

Measurably better

Assessing the performance of procurement is much more complex than adding up savings - it must gauge current work and provide a basis for future improvement. Sir Andrew Likierman explains how:

Procurement has fought hard for its contribution to be recognised. More heads of purchasing are reporting to the board, but technology, cost pressures and organisational change continue to threaten full recognition. So the function needs a robust method of measuring its performance to show how it adds value as a strategic resource and provide powerful ammunition in the competition for scarce resources. Lack of good measures leaves it vulnerable and in the dark.

Where do you start?

When asked for performance measures, the first instinct may be to reach for a traditional savings figure. But this is a trap. The problems of using such measures are well established - not just the focus on a narrow aspect of procurement but the unstated trade-offs with quality, inventory levels and long-term supplier relationships. There are then issues with the credibility of any comparisons - the most important evaluating what might have been spent if purchasing had not intervened.

The next stage might be to try a range of measures. These could cover cost - including overall cost for the function, cost of the function as a percentage of turnover, or cost of raising an order. There could be competence measures, such as number of staff with professional qualifications or time spent training. There might be process measures such as transactions per person, value of purchases per member of the function, accuracy, proportion of time spent with suppliers, percentage of e-procurement, or the proportion of spend under the function.

But beware, all these are vulnerable to attack. Cost and competence measures are about inputs, not performance. It may be wise to spend more money, not less. And competencies need to be turned into superior performance, not treated as a measure of success in their own right. Process measures are of

interest to the procurement function in looking at progress over time and against its plan. But they are not about performance either and leave further questions about trade-offs between quality, cost and time.

Measures related to results clearly carry a great deal more weight. The question is: what are results? We can try intermediate measures, such as relationships with suppliers, numbers of suppliers or inventory levels, or final results, such as added value or customer satisfaction.

Some of the above are difficult to link explicitly to what procurement alone has done - inventory levels, for example, will be affected by other departments. Some involve complex trade-offs - the numbers of suppliers is neither good nor bad in its own right, what matters are the compromises with cost, flexibility and so on.

And how do we get an independent assessment of whether relationships with suppliers are so close that the organisation is losing out or so distant that a long-term relationship is jeopardised? Some are difficult to measure. It's all very well to chant the mantra of the need to add value, but how would we know? As with the cost of purchases, the comparison is with what might have been, not with budget or what it cost last year.

Customer satisfaction measurement is equally complicated. Unless they have recently worked elsewhere, most "customers" will not have enough information to make judgments about purchasing quality. They also usually lack experience about even basic elements of procurement, such as cost-quality trade-offs, opportunity costs and risks. Only when a new chief procurement officer arrives do they realise that the old system was not nearly good enough.

Lastly, because responsibility for many parts of the work is shared, it is often difficult to ascribe success or failure directly to procurement. As with other functions, this measurement

problem becomes worse the deeper the function is embedded into line management.

Time to give up? No. Procurement needs not only to tell others how it is doing, but must make sure it has the basis for further improvement. There are four ways to use performance measures to provide solid evidence for both.

These suggestions are designed to test existing practice. They are not an answer, regardless of circumstances, as there are many variations between functions. The coverage is also private sector, though there may be aspects relevant to the public sector.

Link work to what people want

First, the performance of the function must be clearly connected to the organisation's objectives and constraints, and to the expectations of senior management. This connection needs to be reviewed each year at budget time, when expectations are formed.

One example is an agreement with the marketing and finance departments about delivery of target costing and pricing as part of the overall commercial strategy. Another is understanding the impact of an aggressive focus on price alone on operations and quality. A third is a timely change of emphasis in the trade-off between price and security of supply to reflect a commercial strategy change.

Procurement can contribute to overall objectives by helping other functions. This means thinking of the organisation, not just the function - a change in purchasing patterns may, for instance, help to simplify operations or cut ownership costs.

Because managers will not have had wide enough experience, procurement may have to advise on what is possible. Owing to purchasers' more informed expectations, this probably means help on target-setting, if necessary through

formal service-level agreements.

Targets must also take account of agreed risk levels. If service functions are criticised more when things go wrong than praised when they go right, they understandably become risk averse. But avoiding all risk - say on quality or delivery - could be costly. Senior management must help by clarifying risk tolerance.

Sophisticated measures

A second approach is to improve the sophistication of the measures and how they are used. This should start by getting away from cost and process and putting the focus on outcomes, which signals that performance is about delivery. The message should be reinforced by setting targets at levels defined by the organisation's objectives and customers, not procurement. For example, a reduction in the number of suppliers should be part of a plan and with a clear understanding of the implications for end-users and finance, not a goal in its own right.

