

**A survey of suppliers and paper company purchasing executives reveals that major cost reductions are possible with continuous improvement-based, gain-sharing agreements**

## Incentivized Buyer and Supplier Alliances Drive Continuous Supply Chain Improvement

By STEVEN J. TRECHA

The realities of the pulp and paper industry are tight market conditions, shrinking margins, and the continued need to drive real operations productivity and overall profitability. This scenario presents the perfect opportunity for collaboration between paper companies and their suppliers.

According to a pulp and paper buyer/seller collaborative survey conducted earlier this year by Integrated Strategies, buyers and sellers agree that there exists an additional 4% to more than 15% price/cost reduction potential across the supply chain, equating to millions of dollars annually for each firm involved. In fact, the preponderance of the respondents believes the percentages are double-digit, even with today's e-enabled bidding mania and alliance-prone business environment.

MORE THAN JUST PURCHASING. A pulp and paper company's purchasing, materials management, and logistics network makes up more than 70% of its operating revenue. Tie in the asset reliability factors (maintenance planning, preventive maintenance, and predictive maintenance) in mill and plant operations, and it becomes clear that the effectiveness of the overall supply chain determines the operating cost basis and asset reliability. Fundamentally, all firms must scurry to become low-cost producers and more effectively utilize their assets in this situation.

Too frequently, forest products companies have defined the supply chain simply as "purchasing" and total cost as simply "price." Success is usually measured as lowest price paid instead of total cost of ownership. Traditional practices are renamed and called "best practices." For example, competitive bidding is now "e-enabled" and longer-term blanket orders are now masked as "alliances." The satisfaction from both the

buyer's and seller's perspective is dismal.

"The industry continues to ride the same tired horse," notes Jim Byrd, former purchasing director for Georgia-Pacific Corp., referring to the practice of aggressively bidding one supplier against the next. This approach severely limits achieving a truly sustainable competitive advantage. In reality, the pulp and paper supply base has shrunk significantly, product offerings are diminished, and full customer service is now a luxury. Supplier margins have been so aggressively reduced, while buyers' demands have spiked, that suppliers are much more judicious in terms of which companies they will supply with products and which ones they will service effectively.

All firms chant the mantra of the supply chain. In fact, most purchasing organizations are now referred to as sourcing, blanket orders are referred to as alliances, and sales representatives are carded as alliance managers. Material prices are searched for on the Internet, and each purchase requirement is referred to as an "event." Now, suppliers' awards are "lotting strategy," and simple data analysts are replaced as "market makers." In the meantime, plant managers are still trying to drive productivity, and the quest for profitability has become more intense. What has changed, and more importantly, what needs to?

CAPTURING SUPPLY CHAIN POTENTIAL. There are earnest efforts to drive true supply chain integration and effectiveness, yet the realities of the business are often daunting and overwhelm the significant improvement potential that exists. What are these advantages and what do they look like? In short, they are double-digit percentage price and cost reductions, as well as asset reliability

improvements. They are two pronged benefits in truly advancing supply chain potential that come in terms of short-term measurable pricing and customer service improvements, as well as long-term total cost reduction and plant asset reliability advancements. Most have focused on short-term product pricing since it is easiest and measurable.

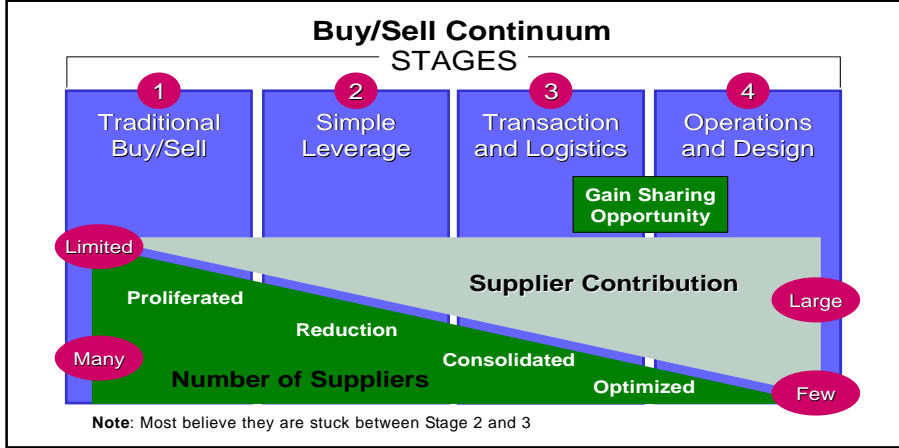
Beyond price, measured improvements can be achieved in product development cycles, customer responsiveness, inventory investments, logistics networks, and planned asset reliability. Most pulp and paper companies have captured improvements in each of these areas, yet studies have shown that firms have achieved only 40 to 70% of what is actually available. This leaves another 30 to 60% of available improvements.

More reality intrudes as roles and responsibilities across the organization continue to be redefined and shifted. In effect, we are simply changing the riders on the same dead horse. Supply chain advancement is often impeded by other competing initiatives, including enterprise resource planning systems, and the day-to-day emergencies created by customer demands and shifting production schedules. In the meantime, pushback from key users continues, while demands from senior management to deliver more and faster also continue.

Most firms have instituted cross-functional teams to drive cost reduction performance, yet based on the buyer/seller collaborative survey, more than 80% of the respondents stated that cross-functional teams are not achieving their goals. What most firms have in place today is insufficient to capture the full supply chain improvement potential that exists.

Cross-functional teams were the panacea of the 1980s and 1990s. The concept and objectives are sound, but the cross-functional infrastructure and recognition of the individual beliefs of

FIGURE 1: Focused collaboration drives value.



team members are lacking. As an example, Integrated Strategies has researched the teaming process, surveying team members about their beliefs concerning their team’s probability for success. At the inception of the team, it was found that only 30% of team members actually believed their team would be successful in achieving its goals. A 100% belief only occurs if implementation is complete and positive results have been achieved.

Teams typically represent the best, most knowledgeable talent within the organization. If they start out with an expected success rate at only 30%, what about the rest of the company, the supply base, and the customer base? The

reality is that their belief level is even lower. Will these statistics be changed as teams are launched in the future? Absolutely not. What can change is the understanding of these statistics and the building of frameworks and systematic and aggressive approaches that can bring faster success. This is particularly critical in advancing supply chain strategy development.

DEVELOPING SUPPLY CHAIN STRATEGY. Supply chain strategy is heavily determined by the type of buyer and seller relationship in place. Integrated Strategies’ buy/sell continuum identifies four stages of the relationship. As firms

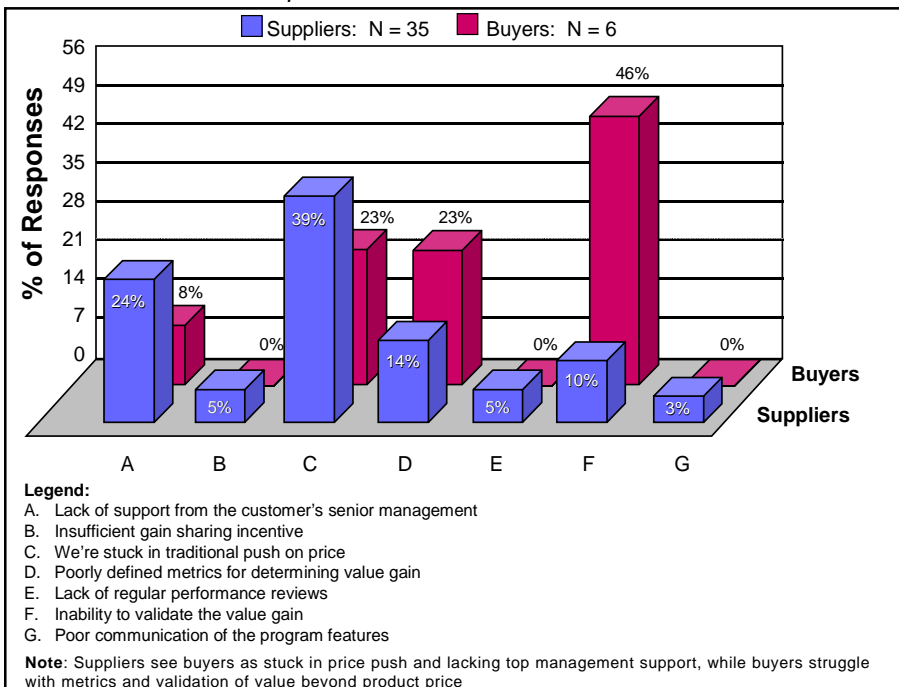
move along the continuum, supplier contribution becomes greater and the number of suppliers becomes fewer. The focus is on extracting and leveraging value from both the buyer and supplier perspective (Figure 1).

