

Trends in Services Purchasing and Supply Management

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Agenda

- Survey Background and Demographics
- Responsibilities and Salary information
- Nature of buying activities in services
- Onshore and Offshore Services Management and Satisfaction

Survey Background

- Survey sponsored by CAPS Research and the ISM Services Group
- E-mailed to approximately 3,000 people; primarily CAPS Research sponsors and ISM Title 1 Members
- Received 160 useable surveys

Respondent Characteristics: Companies

Total Companies Reporting	162	
Government Organizations	10	6%
Manufacturing Organizations	70	43%
Service Organizations	82	51%

83.9% reporting from a corporate perspective

16.1% reporting from a business unit perspective

Respondent Characteristics: Industries

Aerospace/Defense	1.8%	Media	1.2%
Automotive & Transport	1%	Metals & Mining	3.7%
Chemical	1.8%	Municipal, State & County Governments	3.7%
Computer Software and Services	5.5%	Personal Care	1%
Consumer Products Manufacturers	4.9%	Petroleum	1.8%
Diversified Foods/Beverages	4.9%	Pharmaceutical	3.7%
DOE	1.8%	Retail	1.8%
Engineering/Construction	2.5%	Semiconductor	1.8%
Environmental Services	1.2%	Services	6.8%
Financial Services	9.9%	Telecommunications Equipment	2.5%
Healthcare	3.7%	Telecom Svcs	1.8%
Industrial Mfg	16.7%	Transportation Svcs	7.4%
Leisure	1.2%	Utilities	4.9%

Respondent Characteristics: 'CPO' Title

Title	% Reporting	Services	Mfg.	Govt.
Number	162	82	70	10
Director	32%	34%	29%	40%
VP	32%	24%	43%	10%
Sr. VP	10%	13%	6%	0%
CPO	9%	7%	9%	20%
Other	17%	21%	14%	30%

*Other includes General Manager, CFO and Exec VP

Respondent Characteristics: Functional Area

Functional Area	% Reporting	Services	Mfg.	Govt.
Administration	7.8%	10%	3%	20%
Business Opns	7.8%	10%	5%	10%
Finance	9.8%	11%	6%	10%
Logistics	2.0%	1%	3%	0
Manufacturing	3.3%	3%	5%	0
Operations	14.4%	14%	17%	0
Supply Chain	38.6%	33%	43%	60%
Other	16.3%	18%	17%	0%

Respondent Characteristics: CPO Reports to:

Title	% Reporting	Services	Mfg	Govt
CEO	18.7%	13.8%	20.9%	11%
CFO	23.7%	23.8%	17.9%	22%
COO	5.8%	6.3%	4.5%	
Executive VP	11.5%	7.5%	14.9%	
Senior VP	15.8%	17.5%	11.9%	
VP	4.3%	15%	16.4%	
Director	3.6%	2.5%	1.5%	22%
General Manager	4.3%	3.8%	4.5%	
Other	12.2%	10%	7.5%	44%

Respondent Characteristics: CPO Reports to-

Functional Area	% Reporting	Services	Mfg	Govt
Administration	18.4%	15.8%	16.9%	50%
Business Operations	14.9%	19.7%	10.2%	
Finance	22.0%	30.3%	13.6%	25%
Logistics	0.7%		1.7%	
Manufacturing	6.4%	3.9%	10.2%	
Operations	14.9%	11.8%	20.3%	
Supply Chain	8.5%	6.6%	10.2%	12.5%
Other	14.2%	11.8%	16.9%	12.5%

Respondent Characteristics: Purchasing Organization

	Centralized	Decentralized	Hybrid	Outsourced
Direct Materials	56%	12%	29%	3%
Indirect Materials	45%	17%	35%	3%
Onshore Services	44%	23%	32%	2%
Offshore Services	47%	22%	26%	5%

Respondent Characteristics: Revenue

Revenue Breakdown:	No. of Respondents	% Reporting
Greater than \$10 billion	19	13.7%
Between \$5 and \$10 billion	16	11.6%
Between \$1 and \$5 billion	38	27.5%
Between \$500 million and \$1 billion	17	12.3%
Less than \$500 million	49	35.5%

Respondent Characteristics: % of Revenue

Respondent Revenues: all companies	Purchase Spend as a % of Revenue	Services Spend as a % of Purchase Spend	Services Spend as a % of Revenue
Greater than \$10 Billion	41%	43%	18%
Between \$5 and \$10 Billion	30%	43%	13%
Between \$1 and \$5 Billion	37%	22%	8%
Between \$500 million and \$1 Billion	45%	12%	6%
Less than \$500 million	47%	31%	15%

Respondent Characteristics: Spend as a Percentage of Revenue

Respondent Revenues: Manufacturing vs. Services firms	Purchase Spend as a % of Revenue		Services Spend as a % of Purchase Spend	
	MFG	SERV	MFG	SERV
Greater than \$10 Billion	43%	31%	50%	33%
Between \$5 and \$10 Billion	42%	23%	21%	60%
Between \$1 and \$5 Billion	49%	30%	16%	31%
Between \$500 million and \$1 Billion	45%	35%	9%	18%
Less than \$500 million	48%	43%	35%	29%

Respondent Characteristics: **Full Time Employees**

Organization:

- Average: 12,162 / firm
- Median: 2,400 / firm

Engaged in Purchasing & Supply Mgmt:

- Average: 105 / firm
- Median: 22 / firm

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Responsibilities and Salary Information

Employees Who Source & Purchase

	Direct Materials	Indirect Materials	Onshore Services	Offshore Services
Average number involved	43	26	21	10
Percent of PSM Employees	41%	25%	21%	10%

Percentage of Employees by Spend Type and Sector

Spend Category	Direct Materials		Indirect Materials		Onshore Services		Offshore Services	
	Mfg	Svs	Mfg	Svs	Mfg	Svs	Mfg	Svs
Average number of PSM employees engaged in:	63	45	46	13	32	20	20	17
% of PSM Employees by Sector	39%	48%	28%	14%	20%	21%	13%	17%

Spend Managed & Controlled by PSM

	Direct	Indirect	Services
Average	\$1,059 Million	\$337 Million	\$621 Million
% Involvement	65.5%	48.2%	68.1%

Supply Base Size

	Direct	Indirect	Services
Total Firms Reporting	107	113	114
Average Number of Active Suppliers	1,533	2,578	2,997
Median Number of Active Suppliers	200	425	295

Size of Service Supply Base

Number of active Service Suppliers	Respondents
< 1,000	68%
1,000 - 5,000	20%
> 5,000	12%

42% report an increase in number of offshore service suppliers over the past year

32% report an increase in number of onshore service suppliers over the past year

PSM Staffing Levels and Workloads

	Direct Materials	Indirect Materials	Onshore	Offshore
Average number of Active Suppliers per PSM Employee	36	101	105	71
Average Spend per PSM Employee (in Millions)	\$25	\$13	\$25	\$15

Note: a 2002 CAPS benchmarking study indicates average number of suppliers per buyer was 32-DM, 62-IM and 74 for services

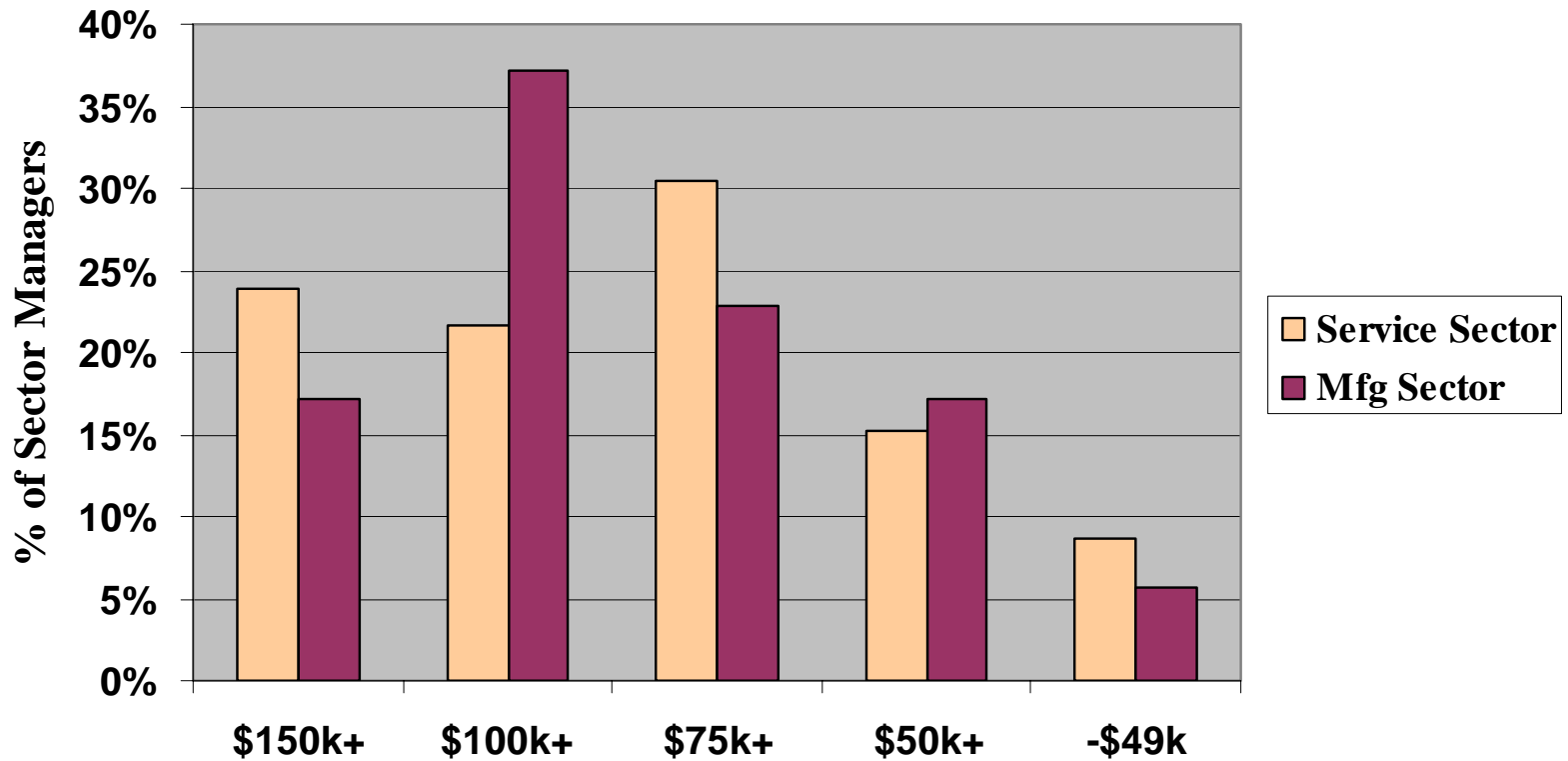
PSM Staffing Levels and Workloads by manufacturing and services industries

