

Structures for Success

Organising procurement to deliver results

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Introduction

Procurement is still a relatively young function. It is only in the last two or three decades that it has been recognised as a separate sphere of expertise in its own right and companies have created procurement functions.

Inevitably, this means procurement operations vary widely from one organisation to another. This in turn raises the question: which ways of organising procurement work best?

At Efficio, we see many procurement organisations and have developed expertise in identifying the factors

underlying different forms of organisation and their relative success. In this guide, we aim to highlight the essential issues underlying discussions over how best to organise procurement functions.

Structures for Success reflects our experience and knowledge of procurement organisations and we hope you will find it stimulating and thought-provoking.

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Section One: The need for structure

It is well understood why companies need defined product and service organisations when it comes to revenue generating activities. The ability to maximise revenue by adapting quickly and expertly to changes in the market is crucial. Income is the lifeblood of every commercial organisation.

But on the cost side of the business, the picture is much less clear. Procurement, the function responsible for acquiring goods and services on behalf of the organisation, has historically been paid far less attention than sales, marketing and operations.

But times are changing: many companies now realise the value an effective procurement function can bring to the organisation.

An effective procurement organisation manages costs effectively by ensuring the best possible deals are done in the marketplace, utilising all the tools at its disposal. These include leveraging the company's reputation in the marketplace, maximising aggregation of procurement across the organisation wherever possible, and deploying expert negotiating skills to ensure that best value-for-money is achieved.

However, excellent procurement does not only deliver on cost leadership. Other factors are also crucial in ensuring that the company's money is spent wisely and effectively. These include improving service from suppliers, ensuring compliance with all prevailing legal and ethical considerations, maximising efficiency in the procurement process and even generating revenue. Further, procurement can play a valuable role in aligning the different operating units within the organisation and helping them to achieve their targets.

But to realise its full potential, a procurement organisation cannot operate in isolation or as a stand-alone function. It must itself be aligned with the rest of the business and clearly understand the requirements of each operating unit. Equally important is a clear understanding of the full procurement lifecycle across the business.

A structured procurement organisation supports this process by aligning itself with the business and ensuring that commercial decisions can be made using all available facts and with the input of all relevant parties.

CASE STUDY: FINANCIAL SERVICES COMPANY

Establishing a CPO role was central to reorganising previously ad-hoc procurement activities at a major financial services organisation.

Background

The client was a major financial services organisation focusing on retail, corporate and wealth management activities. It had a single-country geographic focus, although it operated globally through a number of wholly-owned subsidiaries.

Its procurement functions were decentralised, although some co-ordination across sourcing categories had been achieved on an ad-hoc basis. There was no CPO position. The head of procurement was several reporting levels removed from the board.

Approach

Efficio focused on two areas: assessing current procurement capabilities and identifying the organisational model required to embed and extend strategic sourcing benefits.

Procurement capability assessment was performed through structured one-to-one interviews with procurement sourcing / category managers, divisional buyers and senior members of the organisation who were major users of the procurement function.

The organisational design was developed through extremely detailed analysis of spend by commodity, by division and supplier. This was used to determine the right combination

of centre and business-led procurement, and to identify suppliers who could benefit from more active management.

Decisions on global category management were supported by additional market analysis. Benchmark ratios were used to size the new procurement organisation.

Results and Conclusions

The model adopted was two-phased. During the project-based strategic sourcing transformation an interim steering committee and procurement leadership council was formed to provide cross-divisional governance and direct access to board-level decision making. At the same time, pilot category management activities were performed and benefit tracking was implemented.

The longer-term model centered on establishing a CPO role. The skilled resources identified during the strategic sourcing process were moved to a single procurement function. Procurement activity would be supported through the development of a single set of procurement tools and processes to be used on a global basis, and the roll-out of a group-wide e-procurement system.

The distinction between centre- and business-led procurement was based on size and concentration of spend, the degree to which product specification was business-specific, the nature of purchases and whether a natural business owner could be identified. All business-led procurement would be supported through the central procurement function.

