

10 Fundamental Strategies and Best Practices of Supply Chain Organizations

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Abstract. One of the gratifying trends in supply chain management is that most companies are actively realizing the importance of their supply chains. The positive impact is that as supply chain professionals, we can not only achieve saving money for our company but also be a participant in improving company performance, effectiveness, and efficiency. Many companies and supply chain organizations, in fact, have begun taking steps to move towards implementing philosophies, methods, and processes that would be considered “world class or best practice”. Supply Chain organizational leadership is now challenged with taking the reins to lead their organization to new levels of achievement. Here are 10 fundamental supply chain initiatives that we believe are key for building a best of class supply chain organization.

Objective. To provide thoughtful and meaningful information regarding the key strategies and practices to build a road map for becoming a more effective supply chain organization.

10 Fundamental Strategies and Best Practices of Class Supply Chain Organizations.

This manuscript does not pretend to have a precise roadmap to follow in order to achieve desired supply chain maturity and excellence. It does, however, offer insight as to the key attributes that should be adopted or addressed. The 10 fundamental strategies and best practices discussed below are common elements that should be embraced. The sequence order of these “10” do not specify or recommend a higher vs. lower importance ranking, but does offer a systematic sequence when developing a scorecard of effectiveness in building a best of class supply chain organization. That said, lets examine these 10 initiatives.

The ten are:

1. Establish a governing council.
2. Align the supply chain organization.
3. Recruit supply chain professionals.
4. Set the strategic sourcing strategy.
5. Establish key supplier alliances.
6. Manage total cost of ownership.
7. Manage compliance and risk.
8. Reduce company-owned inventory.
9. Gather information on a timely basis
10. Establish processes and controls

1. Establish a governing council. As our first listed strategy and best practice, the establishment of a Supply Chain Governing Council is absolutely critical for the success of the company’s supply chain effectiveness. Who should be on this council?? Well, certainly the

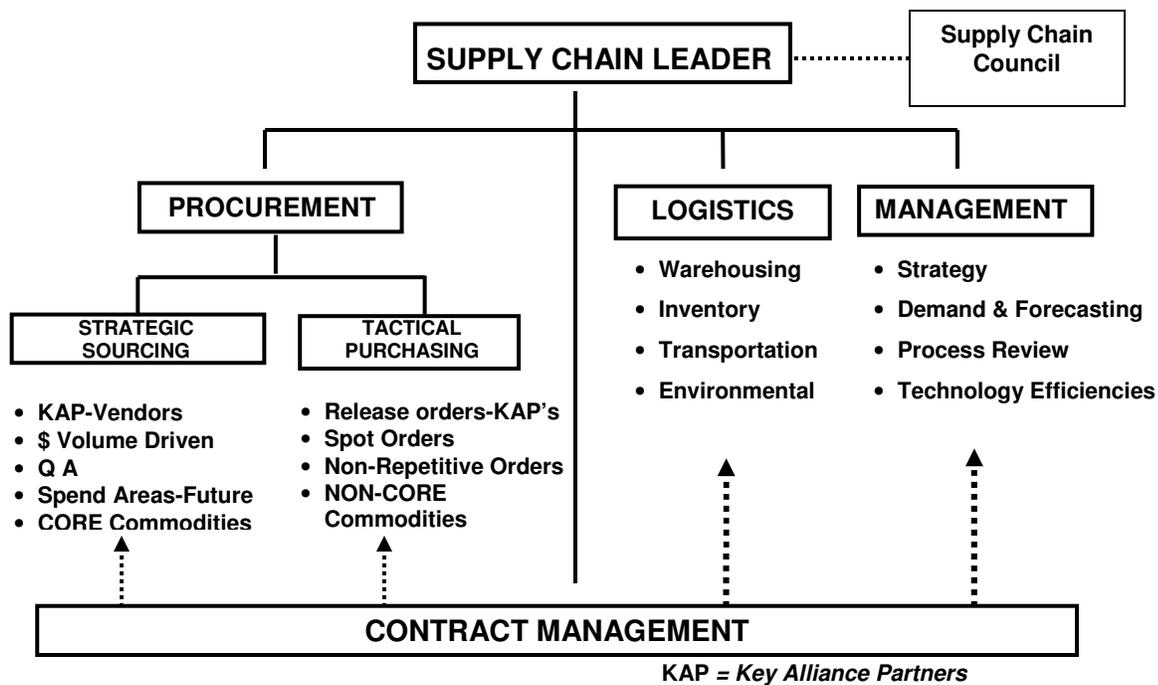
supply chain organization leadership but more importantly it should consist of members of the executive group, key internal business unit leaders, and other influential company leaders. Such a council is so very valuable in that it:

- ***Gives direction to and helps align supply chain strategy.*** It is very important that the supply chain strategy be in direct correlation with the company strategy. Often we see supply chain organizations that are struggling for recognition because their objectives differ from the stated company objectives. For example, if a high priority company objective is to improve or obtain a higher quality product sold to customers, then the supply chain leadership needs to ensure that supply chain activities are focused on quality and value. A disconnect will result if the supply chain organization is primarily focused on lowest cost with lesser regard to value and quality. The governing council can provide constant and consistent validation of strategy.
- ***Helps in removing barriers within the organization.*** Every company has these barriers that are usually those individuals or organizations who don't see or accept the value that supply chain can provide. The operational members of the council can help address, remove, or steer the supply chain efforts in such a manner to ensure that the supply chain organization is given the opportunity to perform.
- ***Fosters internal organizational buy-in that is needed to be an effective service organization.*** Once the organization sees that the executive leadership is fully embracing the supply chain organization, it is likely the key business unit stakeholders will follow suit and will be more willing to work with and support the supply chain efforts and initiatives.

2. Align the supply chain organization. Once the supply chain council has set a strategy, the supply chain organization must be prepared to execute. They must organize, prioritize and partner. One significant challenge has been how to organize the function to realize the full potential and benefit of being an effective organization. Certainly, organizational structures will take on different looks from company to company. For some companies, it is well served to embed a proficient supply chain professional in the internal business unit, and for others the most effective way is to provide a more centralized approach. And a "hybrid" approach of these two would also merit consideration. But a leading strategy of progressive companies is in centralizing strategy to gain consensus, with decentralized execution to improve service.

Regardless, the emerging trend in supply chain organizational effectiveness is to roll up under the supply chain leader the functions of Sourcing, Materials Management, Logistics, Forecasting/Demand planning, and Contract Management. One significant trend is that more and more organizations are organizing the Contract Management function under the leadership of the supply chain organization since the focus of agreements, supplier relationships, and corporate governance indicates that the logical placement of responsibility lies within the supply chain realm. The organizational chart on the next page is not listed to suggest this chart is correct for all companies, but more so to give a pictorial view of what today's modern organization may look like.

Supply Chain Management Organization



3. Recruit supply chain professionals. As the supply chain function evolves and as we have matured as a vital part of our company's management team, the overall SCM organization skills and knowledge must also be elevated. A study from CAPS Research of Arizona State University summarizes the top **skills** required: ethics, interpersonal communication, negotiation skills, project and team orientations, and strategic thinking. The study also describes the critical **knowledge** required: supplier relationship management, total cost analysis, purchasing strategies and plans, and supplier analysis.

To expand the capability of their team, many supply chain leaders are recruiting, internally as well as externally, for two kinds of skills:

- **Technical skills.** Leaders are recruiting for analytical skills to assist sourcing teams, new procurement skills (such as contract management), and subject matter expertise in a wide range of product and service categories.
- **Project Management skills.** In addition, leaders are recruiting experienced professionals with a partnering and internal marketing mindset. They are looking for professionals who can partner with business unit leaders to: (1) follow their customers' changing needs, and (2) find key suppliers who can continually address those changing needs.

4. Set the strategic sourcing strategy. Strategic sourcing is a cornerstone of supply chain management. A successful **collaborative** strategic sourcing initiative not only ensures availability of supplies, but will result in the obtainment of overall lower total cost, streamlined processes, and increased responsiveness to customers' changing needs.

Strategic sourcing is not just a purchasing department initiative. It requires input from all functional areas such as finance and accounting, engineering, operations, maintenance, safety/health/ & environmental, quality assurance, and internal business unit team members that will contribute to the initiative's success. That's the essence of the collaborative side and the success of achieving true buy-in from our internal clients is getting them involved in the decision making process. After all, aren't our business units our customers?? And shouldn't they be actively involved in not only assisting with the decision making process, but more importantly giving key feedback and information regarding their objectives and strategies?

5. Establish key supplier alliances. The ultimate success of strategic sourcing depends on the team's ability to select key suppliers and to manage supplier alliances for critical spend areas. Perhaps one weakness in most strategic sourcing efforts is the follow through with the selected suppliers. In most circles today, this final step has traditionally been called "supplier relationship management." In reality, perhaps a more appropriate term should be "Alliance Management" since supplier management has a tendency to infer one way communication (telling the supplier how to do it) vs. the correct mindset of two way communication which requires both buyer and seller to team together (Alliance) to manage the relationship.

A primary goal of most supply chain organizations is to channel their relationships with their key suppliers so that maximum focus can be achieved for the major or core spending areas. With a well founded and fundamentally sound Alliance Management program in place, supply chain organizations are equipped to use the talents of the supply base to not only create sustained value, but constantly seek continuous improvement. The three primary objectives of an effective Alliance Management program with key suppliers are:

1. Provide a mechanism to ensure that the relationship stays healthy and vibrant,
2. Create a platform for problem resolution, and
3. Develop continuous improvement goals and objectives with the objective of achieving value for both parties.

