

Lecture 6:

Approaches to sourcing of supplies



Lecture content

- What is sourcing
- Surveying the market
- Supplier appraisal
- Inviting quotations and tenders
- Assessing quotations and tenders
- The use of e-sourcing technologies
- Measuring supplier performance



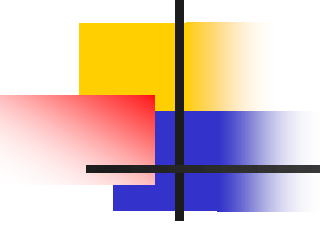
Definition

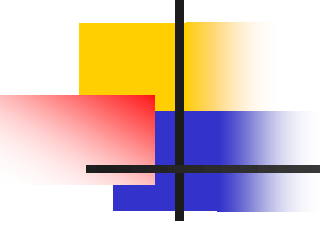
- The **sourcing** process includes every activity that revolves around identifying and assessing potential suppliers as well as selecting and engaging with an appropriate supplier who offers the best value
- It involves identifying sources, evaluating the sources and making selection




Sources of Information on Potential Suppliers

- A number of sources of information may be consulted to identify and research potentially suitable suppliers
- The buyer's own database of existing and past suppliers
- The marketing communications of potential suppliers: advertising, direct mail, brochures and catalogues, visits from sales representatives, websites and so on.

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- 3. Internet search for websites including business directories and listings, searchable databases designed to promote exports and specialist procurement resources.
 - 4. Online market exchanges, auction sites and supplier/buyer forums, which may also allow the posting of requests for quotation and other exchanges.

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- Trade fairs, exhibitions and conferences, which may provide opportunities for visitors to view competing products and prototypes, meet supplier representatives.
 - Organisations promoting trade such as trade associations, embassies, chambers of commerce,
 - Export associations and so on – and their websites



Information About Existing Suppliers	Sources of Information
Contact details (including details of account managers, where relevant)	Trade registers and directories, trade and industry exhibitions and conferences
Product and services offered	Supplier literature, websites, corporate reports and accounts
Standard or negotiated terms and conditions of trade, including prices, rates or fees where known	Supplier sales and customer service staff
Approved or preferred status of supplier	Feedback from own staff, vendor managers etc.
Average value and frequency of spend with each existing supplier (used to identify key accounts)	Contract and transaction files and records



Special capabilities (e.g. late customization capability, EDI) suggesting supplier selection when special needs arise	Reported financial and operational results (e.g. cost reductions, new product development, lead times)
Results of supplier appraisals, audits and ratings	Supplier appraisal, audit and rating reports
Vendor performance history: quality, lead times, delivery, compliance, disputes	Testimonials or reports from other customers (e.g. by request or business networking)
Current systems, framework agreements and call-off contracts in place	Electronic performance monitoring (e.g. goods inwards tracking)



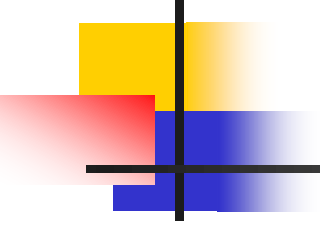
Supplier evaluation

- Supplier evaluation is a continual process within purchasing departments and part of the pre-qualification step within purchasing.
- It includes appraisals of various aspects of the supplier's capacity such as financials, quality assurance, organisational structure and processes and performance
- Evaluation can take the form of a questionnaire, an interview, or site visit.
- In some situations, pre-qualification is undertaken as part of the evaluation process



Supplier evaluation

- **Why Pre-qualify Suppliers?**
- The purpose of supplier appraisal, evaluation or pre-qualification is to ensure that a potential supplier will be able to perform any contract or tender that is awarded, to the required standard.
- This avoids the risk of later problems in the tender or negotiation process.

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- The buyer does not want the wasted cost, time, effort and embarrassment of awarding a contract (on the basis of lower price) to a tenderer who subsequently turns out to lack capacity or technical capability to handle the work,
 - In addition, having a list of pre-qualified suppliers reduces the investigations needed for individual tenders and purchases: the buyer already knows that any supplier on the approved list has been assessed as capable of fulfilling requirements.



