

# SUPPLY MARKET INTELLIGENCE:



Think

Supply market intelligence (SMI) is a proven approach to reducing risk and gaining a competitive advantage. It begins with the collection and analysis of market data—but doesn't stop there. The leaders excel at engaging key stakeholders in the SMI process and then disseminating the information in a way that leads to better business decisions. It's a new way of thinking that can pay big benefits.



# Differently, Gain an Edge

By Robert Handfield

Facing increased uncertainty in economic markets, organizations are increasingly aware of the need to closely monitor market conditions and respond appropriately through improved supply chain strategies. As more organizations seek to build sourcing strategies that capture cost savings opportunities, they are finding major shortfalls in the market intelligence and cost modeling capabilities that form the basis for effective strategies and negotiation. Further, they are discovering that the needed integration of market intelligence into operational decisions, including budgets, profit objectives, market pricing, technology insights, and global expansion is generally not well executed.

The result is misalignment between demand and supply planning, and major gaps in operational performance and risk mitigation. To address this situation, organizations need to develop deep market intelligence that will provide insights into core elements of market trends, commodity pricing, global capacity, and government and regulatory changes that could have an impact on global sourcing. They also need insight into economic trends that will affect their organization's supply chain. Unfortunately, these capabilities seem to be lacking in most organizations, based on the results of a study we recently conducted among supply management executives. Our research

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is based on interviews with subject matter experts in a number of industries who have deployed or are in the process of deploying Centers of Excellence for supply market intelligence (SMI). In addition, we surveyed 89 global supply chain executives through the International Association of Commercial and Contract Management (IACCM). (See sidebar for more on the study sample.)

This article explores the concept of supply market intelligence. We describe how companies are structuring their supply management organizations to optimally collect market data, identify best practices for synthesizing and deploying this information, and establishing metrics for measuring outcomes of SMI. Further, we discuss how some leaders are now beginning to extend the application of SMI to other strategic business decisions that lie outside the realm of contracting and category analysis—an activity that is positively affecting decisions in annual budgeting, customer markets, technology integration, and financial budgeting. We believe that the innovative application of SMI to these areas, though still in a nascent stage, will enable many organizations to achieve superior market performance and outcomes.

## **What Is Supply Market Intelligence?**

One of the foundational themes underlying this research is that an effective SMI organization does much more than simply collect and analyze data. Truly successful SMI organizations excel at engaging stakeholders in defining knowledge requirements as well as disseminating information to ensure that it is effectively applied in key impacted business sectors across the organization.

Supply market intelligence can be defined as a process for creating competitive advantage and reducing risk through increased knowledge of supply market

dynamics and supply base composition. SMI includes:

- Global market intelligence—forecasting and market intelligence to assist sourcing professionals in making strategic decisions.
- Benchmarking—price and process benchmarking to assess sourcing performance.
- Global competitive sourcing—identification of strategic sourcing opportunities in global markets that will lead to cost reduction.
- Emerging market sales and channels—sourcing and purchasing initiatives to support expanding activities in emerging markets.

The process of creating intelligence involves the application of individual and collective cognitive methods to weigh data and test hypotheses within a secret socio-cultural context, according to Rob Johnston, Director of the Center for the Study of Intelligence. Johnston's observation, noted in our review of government intelligence services, recognizes that SMI is much more than a set of analytical tools. Specifically, sourcing executives need to realize that creating intelligence is inherently an unstructured process in that it requires the analyst to first interpret the user or stakeholder requirements before even beginning the process of data collection. Johnston notes that the importance of making explicit something that is not well described (which is the very interactive, dynamic, and social nature of intelligence analysis) is a fundamental component of creating an intelligence analysis capability.

In his book, *Analytic Culture in the U.S. Intelligence*

### Details on the Study

Our research involved detailed interviews with eight senior supply management executives in different industries who had developed Centers of Excellence for market intelligence. The industries represented spanned a wide variety of environments, including automotive, oil and gas, healthcare, manufacturing, retail, technology, and others. This diversity emphasizes the importance of SMI capability across a wide variety of contexts and environments.

Subsequent to the interview coding process, we developed a survey to identify the extent to which a larger sample of organizations were deploying best practices in establishing competitive MI processes. This survey was then administered to the International Association of Commercial and Contract Management (IACCM) membership, an organization of approximately 1,000 members who are either buy-side or sell-side contract managers. A response was obtained from 59 managers, a 5.9 percent response rate. Respondents consisted mainly of buy-side contracting entities, a handful of supply side contractors, and some respondents that managed both. The majority of respondents were from North America and Europe, with some Asian representatives.

