

Public Sector Practice

A path to successful state procurement transformation

Transforming the state procurement function is a large undertaking, but it can result in significant improvements in compliance, speed, cost, and quality.

by Greg Pappianou and Aly Spencer



Procurement organizations perform a vital and diverse role in delivering citizen services and facilitating government. Across the public sector the value at stake in procurement is massive—and states alone collectively spend more than \$2 trillion each year on a spend portfolio that ranges from nuts-and-bolts operations such as snow removal to complicated IT systems such as whole-of-government enterprise resource planning (ERP) software.

Today, state procurement functions are under mounting pressure to deliver results in an increasingly complex environment. States face unique challenges that other public entities—including federal departments, cities, authorities, and universities—often do not. Many state procurement functions have a complex mandate that includes directly procuring administrative or commodity goods and services, supporting procurement of department-specific purchases like infrastructure construction, and providing cooperative contract vehicles to municipalities and other local government entities. Beyond this customer and process complexity, the range of products sourced and the aggregate value of procurements exceeds that of many multinational corporations. With many state governments also facing waves of retirements and civil-service restrictions, sourcing the talent to handle these challenges can be particularly daunting.

In response to these challenges, more states are seeking to transform their procurement function. Successful transformations can result in substantially faster processes, better risk management, and higher-quality, less-expensive goods and services. Yet despite their best intentions and efforts, states that attempt transformations often fail to achieve their objectives.

To increase the likelihood of a successful transformation, states are approaching transformation in a new way. Our analysis uncovered the barriers preventing states from fully transforming the procurement office and how to address them, as well as the core elements found in a successful procurement transformation.

State procurement challenges and why transformations fall short

The diversity of procurements and expectations of customers—both employees and citizens—are changing. As private-sector companies reshape customer-experience expectations, citizens and state employees have come to expect speed, convenience, and accessibility from public-sector functions as well. The types of procurements have also changed as states provide more digitized and niche services. Yet as complexity grows, states still find their approaches to procurement are firmly lodged in traditional methods, including the tendency to make individual purchases without a big-picture view of the implications and objectives. This often leads to a number of procurement challenges for states:

- **Long timelines.** End-to-end timelines are too long or increasing under the weight of complex processes and compliance needs.
- **Poor requirements definition.** The type of procured goods and services is evolving into areas where the government has limited in-house experience (for example, cloud-computing services) and therefore has difficulty articulating its need and assessing performance and cost trade-off decisions.
- **Supplier performance management.** Public-sector organizations lag behind the private sector in applying outcome-based performance measures and establishing effective performance assessment and reward systems for their vendors.
- **Difficulty adapting to customer needs.** Highly variable internal “customer” populations have similarly variable needs in terms of cost, speed, quality, and compliance—a one-size-fits-all procurement system rarely satisfies all of these needs.
- **Lack of transparency.** Spend is diffused across government components, with limited central visibility into data necessary for a consolidated procurement-management approach.

- **Talent shortages.** Demand for procurement support outstrips capacity, worsened by an impending loss of expertise from retirements and lagging recruitment and knowledge-transfer efforts.

Procurement functions grapple with these challenges as they attempt to balance their performance against four attributes—speed, cost, quality, and compliance. Organizations that are unbalanced (for example, over-indexed toward one of the attributes) are likely to sacrifice overall performance and create unintended consequences in one or more of the other attributes (Exhibit 1).

Organizations that over-index toward an element without strategic thought almost always end up leaving users unsatisfied across one or more

