Management of Supplier Innovation for Competitive Advantages

Purchasing as a Tool for Growth
Michel Philippart

- 7 years in consulting
  - Booz Allen Hamilton
  - McKinsey

- 7 years in international purchasing development
  - PepsiCo / Frito-Lay
  - Scotts

- Today working independently - “Sourcing Plus”
  - Consulting
  - Training / Teaching / Coaching
  - Interim
  - Site: www.sourcing-plus.com
Is Purchasing a Basic Survival Skill?

- Your best competitors work on purchasing as hard as you do
- … and obtain similar price decreases
- … that the sales force must give away to stay competitive
- … which does not improve either competitive position or profitability
- Those who cannot follow disappear. Is purchasing a basic survival skill?
Or Can We Leverage Supplier Relation to a Hidden Competitive Advantage

**Competitive Advantage**
- Open to competitor scrutiny
- Largely hidden

**M&S**
- Price premium
- Product positioning
- Sales activity/market share
- Quality
- Product performance
- Productivity

**Production**

**R&D**
- New product introduction/Patents
- Innovation rate

**Purchasing**
- Privileged supplier relationship/development
- TCO/value generation across business system
- Unique capabilities
Exclusivity Can Generate Profits Much Faster Than Price Decrease

Increase sales revenues by 10%: Contribution: +200k€

Decrease cost of key component by 10%: +68k€

Market Share 50%!
Agenda

1. Revenue focus in Purchasing
2. Levers of supplier contribution
3. Discussion
• Everybody negotiates hard
• Differentiation is limited as many good companies leverage the same approaches
• Competition for market share quickly erases the negotiation benefits as they flow to the end users

Can I decrease my costs continuously?

Do I need to outsource or maintain internal capability?

How do I speed international growth safely?

Who will provide the innovation that will grow my markets?
Across Industries

Retailers
- Can suppliers help me reduce working capital?
- Can suppliers help me improve store appearance?
- What supplier strategies will allow me to differentiate from other retailers?

Luxury Goods
- How can I secure strategic raw materials in short supply?
- How do I control and improve the performance of essential subcontractor craftsmen?
- How do I insure that my best subcontractors are not attracted by competitors?

Packaged Goods
- How do I leverage supplier innovation to differentiate beyond advertising?
- How do I speed up development of countries where I have acquired local players?

P&C Insurer
- How to move claim related purchasing from an administrative task to a way of securing competitive advantages
  - Better, faster claim processing
  - More replacement options
  - Regional agreements with suppliers

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Expanding the Role of Purchasing

<table>
<thead>
<tr>
<th>Impact</th>
<th>Profit</th>
<th>Tactical</th>
<th>Strategic</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenues</td>
<td>Supplier Management for growth</td>
<td>• Source of innovation / unique capabilities and raw materials</td>
<td>• Faster introduction to new markets</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>• Exclusive knowledge capture and leverage</td>
</tr>
<tr>
<td>NA</td>
<td>Traditional Purchasing</td>
<td>• Leverage scale</td>
<td>• Simplify</td>
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<tr>
<td></td>
<td></td>
<td>• Negotiate</td>
<td>• Optimize TCO*</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Divide and conquer</td>
<td>• Increase transparency, knowledge of supplier markets</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• etc.</td>
<td>• e-Purchasing</td>
</tr>
</tbody>
</table>

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Benefits of Each Level

Focus of Supplier Management

- Differentiation and lifecycle market value
- Total cost of ownership
- Negotiation

Benefits of Supplier Management

- Exclusivity pricing
- Full cost optimization
- Price
- Value

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### Potential Impact of Supplier Development Across Industries

<table>
<thead>
<tr>
<th>Industry</th>
<th>Development</th>
<th>Manufacturing / Back office</th>
<th>Distribution / Delivery</th>
<th>Marketing and Sales</th>
</tr>
</thead>
<tbody>
<tr>
<td>Automotive</td>
<td>●</td>
<td>●</td>
<td>●</td>
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<tr>
<td>Consumer Products</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
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<tr>
<td>Financial Services</td>
<td>●</td>
<td>●</td>
<td>●</td>
<td>●</td>
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<tr>
<td>Fine Chemicals/ Pharma</td>
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<td>●</td>
<td>●</td>
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<tr>
<td>Electronics</td>
<td>●</td>
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</table>
### Examples Across the Value Chain

<table>
<thead>
<tr>
<th>Development</th>
<th>Manufacturing</th>
<th>Distribution</th>
<th>Marketing and Sales</th>
</tr>
</thead>
<tbody>
<tr>
<td>Packaging and flavoring suppliers develop and produce winning differentiation from competitors (Frito-Lay)</td>
<td>Equipment manufacturers co-develop exclusive production line technology that increases yield and quality (multiple)</td>
<td>Distribution partner makes product ubiquitous, with lower working capital and more availability than competition (Dell)</td>
<td>Effective promotion design and production provide market pull (McDonald)</td>
</tr>
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<td>Global branding drives complexity reduction, more effective promotion, etc (Multiple)</td>
</tr>
</tbody>
</table>
Agenda

