



Supplier Relationship Management at Kraft Foods

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Introduction

- **In this session we will share how Kraft Foods defines and manages supplier relationships in order to:**
 - **Drive out costs**
 - **Optimize service quality**
 - **Uncover innovative business solutions**
 - **Leverage the full capabilities of its suppliers**

Agenda

- **SRM Definition and Business Rationale**
- **Elements of an SRM Program Structure**
- **Areas of Opportunity/Leverage**
- **Getting Started on SRM**
- **Implementation Expectations**
- **Questions**

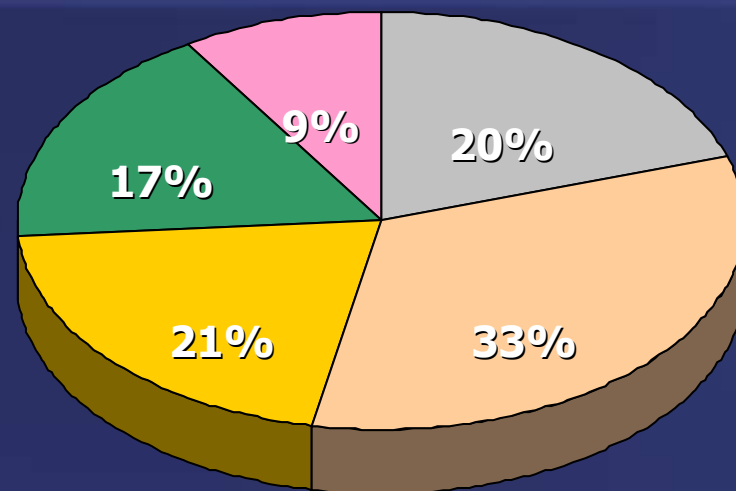
Business Rationale for Supplier Relationship Management (SRM)

- **Companies continue to look for ways to improve shareholder value**
- **Value can come from growth, innovation, service and improved cost effectiveness**
- **Leading edge Supply Chain Managers are now recognizing the importance of fully leveraging their suppliers to achieve their business goals beyond cost**

Why Improve Supplier Relationships?

- 80% of industry execs say that strong, effectively managed relationships with suppliers deliver **at least 25% greater value** than poor relationships with suppliers