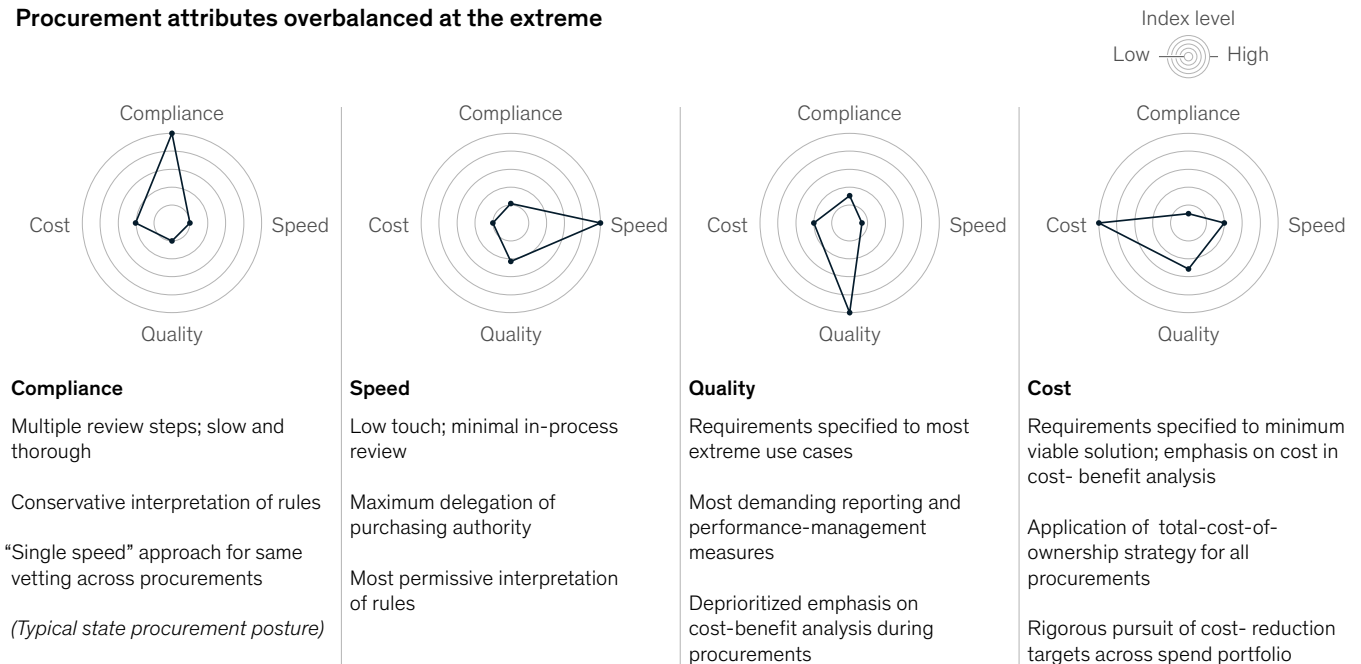
of the other elements. In state government, procurement functions often find themselves over-indexed toward compliance. External pressures like legislative mandates, executive rule making, decades of additive bureaucratic processes, and even serious scandals have combined in many states to generate this compliance focus, and getting compliance right will remain table stakes for any procurement-system change. However, delivering on compliance alone is not sufficient; many state chief procurement officers face “customers” angry about long timelines and products and services that don’t meet their needs, and executives on the hunt for budget savings.

A transformation can help states promote balance along each of these axes, address existing challenges, and rethink the procurement function

Exhibit 1

Many state procurement organizations have overweighted one objective (often compliance), resulting in unsatisfactory performance on other objectives.

Procurement attributes overbalanced at the extreme



A transformation can help states promote balance, address existing challenges, and rethink the procurement function as a vital part of a state's economic growth and development.

as a vital part of a state's economic growth and development. Many states have indeed attempted to transform. Yet state procurement transformations often fail to achieve their objectives (for example, a goal of reducing cost, improving performance, or accelerating timelines) or achieve them—and quickly backslide.

These failures are not driven by a lack of effort or the “wrong” solution being adopted, but rather by failure to build a comprehensive operating model, inclusive of processes and capabilities, that supports a full transformation. The challenges state procurement functions face are interrelated, meaning that change programs targeted at improving a single outcome are rarely effective.

In our experience, organizations attempting to achieve enterprise procurement improvements through highly targeted, narrowly scoped interventions typically fail to realize overall improvement in their procurement performance for several common reasons:

- A full enterprise view of customers and spend behavior is not captured, limiting the interventions to “firefighting” rather than proactive or preventative practices.
- There is a failure to partner with department leaders, the governor's office, and other stakeholders to ensure they have a stake in the outcome and contribute to design.

