Strategic Sourcing and Category Lifecycle Management

Summary

The processes performed by strategic sourcing professionals have evolved beyond sourcing initiatives to include supplier relationship management and continuous category-based opportunity assessment. This comprehensive set of processes is best described as "Category Lifecycle Management" or CLM. Enterprises that understand and leverage CLM in its broadest sense will gain a strategic edge over those that miss the opportunity or are late to adopt CLM. The five value-adding principles of CLM can be remembered as: Discipline, Visibility, Learning, Knowledge Retention, and Process Efficiency.
Introduction

Strategic sourcing processes—and the tools that support and enable them—are rapidly evolving. Organizations that perform strategic sourcing are adapting and maturing as well. Together, these evolutions are driving the best strategic sourcing organizations to a new level of interconnectivity, performance, and value delivery. Intensely focused on delivering best overall cost and value to their companies, these top performers use cross-functional teams and intra-supply chain collaboration to achieve their goals. Their sourcing professionals work closely with all parts of the enterprise—business unit leaders, design teams, engineering, manufacturing, quality, operations, customer service, and research and development (R&D). They also serve as experts on the markets and suppliers of the categories of goods and services their organization procures or buys—categories that are critical to each business unit and to the company overall.

Strategic sourcing, provides procurement departments with a strong, category-based focus on the spending of the highest impact enterprise. The evolving sourcing roles and enabling technologies are allowing enterprises to extend their strategic management to include all of their categories of spend throughout the entire lifecycle of each category—a framework that can best be called Category Lifecycle Management (CLM).1

**CLM is a set of business processes for continually managing classes of purchases to optimize total cost of ownership.**

The CLM term provides a comprehensive framework through which leading-edge strategic sourcing can be defined. It carries with it a holistic and continuous view of the main processes of strategic category and supplier management: continuous category-level opportunity assessment, strategy formulation, strategy execution, and supplier relationship management. Just as brand managers manage the strategic market lifecycle for a particular product or offering, sourcing managers manage the category lifecycle for particular goods or services. The fundamentals of CLM are rapidly gaining ground. In fact, some sourcing or procurement organizations have already adopted the title of Category Manager or Commodity Team Leader for their sourcing professionals to better represent their heightened focus and accountability.

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1 For further discussion of the choice of the term *Category Lifecycle Management (CLM)*, see the appendix to this paper. Additional papers on CLM and related topics for strategic sourcing are scheduled for publication by B2eMarkets.
The purpose of this paper is to explain the CLM framework and how world-class companies are applying it to deliver the greatest value to their enterprises. Enterprises that understand and leverage CLM in its broadest sense for all categories of their purchases will gain a strategic edge over those who miss the opportunity. The early leaders will be motivated by the high return on investment (ROI) from lower total costs, while those that follow will be forced to adapt to avoid losing position and profit to their more efficient competitors, customers, and suppliers.

**Evolution: From Buying to Category Lifecycle Management**

**History**

Throughout the evolution of the market, some companies have proven themselves leaders and others, followers.

The timeline below illustrates the changing focus of the leading procurement and purchasing organizations over the past three decades:

- **1970s**: Companies bought things and issued orders through requisitioners and expediters.

- **Early 1980s**: Companies still bought things, but through a purchasing department. The department used a standard process we might lightheartedly label, “Three Bids and a Cloud of Dust.”

- **Mid-1980s to early-1990s**: Supply management was developed to focus on such issues as supply continuity and supplier metrics.

- **Early-1990s to late 1990s**: Strategic sourcing arrived, using waves of initiatives to improve the supply base and focus on such key needs as continuous improvement, six sigma, long-term partnerships, and global capabilities. Reverse auctions emerged in the late 1990s as a highly visible negotiation tool, highlighting just one potential value of the Internet for sourcing professionals.

- **2000 and beyond**: CLM becomes possible as technology extends and improves the strategic sourcing processes to cover the entire lifecycle for the categories being sourced and enables the sourcing organizations to manage across the entire spend of the enterprise.
Evolving Roles

As the market evolves, so does the role of sourcing professionals. For the supply base, they offer knowledge of the enterprise, the specifications and total requirements for their particular categories, and the organization’s issues and alternatives for their categories. For the enterprise, they provide knowledge of the market, suppliers and their performance, alternative suppliers, and procurement best practices.

