Today's Business Climate Calls for Formalized, Holistic Approach to Supplier Risk

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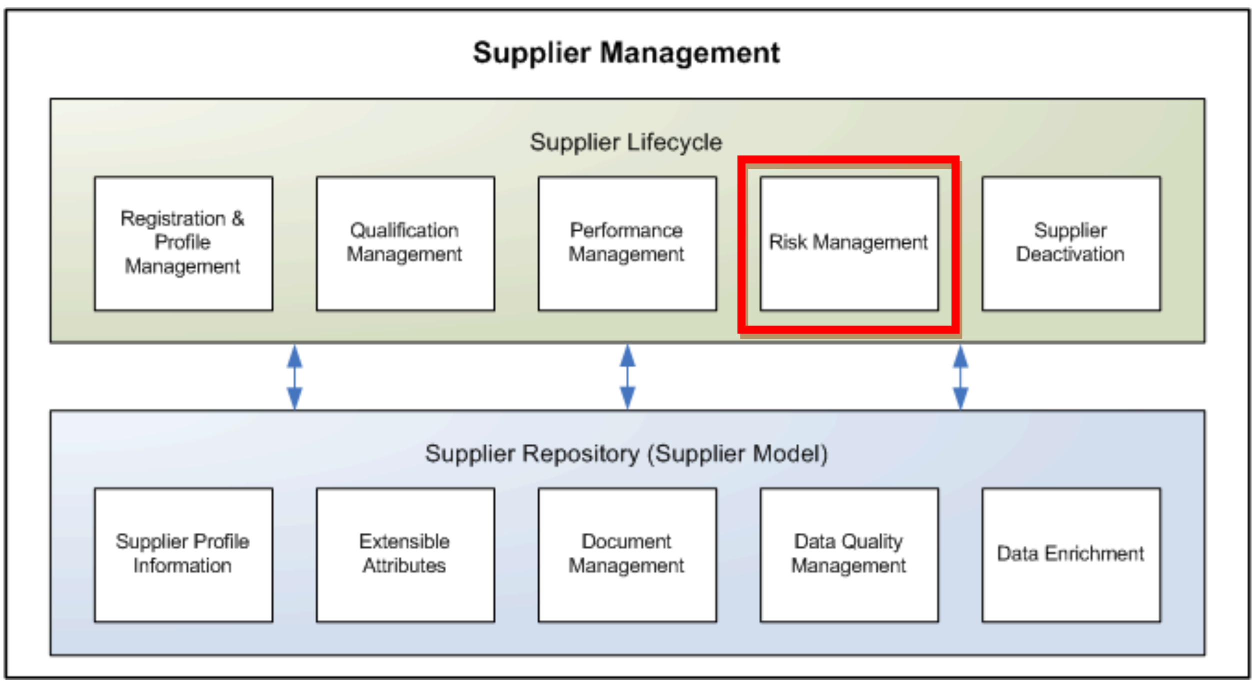
Various business processes occur throughout the lifecycle of the relationship between an organization and a supplier. Initially, procurement systems focused on transaction automation such as issuing orders and processing invoices. Over time, solutions addressed more complex processes such as strategic sourcing and contracting. In addition, business intelligence became important so that organizations could better understand performance and identify opportunities for improvement. Ultimately, systems that addressed these areas matured.

Supplier management addresses two additional areas. First, supplier management addresses the need to harmoniously handle the supporting aspects of the primary supplier relationship (that of buying and selling). This includes processes such as the initial registration and on-boarding of a supplier and the thorough managing of information about that supplier (e.g., the process of verifying claims the supplier makes about themselves—claims that could be decision criteria during sourcing, as well as additional information from third parties). Second, supplier management empowers customers to use all aspects of their knowledge of the supplier in order to drive more value out of the relationship and mitigate risk.



Supplier risk management refers to a new area within procurement that allows organizations to quantifiably model the riskiness of the supplier relationship leveraging all the available knowledge about individual suppliers and the supply base. This could include supplier specific metadata as well as macro data about the economics of the categories provided, geo-political considerations, etc.

To help illustrate and provide some context on the impact supplier risk can have on an organization, and the risk-related information needed in today's global and constantly evolving economic and geo-political climate, below are several use cases. Each example demonstrates different kinds of information that technology can make readily available to procurement and risk professionals that they can leverage in their everyday supplier management decisions.

Supply base risk analysis for geo-political event mitigation

Suppose there is a sudden destabilization in the Korean peninsula. A company then wants to review its supply base and ascertain what possible risks this could have and also review what contingency plans are in place. It may also wish to adjust the riskiness associated with doing business with suppliers in that region. Ideally, a category manager, a buyer, a procurement contract administrator, or other user with a role in sourcing or managing suppliers should be able to conduct a risk analysis on the fly to make a more informed decision on whether to increase the riskiness of suppliers having the geographic attributes associated with the region and then query on a list of the most risky suppliers. In addition, there is a need for increased visibility into what contingency plans are in place for this situation and/or these suppliers. It can then be determined whether a new contingency plan should be created, or whether pro-active action should be taken, such as conducting a new sourcing project to identify alternative sources of supply.

Use of risk data in sourcing RFP evaluation

When performing an evaluation of bids that suppliers submitted in response to an RFP, buyers often use additional decision criteria that may not come directly from information provided by the supplier. Past performance is a typical example. In the case of risk, if a company has taken the time to put in a risk model for the supplier base, it likely would want to include risk criteria as additional information to be weighted into the award decision. Following on the scenario mentioned above, if a new negotiation has gone to bid and two suppliers make functionally equivalent bids but one has operations in Seoul and the other in Denver, the Korean supplier may generally be more risky to do business with. Hence the local U.S. supplier would be awarded the contract. Based on the risk factor, it may still make sense to award locally even if the price is slightly higher. The impact of the risk needs to be quantitatively factored into the projected cost of doing business so that the user can see the tradeoff and make a decision.

