Technology’s Double Edge, Supplier Innovation Management, and the Procurement Operating Model

27th CPO Executive Roundtable

Chicago | 14–15 October 2015
A.T. Kearney’s 27th Chief Procurement Officer (CPO) Executive Roundtable focused on the topics of technology’s double edge, supplier innovation management, and the procurement operating model. These three topics remind us of the need for procurement to continually refresh its capabilities to evolve in order to meet tomorrow’s challenges.

This document presents highlights from the interactive presentations, panel discussion, and roundtable discussions that took place over the course of the CPO Roundtable’s two days.

Day One
On the Road to Disruption: The Impact of Exponential Technologies

Speaker: Erik Peterson, partner and managing director of the Global Business Policy Council, A.T. Kearney

We are at a remarkably volatile point in history that makes it difficult to forecast where geopolitical circumstances, economic events, social churn, and a range of other factors will take us. Compounding this challenge is the rapid evolution of six key technologies—deep and pervasive information technology (IT), artificial intelligence (AI), robotics, the Internet of Things (IoT), biotechnology, and nanotechnology—that are individually and collectively poised to disrupt business and society in unprecedented ways.

Rapid advances in data generation, data storage, and analysis are allowing for unprecedented levels of personalization while bringing significant potential to disrupt entire industries. Big data allows advertisers to send targeted ads to consumers’ mobile devices. Start-ups are democratizing finance through alternative electronic lending platforms. Industries such as hotels and transportation also face disruption through network orchestrators that utilize mobile labor pools and underutilized assets through the so-called sharing economy. Yet companies are also utilizing IT to grow, as Siemens is doing via the development and manufacture of the technologies that power the IoT. Executives perceive phenomena such as cloud computing, big data, and mobile technology as both a challenge and an opportunity in equal measures.

AI, although it has advanced relatively slowly, appears to be on the verge of a significant breakthrough. Artificial narrow intelligence, which specializes in a single specific area or task, is already in use, while two more advanced types—artificial general intelligence that can perform any cognitive task that a human can and artificial super intelligence that will overtake our own capabilities for thought—are expected to come into existence in the coming decades. IBM is developing commercial applications for its Watson cognitive thinking system that uses natural language processing and machine learning to derive insights from unstructured data. The U.S. Department of Defense’s Defense Advanced Research Projects Agency (DARPA) has launched a Watson-esque project called Big Mechanism to scan existing literature on cancer to develop new hypotheses. Self-driving cars and AI trading tools are also close to becoming a reality.

IT and the physical world converge in the IoT, which already has a population of 4 billion devices—a number that is expected to increase sixfold by 2020. These devices encompass trillions of dollars in value that touch every sector, segment, and consumer: industrial
applications, transportation, healthcare, personal wearables, and beyond. Similarly, the use of robotics in the form of flying drones and industrial robots will see notable growth. Robotics is rapidly evolving into creations such as self-driving cars and micro-drones.

The pace of developments in biotechnology is speeding up as the costs of DNA sequencing and computing power drop. This is a double-edged blade, as every single organism’s DNA can be genetically manipulated, with implications both marvelous and horrifying. Bioprinting, which applies 3D printing to biotech, will allow for the manufacture of animal tissue. Finally, the movement toward nanotechnology continues as all sorts of devices continue to take on smaller forms.

As has already been made clear by our experiences with the Internet, technology brings threats as well as benefits. Cyber crime losses are estimated to be in the range of $500 billion annually across the globe; connected devices and systems are vulnerable to attacks ranging from data theft to “ransoming” and even physical damage to properties.

Corporations are challenged by the need to keep up with technology’s evolutions and to protect themselves against the potential downside of these developments. On both ends, alliances will be critical—through deals in which procurement plays a leading role. In order to do so, procurement will need to improve both its people skills and its technical skills. Small, disruptive suppliers will become highly prized and be able to choose which companies they work with.

Even as technology brings change, it will help companies respond more quickly and in better ways as they get better at using data. As network orchestrators continue to emerge and new technologies allow for manufacturing on demand, the value of traditional procurement and supply chain work will become marginalized. Procurement will need to be more than a doer; CPOs will need to become change agents.