In many enterprises, sourcing professionals are accountable for Supplier Relationship Management (SRM), a term that has emerged to define key supplier management and development processes. Although SRM is not yet globally defined, it includes most or all of the following activities:

- Contract Management—Ensuring performance of all parties to the requirements of procurement contracts
- Supplier Management—Managing supplier relationships through such tools as supplier metrics, scorecards, and performance awards
- Supplier Improvement or Development—Improving performance and reducing the cost of poor quality (COPQ) in supplier processes
- Supplier Feedback—Requesting and managing opportunities to improve the enterprise with collaborative feedback from suppliers
- Organizational Feedback—Requesting and managing feedback from staff throughout the enterprise on their experience with suppliers, goods, and services
- Supply Chain Communication and Collaboration—Sharing critical information among the various functions of the enterprise and across multiple tiers or levels of suppliers

Sourcing professionals are also key members of teams working on continuous processes such as Product Lifecycle Management (PLM) and Component Supplier Management (CSM). PLM represents the processes of the cross-enterprise and intra-supply chain teams in managing the full product lifecycle. This function is particularly important in the manufacturing sectors, where high production volumes and high setup costs require strong collaboration and planning for efficient operations. Sourcing professionals or category experts are almost always members of these teams to support speed-to-market initiatives.
CSM manages bill-of-material (BOM) and part-level detail for assembly or manufacturing-intensive companies. Sourcing of BOM or item-level parts requires substantial knowledge of specifications and the supplier industry, capacities, capabilities, and performance, an integral component of the sourcing professionals’ role. Sourcing expertise, then, is tightly integrated into product design, manufacturing, engineering, and the entire product lifecycle.

Through these integrated processes, sourcing professionals in high-performing companies are connected tightly and continuously to their teams, suppliers, and markets. They have progressed to leadership and team roles in supporting product design, manufacturing, operations—essentially, every organization critical to the company. This is a much more complex role than that of the early days of strategic sourcing.

Once-Through Becomes a Lifecycle
As shown below, the original or classic application of strategic sourcing was that of a once-through process, from opportunity assessment through selection and contract implementation.

The number and names of the process steps tend to differ from company to company but the high-level view of the process is almost always similar in most organizations. Driven by improvement and cost reduction initiatives, the process is originally introduced to the enterprise through either internal reengineering and/or external consulting organizations.

Once the strategic sourcing process is defined and has proven to be successful in an organization, it is then repeated for each new category of good or service being sourced. Companies focus their resources on the categories of purchases with the highest strategic importance and/or those on which the most dollars were spent.

The process of handling these categories does not end at the start of the new agreements. Implementation of new or improved agreements requires the beginning of the processes included in SRM, including performance and collaboration.
In addition to SRM, sourcing professionals lead other continuous processes best described as category-level opportunity assessment.

These high value-adding processes include:

- Monitoring markets for changes, trends, and opportunities
- Monitoring for demand, utilization, and forecasts
- Assessing design or technology changes and forecasts
- Monitoring spend and financial impact
- Identifying value improvement and value engineering opportunities throughout the supply/value chain
- Identifying opportunities for cost of quality improvements
- Tracking business, product, and technical forecasts that effect future goods, services, and suppliers

The SRM and continuous category-level opportunity assessment processes are where most sourcing professionals in high-performing strategic groups spend most of their time and energy. When enterprises first implement strategic sourcing, they are focused on a series of quick-hitting initiatives. As they evolve and mature, they become focused on forecasting needs, improving performance, and integrating critical suppliers into their businesses. When such triggers as business and market conditions, supplier performance, or contract expirations bring the need for new supplier relationships or adjustments to current contracts, new initiatives and negotiations are launched.

Transactional procurement, where simple automation and machine efficiency are the top drivers, CLM requires top-performing, knowledgeable people. High value is placed on organizational design, learning, development, and collaboration across the enterprise and supply chain to educate and energize these teams to support corporate initiatives and drive performance, efficiencies, and, ultimately, bottom-line savings.
This high-level view of the category lifecycle evolves as shown in the illustration below. It depicts the cycle’s processes, with people and organizational issues at the center.

