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Procurement Transformation

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- **Provide an Overview to Procurement Transformation:**
 - **Strategic Sourcing**
 - **Total Cost of Ownership**
 - **Global Sourcing**
 - **Supplier Assessment & Development**
 - **Make vs Buy**
 - **Value Engineering**
 - **Capability Development**

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III How is Procurement Transformation performed?

Procurement is the single most impacting value lever available for companies today to positively affect shareholder value

- ❑ Direct materials costs typically represent **50-80% of COGS** and **30%-50% of revenues** in most industries
- ❑ Indirect procurement costs (e.g., capital equipment, office supplies, MRO, IT, travel) absorb as much as **15 – 25% of revenues** for most companies
- ❑ Every dollar saved in procurement is a **dollar to the bottom line**
- ❑ The current competitive climate requires greater efficiency in costs to **maintain and grow margins**



Financial Impact of Procurement Transformation

Improvements in procurement have a significant impact on a company's profitability and associated shareholder value

— \$5 Billion Company Illustration —

(\$M)	Baseline
Revenues	5000
Cost of Goods Sold	3000
Gross Profit	2000
SG&A Expenses	750
Operating Income	1250
Addressable Spend	2000
Increase in Operating Income	
% Increase	

Spend Reduction Scenario	
5%	15%
-100	-300
100	300
8%	24%

Taking this farther...

If we assume that this company makes a 5% improvement on the addressable spend, has a 33% income tax rate, and a PE ratio for its stock of 20:1, the equity equivalent is an increase of **\$1.3 billion** of share holder value.

$$(\$100M \text{ in savings} - \$33M \text{ in taxes}) * (PE \text{ of } 20) = \$1,3 \text{ billion}$$



In working with many large companies on hundreds of supply chain engagements, we have found that a common set of issues and challenges often impacts procurement

- **Multiple purchasing units** exist across the company where planning and purchasing are performed and managed independently
 - Each site has duplicate personnel
 - Procurement is locally negotiated and locally executed
 - Several suppliers are common across the various independent purchasing units
 - Inventory information is not tracked at a global level (across sites)
- Companies **do not leverage scale**, exploit volume/preferred customer discounts; **limited control** on managing the number of suppliers
- **Information exchange with suppliers limited** to the necessary operational level, rather than extensive data exchange to improve mutual logistics performance
- Supplier **performance not actively measured** and monitored against comprehensive qualitative and quantitative criteria
- **Little differentiation** in purchasing activities for strategic purchases versus routine purchases
- Rampant, **uncontrolled “shadow spending,”** inability to proactively manage demand
- Lack of a true global purchasing system – **numerous paper based, ad-hoc processes**



INCREASED PROFESSIONALISM

To effectively overcome the many challenges facing procurement, companies should not focus on individual projects to drive incremental benefit, but rather embark on a holistic step-change improvement in performance – a Procurement Transformation.

