STRATEGIC SOURCING AND THE IMPACT ON SMALL BUSINESS OPPORTUNITY

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What is Strategic Sourcing?

### STRATEGIC SOURCING DEFINITION

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<tr>
<th>DEFINITION OF STRATEGIC SOURCING</th>
<th>Strategic sourcing is a structured, analytical and collaborative process for optimizing an organization's supply base while reducing Total Cost of Ownership and improving mission delivery</th>
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| SUPPORTING DETAILS | Strategic Sourcing is:  
• A **process** for systematically analyzing and developing optimal strategies for buying goods and services.  
• A **data-driven, fact-based** analysis to drive decision making rather than just "hunches"  
• A **holistic** process that addresses customer needs, market conditions, organizational goals and objectives, and other environmental factors  
• Based on **market intelligence**, and takes into account **small business** capabilities  
• Based on a **cross-functional approach** that involves multiple parts of an organization  
• About supporting an **organization's mission** through procured goods and services |
| COMMON MISCONCEPTIONS | Strategic sourcing is **not**:  
• Leveraged buying  
• Bundling  
• A pre-conceived answer |
The benefits of strategic sourcing are numerous and go far beyond pricing improvements and leveraged buying.

### Primary Benefits of Strategic Sourcing

<table>
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<tr>
<th><strong>Reduction in Cost Per Unit</strong></th>
<th><strong>Change in Consumption/Volume</strong></th>
<th><strong>Improved Operating Efficiency</strong></th>
<th><strong>Improved Supply Management</strong></th>
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<td><strong>Pricing Improvements</strong></td>
<td></td>
<td><strong>Reduced Procurement-Related Operating Expense</strong></td>
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<tr>
<td>• Lower unit price</td>
<td>Demand Management</td>
<td>• PO processing</td>
<td>Socio-economic Goals</td>
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<td>• Volume rebates</td>
<td>• Manage consumption</td>
<td>• Accounts Payable</td>
<td>• Structured analysis of small/disadvantaged business opportunities</td>
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<td>• Payment term discounts</td>
<td>• Encourage substitution</td>
<td>• Receipt/Warehousing</td>
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<td><strong>Supply Chain Savings</strong></td>
<td>• Change product mix</td>
<td><strong>Standardized procurement process</strong></td>
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<tr>
<td>• Cost of capital</td>
<td>Specification Review</td>
<td><strong>Reduced Non-Procurement Related Operating Expense</strong></td>
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<tr>
<td>• Warehousing costs</td>
<td>• Eliminate “gold-plating”</td>
<td>• Other operating efficiencies</td>
<td><strong>Optimized Supplier Relationships</strong></td>
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<tr>
<td>• Shipping costs</td>
<td>• Simplify specifications</td>
<td></td>
<td>• Improved joint understanding of needs and capabilities</td>
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<td><strong>Reduced Lifecycle Costs</strong></td>
<td>• Alternative products</td>
<td><strong>Performance Monitoring</strong></td>
<td>• Increased efficiencies across the entire supply chain</td>
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<td>• Maintenance costs</td>
<td></td>
<td>• Structured metrics and periodic review of contractor performance</td>
<td></td>
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<td>• Operating costs</td>
<td></td>
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<td>• Disposition costs</td>
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Over the past 20 years, commercial firms have successfully implemented Strategic Sourcing programs to generate significant savings and efficiencies.

Strategic Sourcing has emerged as the standard best practice for private sector firms. Below are three examples of successful commercial Strategic Sourcing initiatives:

**Fortune 100 Manufacturer Uses Strategic Sourcing to Manage Supply Risk and Cost**

- Facing an increasingly volatile supply market and inflationary environment for metals, this manufacturer needed to ensure continuity of supply while managing costs.

- Utilizing Strategic Sourcing analytical techniques to analyze the metals supply chain and benchmark various pricing and hedging strategies, the company shifted its sourcing to suppliers further back in the supply chain to “lock in” the supply of metals.

**Fortune 100 Information Technology Company Streamlines Worldwide Sourcing**

- In the past, this firm had more than 60 disconnected procurement organizations managing nearly 5,000 production suppliers around the world.

- Through implementation of Strategic Sourcing initiatives, the company saved $5 billion over five years. It consolidated approximately 85% of its $17 billion in production spend to 50 suppliers. And its e-procurement initiatives resulted in savings of $377 million.

**Fortune 500 High-Tech Manufacturer Focuses on Supplier Relationships for Best Value**

- The challenge for this high-tech manufacturer was to stabilize prices and ensure best value in a fast-changing and complex hardware components market.

- The firm implemented a Strategic Sourcing program to look at all components. For the most critical components, the company determined that shifting from quarterly contracts to long-term supplier relationships was the optimal strategy resulting in larger volumes for suppliers, better prices, and standard hardware component.
Strategic Sourcing has now been endorsed and is officially prescribed for use across all Federal agencies.