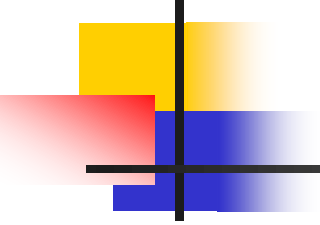
Models for Supplier Appraisal

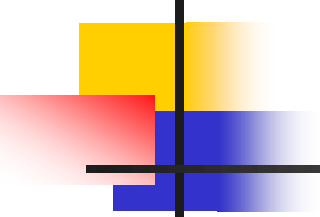
- A helpful checklist of areas for supplier evaluation is suggested by Ray Carter's 10Cs of supplier evaluation.
- **Competency** of all staff all of the supplier: this includes managers, sales staff, technical and production staff etc.
- **Capacity** of supplier: must have sufficient, flexible production capacity; must have sufficient financial capability to respond to needs, and to market and supply fluctuations

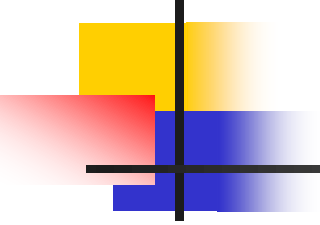


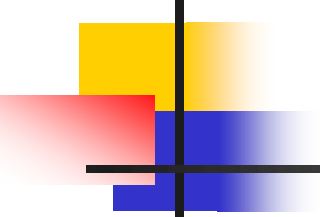
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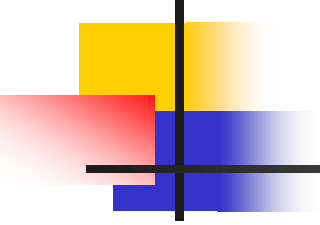
- **Commitment** to quality, evidence of commitment to quality systems and perhaps by external accreditation such as ISO 9000
- The supplier must also show they will be committed to you, as a customer, throughout the time that you expect to work together.
- This is particularly important if the procuring entity is planning a long-term relationship with the potential supplier.

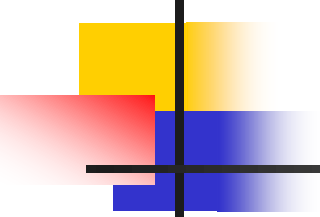
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- **Control of process:** again ISO 9000 may be relevant).
 - Ask how much control this supplier has over their policies, processes, procedures, and supply chain.
 - How will they ensure that they deliver consistently and reliably, especially if they rely on scarce resources, and if these resources are controlled by another organization

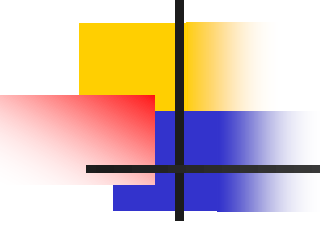
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- **Cash:** must be financially sound)
 - Your supplier should be in good financial health. Positive Cash flows firms are in a much better position to weather economic ups and downs.
 - **Cost:** total acquisition cost.
 - Look at the cost of the product or service that this supplier provides. How does it compare with the other options that you're considering?

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- Most people consider cost to be a key factor when choosing a supplier.
 - However, cost is in the middle of the 10 Cs list for a reason.
 - Other factors, such as a commitment to quality and financial health, can potentially affect your business much more than cost alone, particularly if you plan to rely on the supplier long-term

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- **Consistency** of output, delivery and service
 - How will this supplier ensure that they consistently provide high quality goods or services? Do they have a strong track record, or are they an industry newcomer with an innovative approach?
 - No one can be perfect all the time. However, the supplier should have processes or procedures in place to ensure consistency

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- **Culture** (must be compatible with buyer organization)
 - The best business relationships are based on closely matching *organisational culture* .
 - This is why looking at the supplier's business culture is important. For example, what if your organization's most important value is quality, and your main supplier cares more about meeting deadlines

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- **Clean** (i.e. environmentally sound)
 - This refers to the supplier's commitment to sustainability , and their adherence to environmental laws and best practices. What are they doing to reduce their environmental footprint
 - **Communication**
 - Find out how the supplier plans to keep in touch with you.

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- Will their proposed communication approaches align with your preferred methods? And who will be your contact at this firm?
 - It's also important to find out how the supplier will handle communications in the event of a crisis. How quickly will they notify you if there's a supply disruption

Another model, even easier to remember and popular with examiners, is the FACE 2 FACE checklist (originated by Dawn Dadds)



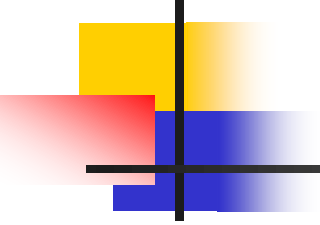
FACE2FACE Model

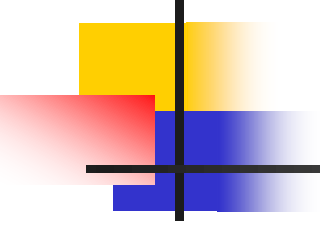
Fixed asset Physical resources to meet buyer needs	Financial stability For continuity of supply
Ability to deliver the goods Production capacity and reliability of deliver, quality and service	Ability to work with the buyer Compatibility to culture, contacts, willingness to cooperate
Cost Competitive total acquisition costs, willingness to negotiate terms	Commitment to quality Reliability to quality standards and systems, willingness to improve
Efficiency Use of resources, minimization of waste	Environmental /ethical factors Policies and practices on CSR