This is Category Lifecycle Management (CLM)

Since the processes in each lifecycle step are not discreet, but continuous, the steps in CLM can be better represented as stages of a repeating lifecycle:

The key issue is not the exact number of stages or even the wording of each stage. What is most important is that CLM activities follow a continuous lifecycle of best practices—practices that the enterprise should define or configure for its own performance. The stages repeat whenever the enterprise, the supplier(s), the market, or the members of the extended supply chain drive the need for change.
chain trigger the requirement for new strategies or new or improved supplier relationship(s). In general, most enterprises that have adopted elements of category lifecycle processes have strong similarities when examined at the highest level. They can be well represented in the four-stage lifecycle shown previously.

The Four Stages of CLM
To show the continuity of CLM, a brief description of a four-stage lifecycle follows.

Stage 1. Assess Business Needs, Markets, and Opportunities. This stage includes gathering, consolidating, and interpreting the key factors relevant to the category of purchases. It covers such steps as assessing stakeholders and their requirements; assessing current suppliers and their performance and capabilities; understanding supply, demand, and utilization issues; considering alternatives to current goods or services; assessing the market, industry, and technology trends; and evaluating alternative suppliers.

Stage 2. Develop and Refine Strategy. Building on the findings of the previous stage, Stage 2 proceeds to developing a strategy with cross-functional support; gaining agreement on key success factors and targets; and developing the overall category strategy and negotiation strategy.

Stage 3. Identify, Negotiate, and Award. Stage 3 includes performing all activities in the strategy up to and including contract award: setting final specification and critical performance factors; identifying and assessing alternative suppliers by executing all supplier requests for information, proposals, and quotes; confirming market knowledge; and conducting final negotiations and contract negotiations ending with award(s).

Stage 4. Manage Contract and Supplier Performance. This last stage includes the major elements of supplier relationship management and supplier development. It begins with implementing the new or refined contract and includes contract management; supplier management; supplier improvement or development; supplier feedback; organizational feedback; and supply chain communication and collaboration.

After a given category is taken through the entire process, the steps become continuous and recurring. This recurring lifecycle approach is a key difference between traditional strategic sourcing and CLM. In the CLM process, an evergreen strategy—a strategy that is always kept current—is checked against the needs and performance of the organization and its suppliers. Sourcing professionals will monitor trends and changes in organi-
zation, demand, technology, markets, and spending, constantly considering cost reduction, or other quality improvement and value-adding opportunities, and staying current with relevant and emerging processes and technologies. The knowledge, findings, and performance measures from their work can trigger the launch of new sourcing activities to refine existing relationships or create new ones.

A major challenge for most sourcing organizations is providing structured knowledge retention, sharing, and visibility throughout and across each of the four stages of CLM. It is those organizations with well-structured processes and enabling tools that will excel. They will be able to create far more value than those that are less enabled, even if they are performing the same processes.

Five Principles for Delivering Value From CLM

Organizations that can consistently and effectively perform the CLM processes will yield high value for their business units. As is true for most new and critical capabilities in the supply chain, those who are first to succeed will have the most to gain by driving costs out of their own supply chain while holding prices as best they can. This enables the leaders to enjoy a period of either premium profits, or lower selling prices to capture market share, until competitors follow suit and implement similar processes. After that, market forces, such as competitors who can replicate the low-cost structures, will likely reduce the pricing and evaporate the profit premium. For those organizations not yet employing all of the power of CLM, it then becomes a game of “adopt or lose even more ground to the competition.”

Five key principles drive the value creation and return on investment (ROI) gained in successfully implementing CLM. The most successful sourcing organizations have leaders—such as Chief Procurement Officers (CPOs) or VPs of Sourcing or Procurement—who understand and endorse all five principles and focus on continuous improvement in each:

• Provide discipline through a structured process

Organizations need good processes, and they need to practice them continuously. To be truly effective, they must perform these processes enterprise-wide and with constancy and rigor. Leading CPOs institutionalize best practices, providing structure, crafting leading-edge category strategies, and following critical processes for creating maximum value.

