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Collaborative sourcing

**How GCC group
organizations can
optimize their
procurement spend**

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Executive summary



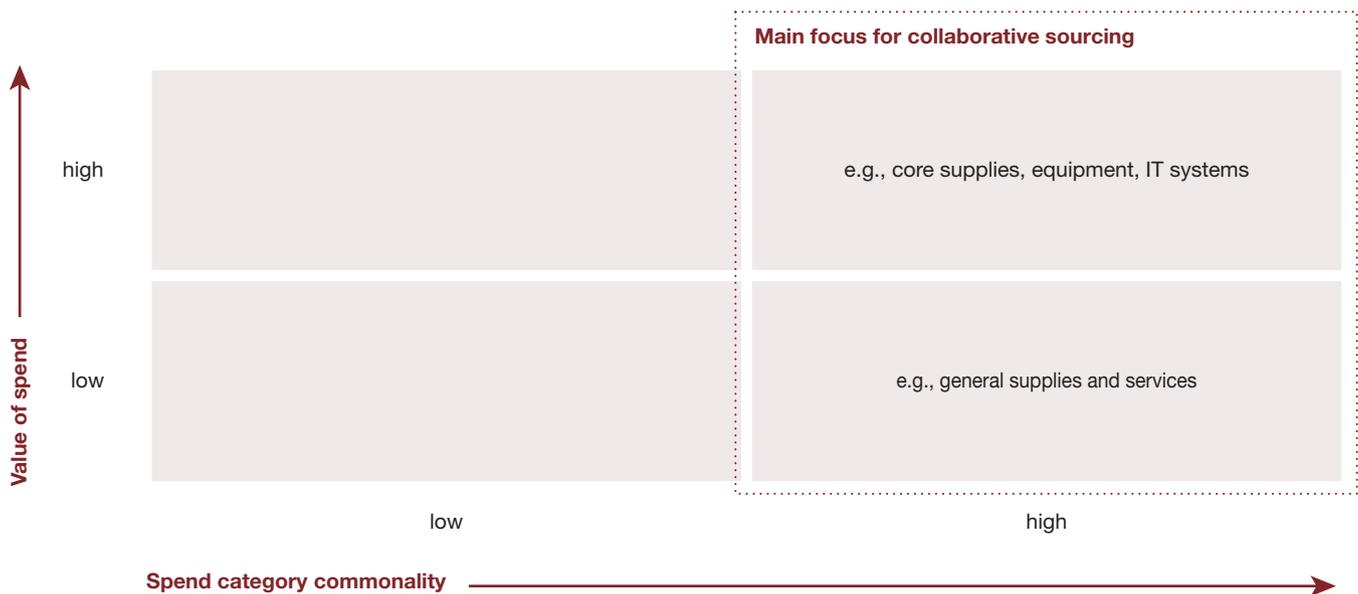
Many large group organizations have not yet mastered the art of group-wide collaborative sourcing. These organizations may be family conglomerates, multi-business-unit corporations, investment portfolio companies, or government bodies with multiple departments. If this shortcoming in procurement could be addressed, a significant amount of value could be captured through various factors: product standardization, economies of scale, reduction in supply chain complexity, strengthened negotiating power with suppliers, and improved sourcing capabilities. With mounting cost pressure resulting from increased competition and the macroeconomic environment, these group organizations need a more comprehensive approach to collaborative sourcing.

A comprehensive approach to collaborative sourcing

To create the case for collaboration at the outset, the organization must conduct a detailed spend analysis. This analysis should identify the common spend categories across the group entities and the values associated with them. This reveals the potential size of the opportunity. Group organizations whose various entities have several spend categories in common should benefit the most from collaborative sourcing (see Exhibit 1). At the very minimum, most group organizations can collaborate on the spend related to general supplies and services, such as office equipment, facilities, and travel.

