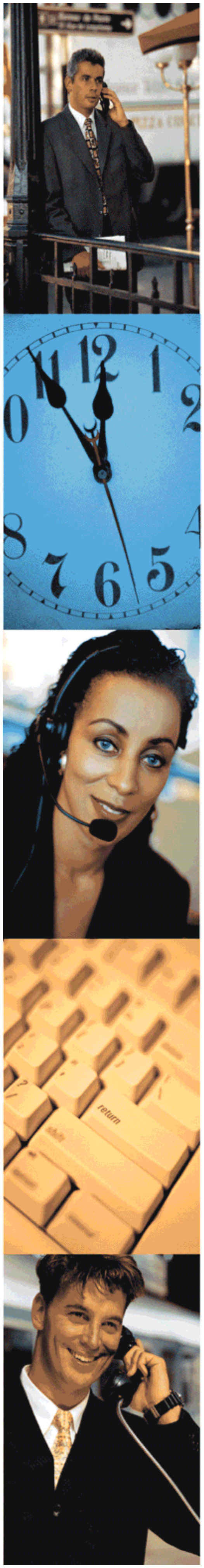
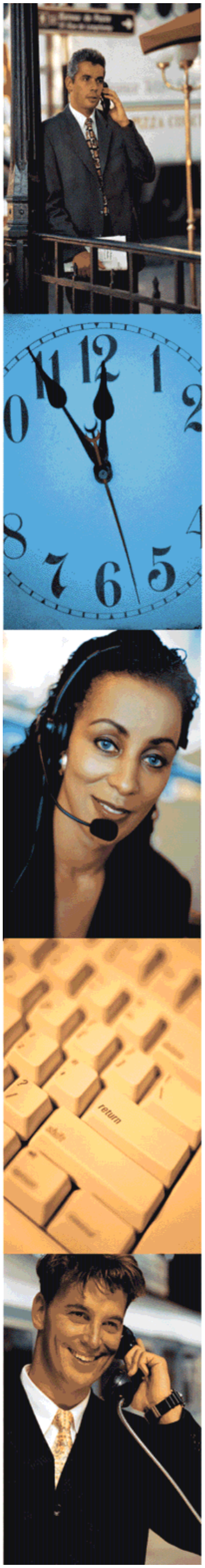


A Logistics Perspective: Being a Preferred Supplier

A guide to help you become and stay a preferred supplier to your customers

By Craig Thompson
Associate
Customer Centricity, Inc.

www.customercentricity.biz



A Logistics Perspective: Being a Preferred Supplier

Achieving *preferred supplier* status is one of the best strategies for ensuring a long-term relationship with your key customers. In this whitepaper, ***A Logistics Perspective***, we will: 1) explore the role and meaning of being a Preferred Supplier, 2) identify the attributes common in preferred suppliers, 3) share some successful methods to gain (and maintain) that status, and 4) provide helpful tips and insights as well as reveal some pitfalls to avoid.

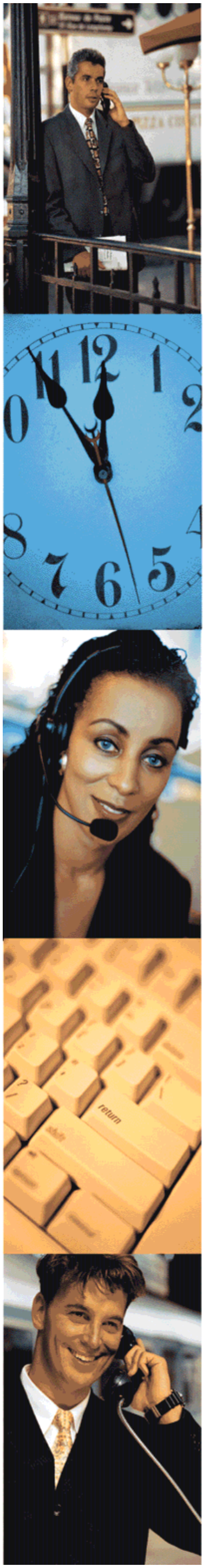
Being your customer's preferred supplier means that your enterprise is perceived to provide services of higher value to that customer than the corresponding services of your competitors. In this regard, preferred supplier status goes beyond product and price to comprise the set of activities that define "doing business with you." Typically, these activities include fulfillment, order management, billing and collection, claims and returns, sales and communications, special services, and adherence to the customer's instructions and requirements and the total cost of doing business. Collectively, these determine what is required to do business with you.

