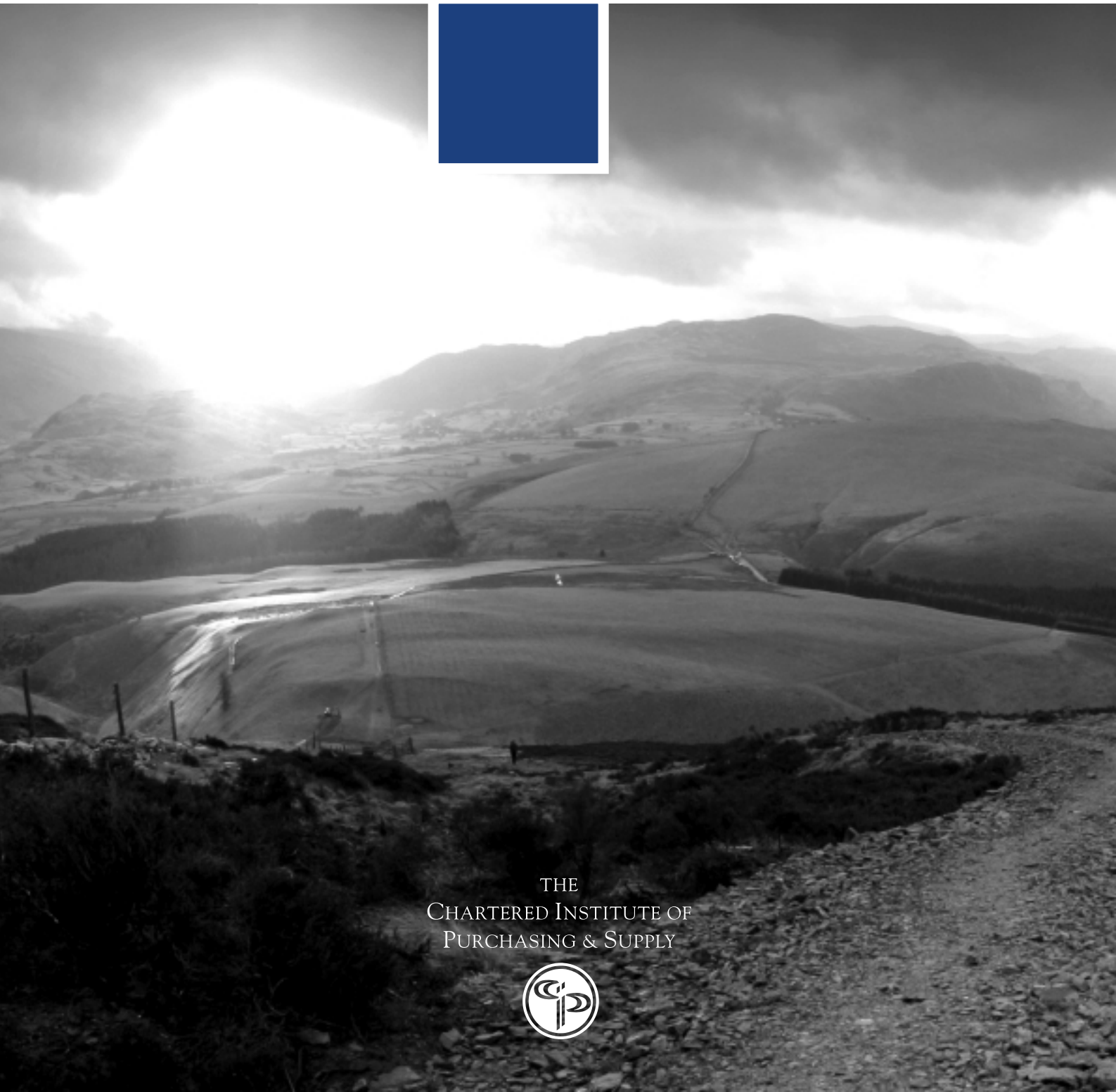




Selling the benefits of purchasing



THE
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Welcome to selling the benefits of purchasing



Dear Colleague

In today's high-pressure environment, the role of purchasing and supply management has taken on an air of additional importance. For organisations of all types, the challenge is to improve the quality of products and services while driving down costs.