Section Two: Assessing procurement organisations

Procurement operations come in all shapes and sizes in modern organisations. They range at one end of the spectrum from those organisations in which procurement is undertaken by a variety of individuals, none of them bearing any indication of their procurement role in their job title. Procurement in such an organisation -- more likely nowadays to be a small or medium-sized company than a large corporate -- has historically been carried out by whoever needed to do it. Procurement as a recognised function was yet to emerge.

At the other end of the spectrum there are fully functioning procurement departments carrying out a wide range of activities on behalf of the business, recognised as a crucial function at board level and with a chief procurement officer at its head.

The way departments are organised also varies widely. It is clearly worthwhile for companies to consider how their procurement is organised, to ensure that it is efficient and agile enough to meet the needs of today's extremely competitive marketplace.

When assessing a procurement organisation with a view to structured improvements or a redesign, there are broadly two areas to consider. First, there is the organisation itself:

Secondly, there are the processes within the procurement operation to consider. Information and evidence from these areas should be supplemented with the analysis of procurement data, and the examination of interactions with other departments.

Organisation

An organisation chart is a basic piece of management information showing the people within a procurement operation, their job titles and reporting lines. A more detailed look at job descriptions will show who is responsible for which areas of spend.

However, all of this is theoretical. Assessing an

organisation solely from these items would be like judging a car according to its design drawings -- any inherent flaws in the intended operation could be detected, but it must be seen in action.

To draw an accurate picture of how an organisation works day-to-day, other sources of information must be examined. An assessor, for example, could talk first-hand to people in the procurement organisation. By giving these conversations a consistent structure, a clear picture can be drawn showing not just how the organisation is supposed to function, but the reality.

It is important to examine why the procurement organisation exists: the answer is likely to be, of course, to provide goods and services to the business.

These goods and services should be assigned to categories that correspond to the way the associated supply markets operate, and subsequently, can be leveraged.

The procurement organisation will be largely determined by the categories of goods and services in scope. The Efficio methodology for assessment of category management, and, therefore, procurement organisation, is to consider categories against several criteria.

The matrix in Figure 1 shows two of the most useful criteria. Business criticality, on the horizontal axis, is a measure of how much the delivery of the company's core products and services rely on success in sourcing this category, and security of supply.

The benefits of group-wide sourcing, on the vertical axis, can come both from attracting volume discounts with aggregated demands and internal cost reductions from centralising the procurement effort, for example by reducing overheads, ensuring there is no duplication of effort and establishing a single point of contact in the company for suppliers.