*Community*, Johnston describes the typical intelligence analytic process, in the words of an analyst:

*"When a request comes in from a consumer to answer some question, the first thing I do is to read up on the analytic line. I check the previous publications and the data. Then I read through the question again and find where there are links to previous products. When I think I have an answer, I get together with my group and ask them what they think. We talk about it for a while and come to some consensus on its meaning and the best way to answer the consumer's question. I write it up, pass it around here, and send it out for review."*

The fact that there is a significant cognitive element of this basic description ("when I think I have an answer") suggests that asking the right question is an important component of the SMI process. In particular, there is a need to generate a hypothesis to drive the analysis and to gain consensus and do a final check. These are key elements that set the right direction and enable the stakeholder to proceed.

### Defining the Need for Market Intelligence

Organizations collect different types of data and intelligence. So what is unique about supply market intelligence? To answer this question, we first need to define exactly what kinds of information people require to render better sourcing decisions. Our analysis found that they most often want information on product and service market conditions for a particular sourcing requirement.

There are clearly a number of potential outputs from an SMI analysis. These typically center on commodity cost driver analyses and supplier monitoring to prevent major disruptions in supply. The former could focus on identifying both internal cost drivers (leverage, order volume, proximity, contract management) and external drivers (such as overall demand, raw material costs, investment in R&D). Another output is a PACE (Pressure Action Capability Enablers) framework that evaluates pressure points in the industry, actions taken by industry players, capabilities required to support actions taken, and business enablers to mitigate pressure points. Regional analysis of market share, growth rate, and projected revenue would fall in this output category as well.

Supplier monitoring outputs would include quantitative financial analysis—calculating financial ratios from income statements and balance sheets and comparing them with industry average numbers for public companies and checking for solvency of each supplier. It would also include

qualitative analysis such as capacity utilization, economic impact, job losses, and impacts of currency fluctuations. A SWOT analysis based on these internal and external risk factors are other important SMI outputs.

To a large extent, the need for market intelligence and development of these outputs needs to be formally scoped prior to actually executing the tasks. Our survey results suggest that in most cases, the primary consumers for this output are category managers, who are seeking to enter into a new sourcing event for a specific category (maintenance, copper, steel, and so forth) as part of an overall category strategy. In other cases, requests are for internal business requirements that require analysis of spend data, production levels, customer spending trends, market pricing, competitive actions, and other miscellaneous forms of data collection. As the financial risk in the supply base has increased, there is a growing demand for risk information and specific risk monitoring assessments.

Requests for SMI come in a variety of formats. Some occur as part of an annual budgeting process. Others are periodical, requiring some advance notification—for instance, a category team contacts an SMI group with a request for a sourcing event that will be occurring sometime in the future. Still others are short-term, ad hoc requests for “quick-hit” information that can provide a quick update on a specific issue or risk (“Is this supplier about to go under?”) SMI organizations need to be prepared for all forms of requests, and establish a process and realistic expectations as to their ability to turn around these requests. Best practice companies are in effect “getting ahead” of these requests, by establishing formal requirements for stakeholders to engage the team.

This characteristic of establishing stakeholder requirements is clearly the most important of the SMI attributes associated with the intelligence-gathering process. This is made all the more important because of the investment required to complete a full market intelligence report. Our research shows that the typical lead-time required for most SMI reports is 60-90 days at a minimum. Best-practice companies we studied can provide an overview (high level insights) in 10 days, or an in-depth analysis (detailed information leading to strategic recommendations) in 45 days. These companies are relying heavily on external sources for market intelligence data gathering and reporting, and have structured their groups to primarily facilitate and engage with stakeholders.

One common mistake we observed is organizations creating a centralized SMI team without considering what information will be gathered and how it will be

used. To cite one example, a senior commodity manager at a large oil and gas company expressed her frustration at information obtained from a team of MI analysts in Asia who were disconnected from the day-to-day activities of category managers dealing with decisions that required forward-looking perspectives. Essentially, the analysts were providing information on what was already known about a category.

### The ROI OF SMI

The supply management executives we interviewed repeatedly expressed their frustration with the process of justifying the quantifiable benefits of funding an SMI group. This has become especially challenging in the current economic environment in which just about every company in every industry is facing head count and budget cuts. Many CFOs are quick to cut funding for an SMI group, mainly because they don't recognize the tangible value that this function brings not just to sourcing cost savings, but also to corporate strategy, budgeting, market pricing, and competitive advantage. Best-in-class companies have dedicated SMI groups that are committed to full-time research and reporting of market indices, price inflation, cost economics, market trends, and other elements that feed into budget planning and marketing initiatives across the enterprise.

