

The Role of Strategic Purchasing and Supply Management in Risk Management



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Value generators and value protectors

Procurement's profile in organisations is on the increase. A wider spend remit is being influenced and internal barriers are being broken. Some of the most valuable assets the purchasing team can bring to an organisation is due diligence of vendor rating and regular detailed monitoring of supplier performance to identify, monitor and manage enterprise-wide risks whilst encouraging innovation and continuous improvement. This has manifested itself through enhanced relationship management skills in purchasing teams both internally and externally.

This resource is yet to be fully exploited and although procurement has made some progress in influencing spend areas such as marketing, human resources and legal services, the skills and value that procurement can add to the purchasing process is yet to be maximised on a company-wide scale. There are vast sectorial differences too, as procurement teams still struggle to make an impact in the service industry, while their presence is deep rooted in manufacturing and retail.

The role of P&SM professionals has transformed, and there has been a shift from a transactional, back-end administrative function to a fully embedded, cross-departmental, value-adding function – in many industries. Procurement professionals are taking on a more consultative role and are working along-side business units to deliver shared goals. To become more strategically focused P&SM professionals have begun to investigate what is important to the organisation and the end customer in order to identify what delivers both customer and shareholder value. Once you have established what the important issues are, you then begin to understand the risks and vulnerable points and can start building a resilience plan. The role of procurement is that of risk management and building robust supply chains, both upstream and downstream, that can weather disruptions with minimal impact. Professor Paul Cousins, Director of the Supply Chain Management Research Group at Manchester Business School, summarises the role of procurement as that of 'value generator and value protector'. All initiatives, including risk management programmes, must be tied back into shareholder value and customer perceptions, and procurement professionals are the custodians of this.

However, research shows that procurement professionals still have some way to catch up in the risk management stakes. "High-profile events such as corporate governance scandals, international terrorism and civil contingencies requirements have propelled corporate risk management and security into the headlines; although they appear to have had relatively little impact on awareness of risk management in purchasing and supply." These are the findings of a CIPS commissioned report compiled by Dr Helen Peck from The Resilience Centre at Cranfield University.

McKinsey's also report in their recent Understanding Supply Chain Risk global survey, that almost two-thirds of respondents said that the risks to their supply chain had increased over the past five years. As we operate in a global environment this pattern is likely to continue and risk management will become a major focus for P&SM professionals. So why are you still struggling to get involved and noticed?

It is paramount for procurement professionals to ensure they have the ear of the board in order to play a key role in risk management strategies and prove their worth. Successful risk management programmes assess the risk in terms of likelihood and impact as well as what it means to your organisation. Why is this important to my organisations? How will it impact

value? Until this connection is made it is difficult to obtain senior management buy-in or even to be taken seriously at all.

The business risk environment

Modern organisations operate in a very commercially pressured global environment. Competition is strong and to remain efficient and competitive risks must be taken. We often see risks as having a negative impact on our organisation; however with risk often come opportunities and innovation and not always threats. Like finance, and auditors, procurement professionals have had a reputation for being risk adverse, providing a hundred and one reasons for not to do something.

A more modern approach is to find solutions and provide a robust framework for business to operate in, allowing scope for risk takers, and closely monitoring the process step by step. Organisations have become very lean and mostly operate on a just in time basis. Therefore the slightest disruption to any element of their supply chain can have devastating results. There is often no 'slack' to withstand a major movement in an organisation's operations. Procurement practices such as outsourcing, low cost country sourcing and lean supply have exposed us to new risks but have also given us the experience to mitigate and avoid their impacts. Trends such as reducing the supply base and using sole sourcing have forged closer working relationships in order to collectively monitor and manage risks in the supply chain. BA more than anyone discovered these risks with a relationship breakdown with gate Gourmet resulting in their planes being grounded for several days in 2005. BA probably didn't view their catering supplier as particularly high risk at the time.

Wherever possible, the purchasing organisation should adopt a partnering approach to the important and vulnerable supplier relationships as a way of mitigating the risks of supply chain vulnerability. Whenever an organisation is significantly vulnerable to the consequences of failure of supply, the appropriate style of relationship to manage a supplier would usually be partnership.

Industries have also become consolidated and therefore if one major player is effected the knock on effects can be catastrophic. It makes switching to alternative suppliers who have the same capacity almost impossible, especially when non standard products are used. Generally there is not any slack in these manufacturers capacity, therefore finding a supplier to switch too may be impossible. The packaging industry is one example where there are only a few large consolidated businesses. Organisations must become agile and risk aware. We need to be able to switch on contingency plans at short notice.