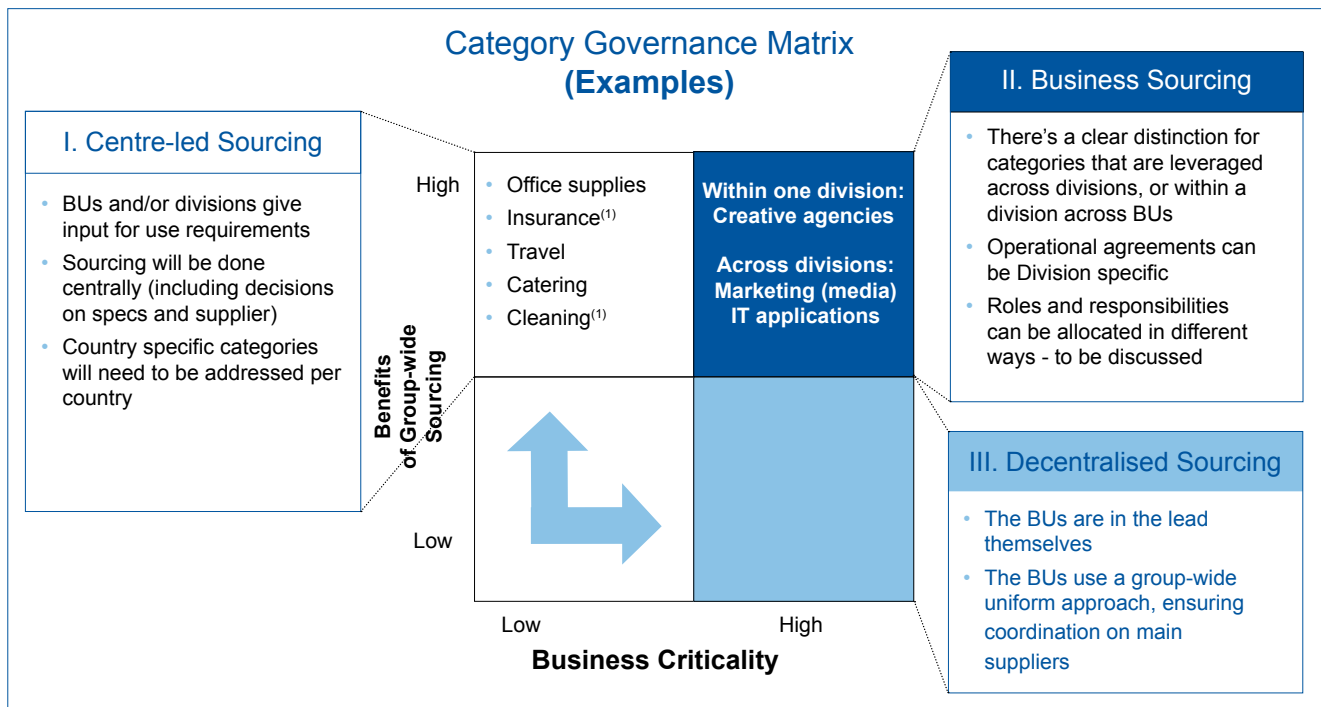
Rating the category on these criteria gives an answer to the first question in the organisational assessment: who should be responsible for managing the category. This could fall to either a central procurement operation, to the business itself or to a business-specific procurement team.

A workshop session with key stakeholders from across the business could raise the probability of end users feeling they truly own the output of the project. The workshop agenda should assign a suitable management technique to each category, which in turn determines the number, location and responsibility of the resources required in each case.

After assigning a management style, each category may be placed in a geographical context. Again considering the benefits of group-wide sourcing, the category is plotted on the fairly objective dimension of "scope of supply market". There is great scope at this point for creating category teams that align to both their own business strategies and the nature of the supply market in which they will source their goods.

The overall process also takes into account the size of the organisation; several innovation techniques can be employed to minimise disruption to existing resources, such as developing a "networked" category management team that may be split across several locations.

Figure 1



CASE STUDY: DIVISION OF A GLOBAL GROUP

Background

The client was a division of a global group where no formal procurement organisation for indirect material was in place. This was handled at national level. In some key categories, buyers were not involved at all, while in others, initiatives at group level had been launched but could only achieve part of the savings potential because of their very informal character and the absence of a structured company-wide procurement organisation.

Approach

A procurement transformation programme was launched to set up a company-wide procurement organisation for indirect materials. A procurement director was appointed to lead the effort.

Workshops with buyers and key stakeholders defined the mission, vision and strategic principles to give direction to the new organisation. This was a very important step in terms of cultural change. Procurement had always been perceived as a service function, especially in some countries where the status of buyers was very low. The new mission clearly stated that the procurement organisation had the same standing as marketing, sales and other functions.

Existing strategic and transactional processes were mapped through interviews with buyers and users in the top three countries. New processes were validated with key-stakeholders.

The new procurement transactional processes needed to be easy to integrate with those of the regional financial

shared service centre. The payment processes were jointly redesigned with a dedicated team.

Clear roles and responsibilities between procurement and other functions were established for each key category, backed by the management board.

Resources needed, roles, job descriptions, KPIs and a document defining the annual procurement cycle were decided. The newly appointed procurement managers were trained in the use of the tools and could become operational while the project was still ongoing

Results and Conclusions

The indirect procurement organisation exceeded its yearly targets and took a leading role in cross-divisional procurement coordination efforts.