**There is a growing trend toward the use of external resources to conduct supply market intelligence.**



The frustration expressed by these executives who were seeing their teams reduced was, in fact, part of the motivation for this study. To delve more fully into the issue, we collected information on relative levels of funding committed to by different organizations. One of the relevant metrics is a simple measure of \$B of spend supported by SMI per analyst. The majority of companies we spoke with have a very small number of fully dedicated individuals assigned to SMI data collection and analysis. Instead, most organizations have individuals who are held accountable for conducting MI as part of their broader roles and responsibilities. In theory, these individuals might be expected to devote one-quarter or one-half of their time to SMI activities. In practice, however, their time is being consumed by other “fire fighting” activities—so that expected time allocation is misleading. In addition, many SMI team members are required to provide other forms of analytic support in

addition to external SMI, such as spend analytics, compliance information, and contract pricing and renewals.

In general, organizations interviewed said that they required one FTE for each \$1 billion to \$2.5 billion in spend. This estimate is somewhat misleading, however, as this also includes part-time SMI resources who have other duties as well. Again, one of our observations is that if SMI is a “part-time” activity, it often falls to the bottom of the priority list.

### Organizational Structures

A fundamental tension exists regarding the role and scope of an SMI organization. Strained financial budgets have drained sourcing organizations of the resources needed to conduct detailed external market research and cost models. Yet it is these very resources that are best able to develop critical insights into environmental shifts that can enable teams to fully leverage their sourcing capabilities and identify potential bottom-line savings.

Our best-in-class companies recognize that SMI is a differentiated activity that requires a dedicated cadre of individuals with specialized skills, supplemented by external MI resources that improve responsiveness to stakeholder needs. However, the survey respondents for the most part are equally split between those assigning MI to sourcing managers as part of their category management responsibility and those that have a developed centralized MI team. Others have assigned individuals to an SMI team but also given them business intelligence and analytics responsibilities with other parts of the organization. (See Exhibit 1.)

Category managers are at the center of the tension mentioned above. Many executives we spoke with expressed frustration with the way in which category manager roles are structured. They noted that these individuals were often being pulled in so many directions that it impeded their true understanding of the category. This, in turn, dictated the need for dedicated

internal and external market intelligence resources. Our research showed that many category managers do not have the experience or know-how to conduct the detailed research required to build an intelligence profile for a market. Reflecting this, several organizations are assigning analysts full time to category support. These individuals are performing the analytics and market research to support the category lead.

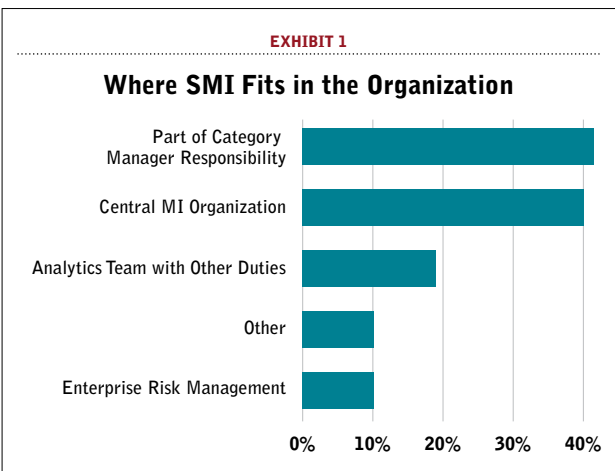
Some of our study participants asserted that MI should be driven into these managers’ roles through formal reviews, with the expectation being that they need to become experts within their category. This has important implications for how organizations need to structure talent and training for individuals in these roles. Finally, we observed that the leading companies with centralized SMI teams are leveraging external resources to gather external data, which we discuss below.

