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# Purchasing power: Lean management creates new value in procurement

Lean management is about much more than cost reduction, making it a powerful set of disciplines for increasing purchasing's effectiveness.

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From its roots in automotive manufacturing, lean management has expanded quickly through much of modern business, from manufacturing-related functions such as maintenance and R&D to industries as varied as healthcare and financial services. Whatever the concept has touched, it has transformed, delivering dramatic improvements in productivity and quality while empowering employees to continually improve the systems in which they work.

In most organizations, however, lean management runs into an important wall: the one by which the

purchasing department sits. In our experience, to the extent most procurement functions have thought about lean management at all, they have viewed it primarily as a way to streamline and automate procure-to-pay (P2P) activities. Lean management's capacity to deliver significant value in strategic procurement has largely been ignored.

The reason may be obvious. Despite procurement's influence, its operating costs are usually very low: on average, between 0.3 and 1 percent of spend in most industries. For procurement leaders who

see lean as a tool for wringing out efficiency improvements, those numbers hardly seem to promise much potential.

That mind-set should change. Properly applied, the disciplines and systemic thinking of lean management can become a strategic weapon: aligning purchasing more tightly to internal customers' real interests, helping leaders rethink the end-to-end procurement process (from suppliers through to manufacturing and ultimately to external customers), and transforming the effectiveness of strategic procurement activities.

Think of what procurement people do each day. How much time do strategic buyers spend on truly value-adding activities, such as building a deeper market understanding in key categories, identifying and qualifying new potential suppliers, or negotiating the best possible contracts? In all likelihood, much less than you think. At one large industrial company, our workload analysis found that strategic buyers often devoted less than 40 percent of their time to these core activities. The rest was lost on distractions such as administration, filling in reporting templates, and completing tasks that should have been the responsibility of operational procurement staff.

Now imagine you could change that situation. Cutting your administrative and reporting burden and optimizing your core processes could allow your buyers to focus more than 70 percent of their time on strategic activities. That's the equivalent of doubling the size of the strategic procurement function without adding a single person.

A broader and more thoughtful lean-management perspective doesn't just help companies maximize the effectiveness of their current processes. It also allows companies to take a more integrated view of the value each individual buyer creates. It helps them answer important strategic questions,

such as which activities should be kept in-house and which should be automated, allocated to near- or offshore shared-service centers, outsourced, or stopped altogether. Standardized activities, fewer processes, better-qualified buyers, continual people development, and resources sharply focused on activities that add real value—this is what we understand as lean procurement.

The advent of lean discipline in purchasing is timely for another reason: digital is set to have huge impact on the function, with many new solutions that extend beyond today's P2P automation and could transform the end-to-end procurement process. Tools such as standardized should-cost analyses, workflow portals to manage the full strategic-sourcing process, and access to huge external supplier databases for market research will allow strategic buyers to spend even more of their time focusing on the right things. And the efficient, structured processes enabled by lean management provide the perfect framework for integrating these new tools.

### **Applying a lean lens**

Bringing lean-management discipline to purchasing requires action in five areas (see sidebar, "How one leader brought lean management to procurement"). The first step is to develop a deep understanding of the needs of procurement customers: not only the business units that work directly with the procurement department, but also the organization's end customers. Next is to simplify, automate, and streamline processes to meet those needs as efficiently and effectively as possible, both in strategic procurement (such as with standardized request-for-quotation—or RFQ—systems) and in operational procurement (such as with no-touch order processing). Third is to build the skills and structures procurement needs to achieve those goals, including a clear split between strategic and operational procurement roles. Fourth, the function must tighten its

# How one leader brought lean management to procurement

The head of procurement at a global insurer describes how lean management enabled her team to increase capacity dramatically while reducing risk and delays.

When we started, we were already tracking a wide range of metrics—too wide, actually. The challenge became, “So what? What are the metrics telling us?” We started digging further into the purchase requests, or “tickets.” Most were for fairly minor purchases, such as hiring a training consultant for a few weeks for \$100,000. Only a few were for bigger deals, say, \$50 million to outsource a significant amount of work for one of our business lines. The trouble was that the low-risk, low-dollar tickets and the high-risk, high-cost tickets went through exactly the same process.