Sector	Direct Materials		Indirect Materials		Onshore Services		Offshore Services	
	Mfg	Svs	Mfg	Svs	Mfg	Svs	Mfg	Svs
Avg # Active Suppliers Per PSM Employee	21	29	84	104	67	129	33	47
Avg Spend per PSM Employee (in millions)	\$37	\$20	\$21	\$27	\$28	\$34	\$15	\$18

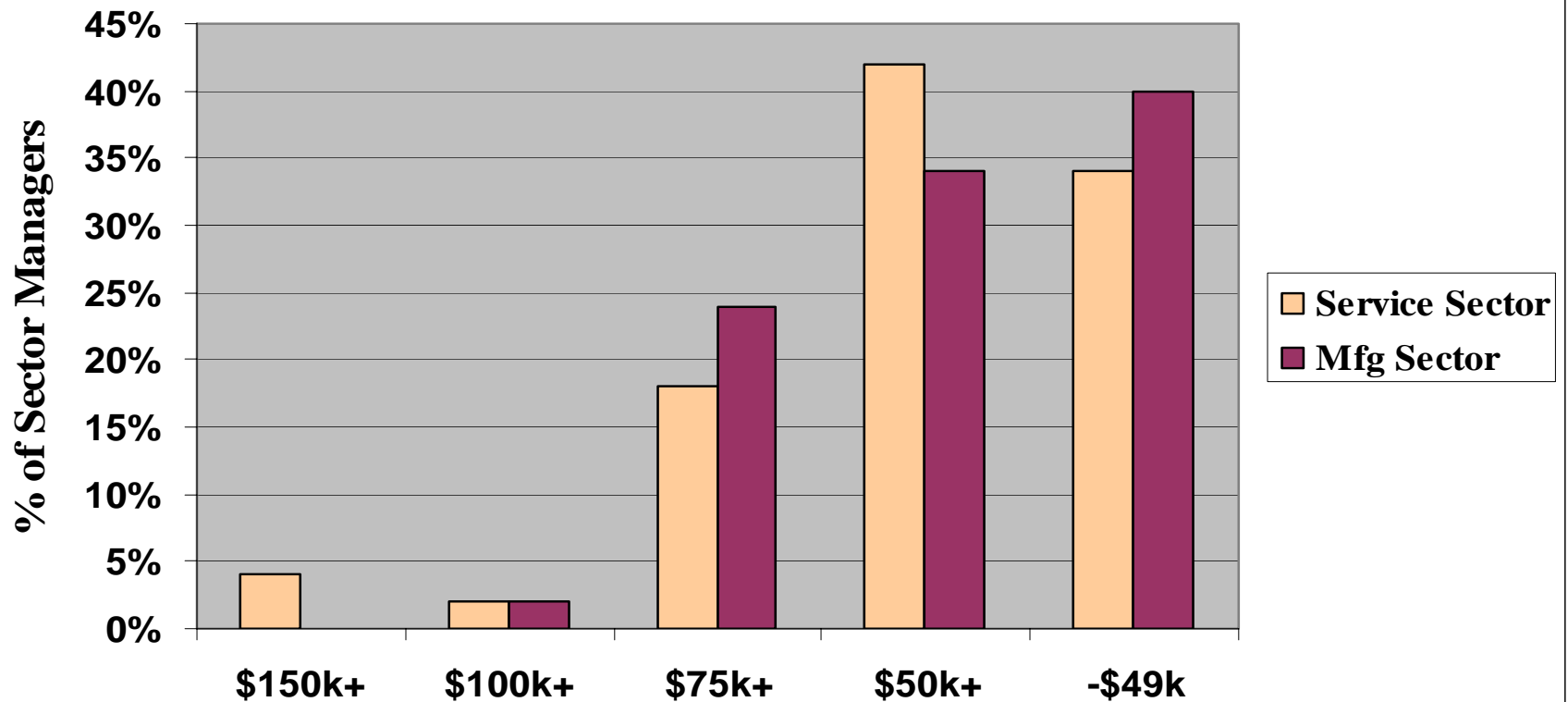
Salary Range



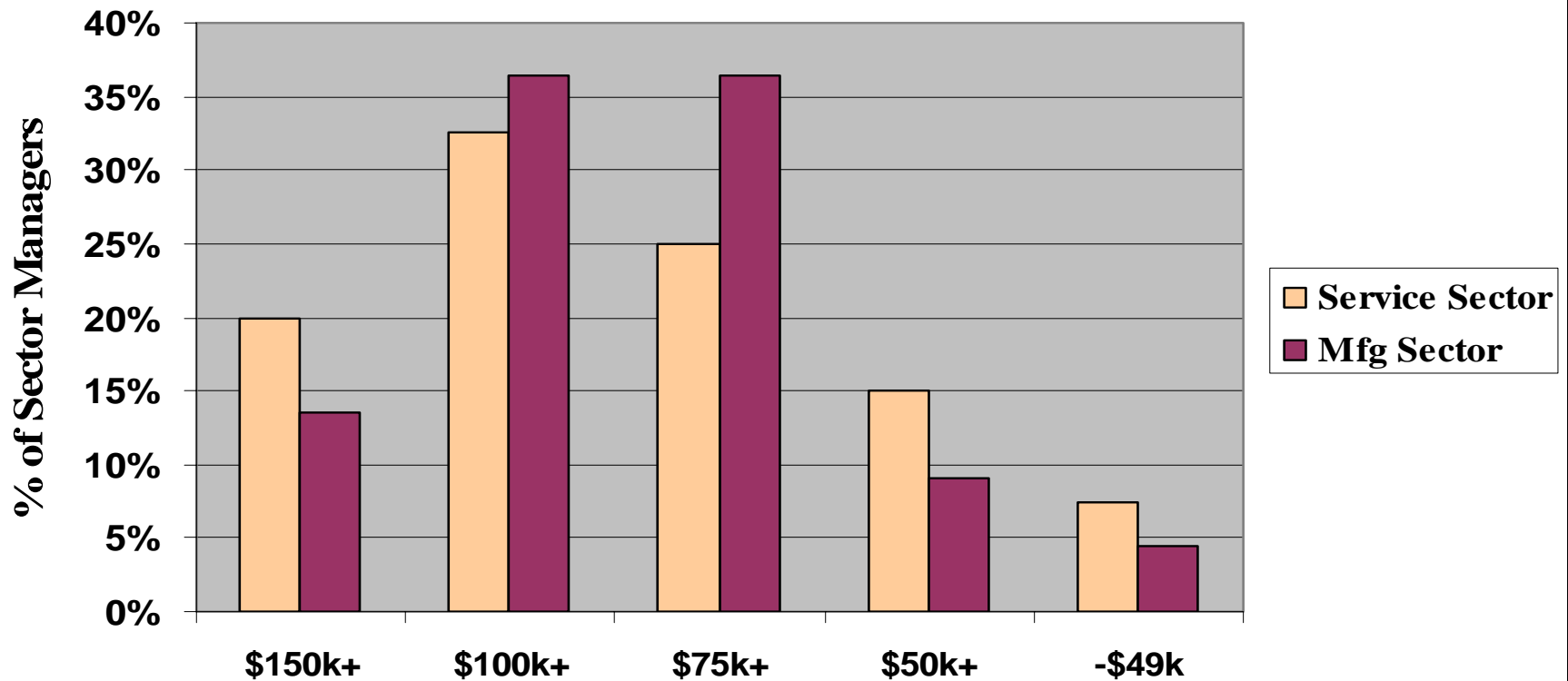
Salaries for those who Manage Services



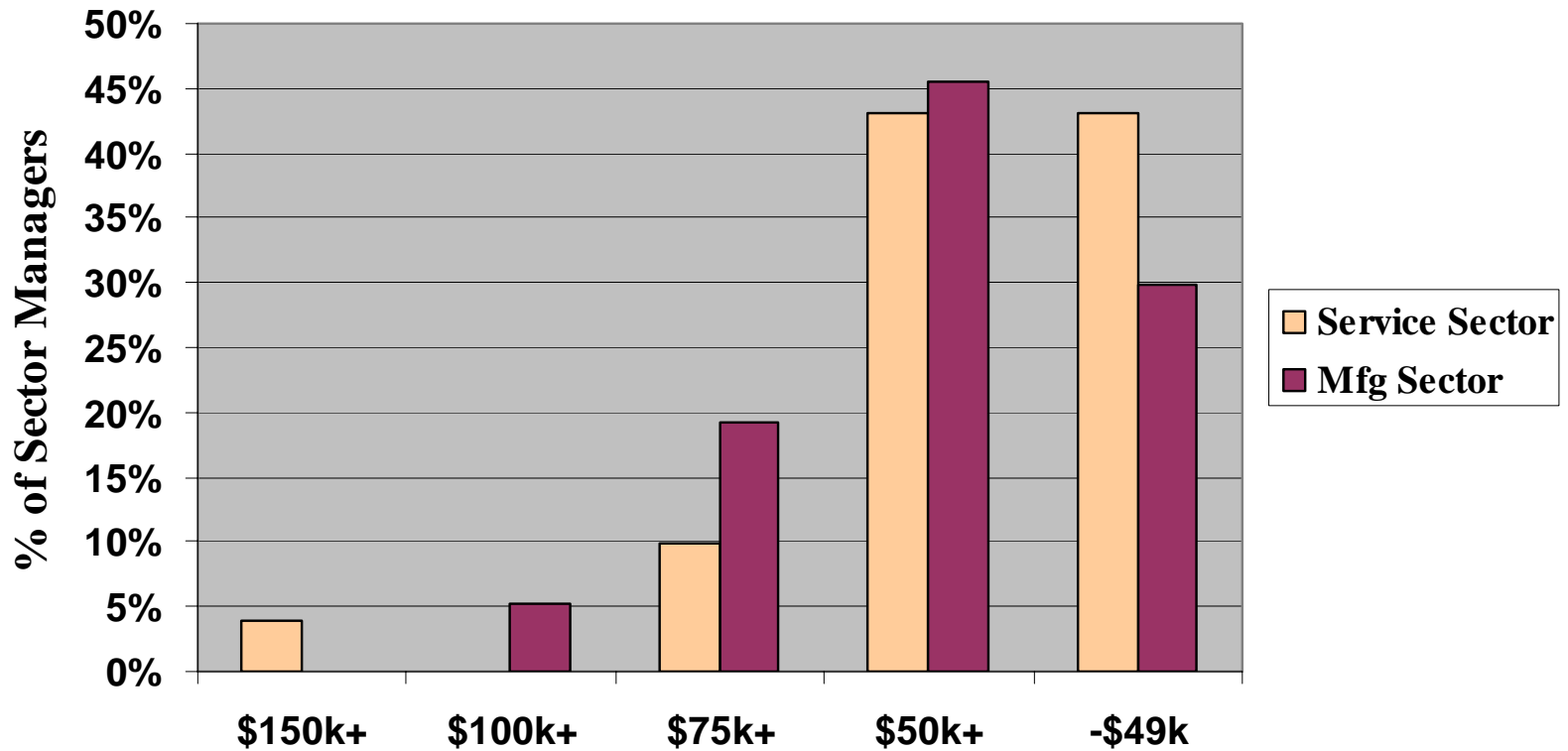
Salaries for those who Buy Services



Salaries for those who Manage Direct Materials



Salaries for those who Buy Direct Materials



How would you view a move from managing direct materials to managing services procurement?

	Manufacturing	Services
Promotion	4%	17%
Demotion	21%	2%
Lateral	73%	74%

Spending Patterns and Approaches