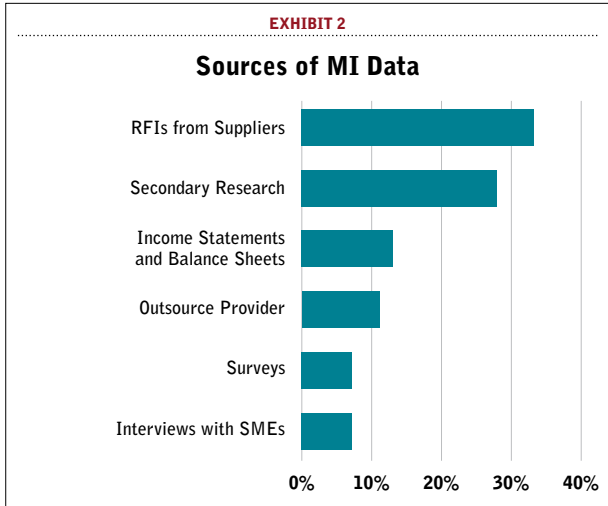
### The Role of Outsourcing in SMI

Organizations utilize a variety of data sources as input into MI reports for stakeholders. Suppliers are the most obvious data source, mainly via Requests for Information (RFI). RFIs can be structured in such a way to yield detailed cost estimation, competitive information, and other forms of data that can be triangulated across various suppliers to provide insight into market conditions. One caveat: RFIs are often biased and do not reflect true market conditions. To complement this information, therefore, companies often subscribe to secondary research such as trade journals, website, and third parties. The third major form of external information is income statements and financial balance sheets, provided through services such as D&B and Hoovers. A smaller set of companies are now relying on external information provided through third party outsourced MI providers such as Beroe and Spend Cube.

Finally, a minority of companies undertake detailed MI reports through focused interviews with subject matter experts. We believe this approach often provides the most in-depth contextual information and detailed “street knowledge” that is often key to making strategic sourcing decisions. The big challenge here is that few people have the access and time to track down and interview these valuable sources of information. (Exhibit 2 gives a breakdown of the various data sources used.)

There is a growing trend toward the use of external resources to conduct supply market intelligence. Research suggests that 65 percent of companies are using some form of external resources for SMI, and an increasing number of them are utilizing several parties. This is not surprising as companies increasingly recognize that triangulation of results from multiple parties



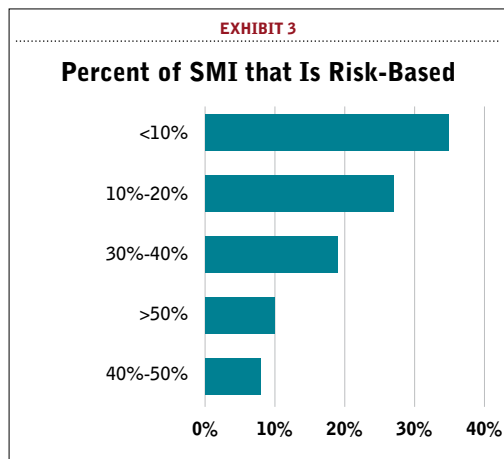


is essential to building solid market intelligence. When the same message comes from multiple parties, the probability of its veracity increases.

Our survey found that most companies have between one and four external full time equivalent (FTE) dedicated individuals as part of the MI team. In a few cases, these external team members are co-located on-site. They work closely with the internal team to better understand requirements and to more closely integrate with the business and its resources. This external presence still represents a relatively small portion of the overall MI budget; three-fourths of the respondents spend less than 20 percent of their MI budget on external resources. A handful of companies are heavily reliant on external sources of information, which we defined as spending more than 50 percent of the budget on outsourced providers.

**Risk Assessment**

Almost all of the companies interviewed noted that risk assessment was part of the output of the MI team, with external providers doing the bulk of the transaction risk assessment. In almost all cases, financial risk was the primary element tracked by MI teams. As shown in Exhibit 3, however, fully two thirds of the executives surveyed (the top two bars in the exhibit) said that their risk-based MI constituted less than 20 percent of the total market intelligence effort. So while supply risk is important, there are clearly other forms of MI that are also viewed as critical in this environment.



**Measuring the Outcomes**

The majority of respondents to our survey said that the main methods of assessing the outcomes of SMI are the traditional cost savings measures attributed to category teams. Yet, we believe that this is an unreliable and often short-term metric because it does not fully capture the value of SMI to the business. In many cases, effective SMI can be extended to better inform strategic decisions in production levels, capacity, outsourcing, technology initiatives, and growth and revenue-producing opportunities. Comparatively few companies, however, are applying SMI to create these types of opportunities. In many cases, the reason is that the SMI message is not being heard in the appropriate forums where these strategic decisions are being made.

To capture the full benefit of an SMI report, many companies conduct internal customer surveys after the report to evaluate how well the project served the client's needs. Internal customers could include lines of business or functional groups such as marketing, production, IT, or logistics. These surveys focus on internal customer feedback using scales as well as open-ended questions that provide a mechanism for evaluating how well the information met the internal customer's requirements. The results are evaluated to understand how well the SMI team performed and how the process could be improved. In many cases, internal customers' most important criteria is the speed of completing an SMI report. As such, the analyst needs to set expectations at the outset in terms of what can be delivered within the customer's expected time frame.