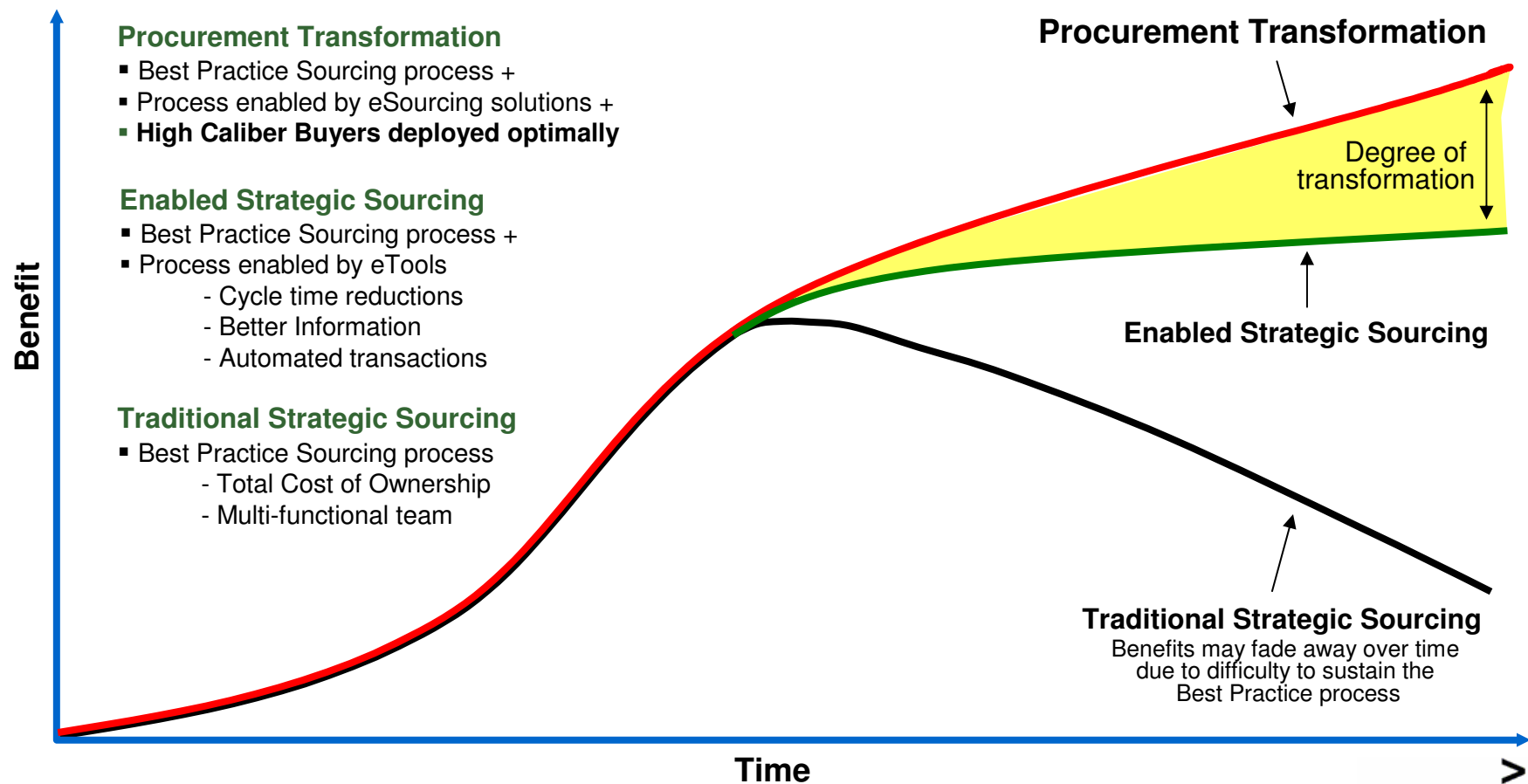


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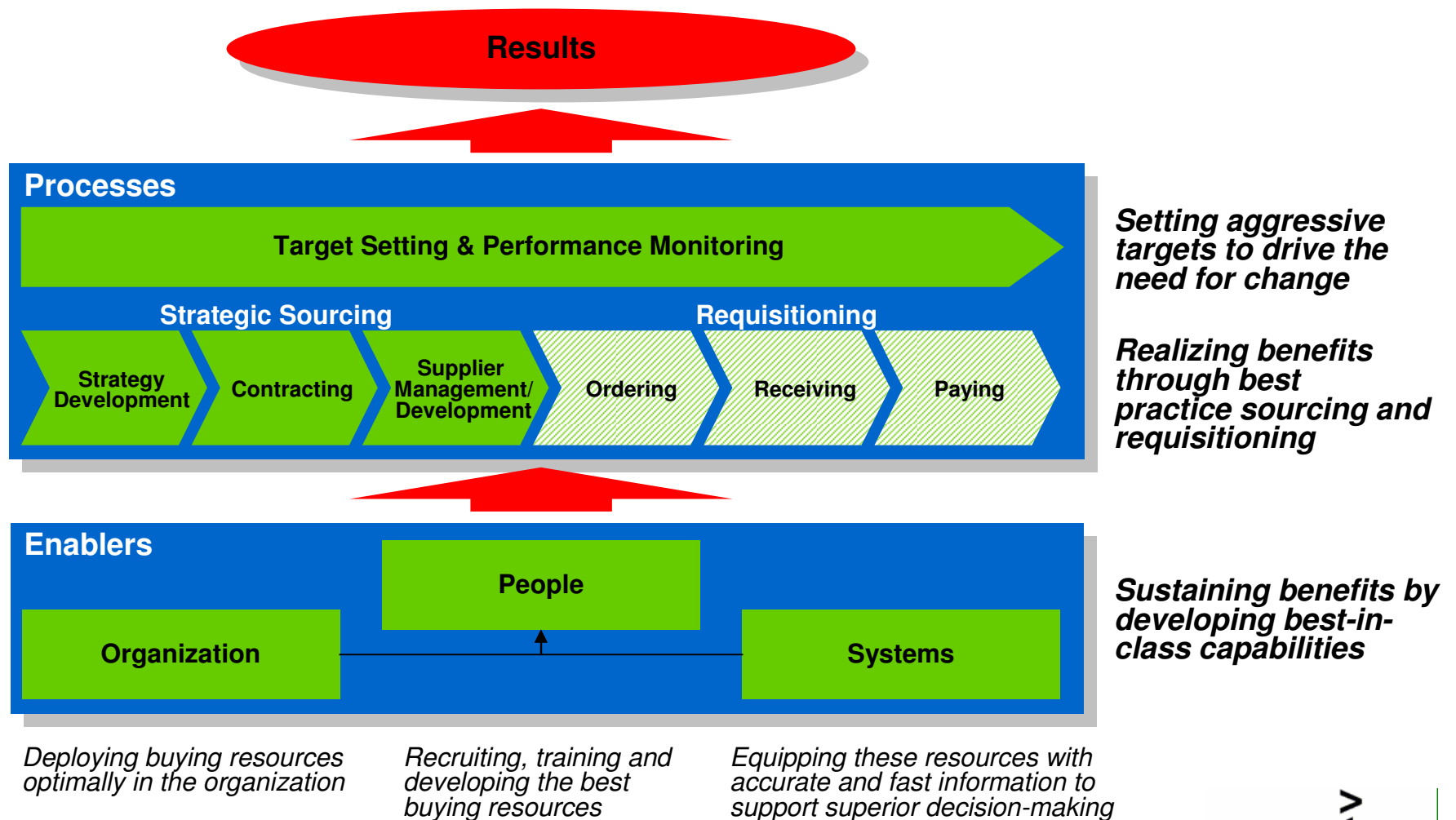
II What is Procurement Transformation?