- The current procurement workforce doesn't have the skills to complement new processes or business models, so they turn to traditional ways of working or adopt new practices and methods in an ineffective or noncompliant manner.
- Behavioral changes in the procurement workforce and customer base are not addressed, and the focus is instead placed on technical improvements—personnel are left with little understanding of why change is happening or how it benefits them.
- An overfocus on IT advancements derails attending to underlying challenges with processes, capabilities, and relationships that provide the base for automation.

The states that take an integrated approach and consider each of these areas are more likely to sidestep derailments and see return on their procurement transformation.

The path to a successful transformation

To address all of these needs simultaneously and rebalance the organization's focus, successful state procurement transformations begin by reevaluating procurement's core function—what is being procured for whom?—and building tailored processes for their customers' needs. This allows procurement professionals to think

and act differently across diverse purchases such as a high-risk, high-cost IT buildout for the state chief information officer versus a cooperative purchasing arrangement that municipalities can use to procure commodity office supplies. Answering this question also helps procurement functions find the right balance of compliance, speed, cost, and quality—for example, a highly resourced procurement function may elect to index toward an increased speed profile knowing faster delivery will incur cost premiums. High-performing organizations make the decision to trade off these elements quite deliberately—they can clearly articulate both why and to what extent they have chosen to overweight a certain element, and what costs and trade-offs they are therefore making on other elements, and achieve the necessary results within each dimension (Exhibit 2).

Once the procurement office establishes its vision and articulates its goals, it can address those common pitfalls and take a step-by-step transformation approach that includes detailed customer segmentation and category grouping,

supported by spend transparency; in each of these segments, the procurement office can then clearly articulate its objectives. From there, the office can develop an integrated perspective on the structure, processes, people, and technology it will need to deliver those objectives.

Start with the foundational elements of a procurement transformation

Customer segmentation

Truly exceptional procurement organizations modulate trade-offs between speed, cost, quality, and compliance to accommodate individual customer segments, each of whom may have different priorities. Similarly, high-performing central procurement functions understand the organic procurement capabilities within each customer segment, as that will dictate the level and type of support necessary for a successful procurement.

For example, a state department of transportation may be most interested in cost and schedule performance of capital projects and have an

Exhibit 2

Balanced procurement comes from designing the procurement operating model to optimize each objective.

Balanced weighting

Index level
Low — High



Compliance: satisfaction of legal and procedural requirements



Speed: end-to-end time from need identification through in-place goods or services



Quality: degree to which procured goods or services satisfy the need



Cost: total cost of ownership for lifetime use of goods or services

established procurement function in-house, whereas an office of information technology may be most concerned with adoption of innovative technologies and have little in-house procurement expertise. The central state procurement function will necessarily need to support these two “customers” in different ways.

Category grouping

Beyond understanding customers, top procurement organizations build their processes differently based on the risk, cost, commonality, and level of innovation needed in a good or service. For example, the compliance requirements and level of detailed technical knowledge needed to procure IT service providers handling sensitive state data is very different from the purchase of commodity goods from well-established vendors.

Grouping similar goods and services into clearly defined categories based on risk, cost, commonality, and level of innovation can aid organizations in procurement analysis, sourcing strategy, and governance. The category approach typically allows an organization to view its entire spend in a common language across components and target its effort where it is most needed to achieve its desired procurement posture. Every organization’s category structure is different and reflects its unique spend profile and priorities, but getting it right is a prerequisite to achieving a balanced procurement posture.

Spend transparency

To inform procurement activity, central procurement functions must establish a full, enterprise-wide view of spend, which is a summary of all enterprise spend typically shown by customer segment (for example, organizational component), suppliers, and category. It provides a fact-base for resourcing decisions by the central procurement function or by individual components, as well as providing the data needed to drive improvements across each dimension of the balanced procurement posture.

Maintaining a centralized view of who is purchasing what enables a central procurement function to implement a system in which core procurement

processes are tailored by customer segment, the procured item’s complexity, and potential value to be gained by aggregating similar procurements across the state. In practice, this customization is typically reflected in variable decision rights between the requirements owner and the central procurement function for requirements definition, category-strategy creation and enforcement, negotiation and procurement approval, and ongoing supplier management. Delivering a balanced procurement approach that fits customer segments well requires a specific set of structural, process, people, and technological attributes.