Where’s the **value for our customer** in that? The person requesting the trainer was waiting for days or even weeks to get a reply. Meanwhile, my people were having a hard time finding the capacity to think through all of the due-diligence issues that a big outsourcing contract raises.

We had to think through **standardization in a new way**. Now each of these types of ticket has its own standard, one that relies on automation for low-value tickets so that we free more time for the high-value, high-risk ones. We’re separating our strategic decisions from our day-to-day operations.

Most of these changes are coming from our own people, **building their capabilities** for problem solving along the way. They told me what the top five problems were, and I then asked them to get their own teams to solve them within 90 days. My view is that even if the idea your associates come up

with solves only 80 percent of the problem, because the solution came from them, they’ll implement it so much better than they would a 100 percent solution that came from somebody else. My job is to coach and guide and ask questions.

We’re also reconfiguring how we **assess performance**, and using it to make further improvements. The ticket process sends out an automatic survey after every request. Although the response rate could be higher, even what we have received has helped. Quite a few requesters said they didn’t know how long the process would take. Now we send an email within 24 hours to set expectations: “Joe or Jane will be handling your request. Given the dollar value, etc., we expect that the approval process will take X days.”

We’ve standardized how we do due diligence on our larger vendors, and outsourced some of the work so that we can get a report in 15 minutes instead of hours or days. That means I can use people’s skills a lot more effectively.

All of these changes have allowed us to reduce the number of tickets in our queues by about 40 percent. But the **biggest changes are in people’s mindsets**. They’re pushing for bigger improvements, bigger targets. They understand that it’s better to set an 80 percent target and achieve only 60 percent than to set a 25 percent target and achieve 32 percent: 60 percent is a lot more than 32 percent.

performance management, using indicators that focus on real value creation (for example, the function's overall cash and profit-and-loss contributions). Finally, and most importantly, the organization must systematically change the mind-sets and behaviors of its people, creating a culture that focuses on continuous improvement in meeting customer needs and eliminating waste.

### **Understand the customer**

The starting point for lean management is always the customer. Sometimes, purchasing functions are guilty of delivering what they *think* is best for the rest of the business, rather than what *actually* is best. To bridge the gap, companies need a systematic approach to understanding their customer needs, with structured interactions, business collaboration portals, and voice-of-the-customer interviews. Strategic procurement councils, for example, ensure that representatives from individual business units and their counterparts in procurement can meet to discuss current performance and future plans. At one company, the council learned that business-unit leaders don't actually read the company's centrally generated purchasing reports. Scrapping these reports, which were labor-intensive to produce, freed up central purchasing capacity to focus more effort on strategic raw materials.

The most advanced companies ensure these platforms are a forum for two-way conversation. Their business units recognize the role of procurement as a "demand shaper," and they value its input on topics such as specification management or purchase volumes that can often unlock savings.

### **Standardize processes**

Once a company understands how procurement's activities generate value for the business, it can explore new paths to do deliver the value more

efficiently. Value-stream mapping—a tool adapted from manufacturing—can be a powerful way to separate the worthwhile steps in a process from the wasteful ones, so that the process can be simplified and redesigned.

The approach applies equally well to strategic and operational procurement processes, but with a few important differences in execution.

#### **Standardize strategic processes**

Understanding exactly why particular activities exist can lead to rapid, significant savings in time and resources for strategic personnel, whose workloads tend to be more complex and varied to begin with. Long, tedious update meetings become dramatically shorter through simple measures such as exercising better control over the agenda or sharing data with participants in advance.

Standardization can considerably reduce repetitive or duplicate activities. For example, a central department can find potential new suppliers in external databases, while developing standard criteria for supplier selection can greatly accelerate the prequalification process. Similarly, standard templates simplify the development of category strategies, and modular contract terms make agreements faster to generate and less likely to omit important safeguards. To avoid stifling creativity and entrepreneurship, however, companies must carefully distinguish between the activities that can be standardized and those that need more flexibility. A collection of the best "carrots and sticks" for negotiation preparation, for example, can provide the right balance.

Automation, already widely used in operational processes, is an underdeveloped area in many companies' strategic-procurement activities, and can further support standardization.



Electronic request-for-X (eRFX) tools simplify the collection and comparison of supplier quotes, and e-auctions can speed up regularly recurring negotiations. Cleansheets linked to raw-material price indexes can be updated at the push of a button, giving teams powerful support for fact-based supplier negotiations.

