



Supply Management 2006: Stay Out of the Dog House by Setting the Right Expectations

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With 2005 soon ending on the Western calendar while the Chinese calendar starts the Year of the Dog on January 29, we thought it was a great time to look at management objectives to keep you out of the dog house the coming year.

While supply management priorities should change based on market factors, recent survey data shows that most companies are setting targets based on internal measurements, leaving only supply management leaders aligning goals based on market conditions.

Closing the gaps

In a recent study of supply management and IT executives, 264 North American respondents reported their largest gaps in current performance:

- Reliable supply
- Understanding and measuring customer or end-user demand
- Supply analytics and visibility
- Cost savings and avoidance measurement and attainment

These gaps convey that supply management is more than cost control, yet most organizations that we speak to are absorbed only in cost targets and miss a more balanced approach.

Areas of concern

Here are two survey data points that cause us to worry:

- **Objectives are set based on internally driven cost reductions**—In the study, 44% of cost reduction targets were dictated by the CEO, COO, or CFO for 2006 based on a percentage of historical spend in direct, indirect, services, and Maintenance, Repair, and Overhaul (MRO). Respondents indicated that third-party benchmark data and inflationary indexes are seldom used. This is problematic with the rising commodity prices and supply reliability issues we expect in 2006.
- **Monitoring based on purchase price variance**—We also expect 2006 to be rocky with inflationary spikes in major commodities. This will be problematic for organizations that are focused on purchase price variance, but not market conditions. In the same study, 37% of companies said they are measured by monthly and quarterly Purchase Price Variance (PPV), 17 % on annual PPV, and 15% monthly or quarterly contract compliance. Annual contract compliance is seldom used.

With rising market inflation and increasing issues with supplier reliability, it is time to act now to ensure that your career in supply management does not go to the dogs. Targets and controls that do not reflect market conditions will yield a miss in expectations and supply chain performance.

Holiday reading

As you set out on the holidays to tackle these issues, we recommend two books to help streamline key initiatives, improve supplier reliability, and improve tracking and monitoring of supply management savings:

- *Straight to the Bottom Line*, by Robert Rudzki, Douglas Smock, Michael Katzorke, and Shelley Stewart, is about better understanding the relationship between supply management cost structures, Return on Investment (ROI), risk management, compliance and governance, and customer satisfaction. It is also a good holiday gift for your boss if you are struggling to get consensus on the relationship and importance of supply management to the bottom line.
- *Collaborative Sourcing: Strategic Value Creation through Collaborative Supplier Relationship Management*, by Michel Philippart, Christian Verstraete, and Serge Wynen, offers an insightful framework for developing supplier relationships. The model provides good insight on the classification of supplier interactions: traditional procurement, procurement collaboration, supply chain collaboration, value chain integration, and sustainable partnership. The five represent the maturing of the supply management marketplace, and each is a foundation for the progression to the next stage of capability.

Enjoy the holidays with a glass of wine, a roaring fire, and some great books. If you stumble onto a good book on supply management and want to share it, please forward the title to me at mnorthrizza@amrresearch.com.