- Another division decided to create a central procurement organisation.
- Procurement of direct materials was organised and coordinated on a national basis.
- Relevant savings had been achieved by making a yearly plan of areas and initiatives for global leverage and addressing them on a project basis and, due to this, direct procurement had been kept out of scope from the initial project. Now, given the results of the indirect procurement organisation, direct materials were added to the procurement director's responsibilities.

Section Three: Aligning with the organisation

An effective procurement function needs to relate effectively, not only externally with the supply market but also internally with business users. Clear commodity responsibility is essential, and procurement must demonstrate its credentials when it comes to developing robust commercial solutions.

The way a procurement organisation should be structured is driven by a number of factors, mainly related to the nature of the external spend:

- Size and fragmentation of external spend
- Split between indirect and direct purchases
- Concentration of spend by commodity across the business
- Geographical split of spend
- Geographical nature of the supply markets

Also important is whether purchasing activity is led by procurement or by business units and whether it is done globally or locally. As a general rule, commodity-based, high volume purchases are best led by procurement. Where a commodity is concentrated in a specific region, or has a technical requirement particular to a single user, procurement can be decentralised.

As procurement becomes more strategic, with greater board-level access, it needs to be involved in setting the business agenda. It needs to become involved earlier in the product development process, outsourcing and

supplier selection. To do this, it needs an organisation that supports and develops the required expertise.

As procurement's remit rapidly becomes one of managing external supply chains, the breadth of roles performed by procurement must also increase to meet these added demands. For this reason procurement needs to organise itself to take on more diverse activities, such as low-cost country sourcing and supplier relationship management.

Sitting behind procurement's ability to deliver, and the structure it takes, are the function's core building blocks – the skill-sets of its employees. As procurement takes on added responsibility and forms relationships with a wider set of stakeholders, so too must the underlying skills of its practitioners expand. It is no longer enough for procurement professionals to be good negotiators – they must now possess a range of skills including supplier and stakeholder management, business problem solving, supply chain and operations management, commercial deal structuring, data analysis and modeling.

A successful procurement organisation relies upon clearly defined roles and responsibilities. Equally, it is critical to define the procurement processes as well. It is one thing to know who does what, but procurement activity can fall down when participants cannot agree on how to do it, and when it should be done.

Procurement processes are best defined in parallel with the design of the procurement organisation. If they are identified in isolation, the new procurement organisation may lack the skills required to perform key activities.

CASE STUDY: MEDIA CHAIN

Background

The client was a media chain including several regional newspapers and a magazine. A small procurement function had been set up centrally. The business could decide whether to involve procurement and set requirements that could not be challenged. Procurement was not involved in marketing and freelance contracts and was involved only in the contractual phase for the outsourced printing of the magazine.

Approach

A redesigned organisational model for procurement was introduced to support improved ways of working.

A purchasing management team including the CFO, the director of one newspaper, the COO and the procurement director was established to set the overall procurement direction and resolve key issues in quarterly meetings. The optimal governance model between centre-led, business-led and decentralised was determined for each category based on leverage potential and business criticality. In the business-led model, where decisions were taken by a team, an escalation mechanism was set up in case the team could not agree on, for example, specifications. The issue was submitted to the purchasing management team who made the final decision.

A category leader with an appointed category team or the local purchaser was made responsible for implementation. Job descriptions and KPIs of the procurement organisation were reviewed to reflect the new setup. A simple benefit tracking system was put in place in agreement with finance. New strategic procurement processes were formalised into handbooks also containing tools and templates to support the procurement managers.

Training sessions on procurement methodology and general skills laid the foundation for an active and motivated procurement team.

Results and Conclusions

The new procurement organisation played a key role in improving short-term company profitability. They delivered significant savings whose impact to the bottom-line could be quantified. Procurement gained control of most of company spend and added value to the other functions, achieving systematic involvement in new initiatives.

Once the procurement managers had achieved the mental switch between an advisory and a decision-making role, they found the process and the breadth of their new role valuable in terms of personal development, and rewarding in terms of their increased impact on key decision-making.

