Abstract: Many procurement professionals are looking for ideas for and approaches to developing a good supplier scorecard or improve their current scorecards. The challenge is developing supplier performance metrics that are meaningful to your organization and lead to action. Performance metrics should give insights that help you avoid risk, reduce costs and help your suppliers improve their performance. Developing metrics is one part of a supplier performance management business process. There are several steps for developing meaningful metrics including: 1) defining goals and strategies; 2) developing an evaluation strategy; 3) determining what to measure; 4) defining KPIs (key performance indicators) and scorecards.

Defining Goals and Strategies. Many procurement departments create scorecards in a vacuum, without first thinking about the big picture; that is, what are their companies overall goals, objectives and strategies and how does procurement align with those goals? Before choosing appropriate supplier performance metrics and KPIs, you have to start the process from the beginning. Just about every aspect of supplier management can be influenced by corporate goals and strategies. Therefore, procurement should actively support them. If procurement is out of synch with corporate goals and strategies, it may be working at cross purposes with the rest of the company and not adding its full value. Senior management may give a supplier evaluation initiative less support and resources if it cannot see the link to overall goals. Procurement should try to ensure that the suppliers it chooses to develop relationships with are aligned with procurement’s goals and ultimately the corporation’s goals. This linkage to corporate goals may not be self-evident to senior management and require active communications throughout the supplier evaluation process, particularly in the areas of results and return on investment, in order to gain and maintain management support.

For example, if the customer firm is trying to be more responsive in getting orders to customers, then procurement should be looking beyond price at purchasing lead times and supplier cycle times. Ideally, corporate objectives should be flowed down to the operational level. Procurement objectives and strategies can be based upon them and ultimately supplier performance expectations can flow from procurement objectives.

Developing an Evaluation Strategy. To create a supplier evaluation strategy, you need to determine which suppliers you want to measure. In most companies, resource constraints make it unrealistic to measure all suppliers, and there is little reason to do so. Therefore, the supply base should be segmented or characterized for purposes of supplier evaluation.

Segmentation means categorizing suppliers for the purposes of allocating the appropriate resources to manage and monitor them. For the purpose of understanding and evaluating supplier performance, segmentation will help uncover the key types of information about
different categories of suppliers that should be measured, if possible. However, just because your firm decides that certain types of information are important to gather, it doesn’t mean that the information will be readily available or easy to collect.

In segmenting the supply base for the purposes of performance evaluation, important considerations are typically risk, spends and switching costs. How much risk of supply interruption is associated with certain categories of suppliers and how high is the impact of supply interruption on your own firm? Another way to segment is by level of spend. The assumption is that suppliers with whom spend is high require the most attention. In other cases, spend can be low with certain strategic suppliers, but the impact of supply interruption is still high. The concept of switching costs looks at how much it costs in both money and resources to switch sources. Many segmentation matrices have been developed, but no one matrix applies to any organization. They can stimulate discussion and analysis, but cannot provide answers.

Once you segment the supply base and figure out which types of suppliers are important to measure, the next step in developing an evaluation strategy involves determining:

- The types of information desired
- How the information is going to be used
- Availability and ease of obtaining the desired performance information
- Resources required to gather the information
- The most effective evaluation methods to use (i.e., questionnaires, site visits, scorecards and so forth)

**Determining What to Measure.** Knowing which suppliers you wish to measure and the types of information that are important is the first step. Next you will need to define supplier performance expectations so that you can figure out how to tell whether and to what extent supplier are meeting your requirements. Performance expectations should be:

- Attainable
- Measurable
- Appropriate to the supplier being measured
- Communicated
- Actionable

While performance expectations should be derived from and aligned with your company’s goals and strategies, they can come from other sources. For example, in many companies, the business drivers of cost, quality, time and technology can be used a starting point for developing performance expectations. Or refer to the Balanced Scorecard categories of financial performance, internal operations, innovation and learning, and customer satisfaction.

**Define KPIs and Scorecards.** After supplier performance expectations have been defined, the actual KPIs can be defined and developed. Metrics should be meaningful, valuable, relevant, and actionable. KPIs should be a balance between leading and lagging indicators. Leading indicators are predictive, while lagging indicators tell more about what has happened in the past. Risk avoidance, for example, requires the use of leading indicators. You need to
develop metrics and evaluation approaches that help you and your suppliers determine the root causes of performance problems and trends so that performance improvement opportunities can be uncovered and addressed.

While it is very common to look to other firms to see what they are measuring and borrow those metrics, measurements should be relevant and useful to your organization – and readily accessible to gather. Measurements bolted on from other companies may not be aligned with your firm’s goals and objectives. Also, start small and expand. Too many metrics are unmanageable, not actionable, and often meaningless. Do not fall into the trap of collecting data, but not using it or acting on it.

REFERENCES:

Web reference:
Balanced Scorecard: www.balancedscorecard.biz

Book reference: