Collaborative Sourcing: Leading the Change

By Serge Wynen, Christian Verstraete and Michel Philippart

Ask a group of Procurement people how often they think about the impact of their sourcing practices on the company's competitive position or the company value. You probably will hear silence in the room. In this article, we show how achieving such value creation capability is intimately linked to sustaining fundamental changes in Procurement competences and leadership, and developing a portfolio of collaborative relationships with suppliers. We also hint at how such changes can be implemented.

In today's rapidly changing global environment, setting and achieving aggressive cost control targets has become the norm in many industries, often resulting in a pattern of ruthless annual supplier price reductions. Cutting cost however is no longer enough to stay ahead of the competition. Manufacturing industries have done this for years. But relentless cost cutting did not save companies such as GM from the brink of bankruptcy, did not prevent Compaq from being acquired by HP and was not sufficient to satisfy HP shareholders after the merger. Price reduction is not the only value that buyers and suppliers can provide. The message is becoming increasingly clear: Procurement will need to contribute more to deliver sustainable competitive advantages that grow profit and market share.

Is There Any Urgency?

Albert Einstein once said "the definition of insanity is doing the same thing over and over again and expecting a different result". Can Procurement deliver competitive advantages by doing the same thing it has been doing for years? Or does it fundamentally need to change its attitude towards suppliers? And how urgent is this anyway? Well, while you are reflecting on this question, your strategic suppliers, those whose innovations provide the differentiation your sales people desperately need to keep winning in the market, may already be crafting unique collaborative supplier relationships with your direct competitors.

In highly competitive industry segments such as automotive and electronics, key trend setters are already well advanced in creating sustainable competitive advantage through collaboration. Airbus' highly collaborative product development and manufacturing approach forced Boeing to transform itself drastically. Toyota USA's focus on building and maintaining collaborative supplier relationships allowed the company to take full advantage of the innovation power of its supply chain network, creating a very successful competitive advantage in the U.S.
Such an approach requires a fundamental change in company culture. The first step is to create a clear sense of urgency around the needed changes. Making

sure that management realizes the need to change and is acting with sufficient urgency to limit the damage is also the responsibility of the CPO.

A Change Starting at the Top

Successfully implementing such a profound change in sourcing culture takes more than one person or the Procurement team to achieve. The concept and vision of tight collaboration with strategic suppliers needs to become an integral part of top management thinking. Performance measurement has to be aligned with the new vision. The Procurement organization can for example no longer just be measured on cost reduction targets. Clearly articulating the direction for change, demonstrating support in day-to-day communication and monitoring progress requires top management involvement and support.

Together with the CPO, senior Management needs to start with one key decision: “Do we have time to transform our existing organization, or do we need to act faster by attracting external, ‘collaborative-literate’ resources, while focusing the current Procurement organization on managing our less strategic suppliers?”

Regardless of the approach taken, a guiding team needs to be formed. This team will need change agents who will become catalysts of change and role models for the rest of the organization.

Building a Vision

To make change tangible, a picture of the desired outcome will steer the change in the right direction. How does the enterprise envision new ways of working in tight collaboration with key suppliers? What would that imply for the employees and the organization? What are the risks? And what benefits would be gained?

Many aspects need to be taken into account to address these questions. We would like to propose a framework to guide this change. We believe that by creating a portfolio approach in managing supplier relationships, organizations are able to optimize the value generated, by creating sustainable differentiation and shareholder value. Figure 1 illustrates such portfolio approach. The horizontal axis shows the level of maturity and sophistication of the relationship; the vertical axis, the value created.

Suppliers of commodities for which many alternatives are available should continue to be approached “confrontationally,” as the buyer is mainly interested in the lowering the commodity cost. On the other hand, if a supplier adds a specific component that differentiates your product from your competitor’s product, a very close and collaborative relationship can create and solidify a competitive advantage. You may for example, create close links between the respective R&D departments ensuring the best use of the component. You may even want to establish an alliance, a joint venture or take an equity stake to ensure that your competitor does not buy your strategic supplier. This is what Type IV and V are about, recognizing your supplier added value, ensuring the best use of it while protecting your position in the market.

Collaborative relationships are far away from the typical buyer-supplier approach. They involve many parts of the buyer and supplier organizations, such as R&D, production, quality and after-sales services. The collaborative buyer orchestrates the different levels of relationships between individual departments in both organizations.

Collaborative Sourcing Model

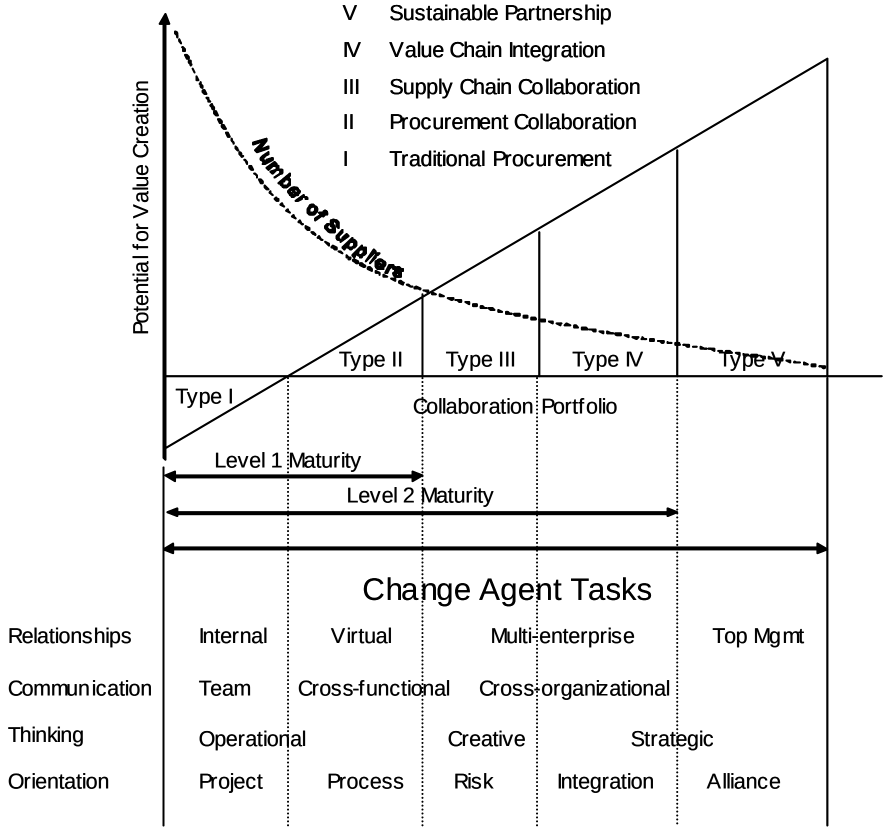

Figure 1 – Change Agent Tasks

In implementing this vision, three key barriers of change will need to be dealt with: culture, risks and trust. Let's take a minute to review how we can address each one.

Beyond Cultural Barriers

For most organizations, collaboration is not natural. The idea of building collaborative supplier relationships goes deep against the prevailing societal or managerial culture. Many managers still view their suppliers in a hostile or adversarial way. For many the default view of a supplier is that of the ‘enemy’, collaborating is risky, elusive or at best naïve. Europeans in particular are suspicious of the word ‘collaboration’: weren’t the ‘collaborators’ during World War II the traitors to their own country?

The individualistic nature of North-Americans and Europeans societies do not promote collaboration, they push competition. Supplier relations are cutthroat negotiations, confrontational problem solving and a total lack of recognition of the value added by the supplier (he might increase his price…). Asia is different as societies tend to dislike direct confrontation. One needs to save face. Negotiators are concerned with group reputation and more “win-win” oriented and expect a similar approach from their suppliers.

When Japanese car manufacturers set-up their plants in the U.S., they surprised local suppliers by approaching them in a more collaborative way. However, the suppliers had to learn the real meaning of partnership and understand that mid-term price ranges for example were not acceptable to their Japanese counterparts. However this learning experience resulted in better relationships than the ones of the North American automotive companies (see annual WRI North American Automotive Survey).

Major automotive companies have requested their suppliers to reduce their price by X%, threatening to no longer do business with them. But what would happen if their supplier of injection systems (of which only a few companies have survived across the world), would refuse the price reduction and walk away? Will they ultimately benefit of pushing their tier one suppliers to bankruptcy?