New supplier identification for sourcing with self-registration

A manufacturer of traditional audio and video equipment decides to enter the market with a new product for digital media server. After spending months researching, designing and prototyping the product, the company decides to start the manufacturing and launch the product before the holiday season starts. To make sure it meets the timeline the company finds it important to source the parts from the right suppliers who could help the company meet its goals. It wants to make sure proper due diligence is performed in indentifying these suppliers. The company first finds a pool of suppliers that satisfy the basic requirements. This pool is derived from a mix of existing suppliers as well as potential suppliers including the ones identified with the help of an external partner such as Dun and Bradstreet. The company then selects a smaller set of suppliers from this pool who meet the requirements and invite them for negotiations. The requirements include many factors such as size, capacity, geography, financial condition, customer base, and its technology. All invited suppliers are required to register with the manufacturer by providing the requested information and documents. The manufacturer reviews the registrations and approves them to make sure they have the right mix of suppliers approved so that they can meet their production plans.

Supplier risk – what's the bottom line?

So what's the bottom line impact and potential value in managing supplier risk more effectively? It's typically not necessary to convince stakeholders to prioritize risk management after a major disrupting event occurs, such as the 2011 disaster in Japan and its impact on numerous global supply chains. However, getting executives to make the necessary investments ahead of time, and proactively manage supplier risk in a holistic manner *before* something goes wrong can require a little selling.

First, the value of proactively managing supplier risk as part of day to day operations can be made clearer to management once they understand that there are many different kinds of risks that must be managed when thinking about their suppliers. This goes well beyond just looking at financial risks and viability by reviewing in silo a D&B score or other similar financial health metric. Other supplier risks that need to be incorporated into a more holistic framework should include:

- ***Reputation risks*** and brand impact from negative media coverage
- **Compliance *risks*** such as code of conduct or contract and SLA violations
- ***Transaction risks*** that drive on-time delivery, product quality issues, and warranty support
- **Operational risks** including business continuity, competitive pressure, or insurance coverage
- ***Other risks*** often specific to industries or regions, such as geopolitical events and unrest

Second, the organization is exposed to a multitude of these related supplier risks as part of conducting normal business operations; so monitoring these risks in a formalized, and continuous fashion can be critical. With this in mind, it's probably not surprising to find numerous studies revealing that supplier disruptions can not only delay product delivery, but also directly impact stock price, working capital, and bottom line profitability. This line of reasoning is reinforced by a 2010 study put out by Accenture and MIT entitled *High Performance in Procurement Risk Management,* in which the findings demonstrated that supplier related risks "…have a greater cost impact—and take up far more time—than most buyers' efforts to capture savings through negotiation."

To further help put a value on the impact of supplier risk, it's worth revisiting the 2011 Japan disaster example, and its impact on the automotive industry alone. For instance, Wall Street analysts at Goldman Sachs estimated that shutdowns are costing Japanese automakers more than $150 million a day, with Toyota Motor Corp. losing an estimated $73 million dollar each day because of the disruption (*source: Marketwatch.com*). And automakers in the U.S. are hardly immune - General Motors reported that it had to stop production at one its plants in the U.S. because of parts shortages caused by the Japan crisis.

Organizations have an opportunity to further leverage risk-based data to improve their supply chains and reduce disruptions and their resulting impact. People, processes, and technology all play a critical role in helping get the right and more complete, timely set of information to those responsible for supplier management.

Embedding risk data directly into business applications

Oracle, the largest enterprise software vendor in the world, has been providing customers with advanced, automated controls and transaction monitoring tools for many years, including our Governance, Risk, and Compliance (GRC) Suite of applications. With the increased volatility to supplier ecosystems, in large part due to the global financial crisis that started in 2008, many of our customers have indicated a need for a more consolidated view and access to actionable, risk-related information when managing their suppliers. As a result, Oracle has extended the value of its GRC applications by building a solution called the GRC Accelerator for Supplier Risk Management.

The Oracle GRC Accelerator for Supplier Risk Management ("Accelerator") embeds proven enterprise risk management practices and actionable dashboard reporting directly into the processes and business applications that companies use every day to manage their relationships with strategic suppliers and vendors. This added visibility and control enables risk managers and procurement departments to better identify and more effectively address those risks that could impact overall business performance by disrupting the delivery and cost of a company's product and/or service.

The Accelerator utilizes sophisticated risk scoring technologies that are easily maintained by the business, to articulate and dynamically respond to corporate policy. It applies the scoring process to a range of information, sourced from multiple data repositories which are either automatically updated, or manually maintained, to proactively manage supplier risk.

The resulting supplier risk score, which represents the inherent level of risk in working with a supplier, can be utilized to make more informed and risk-based decisions. Supplier risk information can be delivered in a number of ways, such as across your source-to-pay process during a sourcing transaction, via email alerts, and through integrated supplier risk dashboards.

CONCLUSION

Corporations have no shortage of data available to them for managing supplier risk; the challenge is to source it on a timely basis, make sense of it given the context and volume available, and translate this data into high value information for decision makers to easily consume.

Having the inherent level of risk of a supplier readily available enables the procurement team to make informed choices between suppliers when making a souring decision. It also assists in broader strategic discussions related to the likelihood and potential impact of a failing supplier(s) on an organization's supply chain. This in-turn leads to the development and use of proactive risk mitigation strategies and contingency planning.

More information on Oracle's Governance, Risk, and Compliance applications can be found at www.oracle.com/grc .