In recent times CIPS has been asked to provide help on how best to meet the challenge faced by purchasing professionals to "sell" the benefits of their role and function to leaders within their organisations. Many members are concerned that CEOs do not always appreciate the benefits that good purchasing and supply management can bring to their business. This guide provides just one route to help educate business leaders that good procurement practice can help significantly improve the performance of their organisation and achieve success.

You should decide how best to use the guide from your own perspective and apply some of the messages to the particular situation in your organisation. For example, is CSR a major issue or is product innovation the key driver? Whatever is at the top of your CEO's agenda you need to contextualise the information contained here to suit those particular drivers. Which of the benefits listed in the guide are most appropriate to use when shaping your message in relation to the key priorities for your organisation?

So digest the information provided, research and understand your organisation's strategic imperatives, answer for your own situation the questions listed overleaf and then decide how best to communicate the appropriate messages and benefits to your internal customers.

Remember, that success will come from a position of understanding – without it you could be faced with a recipe for disaster.

Good luck.

A handwritten signature in blue ink that reads "Kw James". The signature is written in a cursive style.

Ken James
Chief Executive Officer

In today's high-pressure environment, the role of purchasing and supply management has taken on an air of additional importance. For organisations of all types, the challenge is to improve the quality of products and services while driving down costs.

Why purchasing is key – the message to business leaders

REALITY CHECK

Can you answer these questions?

- Do you have a really good understanding of the corporate strategy/plans/priorities within your organisation?
- How is this being interpreted by each department? What do they each see as the key drivers/measures of success?
- What are the real challenges in delivering organizational plans?
- What is going well? What are the main challenges the organisation is facing now and what are those just around the corner?
- What are the particular problems/opportunities for the CEO and key leaders of change/business development?
- Who are the powerful influencers on business success? How do they inter-relate/influence the agenda?
- What is the background/business interests of key influencers in the organization? Which language, culture etc do they best relate to? For example, when speaking with the finance director are figures the only language understood? Who could be your champion at a senior level?
- What do they think about purchasing and supply management, and about you and your colleagues? Can they answer the checklist at the end of this guide? If not, how do you get the answers on their behalf to help inform them about the benefits?
- How can purchasing and supply management really contribute to dealing with hot issues and major business challenges? What benefits can you bring relating to cost, innovation, security, reduced risk, improved quality, etc?
- How should you best communicate your messages, to whom, how, which language, which benefits, etc? What would you say to the CEO to really get his/her attention?
- What would you start in terms of delivery to give yourself, your colleagues and your activity a level of credibility?
- What would make business leaders believe in the benefits – case studies, examples of achievements to date?
- How can you make yourself heard against a busy agenda? How can you really add value to the overall organizational success?

Now read on.

Cutting costs, improving efficiency

Over the past few decades, efforts to cut costs have tended to focus on headcount. The elimination of unnecessary activities, productivity drives, automation and contracting out (or outsourcing) have all seen workforces shrink. Although right and necessary in many cases, such programmes have obvious drawbacks.

SUMMARY

- Organisations spend 30-80 per cent of turnover with suppliers
- Improvements in purchasing and supply management will have a direct impact on the bottom line and on service and on reputation
- Only a co-ordinated, boardroom-led approach will deliver optimum benefits
- Purchasing and supply management as an integral part of organisational strategy will deliver real value/differentiation to your organisation.