Securing Growth with Supplier Innovation

Speaker: Kai Engel, partner, A.T. Kearney

Collaborative innovation is critical to competitiveness. Yet most have more questions than answers around how to collaborate, especially with suppliers. The best processes, skill sets, and technologies have yet to be defined. What is clear is that the competitive, confrontational behavior of the strategic sourcing era will need to be toned down in order to build the openness and trust needed to collaborate effectively. While suppliers are bursting with ideas and new technologies, the guidance they receive in collaborating with a larger company helps them to better target their efforts and increase their efficiency.

A number of key factors are driving the move toward collaborative supplier innovation. Companies continue to face cost pressures, leading them to look to reduce cost in their value chains and through collaborative cost reduction. The challenges of singlehandedly making the technological breakthroughs needed to drive the development of new high-margin products also drives supplier collaborations—no company working alone can develop all of the systems needed for a self-driving car. Similar breakthrough technologies are needed to keep pace with the increasing role of connectivity and the IoT.

While product innovation is critical, innovation is not limited to breakthrough products. Process, service, and even business model innovation are also important. Business models must evolve in order to support innovation efforts and differentiate brands. Incremental innovation helps to extend product life cycles and launch variants.
The innovation framework begins with the definition of the innovation strategy, which must be well articulated across the enterprise and endorsed by key stakeholders. Procurement contributes to the strategy by providing insights on technology dynamics and maturity. Ideas and investments must then be leveraged to maximize portfolio value; procurement works with the supply market to provide, evaluate, and improve ideas. As companies succeed with innovation efforts they can increase their efficiency and speed; supply partners help to reduce development cost and time. Maximizing the value of successful innovations can improve lifetime profitability; supplier efficiency helps to reduce the cost of goods sold. Building and maintaining the foundation for innovation and execution via organization, culture, processes, and tools can ensure ongoing success; as part of this, the company and its innovation-focused suppliers must jointly invest in governance structures. A robust supplier relationship management (SRM) program that includes investments in suppliers can be effective.

Innovation leaders set targets, agree on a joint purpose, and focus on building trust through a win-win value proposition.

Innovation leaders are achieving results that are superior to those of the general population of companies by several degrees of magnitude. They are doing so by including collaborative supplier innovation in their innovation strategy and emphasizing value creation over cost reduction. They are open to change and new ideas from outside. They set targets, agree on a joint purpose, and focus on building trust through a win-win value proposition that can include aspects such as gain sharing and exclusivity agreements that help to grow value.

Successes take on a wide range of forms. More than a decade ago, P&G turned to open innovation to systematically search for proven technologies as well as products that could be improved and scaled up, increasing its R&D productivity rate by 60 percent, doubling its innovation success rate, and reducing its innovation costs. Sartorius worked with a machine manufacturer to reduce more than 100 parts in a scale to a single modular component to shrink costs, cut time to profit in half, and increase flexibility in order to respond better to customer requests. Leveraging the services of a digital solution provider allowed a warehouse operator to take out more than 20 percent of its fleet management costs through real-time asset utilization information. CEWE Color recognized the dual threat and opportunity posed by the move from analog to digital photography and moved early to work with software companies to develop and continuously improve its online applications, allowing it to expand its leadership in the European market.

Procurement is critical to success in collaborative partnerships. It starts by segmenting suppliers according to their innovation potential against the innovation strategy, then clearly communicating intent to these potential partners. After decades of engaging in cost-based strategic sourcing efforts, not every procurement professional is suited for the softer negotiations required to establish partnerships. New talent is needed as the expectations for procurement continue to evolve. So, too, is a new awareness of which suppliers can be aggressively sourced; Toyota has long taken this into consideration, as it prizes supplier innovation. Procurement is uniquely positioned to provide end-to-end solutions that make it a key contributor to external innovation efforts.
Panel Discussion

Moderator: Jim O’Connor, managing director and global head of venture capital, William Blair, and board chair, CEC 1871