Incremental value generated through strong working relationships with suppliers

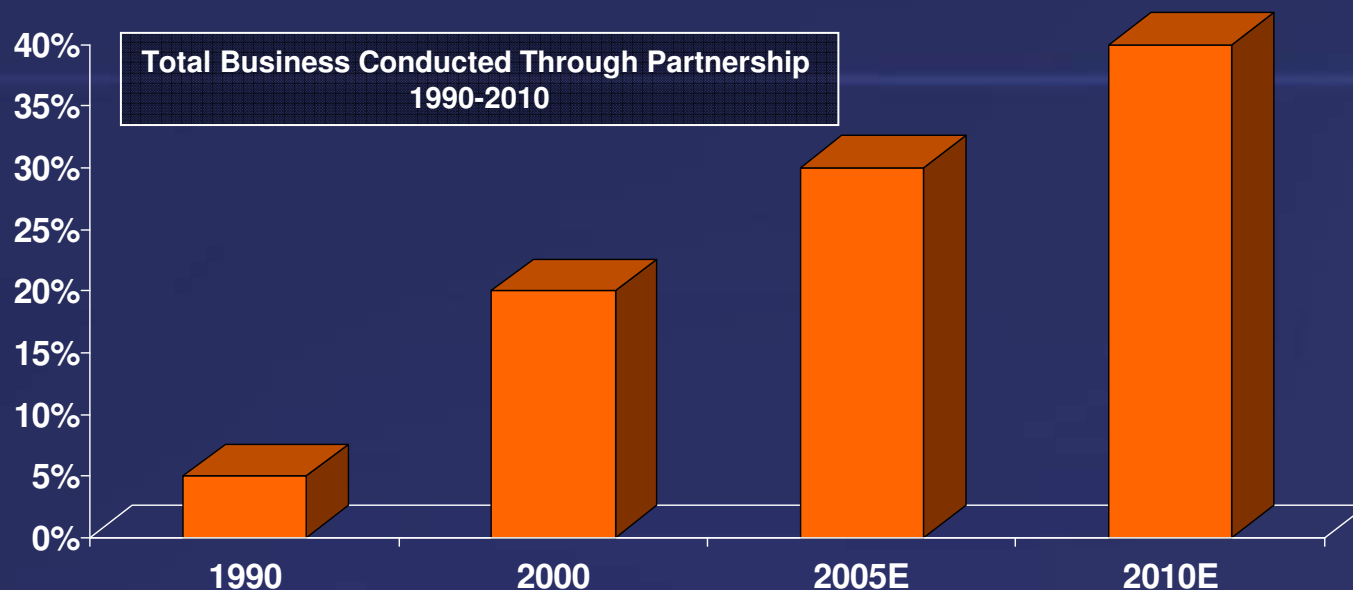


- 0-25% more value
- 26-50% more value
- 51-75% more value
- 76-100% more value
- >100% more value

Negotiating and Managing Key Supplier Relationships: A Cross-Industry Study of 20 Best Practices. Vantage Partners, 2003.



Utilizing partnerships as a fundamental part of their business models is a growing trend among top companies



A 2002 Institute of Supply Management study found that partnering with suppliers is one of only two important tools or solutions reported to be significant for the future of supply chain management and purchasing (the other is e-commerce)

Source: EDJ Global Executive Survey, Accenture Consulting, Warren Company



The main benefits of advancing supplier relationships are increased profit & revenue growth



Consortium Benchmark Survey, AT Kearney

% of companies citing benefits (unprompted). Based on interviews with over 200 companies from five consumer goods supply chain segments: raw material & packaging suppliers, finished goods manufacturers, third-part logistics and transportation companies, distributors, retailers.

So what is SRM?

SRM is the practice of determining, developing and maintaining the optimal business relationship with each supplier

- ... *determining* through a process which segments the supplier base to identify the appropriate relationship for each individual supplier
- ... *developing and maintaining* through recommended practices for
 - Customized relationship governance
 - Managing people and team interactions at all levels across both parties
 - Appraising supplier performance and when appropriate, joint relationship performance through development, use and reporting of metrics
- ... the *optimal business* relationship with each supplier enabling an ideal return on the resources invested in each supplier relationship

SRM Program Elements

- **Supplier Segmentation Methodology**
- **Performance Management**
- **Organizational Alignment**

Supplier Relationship Segmentation Methodology

- Developing a supplier relationship segmentation methodology allows you to determine the optimal type of relationship with each supplier
- The Relationship Segmentation Assessment (RSA) tool allows suppliers to be evaluated consistently with a pre-defined criteria
- The RSA process results in a recommended relationship type – *Transactional, Collaborative or Alliance*

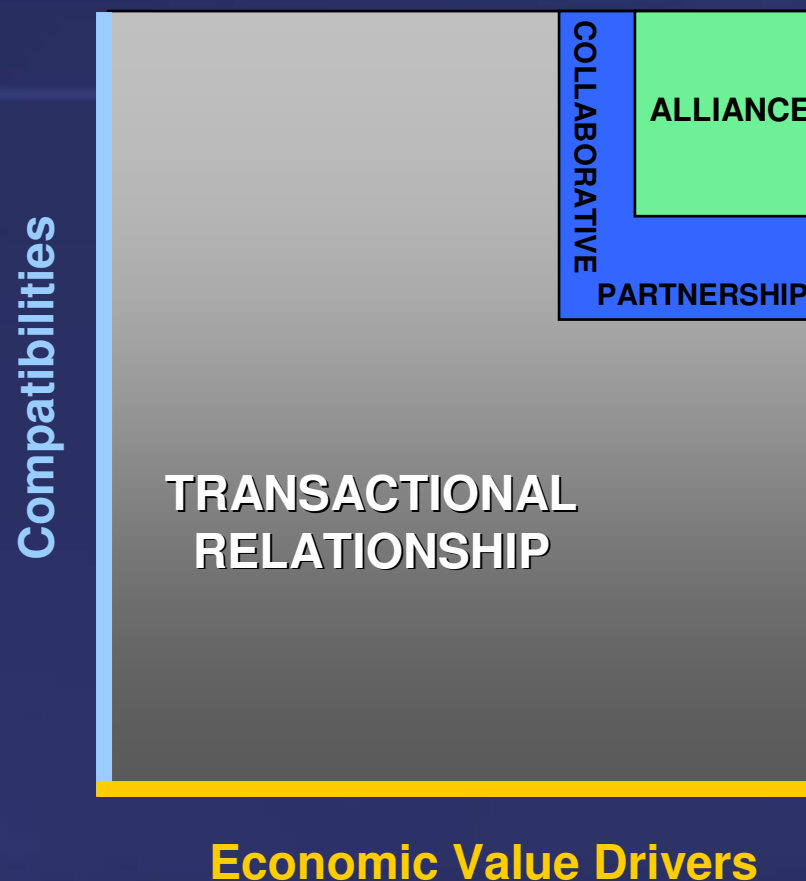
The RSA evaluates suppliers on 10 criteria

