Procurement as a Value Lever

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Introduction

Companies across industries are adjusting to volatile market conditions and reduced demand, leading executives to focus on cost reduction. The procurement and supply chain function serves as a key lever for improved cost performance, and many companies have launched initiatives focused on cost optimization.

However, a narrow focus on costs can miss the bigger value opportunity. Leading companies are balancing other factors, such as enhancement of revenue through supplier capabilities and planning for the potential of constrained supply markets in the future, to gain sustainable value.

Our Mission

Our goal is to assist our clients drive structural improvements in the procurement function, to make it a source of value and innovation. We help them assess where they are, advise on where they need to be, and provide support through the procurement transformation journey. Our approach balances enhanced business performance through better spend management and productivity gains with internal controls and risk management.

Practice Overview

We have over 250 experienced, supply chain resources globally across all major industries and sectors.

Our professionals understand the interconnectedness of the functional processes and capabilities of enabling tools. They recognize the importance of changing behaviors when designing and delivering procurement transformation programs.

Our practitioners have the knowledge and capability to embed leading practices, tax effectiveness, and internal controls to help balance risk with efficiency. Our familiarity with many of the leading procurement packages helps deliver a fit-for-purpose design that is real and practical.
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Driving Business Value through Improved Procurement Performance

Look Beyond Strategic Sourcing
Companies often focus their efforts simply on strategic sourcing, but strategic sourcing alone cannot drive sustainable benefits. A limited focus on strategic sourcing may initially reduce costs for the buyer, but it may not ensure long-term realization of those benefits. More importantly, if executed in a manner where cost is the only focus, strategic sourcing can result in damage to a supplier relationship that may become critical in times of supply constraints. Instead, the focus should be on enhancing long-term value obtained from suppliers rather than on simply finding the lowest price.

Companies should seize upon the current economic conditions as an opportunity to hone their supplier relationships. This includes incorporating key suppliers in efforts to increase revenue, seeking ways to balance risks and costs, and collaborating to reduce buyer costs while helping key suppliers maintain and even improve their profit margins. Overall, companies should adopt a more holistic lens to the supply base that aligns the needs of the internal customer with long-term supplier relationship management. This approach also includes making structural improvements to procurement processes and operating models, as well as emphasizing category management from identifying needs to fulfilling those needs. This approach shifts the focus of the procurement organization to the concept of Total Value Delivered.

This concept is predicated on recognizing the interconnected elements of demand planning, strategic sourcing, transactional procurement, contract management, procurement analytics, master data, supplier relationship management, and category management as shown in figure 1.

Our View of Category Management
Improved performance in the procurement and supply chain function is a journey, not a destination. Companies that employ better supply chain practices are continually evolving and developing to meet the needs of their internal customers. As they evolve, the emphasis shifts from purchase costs to total cost of ownership, which takes into account cost contributors such as warehousing and logistics; payment costs; taxation, customs, and duties; transactional costs; and warranty.

The shift to the Total Value Delivered lens is a change in mindset. Total Value Delivered is predicated on the supply chain organization being a partner to the company’s profit centers and corporate services with the goal to enable the profit center to achieve its business objectives. Thus, the partnership defines the value that is sought from external supply relationships. This value can be safety, cost, quality, product and technology leadership, service, delivery performance, revenue enhancement, or a prioritized combination based on current needs. For example, an oil and gas company that is expanding the number of wells in a production field with a low operating cost may want to emphasize bringing wells online quickly during a spike in oil prices. A day of additional production may easily outweigh any rise in costs. In this case, safety and schedule—and not costs—could be the driving factors.

Procurement and supply chain organizations that adopt a Total Value Delivered lens are distinguished by six main attributes: customer alignment, operational excellence, talent management, supply chain innovation, supplier relationship management, and right sourcing as shown in figure 2.