Participants

• Jeff Ge, vice president of global procurement, Steelcase
• Alan Rice, vice president of corporate procurement, Southern Wine and Spirits
• Uldis Sipols, vice president of procurement, Sonoco Products
• Arnold Sowa, senior vice president and chief procurement officer, MetLife
• Kai Engel, partner, A.T. Kearney

There has never been a time when opportunities and threats alike have been as plentiful as they are now; innovation presents both. Disrupters will undermine traditional companies that fail to innovate and evolve to meet tomorrow’s consumers. Industries also have the potential to drive new disruptive technologies that will in turn transform other industries. For example, insurance companies may come to push their customers toward driverless cars through reduced premiums if these vehicles prove to reduce collisions; not every automaker will adapt to such a shift. Some are exploring a more holistic approach to product and service innovation that can be used to develop offerings for multiple business units. Technology can offer up on-demand sales opportunities; for instance, people may be able to insure themselves for specific activities or time periods rather than entire terms.

With so much pressure on quarterly earnings, some are challenged to invest in innovation. These efforts must show a measurable return on investment. Cost reduction and innovation are not diametrically opposed; the former can be folded into the latter, especially around incremental innovation, which can cost aspects out of a design as technology evolves. This is crucial as leading-edge products come to be commoditized; no company can allow its suppliers to reap long-term benefits from an expensive design when lower-cost options become available.

Though few will claim to have mastered innovation, a consensus is emerging that it is all but impossible to succeed through an innovation strategy that does not allow for contributions from the outside. This is in part a simple matter of mathematics; even for companies that have armies of engineers with a deep core competency, there are many more people with similar skill sets working elsewhere, including in the supply base. For this reason, even those companies that have yet to do so expect to increase the amount of innovation they adopt from outside. Both “big” questions and more narrowly focused ones are being taken to the supply base in order to increase the rate of innovation. Some anticipate increasing their internal innovation ability as well as their collaboration skills as their workforce ages out and is infused with younger hires who want to innovate.

While a wide net helps to capture innovations, wading through thousands of potential partners is no small task. Segmentation helps to rank these suppliers. Over time, too, some learn how to quickly filter whether a supplier is offering a genuine, marketable innovation even before meeting. Fully leveraging the supply base’s innovation potential may well require revamping governance and key performance indicators to help encourage this activity. Procurement can act in a manner akin to a venture capitalist by creating value for the company.
Open-Forum Discussion

**Moderator: Tim Coats, former vice president of worldwide sourcing, General Mills**

Topics of interest during the open-forum discussion that closed out the formal part of the day one program included talent recruitment and ways to apply supplier segmentation and SRM to supplier innovation.

Half of the roundtable participants have systematically changed how they recruit procurement talent in order to foster innovation. One move being made is to broaden innovation thinking by recruiting graduates from a wide range of academic majors. Others have increased their focus on emotional quotient (EQ), hiring people for their interpersonal skills first and procurement experience second in order to develop trusted advisors to the business who can open doors and help to drive the right discussion. Both practices represent longer-term investments rather than quick fixes.

High-potential suppliers are often the recipients of SRM programs that invest in the supplier with the expectation that they will yield innovations down the line.

Relatively few participants have changed their supplier segmentation process in an attempt to increase innovation. Some have done so with specific types of suppliers, such as technology providers. Others are taking more robust approaches with their critical suppliers, as well as those that are relatively unique in terms of the supply they provide or their capabilities. Another emerging filter centers on the potential a supplier may have to become a source of competitive advantage over the next several years.

These high-potential suppliers are often the recipients of SRM programs that invest in the supplier with the expectation that they will yield innovations down the line. SRM efforts also include supplier summits that join key suppliers together to share innovation plans and find common points to address together. Mutual trust and goal alignment are just the price of admission to events of this sort, but the value to be unlocked is sizable.
Day Two
Procurement Branding Messaging Report Out

Participants
- Quave Burton, vice president of procurement, Abercrombie & Fitch
- Tom Derry, chief executive officer, Institute for Supply Management
- Barbara Kubicki-Hicks, senior vice president and vendor sourcing executive, Bank of America
- Andrew Walker, senior vice president and chief procurement officer, Nationwide Insurance
- Tom Weill, chief procurement officer, Campbell Soup Company
- John Blascovich, partner, A.T. Kearney
- Joe Raudabaugh, partner, A.T. Kearney
- Gary Singer, partner and chief marketing officer, A.T. Kearney