Economic Value Drivers

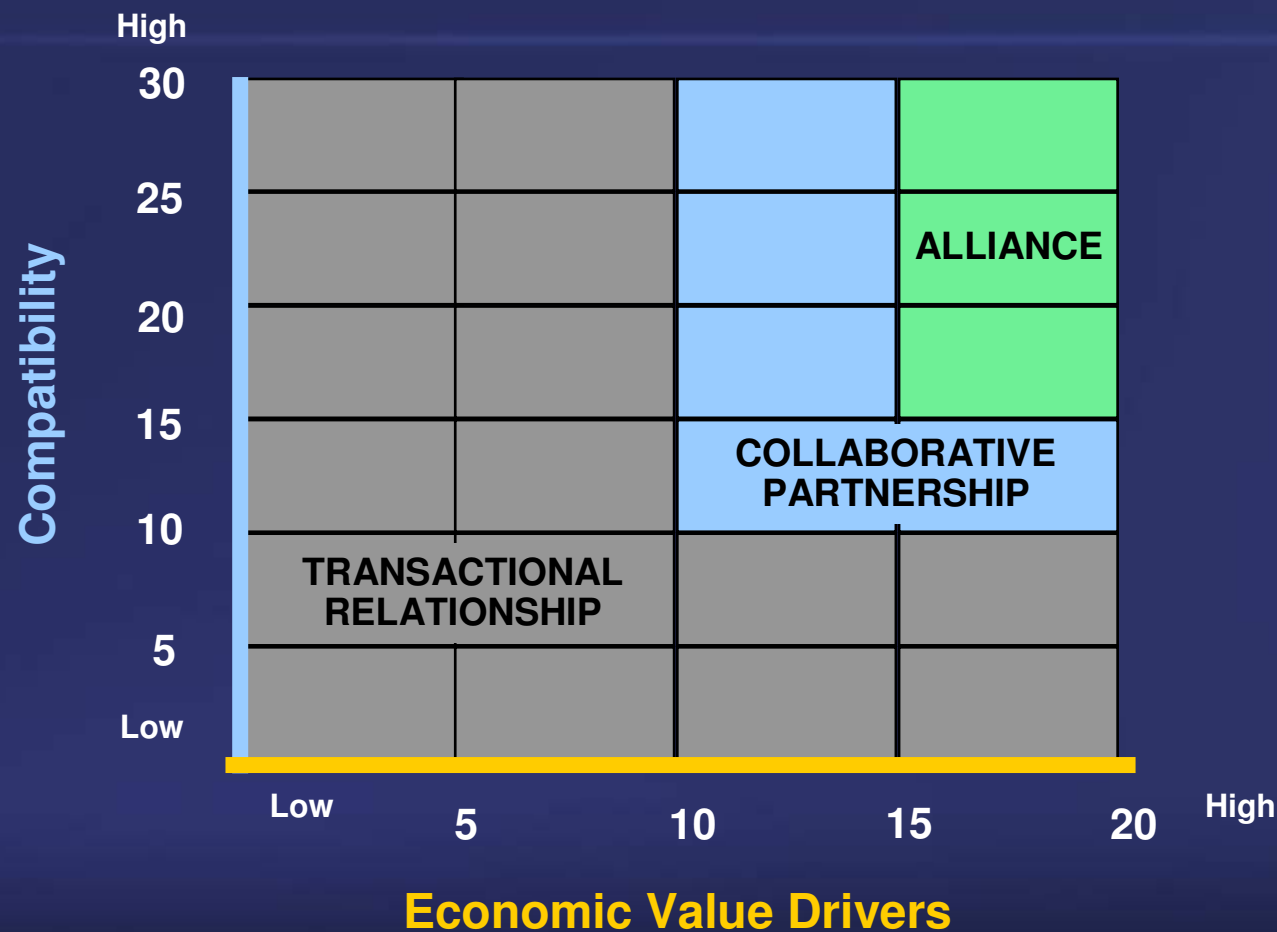
1. Company View of Category (spend, material/service complexity)
2. Total Supply Chain Impact (Cost & Value)
3. Innovation Potential
4. Supplier Risk Profile