• Establish visibility to ensure measurable ROI

Processes that are not measured cannot be controlled. To be effective, the strategic sourcing organization must have access
to critical information, and also provide clear and visible results from its efforts. Spending data and knowledge are key to understanding the enterprise’s performance. Showing total spending reduction in a category or reduced spending with non-preferred suppliers is one clear demonstration of good sourcing performance and value delivered to the bottom line. Critical measures are defined and monitored within the sourcing organization to manage not only performance of the sourcing function, but also that of cross-functional teams and suppliers. Leading CPOs are personally accountable for clear measures, financial targets, and forecasts that are linked to business unit performance. The CPO’s measures and accountabilities are cascaded throughout the sourcing organization to the appropriate category managers and directors.

• **Foster continuous learning for a high-performance organization**

Learning is a never-ending process—especially in today’s world of rapid change in markets, technologies, and industry structure. CPOs of leading sourcing organizations provide and encourage individual development and learning and reward high performance. Learning is accomplished through coursework and practice. It can be built directly into the organization’s process-enabling tools. Excellent learning also occurs when sourcing organizations take good metrics from principle 2 and develop forecasts and hypotheses for continuous improvement in the supply base.

• **Create a repository for knowledge retention**

Knowledge is stored in an organization’s people, processes, and tools. Organizations that do not have structured processes and systems for capturing their knowledge are at a significant disadvantage to their suppliers and competitors who do. CPOs of high-performing sourcing organizations place high value on capturing and sharing critical knowledge across their enterprise. These practices increase performance, reduce startup costs for new or transferred employees, and form the foundation for collaborating within and across the enterprise and with supply chain partners. Knowledge capture and retention are extremely difficult to accomplish without world-class tools specifically designed to reinforce the processes of CLM.

• **Implement tools for process efficiency**

Good people and good processes are key to high performance—but cannot alone guarantee success in today’s market. The best organizations are using world-class tools and technology that promise a rapid ROI. Strategic sourcing technol-
ogy that empowers sourcing professionals and enables efficient and effective CLM processes is now a valued option for leading-edge CPOs.

These five key principles serve as beacons for leading CPOs as they take action to improve processes and select enabling tools and service providers to support the next level of improvements for their organizations. All five are imperative and when accomplished simultaneously, ensure the strategic sourcing organization creates maximum value.

As CPOs help navigate their organizations to new levels of performance, these five key principles can lead to cost reduction and quality improvement throughout the enterprise.

**Leading companies are already using the CLM principles to gain a strategic advantage**

Today, strategic sourcing is fast becoming the tool of choice for top-performing global organizations to gain sustainable cost savings and performance improvements. Consider these examples:

- In a recent call with industry analysts, 3M’s chairman and chief executive officer James McNerney said that sourcing and procurement initiatives were among his top five priorities for delivering even greater returns to shareholders. Like many other leading CEOs, McNerney understands that each dollar that is reduced in total cost of goods goes directly to enhancing the company’s bottom line.

- One company with over 100 procurement professionals worldwide has a primary goal for its sourcing organization to achieve a sustainable 10 percent reduction in total cost and consolidate its supplier base. This company started with a consulting engagement to reengineer the sourcing processes and then internally drove the global development and deployment of other CLM processes and tools. Now it is adopting Internet-based tools to shorten negotiation cycles, further globalize sourcing best practices, create a competitive advantage, provide high visibility to critical measures, and capture and share critical knowledge among teammates. With its continuous CLM approach, the company is already averaging 25 percent cost reductions and slashing sourcing cycles from two months to two weeks.

- A global manufacturer of consumer packaged goods sought to improve the sourcing processes and costs of its materials procurement. It determined that a balanced approach between both public and private online marketplaces would deliver sustainable savings and process improvements. This longer-term
approach has slashed up to four weeks from the company’s traditional sourcing process and produced savings as high as 12 percent—a process it is now applying to other spend categories.

• One market leader spends more than $7 billion each year to acquire direct and indirect materials. Rather than driving this initiative out of the chief procurement officer’s organization, this company’s strategic sourcing efforts are being driven from the top down. The CEO has added great weight to adopting strategic sourcing as a key initiative—increasing the imperative that sourcing performance be sustainable and repeatable. The company has placed a high priority on global process standardization, knowledge retention, and measurements, and early results are highly favorable: more than 12 percent cost savings, up to 30 percent productivity savings, and cycle time reductions from up to four months to six weeks.