What are the trends in spend, and what tools and approaches are used to manage this spend, with an emphasis on services?

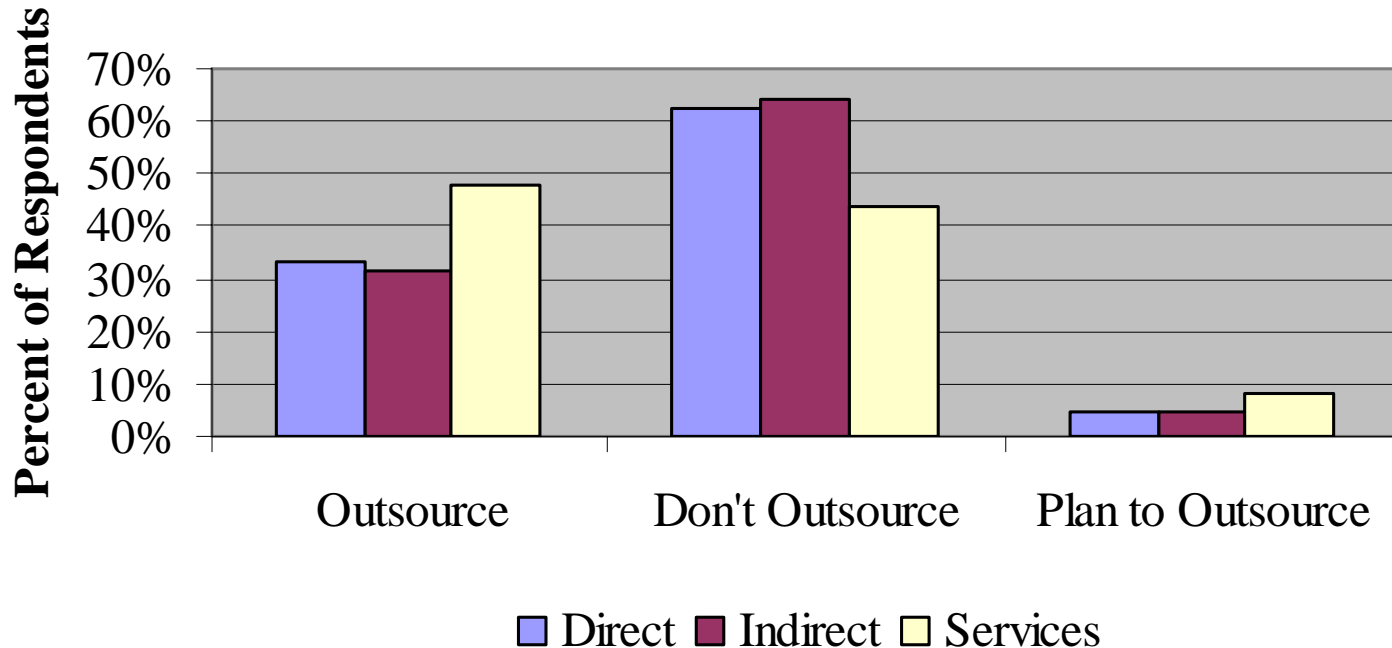
Overall PSM Spending Trends

	Increase	Decrease	No Change
Direct Materials	69%	10%	22%
Indirect Materials	66%	14%	20%
Services	77%	5%	18%

Currently, 74% of services spend is onshore, and 26% is offshore

Outsourcing Intentions (by spend category)

Outsourcing



Trends in IT Usage to Manage and Monitor Spend

	Direct	Indirect	Onshore	Offshore
ERP (such as SAP, Microsoft, Peoplesoft, Epicor)	71%	66%	59%	48%
B2B or Supply Chain Software (such as Oracle, SAP APO, I2, Manugistics)	37%	31%	28%	17%
PSM (such as Ariba, Perfect Commerce, Rearden, SABRE, Chimes)	35%	39%	37%	26%
Custom/Legacy	48%	39%	34%	22%

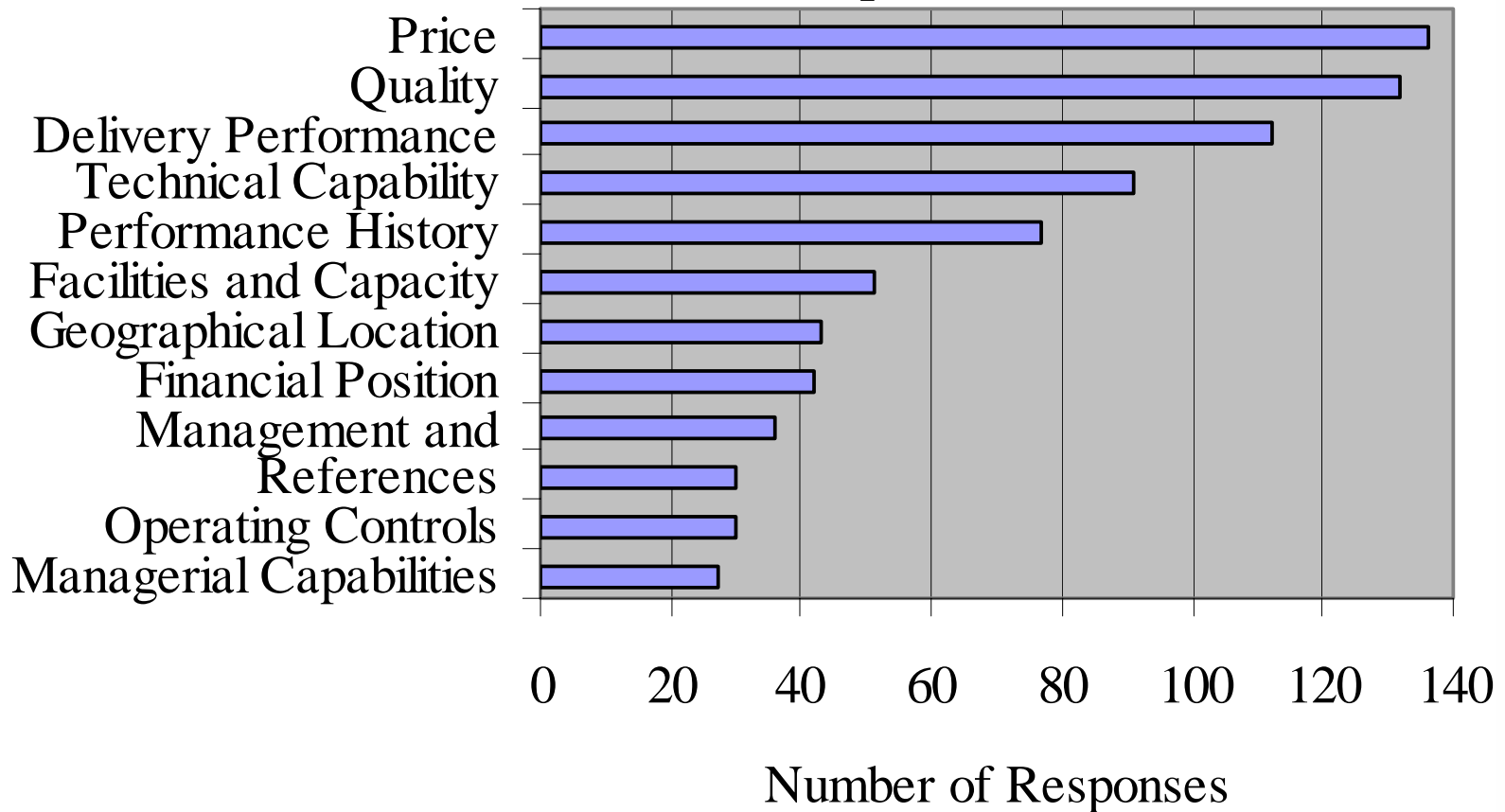
Primary Strategies for Managing Services by Sector

	Services	Manufacturing	Government
Business Process Outsourcing	17%	23%	30%
Maintaining Services in House	38%	19%	30%
Out-Tasking while Maintaining Significant Control	45%	58%	40%

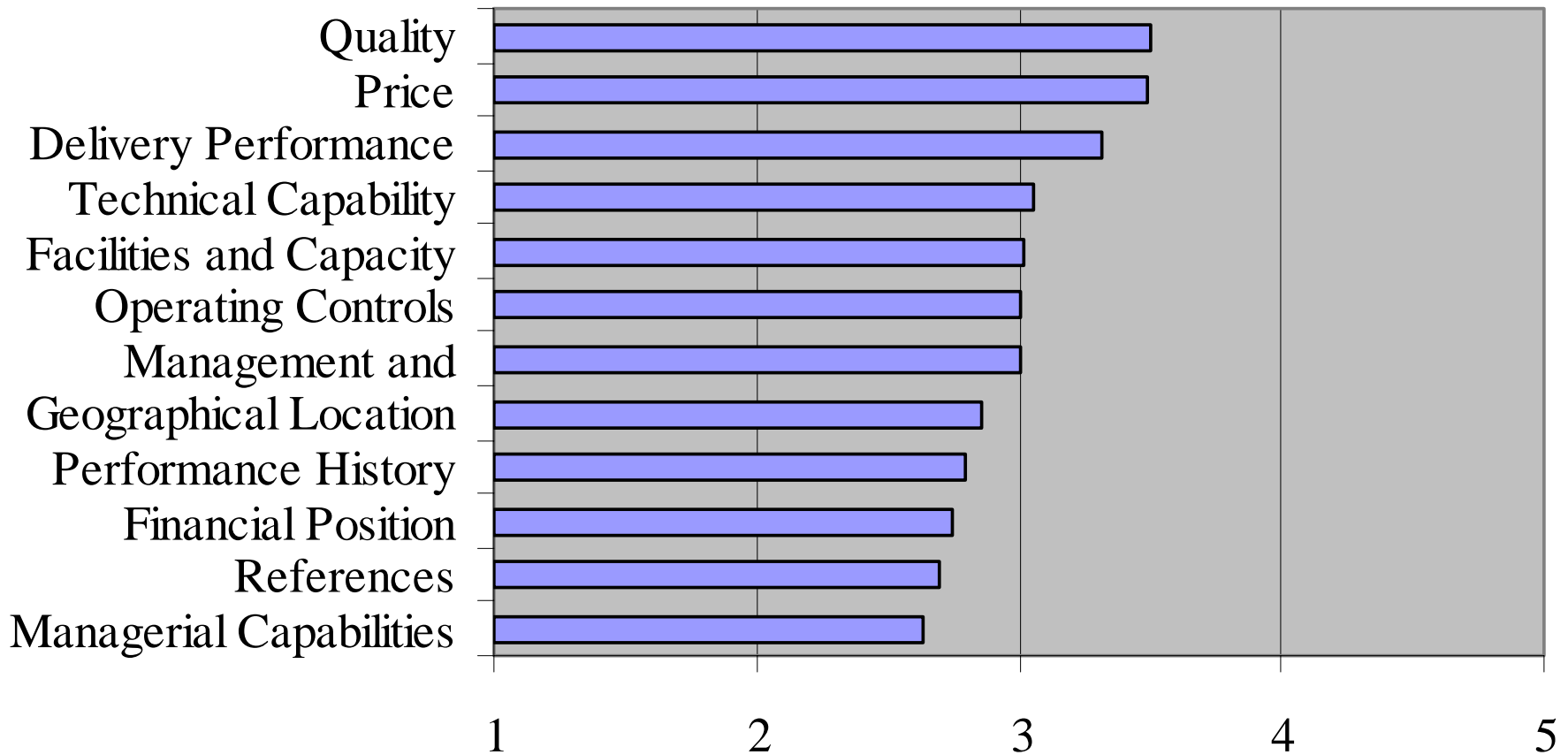
Service Supplier Selection Criteria: Top 5 Most Frequent Responses