The right tools for the job

Procurement professionals have a wealth of tools and skills that are appropriate for risk management; from close working relationships within both buying and supplying organisations to monitoring and performance measurement techniques. As procurement professionals we are experienced in calculating savings and this is one way of demonstrating the value we can add to an enterprise-wide risk management programme. If you are able to price a risk or disaster in terms of the cost of the loss; you are then able to cost, or calculate a 'saving' on avoiding that loss. This is indeed a powerful tool to obtain the deserved attention from the board and shareholders.

Successfully managed risk taking is also likely to attract attention. Showcasing examples of increased profit, innovation or sales through the successful mitigation of risks will also raise the profile of the procurement team.

As value generators and protectors, customer perception and value is considered throughout the procurement process as well as shareholder value. Dr Helen Peck's research also looked at the downstream indicators that impact customer satisfaction to establish the level of involvement that procurement teams had in measuring and monitoring these indices. She found that in nearly three in four cases respondents stated that lead times to customer is included in routine monitoring.

Just over 60% also indicated that availability of company products/services was also routinely included. As ever, the devil is in the detail and marked differences appear between the sectors. Lead time to customer featured in routine monitoring in 95% of public sector organisations, over 81% of the manufacturing businesses, nearly 65% of the transport, retail & distribution sector and under 64% of financial/business services.

When asked to describe what respondents believed to be the single most important factor influencing awareness of purchasing and supply risk within their own organisations, customer requirements had emerged as the overall front runner. Through carefully monitoring supplier contracts, relationships and performance, comprehensive risk assessments can be profiled and problems foreseen and avoided, or opportunities successfully managed to fruition. Partnering and outsourcing has led to increased relationships and more prudent performance measurement tools.

Example – Risk management for temporary staff

The recruitment and management of temporary labour is often a very strategic spend category for organisations. People, their quality of work and overall attitude, integrity and appearance can have a major impact on the performance and image of your organisation. For some industries, where customer facing personnel deal with highly personal and data protected information, the risks of getting it wrong are high. There have been several reported incidents where bank account details have been sold from customer call centres costing one particular bank over £230,000, not to mention the reputation impact on customer security assurance.

The role of the P&SM professional is to pre-empt these risks and put processes in place to highlight, mitigate and avoid them where necessary. A starting place is thorough pre-screening of suppliers prior to contract negotiation. It is good practice to carry out site visits and screening of the suppliers internal processes. In a call centre environment criteria such as monitoring staff calls and e-mail, the use of USB data sticks and CDs in hard drives, restricted access to reporting and the storage of customer data are just some examples of issues that should be considered; as well as system support, data back-up and business continuity plans. Critical issues such as these should be written into the supplier contract and the relevant KPI's logged and regularly monitored.

Once the supplier has been awarded the contract it is advisable to regularly audit both the suppliers and buying organisations processes. Suppliers should be encouraged to self audit and report back with regular management information, as well as the buyer carrying out spot checks and regular scheduled audits. Where this level of detail and potential risk exists a collaborative relationship should be formed. By meeting on a regular basis and implementing a

process of continuous improvement of joint objectives, risks are generally reduced and often avoided. Relationships must be forged to ensure that both parties have a shared and mutually agreed value proposition, allowing scope for innovation and process improvement from both parties. Selecting the right supplier to engage with is critical; too small and their internal resources may not stand the pace, too large and you will be seen as a nuisance to them and they will be less likely to employ joint initiatives.

As well as considering the confidentiality and data protection issues, often the more perceived simple issues such as getting the right person on site in a timely manner and reconciling accounts are over looked. The aged debt for temporary staff agencies is a problem that has been around for some time. These aspects of the purchase to pay process are of equal importance as they have the potential to damage a strong working relationship between buyer and supplier and therefore impact security of supply. This value-adding, end to end risk consideration is where procurement professionals really make a difference.

Summary

The Cranfield study concluded that when it comes to best practice risk management in purchasing and supply, one size is unlikely to fit all. Analysis of how companies assessed and managed risk revealed a complex picture with distinct differences between sectors. For example, while recent disruptions to supply were a major influence in manufacturing, it was corporate responsibility risks that had the greatest impact in retail and the public sector. For financial services companies, it was changes in business strategy that drove change.

The risk management tools however are more commonplace. Fixed price contracts, collaborative relationships and closely monitored key performance indicators are common across most sectors. The role of the procurement professional is to ensure that both internal and external contacts are on red alert to monitor the identified weakness in the supply chain and act quickly to remedy them.

Risk management in the supply chain is more about resilience; risk is on the increase and is part and parcel of our business lives. Often it cannot be avoided so a method for managing and minimising its effects is the only way forward. A lack of time and resources is a common problem; therefore procurement professionals need to raise the awareness and understanding of supply chain risk management tools and techniques in order to obtain recognition at a senior management level, and ensure it is given the time and attention it requires.

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