Beyond the activities themselves, it is the manner in which they occur that will make the difference. More than just the "whats", it is the "hows" that will form the basis of your customer's perception of your performance and shape his evaluation of you as a service provider. Above all else, a preferred supplier is seen as one that is **easy** to do business with!

So, what are the characteristics of a supplier that is easy to do business with? Since we are all customers ourselves, we can think of those suppliers (to us) that we like, frequent, and often rely upon. With a specific example in mind, it is a straightforward process to identify those things that differentiate our preferred suppliers. Let's take the case of transportation to and from the airport (being a "road warrior" this is a category close to my heart). There is a variety of products (and prices) available at all major airports: buses, taxis, courtesy vans, rental cars, personal cars, "public" limousines, "private" limousines, etc. In my case, I frequently travel long distances and arrive home at late hours. A high level of comfort and service is important to me at these times and I usually choose a private limousine service. There are several limousine companies I could choose from and I have tried many of them. It didn't take long, however, for me to identify one in particular that I preferred doing business with.

How did I single out a preferred supplier? I had found that all of the companies offered similar services, but one in particular provided something else. Airplanes often arrive late and, sometimes, flights are cancelled. At other times, I find I must change my flight at the last minute. With most of the limousine services I used, I found they couldn't (or wouldn't) make the necessary adjustments to accommodate my last minute schedule revisions and I would drag my weary bones to the long taxi lines and ride home in a clearly inferior level of comfort. However, one supplier was always able to adjust to my circumstances. Even though in more extreme circumstances there might be a price increase, the fact that I could count on them being there was clearly a greater value to me. I perceived their services as being clearly superior – they were, therefore, providing greater value. They were my *preferred supplier* and I would use them all the time, just in case I would have a last-minute schedule change.

In logistics terms, we would identify the differentiating characteristics of the preferred limo service in terms of responsiveness and flexibility. These are, in fact, two of the attributes defined by the Supply Chain Council that shape logistics performance. There are several others and they all will be reviewed in the following section.



Characteristics of Preferred Suppliers

When you consider what it takes to be a preferred supplier, the first thing to realize is that this distinction awarded by the customer based upon his *perception* of the value added to his business by the service you provide. This carries some implications:

- The perception of the supplier's actual service can be distorted, even wrong, because of a lack of accurate performance data, a mismatch between the actual service received and the service desired.

- Preferred suppliers are perceived to add value to the customer's business. The least objectionable supplier (the best of a bad lot) will not achieve this status although it is conceivable that a lot of unfavorable characteristics can be outweighed by a single virtue.

- The awarding of preferred supplier status can be significantly influenced by other tangible or intangible factors which may differ across competing suppliers and which may carry varying degrees of relevance. The lack of uniformity or "fairness" introduces a human element to the competition.

We said earlier that customers view preferred suppliers as being easy to do business with. The word "easy" pretty well matches the implications described above. So, if you add this all up, what can you conclude about preferred suppliers' characteristics that you can put to good use? Try this:

Suppliers are easy to do business with when they do a good job supplying, when they minimize the work and cost involved in supply, when they operate as a partner in the total supply chain and when they communicate to ensure accurate information and common understanding.

The Supply Chain Council identifies 5 attributes that comprise supply chain performance:

1. <u>Reliability</u> – This is the ability of a supplier to deliver the right product, in the right quantity, to the right place, at the right time, in the right condition and packaging and with the right documentation to the right customer. The key metric is Perfect Order Fulfillment and the supplier's additional burden is to correctly understand what is 'right'.