1. Price
2. Quality
3. Delivery Performance
4. Technical Capability
5. Performance History

Services Supplier Selection Criteria: Frequency of Mention in Top Five



Mean Importance Scores for Service Supplier Selection Criteria



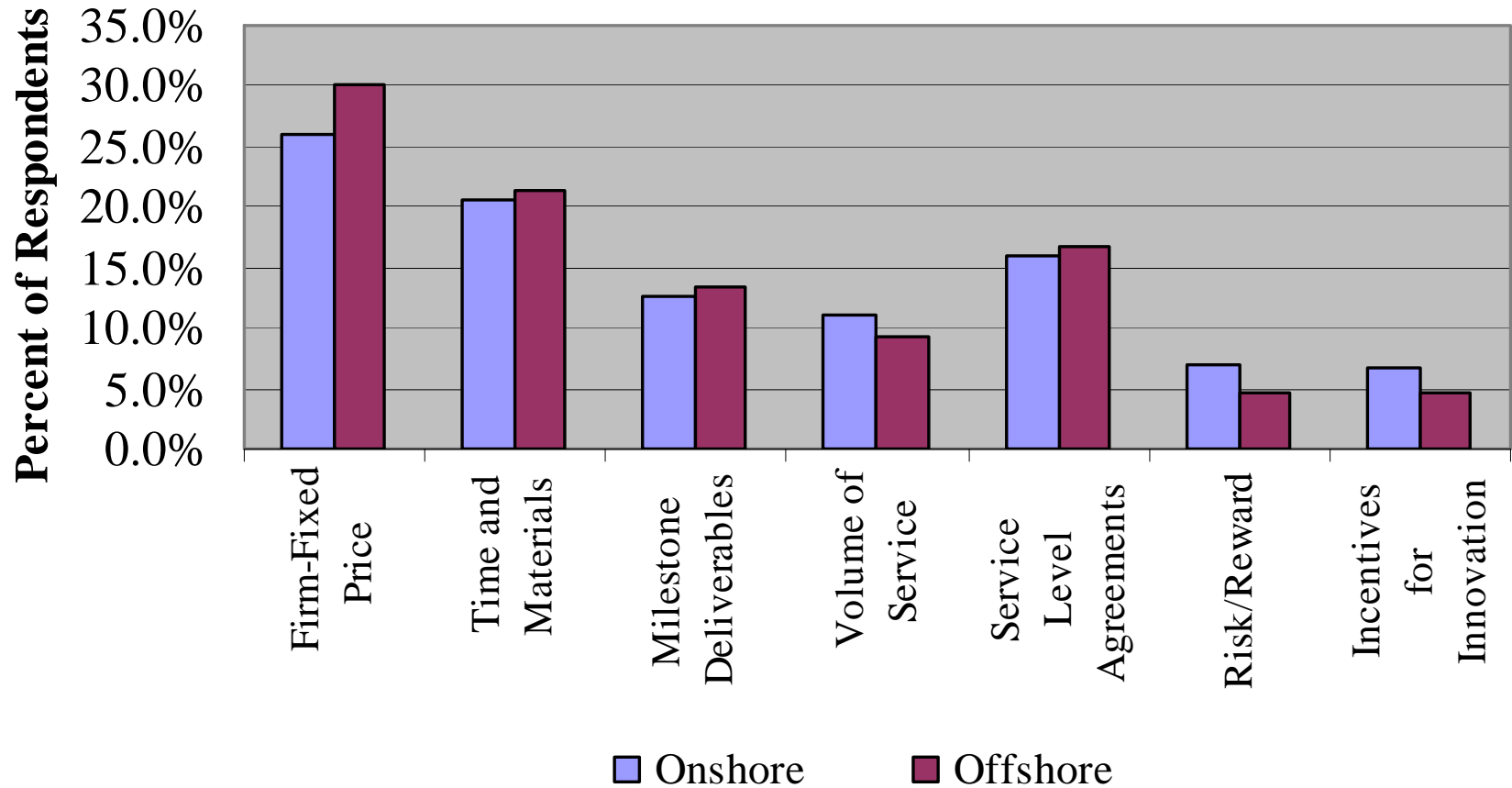
5=most important; 1=least important

Mean Scores

Onshore and Offshore Services Management and Satisfaction

How do we manage services, how involved are we in services procurement, and how satisfied are we with the outcomes?

Contracting Methods: Percent of Respondents that use the following methods for Services



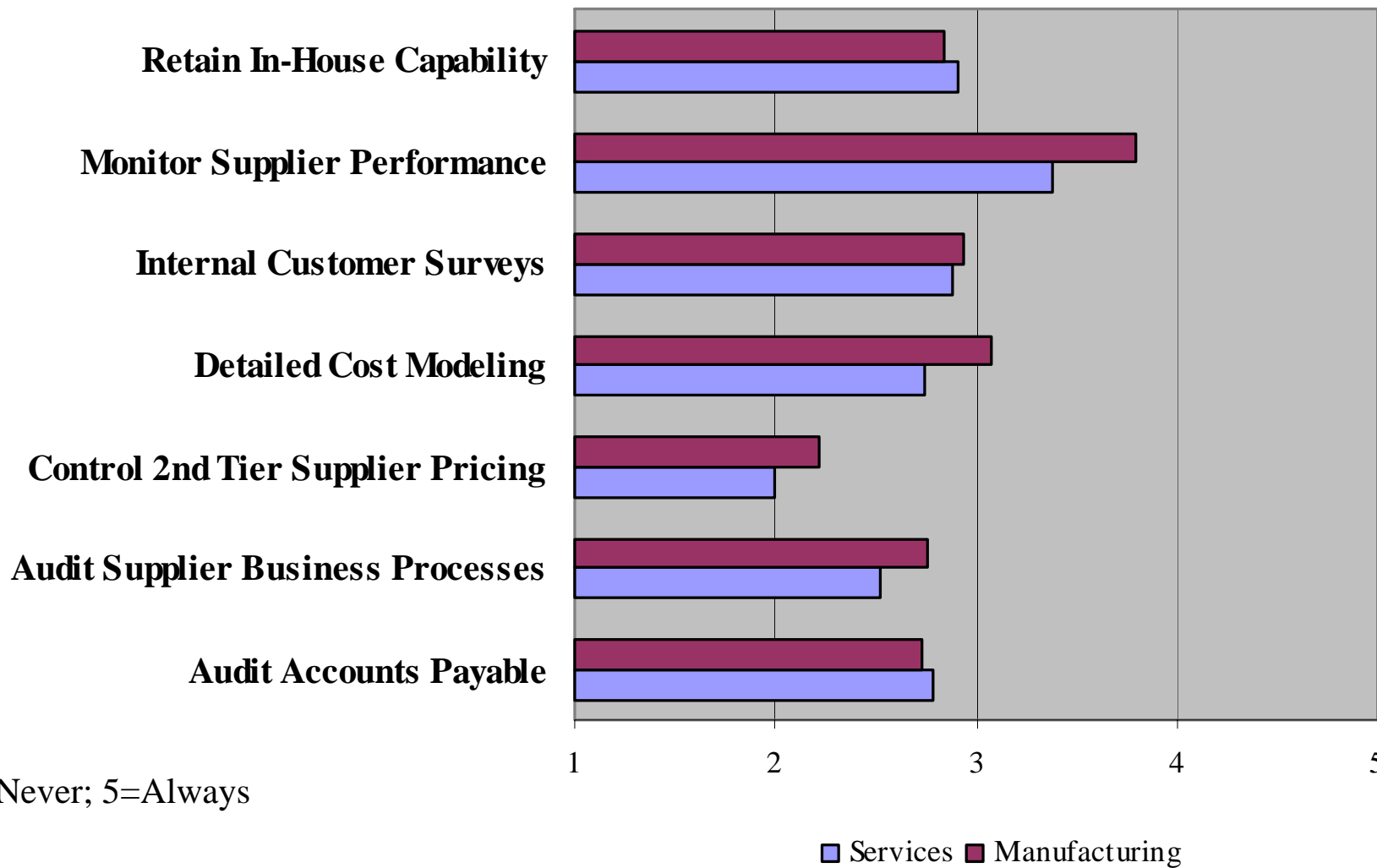
Measuring Supplier Performance

	Onshore	Offshore
Percentage that measure active supplier performance	65.3%	38.1%
For those who measure, percent of active supply base covered	46.5%	56.9%

Meeting Supplier Performance Expectations

- **80%** of active onshore suppliers met expectations
- **74%** of active offshore suppliers met expectations
- **82%** of active direct & indirect suppliers met expectations

Approaches for Managing Service Supplier Performance



1=Never; 5=Always

■ Services ■ Manufacturing

PSM Control Over Services-Related Purchasing

Positive:

- **26%** Always monitor supplier performance
- **12%** Always perform detailed cost modeling
- **11%** Always conduct internal customer survey

Negative:

- **33%** Never control 2nd tier pricing
- **20%** Never monitor supplier performance

Reliability of Onshore versus Offshore Service Suppliers

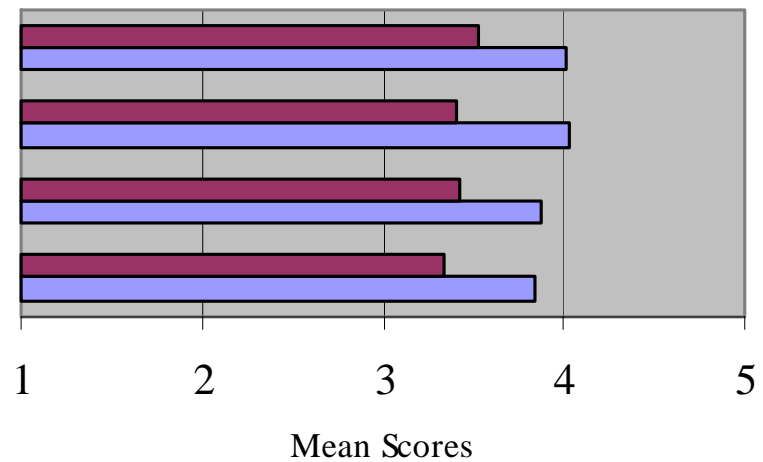
Reliability of Service Providers

Services are provided correctly the first time.

Services are provided when promised.

Accurate billing is provided.

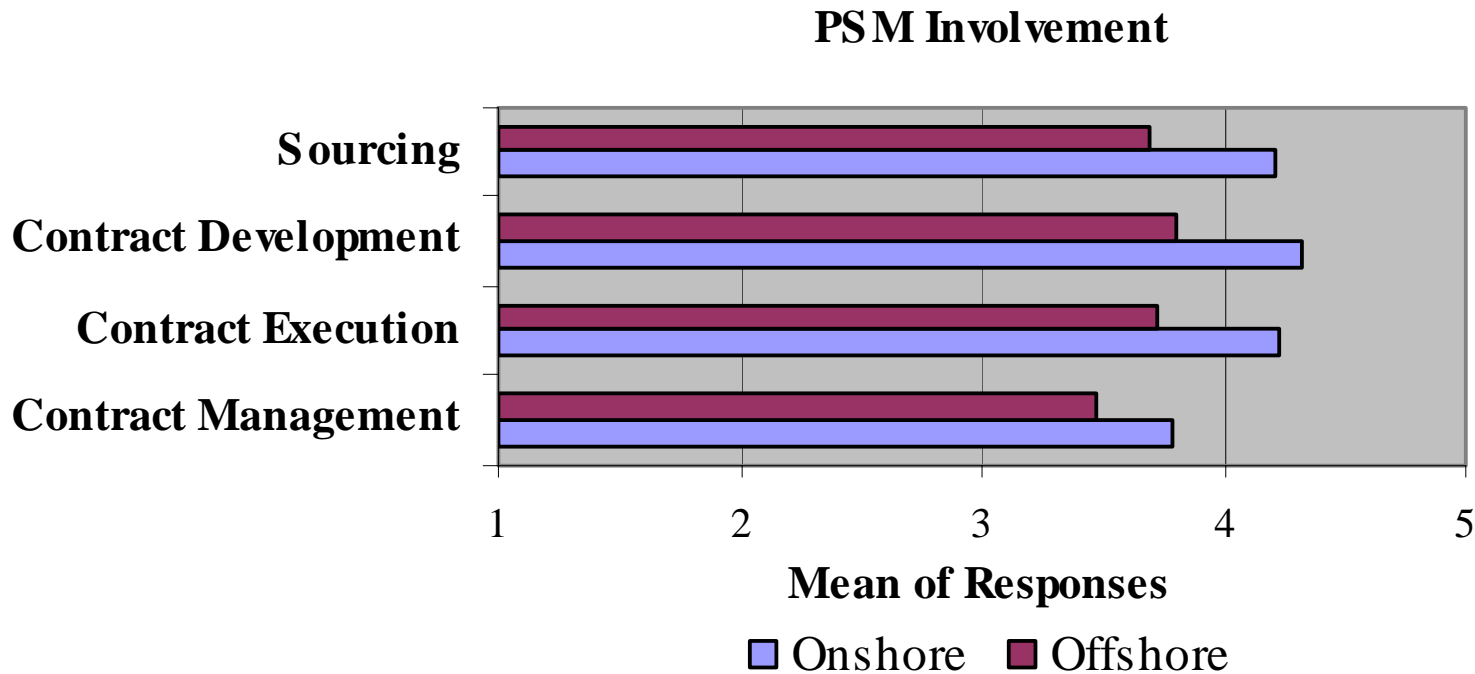
Services suppliers records are reliable and accurate.