Stage 1 of the buy/sell continuum is the traditional buy and sell relationship. This bid and buy approach is predicated upon one-off purchase orders and competitive pricing. Standard lead times and conventional purchase order terms and conditions are the norm. Quite simply, there is a high degree of uncertainty, and both buyers and sellers understand their business relationship is one purchase order long. Both have developed backup contingencies to ensure success over time, but these contingencies cost money.

The second stage of the buy/sell continuum is simple purchase volume leverage to achieve a low price. This fundamental buying strategy is predicated on leveraging purchase volumes across time and multiple locations. In general, there are no commitments made by the buying organization. The seller, on the other hand, is expected to make commitments in a number of areas, such as special delivery schedules or reserved inventories, but these behaviors drive up costs. Simple leverage most accurately represents what is taking place in the e-procurement arena today. This is merely a throwback to fundamental competitive bidding and volume leveraging.

The transition and logistics stage is next. Here, the buyer and seller have reviewed multiple inventory and logistical options. Planning information and materials release programs are designed earlier on in the supply chain process. Inventory assets are co-managed. As appropriate, e-catalogs and supply chain transactions are automated to relieve the transactional cost and burden associated with the business processes. However, the key here is that the transaction automation is put in place based on mutual buyer and supplier technology leverage. This scenario avoids the situation where the buying organization simply mandates that suppliers move to a particular exchange or technology to satisfy that specific buyer’s need. Buyers explore what suppliers’ technology capabilities are and attempt to leverage them versus trying to force high-cost solutions into the supply base.

FIGURE 2: What are the impediments to collaboration?



Stage 4 of the continuum represents the most advanced, integrated stage—the operations and design integration stage. Suppliers are integrally involved in product and engineering design. They are also closely aligned with the production and/or maintenance planning of the buying organization, and the focus is on maximizing suppliers' technology capabilities and production capacities. The buy/sell relationship is fully defined with specific accountabilities assigned at the technology, operations, contract management, and overall continuous improvement level.

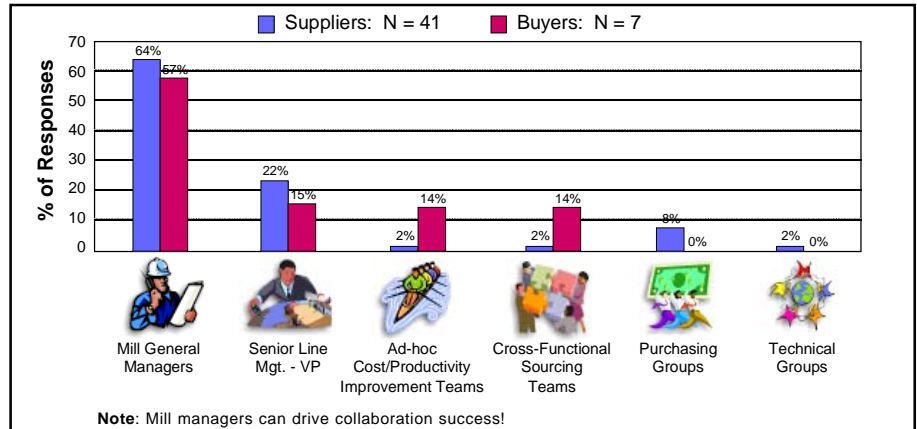
In Stage 4, continuous improvement programs are defined across all dimensions of the supply chain with goals supported by tasks, timing, resource requirements, and deliverables. Individual buyer and seller personnel accountabilities are documented and even contracted for. E-commerce technology is pervasive across the planning, catalog, ordering, acknowledgement, delivery, receipt, inventory, payment, and performance loop. Measurable lowest total lifecycle cost reduction is the target for both the buying and selling organization. Also, gain sharing is introduced and effectively managed for multiple years.

The Integrated Strategies' pulp and paper buyer/seller collaborative survey identified that additional cost reductions existed as a result of incentivizing collaborative relationships. Specifically, 14 purchasing executives and 58 supplier sales executives were asked what percent of their total purchases are in strategic alliance agreements. Alliances were defined as containing written continuous improvement programs, performance metrics, and time-phase goals that are actively managed.

Surprisingly, 71% of the buying organizations responded that less than 10% of their purchases are made under continuous improvement-based agreements. Similarly, suppliers indicated that the vast majority of their agreements were not under continuous improvement-based relationships. Participants agreed that the pulp and paper buy/sell relationships are firmly entrenched between Stage 2 and Stage 3 of the buy/sell continuum.

What are the impediments? Suppliers in the collaborative survey believe the industry is stuck in the traditional push on price and that top management

FIGURE 3: Who can make collaboration work?



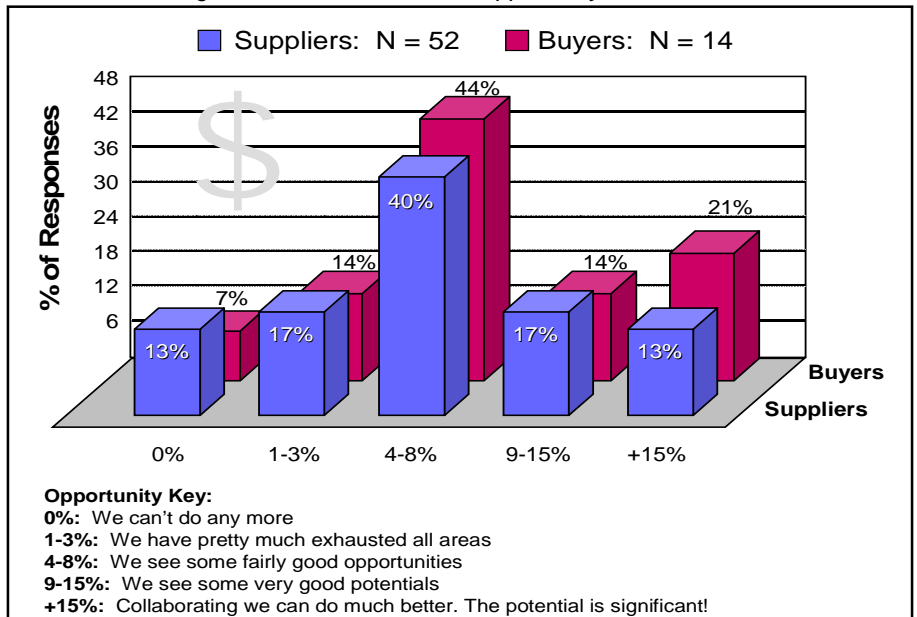
at paper companies has limited support for approaches that consider total cost instead of price alone. The majority of buyers believe the inability to validate the potential cost savings and lack of fundamental total cost measures continue to add to the predominantly price-focused mentality (Figure 2).

MILL MANAGERS DRIVE IMPROVEMENTS. So, who is best positioned to drive continuous improvement in the industry? Both buyers and sellers in the collaborative survey agree that it is the mill general managers who will determine the success of these programs (Figure 3). The question is how to most effectively transform from an operationally focused buyer and seller relationship to one that is fully integrated, tapping all the value available across the supply chain. This

type of insight and education must be designed and integrated within cross-functional teams and key selected suppliers who, in a collaborative manner, will work with mill management and create the vision for further supply chain contribution.