Greater sophistication could also mean differentiating between types of purchase - say, commodity versus critical replacement - in the measures chosen. It will certainly mean basing measures firmly on reality. So in measuring the proportion of purchasing covered by the function, it's important to identify "independent" purchasing (for example, flights or IT equipment) even though the rules say this isn't supposed to happen.

A procurement scorecard may be worth considering under the more sophisticated label. At best, it provides a way of gathering measures into a coherent framework and the raw material for performance assessment. But there is a risk of being overwhelmed by numbers. So the scorecard should be unbalanced in giving proper weight to the objectives of the organisation and any overall organisational scorecard.

However the measures are organised, it's important to use relevant comparisons wherever possible. These are crucial not only to improving the way things are done but to provide ideas for better measures as part of a constant search for best practice. They will also give insights into ways of working that could give you a competitive edge. The ideal is obviously to compare functions that are as similar as possible.

So where do you start? In very large organisations with decentralised procurement functions, it should be through intra-firm comparisons. For smaller organisations, it could be with other procurement functions, perhaps through a benchmarking scheme set up within the industry. These comparisons will almost certainly be more useful when they break the function down into activities. These may include response times for queries and take-up of the latest techniques, rather than procurement expenditure as a percentage of turnover for the firm as a whole.

You should use non-procurement people, wherever possible, for evaluation. These could include someone from another function, such as HR; someone from another organisation (I'll appraise yours if you appraise mine); auditors or an outside consultant. Each has advantages and disadvantages in terms of knowledge, independence and cost, but their most important asset is their fresh view.

Lastly, what about using relevant parts of other service functions in your own organisation as models and discussing performance with finance or marketing? The right point of comparison will again be individual activities, such as response to queries with IT, or quantifying benefits with research and development.

Better feedback

A third step is to improve the quality of feedback to and from procurement. Getting proper feedback on customer

perceptions and educating them about the role of procurement is important.

Questionnaires need to be constructed with great care. The internet has convinced many managers that everyone is a procurement expert, so: Are you satisfied with the service offered by procurement? (Answers: very, a little, no) is just not good enough if the recipients have no real way to gauge what good procurement could do.

Questions need to be framed in such a way that good service is defined, but without leading the answer. They should cover process: How prompt was the response to your calls or e-mails? And outcome: Did the service fully meet your requirements?

But questionnaires alone are not enough or may not even be appropriate. Face-to-face feedback on the basis of indicative questions sent out beforehand, probably when the organisation is setting budgets, could get a better feel for what people really think. These discussions are also a good time to check whether what procurement thinks is important corresponds to what the customers think (for example, trading off quality against on-time delivery), as well as to brief customers on how to use procurement better and to try out new ideas.

Another way to improve feedback is for the head of purchasing to use the annual appraisal cycle to report on progress against objectives and provide a fuller explanation of events. This is the chance to discuss the impact of changes to requirements during the year and give sufficient weight to quality and service.

Lastly, there's the question of how much purchasing knows about the wider organisation. If nobody in procurement has experience of working in other functions, understanding is less likely to be profound. If so, it is worth thinking about secondments to improve the ability of purchasing to get the most out of feedback.

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Recognise limits

Lastly, recognise the limitations of measures and, where possible, mitigate them. All of us are aware of the destructive power of poor performance measures or of good measures badly applied. A number of measurement problems have technical solutions. But many do not. So it is crucial to make a clear distinction between what can be improved and when limitations will persist, no matter how hard we try to get rid of them.

The most obvious example is the comparison with what might have happened if procurement had not intervened. Those who get regular demands from finance to justify themselves need to ensure that their savings claims are not open to challenge. They need to give the full picture of the implications for risk factors such as security of supply and quality. They also need to take every opportunity to educate senior management of the full range of benefits that go beyond a notional cost calculation. None of this will make the problem go away, but it can be mitigated.

When faced with aggressive questioning from finance, resist the temptation to over claim: unsubstantiated claims will harm your credibility. Improved inventory levels and better quality may or may not be due to purchasing. So a clear commentary to accompany the figures is essential, especially for those elements that are difficult to measure.

The obvious example is contribution to the objectives of the organisation. Even if a clear line of sight can be established between the organisation's objectives and procurement's contribution, words are necessary to supplement figures and explain why the measure is useful. Commentary is also essential for benchmarks such as savings from spot buying or the quality of long-term supplier relationships, where you should set out the difficulties of measurement, as well as the trade-offs.

Cost and process are important to procurement in improving efficiency and will be part of the budgeting process. But they are of limited general interest and should be used sparingly outside the function.

The incentive of applying these suggestions for improvement is that the function and the organisation as a whole will benefit from a better appreciation of what it can do.

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