2. <u>Responsiveness</u> – How quickly products are provided to customers measured as Order Fulfillment Lead Time.

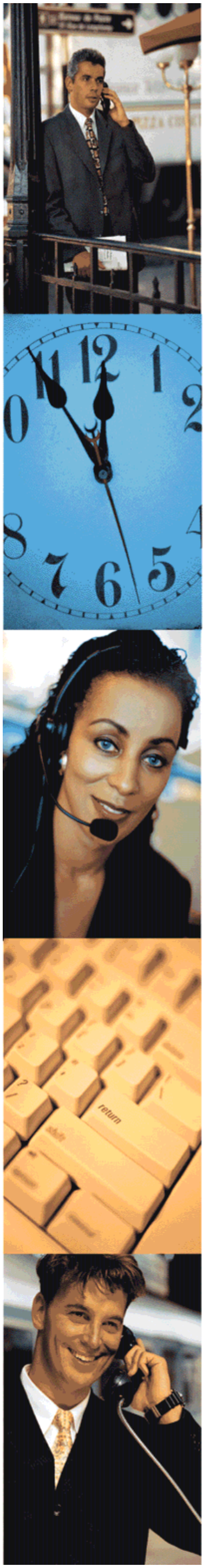
3. <u>Flexibility</u> – How adaptive a supplier is to changed circumstances that render existing capabilities incapable of meeting customer requirements (e.g., plant strike, warehouse fire, new governmental regulations, etc.). Quickness is the measure.

4. <u>Cost</u> – All supply chain costs need to be considered, cost shifting does not equal cost reduction. Total cost is the best measure; individual enterprise cost, although easier to obtain and more commonly measured, can be misleading and, worse, poison perception.

5. <u>Capital Asset Management</u> – How effectively total supply chain assets are managed and employed in satisfying demand. Return on assets, cash-to-cash cycle time and inventory days of supply are key measures.

Each of these attributes can be measured at several levels of process detail and, being consistently defined, enable benchmarking. This makes it possible to determine not only if a supplier is doing a good job supplying but also if they are doing a better job than their competitors.

So, being a good supplier is a key to being a preferred supplier and being a good partner can



provide the added tangible and intangible value that tips the balance toward preferred supplier status.

Becoming – and Remaining – a Preferred Supplier

We have talked about Preferred Suppliers as those perceived by their customer as being easy to do business with and who provide higher service value than their competitors. We looked at some characteristics typically shared by preferred suppliers; specifically that they do a good job, minimize the effort and cost of supply, and act as good partners conscientiously ensuring effective communications and common understandings. We also acknowledged that these considerations involve humans, ensuring a certain potential of irrationality compounding the "quirkiness" normally associated with perception.

From the logistics perspective, it's safe to conclude that becoming and remaining a better performing supplier than your competitors is one of the higher-percentage roads to preferred supplier status. Another advantage of this approach is that it is the least susceptible to falling in and out of favor with the customer. The trickier part lies in knowing when you are better (so you can work on making your customer see that you are) or, inversely, when you're not and why (so you know what to fix). In this section, we present four suggested strategies for becoming, and remaining, a preferred supplier.