Managing the brand of procurement was identified as an area of high importance and potential at the CPO Roundtable last April. Communicating just what it is that procurement does beyond “buying” is challenging, but doing so is critical to reaching our audiences. To explore how CPOs can collectively be more effective in this endeavor, a pilot branding strategy session was conducted with the participants listed above for several days in advance of the October 2015 CPO Roundtable. The pilot focused on two key audiences: young or potential practitioners (new talent) and the finance group or chief financial officer (CFO). What follows are some of the issues, thinking, and narrative that evolved from the participants’ efforts to fine-tune messages to address these audiences.

With start-ups appealing to so many younger professionals, corporations are challenged to attract these workers. Because the function is not well understood, procurement is not bringing on the socially networked, high-EQ individuals needed to take on strategic work. The assumption is that young professionals like to do volunteer work, be recognized for their achievements (though money does not motivate them as strongly as previous generations), and live up to the tenets of corporate social responsibility (CSR).

Selling young professionals on a job in procurement requires an emphasis on the many aspects of the field that play to this generation’s desires. Thus, procurement is portrayed as a function that provides an end-to-end enterprise perspective and access to executives both within the company and at suppliers. This plays to young professionals’ desires to network without the constraints of traditional hierarchies and siloes. Other procurement characteristics to emphasize include the facts that the function plays a change agent role and that innovative thinking is prized. Ultimately, the key messages to present are that procurement professionals can make a difference early in their careers, that they can take on significant responsibility, and that they can commercialize their passions. In short, procurement provides an unparalleled opportunity to attain access, flexibility, and empowerment.

At many companies, the CFO views procurement as a way to save money first and foremost. Value-added and strategic work in areas such as risk management, merger-and-acquisition support, and supplier innovation are often overlooked and must be emphasized in marketing
procurement. Failure to do so may well lead toward the function’s elimination as outsourcers and technology prove able to take on so much transactional and even strategic work. To some extent these discussions are a matter of framing all available data in terms the CFO will understand, such as how cost avoidance can help to beat inflation and how procurement influences the top as well as the bottom line. The key message to CFOs is that procurement is a high-impact value creator that can help them achieve a stronger leadership team role by empowering and challenging the function.

Some leading procurement organizations are already undertaking this sort of marketing effort through the employ of a dedicated procurement communications specialist who knows the multiple audiences to be reached and can articulate appropriate messages for each in order to promote the brand. In doing so, these communications people demonstrate the sort of EQ that is increasingly in demand for procurement professionals as they seek to understand how others think in order to better influence them.

As procurement’s span of influence continues to evolve, the role of the CPO itself could come to be rebranded as something along the lines of the “chief market dynamics officer” who works on commodity trends, inflation, technology substitutions, and the like. This will challenge us to become even more effective at managing the brand of procurement and shaping our messaging to lead our staff and improve our influence with various stakeholder audiences.

The roundtable audience was keenly supportive of the discussion of the branding pilot team and many volunteered to support the effort to advance this together going forward.

**Implications for the Procurement Operating Model**

*Speaker: Yves Thill, partner, A.T. Kearney*

A number of trends will influence the future direction of the procurement operating model. Volatility and the disruptive potential of new technologies will present both threats and opportunities. An increasing number of hyper-connected millennials will join procurement, helping to move the function toward more external innovation efforts that will require increasing levels of trust between buyer and supplier. Centralized procurement organizations built around standardized processes and leveraged buying power will be challenged to react and adapt quickly.

Procurement leaders from the 2014 *Assessment of Excellence in Procurement (AEP)* study have a broad mandate to generate value for the enterprise by taking on value creation opportunities. While short-term cost reduction will remain important to procurement, it will be somewhat deemphasized in favor of long-term strategic cost advantage efforts and strategic risk management. Supplier-driven innovation is projected to take on much more importance, while supplier diversity and CSR will remain secondary goals for most.