Section Four: Key steps in the process of organisational design

Redesigning a procurement operation - or designing one from scratch – can be divided into a series of steps. Here we describe a four-step model of the kind Efficio would typically follow.

Step One: Setting the mission, vision and principles

Before designing a procurement organisation, its strategic direction must be defined. The fundamental elements of the organisation's strategy are its mission, vision and its principles. These elements must align with those for the company, but should be more detailed and function-specific.

The mission is the *raison d'être* for the procurement organisation. It should describe precisely what the organisation does and help explain the assumptions and purposes that guide its planning and activities. It can focus on several different factors. It may, for example, concentrate on individual relationships with users, focusing, for example, on cost, service, innovation, and training, or towards larger organisational goals such as value, control and results.

The vision describes where the procurement organisation needs to be in the future. It sets the long-term objectives giving shape and direction to the organisation. It sets a global framework that encompasses all members, inspires commitment and stimulates progress. The vision should stretch the organisation's capabilities and ambitions: how would the ideal procurement organisation be? What should the organisation be aiming for?

Strategic principles guide and drive the development of the organisation towards its vision. They provide direction in the operational development of the organisation, give support in everyday activities and build a common set of values that the organisation wants to reflect.

Mission, vision and principles are best defined by the end users through a series of brainstorming sessions. These

should also involve members of the future organisation in order to clarify objectives and, ideally, their commitment to the underlying values. Another objective is to increase the readiness for change by achieving buy-in for the new role of the procurement organisation. For this reason, mission, vision and principles should be further validated with the other functions that will interface with procurement in the new organisation.

Step Two: Designing procurement processes

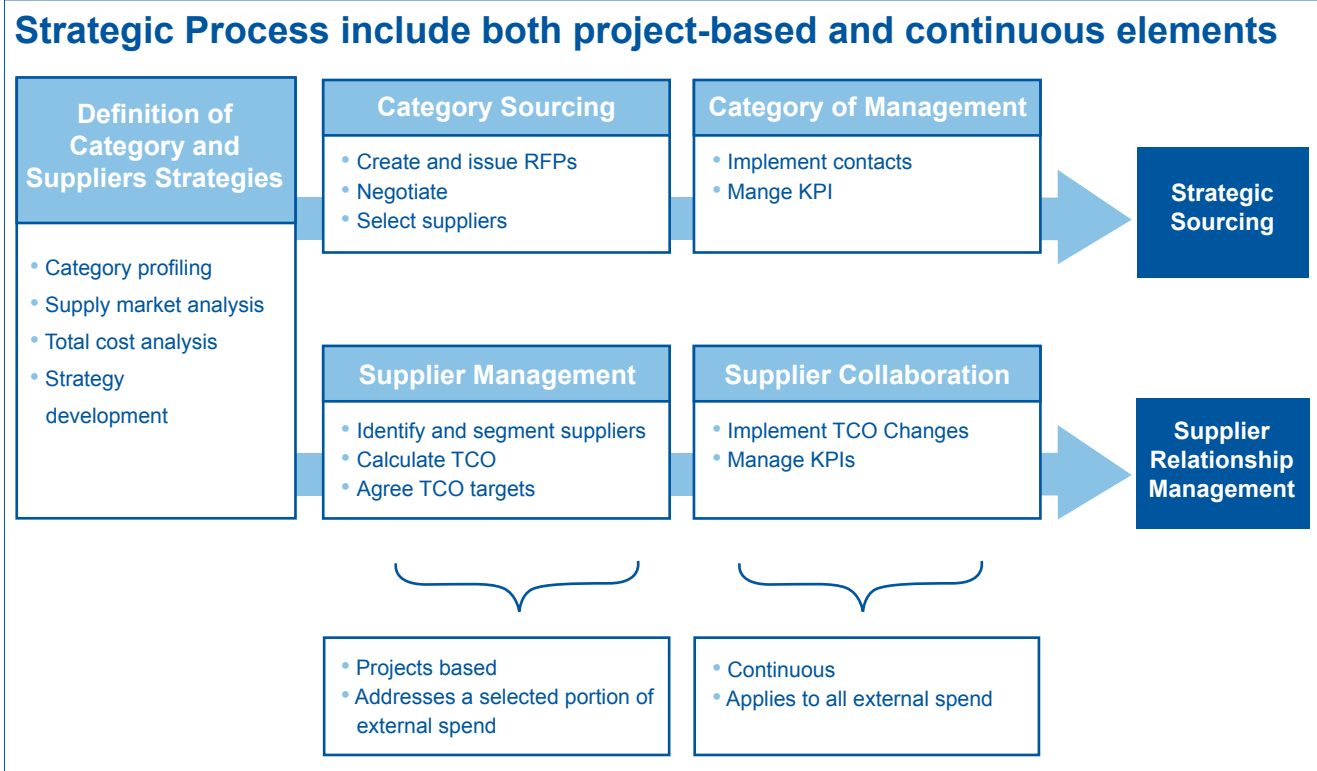
Once the mission, vision and principles of the procurement operation have been clearly defined, strategic and transactional processes need to be mapped and redesigned. Existing processes can be mapped and analysed by means of interviews and workshops with users and key stakeholders. This allows stakeholders to reach an agreement on strengths of the current system and the bottlenecks to be removed.