Business attitudes (or the lack thereof) tend to be deeply ingrained. Both the buyer and supplier need to be convinced that more collaborative supplier relationships enable value creation. As it takes time to achieve results, there is a real danger of stopping early with collaborative initiatives, and missing the opportunity to get the enterprise and Procurement to the next level. Again, management needs to show endorsement and commitment by formalizing this key idea in a change program, and demonstrate continuing support to keep the momentum of change up.

Then there is technology. While technology is an important enabler of change, too many managers view collaboration as a deployment of software solutions that are necessary but also sufficient to collaborate. In reality, collaborative

technologies have been available for many, many years. If organizations wish to work more collaboratively, they will need to align systems and processes.
The takeaway: collaborative solutions do not deliver change unless people using these solutions also change their behaviors and attitudes.

Collaboration: What About the Risks?

"And you expect me to fully rely on this supplier?" This phrase is often heard in procurement departments. Trusting a supplier is seen as risky.

The first step then is to identify potential risks and their negative consequences, then to identify possible responses. Indeed, collaborative relationships are not without risk, and companies should enter into such relationships with eyes wide open. Often the benefits will outweigh the risks, but addressing the risks is still important. Through detailed analysis and "scenario planning" companies can prepare alternative plans, in case the supplier comes short of expectations, or if a natural, political or economic adverse event would make it impossible for the supplier to deliver on their promises. Some companies sourcing from Asia today have established contingency plans in case of a pandemic of avian flu.

Let us review some of the more common risks:

- Organizational risk: lack of leadership and internal or external sponsorship limits the collaborative behavior. Complementing the procurement relationships with top management linkages allows a quick and smooth escalation path if required. This is achieved if both parties nominate an executive sponsor for the relationship.
- Economic risk: important changes in demand may create a different perception of the risk of engaging in -, or pursuing a particular collaboration. Designing flexibility and an exit strategy in the contract is one way to mitigate this risk. As described above, scenario planning is another. .
- Dependency risk: partnering in an integrated product or service offering with a supplier who might not perform, or go out of business is always a risk. Performing audits and performance reviews help get the problems on the table early and make room for improvements. The buyer may also think at helping the seller addressing the problem, developing a deeper relationship and better understanding along the way. Continuously scanning the market for alternative suppliers is a best practice, even if there is no willingness to change.
- Information security risk: information will be exchanged in the collaboration. The accidental leakage of private information by the supplier may cause great harm to the buyer. In an information intensive business auditing the security systems and procedures of the supplier is a must. An American bank for example lost 3 million customers after some of their back-up tapes (managed by a third party) got missing.

- Knowledge risk: collaborative sourcing involves the sharing of expertise, i.e. explicit and tacit knowledge between buyer and supplier. By collaborating in product development strategies for example, partners are bringing sensitive product and market information to the table and learning from each other. This may result in the loss or theft of intellectual property, trade secrets and copyrights. In a similar way, the supplier may have infringed other companies' patents and IP, creating unknown liabilities. IP protection and patent search are key best practices to reduce such risk.
- Complacency risk: by engaging in a long-term collaborative relationship there is the possibility that parties take the relationship for granted, or that a supplier takes advantage of a less adversarial supplier relationship to make more than his fair share of money. Conducting regular performance reviews, benchmarking prices and competitors, or technology can mitigate this risk. By imposing periodic qualification processes and audits, both the Procurement department and suppliers are kept on their toes. A consumer electronic company certified a second supplier of a critical component to bring his original supplier back to the negotiation table.

Increased collaboration improves operations, resulting in financial benefits. It is a normal tendency to let those benefits flow to the bottom line, resulting in increased shareholder value. However, we would argue the importance of creating a small team to assess risks and to develop plans for each possible scenario, hoping those plans never need to be used. Risk management complements collaborative sourcing.

The more partners trust each other, the more they increase their vulnerability. This is a shared and measured risk. As one Sourcing Manager put it: "Being collaborative does not mean being stupid!" This brings us to the topic of trust.

Trust Impacts Collaboration

Trust is an essential ingredient that impacts, builds and sustains collaboration. The need for trust is dramatically rising as organizations increasingly rely on other organizations to create value.