III How is Procurement Transformation performed?

- Procurement Transformation is an *integrated multi-year program* that provides a truly transformed procurement organization, well on the road to *best-in-class status* with the ability to constantly reinvent itself
- Generates *immediate savings* through strategic sourcing – typically reaching *5%-15%* of total addressable spend – and allows for a *self-financing* structure where savings generated are *reinvested* in capability building initiatives
- Leverages *best practice processes* and key enablers to achieve *sustainable procurement capabilities* within the client's organization

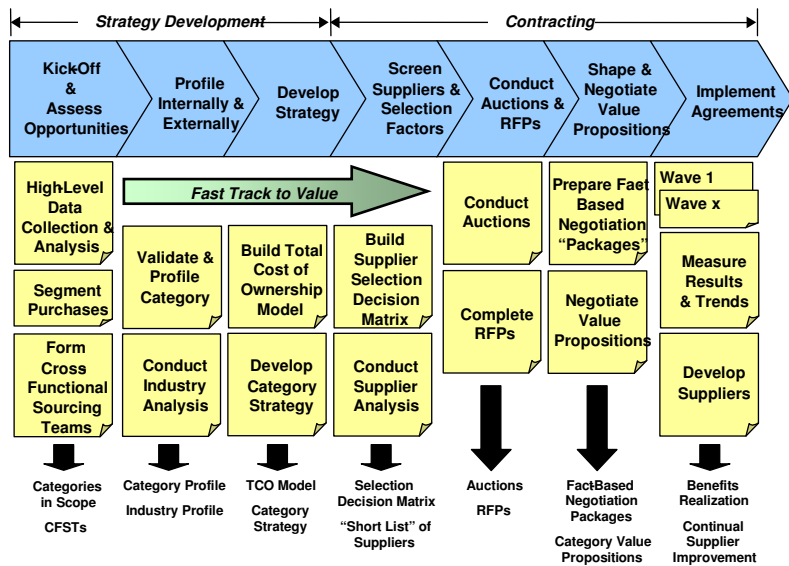
Procurement Transformation Components

The Procurement Transformation Program requires the re-engineering of all drivers of procurement value creation

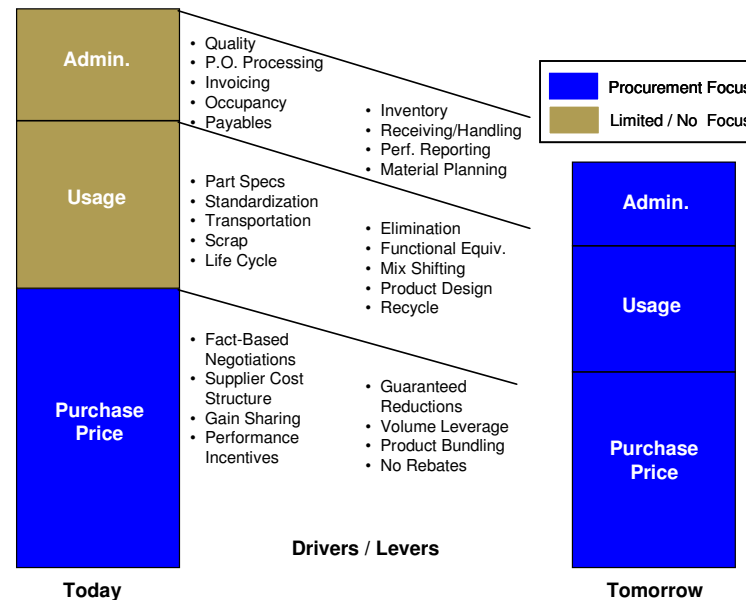


The Strategic Sourcing methodology is deployed to help drive a lower total cost of ownership