Based on this analysis, a process redesign can take place. The starting point is to separate transactional from strategic processes. Detailed design of strategic and transactional processes is heavily dependent on individual company characteristics such as structure, but some general principles apply.

Transactional processes

At a transactional level, processes begin with the request for a good or a service by the internal user, and end with the payment to the supplier. Day-to-day "call-off" against framework contracts and supply chain issues are the responsibility of, and will be managed by, the relevant business unit or stakeholder. Procurement needs to maintain visibility on the input, output and efficiency of these processes, for example through the use of framework contracts and supplier performance monitoring, but execution can be done by another department.

Requests and orders for goods and services can flow through different types of purchasing channel, ranging from continuous automated systems to one-off bespoke



approaches. Depending on its characteristics, each spend category can be managed within one of five generic channels:

Continuous - After one initial contract, no order is placed for these recurring goods or services. For example, electricity, rent

Pre-specified - Standard materials, for example PCs, office equipment, handsets

Pre-sourced – Sourced from a framework contract but detailed specifications need to be defined with each purchase, for example, marketing print, forklifts

Special – No framework contract. Depending on the type of purchase this channel is linked to the strategic sourcing process. With sourcing process: innovation projects, new items. Without sourcing process: pizzas, flowers, cocktails

Emergency – Urgent requests outside SLAs. No contract in place. For example, out of hours repair services

An appropriate process needs to be designed for each channel. Also, where appropriate, orders will be shifted to channels with higher levels of standardisation. This optimises the use of existing contracts and helps drive the organisation towards higher usage of more streamlined processes.

The key to designing transactional processes is to develop a common structure and a common language to form a consistent way of working.

Strategic processes

Strategic processes are often not formalised. Individual procurement managers, as well as stakeholders responsible for categories not controlled by procurement have their own way of working.

Strategic sourcing processes should cover all key aspects of sourcing and supply relationship management including how to determine the sourcing initiatives and targets for the appropriate time period and how to staff and start individual work streams.

As shown in Figure 3 below, some strategic processes, for example, category management or supplier management, are continuous and cover total company spend. Others, for example, category sourcing or supplier collaboration are project-based and address a portion of the external spend determined by the annual planning cycle.

Step Three: Who does what

The next step is to decide who does what: which activities the procurement organisation should perform and which should remain within other functions or departments. You need to decide who has the ultimate responsibility for a certain task and who has a supporting role.

In many organisations, the effectiveness of procurement is limited by the lack of clear answers to these questions. For example, where procurement is not perceived as important by other functions such as operations or marketing, and people in these functions are not rewarded for working with procurement, there are delays in providing data and assessing specifications.