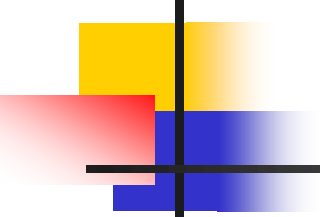


Criteria For Supplier Appraisal

- **Financial Status and Stability**
- This refers to the supplier's profitability, its cashflow position (whether it owes, how its costs are structured and allocated, and so its overall financial 'health').
- These factors will reflect on the ability of the supplier to fulfil its contract with the buyer.
- They may raise the risk of delivery or quality problems – and more drastic disruption to supply

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- **Capacity to Produce and Technical Capabilities**
 - This refers to factors in the supplier's operational capacity and facilities, such as the following:
 - 1. Whether it produces (or can produce) the kinds of items, or deliver the kinds of services, required.
 - 2. How much volume the supplier will be able to handle (its production capacity).
 - 3. What engineering, innovation and design capability it has (where relevant)

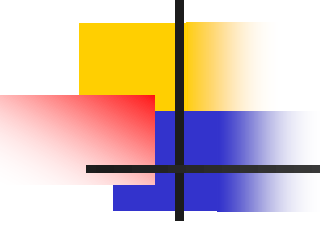
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- What type of plant and machinery it has, and whether it is capable of producing items within the tolerances set by the buyer's specification
 - The efficiency of factory layout and processes (which will impact on productivity and also cost).

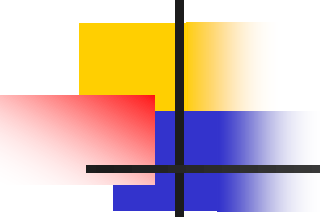
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- Capacity and capability may also be assessed with reference to:
 - The human resources of the supplying organization: A supplier appraisal may take into account the skills of the supplier's workforce; the ability and drive of its management; employee morale and motivation
 - Organisational structure: How clear is accountability for performance? Will the supplier be able to respond flexibly to the buyer's demands and changing circumstances



■ **Adherence to Systems and Procedures**

- This may embrace a number of criteria, including:
- Compatibility of the supplier's systems and procedures with those of the buyer (or its ability and willingness to adapt to the buyer's requirements)
- Willingness of the supplier to comply with any procedures, rules or systems required by the buyer.
- Quality management systems: the supplier's standards accreditation (if any); its quality management methods

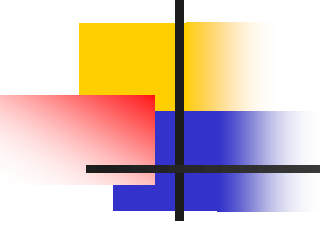
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- **Conformance to Legislation**
 - Conformance to legislation or compliance may be part of a wider assessment of environmental and ethical considerations: the supplier's compliance record (on workplace health and safety, product safety and labelling, environmental protection and so on), and its stated policies and values in these areas.

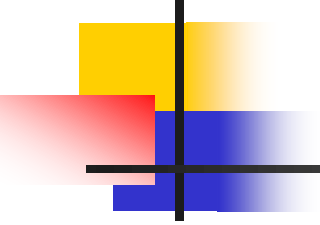
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- **The Supplier's Supply Chain**
 - Can the supplier dependably access the materials, services, expertise and extra capacity it may require to fulfil the contract, from its own suppliers?
 - A supporting factor in its legal, ethical and environmental compliance – and in the management of reputational risk to the buyer

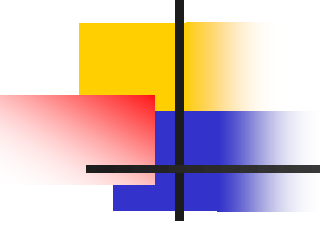


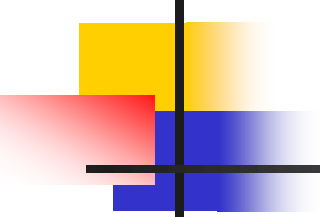
Sources of information for supplier appraisal

- **Supplier Questionnaires**
- Detailed questionnaires should be sent to the potential supplier for completion, posing a range of evaluation checklist across relevant areas.
- Many firms use multi-page checklists similar to vendor rating forms. The answers are analysed by the buyer, and scored according to a predetermined marking scheme

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- **Sites Visit and Capacity Survey**
 - Where a potential supplier is accessible, the buyer may use a supplier audit or site visit: a visit to the supplier's premises by a cross-functional appraisal team
 - A supplier visit can be used for the following purposes:
 - 1. To confirm information provided by the supplier on an appraisal questionnaire.