• With the rapid evolution of strategic sourcing, leading corporations will continue to embrace the concept of CLM. Fueled by knowledgeable people, well-structured processes, world-class enabling tools, and a continuous lifecycle of best practices, CLM is a vessel for creating value and a vigorous competitive advantage. Those who seize today’s opportunities to understand the continuous and holistic nature of CLM, and enable their organizations around its critical processes and measures, can achieve a high return on investment from lower total costs well ahead of their competitors and a distinct strategic edge in the rapidly changing currents of today’s marketplace.
Appendix

Why CLM?

CLM may be a new term, but it is not a new concept. Leading-edge strategic sourcing organizations are already performing, or expecting to perform, all of the processes that CLM includes. So why not just expand the definition of strategic sourcing to include all of the processes in this definition of CLM? The reason is that new concepts must stand up when examined from different perspectives. The following discussion offers a few explanations for why CLM is the most reasonable designation for this space.

Strategic sourcing is classically defined as an initiative-based process

Even though strategic sourcing organizations are evolving to perform all of the processes of CLM, the term strategic sourcing was coined to describe a once-through process, or an initiative that can be repeated across multiple categories. In almost all of the literature, strategic sourcing is described as a linear process and almost always ending at or after contract implementation.

Many enterprises adopted strategic sourcing after a consulting engagement indicated its potential for yielding high value. The repeatable initiative process was an easy way for consulting firms to achieve rapid ROI across many categories for their client in a limited engagement. The consultants would leave after performing several initiatives and often, after teaching the once-through process to the new sourcing organization. After the engagements, the newly formed strategic sourcing organizations were left to develop and manage continuous processes around suppliers and category management.

Because the processes that result from CLM are clearly a set of continuous processes, or a lifecycle, the term for this space must include the word lifecycle.

Individual supplier lifecycles are subordinate to the category lifecycle

Many thought leaders consider the three non-financial and truly strategic assets of a firm to be its employees, customers, and suppliers. For more complex enterprises, one can add partners and channels to the mix. One leading professor of marketing views the relationships with these strategic assets as the relationship equity of the firm. So one question might be, “Why not call the space Supplier Lifecycle Management?”
Although suppliers do indeed have their own lifecycle from the beginning of the supply relationship throughout its entire life, it is the lifecycle of what is being purchased that drives supplier deliverables and performance issues. The category lifecycle is therefore at a higher strategic level than the supplier(s)' lifecycles.

A parallel relationship can be found on the sell-side of the business with customers and markets. It is the market lifecycle that drives the deliverables and performance issues for the business to its customers. Customer relationship management is all within the context of the strategic markets in which the business decides to enter or operate.

The other parallel is the concept of employees as part of the organization lifecycle. Employees are clearly part of the organizations created to serve their customers. The organization lifecycle is really about the design, staffing, management, development, and improvement of organizations—factors that allow the company to serve the markets for its products and services. Therefore, the individual employee lifecycles are all part of the higher-level organization lifecycle.

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The parallels among markets, organizations, and categories are strong. They support the adoption of CLM to represent the process space that drives the performance of all goods, services, and suppliers to deliver continuous improvement—and differentiate a company from its competition.

2 The term category represents a group of goods and/or services that an organization procures or purchases. Some firms refer to these groupings as commodities, but this word has connotations of low differentiation and possibly, low value. The grouping into categories, or commodities, provides structure based on the particular needs of the buying organization. The category is often based on the supply market or industry, for example, chemicals, raw materials, or energy, or possibly the structure of the buying firm, for example, assemblies, equipment, or services. Organizations often have titles of Category Team Leaders or Commodity Managers or Strategic Sourcing Managers for the people who manage the procurement of the categories. These organizations are generally subdivided along logical category lines.

3 From a seminar presentation by Mohan Sawhney, Kellogg Graduate School of Management, on September 2000, entitled “Beyond CRM: Managing Relational Equity.” At the time of this writing, this presentation is available on the Internet at the following address: http://www.mohansawhney.com/registered/content/presentations/workjobandtheneweconomy.pdf
References / Notes:
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