Strategy 1 – Talk to Your Customer

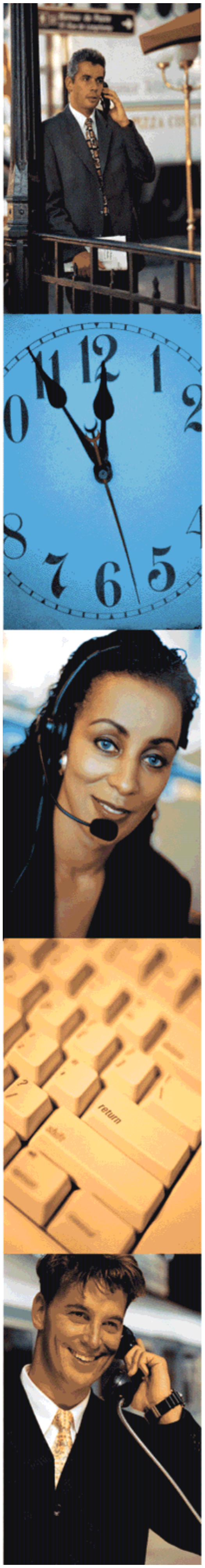
A good place to start is usually your customer, who probably knows what supplier actions are valued and can fill you in on his perception of how well or badly you're doing. A note of caution: Be sure the review is thorough and that it covers all aspects of your supply performance. Avoid getting bogged down in anecdotes of specific problem areas, further eroding perception. Be prepared that your customer, quite naturally, wants to dwell on your relative weaknesses rather than extol your virtues.

It's a good idea to take along a checklist, one that you used in preparing for this review by filling in your side of the form with the facts as you know them along with your expectation of your customer's views. The checklist needs to include your metrics for the various service goals you prioritize, other measures that may be utilized by your customer, and business review information including volume growth, special requests that were met, order management and other systems improvements, etc. When you have finished the meeting, document the results to all parties present and quickly follow up on any points of disagreement and misaligned data. Get back to everyone with clarifications and corrections. This will put both you and your customer are on the same page and ensure you understand where problems and issues lie and that your customer is aware of your strengths.

Where problems and issues are identified, it is important to devise solutions and create action plans identifying how and when they will be achieved. These need not (and maybe should not) be decided at the meeting, but they must be timely in their preparation, in their communication back to the customer and in their enaction to demonstrate responsiveness and the strong desire to service your customer well.

Strategy 2 – Talk to Your Partners

Collaboration is a way an enterprise corresponds with its supply chain partners. As an ideal, it depicts a relationship in which partners jointly devise better plans by sharing information and decision-making. In practice it can mean as little as the willingness of trading partners to exchange little more than requirements and fulfillment commitments so as to increase long-term supply and demand planning horizons. Whichever view is yours, it points in the right direction. Unfortunately, as a buzz word, collaboration is advertised as a relationship that is just between you and your customer.



Restricting its application to just that channel also restricts the range of benefits that are available. To readers of this newsletter, the advantages of the broader view are obvious.

We have all heard the expression that "companies don't compete, supply chains do." That may be an extreme view, but I have seen the 2nd half of the expression bear out numerous times; namely, that "supply chains compete." As a long-time user and proponent of outsourcing, I have repeatedly enjoyed the luxury of having another company help me solve my problems and extend my capabilities. This is particularly relevant to striving for performance improvement when that company has additional expertise and the wherewithal to apply it. There are a lot of supply considerations and it can be very expensive to be great at all of them. If you chose your service providers well, they are experts in their field and they also want to be your preferred supplier.

Strategy 3 – Audit Your Supply Chain

When you consider the major business processes involved in supply (characterized by some as Plan-to-Position, Purchase-to-Pay, and Order-to-Cash) it's important to know that, despite the particular way your company is organized and operates, these processes already exist. They are common to you and your competitors and link to the corresponding processes of your customers and your suppliers. What's at issue is how well they are designed, managed and executed and what other factors may be present that facilitate or impede performance. The purpose of the audit is to address these issues.

Thankfully, there are various tools available to accomplish the audit. In addition to the templates and analytical process decomposition techniques that improve visibility into an enterprise's actual detail processes there are compendia of "Best Practices" that depict what they should be and how they should link that include descriptions of corresponding inputs, outputs and enabling factors. On top of this, they also identify appropriate performance metrics. All of this provides numerous opportunities for consultants like me to analyze "as-is" supply operations and create road maps for a "to-be" state that efficiently and effectively embraces best practices and increases customer delivery value.

