

RISK AND THE CITY

Identifying, understanding and mitigating increasingly complex risk factors is the first challenge for procurement. Getting the right talent on board with the drive and experience to influence the decision-making process is the next

There has never been a more opportune time to instil a robust risk management strategy in multinational organisations. After all, a combination of economic meltdown and rampant globalisation means companies are increasingly vulnerable to failure. It's what Don Klock, former CPO of Colgate-Palmolive and professor of supply chain management at Rutgers Business School, refers to as a "perfect storm".

"What people forget is that this economy will turn around and those tight capacities will occur," he said at a recent *Procurement Leaders* roundtable event sponsored by BrainNet EAC. "If you think about some of those suppliers that have financial problems, they may cut some corners that you may not be aware of. It's a perfect storm."

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Klock was among 11 procurement executives debating risk management at Morgan's Hotel in New York City. And, while there was a wide cross section of industries present, the issues raised hit a nerve with all attendees.

So what are the risks that procurement organisations face and are in a position to influence? "I think of risk as much broader than supply risk," said Klock. "I think of currency risk, I think of capacity risk, I think of volatile commodities."

Patrice Knight, vice president of global procurement operations at IBM, added to that. "There are geopolitical risks, there are natural disasters, there are logistical failures and there are issues where

strategically you could be doing business with the wrong person. So it's much broader than what old-school procurement would look at. Globalisation has made you look much more broadly."

And the increasing complexity isn't just restricted to new areas of risk. The complexity of today's business world means that risks exist several tiers down the supply chain. "The environment we have now is so dynamic that when we look at supplier risk, I'm not necessarily looking at just their subcontractors or the relationships they have – I'm looking at their customer base," said Kevin Giblin, director of global procurement at The McGraw-Hill Companies.

So, it's clear that procurement functions have an extremely important role to play in managing risk – and not

just from a procurement and supply chain perspective, but from an overall corporate perspective. As such, CPOs should play a central role in managing and acting upon all types of risks when they are discovered.

"Fundamental to that is what level of risk is appropriate," argues Quentin Roach, chief procurement officer of Bristol-Myers Squibb. "Just because you identify an issue or a potential risk, it may be okay. What level of risk is tolerable for your organisation? Procurement has to play a big part in being at the table with the other executives in the organisation to make that determination."

IBM's Knight agreed. "You're in a far better position if a procurement person is influencing the [business] decision and is in to the line of business with the insights and supply chain knowledge that we bring," she said.

And William Hatzichristos, director of corporate procurement at the New York Mets, added that the secret to success was negotiation and compromise. "It's attempting to say, 'okay here's what procurement is doing, here's what sales should look at,'" he said. "And while I'm not telling them how to do their job, at least there's a framework and metrics they should look at. Then it's up to us both to make a decision on what type of risk or how much risk we want to assume."

Integrated role

Of course, saying that procurement should be intimately involved in all areas of the business is easier said than done, but Roach believes it's something procurement has to drive forwards. "It's a challenge that all of us have talked about, and it's how do you get procurement to be a more integrated part of the organisation," he said. "It's incumbent on the procurement department to integrate itself into the business versus asking the business to integrate us."

David King, director of global strategic sourcing at Air Products and Chemicals, said the key was to embed supplier risk management within all areas of the business. "A lot of the time, our primary client is the engineering group," he explained. "Engineers have their heads down doing engineering. We found in the environment where commodities were going crazy that some of these



people didn't even realise that steel had doubled or trebled in price. Only after numerous beatings was there some recognition around that."

Strategic process

Axel Schulte, partner and managing director of BrainNet, argued that the discussion goes beyond that of risk management. "It goes to the point of 'what is the role of procurement? And what is strategic procurement,'" he said. "Involving stakeholders, you don't only want them involved in talking about risk mitigation – you want them involved with sourcing decisions, demand management. It's all part of the strategic sourcing process."

Portraits: Ben Asen

Globalisation isn't the only contributor to a huge increase in risk. Over the past decade, procurement organisations have been keen to consolidate their supplier base to improve efficiencies. However, with that comes increased risk because if something goes wrong with a supplier it's likely to have an impact on a much wider scale.

A good example of this was the melamine scandal, which started life in pet food. Unfortunately, many western organisations were using the same Asian suppliers and it wasn't long before the melamine, which found itself into pet food, also found itself into milk, with well-reported and devastating results.

"When you look at the sourcing, obviously you need to think about whether you want to consolidate," said Robert Brown, chief procurement officer at Marsh & McLennan.

The consolidation of suppliers and the geographically disparate nature of modern supply chains are two of the biggest contributors to an increase in corporate risk. It's what James Martin, senior director of global sourcing at News Corporation, describes as the "Wal-Mart reaction" – organisation's looking at the success of the US retail giant in low-cost regions and jumping on the bandwagon regardless of the associated risk. ➡



Don Klock
Rutgers Business School

However, regardless of the motivations for the strategy, it follows that central to mitigating that risk is to ensure the right people are on the ground in the relevant regions of the world to provide early warnings of potential risk. “That’s a key issue for us right now – the geographical distribution of talent to mitigate risk in the supply base and also help support emerging market businesses,” said Frank Callaghan, senior director of worldwide procurement at Pfizer.

Skills deficit

Talent, as is often the case at roundtable discussions on procurement, was a central theme, with all the attendees agreeing there is a dearth of skilled

applications that are coming through that have been in procurement for years, but, when you’re looking at hiring to transform the organisation, they don’t have the skills.

King, agreed. “It really comes down to talent,” he said. “These are tough jobs to fill these days.”

The conversation soon turned to the practical measures and processes that must be put in place to support a robust risk management strategy. Sanjay Setty, director of ingredients procurement at Cadbury North America, described how his organisation meets regularly to run through potential risks. “We identify which are our top five or 10 suppliers at risk,” he said. “Every month we have a traffic light report that is reviewed by our head of supply chain and his direct reports.”

Giblin said Mcraw-Hill had a similar way of looking at risk. “We have a similar approach, even down to a red and green light approach to suppliers that look like they have a potential for risk,” he said. “We look at this proactively – [maybe] we’ve noticed a trend in a supplier’s financials, either there’s a downwards trend in sales, in employees or in profitability. Is this something we have to keep an eye on?”

The approaches for assessing risk differ from company to company – some have chief risk officers who manage it across the organisation, some establish cross-

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procurement employees who can do all of the basics as well as possess the more advanced skills such as risk analysis and the ability to influence senior leadership.

All attendees expressed concern that much of the current crop of procurement talent doesn’t have the expertise to reliably assess risk. The skills required of world-class procurement experts are now so myriad that finding the right people has become increasingly difficult.

BMS’s Roach, for example, has 25 openings available in his procurement function and simply can’t find the right people. “The things we are asking our people to do, frankly, there are very few people capable of doing them,” explained Roach. “I have 25 openings in our organisation today in my staff area and we’re having a significant number of

functional working groups which meet regularly, others embed robust processes which take account of risk at every stage of doing business. Some have a combination of some or all of the above.

But what was clear, is that risk management is one of the most pressing issues currently facing procurement executives and that successful risk mitigation is not an easy nut to crack. It involves getting the right talent on board, establishing robust processes, influencing senior management and calculating the right mix of risk and reward.

Only then will procurement executives have the right toolset to meet the demands of modern purchasing. [P](#)

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