6. Manage total cost of ownership. Strategic sourcing shifts the company's and team's focus from just looking at the purchase price, to understanding the dynamics of the total cost of owning or consuming a product or service. For significant spend areas, procurement teams are abandoning the outmoded practice of receiving multiple bids and selecting a supplier simply on price. Instead, they consider many other factors that impact the total cost of ownership. In fact, acquisition costs accounts for only 25% to 40% of total cost for most products and services. The balance (and majority) of total cost is comprised of operating costs, training costs, maintenance costs, warehousing costs, environmental costs, quality costs, transportation costs, and consideration for the salvage value. Identifying total cost requires cooperation and input from both the buyer and seller organizations. It requires: (1) looking at the entire process of procurement and consuming the product or service, and (2) asking our suppliers as well as our internal business units "How can we work together to reduce the total cost of ownership?" Establishing a Total Cost of Ownership mindset is a goal that the supply chain organization needs to embrace and perpetuate throughout the entire enterprise.

7. Manage compliance and risk. In actuality, supply chain leaders and their teams do negotiate significant potential savings during the sourcing process. However, the reality is that in most cases companies never do fully realize the full extent of these savings. The reasons are varied, but include a lack of communication of contract terms within the organizations and a failure to monitor contract compliance. All too often the fully executed contract is filed away in some drawer and forgotten. In a recent Aberdeen survey of supply chain leaders, the question raised was “*how do you manage your company’s contracts?*” The answer was startling in that two thirds of the respondents stated that “*we can’t even find the contracts much less manage them.*”

More and more companies today are moving the contract management responsibility to the supply chain organization rather than having it in legal, finance, or operations as organizations have come to realize the importance of contract management. A driving force of this movement to the supply chain organization is the need to ensure the contracts are collected and maintained in a central repository. Furthermore, the migration of the contract management function to the supply chain organization allows the supply chain leader to more effectively leverage spend particularly in the areas of services, where there is a greater opportunity for cost reduction and risk mitigation.

Reducing maverick buying and optimizing the value of new and existing contracts is a fundamental tenet of supply chain organizations. Nothing can be more embarrassing than establishing agreements only to find out that they are not being utilized as expected. Leveraging compliance should be at the top of every supply chain leader’s goals and objectives.

8. Reduce company-owned inventory. With key suppliers in place and delivering against their contracts, supply chain organizations should strive to constantly review their inventory levels and to keep them at an optimized level. Inventory is money, and the financial team is constantly looking for new ways to improve the bottom line and reduce working capital. Supply chain teams often begin by defining the “real” cost of holding that inventory. This cost is often higher than the generally assumed 20% to 25%. In fact, ISM has compiled documentation to indicate that many times the inventory holding cost could be up to 40% or higher of the cost of the item. To achieve this objective, Vendor Managed Inventories (VMI) is a logical scenario and alternative. But with the current sellers market, VMI’s can prove to be challenging in regards to lead times, deliverability, logistics, etc. And this puts more emphasis on demand planning and forecasting to assist in achieving the goals of this best practice.

9. Gather information on a timely basis. In all of the above initiatives, supply chain strategy is set and executed. One traditional “gap” or stumbling block has been the ability of supply chain organizations to retrieve critical and detailed data from the ERP or accounting system. The need for timely, complete and accurate information is the foundation for understanding how, when, where, and for what are we spending our money. Yet, most organizations do not have the mechanism to retrieve the necessary data and information from their various information systems. And the difficulty expands exponentially where disparate ERP or other information systems are in play and do not have the means to “speak” to each other. For organizations in this situation, the decision must be made whether to combine the systems into one, or to keep separate. Each company will have differing approaches to this issue, and a potential solution may be that of considering the deployment of data cleansing software to

assist in the gathering of good, reliable data. Sounds simple? Not really as time and time again, companies struggle with the ability to gather needed information and they view this process as complicated and time consuming. Best of class supply chain organizations must find a way within their information systems to retrieve the meaningful data.

10. Establish Processes and Controls. In our high tech world, we see an inherent fallacy Of companies who first select technologies to make them more efficient and then structuring the processes around the chosen technology. In reality, the focus should be on “what technology is going to help me become more efficient.” The answer will come when you first review the processes under consideration, determining the needs and then select the technology that best satisfies those process needs. Don’t select and install the technology first and then structure the process around the technology. That is a recipe for disaster. Technology should be considered as the tool to help increase efficiency, not the focal point of what is to done.

And it’s not only the processes and technologies that must be in sync, but we also need to review our supply chain policies and procedures as well. Most, as we know, are often found to be culture driven, and do not accurately reflect today’s environment. Review them constantly, and bring them up-to-date keeping them realistic and easy-to-understand and follow.

SUMMARY

The ten initiatives described above represents a framework of strategies and best practices that best of class supply chain organizations should strive to achieve. One issue at hand is that over the past several years, we have witnessed a changing market environment and that our effectiveness as supply chain organizations revolves around short term flexibility with long term maturity. And we must remain flexible in prioritizing these initiatives in order to meet the challenges of the day.

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