■ Onshore ■ Offshore

1=Rarely; 5=Usually

How Involved is PSM in Onshore and Offshore Services Sourcing?



1=Rarely; 5=Usually

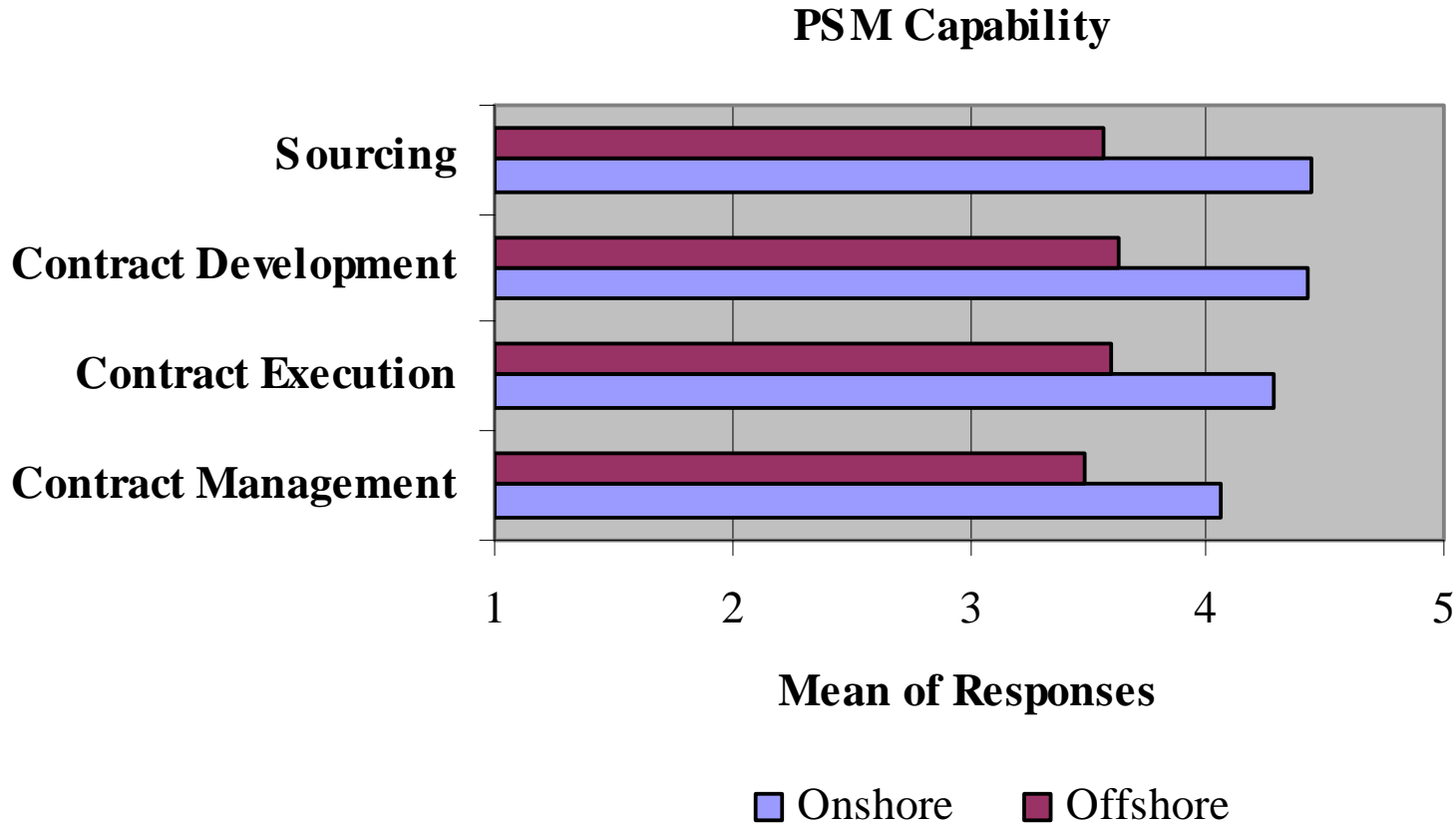
Percent of respondents that indicated they are always involved in these activities (a score of 5)

	Onshore Services	Offshore Services
Sourcing	54%	43%
Contract Development	55%	47%
Contract Execution	56%	48%
Contract Management	42%	38%

Percent Indicating they are rarely involved (Score of 1)

	Onshore Services	Offshore Services
Sourcing	3%	17%
Contract Development	2%	15%
Contract Execution	3%	17%
Contract Management	7%	18%

How capable does PSM feel in onshore and offshore services sourcing?



1=Low; 5=High

Percent of respondents that indicated they feel they are highly capable in participating in the following activities (a score of 5)

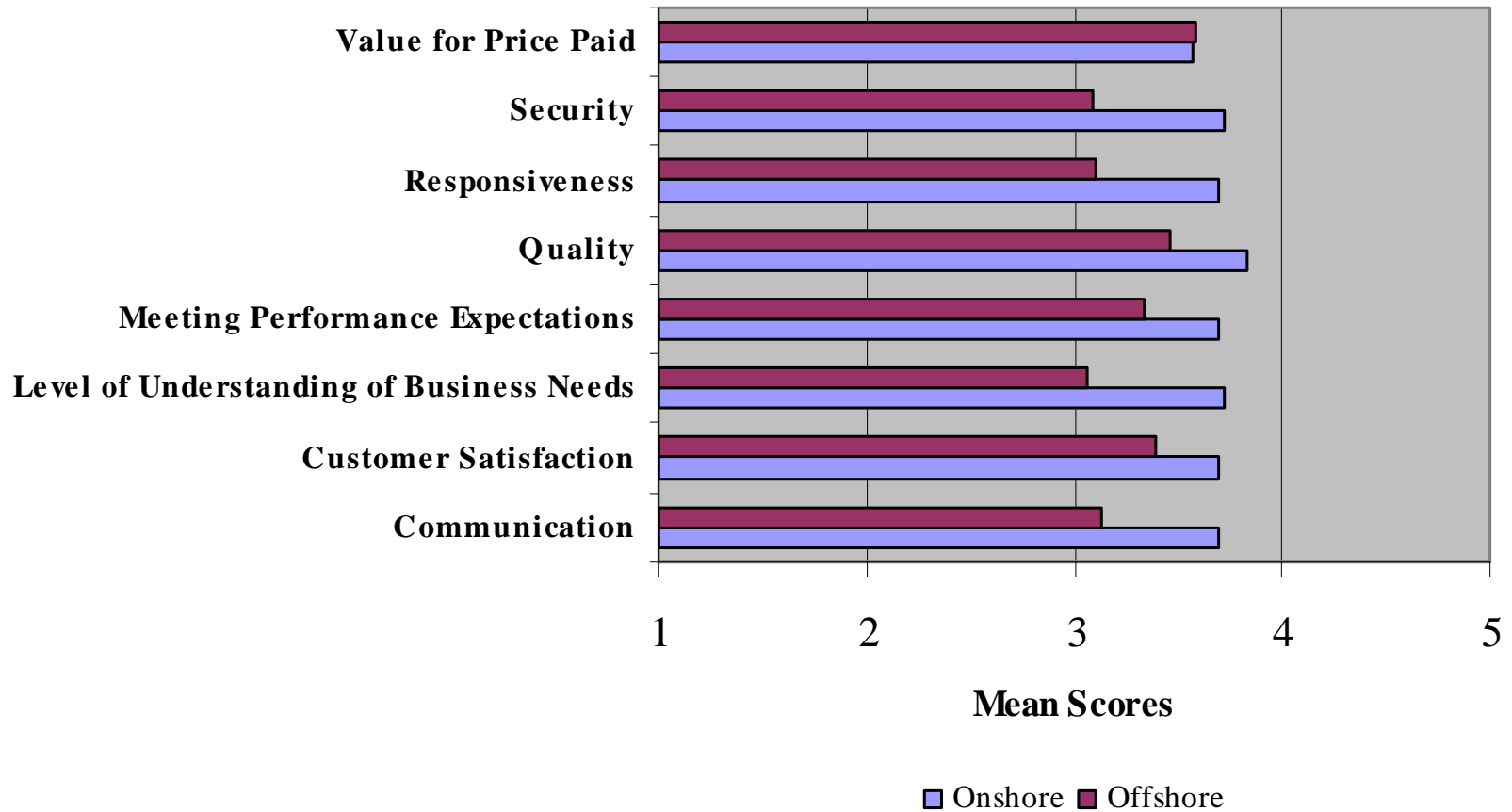
	Onshore Services	Offshore Services
Sourcing	58%	29%
Contract Development	58%	32%
Contract Execution	55%	34%
Contract Management	43%	27%

Percent of respondents that indicated they feel they are a low capability in participating in the following activities (a score of 1)

	Onshore	Offshore
Sourcing	1%	9%
Contract Development	1%	9%
Contract Execution	3%	11%
Contract Management	2%	11%

How Satisfied is PSM with Onshore and Offshore services sourcing?