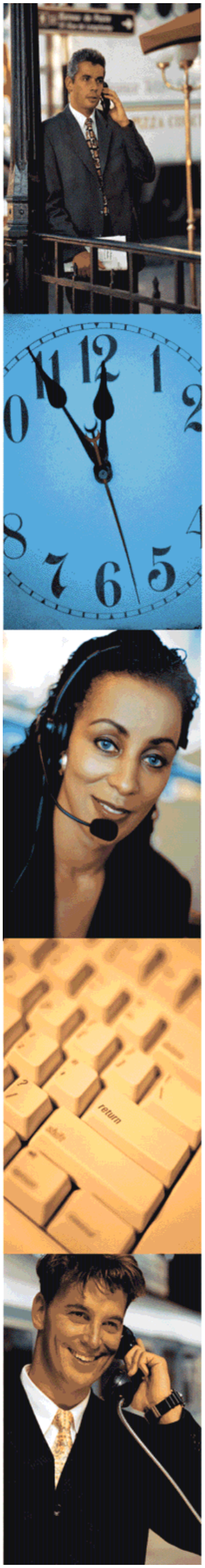
Advantages of this strategy include greater objectivity, a clearer focus on strengths and weaknesses, and a comprehensive view of your supply processes. Additionally, I have always found the analytical exercises themselves to be tremendously valuable as an education for the process owners. They invariably emerge more as knowledgeable and effective implementers and managers of the "to-be's".

Another nice feature in this approach is the ability to meaningfully benchmark your firm's performance with others since with best practices you measure consistently designed processes with common metrics. With some external support you can know how your operation stacks up to your competition and where your relative strengths and weaknesses lie.

Strategy 4 – Work with Your Customer

We talked in the previous installment about talking to your customer to identify his supply-related priorities and the perceived strengths and weaknesses in your company's performance as they relate to them (Strategy 1). Now let's take a look at some of the improvement opportunities that open up when you consider changing the whole supply equation. There are a growing variety of methodologies that deliver direct, measurable benefits that are readily identifiable by all involved parties, including your customer. Some of the better known are vendor-managed inventory, scan-based trading and rapid replenishment. Others are process improvements that enable, rather than deliver, benefits. This type includes CPFR and rapid/accelerated planning.

These are just a few examples and they all deserve a separate article in this newsletter just to describe how they are applied to increase supply value. Whether the measurable benefits lie in cost



reduction or sales increases or both, the key is the value is linked to a tighter relationship between your company and your customer.

To summarize, there are several approaches to improving your customer's perception of your service. Not surprisingly, better communications lies at the heart of most.

Common Pitfalls in Pursuing Preferred Supplier Strategies

Implementing a preferred supplier strategy is not without some potential hazards, if it is not properly thought out. In this final section, we enumerate the concerns, risks and pitfalls that often haunt programs designed and implemented to achieve (and remain) preferred supplier status. We will review these in four main categories: Goal, Customer, Capability, and Realization.

Goal

Probably the best first step in committing an enterprise to achieving preferred supplier status is having a **great reason**. Ideally, every action of an enterprise is taken in order to realize value – increased volume, margin, reduced cost, etc. Due to its nature, becoming a preferred supplier should provide *strategic* value. I stress this for several reasons: managing a program that differentiates cost and service deliverables to a single customer can be difficult, requires the specific commitment of new and/or scarce resources and builds and relies on the motivation of the rank and file.

Strategic value delivers capabilities for increased long-term profitability, whether through volume or margin growth. Becoming a preferred supplier in order to 'hitch your wagon to a star", increase the net new customer growth rate, achieve lower cost operating capabilities are examples of great reasons. The idea of having one is to provide the common focus of both your organization and your customer to ensure the necessary and appropriate level of commitment to the gain-sharing that will cement the long-term relationship.