They increase short-term costs, are time-consuming to administer and, if not properly managed, run the risk of creating severe staff morale problems – possibly leading to industrial action. They can also store up trouble for the future: if you let good staff go you might have a skills crisis when things pick up again. The emphasis on personnel reduction has been combined with action to reduce the number of facilities required to run the business. This has resulted in the amalgamation or shut down of manufacturing plants and sales, service and administration offices.

In lots of organisations, such 're-engineering' is now complete. Having exhausted opportunities to save money by cutting staff numbers and rationalising operations, directors are having to look elsewhere.

Procurement is the obvious place. This is because the value of bought-in goods and services is usually a high percentage of turnover or revenue. The amount varies from 30 to 80 per cent. The figures per sector are as follows:

- general goods manufacturing and retail – 65 per cent to 70 per cent
- electronics and aviation – up to 80 per cent
- the process sector (pharmaceuticals, oil and food industries) – 30 per cent to 40 per cent
- the service sector (banking and insurance) – 30 per cent to 40 per cent.

In both the process and the service sectors, the values will equal, if not exceed, the amount spent on payroll and facilities. In the public sector, expenditure on goods and services is in the region of 50 per cent of total expenditure. It is clear, then, that cutting the cost of in-bought goods, services and capital items can make a dramatic improvement to an organisation's bottom line. A simple calculation shows that if an organisation saved just 10 per cent of its total spend on purchases, its profit would increase by five per cent of turnover, nearly doubling to 11 per cent.

REALITY CHECK

What is the ratio in your own organisation?

CASE STUDY: BRITISH AIRWAYS

It has been a difficult few years for the world's major airlines. Even before two hijacked planes flew into the twin towers of New York's World Trade Center on 11 September 2001, economic downturn was hitting them hard as demand for business travel fell away.

Since that fateful day, things went from bad to worse as a result of the deteriorating business climate, the threat of further terrorist attacks, the war on Iraq and panic over the SARS virus. In February 2002, British Airways responded to this crisis with a new business plan entitled "Future Size and Shape". The plan called for 13,000 job losses and annualized cost savings of £650m a year by March 2004. In February 2003, it stepped up the pressure to reduce costs by setting a target of an additional £450m in savings.

This has put the airline's procurement function firmly in the hot seat. At the company's annual investor day, BA's procurement director, Silla Maizey, was asked to address major shareholders and financial analysts for the first time, explaining how the airline will shave £300m, or 10 per cent, off its annual purchasing bill by 2005. Good progress has already been made with £95m of procurement and IT

savings signed off by the end of March 2003.

These savings have been achieved partly by negotiating lower prices through electronic auctions (which has saved over £20m) and by channelling a greater proportion of spend through fewer suppliers. BA has already cut its supply base from 14,000 to 5,000 and aims to further reduce it to just 2,000.

But costs are also now being taken out by managing the internal demand for goods and services more effectively, and by reining in specifications so that money is not wasted on unnecessary features. This has meant creating a different mindset among the 200 members of the procurement department and following a more rigorous and consistent approach to purchasing.

"Historically through price, we were able to deliver two to three per cent reductions in the external cost base," notes Maizey's boss, BA's chief financial officer, John Rishton. "Through deeper implementation of the strategic sourcing process, we are able to consider savings of 10 per cent." Procurement, Rishton concludes, is now "recognised as essential to our business, not just an 'add on' support department".

Geraint John

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Creating value, improving effectiveness

Raising the standard of purchasing and supply management can create benefits far beyond price reductions for goods and services. In many instances, it is the ability to get suppliers and the supply chain to perform in ways that serve the purchasing organisation better that provides the real benefits.

Few things illustrate this more than building and refurbishment contracts. Suppose, for example, you are a retailer, about to refurbish your sites. You want the work to be done well to guarantee the maximum long-term return on your investment, but you want your outlets to be able to re-open as soon as possible. By carefully evaluating the supply market, by inviting the right companies to tender for your business and by working together with the selected contractor, you can get the value for money you need and keep the number of lost trading days down to a minimum. Conversely, if you fail to manage the procurement process in this way the project is likely to drift on, incurring more costs and losing you more money.