It is also important to conduct a thorough post-mortem of the process. As Rob Johnston of the Center for Study of Intelligence emphasized to the author in a 2009 interview, information distilled from the post-mortems need to be made available as "lessons learned" that can be filtered back through the organization.

One related observation regarding the knowledge transfer of SMI outcomes: The majority of organizations we spoke with do not effectively transfer SMI knowledge and information to parts of the organization that could strategically benefit from this information. This is a major shortcoming that was underscored by the frustration expressed in multiple interviews we conducted with market intelligence directors. Clearly, the opportunity for leveraging SMI into other parts of the business represents a significant and unexploited opportunity to achieve a

major competitive advantage. There remains a major gap in understanding how to transfer SMI into business decisions.

## Seven Insights for Advancement

In the course of our research, seven insights emerged on successful supply market intelligence. Companies that want to develop this competency—and realize the associated benefits—should carefully consider them.

1. *Organizations with successful SMI programs may not necessarily excel in data collection and analysis.* Rather, they succeed in developing a team of internal MI analysts who are proficient in defining knowledge requirements and disseminating information in a way that leads to better business decisions. Current research suggests that successful organizations are creating Centers of Excellence for MI, with analysts co-located in multiple business units globally and coordinated through centralized processes.

2. *The leaders increasingly recognize that category managers are often not well equipped to conduct MI analyses, mainly because of the demands on their time to perform other activities.* This justifies the need for a dedicated MI function. Further, the ROI on these individuals dictates that it does not make sense for them to be conducting routine market analyses. The executives interviewed believe that over time these individuals should become full-fledged experts in their category. Best-in-class companies are all focused on having their category leaders rely on an SMI Center of Excellence for coordinating data collection, analysis, synthesis, and insight as a core foundational component of sourcing strategy. Internal MI analysts are best equipped if they come from an engineering, financial, supply chain, or cost accounting background.

3. *There's a growing trend towards outsourcing of MI data collection, synthesis, analysis, and reporting.* Third parties are proving these services in such areas as global market analysis, benchmarking, inflation/deflationary pricing, value-chain mapping, global cost-reduction sourcing opportunities, and emerging markets. Implicit in this trend is that best-in-class companies recognize that MI is fundamentally about the application of individual and cognitive methods to weigh data and test hypotheses. As such, the primary role of an MI function is not to collect and process data. Rather, the goal is to fully understand internal client requirements, context, and the process of applying the information to business decisions.

4. *Best-in-class companies establish expectations to internal customers about what can and cannot be delivered through an SMI Center of Excellence.* The breadth and depth of data will determine the lead time required to create a specific report. Clear scope guidelines must be communicated to and acknowledged by the cli-

ent in the early stages of proposal development. This gives the internal customer an understanding of what can be produced within a given time horizon vis-a-vis the outputs required for that customer to make a business decision. For example, if an internal customer wants an in-depth analysis of a market in ten day's time, this is not feasible. However, a high-level overview of market characteristics may be possible within this time frame.

5. *The research points to the importance of conducting performance evaluations of SMI reports, and of tying these back into lessons learned that can be communicated to the organization.* Many companies seek to tie SMI investments to cost savings. In our opinion, this is difficult to do in a systematic way. While anecdotal data can point to cost savings achieved by applying SMI to specific projects, these are highly contextual and specific in nature. Instead, best-in-class companies are relying on a systematic evaluation of client feedback, focused on a long-term and strategic understanding of the importance of SMI to key enterprise-wide procurement metrics and value.

6. *Most organizations are not effectively linking SMI reports and insights into operational decision making.* In mature organizations, for example, cost models need to be aligned with savings projects and profit targets for corporate and business unit level budgeting processes. Our research identified several examples of how successful organizations are achieving this. The key is to have multiple communication channels—for example, through simple lunch-and-learn discussions that provide opportunities for face-to-face dialogue, discussion, Q&A, and debate.

7. *Finally, the majority of organizations do not have a good process for meaningful, ongoing monitoring of supply risk.* While many track the financial health of suppliers, they are not capturing other market-level information. Thus, they remain susceptible to intelligence failure because of the inherent nature of surprise associated with supply market incidents. Surprise is not attributable to omission or commission of information. Anticipating surprise, then, requires analysts who can think broadly about a problem expressed to them by an internal customer and who understand the business context of the potential risk. This may require “structured brainstorming”—thinking about the unthinkable—around potential risks that are not immediately apparent to the organization. ☺☺

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