Strategic Sourcing Approach



TCO Model



Procurement Transformation focuses on “Total Cost of Ownership” to identify Cost Reduction Opportunities

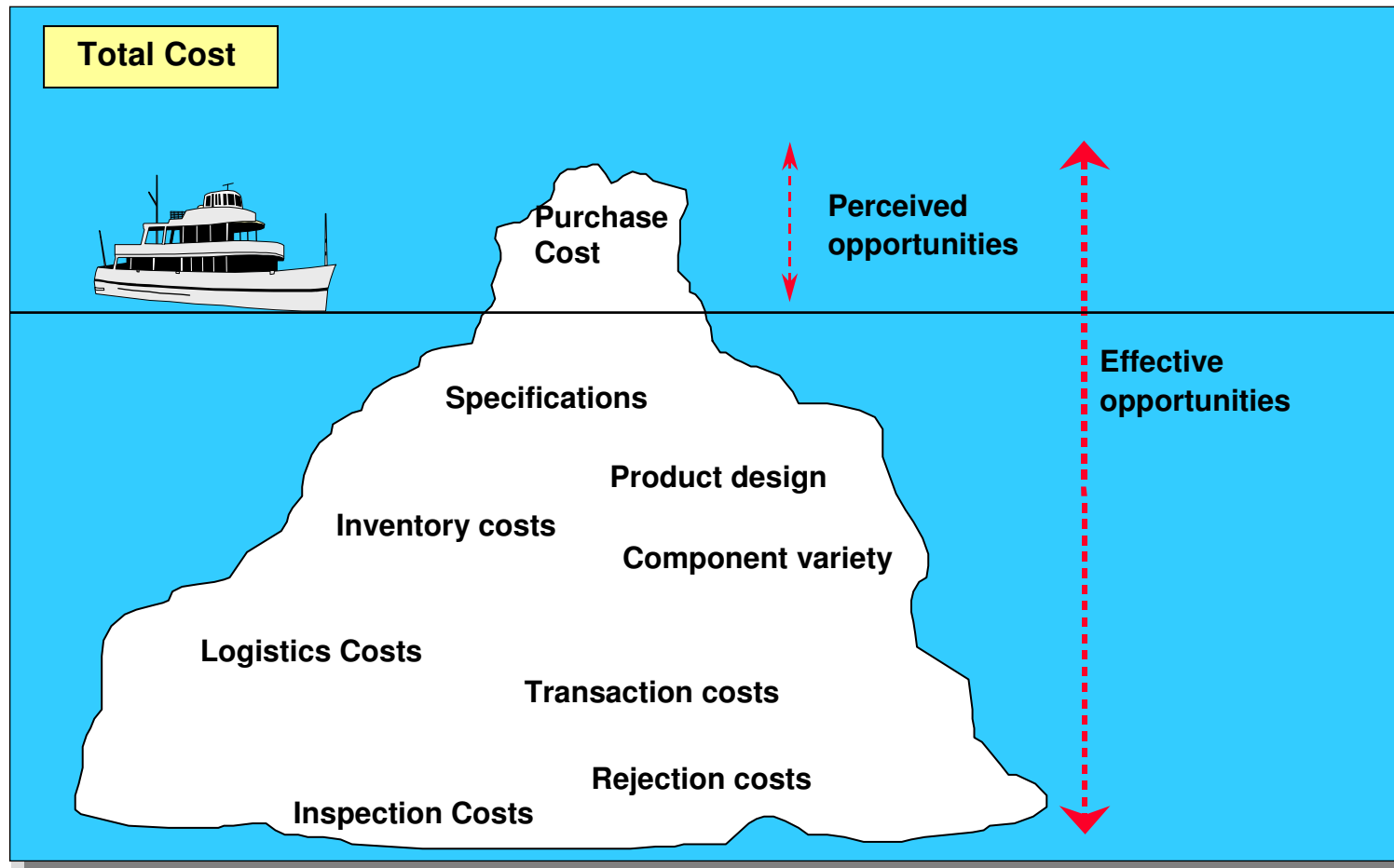
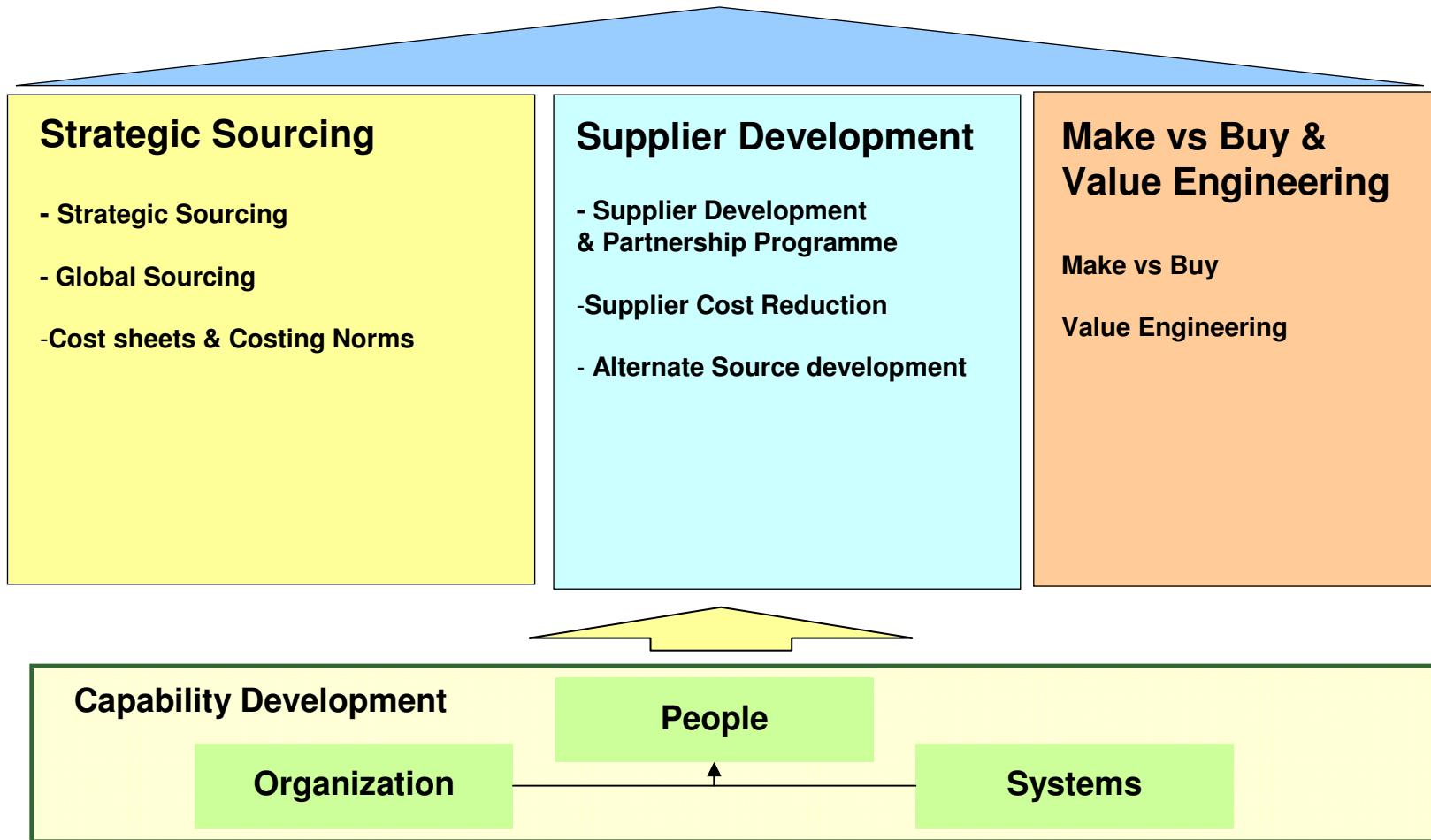