Exhibit 1

A spend matrix identifies collaborative sourcing opportunities



Source: Strategy&

Select the right operating model for collaborative sourcing

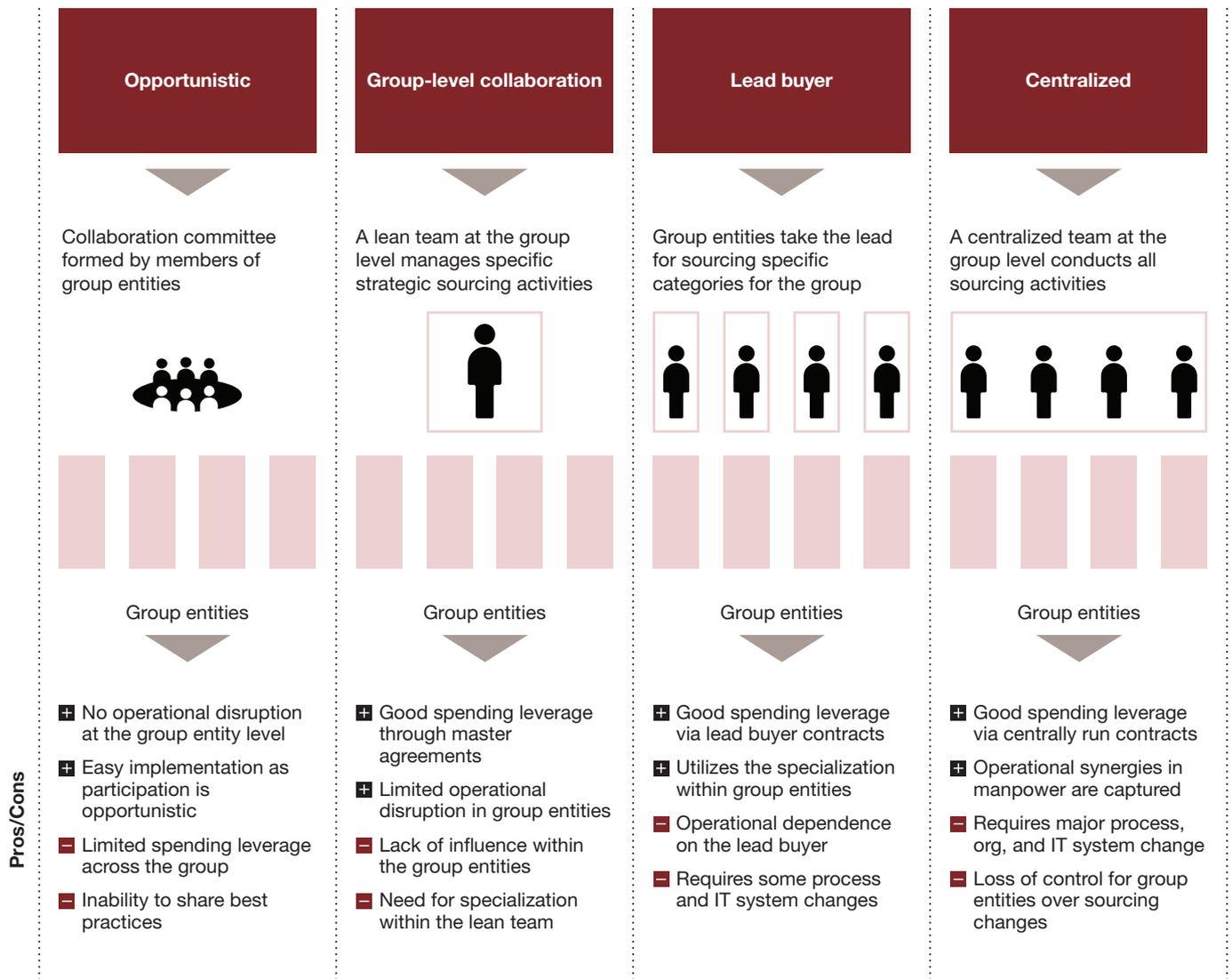
Once the case for collaborative sourcing has been established by identifying sizable common spend across the entities, the target operating model is selected. The model could include a mix of collaboration options that are most suited to the nature of the particular spend categories. These possible options are: opportunistic, group-level collaboration, lead buyer, and centralized (see Exhibit 2, page 6).

For the **opportunistic** option, the group entities collaborate on sourcing opportunities on a case-by-case basis. The collaborative effort in this option can be carried out by a committee with representatives from the group entities. Those on the committee would meet on a regular basis to discuss potential opportunities for collaboration. At the very minimum, they would share sourcing strategies and plans with each other.

