

## Best Value Sourcing

# From Price Squeezers to Value Creators

Between 60 to 90 percent of industrial value added is no longer generated in-house. Increasingly, supplier performance determines corporate competitiveness.

The necessity of concentrating on core competencies and the resultant purchasing of externally generated goods and services is reducing the level of in-house value added. Consequently, success in the marketplace increasingly depends on the performance of a company's suppliers. Not surprisingly, value creation management in purchasing has evolved into a key function of business operations. A «best value sourcing» strategy can make a significant contribution: it supports the selection and integration of suppliers when building sustainable value creation partnerships.

### Room for optimisation

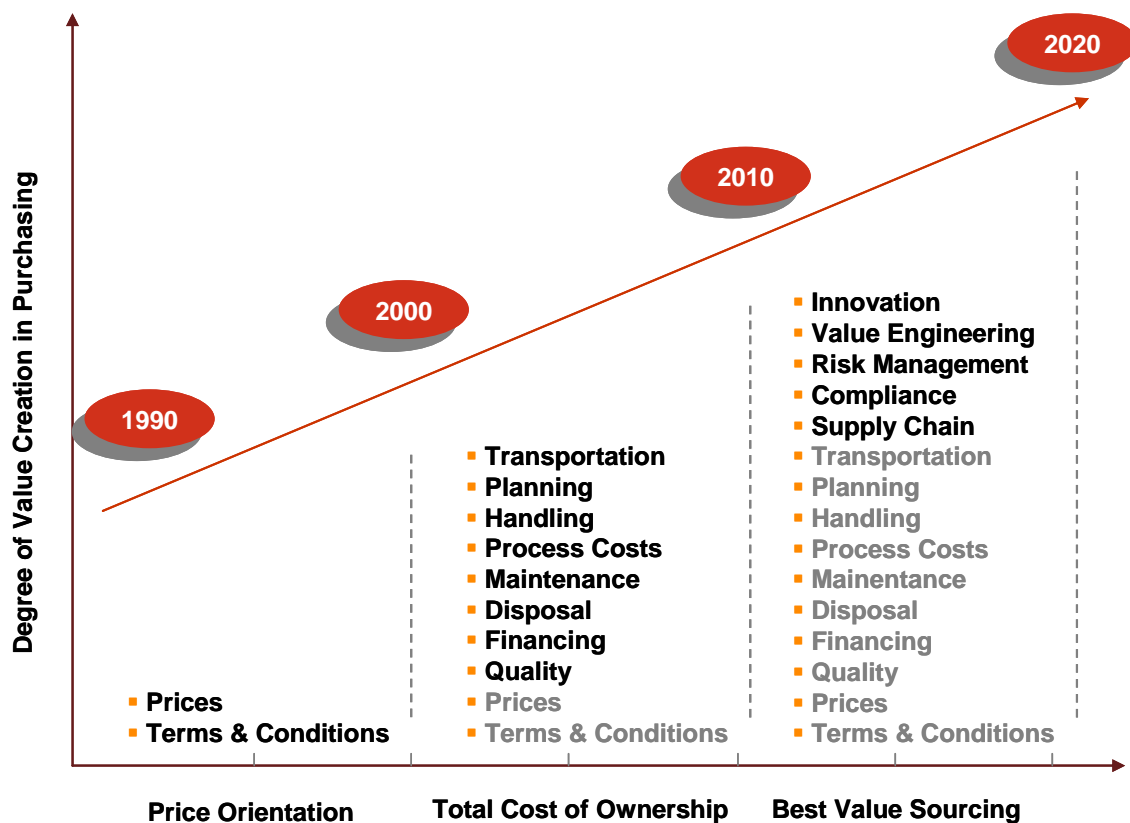
In the past, lowest-cost purchasing strategies served primarily to force down purchase prices and consequently, costs. Purchasing managers fulfilled their responsibilities if they conducted negotiations with the clear objective of squeezing prices. The problem with this approach, however, is that it does not allow cost-cutting potentials to be exploited to the full. This is because the development of other costs that are incurred when carrying out business with the selected suppliers tends to be overlooked. It is from this perception that

the concept of «total cost of ownership» (TCO) – the overall consideration of costs – has developed. This method also takes into consideration those cost components that are not included in the purchase price, e.g. logistics, handling or transport costs. Only through TCO is it possible to compare the true purchase prices offered by different suppliers in the quotation phase already. However, here too, the focus is exclusively on cost.

### More than just costs

By applying the «best value» principle, the value creation processes beyond the in-house limits are taken into consideration. In addition to the straightforward optimisation of total purchasing costs, performance and value creation potentials of the individual suppliers are taken into account. This perspective allows the supply chain partners to generate joint strategies along the supply chain, both in the sectors of innovation and development, risk management and compliance, as well as in logistics and materials management. This logically requires close coordination with the suppliers. The structures and processes of such value creation partnerships have to be consistently optimised in the context of continuous improvement. Hitherto unimaginable scope for potential benefits is often opened up.

Original article published in Handelszeitung | No. 20 | 19<sup>th</sup> - 25<sup>th</sup> May 2010 | Special Beschaffung



((Fig. 1)) Evolution of purchasing value creation

The parameters for value creation partnerships are demanding and lie within the scope of responsibility of the management board. Purchasing and supply chain strategies must closely match the corporate and value creation strategies. Professional supplier management, which clearly defines the methods for evaluating, selecting and developing supplier potentials, is a success factor. Through effective supplier relationship management (SRM), suppliers are incorporated into the planned value creation strategies. This provides the parameters for common orientation and successful cooperation. Depending on the significance and intensity of the partnership, differentiated collaboration strategies within the supplier network need to be generated. This in turn calls for a high degree of willingness for cross-functional cooperation at all levels, which frequently goes hand in hand with an improvement in the qualifications of the company departments involved.

### Exploiting the challenge as an opportunity

What was considered a vision only a few years ago has since become reality: increasingly, success in the marketplace is determined by the competitiveness of the value creation chain, which depends on the performance capacity of the partners. Companies wishing to improve in this area need to review their business processes, while focusing sharply on their purchasing operations. The strategic and operational implementation of the findings is a challenge for both the company and its employees, but pays dividends in the future. A number of industrial companies have already begun to take on this challenge and are exploiting it as an opportunity for developing a solid competitive position.

### Markus Götz

Senior Consultant  
Inova Management AG  
[www.inova-group.com](http://www.inova-group.com)