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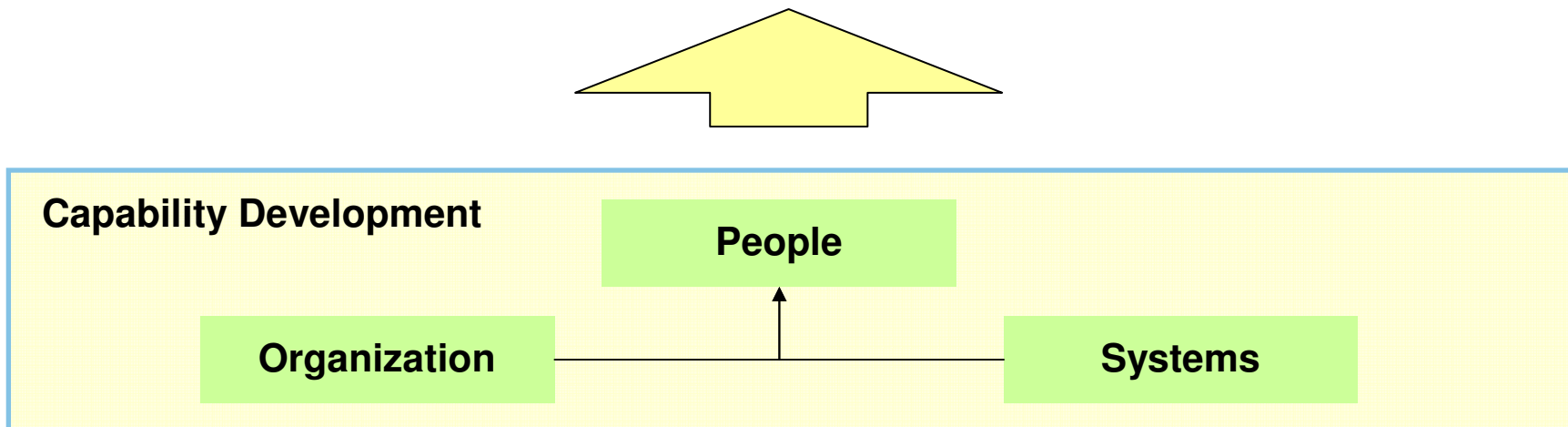
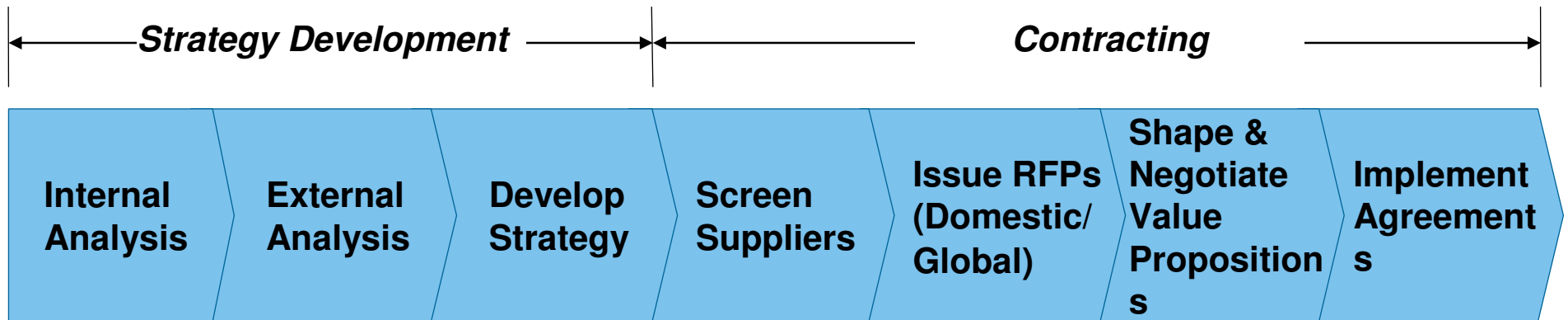
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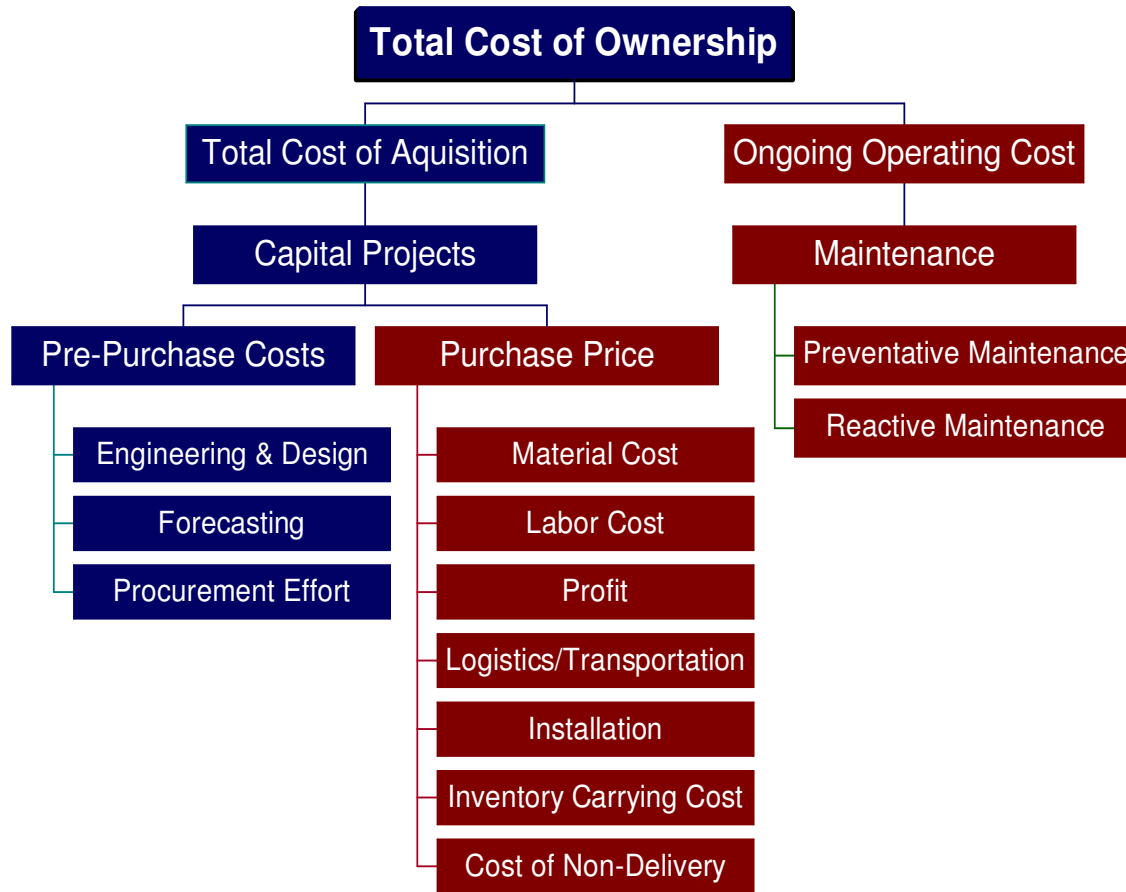