Build an operating model that enables transformation

Organization and governance

The following structural elements are common in the foundation of an agile, high-performing procurement organization, providing an architecture that allows organizations to create transparency and deliver exceptional outcomes:

- ***Thoughtful and dynamic category strategies, refreshed at regular intervals.*** Category strategies, resulting from rigorous analysis of requirements, spend, and suppliers, outline the ideal acquisition approach and provide guidance to requirements owners and contracting officers in all components. They typically include detailed guidance on supplier strategies, risk management, approaches for maximum value (cost), performance management, and contracting vehicles. The strategies are typically developed by a cross-functional team led by the category “owner” and refreshed on an annual or semiannual basis.
- ***Clear ownership and accountability for each category.*** Categories are typically managed by an accountable individual or team and are often aligned to the organization that is the natural owner. For example, a state office of information technology may “own” the end-user IT-services category. Category owners develop category strategies, provide guidance enterprise-wide, and help ensure the organization adheres to the guidance.

Processes

High-performing organizations most often invest heavily in ensuring processes are streamlined and standardized enterprise-wide, as appropriate. The following features are typical:

- ***Streamlined end-to-end processes from requirements definition through to contract close.*** High-performing organizations apply a full set of levers to make core procurement and acquisitions processes user friendly, fast, and compliant. End-to-end processes are typically designed using classic lean principles based on value-stream mapping and end-user experience. Some organizations have customized or tiered processes based on the procurement size, risk, and procuring entity.
- ***Rigorous contractor-performance-management processes.*** High-performing procurement organizations consider contractor performance management a deeply integrated part of their process. They have clear performance-management processes and provide appropriate training.
- ***Efficient and effective internal acquisition-review processes*** that help ensure acquisitions align with category strategies and meet organizational objectives. High-performing organizations often have one quick review process at the business unit (with lower thresholds) and one at the enterprise level, provide clear guidance as to what's required, and are timed to allow appropriate change of course.
- ***Regular process to assess the value and performance of major contracts*** to ensure they are optimized for speed, cost, quality, and compliance. High-performing organizations typically conduct cleansheet analyses based on real performance data and best practices, ahead of new acquisitions, when contracts come up for renewal, and periodically throughout the life of long-duration contracts.

People

High-performing procurement organizations are typically built upon a talented, motivated workforce with capabilities that are regularly refreshed and a culture that prioritizes citizen and government outcomes. Key elements include the following:

- ***Training and capability building for the core procurement workforce across all elements of the procurement value chain.*** Leading organizations provide training and development opportunities throughout a career; state functions often don't adopt these practices, but investing in training and professional development can help with overall performance and employee retention and motivation. The best results are obtained through experiential-based training. Typical training topics include acquisition-authority myth busting to ensure full use of existing authorities, category management to improve the strategies for procuring goods and services, cleansheeting, and value analysis to examine processes and eliminate costs.
- ***Accessible, timely training and support for those who work with the procurement workforce.*** The best organizations recognize that much of the end-to-end procurement process happens outside of the official procurement office. As such, some central procurement functions act as advisors to requirements owners, preventing them from reinventing the wheel, harmonizing standards, and allowing them to offer easy-to-access support. Examples include online repositories of best-practice contract documents, and centers of excellence to offer advice. They also use tracker mechanisms in processes to improve communication and transparency and shine a light on where slowdowns occur.
- ***An empowered culture.*** Top-performing organizations view procurement professionals as critical to every element of the organization's performance, treat them as important thought partners, and allow the procurement workforce opportunities to embed with nonprocurement

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offices. They build an appropriately risk-acceptant workforce that balances cost, speed, and quality with compliance.