Individual approaches by either purchasing or by suppliers as they communicate with mill management are insufficient to drive the significant need for change that exists within the industry today. In effect, if collaboration is to be successful, mill managers must instigate and bring the benefits to reality at the mill level. Traditional top-down, corporate-driven purchasing initiatives have brought mill-level value, but primarily at the pricing level. Continuous improvement programs that drive real, sustainable results at the mill level must be

FIGURE 4: On average, an +8% cost reduction opportunity is still available.



instigated and executed there.

So, what are the roles of senior management and corporate procurement, as well as supply chain and supplier sales groups? These groups can bring forward the resources, training processes, analytical ability, and business insight that are needed to assist mill cross-functional teams in developing and advancing collaborative supply chain improvement programs. They can integrate collaborative best practices from mill to mill. The ability to leverage process, time, and talent from a buyer and supplier perspective should be coordinated company-wide and systematically applied at the local level, ensuring mill and mill manager success.

INCENTIVIZING COLLABORATION. Similarly, when the buyer/seller collaborative survey asked about the top attributes that make continuous improvement agreements work, buyers and sellers pointed to the operating management and senior leadership of the organization. Following close behind as top attributes of performance listed by respondents are planning, solid communications programs,

and conducting regular continuous improvement status reviews. The survey found that most firms have simply not considered or do not understand the potential of gain-sharing agreements as part of a supplier continuous improvement initiative.

Now, back to the reality. Incentivizing collaboration brings cost advantages and immunity from the tough bidding war competition. More than one-third of the buyers and suppliers surveyed believe that by entering into a collaborative gain-sharing type of agreement, an additional double-digit percentage price/cost reduction savings could be achieved from their supply chains. Further, the average respondent believed there is at least an 8% price/cost reduction available (Figure 4), which can mean millions of dollars. All of these available reductions are based on significantly changing the way buyers and sellers operate and on shifting from the traditional "beating of the dead horse" price path to invigorating a new breed based on total lowest cost.

What's needed? A systematic and aggressive means of establishing the opportunity and focusing business unit

and mill general management on significant opportunities associated with gain-sharing agreements. Suppliers and buyers will need to select relationships that are predicated on long-term, lowest total cost success and expect them to operate in a systematic, aggressively aligned approach. Total cost metrics must be established, tied to both buyer and seller performance with the expectation that reductions will be shared between organizations.

Suppliers are looking for longer-term commitments and the opportunity to deliver more and better service for their buying customers. Buyers are looking for certainty and performance across the supply chain. The reality is that buyers' and sellers' goals are aligned. It is planning and execution that stands in the way of collaborative success and immunity, and this is a real business reality.

*Steven J. Trecha is president and CEO of Integrated Strategies Inc., Okemos, Mich.*

*This article reprinted with permission from Pulp & Paper Magazine*



Success is the only option!



## Taking Concept to Reality in Your Supply Chain The Integrated Strategies Difference

Integrated Strategies excels in delivering sustainable advances in supply chain, sourcing, and materials management at the strategic, tactical, and operational levels. More importantly, Integrated Strategies works through the deployment and implementation phase, providing the knowledge transfer and skills necessary to ensure clients achieve bottom-line results and sustainable supply chain improvements.

We've developed more than 250 supply chain and logistics strategies across multiple industries and numerous commodities. If you are searching for competitive advantage, call Integrated Strategies at 517-381-4800 x219.



[www.sourcing.com](http://www.sourcing.com)

Success is  
the only  
option!



# Qualifications

- Consultants average more than 20 years experience
- Web-Based strategic sourcing tools
- “Concept to Reality” approach
- Hands-on implementation
- Worked with more than 200 firms across multiple industries
- Developed more than 250 supply chain and logistics strategies
- Integrate core supply chain with core business strategy

Supply Chain

Strategic  
Sourcing

Logistics

Materials  
Management

Order  
Fulfillment

Six-Sigma

Initiative  
Management

Integrated  
**STRATEGIES**

I N C O R P O R A T E D

Strategy Center  
5000 Marsh Road, Suite 1  
Okemos, Michigan 48864  
517-381-4800 • (Fax) 517-381-4807



MICHIGAN QUALITY COUNCIL  
Quality Leadership  
Navigator Recognition

[www.sourcing.com](http://www.sourcing.com)