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International Suppliers Contribution

Global Supplier Leverage
- Leverage actual suppliers for expansion
- Identify local suppliers in new regions
- Develop suppliers in new regions as global alternatives

Seamless information leverage
- Shared understanding of consumers
- Integrated supply chain optimization
- Production to consumer constrain management

Supplier Innovation
- Product innovation
- Service improvement
- Product line extension

Supplier Contribution
- Unique Skills

Knowledge

International Growth
Skills Lever

Capture of supplier’s unique assets (physical or intellectual) to grow current markets

- Involve Purchasing with marketing when identifying consumer demand currently not satisfied properly
- Develop supplier capability to provide it
- Manage relation with supplier to isolate new capability from competitors
Example: Consumer Goods

- Identify need for packaging with better barrier properties to improve freshness
- Consolidate European volume to key suppliers
- Capture competitive advantage
- Jointly develop new technology
- Produce on new, dedicated lines
- Harmonize across Europe to lower costs

Purchasing leads cross-functional teams to lift company potentials
Impact of Supplier Innovation Capture

- 70 days without flavor variation vs. 15-30 for the competition
- 70/30 consumer preference in blind test
- Capture of category leadership in key markets
- 30% cost reduction over 3 years
Win-Win Supplier Relationships

Purchaser
- Invest volume
- Provide end user market knowledge
- Co-develop specifications
- Commit fair return on supplier assets leveraged

Supplier
- Allocate key capacity for exclusive usage
- Target specific markets for innovation
- Dedicate best staff (research/account service, etc.)
- Open books

Win-Win Supplier Relationships
Influence supplier development and leverage supplier structure for global expansion

- Identify supplier’s capabilities in existing markets that are necessary to develop / improve competitiveness in new markets
- Steer supplier’s development to match
- Scan suppliers in new markets for capabilities that can be leveraged in existing markets and insure transfer
Global Solution Development

From

Need identified locally  Solutions  Synergies

Customer needs expressed at local / country level  Local / country solutions are developed  Synergies and global opportunities are analyzed at a later stage

To

Commonality between local needs identified  Core Solutions  Customization  Synergies

Local / country understanding integrated to find commonality  Standardized approach provide core offering  Global solutions are fine tuned to local needs if necessary. Specific developments are compiled and made available to other markets  Suppliers are managed globally
Example: Consumer Good Industry

Complex flavor

Home Base Region 2 Region 3 Region 4

Price index

Price per Unit

Region 4 Supplier

Price: -42%

Impact: +13%

Home Base Supplier

Consumer Appreciation

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Global Purchasing Leverage

- Global expansion via M&A or green field
- Increasing global trade
- Regional integration to capture competitive advantages

Purchasing Leverage
- Development of new regional supply base
- Extension of current supplier base into new regions
- Leverage of suppliers with global assets
- Regionalization/Globalization of Purchasing
Leverage of New Suppliers

- Integration of suppliers from new regions into supplier network and potential use in home market
- Improve knowledge base about cost of materials, capabilities, etc.
- Targeted identification and development of new suppliers for global use
- Relation with suppliers that are growing via M&A

- Traditional market base leverage
  - Improved supply options
  - Access to new production methods
  - Better information
Jointly manage information from development to consumer

- Targeted development
- Seamless transfer of information from POS to supplier to integrate supply management
Innovation Through Co-Development

Percent of R&D budget spend on co-development with suppliers

Future development
Today's innovators
"The pack"
Relevance of supplier-based innovation

Steel
Commodity Chemicals
Consumer Products
Automotive

Middle
High
Very high

0
20
40
60
80
100

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Example: Restaurant Chain

Purchasing leads cross-functional teams to lift company potentials

Identify safe low cost toy as key traffic builder

Capture growth through « children appeal »

Build relation with properties for continuous stream of toy themes

Design safe toys around themes

Assemble external team of designers and safety experts

Produce in ethical but low cost sources

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Identify safe low cost toy as key traffic builder

USA

USA

Far East
Impact of Supplier Innovation Capture

- Market dominance worldwide
  - Key competitor being sold
  - Other competitors marginal / local players

- Higher return than competitors

- Only chain to grow
The Role of the Supplier Management Team

<table>
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<tr>
<th>Scanning</th>
<th>Identifying</th>
<th>Capturing</th>
<th>Isolating</th>
</tr>
</thead>
<tbody>
<tr>
<td>What are the relevant innovations that can serve my value chain</td>
<td>Innovation scan ventilation suppliers Venture capital</td>
<td>Business case development Win-win proposition Implementation</td>
<td>Constrained assets Contractual exclusivity Co-ownership</td>
</tr>
<tr>
<td>How to access them?</td>
<td>Product / service match</td>
<td>Culture match</td>
<td>Support that innovator needs to deliver</td>
</tr>
</tbody>
</table>
Requirements

- Purchasing integrated at n-1 level, part of CEO leadership team
- Purchasing not driven only by price variance but by overall contribution
- Purchasing is a high value added function staffed with trained professional. They have limited or no tactical tasks such as supply coordination
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