In the case of **group-level collaboration**, a lean team at the group level takes charge of collaborative sourcing for common categories across the group. The main tasks of this team include overseeing a standardized item master-list, creating and maintaining master agreements, and managing key supplier relationships. The master agreements would typically contain a price list and terms of reference for common items, and would be adopted by all group entities as a basis for their contracts. With this option, contracts and procurement activities would remain within the group entities, causing minimal disruption to operations.

The model could include a mix of collaboration options that are most suited to the nature of the particular spend categories.

Exhibit 2
Collaborative sourcing operating model options



Source: Strategy&

In the **lead buyer** scenario, an individual group entity is selected to lead the sourcing of specific categories on behalf of the whole group. Each selection is based on the strength of the group entity in that category. This can stem from the group entity's share of spend, particular technical expertise, or the strength of its supplier relationships. The selected group entity carries out all sourcing activities for the category, ranging from transactional procurement to contract management, for the entire group. This option renders the other group entities highly dependent on the lead buyer for their operational needs.

By centrally managing all procurement activities for common categories across the group, the **centralized** option provides the highest level of collaboration. Such an option produces economies of scale for sourcing and increases operational efficiency by centralizing the procurement staff. This option works best where a group organization is already considering a shared services model for other functions.

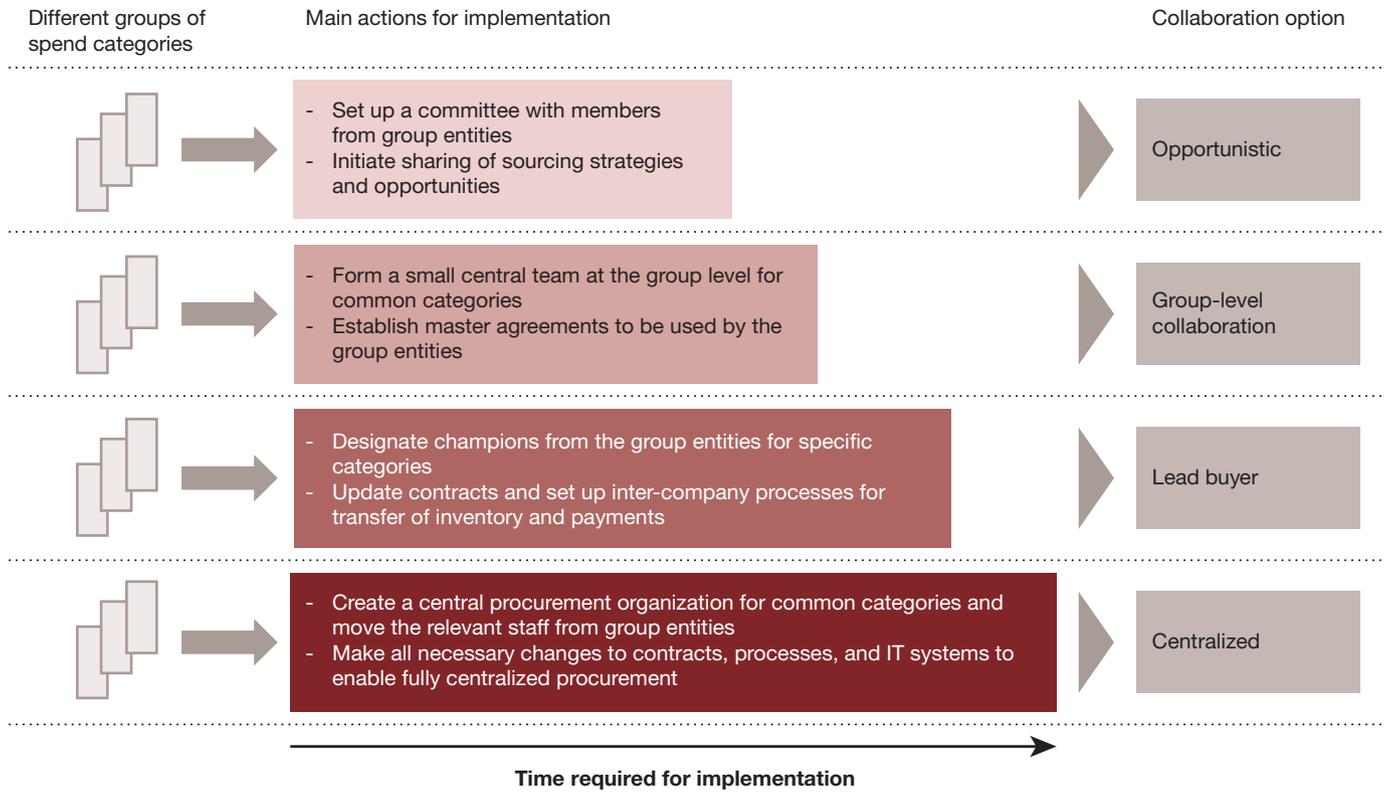
Rather than just defaulting to traditional centralized procurement, organizations can tailor the operating model for collaborative sourcing to suit the relevant spend categories. For instance, a centralized option could be adopted for common and low-value categories. At the same time, master agreements could be set up for common, high-value categories. In the latter case, the group entities take advantage of standard prices and terms negotiated with suppliers for the entire group, but yet maintain control of operational procurement.