Procurement Transformation Approach



Total Cost of Ownership (TCO) is an assessment of all acquisition and ongoing operating costs associated with the purchase of assets for capital projects as well as ongoing maintenance.

Case Study



- This chart shows the generic components for a Total Cost of Ownership for cables.
- There are a number of “pre-purchase” cost elements around design, forecasting and procurement.

Need to implement a comprehensive approach to China Sourcing

Strategy & Planning

1

Category Assessment

- Review of total spend profile
- Country profiling
- Total Cost of Ownership modeling

Plan of what to source where

2

Risk Assessment

- Country Risk Assessment
- Industry Risk Assessment
- Supplier Risk Assessment

Mitigation Strategy

Sourcing Execution

8

Local Procurement Office

- Organization design & "3P IPO"
- Staffing, recruiting, training
- Integration to global organization

Established Procurement Office



3

Supplier Prequalification

- Supply market intelligence
- Supplier search
- Qualification/On-site Audits

Short list of Qualified Suppliers

7

Supplier Development

- Assessment of capability gaps
- Lean mgt program, "6 Sigma",
- Workshops and training

Capable Suppliers

4

Sourcing

- Differentiated bid strategies
- Fact-based negotiation
- Contracting

Selected Suppliers

Long-term Capability Development

6

Fulfillment

- Optimized logistics solution
- Inventory locations
- Global Trade Management

Products delivered to own sites

5

Supplier Integration

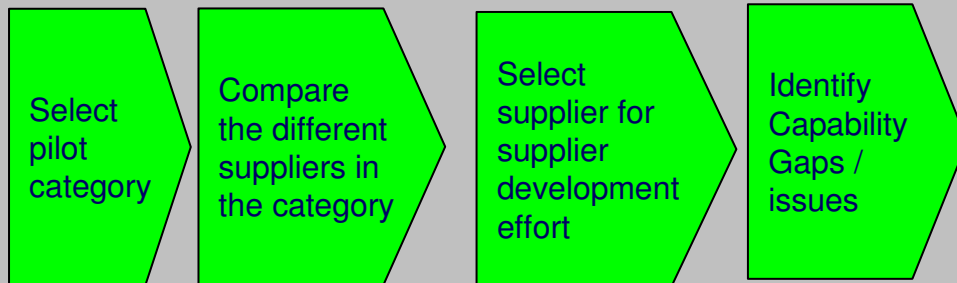
- Production process qualification
- Quality & Delivery assured
- Order-to-Delivery process defined

Supplier integrated in Supply Chain

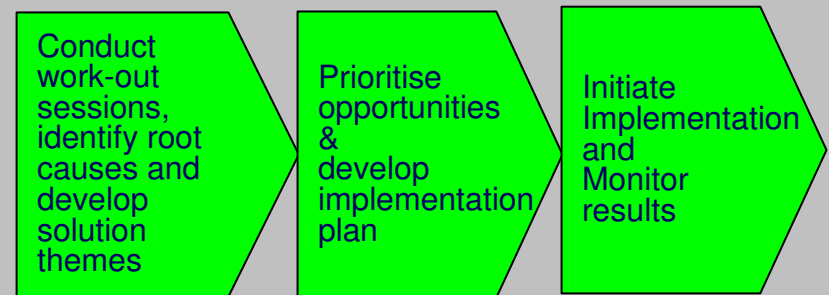
Supply Chain Optimization

Supplier Development

Supplier Assessment



Supplier Development



Make vs Buy Analysis at an Auto-Electricals Company

Strategic Importance Parameters

- Does it impart a competitive edge to the company?
- How critical it is from the point of view of product performance and quality?
- Does the company have opportunity to gain competitive advantage / technology lead?
- Does it involve any risk of sharing proprietary knowledge on technology or design with suppliers?
- How specialised are the manufacturing skills and physical assets related to sub-assembly?