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<th>Federal Organization</th>
<th>Recent Activity and Guidance</th>
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<td>General Accountability Organization (GAO)</td>
<td>• Published reports recognizing the benefits of Spend Analysis and Strategic Sourcing as an Industry and Government Best Practice</td>
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<td>Office of Federal Procurement Policy at OMB (OMB/OFPP)</td>
<td>• Directive issued 5 May 2005 requires each Federal Agency and Department to:</td>
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<td>- Implement Strategic Sourcing</td>
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<td>- Identify commodities for strategic sourcing</td>
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<td>- Report annually to OFPP/OMB on progress</td>
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<td>Federal Chief Acquisition Officers Council (CAOC)</td>
<td>• Formed Strategic Sourcing Working Group (SSWG) to lead and guide Federal strategic sourcing initiatives</td>
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<td>Defense Procurement and Acquisition Policy office at OSD (OSD/DPAP)</td>
<td>• Currently establishing a DoD Strategic Sourcing Governance Structure and process</td>
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<td>• Sponsored study on best sourcing practices for acquiring IT services</td>
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The Federal Government has already begun to see the benefits of strategic sourcing

Federal Strategic Sourcing Successes

US Air Force

- Established the Air Force Information Technology Commodity Council to manage all IT commodity buys for the Air Force
- Established standard desktop PC configurations, continually updated as part of an 18-month planning cycle
- Council’s primary aim is to maximize the value of commercial IT product purchases by considering Total Cost of Ownership
  - Includes factors such as life cycle management costs, cost of support services, and procurement complexities
  - Since 2004, the council has bought 216,000 PCs at a reported savings of $61 million

US General Services Administration (GSA)

- Established a Federal Strategic Sourcing Initiative focused on leveraging spend across the Federal Government
- Launched five commodity teams focused on common spend items across the government
  - Wireless communications
  - Express document delivery services
  - Copiers
  - Printers
  - Office Supplies
- Contracts have been awarded on several commodities; awaiting validation of savings

US Postal Service

- Established commodity councils and conducts extensive price analysis:
  - Savings plus cost avoidance over last five years is approx $1.3 billion
  - Maintenance, repair, and operating supplies costs reduced:
    - Before: 75% local buys, multiple business arrangements, 1,000 suppliers
    - After: awarded two national contracts, standardized product selection, implemented e-buy, used reverse auctioning, saved $30 million in FY04
DoD has adopted a well-defined and structured process for strategic sourcing that is rooted in fact-based analysis.

**STRATEGIC SOURCING PROCESS – HIGH LEVEL OVERVIEW**

1. **Conduct Opportunity Analysis**
   - Assess and prioritize opportunities based on a department-wide spend analysis

2. **Profile Commodity**
   - Develop detailed profile of commodity including spend profile & specifications

3. **Conduct Supply Market Analysis**
   - Conduct market analysis to identify industry trends, supply & demand levers, potential new suppliers, negotiation levers, and available contract vehicles

4. **Develop Commodity Strategy**
   - Develop organization-wide commodity strategy based on Commodity Profile & Supply Market Analysis

5. **Develop & Implement Acquisition Strategy**
   - Develop and issue RFx based on sourcing strategy, hold negotiations, evaluate proposals, and award contract(s)

6. **Manage Sourcing Performance**
   - Implement contract, process and policy changes; continually measure, track and manage performance

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The term “Commodity” is used to refer to ALL acquired supplies or services, simple or complex.
<table>
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<th>Common Misconceptions</th>
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<tr>
<td><strong>Strategic Sourcing is exclusively about leveraging the government’s purchasing volume</strong></td>
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<tr>
<td><strong>Strategic Sourcing is only about bundling purchases with one supplier as a means of negotiating the lowest price</strong></td>
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<td><strong>Strategic sourcing favors big businesses that can deliver high volume</strong></td>
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<td><strong>Small businesses are going to get left out in the cold</strong></td>
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## The Reality

- **Strategic sourcing and small business sourcing are not mutually exclusive propositions**

- **When applied correctly, strategic sourcing can actually help agencies identify entire segments of industry where small business can deliver the best value**
## Small Business Advantages In Strategic Sourcing

- In areas where deep subject-matter expertise is needed, a small “niche” firm might offer more value.
- When speed is of the essence, a small firm might be more nimble and responsive.
- Small firms may offer more flexibility in customizing solutions and products.
- The lower overhead of a small business can translate to more competitive prices.
- Many of the most innovative and creative ideas originate in small entrepreneurial firms.
Strategic Sourcing: An Approach for Incorporating Small Business

**COMMODITY STRATEGIC SOURCING PROCESS**

1. Conduct Opportunity Assessment
   - Include specific small business goals as a design parameter for the overall strategic sourcing program

2. Profile Commodity
   - Define clear requirements to establish criteria for optimal source selection

3. Conduct Supply Market Analysis
   - Understand small business capabilities through rigorous market analysis

4. Develop Commodity Strategy
   - Align supplier capabilities with requirements to see full potential supplier pool

5. Develop & Implement Acquisition Strategy
   - Implement policy, process, and technology changes to ensure successful sourcing results

6. Manage Sourcing Performance
   - Select the most appropriate supplier(s)

7. Develop commodity strategy and revise small business goals as appropriate

8. Monitor supplier performance and overall sourcing performance against goals