Good relationships with suppliers also enable existing products to be improved or enhanced and new products or services to be brought to market quickly and efficiently. In some cases, suppliers can be brought into the product-design process. A kind of technology transfer can take place, whereby purchasers and suppliers swap skills in order to achieve product innovation. The international audio equipment manufacturer Bose, for example, has used supplier in-plant personnel as authorised links between its design teams and its suppliers. This has allowed it to free members of staff for other purchasing duties such as communications and material cost reductions. If your suppliers are your partners, you can introduce joint cost-cutting initiatives. The DIY retailer, B&Q, for example, has made a point of trying to eliminate packaging waste in its supply chain. This not only saves everyone money – packaging and transportation costs both fall – but also helps the company fulfil its pledge to the consumer to be environmentally aware.

REALITY CHECK

What case studies/examples do you have which can reinforce your particular sales pitch?

REALITY CHECK

Do you have a good process for defining appropriate supplier relationships by product category?

The purchasing and supply management challenge

CASE STUDY: PLYMOUTH HOSPITALS NHS TRUST

NHS hospitals are under intense pressure to treat more patients, more quickly, and to make more effective use of taxpayers' money.

The service provided by the cardiothoracic department at Plymouth Hospitals NHS Trust, which serves 430,000 people in west Devon and east Cornwall, has been significantly improved by an innovative approach to purchasing key products. Heart disease is the UK's biggest killer, and demand for treatment is growing by more than 30 per cent a year. Waiting lists are long; budgets are severely stretched.

Despite this, the department had, until the new initiative began in 1998, failed to take a strategic approach to procurement. "Purchasing activity was highly fragmented, buying decisions were made ad hoc by clinical staff, and there was little or no negotiation with suppliers," explains Ian Shepherd, the trust's director of purchasing and supply. Twelve hundred products were being purchased from 35 different manufacturers. Instead of following the old route of awarding contracts product by product, the team of clinicians and purchasing experts decided to put out one invitation to tender for all the department's core requirements, including pacemakers, heart valves and diagnostic devices, representing around 80 per cent of its £9m annual expenditure.

The results have been impressive. Cost savings of £1.7m, or 19 per cent, have been made against a target of 10-15 per cent. The average cost of treating a patient has fallen from £496 to £258, enabling an extra 450 people to be treated. There is far more cohesion in purchasing activity. The department now purchases 560 products from just three primary suppliers. The burden on administrative staff is lower; the clinical risk for doctors and nurses using the equipment is reduced.

Shepherd has now expanded his purchasing team and is beginning to introduce similar philosophies to other departments, not only at the Plymouth Trust but throughout Devon and Cornwall. Within the next five years, he hopes to achieve additional savings of £15m. "We are challenging the status quo in the health service, thinking differently about how goods and services are purchased," he says.

Looking further ahead, the purchasing department is talking to equipment suppliers about the potential of robotics and other automated technologies to improve the next generation of NHS hospitals – whether it be assisting with surgery or simply moving products around.

Geraint John

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The purchasing and supply management process will only deliver optimum benefits if it is a coherent whole, if the disparate and often dispersed people involved in purchasing decisions work together for the good of the organisation. You cannot simply bolt-on a discrete purchasing and supply management function and hope for the best. Nor can you assume that the diverse groups involved in the procurement process will come together naturally to work things out – experience shows that each function pursues its own interests to the exclusion of others.

A co-ordinated, boardroom-led approach is needed – otherwise supply failures and excessive costs are likely to result. Purchasing and supply management decisions must be consistent with the organisation's objectives and culture and ethos and be compatible with its structure and geographical reach. The board should resist jumping on the bandwagon of purchasing fads and fashions and rather ask: does this suit us?

There are many types of purchasing and supply management strategies. Good purchasing and supply management people use the right ones, at the right times. And they usually discharge their responsibilities best by working within cross-functional teams.