The criteria determining the allocation of roles and responsibilities are also driven by the individual characteristics of each spend category. An effective relationship model can be built by analyzing two dimensions of each spend category.

First, the concentration -- or fragmentation -- of demand in the organisation.

This dimension deals with the degree of complexity in defining demand. The main complexity drivers are the number of different specifications necessary to define the goods and services within a spend category, and the number of people within the organisation who need to be involved in defining the specifications.

Second, there is the extent to which other departments focus on sourcing. This dimension assesses how specific

and localised within the company the category sourcing expertise is. For example, in manufacturing companies the specification for capital equipment and spare parts requires a high degree of technical knowledge that can only be found within the engineering function.

As shown in Figure 4 below, four different relationship models can be distinguished:

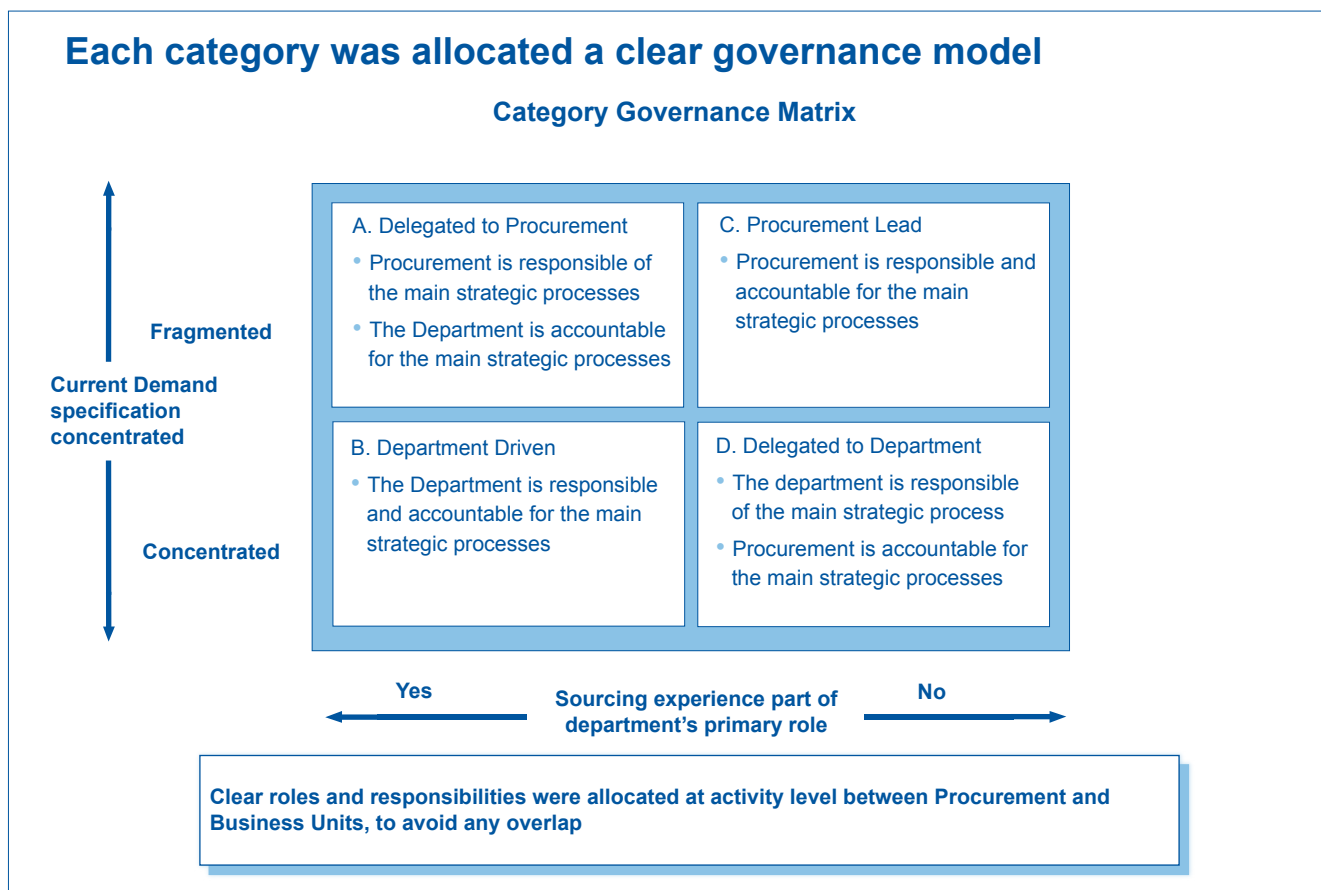
Procurement-led: demand is highly fragmented and no other department has a major role in sourcing