Leading procurement organizations currently emphasize role specialization in order to achieve effectiveness and efficiency. This applies to value-added activities such as category management and SRM, as well as enabling activities such as process design and both spend and cost analysis. Category managers have primary accountability to drive a range of activities from short-term cost reduction to strategic work such as risk management and supplier-driven innovation through to CSR and supplier diversity.

The move toward role specialization makes sense in light of the many things that category managers are expected to do. On the one hand, they are responsible for much of the
procurement-specific value add. But increasingly they are also asked to add value in tandem with the business via R&D and innovation management. Already, many procurement organizations are separating the “confrontational” sourcing personnel and the SRM teams.

In order to support the business in pursuing broader strategic objectives such as innovation, sustainability, or risk, the procurement function has to work with different parts of the business in a cross-functional effort. Unsurprisingly, procurement takes a strong lead role for driving both short-term cost reductions and longer-term strategic cost advantage, and partners mostly with the business and finance to pursue these two objectives. In comparison, procurement has less involvement and less of a lead role when addressing strategic risk management and long-term capacity objectives. In the pursuit of supplier-driven innovation, surprisingly the business takes on the lead role while procurement typically plays a more supporting role. Similarly, procurement is supporting rather than leading CSR efforts, and is all but left on its own to drive the supplier diversity agenda. Opportunities exist for procurement to do more and take on more of a leadership role within the organization. Doing so requires that it act as a business partner to the internal stakeholders and can instigate, initiate, and drive efforts to pursue broader business objectives, rather than act as a supporting service group. Easier said than done. Based on our CPO survey, the key obstacles that are preventing procurement from taking on such an elevated role include misaligned objectives, internal processes, and a lack of resources or skills.

While more than half of attendees reported that they have the flexibility to capitalize on changing market conditions, few are confident that they can launch comprehensive efforts quickly. Those that are prepared to act have some combination of embedded flexibility in the sourcing approach and category strategy, an organizational setup conducive to doing so, strong relationships, and a corporate culture that emphasizes flexibility.

Leading procurement organizations currently emphasize role specialization to achieve effectiveness and efficiency.

Open-Forum Discussion

**Moderator: Tim Coats, former vice president of worldwide sourcing, General Mills**

The open discussion that concluded day two of the CPO Roundtable touched upon several subjects of interest to the attendees, including the need for organizational change, new talent sourcing, extending into more strategic work, the category manager role, and category evolution.

Clearly, the business environment is changing rapidly. Is procurement ready to do so as well? Some organizations are endeavoring to become a “customer of choice” via robust SRM efforts, investing in the supply chain rather than just pulling value from it. Relationships centered on joint value creation are essential. Developing the skills to build these relationships takes time—some organizations are literally undergoing a generational talent change that they expect will be conducive to this development. Some are bypassing experienced procurement people in favor of those with more well-rounded backgrounds and skill sets. Old-style thinking can
actually be detrimental when working toward increased SRM and supplier innovation efforts. Also prized is the ability to calmly deal with surprises and ambiguity. Team players who have the confidence to lead through decisive action are highly sought.

Significant opportunities exist for procurement to increase its role as a connector. The work it does with the business, other functions and geographies, and the supply base position it to do so. One roundtable participant launched a strategic alliances team inside the product development group in order to improve speed to market of the rebranded products it buys from its supplier partners. Procurement’s presence within product development gave the legal and finance functions assurances that the proper processes and contracting procedures would be followed, reducing review time.

While every company is trying to do more with fewer resources, the category manager role may be somewhat overstuffed. They are already responsible for near-term market interventions as well as longer-term category strategies; now, they are increasingly being pulled into alliance and innovation work. Should one person be expected to effectively balance the competitive stance needed for sourcing against the partnering skills needed to collaborate?

Categories themselves are subject to evolution, and some may evolve rapidly in just a few short years. Some less important ones will simply give way to spot buys from online retailers that are moving into the business-to-business space. Technologies such as 3D printing also have the potential to eliminate buys for things such as spare parts, which will also reduce inventory costs.
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