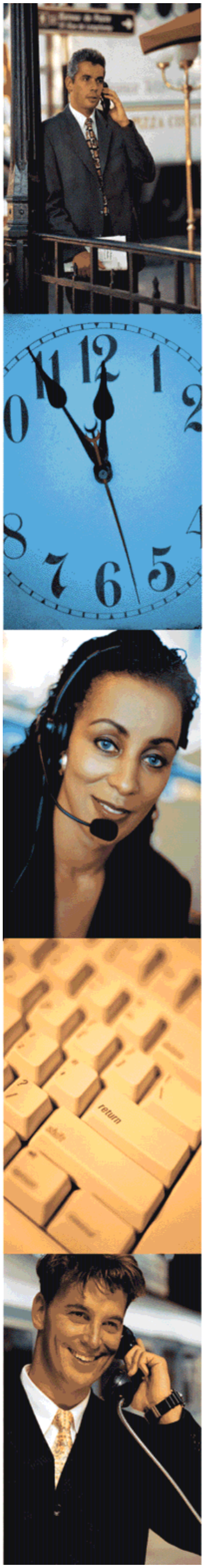
Customer

The choice of which customer you are targeting isn't always up to you. Circumstances are always conspiring to create opportunities. Organizations that are responsive and flexible are positioned to recognize and seize those opportunities that offer strategic value. If these circumstances were created by a particular customer, their selection is probably intertwined with the opportunity itself.

One of the most successful programs I witnessed (and was involved in) was driven by a retailer incurring erratic order completeness from several manufacturers in a particular category. This was especially problematic during advertised specials. Our firm had a solid order delivery track record and the customer gradually began to rely on us to back-stop these events at the last minute. Not only did we realize spot volume gains but this preferred status (in one category) was leverageable to other products – especially advantageous as this retailer quickly grew to become the largest in the world!

In cases where you identify in advance how you will achieve preferred supplier status and then set about identifying the target customer, you have added one huge hurdle – motivating the customer to appreciate/reward (however subliminally) your actions so as to help create the targeted strategic value. Be sure the customer you choose is able to capture the value your program will offer. By the way, would this customer have picked you? Are you already recognized as being a solid supplier? Are you *easy to do business with*?

The true value realized from preferred supplier status isn't the overt recognition or 'pat on the back' or Supplier of the Month Award of your customer. Rather, it lies in the net value received. In fact,



customers who anoint suppliers as 'preferred' sometimes do so with no other increase in net value realized or even intended.

Sometimes the customer's stated desires, if fulfilled, won't necessarily increase overall value at all. This is usually the case when the customer is merely shifting costs back to the supplier. Maybe you, the supplier, can create overall value from this desire (e.g., increasing total inventory productivity through VMI) but, if not, comply with the desire knowing that it won't make you a preferred supplier, just a lower cost one (temporarily).

Capability

Probably the most common pitfall encountered is that of finding out your enterprise can't reliably and efficiently perform in accordance to the commitment. Whether due to the desperation or naiveté behind the original commitment or the lack of know-how, enablement or motivation of the enterprise, the fact is that all the right people weren't involved at the beginning.

One consumer hard goods manufacturer I worked with had identified a preferred supplier strategy it hoped would be the catalyst they thought they needed to raise overall delivery performance. At another, the goal was to restore brand prestige by "getting on the wall/shelf" of a highly regarded retailer. Predictably, both programs failed, beset by erratic performance and negative net value received. Not only was preferred status not gained but the failure to deliver on the commitment resulted in setbacks in the supplier/customer relationships.

This isn't the place to learn "blocking and tackling". Those are prerequisites. The lesson here is to understand the characteristics of preferred suppliers, outlined earlier in this discussion. Possible supply chain partner roles can be settled at this time as well.

