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Developing a Purchasing Strategy

The role of purchasing is being transformed to one of supply management. This new focus requires organizations adopt a strategic orientation to their purchasing function and to look more at the total supply chain management process. This requires linking the purchasing strategies with the overall business strategies and moving from a purchasing focus to a supply management focus. To do this successfully, especially in larger organizations, involves breaking-down functional walls with the use of cross-functional teams. As a result, costs can be optimized across the supply chain and not just within an individual function.

An important step for this transformation is the development of a purchasing strategy. This strategy provides a road map for the purchasing organization and can be used to embed the process across the organization. It is a collaborative and structured process of critically analyzing an organization's spending and using this information to make business decisions about acquiring goods and services more effectively and efficiently. The strategy is a detailed plan on how to approach the marketplace including what you want to achieve and how you are going to accomplish it. In addition, it helps align purchasing activities with company goals both short-term and long-term. The strategy defines the relationship between you and your supplier as well as different buying tactics given different market conditions and supplier relationships. The goal of the strategy is to obtain a competitive advantage by interacting with the marketplace better than your competitors.

A good purchasing strategy provides a document that can be used to communicate strategies within and outside the department to help with buy-in and implementation from different functional groups. While tactical execution is ongoing, strategies should be developed to last for 2-5 years, but they should be flexible to allow for occasional changes if needed. Good strategies are both objective and subjective as they combine data with seasoned judgment. Depending on the size, scope, and complexity of the category, strategies can vary from simple to elaborate – the process is the same, but more time is spent on each step for more complex strategies. An important element of a purchasing strategy is they define what you will do and what you won't do. Too many times, a new strategy is put in place, but old processes are still followed. As a result, the outcome is less beneficial than planned.

There are different models for developing a purchasing strategy, but most contain these major elements:

1. Analyzing the category spend
2. Determine business requirements
3. Assess supply markets
4. Develop purchasing strategy
5. Execute, manage, and refine the strategy

Analyzing the Category Spend

The first step in developing a purchasing strategy is to analyze the category spend. Gather data from internal sources, the industry, and suppliers, and include macroeconomic factors if necessary – this can be a challenge, but it is a key step. This data will be used as the foundation of the strategies and tactics that will be developed and also helps build a knowledge base within the purchasing organization. Gathering and analyzing the data provides a comprehensive look at the internal and external factors that can impact your business and how you source different items. One tool that can be used is TCO or Total Cost of Ownership. This is a useful analysis that can reveal additional costs to an item other than just the purchase price. Often, savings can be found in the other components of the total cost that are either overlooked or unknown.

Determining Business Requirements

In order to develop a strategy that delivers the best results, you need to understand your business needs and capabilities. This analysis is a fact-based process based on company information to gain alignment across other functions and helps prioritize strategies and tactics. It also enables "what if" discussions – challenge sacred cows and disrupt the status quo. Sometimes, this is where big opportunities lie. A category positioning matrix is a great tool to develop for key items and will help in the development of the purchasing strategy.

Assess Supply Markets

After the inward analysis to determine the business requirements, the next step is to look outward and assess the supply markets. This step requires gathering more data, this time on your suppliers and potential suppliers and should be kept up to date over time. There are several tools that can help with this analysis including Porter's Five Forces and a SCOPE analysis. A best practice is to know your market and your suppliers better than anyone else.

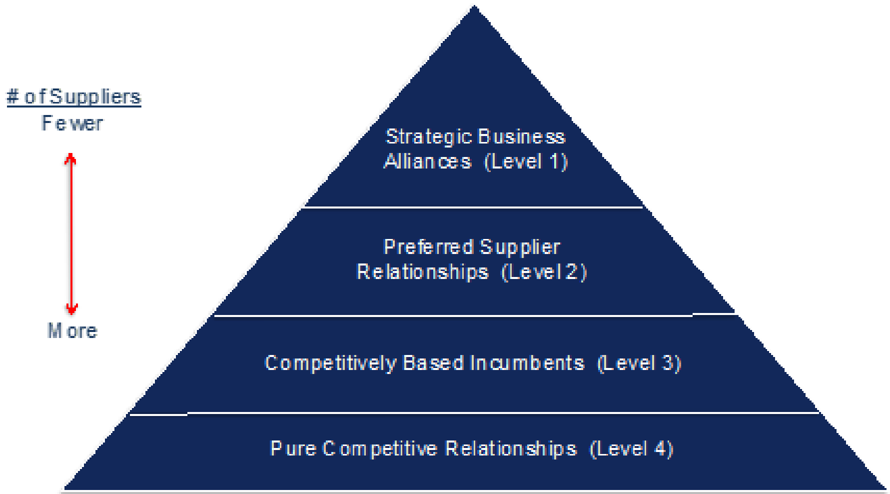
Develop Purchasing Strategy

Utilizing data and information from the prior steps, you then develop a purchasing strategy. It defines the goals of the strategy as well as the tactics used to execute it. The goals should be measurable, time bound, and aspirational yet realistic. A strategy should also incorporate one "Big Idea" into the strategy – this can help push the boundaries of what is possible. The framework of the strategy includes the following:

- Statement of strategy – what you will do and the basis and rationale
- Desired results and time frame – deliverables and deadlines
- Tactical plan and measures – how the strategy will be implemented and results measured
- Approval and alignment
- Tools used to develop the strategy – TCO, SWOT analysis, Porter's Five Forces, Category Positioning Matrix, SCOPE analysis, etc.

Execute, Manage, and Refine the Strategy
Once the strategy is developed, the next step is to execute it. Different strategies require different tactics for execution and a variety of tools can be used depending on your strategy and tactics. As the strategy is executed, it will likely need involvement from other functions (e.g. plants, R&D, marketing, sales, finance). Metrics should be developed to measure the progress and success of the strategy. In addition, the strategy should remain visible and refinements made if necessary.

Before executing the strategy, a Supplier Segmentation analysis should be performed in order to define your relationship with each supplier. The relationship definition then helps guide the type of approach needed to implement the strategy. There are four tiers of relationships shown in the pyramid below.



Using the results of the category positioning matrix and the supplier segmentation analysis, you develop your approach to the market. There are a variety of tools that can be used depending on your strategy and tactics – competitive bidding, negotiations, leverage or consortium buying, joint cost savings initiatives, risk assessment and management, and supplier intervention.

Implementing a sourcing strategy should be approached in the same manner as any other major project. Use formal project management methodology and tools to implement the plan and monitor its progress. The tasks should reflect activities, resources, and milestones for achieving the strategy's targets.

Using this structured process can challenge the status quo and help find new ways of purchasing that can result in cost savings and process improvement. Cross-functional teams should be used to develop and implement the strategies, which should be aligned with management and stakeholders. Finally, devote time to work on it as it can yield significant rewards for the company.

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