Delegated to department: demand is concentrated but no other department has a major role in sourcing

Department-led: demand is concentrated, but procurement is the primary role of another department

Delegated to procurement: demand is highly fragmented and the department has a major role in sourcing

In each model, the role of procurement and the departments interfacing with it changes for some or all of the tasks. Which departments need to be involved and the role performed at task level, depends on the specific company structure and resource availability.



Step Four: Finalising organisational design

To complete the organisational design process three further issues need to be addressed.

First, geography – you need to decide if each spend category is to be organised on a global, regional or local basis. If an organisational assessment has been conducted, this question has already been answered. If not, the same approach can be applied at this point in the process.


Second, organisation for transactional processes. Here, you need to decide which categories should be sourced at global or local levels.

A decision needs to be made as to whether categories managed by procurement should be managed centrally or locally.

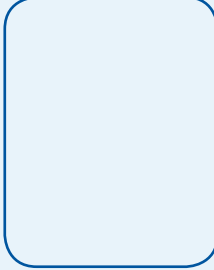
And for categories managed by other departments, the reporting relationship with procurement must be defined.

Finally, there are questions about the organisation of the procurement support function. This involves determining which of the functions is more linked to procurement and therefore needs to stay under central procurement, what relationship there should be with SSC and finance, and where the tasks fulfilled by purchasing support and control should be conducted.

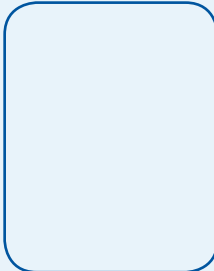
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About Efficio

Efficio is a leading international consultancy focused exclusively on procurement and supply chain performance improvement. Our clients are often blue-chip organisations with strong purchasing functions which look to Efficio to help them accomplish even more. Whether the challenge is delivering significant savings to the bottom line or managing suppliers to create value for the longer term, Efficio provides a range of client-tailored services including:

- Procurement Transformation
- Strategic Sourcing Execution (Directs and Indirects)
- Supplier Relationship Management
- e-Procurement Strategy and Implementation
- M&A Support Services

Made up of experienced professionals with a blue-chip consultancy heritage, Efficio combines the credentials of a top-tier firm with the depth of expertise and execution focus of a flexible niche player.

Our people are specialists in their field. Their unique blend of procurement know-how, change management capability and category knowledge guarantees superior results for our clients.

We have two principal deployment models -

The classic project structure, whereby we deploy a team of experts to work with the client's purchasing department to bring about a step change in performance and the scalable resource model, whereby the client taps into our pool of experts on an as-needed basis that Efficio becomes an extension of the client's sourcing team.

We deliver measurable results not reports and our fees are intrinsically linked to the savings delivered. Our focus on results speaks for itself and ensures a substantial return on investment for our clients

With offices in the UK and Germany and a growing operation in Asia and the USA we provide a global service to clients from a broad range of sectors.

Abbey | Anglian Water | AstraZeneca | AXA | Barclays | BP | BT | Cadbury Schweppes
Chubb | Cognis | Deutsche Post | DHL | DSG International | Exel | Ford | GAP
Gemplus | Grace | Harsco | HBOS | Jaguar | KION | Land Rover
Linde Marsh & McLennan | MultiServ | Nokia | Norwich Union | O2 | Permira | Prudential
RAC | SGB | Survitec | Terra Firma | Montagu | Volvo | Winterthur

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