Trust supplements the supplier contract: when business is rapidly changing, it becomes difficult and expensive to control a collaborative agreement; higher trust lowers the cost of monitoring the agreement.

By continuously reinforcing and nurturing trust, partners are attentive to the negative signals and behaviors that may harm the relationship. Here are some of the warning signs:

- Negative feelings
- Information withholding
- Lack of reciprocity

- Unfair practices
- Opportunistic or passive attitudes
- Lack of face-to-face communication

Trust is reinforcing the flexibility needed to start and manage informal collaboration. By building trust, partners invest in mutually beneficial actions that create goodwill. This fosters the tolerance necessary to weather conflicts and temporary imbalances in the partnership.

Trust is reinforcing performance. Academic researchers such as Cullen, Johnson and Sakano described the feedback loops that exist between trust, commitment and performance. Strong performance reinforces the trust and commitment cycle that makes partners even more trusting and committed.

A manufacturer of disk and tape drives realized it was paying a lot for the inventory that was held in the supply chain due to the variability of its orders. It decided to share and explain forecasts to the whole supply chain and made those available in form of an Excel spreadsheet on a shared drive. Weekly, a teleconference took place to discuss the latest forecast. The inventory in the supply chain dropped by 30%, resulting in savings for all. Within one year, the suppliers were suggesting improvements on how the supply chain was running and on future products. This simple approach had resulted in clear benefits for the manufacturer and its suppliers alike.

Each collaborative relationship has a unique set of characteristics and relies more or less on trust and commitment. A short-term collaboration needs less commitment than a long-term one. The longer the collaboration, the more management will come to rely on trust to sustain the benefits. On the other hand, the more an organization relies on trust, the more it becomes potentially vulnerable. The zone of comfort for the relationship exists below the trade-off point where benefits exceed vulnerabilities.

The CPO as Communicator

Collaborative Sourcing is about changing and balancing the relationships between an enterprise and its key suppliers. Implementing the vision described above requires time and needs to be internalized by the organization. Leading an organization through change means dealing with fear, resistance and uncertainty. Communication is a critical component of successful change and it should come to no surprise that this aspect is often where things go wrong. The first three objectives of the change agent then should be “Communication, Communication and Communication.”

Communication gives a unique opportunity to the CPO to elevate the role of Procurement to that of a critical department in the enterprise, by taking the lead in managing supplier relationships for the company. By taking the lead of cross-functional collaborative projects, Procurement becomes a more credible partner to other functions, such as R&D, Manufacturing and Sales. In highly outsourced environments that rely on effective collaboration, the role of Procurement and supply chain become even more intertwined.

The CPO has a central role in facilitating the adoption of Collaborative Sourcing. He or she steers the relationships and communication between suppliers, procurement employees and internal customers (Figure 2). The CPO can initiate change, remove barriers by supporting agents of change, or be the main change agent driving collaborative sourcing concepts and projects across the organization.

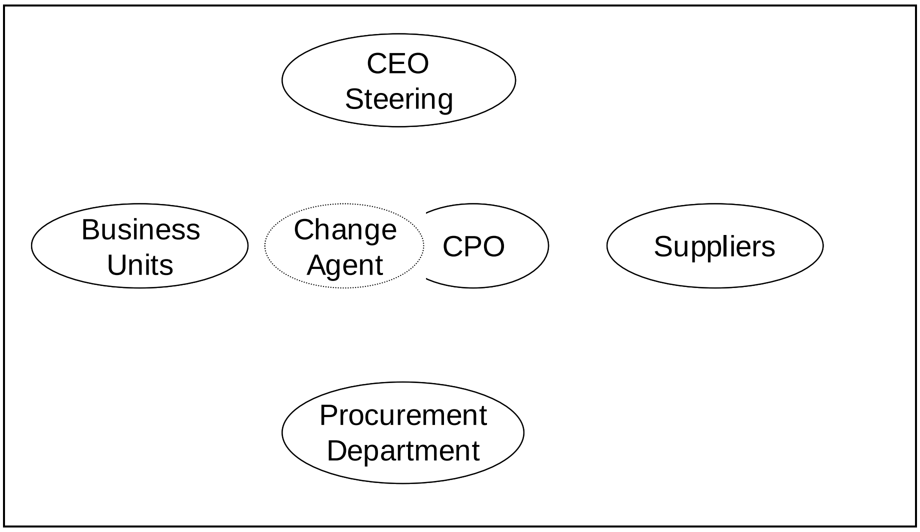

Figure 2. The Role of CPO as Communicator

Where to Start?