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- To observe and discuss, in greater detail, the supplier's premises, personnel, equipment, processes (particularly quality management) and outputs.
 - 3. To enable the buyer to make personal contact with supplier-side account managers and other individuals whose co-operation will be relied on if delivery or other problems occur

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- A capability survey, carried out as part of supplier audit, is designed to gather detailed information about the supplier's capabilities.
 - ***Technical or production capabilities:*** That is its operating capacity, R&D capability, quality management systems, equipment and maintenance, workforce training and productivity and so on.
 - ***Financial capabilities:*** Financial ratios indicating the company's efficiency, cashflow position, debt and profitability.

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- ***Commercial capabilities:*** Customer account management, order handling procedures and systems, e-business systems, distribution channels, lead times for delivery and so on.
 - ***Environmental capabilities:*** Environmental policy, accredited environmental management systems (ISO 14000),



■ **References**

- One source of information on suppliers is to ask the opinion of their current or previous customers. One approach to this is to ask potential suppliers for the contact details of selected customers ('references') and to contact those customers to ask about their experience with the supplier (taking up' the references).



■ **Financial Appraisal**

- Financial information about suppliers can be obtained from various sources, including:
- Their published financial statements and accounts: balance sheet, profit and loss account and cashflow statements.
- Analysis of financial statements and results in the business or trade press.
- Credit rating companies (such as Dun & Bradstreet).




■ **Work Sampling**

- One key way to appraise supplier quality, and/or to verify quality claims, is to evaluate the products or services themselves. This may be done by:
- Requesting samples of the supplier's products, for evaluation
- Randomly sampling the outputs of the supplier's production process, as part of a site visit:



Measuring Supplier Performance

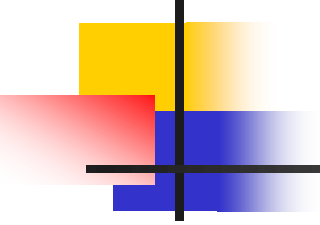
- There are various good reasons to put effort into evaluating supplier's performance. Supplier performance measurement can:
- Help identify the highest-quality and best-performing suppliers: assisting decision-making regarding: (a) which suppliers should get specific orders (or be invited to tender for a contract); (b) when a supplier should be retained or removed from a preferred or approved list; and (c) which suppliers show potential for closer partnership relationships.

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- 2. To evaluate the effectiveness of procurement's supplier selection and contract management processes).
 - 3. Help ensure that suppliers live up to what was promised in their contracts
 - 4. Provide suppliers with an incentive to maintain and/or continuously improve performance levels
 - 5. Significantly improve supplier performance, by identifying problems which can be tracked and fixed, or areas in which support and development is needed.



Vendor Rating

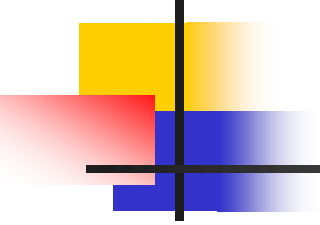
- Vendor rating is the measurement of supplier performance using agreed criteria, usually including:
- **Price:** e.g. measured by value for money, market price or under, lowest or competitive pricing, good cost management and reasonable profit margin.
- **Quality:** e.g. measured by key performance indicators (KPIs) such as the number or proportion of defects, quality assurance procedures.

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- Delivery: e.g. measured by KPIs such as the proportion of on-time in-full (OTIF) deliveries, or increases or decreases in lead times for delivery.
 - Other measurable factors might include: after sales service, efficiency and accuracy of contract management and administration, willingness to commit to continuous improvement, and so on.



Approaches to Vendor Rating

- **There are two basis approaches to vendor rating. They are:**
- 1. The use of supplier performance evaluation form: a checklist of key performance factors, against which purchasers assess the supplier's performance as good, satisfactory or unsatisfactory.
- A weighting is applied to each factor, so that the supplier's performance in key performance areas, and overall, can be summarized as good, satisfactory or unsatisfactory.

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- 2. The use of factor rating method: The idea is to pick out key factors such as price, quality and delivery, and to determine a numerical method of measurement for each. (For example, the measure of quality performance might be '100% minus percentage of rejects in total deliveries'. A supplier whose deliveries contained 3% rejects would score 97% or 0.97 on this measure).