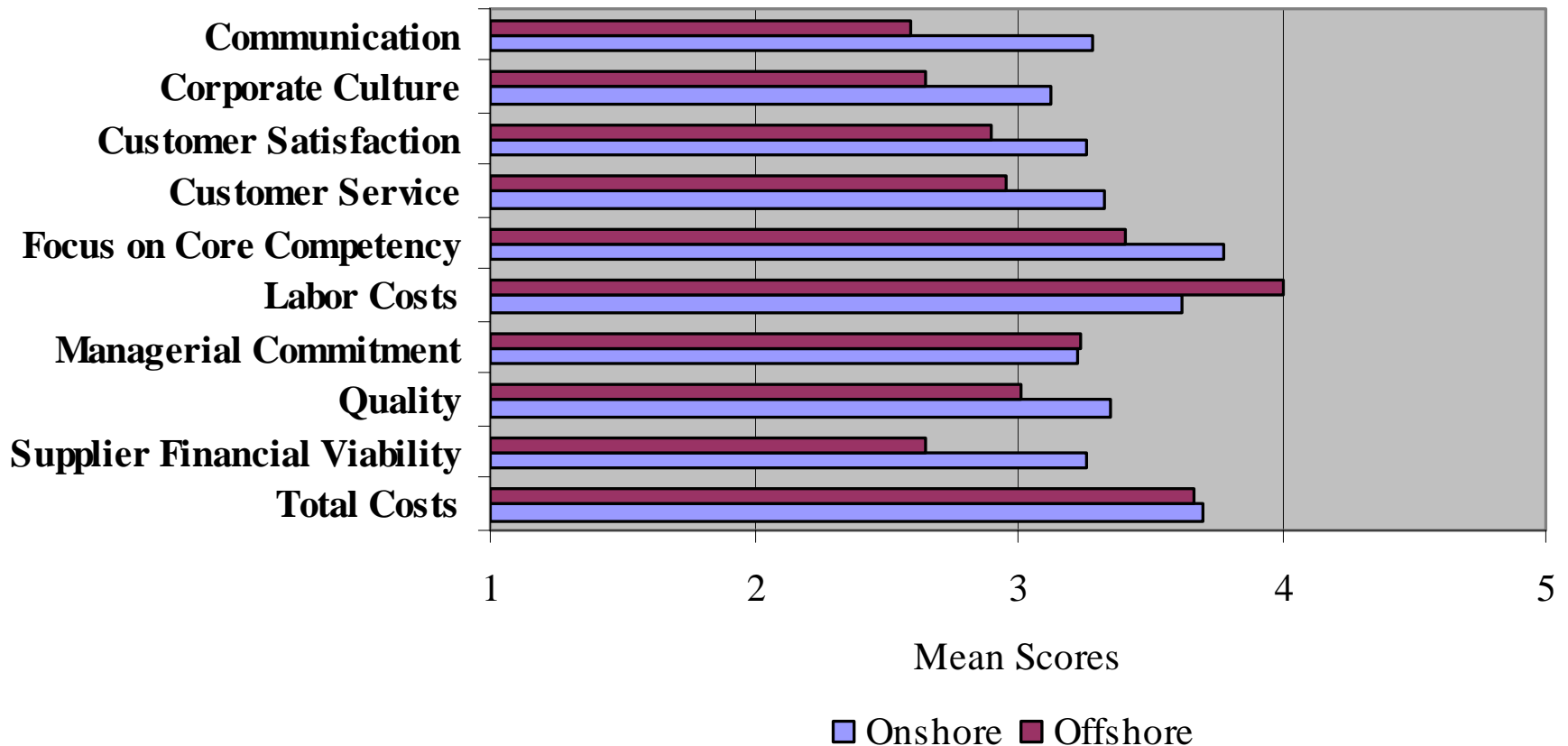
Level of Satisfaction



What are the Outcomes of Onshore and Offshore Services Sourcing versus In-house?

1=Worse; 3= Same; 5=Better

Results of Services Outsourcing



Summary

- High number indicate the CPO is part of “supply chain” area
- More reporting to Finance than in the past
 - May be indicative of high number of service firms reporting, or the influence of Sarbanes Oxley
- Reporting levels are relatively high, still only about 50% report in at the “chief” level
 - CEO, CFO, COO, President

Summary

- This benchmarking data indicates that the area of services supply management is gaining prominence
 - Competitive salaries in both Services and Manufacturing Sectors
 - Perception of a move to a services position is mixed, more positive in Service Sector
- Still seems to be a workload discrepancy
 - Services buyers have many more suppliers, despite a comparable spend level
 - Is even more pronounced for the services sector than for the manufacturing sector

Summary

- Most see their firms spending more in the future, but don't see a huge growth in outsourcing
 - Services is by far the leading area in current and planned outsourcing
- Yet services purchasing management still lags and needs improvement in a number of areas
 - Lowest IT implementation to manage and monitor suppliers of any spend category

Summary

- Supplier performance on service purchases is often not measured, especially for offshore sources
 - Manufacturing used a greater variety of methods in measuring services suppliers than do Services Sector firms
- PSM plays a bigger role, is more confident of its abilities and more satisfied with performance for offshore versus onshore services providers

Bottom Line: Good Progress has been Made

- There is still much opportunity for
 - more involvement
 - higher level involvement
 - improved management and measurement of services suppliers
 - There is a belief among participants that the TCO of offshore suppliers is higher than that of onshore.
 - Yet if we don't measure, how do we really know?
 - If we don't manage, how can we understand the improvement opportunities?

Feel Good---but be Proactive

- Sales people/organizations contact me:
How can we better understand and cope with supplier involvement in services purchases?
- See this as a new phenomenon that “threatens” relationship selling
- This demonstrates progress has been made!

Additional Slides and Glossary of Terms

Other interesting items we did not
have time to cover that were
included in the survey

Respondent Characteristics: **Purchasing Spend**

- \$275.5 billion total spend
- \$1.97 billion average spend
- \$280 million median spend
- 38.4% = purchasing spend / revenue

Respondent Characteristics: **Services Spend**

- \$103.9 billion total spend
- \$812 million average spend
- \$35 million median spend
- 14.6% of revenue
- 39% of purchase spend
- 74% onshore / 26% offshore

Purchasing Spend: Contract Length

	Long Term (>5)	Medium Term (1-5)	Short Term (<1)
Direct	31%	55%	12%
Indirect	5%	75%	17%
Services	13%	75%	15%

Onshore versus Offshore Spend: Contract Length

	Long Term (>5)	Medium Term (1-5)	Short Term (<1)
Onshore	9%	74%	17%
Offshore	19%	70%	11%