Procurement can start with two key activities:

- On the one hand, thoroughly review their supplier portfolio to identify which suppliers are strategic, are adding differentiation and value. Within this short list, approach a couple of candidates for initial collaboration pilots.
- On the other hand, identify and groom lead buyers to become the "collaborative buyers" we described above. Give those individuals the opportunity to experience collaboration, for example in cross-functional innovation projects.

Whether the company needs to hire “collaborative buyers” from the outside, or rely on their internal capabilities requires an honest review of internal talent and market requirements.

How to Keep Things Moving on Track?

As already stated, regular communication is of the essence. Explaining what is happening, describing the next steps, creating short-term wins, articulating how these wins are linking into the broader vision, and keeping management involved are mandatory for success. Start small, but don’t forget to celebrate each success gained along the way. Recognizing individual contributions are important morale boosters in time of stress and change.

Communicating the success stories achieved though pilot projects will fuel the resources required to jumpstart the next wave of collaborative projects. What is important is to start a cycle of collaborative change, and to keep the fire burning.

Conclusion

If Procurement wants to become, or remain a strategic partner to the business, it needs to move beyond cost cutting by creating strategic value. Procurement should no longer just be a function that contributes savings or predictable costs. It needs to take the responsibility for creating external synergies, seeking innovative ways of working with strategic partners, reducing waste along the way.

Value creation is an invitation to the sourcing manager or strategic buyer to become a cross-functional change agent, an active leader in driving the cross-organizational projects and behavioral changes in Procurement. The cost of creating and sustaining these unique relationships is well worth the effort, provided a company is able to tap key its suppliers’ unique innovation capabilities ahead of its main competitors.

Will the CPO live up to this role of leadership is a question. Procurement leaders are already fighting hard to deliver annual cost savings with limited resources. Many are fully absorbed by challenges on the left-side of our Collaborative Sourcing Model. They are reacting to changes that may well be imposed on them by other functions or ad-hoc circumstances. Mature Procurement organizations are by definition more proactive. By leveraging advances in processes, systems and buyer competences, they can better anticipate changes, and gradually develop the competences and resources that make collaborative sourcing come true. Having a mature Procurement organization is a definite asset in supporting collaborative sourcing change, but it does not imply that the cultural transformation challenges are necessarily comfortable or easily overcome.

*The Collaborative Sourcing Model is more extensively described in the authors' recent book: "*Collaborative Sourcing*: *Strategic Value Creation through Collaborative Supplier Relationship Management*," published by Press. Univ. Louvain (PUL) in December 2005.

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Ten Tips to Jumpstart Collaborative Sourcing Changes

1. Increase awareness and urgency by sharing stories of collaborative sourcing that inspire your staff, your peers and your preferred suppliers.

2. Take a deep look at your current portfolio of suppliers and identify the partners adding significant value to your business today and moving forward.

3. Align your agenda of change to where the business is heading: create bottoms-up clarity with your staff that the company strategy is intimately linked to value creation and new buyer behaviors, competences and skills.

4. Increase the change management skills of your senior staff through training and open dialogues that encourage ‘out-of-the-box’ thinking and ownership.

5. Start pilot projects involving your most skilled sourcing managers. Practice collaboration in safe environments, and empower your buyers by involving them in cross-functional innovation projects. Draw and share lessons from experience.

6. Create short-term wins, value new buyer behaviors and communicate for buy-in with staff, internal stakeholder groups and key preferred suppliers.

7. Extend involvement to more people from different functions, such as R&D, manufacturing and sales to reinforce the momentum and cultural change.

8. Launch collaborative initiatives and monitor their progress across different categories to increase chances that new buying behaviors survive the initial change agents.

9. Work with HR to align job descriptions, competences and skills, performance objectives, evaluations and rewards that reinforce collaborative behaviors.

10. Lead the change. Get used to challenge the status quo, and to be challenged. Walk the talk. Remember, if you don’t move, your competitor will.