Procurement Performance Management project

Highlights of an assignment to design and implement a Procurement Performance Management System

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Some numbers and characteristics have been modified to protect the confidentiality of the Client.

The company

- Tier one automotive supplier, headquartered in Canada.
- $407 mi revenue, $312 mi third party expenditure, direct and indirect ($61 mi).
- Specialized in stamping, welding, surface treatments and mechanical subassemblies including some cabling.
- Six industrial sites in Canada, US and Mexico.
- Two sites host Engineering teams for proposals and co-development with OEM's.
- All plants are ISO 9001 certified.
- Historical organic growth, complemented by acquisitions to follow customer base.

Need for change

- Request as expressed by CEO and Group CFO.
- *"… We have a good Procurement function, but claimed savings are nowhere to be found in P&L..."*
- *"… We need an unbiased way to report Procurement savings..."*

- After CEO and CFO input, Initial assessment was performed by conducting 21 guided interviews of personnel from all relevant functions.
- ERP is up to date, used consistently across plants and an effort is made to maintain data clean and accessible.

Initial assessment - Highlights

- Main procurement categories: Steel, metal parts, fasteners, rubber/plastic parts and harnesses.
- About 25% of production items are renewed every year.
- Budget planning every six months.
- Financial review against budget conducted every month.
- Procurement expected “savings” for direct are pre-included in the budget. Not for indirect Procurement.
- Variable compensation calculated and paid twice a year, based on meeting the budget and other functional KPI’s.
- Supplier Quality function reports to Procurement.

Initial assessment - Highlights

- Inconsistencies between plants/countries: Three different methods of calculating savings on production parts.
- No established rules for indirect categories.
- No link between calculated savings and impact on EBIT.
- Cost avoidances mixed with real recurring savings.
- End of tooling amortization counted as savings.
- Price increases not taken into account and reported.
- Unclear “ownership” of savings resulting from multi-functional initiatives, possibly leading to double counting.

- Nevertheless, budget is consistently met each semester.

Re-scoping of the project

- In view of the initial assessment, decision is taken to completely redesign the Procurement performance management and reporting.
- Expected outcomes:
  - Redefinition of Procurement performance.
  - Unbiased calculation and production of relevant KPI’s.
  - Unquestionable performance reporting.
  - Processes and tools raised to the next level.
  - Clear cut clarification of responsibilities.
  - Appropriate training for all stakeholders.

- → Creation of a Procurement Performance Review Board.

Procurement Performance Review Board

- PPRB composed of Procurement and Finance delegates from each country. Representatives of other functions as required for specific multifunctional initiatives.
- Co-chaired by Group CFO and CPO.
- Roles and responsibilities:
  - Definition of Procurement performance and impact on EBIT.
  - Supervision of the timely production of KPI’s.
  - Validation of Procurement KPI’s.
  - Reporting at monthly Financial review.
  - Evolution of KPI’s as needed over time.
  - Organization of audits ref. Procurement performance.

Procurement performance vs. Impact on EBIT

- Procurement performance and its impact on EBIT are two distinct quantities with different purposes.
- Procurement performance is used to manage the function and monitor improvement initiatives. Its impact on EBIT is the financial reality to be reported at corporate level.
- Both amounts are meaningful and should be measured.
- Procurement has a potential impact on main components of EBIT, including revenue, COGS, SG&A and depreciation.
- → Need for a new set of KPI's with clear rules to calculate and report Procurement performance.

New KPI’s and calculation rules

- Most important changes to KPI’s:
  - Introduction of a “Procurement index” and a “Raw material index” to account for price variations in direct goods.
  - Calculation and reporting of “Procurement impact on EBIT”, “Procurement ROI”, and “Cost of supplier non-compliance”.
  - In doubt, savings are not reported.
- Establishment of a set of rules to calculate performance related to ten different types of value creation.
- Examples of application with inclusions/exclusions and required data in a “Procurement Value Creation Matrix”.
- Only four KPI’s for Reporting at Corporate level.

New set of KPI's

	Initial KPI's	New KPI's	Reported Corporate level	Perimeter				Frequency		
				Plant	Global	category	Supplier	Weekly	Monthly	Biannually
Corporate performance	Procurement Savings	Procurememt ROI	X		X					X
	Budget met Y/N	Total Procurement $ impact on EBIT	X		X				X	
Supply Management performance		Procurement index for direct	X		X	X			X	
		Raw material index			X	X			X	
	Contract coverage %	Contract coverage %		X	X	X				X
	Procurement coverage %	Procurement coverage %		X	X					X
	Avg. cost of processing a PO line	Automatic/electronic PO lines %		X	X		X		X	
		Change orders %			X		X		X	
	Requisition to PO turnover time	Procurement lead time		X	X	X			X	
Supplier performance		$ value of implemented supplier ideas		X	X	X	X			X
	Nb. Of red suppliers	Cost of supplier non compliance	X	X	X	X	X		X	
	Late deliveries %	Late deliveries %		X	X	X	X	X		
	Non conformities - Lot %	Non conformities - Shipments/Lot %		X	X	X	X	X		
	Non conformities - Parts %	Non conformities - Parts %		X	X	X	X	X		
Supply Base Management	NB suppliers 80% spend	% spend with strategic suppliers			X	X	X			X
	Nb of suppliers	Nb of active suppliers		X	X	X			X	

Situation at the end of the project

- Separating Procurement performance from reporting of its financial impact on EBIT proved to be instrumental in restoring trust with stakeholders and C-suite.
- Performance validation and reporting under supervision of PPRB is widely accepted.
- All personnel has been trained to KPI’s and calculation rules.
- Production of KPI’s is reasonably automatized.
- A position of Financial Analyst was created in Procurement.
- Savings on Direct and Indirect are pre-included in budget.
- Objectives and variable compensation are linked to KPI’s.
- Increased trust in KPI’s and clear calculation rules fostered multifunctional initiatives with shared objectives.

Thank you

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Questions?

Next steps

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