Company Capability Parameters

- How are the company's manufacturing capabilities / technology relative to potential suppliers?
- Do we have any cost advantages / economies of scale as compared to potential suppliers?
- Does the company have superior quality control capabilities / processes as compared to potential suppliers?
- What is the level of capital investment / resource allocation planned as compared to potential suppliers?

Strategic Importance

Make Buy Decision Matrix

Strategic Importance	High	MAKE or BUY	MAKE
	Low	BUY	MAKE or BUY
		Low	High
		Company Capability	

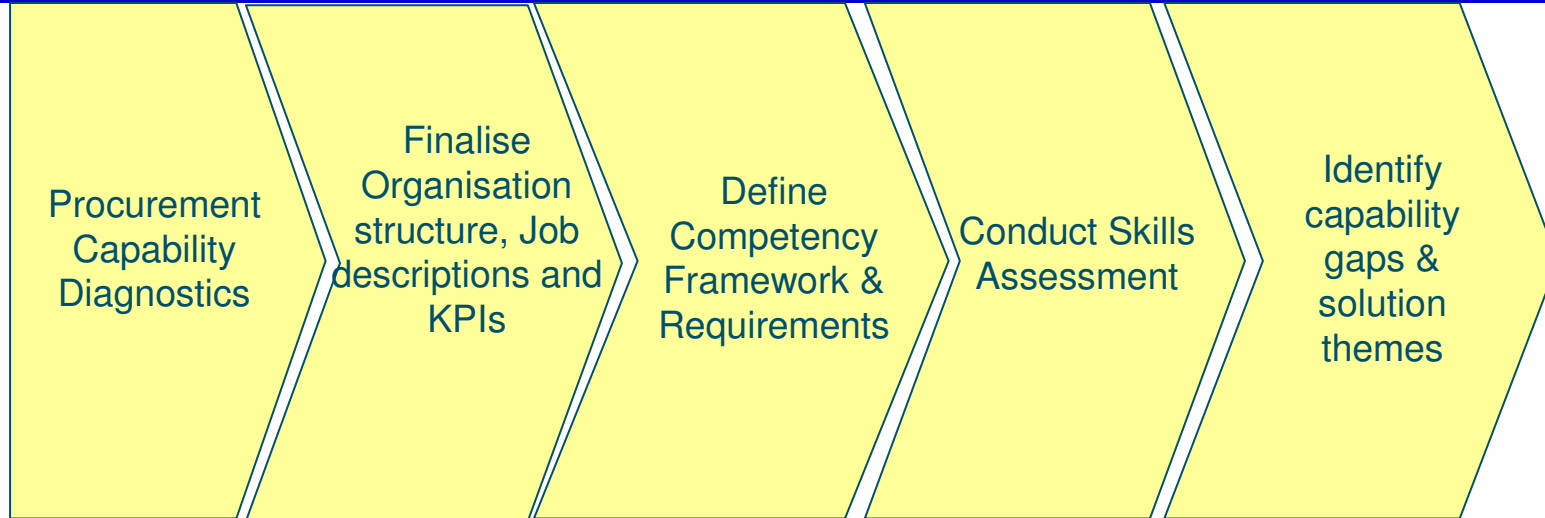
 Grey Zone - Make / Buy decision to be based on detailed Economic Analysis

Accenture experience indicates that Product Cost Reduction Initiatives can result in ~ 3-5% savings in addition to strategic sourcing initiatives

Product Cost Reduction

Initiative	Description
Value Engineering	Initiatives to reduce product costs through changes in type of material used, amount of material used, design modifications, manufacturing process changes etc
Standardisation	Initiatives to reduce component variety thereby increasing component volumes
Feature-Rationalisation	Rationalisation/conversion of low value adding features to options
Indigenisation	Developing imported items with local suppliers
Competitive Cost Analysis	Methodology and supporting tools to perform competitive product cost analyses and feedback results to product development and procurement

Capability Development Approach-People & Organisation



Deliverables

<ul style="list-style-type: none">• Procurement Capability Survey results	<ul style="list-style-type: none">• Org structure• Manning levels• Job descriptions• KPIs	<ul style="list-style-type: none">• Procurement Competency Framework	<ul style="list-style-type: none">• Skills Assessment	<ul style="list-style-type: none">• Gap Closure Plan
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