

## Supplier Evaluation: Benefits, Barriers and Best Practices

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### 91<sup>st</sup> Annual International Supply Management Conference, May 2006

**Abstract:** Measuring the performance of suppliers is vital to ensuring a well-functioning supply chain. This session will feature how to measure the performance of your suppliers and increase your visibility into their operations. We will discuss the business case for supplier evaluation, what should you measure, approaches to assessment, and how to get from performance measurement to performance improvement.

From a lean enterprise view of supply management, the supply chain is full of waste and hidden cost drivers. And from a global perspective, supply management is fraught with risks as companies deal with increasing numbers of offshore suppliers. Measuring and understanding supplier performance is critical to ensure a well-functioning supply chain and to a company's competitive position. Improving the performance of key suppliers is the goal.

Companies who evaluate their suppliers find that they have better visibility into supplier performance, uncover and remove hidden cost drivers, reduce risk, increase competitive advantage by reducing order cycle times and inventory, gain insight on how to best leverage their supply base, and align practices between themselves and their suppliers. Companies pursuing supplier assessment commonly see over a 20% improvement in supplier performance metrics (e.g., on-time delivery, quality, and cost).

Evaluating suppliers can be challenging, costly, inefficient, and inconsistent. From an analytics perspective, many approaches are inadequate and unable to provide the insight needed to drive better decision making and performance improvement. They tend to provide after-the-fact results rather than identifying root causes of performance issues, without which, improvements are difficult to drive. Understanding supplier performance can both prevent problems and facilitate performance improvement.

This objective of this session is to discuss the advantages and challenges of various approaches to supplier performance measurement such as how to:

- Recognize and uncover hidden cost drivers in the customer-supplier relationship
- Make the business case for supplier evaluation
- Determine approaches and metrics
- Understand the merits and shortcomings of various approaches (i.e., is ISO certification adequate? Are quantitative metrics from your enterprise system sufficient?)
- Understand where automation can scale and support your processes
- Identify actionable supplier opportunities for improvement
- Close the loop and get results

## WHY MEASURE SUPPLIER PERFORMANCE: THE BUSINESS CASE

**1. Increase performance visibility.** When companies do not know the facts about how their suppliers are performing, supplier management tends to be based on guesses. Moreover, the simple act of measuring performance can help improve performance. This improvement can be even more dramatic when companies award additional business on the basis of suppliers meeting performance goals.

**2. Uncover and remove hidden waste and cost drivers in the supply chain.** The supply chain is full of inefficiencies. Some of these inefficiencies can be improved by better communications between customers and suppliers. Others are a result of poor business practices at the supplier that can result in increased inventory, quality problems, higher costs, and slow deliveries. Companies can reduce wasteful costs and activities, typically caused by supplier glitches, such as: additional inspections, extra freight charges, overtime (to catch up), safety stocks, obsolete inventory, buying from multiple sources (which reduce price leveraging), etc. Time is money, and by measuring and improving supplier performance and by reducing supplier quality problems, for example, a company eliminates wasteful steps in its own processes. By better understanding supplier performance and supplier business practices and processes, customers can help suppliers drive waste and inefficiency out of the business, resulting in higher-quality suppliers and lower costs.

**3. Leverage the supply base.** By measuring supplier performance, an enterprise can set a threshold for its suppliers that can lead to higher-quality results. Companies can better plan new products and services based on a good understanding of its suppliers' capabilities and performance levels. Understanding local suppliers can help determine if they are capable of reducing total costs enough to outperform offshore suppliers. Also, suppliers can provide technologies to their customers that help them develop new products and services that can add revenue to the customer's bottom line and enhance their competitive position, thus helping customers add value to the top line in addition to removing cost from the bottom line.

**4. Align customer and supplier business practices.** Ideally, suppliers should run their business in alignment with their customers: share the same business ethics, expect similar standards of excellence, show commitment to continuous improvement, etc. Consider how the lean enterprise or any high performance system that drives shorter delivery times, higher quality, and lower prices could actually have an adverse impact on a supplier who is not aligned with these practices. A supplier who is unaccustomed to pursuing continuous improvement may be unable to keep up with its customers' increasing requirements for better, cheaper, faster goods and services.

**5. Mitigate risk.** Insight into supplier performance and business practices helps reduce business risk, particularly given companies' increasing dependence on its key suppliers. Risks can be financial and operational and increase with geographic distance. Or, a risk area of increasing concern is the performance of sub-tier suppliers whom the prime supplier has no contact with or knowledge of.

**6. Improve supplier performance.** The goal of supplier evaluation should be supplier performance improvement. While simply measuring performance has a positive effect, supplier evaluation can be most effective when it leads to continuous improvement activities

and actual supplier performance improvement. Supplier evaluation systems need to address both the traditional quantitative indicators such as quality, delivery, and cost management as well as the underlying qualitative factors. The root causes of performance difficulties can be hard to uncover and require understanding business practices, cultural factors and the leadership at the supplier. Follow-up activities, such as supplier training and development, and corrective actions to address supplier evaluation findings are the best ways to obtain measurable and positive results.

**APPROACHES TO EVALUATING SUPPLIERS:**

Approach	Barriers/Challenges
Questionnaires	<ul style="list-style-type: none"> <li>• Requires knowledge of what to measure</li> <li>• Hard to construct sound survey instruments</li> <li>• Difficult to deploy</li> <li>• Relevance of results</li> <li>• Not always actionable</li> <li>• Supplier compliance issues</li> </ul>
Scorecards	<ul style="list-style-type: none"> <li>• Data integrity</li> <li>• Requires resources for cleansing, massaging, formatting</li> <li>• Disputes with suppliers over data integrity</li> <li>• Not clearly actionable</li> <li>• Do not identify root cause</li> </ul>
Site visits	<ul style="list-style-type: none"> <li>• Resource intensive</li> <li>• Requires trained personnel</li> <li>• Site visit instrument &amp; expertise</li> <li>• Can be inconsistent</li> <li>• Hard to scale the process</li> </ul>
Third-party standards certification such as: ISO 9001:2000, ISO/TS 16949:2002, QS9001	<ul style="list-style-type: none"> <li>• Does not guarantee best practices</li> <li>• Focus on documenting procedures</li> <li>• Not specific to customer requirements</li> </ul>
Supplier evaluation software	<ul style="list-style-type: none"> <li>• Involves funds outlay</li> <li>• Resistance to change</li> </ul>

**CONCLUSION**

Developing a robust, easy-to-deploy method of evaluating suppliers is a critical business competency. The methodology should be sound and the approach practical. Gathering data for the sake of data will not produce the return on investment in supplier evaluation. Most importantly, companies need to use the results as a means to foster communications and a starting point for supplier development and performance improvement. This, in turn, will help companies reap the financial and competitive rewards of high performing key suppliers.

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