**Customer Alignment:** Successful customer alignment means that the procurement and supply chain function is viewed as a strategic partner with the business. The function is engaged early in the demand planning process, and its input is actively sought on how to collaborate with the external supply base. To help achieve customer alignment, procurement and supply chain
organizations should structure themselves to respond to the needs of the profit centers. This requires a focus on service to the internal customer as well as a thorough understanding of the profit centers’ business. Overall, customer alignment is about creating options for the business. Determining whether these options are reducing budgets or yielding higher profits from the existing budget is a decision for company management and the profit center. The role of procurement and the supply chain is about creating the opportunity for them to make that decision.

**Operational Excellence:** Operational excellence is defined as effective and efficient processes enabled by leading practice tools in an aligned organization. This is characterized by clear accountability of roles, transparent and auditable processes, and a shared understanding of what needs to be done and why. The wider business strategy drives the metrics and actions and supports the profit center in meeting its targets. Operational excellence is realized through elimination, simplification, and standardization of activities, exploitation of technology to drive automation, and establishment of a balanced set of incentives to encourage desired behavior.

**Talent Management:** In leading procurement organizations, employees focus on strategic activities such as market analysis and supplier management, and technology helps to address the majority of the tactical activities.

KPMG International’s survey, Beyond Purchasing: Next Steps for the Procurement Profession¹, found that on average, only 29 percent of employees in an organization believed experience in procurement provided a good route to career progression. This perception of procurement’s role is also reflected in the grade levels commonly seen within the function.

Effective talent management policies can help change the perception and improve the relevance of the procurement and supply chain function within an organization. Organizations need defined strategies for career development to attract, develop, and retain leading talent, including mobility policies to meet the expectations of employees willing to work abroad and in other functions. The cross pollination of talent is an effective approach. For example, some companies have taken project engineers and offered them a rotational assignment in procurement. In this approach, employees are taught the aspects of the supply chain and can become an advocate for the procurement function when they return to operations.

**Supply Chain Innovation:** Leading companies require a procurement organization that is proactive and agile and focuses on value and innovation in addition to cost and compliance. This is characterized by individuals who can identify and bring forward new ways to deliver value to the business. For example, suppliers can be a source of innovation as well as competitive insight, and they should be tapped for their expertise and knowledge of the industry. The ability to incorporate market changes

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and evolve rapidly to meet the needs of the profit centers and corporate services is critical in making procurement and supply chain a valuable partner.

**Supplier Relationship Management:**
Supplier relationship management can help create sustainable value. A fully developed supplier relationship program should be established on the corporate sustainability concept of the triple bottom line of economic, environmental, and social factors. The program should balance each of these factors to manage the value from the external supply base while meeting other objectives such as inclusion of local and diverse supplier commitments.

In this process, companies should identify the key categories to manage, create a joint governance process with the supplier, establish performance metrics for both the supplier and the company, and dedicate resources to oversee the execution of the joint program. Supplier relationship management can reduce overall costs, increase the assurance of supply, and improve overall quality. This type of approach can aid companies in reducing the impacts of resource availability for major capital projects if market conditions tighten.

**Right Sourcing:** Effective sourcing is a key aspect in the drive to attain cost, service, and quality improvements. Global, value-driven sourcing decisions have significant implications for the quality and cost of supply chain operations. For example, obtaining materials from low-cost countries often drives significant benefit but lengthens lead times and requires a higher level of quality control. Both of these factors introduce additional supply chain risks that should be appropriately planned for and managed.

Leading companies require a procurement organization that is proactive and agile and focuses on value and innovation in addition to cost and compliance.
The journey to improved procurement begins by defining a procurement vision. This vision should be supported by discrete, specific, and measurable goals to help characterize what the future state of the procurement and supply chain function will look like. Creating this vision should be a collaborative process that involves both internal and external stakeholder groups, each of which has its own set of expectations from the procurement function.

The procurement vision should be aligned with the corporate strategy and in support of the company values. Once aligned to the corporate vision, procurement organizations should then assess where they are starting from in terms of their structure, processes, and technology. After comparing the desired future state to the current situation, the procurement organization should lay out a carefully planned approach to bridge the gaps. The gaps should be considered together, and the key dependencies between them should be recognized, in order to leverage synergies and to maximize benefits.

