were,

1. Joint value creation
2. Reducing cost
3. Security of supply

Other Supplier Relationship Management objectives identified were,

4. Increase innovative power
5. Reduce working capital
6. Enable closed-loop supply chain management
7. Shorten time-to-market, increase supplier service

Supplier Relationship Management is focused on joint value creation based on trust, open communication and collaboration with a limited number of key suppliers. The idea is to leverage supplier capabilities as organisations in real life do not have the means to finance all activities on their own and gaining access to unique knowledge, resources, capabilities, talent and ideas of the suppliers helps to create a collaborative value creation model.

Reducing cost would appear to conflict with the focus on value creation, but cost-cutting is still one of the key imperatives. The main difference with traditional approaches is that benefits are now realised and shared together with partners. This objective is also related to the low maturity level of Supplier Relationship Management as a business process the business perceives procurement, and therefore Supplier Relationship Management, primarily as a contributor to cost reduction.

Security of supply - Due to the globalisation of supply chains, stronger fluctuations in demand & supply, material scarcity, and preferential behaviour by sellers or even countries, it has become difficult for companies to ensure product availability to customers. By means of partnerships, buying companies aim for preferential treatment while driving out strong volume and mix fluctuations through integrated forecasting & planning, product substitution & simplification, and hedging.

Supplier Relationship Management challenges

Although organisations are aware and convinced of the Supplier Relationship Management benefits, many still encounter difficulties in developing, implementing and operating partnerships.

The top three challenges which are most relevant for their organisation.

1. Dominant role of cost
2. Change of mind-set and systems
3. Compatibility of strategic objectives of buyers and sellers

Other challenges include

4. Lack of training
5. Lack of specific Supplier relationship management strategy & objectives
6. Lack of harmonised way of working with a standard toolkit
7. Lack of rigorous programme management
8. Too much focus on operational issues

Cost reduction is an essential part of value creation but too much focus on this aspect discourages a long-term orientation. Buyers focused on short-term optimisation, provoke counterproductive behaviour & collaboration, and emphasise procurement's traditional role of getting the lowest prices.

Traditionally procurement related functional competencies like negotiation skills, market analyses, and cost & risk management were perceived as the key to success. Traditionally, buyers do not naturally have such skills or are not trained to develop them. However, Supplier Relationship Management requires completely different skills like influencing, leadership and change management.

The strategic objectives of the buyer and supplier are incompatible. This situation is aggravated if the buying organisation wants to develop a partnership while the supplier is focused on exploiting the customer.

Competencies required for successful supplier relationship management

The success of Supplier Relationship Management is also highly dependent on the competencies of the supplier. Supplier competencies are the resources, processes and measures a supplier can offer the buying firm, and which are needed to develop and manage partnerships. One overall conclusion from the study is that most organisations score the competencies of their key suppliers significantly higher than their own competencies.

- i. Operational & Technical competencies
The competency to deliver products/services on time in full and according to specifications.
- ii. Relationship competencies

The willingness and the ability to collaborate. Supplier Relationship Management is based on building relationships and trust is an important enabler.

- iii. Developmental competencies
The ability to develop new products or realise product improvements by supplier.

Critical Success Factors

To successfully achieve the Supplier Relationship Management objectives, organisations need to meet several prerequisites. We asked the respondents to select three critical success factors out of a list of ten that are most relevant to their organisation.

It is vital to track the progress of the intended benefits. Positive results build credibility and ensure focus. The second important critical success factor is strategic coherence. First, the business and procurement should be internally aligned so that Supplier Relationship Management fully contributes to business objectives. Once that is realised, a partnership will only succeed if there is a strategic coherence between the buying firm and key supplier. For example, the cost leadership strategy of a buying firm does not really match with a supplier's strategy focused on differentiation by innovation. The third-ranked critical success factor is sponsorship by top management. It ensures that the right priorities are set and that sufficient/appropriate resources are allocated.

Other success factors critical to Supplier Relationship Management that are not presented in the graph but were mentioned during expert interviews are: get the supplier data right, fulltime dedicated supplier relationship managers, cross-functional teams, supply market & supplier intelligence, and clear understanding of supplier relationship management by the organisation.

Benefits of Supplier Relationship Management

Performance improvement and risk exposure reduction are communicating vessels. Taking more risk could result in short-term advantages but threatens long-term financial and operational performance. In our research, we asked respondents to indicate which benefits have already been realised with current Supplier Relationship Management initiatives. The figures do not reflect the level of performance improvement but how often a benefit was mentioned by a respondent.

Other Supplier Relationship Management benefits that are not presented in the graph but were mentioned during expert interviews are: higher contract compliance rates, more successful outsource deals, increased supplier service percentages, strengthened relationships, higher speed-to-market and less waste in the supply chain.

How to establish Supplier Relationship Management

A transformational approach, that considers the value potential, complexity, number of stakeholders and organisational impact, is suggested for establishing a robust Supplier Relationship Management. Typical steps of the same would be,

1. Plan
2. Design and Construct
3. Implement Control
4. Review

Although Supplier Relationship Management ultimately becomes a business process, it initially starts out as a program to establish Supplier Relationship Management or a partnership on programme and change management.

The plan is focused on defining the ambition level, developing a high level design for Supplier Relationship Management, and calculating the business case as a solid foundation for the Supplier Relationship Management programme.

Typical activities include: •

- Mobilising a cross-functional project team;
- Reviewing current supplier management programs, strengths and improvement opportunities
- Defining current maturity level and ambition level
- Developing a tailored Supplier Relationship Management value map that links Supplier Relationship Management initiatives to business objectives;
- Formulating Supplier Relationship Management strategies, objectives and policies;

Although Supplier Relationship Management ultimately becomes a business process, it initially starts out as a programme to establish Supplier Relationship Management or a partnership.

Conclusion

Ensuring the best prices through strategic sourcing is no longer perceived as a strategic capability of the procurement function. As a result of further outsourcing of non-core competencies, organisations are starting to realise that they have become more reliant on suppliers in terms of innovative power, security of supply, corporate social responsibility, and on-going cost savings. Strategic partnerships are at the top of the corporate agenda of many global organisations and Supplier relationship management is seen as one of the few remaining procurement topics that can still make a significant difference. But many organisations encounter difficulties in initiating, developing and managing partnerships. In particular, leadership and soft skills are mentioned as primary reasons for failure, alongside technical & functional competencies. We initiated a study on Supplier Relationship Management to gain a better understanding of the typical challenges involved and to determine how supplier capabilities drive competitive advantage.

Personal interviews and survey has given following key findings of the study.

1. Most important Supplier Relationship Management objectives are leveraging supplier capabilities, delivering cost savings and reducing supply risk exposure.
2. While the benefits of Supplier Relationship Management are acknowledged, the average Supplier Relationship Management maturity level is still low.
3. The top-three challenges respondents encounter are an overemphasis on cost reduction, a lack of specific Supplier Relationship Management competences and insufficient alignment between the business, procurement and supplier.
4. Technical/functional, relational and developmental competencies must be balanced and continuously developed.
5. Innovation, sustainability, leagility and resilience are seen as the key drivers for Supplier Relationship Management value creation.
6. The respondents indicate that there is a positive correlation between the presence of Supplier Relationship Management and an increase in market share, responsiveness to market changes, increased return on investment and shortening order fulfilment lead times.

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