Technology

Implementing a best-in-class procurement model often requires supporting IT systems. High-performing organizations typically derive their IT-system requirements from their target structure and processes, not vice versa. This type of best practice in the design of a procurement IT system most often includes the following:

- **Single procurement data source.** Top-performing organizations with a diverse spend portfolio maintain a single “source of truth” for procurement data, either through a single enterprise contract-management system (ideally) or a reporting process that feeds data from disparate systems into a central, frequently updated hub. The best systems have a simple user interface to enable frequent updating and validation of the enterprise-level spend view.
- **Data standards for procurement data.** In best-practice organizations, procurement information is supported by an infrastructure of common data and reporting standards—for example, product-service codes—that make it easy to match contracts to categories and perform comparative analyses.

Some private-sector procurement leaders are beginning to adopt practices in digitization and automation for contract writing, market research, and spend analytics to build upon their existing advantages in procurement excellence.

A phased path to transformation

So how do organizations undergo an integrated transformation and implement change in those key areas—customer segmentation and category grouping, spend transparency, structure, people, processes, and technology—without disrupting services? A phased path allows procurement functions to meet their potential without bringing the daily business of the function to a halt. Clearly delineating diagnostic, design, and deliver phases gives states the breathing room to be thoughtful and answer the right design questions before beginning execution; and executing in phases allows for ongoing refinement of the model as it is tested sequentially in different areas (see sidebar, “Meeting a procurement function’s potential”).

Many states recognize that modernizing the procurement function is an important step in better serving citizens and advancing the state’s strategic agenda, yet efforts to transform procurement often fall short or have fleeting impact. States have the potential to adopt appropriate procurement best

Meeting a procurement function’s potential

Example activities in a phased procurement transformation include the following:

Phase 1: Diagnose

- Affirm transformation objectives, establish priorities, and set scope for procurement transformation.
- Gather and review procurement data to establish a baseline picture of the state’s contract portfolio, customer base (internal and external), and organizational structure.
- Identify existing pain points and segments of existing operations where the state’s procurement posture is out of balance.
- Determine level of automation or advanced technology to integrate into the transformation effort.
- Prioritize contracts for value analysis (that is, cleansheeting) if being performed.

Phase 2: Design

- Perform detailed review of contracts and spend; develop a single view of enterprise spend.
- Establish initial category structure and prioritize category strategies for development.
- Redesign most critical procurement processes.
- Evaluate and potentially redesign alignment of procurement personnel

against customer segments or categories.

- Initiate workforce training and culture-shaping initiatives.
- Cleansheet a subset of priority contracts.
- Deliver and communicate one or two quick-win improvements in procurement operations.

Phase 3: Deliver and operate

- Refine category architecture based on real-world feedback.
- Develop category strategies.
- Finalize and implement new procurement data standards and reporting processes.
- Stand up any new procurement organizations or complete reorganizations.
- Transition to continuous training and ongoing process refinement.
- Continue cleansheeting activities at sustainable pace.
- Continue to communicate procurement wins to the workforce.

Several key activities can get a state off to a good start as they begin a procurement—or any other—transformation:

- **Engage your stakeholders.** A McKinsey survey on government transformations

found that engaging with stakeholders was a common feature in successful transformations. Not only do different stakeholders identify new areas of improvement and contribute to the change—but also their involvement helps convey the necessity and gravity of the transformation. When multiple parties are working toward a common goal, it is more likely to rise to the top of the priority list.

- **Prepare for the long haul.** Successful transformations often take one to three years to be fully implemented. Communicating timelines early and managing expectations is critical to maintain support.
- **Identify and execute quick wins.** Showing measurable successes in the first six months of execution is critical to maintaining support for broader efforts, especially given the lengthy time frame needed for the transformation. Highlighting these quick wins can help keep the momentum going after the initial excitement. Quick cost savings can also be used to self fund the broader effort.
- **Build capabilities.** The procurement function assesses its workforce capabilities, promotes ongoing learning and training, and continually adds skills and capabilities to modernize and more quickly adapt to changing needs.

practices from leading federal and private-sector organizations that approach transformation as a large-scale, multiphase undertaking that spans people, processes, and tools. States that avail

themselves of such a comprehensive approach will be poised to reach the procurement office's full potential through savings, budget reallocation, workforce productivity, and transparency.

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