REALITY CHECK

Do you have buy in at all key leadership and departmental levels?

Benefits of effective Purchasing and Supply Management

There are many benefits to be gained through effective purchasing and supply management including:

- lower costs and better value for money
- security of supply – certainty that vital raw materials and components will continue to flow to the organisation
- better risk control – sourcing policies that do not damage the company's reputation, conflict with social and environmental responsibilities or contravene legislation
- leverage – the ability to negotiate better deals from suppliers
- quality improvements – supplier relationships that make products and services better and reduce time to market
- process efficiency – the use of electronic and technological tools to improve ordering and related processes
- continuous improvement with suppliers – encouraging innovation.

REALITY CHECK

Think about how you can contextualise the benefits of effective Purchasing and Supply Management to meet the particular circumstances faced by your organisation

The key Purchasing and Supply Management tasks

The role of the director responsible for purchasing and supply is to:

- ensure the purchasing and supply management perspective directly relates to business needs
- select and implement the appropriate strategies to support the organisation's goals
- advise on, and help to implement, strategic changes such as mergers and acquisitions, making sure synergies are exploited and the maximum commercial leverage obtained
- become a good internal consultant to the individual business functions
- arrange appropriate outsourcing of corporate services – with the objective of delivering significant quality improvements and reductions in costs
- set continuous targets for improvement, providing advice and guidance for colleagues and those with significant purchasing responsibilities
- use a range of tools, methodologies and approaches that can add significant value to the organisation with year-on-year improvements
- develop the ability to analyse, evaluate and recommend on risk
- become involved in conception, design and implementation of work systems and processes
- keep up with developments in purchasing and supply management through networking
- keep abreast of new techniques.

Getting started

Re-orienting purchasing and supply management in your organisation is not easy. It takes time and demands commitment and might require investment in training and technology. The starting point is a review, an audit of current procedures. Once the review is complete, you can decide on the action that needs to be taken and start to move forward.

Conclusion

Effective purchasing and supply management helps organisations to win – and sustain – competitive advantage. Provided it is, from the outset, backed by the very top, upgrading the purchasing and supply management process can be one of the best investments an organisation ever makes.

CHECKLIST FOR THE CHIEF EXECUTIVE

- 1 Do you know how much your organisation is spending externally?
- 2 If yes, do you know how much is spent on each category of spend and with which supplier? (A category is a range of purchases – eg. energy, IT.)
- 3 Do you know the total cost of the purchases you make, rather than just their price? (Such costs will include: the costs of the procurement/payment processes; the whole 'lifecycle' costs of major purchases – eg. machines, buildings.)
- 4 Do you know how much value your suppliers provide and create for your organisation's success and reputation?
- 5 Do you know who your key suppliers are?
- 6 Do you have pro-active, close relationships with your key suppliers?
- 7 Do you understand the risks inherent in the purchases you make? Are you managing them effectively?
- 8 Do you know what you should outsource and what you should not outsource?
- 9 Are you outsourcing services successfully?
- 10 Are you managing suppliers of outsourced services successfully?
- 11 Do you know what your purchasing strategies are; are they aligned to your business strategies?
- 12 Do you have appropriately skilled people developing and managing your purchasing strategies?
- 13 What proportion of your external spend is managed by your purchasing professionals?
- 14 If the answer to the last question is not 100 per cent, why not? And, what are you doing about it?
- 15 How do you support your purchasing people to ensure they achieve appropriate business benefits?
- 16 Do you direct your purchasing people to limit their focus to reducing prices by x per cent each year or do you direct them to achieve cost-effective, risk-controlled added value?

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Easton House, Easton on the Hill, Stamford, Lincolnshire PE9 3NZ, UK

Tel: +44 (0)1780 756777 • Fax: +44 (0)1780 751610 • Email: info@cips.org Web: www.cips.org



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