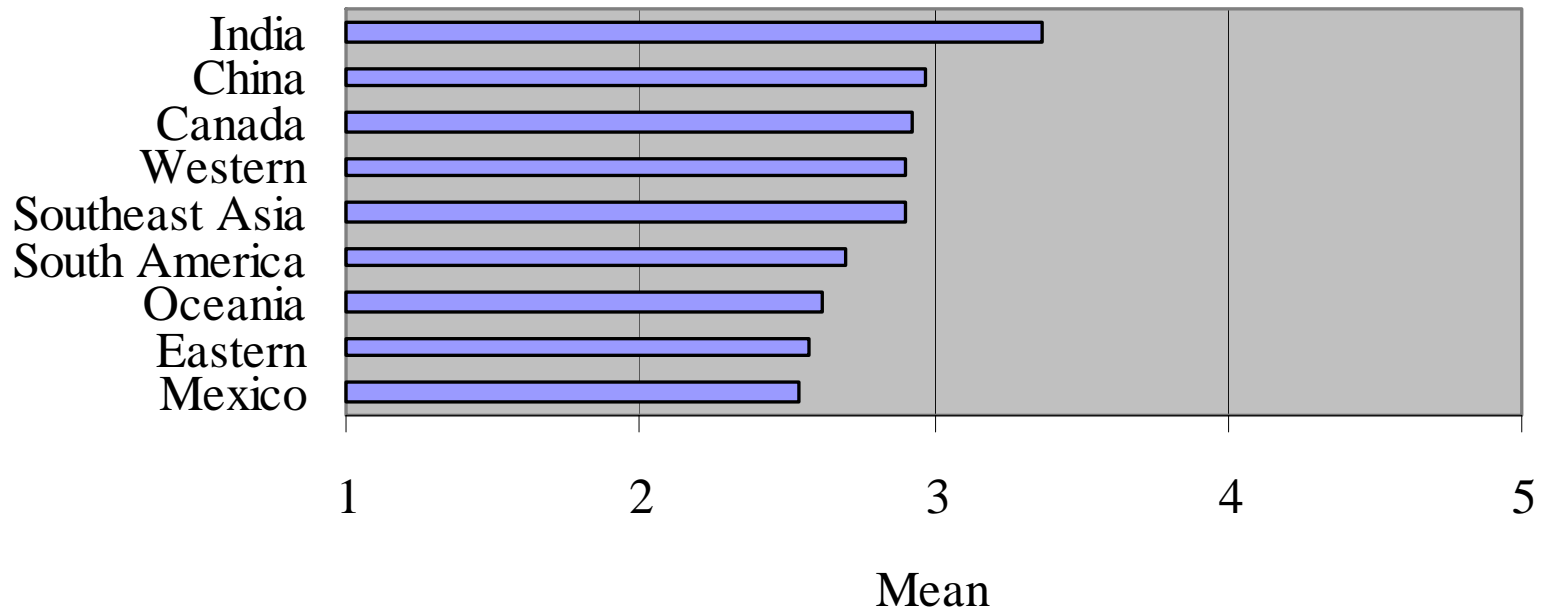
Contract Length- Services

	Increased	Decreased	No Change
Onshore	45%	20%	35%
Offshore	30%	7%	64%

Frequency of Negotiations- Services

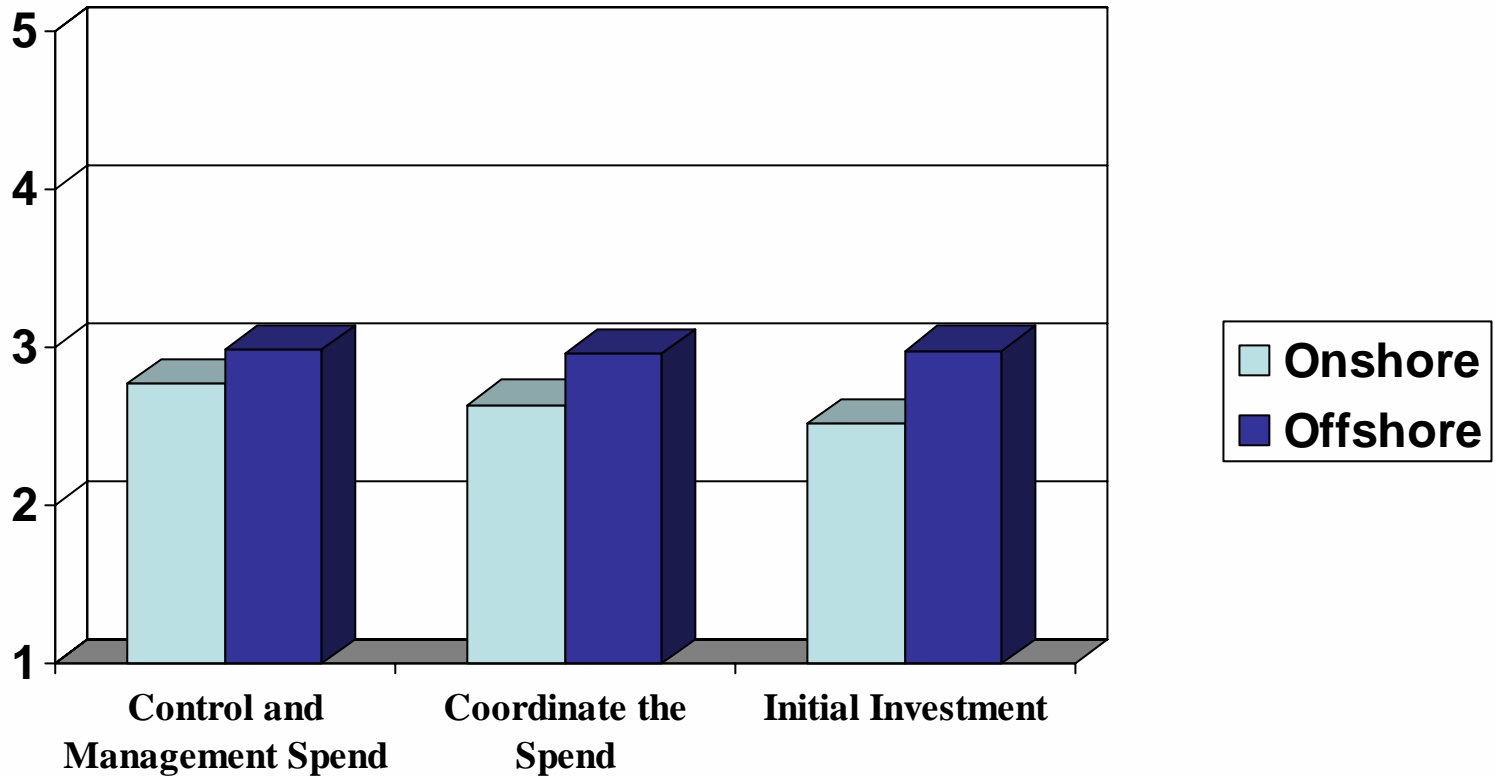
	Increased	Decreased	No Change
Onshore	55%	19%	26%
Offshore	34%	10%	56%

Location for Offshore Service Spend



5=most spend; 1=least spend

Level of Investment Required for Onshore vs. Offshore Service Providers



1=Low; 5=High

Glossary of Terms

- **Business Process Outsourcing:** To turn the management of a business process (transportation, IT help desk, call center) over to a third party with minimal intervention in day-to-day management
- **B2B:** Business to Business
- **Centralized:** The authority and responsibility for most purchasing and purchasing-related functions are assigned to a central organization.
- **Customer call center:** A service center with telephone, interactive voice response, and web-based capabilities to handle customer service, product support, telemarketing and other.
- **Decentralized:** The authority and responsibility for most purchasing and purchasing-related functions are dispersed throughout the organization.
- **Direct Materials:** Materials that can be identified with individual units of output. Costs are usually treated as variable and do not include general overhead or common cost allocations.
- **ERP:** Enterprise Requirements (Resource) Planning
- **Firm-Fixed Price:** A contract that provides for a price that is not subject to any adjustment on the basis of the supplier's cost experience in performing the contract.

Glossary of Term (Continued)

- **Hybrid:** Centralized sourcing with decentralized execution.
- **Incentives for Innovation:** Rewards paid to suppliers for innovation, ideas or value engineering which improves the performance of the buying firm.
- **Indirect Materials:** Materials that are not directly identified with specific products but related to the normal operations of an organization. Also referred to as overhead, indirect costs are composed of fixed costs, variable costs, and semi-variable costs.
- **Milestone Deliverables:** Requires that specific level of effort activities be completed by a prescribed date, or that supplier (s) prepare and deliver to the buyer documentation that reports on the current status of ongoing projects or activities. The requirements for providing milestone deliverables are generally spelled out in the contract document.
- **Offshore Services:** Total spend for services from a non-affiliated company located outside the buying firm's country of origin.
- **Onshore Services:** Total spend for services from a non-affiliated company located within the buying firm's country of origin.
- **Outsourced:** A version of the make-or-buy decision in which an organization elects to purchase an item that previously was made or a service that was performed in-house.

Glossary of Terms (Cont.)

- **Out Tasking:** To hire a third party to assist with services activities, yet the company still retains the management and control of day-to-day activities. Hiring a company to supply security guards, but having an internal employee supervise and direct their activities is example of out tasking.
- **Purchase/Supply Management Spend:** Total institutional spend for all goods and services purchased from suppliers during the reporting period.
- **Purchasing/Supply Management:** An organizational concept whose primary objective is to integrate and manage the sourcing, flow, and control of materials using a total systems perspective across multiple functions and multiple tiers of suppliers.
- **Risk/Reward:** Supplier fee is increased or decreased based on performance levels for certain contractual obligations.
- **Service Level Agreement (SLA):** Contract Agreements developed for a buyer's specified expectations. The buyer and supplier pre-determine which services and performance levels will be provided over a period of time. SLA's identify the services that will be provided and requires the supplier to meet specified target service levels.
- **Services:** Useful labor that does not produce a tangible commodity.
- **Services spend:** The total spend for services from a non-affiliated company that is neither goods nor capital.

Glossary of Terms (Cont.)

- **Time and Materials:** Type of contract that provides for acquiring suppliers or services on the basis of (1) direct labor hours at specified fixed hourly rates that include wages, overhead, general and administrative expenses, and profit; and (2) materials at cost, including, if appropriate, material handling costs as part of material costs.
- **Volume of Service:** Generally embedded in service level agreements (SLA) and related contracts, the volume of service refers to the predetermined services that will be provided over a specified period of time. Volume of service agreements may be more project oriented, wherein the buyer can specify the number of temporary workers needed to satisfy the needs of the project. The scope of work and level of services are usually structured for periods of 1 year or longer.