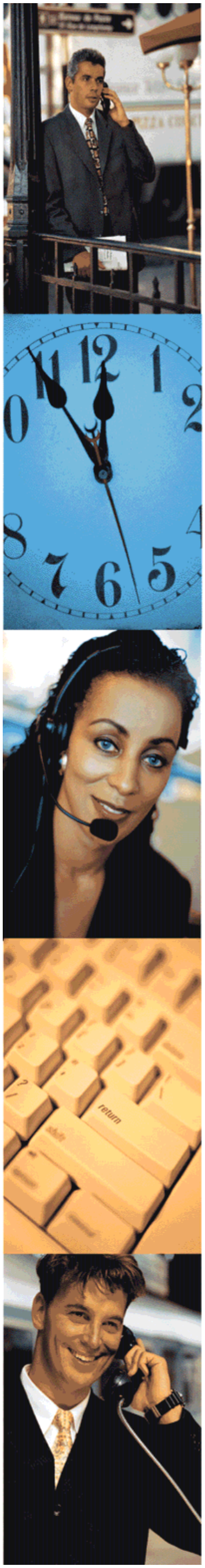
Once the enterprise has gained these attributes, however, it can renew its efforts to become a preferred supplier. At one of the firms identified above, subsequent to its regaining control of its operations and building performance credibility, a hugely successful 'instant-response' fill-in program was developed in conjunction with its largest retail customer and, once perfected, was rolled out across all channels.

Realization

This can be the most insidious trap of all. You have committed to a valuable customer, made the resource investments in people, capital and systems, and modified ongoing operations. But, after all this, is it paying off? Is your enterprise (along with your customer) enjoying the benefits originally targeted or are you just spending money and spinning your wheels? Have other benefits arisen that weren't specifically predicted? Have there been downsides that partially or wholly offset the gains? How do you know?

The original goal(s) should be quantified (or represented) by the use of performance measures (e.g., volume, margin). These metrics can then be computed and reported at intervals sufficient to determine actual achievement as well as how their value is trending. This is normal performance management.

There are potentially big gaps in this *normal* approach to performance management. One leading beverage manufacturer I advised was caught in this trap – all the meters on the dashboard were reading favorable but the car ground to a halt. What was wrong was that something was missing – *everything else*! In other words, they weren't also keeping an eye on those other metrics - those not specifically associated with the preferred supplier program yet that were fundamental to the normal business.



Was a Value Assurance Program in effect? Did the actions required by the preferred supplier commitment impair performance elsewhere ultimately increasing overall costs, reducing total net margin, etc? Did the Program Manager have overall visibility? Was a balanced scorecard being maintained? Were problems recognized and root causes identified?

Conclusion

In conclusion, we all know that customers can be wonderful things. Their care and feeding dominate our enterprise activities. Their 'favors' are our stuff of life. Yet, they can also be fickle gold-diggers - expensive to acquire, hold and lose. Being one of their preferred suppliers is one successful strategy in keeping the shared value-producing relationship alive and positive. In addition to product and pricing, it can be a prominent lever in managing and preserving the relationship and in increasing your long term competitiveness. I hope that this whitepaper gave you an appreciation of this approach along with a better sense of how to become a preferred supplier and keeping the program on a value track. If you would like more information on this or other logistics topics, please contact us.

More About Customer Centricity, Inc.

Customer Centricity, Inc., is a business consulting firm that works with companies to align their resources to exceed customer expectations in the most efficient and effective manner possible. We leverage our real-world experience to help our clients continuously improve their service delivery and management capabilities to:

- Increase profitability
- Improve customer satisfaction and retention
- Increase operational efficiencies
- Improve employee satisfaction

Customer Centricity optimizes the interaction between people, process and technology in several ways:

- Comprehensive assessment methodology to identify the actions that will yield our clients the greatest return
- Skills Training to enable customer-facing personnel to deliver exceptional levels of customer service
- Design and Implementation of business processes to serve the customer and manage corporate resources in efficient, effective and consistent manners
- Identification of the appropriate business processes to automate, enabling companies to get the most from their investments in technology

Customer Centricity's approach is to work closely with our clients to help them understand what they are doing right, and their opportunities for improvement. We provide pragmatic recommendations that provide immediate benefits, and we drive continuous improvement programs help our clients realize significant return on investment in a very short period of time (measured in weeks, not months or years).

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