Set the requisite conditions for implementation

The actions required for each of the collaboration options within the target operating model vary from one to another (*see Exhibit 3*). For example, whereas the opportunistic collaboration option requires only that a committee be set up to start functioning, the centralized collaboration option would necessarily involve significant changes in organization, processes, and IT systems.

A move toward collaborative sourcing will be successful only given certain conditions. First, a standard item codification system should map the spend data of group entities, so that collaborative sourcing opportunities can be identified and acted upon efficiently. Second, the choice of operating model and implementation road map should reflect the actual business priorities of the group entities. Finally, senior management should offer strong support for the transformation, ensuring the necessary commitment is obtained from group entities and effective change management is instituted to guide the organization toward a new way of sourcing.

Exhibit 3
Summary of implementation actions



Source: Strategy&

The centralized model in a large government department

Various units of a large government department, with an annual spend of several billion dollars, were sourcing common categories with minimal coordination or collaboration at the group level. There were multiple suppliers for common items and equipment, and they offered different prices and terms to various buyers from the department. Sourcing was inefficient, and resulted in increased complexity for asset management and the supply chain.

The organization embarked on a multi-year transformation program to institute a centralized option. It created joint sourcing centers of excellence at the group level to specialize in specific spend categories. These centers of excellence were responsible for all end-to-end

sourcing activities for the group, with their level of service monitored via well-structured service-level agreements.

Today, the centers of excellence are the single point of contact within the group for their assigned spend category. They create and monitor the spend budget, maintain contracts and supplier relationships, execute day-to-day actions related to procurement, and push consistently for cost improvements. Such a transformation has enabled the organization to standardize (and reduce) prices, take advantage of economies of scale, reduce supply chain complexity, and build strong sourcing capabilities. The procurement lead time and manpower requirements have both been reduced by around 50 percent.

A mix of the centralized and group-level collaboration models in a hospital group

A group of hospitals with many spend categories and suppliers in common wanted to achieve standardization and sourcing savings by adopting a collaborative sourcing model. Each hospital was using a different item codification system, and procuring several common categories at different prices and terms. The group as a whole was not fully utilizing its combined economy of scale.

As a first step, the group conducted a detailed spend analysis together with an item standardization exercise, using the United Nations Standard Products and Services Code (UNSPSC) system. When designing the target operating model, the group selected different collaboration options for different spend categories. For

instance, a centralized option, where a central team would conduct all procurement activities on behalf of the group, was chosen for non-clinical categories. However, a group-level collaboration option was chosen for clinical and pharmaceutical categories. For this option, operational control of procurement was left with the individual hospitals, which were then supported by a group-level lean team that set up and monitored master agreements.

An estimation of the benefits for key clinical and pharmaceutical categories revealed potential annual savings of 8 to 10 percent from collaborative sourcing, mainly through group-wide volume consolidation, supplier negotiations, and product rationalization.

Conclusion

Many group organizations have not developed an effective collaborative sourcing strategy and so are unnecessarily disadvantaged. By selecting and implementing the model most suited to their specific circumstances, such organizations can exploit an important but often overlooked opportunity to capture major benefits, such as greater standardization and cost savings, thereby securing competitive advantage.

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