#### Standardize operational processes

In operational processes, traditional lean-management tools such as value-stream analysis can reveal significant opportunities to improve efficiency and effectiveness. One industrial company using this tool discovered that the number of purchase orders its operational buyers handled every year varied by a factor of four. It therefore captured the highest performers' practices and codified them into new standard operating procedures for the entire organization. Providing additional coaching and training to lower-performing staff helped fill the remaining skills gap.

Standardization in strategic procurement can be a starting point in enriching operational buyers' jobs, by making it easier to automate, consolidate, or outsource repetitive tasks such as managing

supplier master data. In many companies, operational procurement activities could be automated much more thoroughly. For example, electronic catalogs and automated systems allow business units to place orders directly, and automated tracking systems can follow those orders' progress.

#### Build the organization and capable people

Becoming lean in procurement usually means redefining the organization from the ground up—starting with a clearer distinction between strategic and operational purchasing roles. That way, the procurement function's most expensive staff, the strategic buyers, spend more of their time on their most valuable work.

Ultimately, the resulting changes make these strategic personnel remarkably cost-effective. With process standardization and automation, rapid access to valuable internal and external data, and the ability to focus more than 70 percent of their time on high-value work such as category strategies, demand management, and negotiations, strategic buyers in a lean organization can deliver several times the value they would in most of today's purchasing departments.



As their roles evolve, people's skills and capabilities make an even more decisive difference to procurement's overall performance. Advanced procurement organizations therefore pay considerable attention to capability building. Leading companies work hard to capture and share their knowledge—for example, by building central databases on supplier interactions and specification data, or by creating communities in which purchasers and their customers can share insights on the newest market developments.

Often, the best way to develop purchasing capabilities is to put all strategic buyers through a procurement “academy,” with modules covering not only purchasing-specific skills—such as category knowledge, cleansheet cost modeling, and structured negotiations—but also more general competencies in value-stream analysis, root-cause problem solving, and interpersonal communication. Over time, academies reinforce practice standardization, supporting a single “way of working” that ultimately defines much more than how to run RFXs or build cleansheets—it defines the company's culture.

### **Manage performance**

Lean procurement functions look at performance management from a few different perspectives. They monitor the performance of suppliers, to ensure they are meeting quality, cost, flexibility, and service targets. They monitor the performance of individual buyers, both strategic and operational, to ensure they are working efficiently and retaining a focus on the true needs of their customers. And they monitor the performance of the function as a whole, to ensure it continues to deliver real value to the business it serves.

Effective performance management supports lean purchasing departments in two ways. First, the right metrics, targets, and review processes show where the function is performing well and reveal

opportunities for further improvement. Second, by focusing on the metrics that matter, and rigorously applying automation and standardization, companies can often reduce their overall tracking and reporting burden, freeing up more time for value-adding activities.

### **Encourage the right mind-sets and continuously improve**

Lean procurement organizations make new demands on their personnel, requiring them to continually refine and improve their every-day tasks and to think and act in new ways in their interactions with customers, managers, and colleagues. It becomes the responsibility of each purchaser to continually question the activities he or she conducts and to propose better ways of doing them.

A range of powerful methods helps these new ways of behaving take root. Organizations see significant improvements from even seemingly basic steps, such as a 15-minute daily huddle where each procurement team discusses one best-practice element and one critical problem (and its resolution). At one company, managers encouraged their purchasing teams to start each purchasing project by writing a detailed RFQ template to collect all the relevant information up front, preventing time-consuming additional requests down the line. Once developed, the template was adopted as a standard for future RFQs in related categories, and the team's efforts were publicly acknowledged by leadership.



Procurement functions that have embraced lean management have achieved rapid, significant impact. One large European industrial player, for example, adopted lean disciplines as part of an organization-wide procurement transformation across all its diverse business units. Through

a single set of standard methods, the company increased the efficiency of its direct-sourcing activities by around 20 percent and its indirect-sourcing activities by 25 percent. But rather than reduce procurement staffing, the company assigned its newly freed people to a center of excellence responsible for driving the adoption of new tools. In tandem, it increased its savings targets and invested more time in negotiations than before. The new focus enabled the company to reduce spend by double-digit percentages across a wide range of categories. ■

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