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CONNECT

Ontario Institute of the Purchasing Management Association of Canada

Improving Cash
Conversion

Risky Business

Using technology to
build a better world



CONTENTS

Improving the Cash Conversion Cycle.....	2
SCM – What Lies Ahead	4
Risky Business – How to Protect Your Supply Chain ...	5
Supply Chain Finance	7
Utilizing Empathy.....	8
Freeing Up Cash.....	10
Leadership Perspective	12
New C.P.P. Graduates.....	13



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- Provide and protect the certification process in the province of Ontario
- Encourage the development of the membership through education, research, and standards of practice
- Promote and advance the supply chain management profession

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Supply chain management: “the new normal”?

In the wake of the significant downturn in the global economy, we are hearing a lot these days about “the new normal” in business and industry. There is a general belief that people and markets must alter the way they operate to adapt to a new economic reality.

Finance is one of the first areas where the term “new normal” has surfaced. Market observers are talking about a “new normal” for the investment world. Various assumptions that this sector has relied on for a number of years are likely to be replaced with new ones. The severe downturn is causing fundamental shifts in how the investment sphere operates.

So, is there a new normal for supply chain management?

Dan Gilmore, editor-in-chief of Supply Digest, observes that while supply chain management has always been characterized by rapid change and unpredictability, it does provide a stable means for companies to respond to the needs and wants of customers. Any “new normal” in supply chain management will be driven to a large extent by changes in customer expectations.

As noted in a recent article in the Harvard Business Review, we will see a multi-year trend toward a more conservative and value-oriented customer. This will have significant implications for supply chain management professionals. Gilmore believes that promotion in the supply chain mix will become increasingly important. In the new customer mindset, a promotional package that offers great value will generate significant sales.

There will also be a continuing emphasis on reducing supply chain complexity. The new norm is rationalization of suppliers, clustering of suppliers, rationalization of the carrier base, reduction of the number of logistics service providers, and utilization of hubs.

Strong, lean supply chains will be vital in the rejuvenation of the economy. By focusing on process inefficiencies, companies are improving their performance and coming out of the recession stronger.

Gilmore adds that cash is paramount in the supply chain new normal. Memories of this recessionary period will stay in the minds of customers long after the economy recovers. Credit will never again be as easy as it was before the downturn. Professionals from all walks have learned powerful lessons on the value of a strong balance sheet.

In the supply chain new normal, companies are shedding assets faster than ever. Owning supply chain assets and having high fixed costs

in an economic downturn can be fatal. It means more companies are outsourcing more functions and physical assets to third parties.

OIPMAC continues to equip its members with the skills and knowledge they will require to prosper in the new normal for supply chain management. As previous Board Chair Sandra Gilmer points out in this year’s annual report, we have charted a clear and practical strategic direction for the future of the Institute and the supply chain management profession.

A key strategic imperative we are currently pursuing is the development of supply chain management resources for our members. Our goal is to identify and develop new and emerging practices in supply chain management to fulfill the continuing education requirements of our members and strengthen the competitive position of organizations in the Canadian public and private sectors.

Central to this strategic imperative is the establishment of a new OIPMAC supply chain management web portal and information resource site. The formation of applied research partnerships with leading Canadian universities will be a vital component of this initiative. Reports and white papers generated from SCM applied research projects undertaken through university partnerships will be used to populate the OIPMAC SCM website portal, as well as be presented at OIPMAC conferences and seminars. In addition, articles based on collaborative research projects with the universities will be published in academic, trade and Institute journals. These articles will be accessible to a wide range of audiences and specifically benefit SCM practitioners.

Access to leading-edge research, education and training in the theory and practice of supply chain management will be vital in helping OIPMAC members thrive in the SCM “new normal.” In fact, our members will lead and shape the new normal in supply chain management, however it is defined.

R. David Fletcher *President and CEO, OIPMAC*



Improving the Cash Conversion Cycle



In a recent client mandate, we discovered a ten day delay in the timeliness of invoicing by a manufacturer. The company's accounting department waited for a copy of the bill-of-lading, signed by the receiving department of their customer, to be returned by the shipping department. They wanted to make sure that the customer had actually received the goods before sending out the invoice.

This is a noble gesture on the part of the manufacturer. But does it make good business sense? The longer it takes for the customer to receive the invoice, the longer it will take for the manufacturer to get paid. Delays like these have an adverse affect on working capital. Most businesses understand this, but often fail to look critically at improving the cash conversion cycle.

The amount of working capital "locked-up" in the cash conversion cycle is defined as follows:
$$\text{Inventory} + \text{Accounts Receivable} - \text{Accounts Payable}$$

Companies consume cash when purchasing materials for manufacture or resale and assume them into inventory. The cash is not "returned" to the business until the customer pays the sales invoice, which typically happens some time after the goods have been invoiced to the customer. To the extent that the company owes suppliers for these materials, its cash position is improved.

For example, Dell (computers) perfected this when they set up their on-line order business:

You pay at the time you place your order. Dell draws raw materials from their suppliers after your order has been placed and therefore assume inventory as late in the process as possible. This inventory is converted to a finished product and shipped to you within days. Dell pays for this inventory on terms at some time thereafter.

As a result, inventory is very low and accounts receivable is virtually non-existent. The lock-up formula returns a negative value, meaning that Dell has negative working capital invested. Put another way, they are funding the business on "other people's money."

Of course, the Dell model may not be possible in other industries (although likely no one thought it possible in the computer industry either until Dell tried it). What is important to learn from the Dell model are the concepts that enable companies to improve the cash conversion cycle.

Best Practices

Improving the Cash Conversion Cycle requires examining every step of the cash conversion process. Some of the best practices used to improve the cash conversion cycle include:

By *Barry G. Levine, RSM Richter*

Purchasing

- Where possible, order smaller quantities of inventory closer to the time of use to reduce inventory on-hand. Implement just-in-time inventory systems.
- Negotiate favourable payment terms where possible. Consolidate purchases with fewer suppliers to increase the business you do with each supplier, affording better leverage.
- Set and measure vendor performance measures to ensure consistency of delivery and supply, thereby reducing delays.

Contracting and Pricing

- Negotiate favourable customer payment terms and monitor them to ensure that customers are not unduly delaying payments.
- Ensure that contracts are clearly defined and that items are properly priced in the system to avoid rejections by customers' receiving departments.

Sales Order Processing

- Implement electronic ordering interfaces to reduce paperwork, delays and errors resulting from manual processing of orders.
- Define and implement back-order and substitution policies to speed up order processing for out-of-stock items.
- Implement automatic credit checking and adhere to limits to reduce the risk of delayed payment.

Order Fulfillment

- Automate the release of orders to production to reduce production delays.
- Implement cellular production and lean manufacturing concepts to increase production flexibility and reduce batch sizes, thereby reducing the need for long production runs and significant finished goods inventory.
- Automatically release pick lists to the warehouse and implement paperless picking to reduce time and errors.

Billing

- Issue invoices as early in the ordering cycle as possible to reduce the time to collect payment.
- Implement electronic bill presentment to reduce delays introduced by postal delivery.
- Align billing cycles with customers' payable processes to avoid missing their payment cycle.

Collection

- Encourage electronic payment in alignment with negotiated payment terms to reduce payment delays and discrepancies, and to reduce paperwork, delays and errors resulting from manual processing of payments.
- Implement a formal collection escalation process and dunning letter cycle to reduce extended receivables.
- Apply received funds and deposit immediately to make cash available to the business.

Key Performance Indicators

How do you measure the performance of your cash conversion cycle? That is relatively easy. The most prevalent way to measure it is to measure the lock-up expressed in days:

Days Inventory Outstanding (DIO) + Days Sales Outstanding (DSO) – Days Payables Outstanding (DPO)

This metric serves to measure both the effectiveness of working capital management, but it also serves to measure the effectiveness of the supply chain performance. That is, both financial and operational executives can evaluate performance in a single measure.

The components of this metric can be determined easily from financial statements:

$DIO = \frac{\text{Inventory}}{\text{COGS}} \times 365$	The average number of days between the acquisition and sale of goods
$DSO = \frac{\text{Account Receivable}}{\text{Sales}} \times 365$	The average number of days between the sale of goods and collection of receivables
$DPO = \frac{\text{Account Payable}}{\text{Purchases}} \times 365$	The average number of days between the purchase and payment of goods

Consider these metrics applied to an importer and manufacturer in the example below:

	\$000's	
	Company A	Company B
Sales	365,905	85,249
Purchases	82,531	40,107
Cost of Goods Sold	165,886	62,125
Accounts Receivable	43,144	9,488
Inventory	41,760	18,730
Accounts Payable	32,529	5,264
DIO	92	110
DSO	43	41
DPO	144	48
Total lock-up in days	(9)	103

In the case of Company A, the total lock-up expressed in days is minus nine (-9). This is an enviable position to be in. The company has relatively low inventory and exceptional terms with its suppliers. In the case of Company B, we see a much more typical case. Here the DSO and DPO are roughly equal, cancelling each other out. But a significant amount of cash is still tied up in inventory.

This is one way to measure the effectiveness of the cash conversion cycle. Other relevant metrics include:

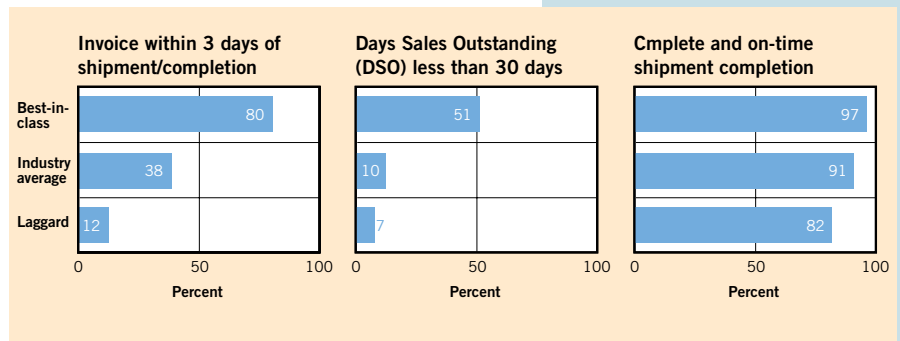
- Order-to-cash cycle time.
- Transactions per full-time equivalent (FTE) employee.
- Complete and on-time shipment/completion of orders.
- Errors per thousand transactions.
- Bad debts.

Benefits

Improving the cash conversion process has a number of benefits:

- Improved cash flow and reduced need for working capital.
- Lower cost to process transactions.
- Shorter cycle times and improved customer service.
- Lower error rates.
- Higher staff productivity.
- Reduced bad debts.

In 2007, an Aberdeen Research benchmarked best-in-class performance against the industry average and laggards on three key metrics as illustrated in the graphs below:¹



Aberdeen's research highlights that companies adopting best-in-class processes in the cash conversion cycle outperform the industry average and laggards significantly.

Conclusion

A critical look at the cash conversion cycle can have a significant impact on the amount of working capital tied up to finance inventory and receivables. Improving the cycle not only improves cash flow, but leads to a more productive and effective set of business processes.

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1 The Order to Cash Cycle—Integrating Business Processes to Improve Operational Performance, Aberdeen Group, April 2007.

Recovery has begun, but what challenges lie ahead within Supply Chain Management

By Shawn Casemore, C.P.P.

...organizations will
look to their supply chain
to be creative,
working to develop an
increasing number of
“local” customers

The economy is showing continued signs of recovery, so it is an opportune time to reflect on the events of the past year and prepare for that which lies on the horizon. One year ago the key issues captivating Supply Chain professionals included Environmental Sustainability, Globalization and the expected near term shortage of skilled labour. Considering the weak improvement in commodity pricing and the slow stabilization of unemployment rates, it will undoubtedly be sometime before many companies and industries return to earlier levels of profitability. Herein however exists an opportunity for Supply Chain management professionals to plan for the challenges ahead, building on trends which existed prior to the market adjustment.

Environmental Sustainability exists as a top priority for many companies, particularly in the public sector. It can be costly to purchase goods and services which are considered “green” as many

suppliers who boast these qualifications charge a premium for such. Reducing an organizations carbon footprint while minimizing or reducing cost can be a challenge and will rely on innovation and collaboration within the Supply Chain. Commencing review in such areas as supplier practices in manufacturing, waste disposal, and chemical application can provide insight into areas where suppliers may already be practicing environmentally friendly initiatives that have not been publicized. In addition, opportunities exist for collaboration in such areas as environmental services, recycling and freight consolidation. Collaboration in these areas can identify more environmentally responsible sources of supply as well as opportunities for shared volume to increase discounts.

Globalization will continue, though the pace of which is likely to slow in the coming months. With the tremendous loss of jobs in the automotive sector as an example,

there will most likely be pressure to keep manufacturing jobs within North America. Hence organizations will look to their Supply Chain to be creative, working to develop an increasing number of “local” supply sources while still maintaining cost competitiveness. There are industries where this may be impossible, however I would suggest that the market adjustment has left many capable suppliers with excess capacity, many of whom are willing to be creative in order to obtain new and sustainable business. Application of Six Sigma and Lean methodologies within such relationships can provide a reduction in process costs as well as the total cost of quality.

The shortage of skilled trades is not as easy to predict. It would appear many who are retiring are resurfacing in new industries as a second career. Market adjustments have also created a short term reduction of demand on labour and although expected to rebound, will likely take sometime as globalization stabilizes and companies focus on leaning out operations. It is reasonable to expect that there will be shortages of labour in some areas, however any significant shortages are most likely not going to be appear for another 5 to 10 years.

To improve the financial viability of our organizations it is important to develop suppliers in new and creative ways, ensuring environmental sustainability is maintained throughout the chain of supply while continuing to reduce the total cost of ownership. The challenges ahead however are just another step in the evolution of the Supply Chain Management professional and serve to ever increase our value within the organization.

Risky Business

How to Protect Your Supply Chain

By John Westerveld, Product Manager, Kinaxis

In today's volatile environment, companies have never been more vulnerable given the increased risks to their supply chain. In response, more and more companies are looking to implement or augment their risk management strategies.

The growing awareness and importance of supply chain risk management can be attributed to several business trends:

- leaner supply chains – less inventory, saving money and avoiding liability, but when events happen, there is no buffer to recover
- global sourcing – limited visibility, difficult communication, lead times stretched
- higher customer expectations – consumers want instant gratification, supply chain slow downs result in lost customers

- complexity and interdependency of supply base – networks of contract manufacturers with materials flowing in all directions
- variability of demand, shorter product life cycles
- increasing commodity costs and tighter logistics capacity – harder and more expensive to ship goods

These trends have been further exacerbated by major events over the past several years – from increased regulation, to natural disasters, to the volatile economy – that have only magnified the risk of supply chain disruption.

Regardless of how well planned or well managed a company's operations are, enterprises face external factors beyond their control that can easily disrupt the supply chain.

Companies with the most effective risk management strategies address both anticipated and unanticipated supply chain disruptions; they are able to assess the impact, evaluate the action alternatives, and most importantly, implement the most effective response as quickly as possible.

The Two Sides of Supply Chain Risk Management:

There are two components to supply chain risk management:

- Proactive risk assessment and mitigation
- Response to unanticipated supply chain disruptions

Both are necessary components of an effective supply chain risk management strategy. With strong risk mitigation strategies in place, a company is ready to handle a variety of supply chain events. And when unanticipated events occur, a company must be prepared to respond quickly and effectively or risk suffering financial and customer service losses.

A Deeper Look at Assessment and Mitigation:

There are three key phases to proactively managing supply chain risk:

- **Visualize and understand risks that apply to the supply chain.** General categories of risk include natural disasters, flu/pandemic, economic risks, political risks, transportation and unstable demand and/or supply. As one example, if your supplier is located in a region known for significant seismic activity, do you have an alternate source for that supplier should a serious earthquake strike?

...enterprises
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beyond their control
that can easily disrupt
the supply chain

- **Measure and prioritize the risks according to the likelihood of occurrence and the business impact.** The mitigation required for a risk will be dependent upon the assessment of how likely it is that the risk will occur and what the impact to the business would be. A risk that is very likely to occur but has little business impact might have a low mitigation priority; same too for a risk that has a large impact but has very little chance of happening. However, for a risk with a high chance of occurring and a significant business impact, a company will have a high priority for addressing this risk.

The drivers of risk (political landscape, consumer behavior, economy) continue to change so risks should be reviewed regularly to ensure that new and changing factors are continuously being considered.

- **Decide which risks need to be addressed and develop mitigation strategies.** Based on the priority, mitigation strategies need to be developed for the risks identified. Mitigation strategies could include developing alternate sources, establishing alter-

over

continued

nate transportation routes and product redesign to leverage more easily accessible items.

Mitigation strategies should be modeled and tested to ensure they are reasonable strategies. If the strategy does not yield acceptable results, different strategies must be developed and considered.

Response and Implementation:

Responding to supply chain events can take two forms:

- Responding to an anticipated supply disruption by implementing the mitigation strategy
- Responding to an unanticipated supply disruption

In either case, an effective and instantaneous response is critical and can mean the difference between an insignificant blip and a full-scale crisis. Technology plays a key role in this process.

A successful supply chain risk management tool should incorporate the following capabilities:

Visibility into the entire supply chain – The tool must integrate with multiple disparate ERP systems, including systems supporting the supply and distribution nodes.

Event detection and alerting – The supply chain should be constantly monitored and an alert triggered

when a disruption has occurred to initiate the implementation process of risk management strategies.

Analytics – The full suite of supply chain analytics needs to be modeled in the tool to ensure the impact of a potential supply chain event is understood. These analytics need to be performed in real-time when responding to an unanticipated supply chain disruption.

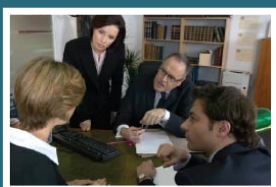
Simulation – Simulation can be used to model different risk scenarios, propose mitigation strategies, and compare the effectiveness of various response alternatives.

Collaboration – Evaluate as a team, several possible mitigation alternatives to ensure that the response alternatives are reasonable and align with corporate objectives.

Conclusion:

An effective supply chain risk management strategy addresses both risk assessment and mitigation, as well as event response.

If companies implement this approach, with a specific emphasis on increased visibility and collaboration across their supply chain, they will be more prepared and better equipped to recover quickly from anticipated and even more importantly, any unanticipated supply chain disruptions.



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Supply Chain Finance: Using technology to build a better world

By Andrew Miller, President, ACM Consulting

Supply chain financing is the flow of money that supports the movement of products between buyers and suppliers. This means that when a company buys a product from a supplier, supply chain financing techniques would facilitate the economic transactions. In this article, I am going to discuss various ways that companies can optimize the availability and cost of capital by leveraging technology and using supply chain financing techniques.

According to a survey done by CGI in 2007 (CGI Supply Chain Finance Report), 85 per cent of global trade transactions occur through Open Account. What that means is that 85 per cent of transactions between buyers and suppliers are done directly between the two companies. This is usually done through wire transfers, cheques, electronic funds transfer, or even cash payments. There are other ways that these transactions can be facilitated – such as letters of credit – but since the other methods represent such a small percentage of the total transactions, why bother discussing them?

Many companies are trying to unlock the mystery of how to use supply chain financing to gain efficiencies and improve performance, but it is never as easy as it may

sound. According to an Aberdeen Research study from 2007, more than 65% of companies are either investigating or putting financing programs in place to lower costs and improve financial metrics. My initial thought when I heard this was; “why aren’t 100 per cent of companies investigating these types of programs?” Time and time again, they have been proven to deliver results and strengthen relationships. The answer is likely that companies do not think of financing as having the ability to improve their bottom line. This is an incorrect assumption. Just by using technology, companies can have an impact on their bottom line and their business relationships.

There are many new types of technology that allow for the automation of many supply chain transactions. Companies can see a significant financial benefit in their invoicing and payment processes by moving these transactions to the electronic world. Imagine a world where a supplier can sell a product and provide the invoice electronically as soon as the product is ordered. The buyer can then electronically match the invoice to what was originally ordered and what was physically received (the “three-way match”), with a few keystrokes on a computer. With the click of a button, payment is

then transferred electronically to the supplier, where it arrives directly into their bank account. This whole process would take no more than 2-3 days and, barring any discrepancies, would not require any hard-copy documents, or the need for paperwork to be physically handled by multiple people, from both the buyer and supplier organizations.

Wouldn’t that be a great place to live? Well, I have a newsflash for you; that technology is here and is being used every day by your peers and your competitors. Imagine the efficiency and time gained by setting up systems for electronic invoicing and automatic payment. Imagine the reduced cost by suppliers not having to print invoices then mail (or courier) them, then buyers not having to cut a paper cheque and mail it back to the supplier. How long would that process take – days? More likely, weeks.

Using technology in this way also allows companies to build stronger relationships with their financing partners (aka Banks) and their business partners. If you are able to develop a reputation for on-time payment and accurate deliveries, and make it easy for people to work with you, it will be much easier to ask for credit, re-negotiate payment terms, or reduce borrowing



costs. Technology can help build relationships. If a supplier knows that by delivering their product on time, they are going to be paid within 24 hours, we can create stronger relationships that will benefit both buyer and supplier in the long run.

There are many opportunities to use technology and relationship management to improve efficiency and reduce costs, through supply chain financing. Know your business partners, know your finance partners, and look to leverage technology to make the invoice and payment process simple and cost effective. The more visibility we can have into the business operations of our partners, the more we can collaborate to find opportunities for mutual benefit. More companies need to take advantage of the technology out there to improve their operations and develop stronger relationships, both of which will help the long-term viability of any company.

Utilizing Empathy

to Drive Strategy via Key Stakeholders

By Hanisha Sharma, B.Comm, MBA, C.P.P.

Corporations can maximize shareholder value by employing emotional intelligence with their key partners across the value chain. By using empathy as a strategic tool, organizations can gain untapped insight from their key relationships.

em-pa-ty: the intellectual identification with or vicarious experiencing of the feelings, thoughts, or attitudes of another

Employing empathy is crucial to capitalizing on 3 key opportunities across the value chain to create better long term strategic value

EMPATHY MODEL[®] ORGANIZATIONAL KEY VALUE CHAIN

	SUPPORTER Vendor	RECEIVER Customer	ENABLER Employee	
KEY EMPATHY OPPORTUNITIES	Gaining Common Perspective	Understanding a supplier's position (break even cost) and intent in the relationship can enable a fair deal, joint innovation and process improvements in the long term	Identifying the needs and wants of customers, along with industry trends, will ensure a sustainable product offering. Additionally, adapting to the changing needs of customers is also essential to remain sustainable	Seeking out proactive feedback from employees can help organizations understand their employees' values and perspectives enabling better alignment to the corporate goals and culture
	Eliminating Pre-determined Bias	Removing pre-determined biases from vendor relations will ensure that the partnership is factual and ethical. It ensures that the relationship is not complacent while giving suffice development opportunity for the vendor offer innovative solutions	Conducting consumer behaviour analysis should be made without biases to avoid making false generalizations that can be costly and detrimental to customer service. It is viable to offer choice where possible rather than creating false hypothesis	Removing pre-determined biases when dealing with employees will ensure fair and ethical practices and enable higher performance. A transparent performance management systems that rewards the right metrics can help to drive this
	Balancing Internal & External Focus	Keeping a fair balance of internal and external focus addresses the organizational needs along with the vendors' needs which ensures a more mutually beneficial relationship with fair profit margins	Placing internal focus to maintain strong customer management processes is essential. Maintaining equal external focus on the customer by including the customer impact in all processes will ensure that the processes support the right customer delivery intent	Enabling the achievement of individual (intrinsic) goals and the financial goals of the company is an essential winning condition for an innovative, high performing organization. This can further spark competitive differentiation and sustainability

Emotional display within business partnerships has traditionally been limited due to the “culturalization based values of independence¹” promoted in corporate North America which hinders the ability to be empathetic in business conduct. While maintaining disciplined emotions is critical to operate a professional business, limited depiction of empathy can stunt the natural development from a transactional relationship into a strategic one. Let’s examine the key areas of opportunity by using Empathy Model² as a tool to manage vendors (one of the key business partners across the value chain):

Key Empathy Opportunities through Vendor Management

Well managed businesses have evolved from the expectation of achieving unrealistic high profit margins to the empathetic understanding that their vendors require a fair profit. Organizations that have grasped this concept early have been able to generate more strategic, proactive and innovative vendor partnerships that can result in both tangible and intangible competitive advantages including: i. shared expertise to develop joint ideas for product expansion and process efficiencies; ii. cost saving ideas that offer benefits to both parties; iii. market intelligence; and iv. greater likelihood of better customer service and quality³.

In order to successfully arrange a relationship that incurs fair profit, business customers (organizations) must first place themselves in their vendors’ position to be able to calculate their vendors’ business angle and break even cost thereby **Gaining a Common Perspective**. This in-

volves a basic understanding of their vendors’ expenses, capital requirements (or obligations), and growth intent. While this information may be proprietary, industry research can be gathered to understand the average profit margins through public reports or an RFI (request for information). To more specifically understand a vendor’s strategic direction, much of this can be gained through official vendor business reviews where two-way performance and strategic information can be shared. Here organizations can gain a better understanding on their vendors’ growth initiatives and product strategy while confirming how much business they represent to the vendor. This valuable information can assist in creating a fair deal for the goods and services supplied by the vendor.

Fair profit is also advantageous as it can assist as a governing tool to ensure that the economic foundation of a customer-vendor relationship is set up for ethical profit margins along the entire value chain creating a good **Balance of Internal and External Focus**. It should be noted that “fair” profit can range depending on where the product or service is produced however should still remain competitive within the respective local market.

When dealing with vendors, organizations should also avoid **Pre-determined Bias** based on their suppliers’ historic performance. By becoming too dependent on perceived “high performing” vendors for example, organizations can become complacent within the relationship and overlook underlying issues leading to unexpected breakdowns (i.e. process or compliance issues). Alternatively, the

micro management of perceived “weak performing” vendors can create limitations of a vendor’s innovation capabilities.

Enabling Open Communication Through Empathy

Exhibiting empathy within a vendor relationship can encourage a voluntary channel of information to source and gain assistance for new ideas, an essential part of enabling innovation⁴. It is critical that a vendor relationship is set up with the right type of penalties and incentives to foster the right behaviour. Penalties placed upon vendors through service level agreements for late product deliveries for example, while recommended, can remove the opportunity to proactively collaborate on a long term value solution⁵ to resolve the root cause of such issues. It is therefore essential to place emphasis on understanding a vendor’s angle when such mishaps occur by including this perspective into the vendor performance management process and not by simply defaulting to the penalty process alone. Coupling this with two-way performance feedback from the vendor can help organizations understand and take action on their own hidden areas of opportunity.

Understanding of a partnership from a supplier perspective is even more crucial within international relations. Here, corporations can influence a more viable trade agreement through empathy by actively engaging in the home country of its supplier to better map their value systems, culturally embedded positions, strategic alliances, and relevant trade barriers – all factors which deeply impact the relationship outcome.

Corporations should be diligent about gaining a 360 degree perspective from all of their key partners otherwise they run the risk of enduring unexpected mishaps and cost gaps. With quick changing industry trends and competitive markets, organizations, now more than ever before, have the opportunity to tap into the intellect carried within partnerships to help instil greater value that is mutually beneficial and sustainable. It is important to pay close attention to the strategic position of key partners and keep open communication channels to stay abreast of changing trends. Additionally, as corporations have become more accountable for their communities, it is essential to their longevity that they foster empathy within their extended parties including government and not for profit bodies to develop a better corporate social responsibility strategy that offers both economic and social reward. Corporations can add significant value to their bottom line by utilizing empathy as a “free”, strategic tool to leverage existing partnerships and influence new ones.

1 Article: “America Culture Destroys Empathy” - <http://tenpercent.wordpress.com/2007/07/21/american-culture-destroys-empathy/>

2 Empathy Model created and copyrighted by Hanisha Sharma

3 Article: “What Should the Professional Supply Chain Manager Know About Six Sigma?”; <http://scm.ncsu.edu/public/sixsigma/6costben.html>

4 Harvard Business Review article “The Innovation Value Chain”, pg. 4

5 Article “Analysis : The Keys to Expedia’s Success” - http://www.businessweek.com/managing/content/sep2008/ca2008092_371191_page_2.htm

Freeing-up Cash: Supply Chain's New Clout

By Jacqueline Iny, Founder, INSTEEL Consulting Corporation

...ability to optimize
working capital is
key to survival

Working capital financing, once treated as the exclusive domain of Finance and Treasury, has become everybody's business. Today, Finance is turning to Procurement and Supply Chain to set strategies and practices that free-up working capital for the entire organization. The ability to optimize working capital is key to survival and strategic to leveraging the window of opportunity emerging with economic recovery.

Taking Stock 2007 - 2009

Over the past twenty-four months or so, we have experienced the deepest, broadest and most pervasive global recession in decades. Volatility in global demand, commodities pricing, interest rates and currency values has become the norm. Credit and equity financing dried up and liquidity contracted sharply. Insolvency rocked entire industries.

Boardroom conversation morphed from "growth and profit" to "cash and survival." In a recessionary time, "cash becomes king." The income statement and bottom-line performance give way to the balance sheet, cash availability, immediate survival, and near term sustainability.

"Cash is King"

Cash is key to survival. Companies need to make payroll and keep the lights on. Cash is key to sustainability. Organizations need to fund inventory and work-in-progress in order to meet commitments. Finally, cash is key to the ability to take advantage of opportunities. While a recession may create opportunity for survivors to increase market share, available cash is necessary to fund the growth and innovation.

As banks tightened lending, and equity financing dried up,

liquidity was severely compromised and working capital became increasingly difficult to finance. Working capital became even more strained as revenues dropped, clients wanted longer terms, suppliers wanted shorter terms, and bad debt and inventory obsolescence skyrocketed.

Managing Working Capital in the Supply Chain

Working capital is managed by three components: accounts receivable, accounts payable, and inventory. In a July 2009 web-cast, Ernst & Young emphasized that, "While markets remain uncertain... cash management is the safest way companies can secure their present... Cash management and release have risen to the top of corporate agendas." The supply chain presents significant opportunities to free-up working capital, including: accounts receivable and accounts payable policies adapted to optimize the cash-to-cash cycle, sourcing and inventory policies adapted to account for the timing of dollar flows, and customer service goals revised to reduce costs.

Organizations are pulling working capital levers and adapting policies and practices for these

Supply Chain Liquidity Tradeoffs – Performing vs Stressed Times		
	Performing	Stressed
Inventory	Total inventory cost: holding + ordering=EOQ	Timing of dollar flow trumps total cost (<EOQ)
Discounts A/P	Take the discount	Forgo discount- take extra 60 to 90 days
Discounts A/R	Fixed intervals e.g. 2/10, net 30	Prorated interval e.g. 2/10, 1.5/15, 1/20, net 30
Contract structure	Total deal value	Timing, and/or extended financing
Finance focus	Earnings, profit, growth: Income Statement	Immediate survival: cash Balance Sheet

stressed times. Companies are realigning supply chain priorities, and purposefully making tradeoffs to support liquidity and ensure business continuity.

Supply Chain Liquidity Tradeoffs – Performing vs Stressed Times (Figure 1)

In performing times, Economic Order Quantity (EOQ) dominates inventory-ordering decisions. In stressed times, companies may order smaller than EOQ quantities to delay the outflow of dollars, the tradeoff being higher total costs.

In stressed times, companies forgo payables discounts, holding on to cash for an extra sixty to nine-

ty days. On the receivables side, traditional discount intervals can be prorated to incent early settlement, say at twenty days, rather than the traditional thirty days.

Contracts, in performing times, tend to focus on total deal value. In stressed times, timing of dollar flows and availability of financing rise on the priority list.

Finally, where in performing times, corporations focus on the Income Statement and growth, in stressed times, focus moves to the Balance Sheet, liquidity, and immediate survival.

“How-To”: Back to Basics

As the economy unraveled, com-

panies were called upon to adopt a systematic approach to deal with the volatility and uncertainty that were becoming the new normal. While we are now beginning to see signs of recovery in the macro-economy, general sentiment is that uncertainty will persist well into 2010. The “how-to” challenge, takes us back to basics:

- Realign policies, processes and procedures with current working capital and risk conditions
- Enlist organization-wide involvement: top-down, bottom-up, lateral and cross-functional
- Integrate forecasting, planning, visibility, and performance indicators, across finance, sales,

operations, and the entire value chain

- Set strategies and tactics, communicate, train, measure and reward

Leveraging the Window of Opportunity

Gone are the days of back-of-the-envelope cash flow forecasting. The rigor, visibility, and collaboration called for in these stressed times, are becoming the “new normal” for cash management. As the economy moves toward recovery, ongoing cash availability to fund growth and innovation is key to leveraging the emerging window of opportunity.

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“The knowledge that I've gained from this program has aided me in transitioning from my (introductory) role to a Procurement Manager position, looking after seven offices throughout North America, and finally into my current position as a Strategic Sourcing Specialist for one of the largest Enterprise Retailers in Canada.”

Douglas Stacey

Submitted by Bonnie Cowan, Area Procurement Manager, Microsoft

I have been a member of PMAC for about 10 years and a C.P.P. designation holder since 2005. My career has changed and evolved over those years and I am currently working for Microsoft in Singapore as the Area Procurement Manager, South East Asia.

My key learning and leadership opportunities have come from stepping up and showing the value of Procurement to the business. Our role is, and will continue

to be, crucial to key stakeholders as we find new and innovative ways of doing things. Remember to always challenge assumptions and ask - Why? I have spent the last few months presenting the value of procurement to the senior leadership teams at each subsidiary in South East Asia. We all have success stories to tell - so get out there and tell them! Don't wait for opportunity, present the opportunity and develop your critical thinking skills.

Most of all; lead the way and deliver results. On my team, we have put together monthly scorecards for the business that demonstrates the value of our projects, but also makes us accountable and take ownership. We are stepping up to the challenge and leading by becoming trusted advisors.

Don't be afraid to put yourself out there and take on those big challenges. You are the procurement and supply chain professionals driving growth and profitability.

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