A transformation map can help companies chart the planned approach to the procurement change. Typically, a transformation map indicates a multiphased approach that includes the definition of an intermediate state of procurement with enhanced, but not full, capabilities of the ultimate goal. The last but critical step in defining the journey to improved procurement is to engage the broader stakeholder community to ensure a shared commitment to the vision and support for the program. Development of a rigorous business case is key, as it serves as a vehicle to garner support for the program.
and establishes a reference against which the program benefits can be measured. A sample map is shown in figure 3.

A common challenge that many companies experience is deciding with which initiative they should begin. The classic approach is to build a business case for each individual component and then use those business cases to set priorities. This approach is fraught with risk as it often falls short in recognizing the interdependencies of the components that yield the total program benefits.

Companies also run the risk of not investing in foundational elements of a program. This could potentially result in the dilution of the initial benefits projected for the program as well as a decrease in the likelihood that the procurement organization will be able to sustain the benefits once the project has been completed. For example, most companies focus on executing a strategic sourcing initiative because of the perceived cash benefit potential, but often do not address the organization structure, procurement and payment processes, benefit tracking methods, and data capture tools necessary to determine if the negotiated benefits have been fully realized. This often results in numerous benefits being left unattained.
In planning a comprehensive transformation of the procurement and supply chain function, companies need to consider several aspects: change management, resource availability, definition of benefits, and company commitment.

**Change Management:** Change requires planning and communication. The level of change that can be absorbed by an organization should be balanced against the benefits that can be achieved as well as the scope of the program. If a program is broad, careful attention should be paid not to allow aspects of the effort to become siloed through a business unit lens. Emphasis needs to be placed on enterprise-wide approaches with solutions tailored to business unit needs. These efforts should be supported by a continual, clear communications effort to mitigate confusion and resistance to change.

**Resource Availability:** Comprehensive transformation programs require resources. Balancing the needs of “running the business” and “transforming the business” are crucial to the success of the program. The procurement and supply chain function should continue to build credibility with the profit centers and corporate service areas while simultaneously redefining itself. In addition, the internal stakeholders are a required part of the process. Getting the commitment of stakeholders to the program requires clearly articulating the long-term value that they could obtain and why the investment of resources is warranted. Companies should involve stakeholders in the change process when decisions and guidance are critical, but they should not inundate them with every aspect of the process in an attempt to increase ownership.

**Definition of Benefits:** Success of the procurement program requires defining the benefits to be delivered. As the program is initiated, the procurement function should work with the internal stakeholders to develop a common definition of real value. This definition then needs to be embedded into the transformation process and tracked from the initial benefit opportunity through the realization of benefits. A key aspect of benefits tracking is developing a benefit definition that is rooted in business terms. Cost reductions, cost avoidance, revenue enhancements, and risk reductions are the types of benefits that can be generated by a program and should be factored into the overall framework. Early identification and agreement among stakeholders on these benefits is also necessary.

**Company Commitment:** Success in a procurement initiative depends largely on company commitment, which entails active championing of the program by appropriate levels of management. In a full transformation effort, one executive should be the program champion to communicate...
expectations, reinforce commitment to the program, remain actively engaged with the effort, and resolve significant issues. The champion should also work to secure the budgets and personnel to conduct the program. The company commitment also includes the willingness to drive the program through the completion of all of the interdependent and supporting components, and not just through the completion of the components that provide initial returns. For example, the strategic sourcing component might never fully realize the projected benefits without the supplier relationship management component.
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Michael’s focus has been on how to optimize the value achieved from supply chain and strategic sourcing. He has helped organizations more effectively collaborate to select suppliers that create the greatest profit opportunities for the company—not just the lowest cost—and how to forge more cooperative and effective supply chain/business area relations. This has involved how to best position for rising/falling commodity markets, reducing risk for the company, acquiring/planning for resources in short supply, and rearchitecting the manner in which supply chains engage their internal customers and suppliers.