Compatibilities

5. Supplier View of Company (potential, attractiveness)
6. Strategic Fit
7. Business Processes/Systems Fit
8. Geographic Fit
9. Assets/Resources Fit
10. Cultural Fit



The strength of the Economic Value Drivers and Compatibilities *segments* each supplier



Segmentation then helps determine the appropriate relationship

Alliance

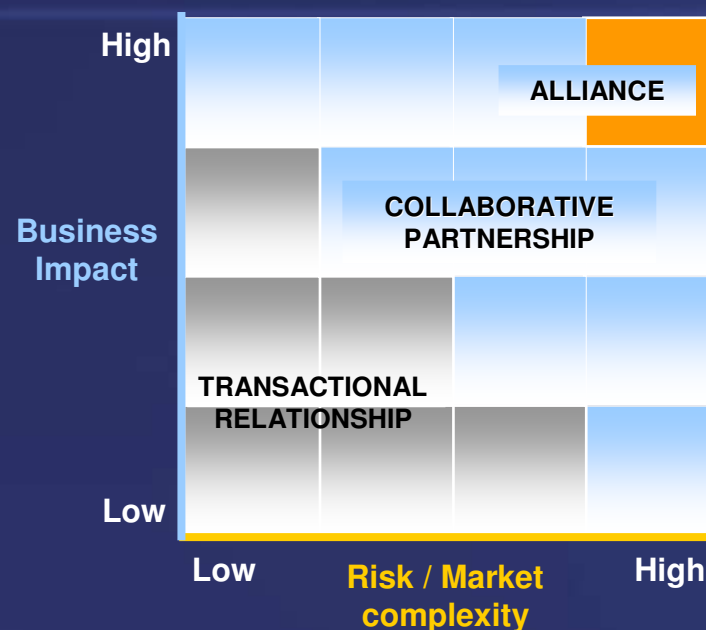
- Tailored business relationship with high level of integration
- Mutual trust, openness, shared risk and rewards
- High level of investment required
- Creates new forms of value, strategic competitive advantage
- Superior performance beyond what would be achieved w/o partnership
- Long term or perpetual time horizon

Collaborative

- Cooperative business relationship
- Varying levels of coordination of activities and planning on a limited basis
- Short to mid-term focus
- Moderate investment required
- Across a few divisions or functions within the two organizations
- Arm's length business relationship

Transactional

- No joint commitment or operations
- No investment required
- Standard products, services, terms & conditions
- One-time exchanges, ending with current exchange



Performance Management

- **Create an SRM measurement framework**
- **Create library of SRM metrics/KPIs**
- **Develop guidelines for developing, using, and reporting metrics jointly with your suppliers**
- **Determine metrics systems and IS/IT tools that best support SRM practices**
- **Manage metrics with cross-functional leadership**

Metrics are defined to predict, measure & manage outcomes

- **Predictive Measures**

- Identify problems (early)
- Enable root cause diagnosis of problems
- Facilitate corrective action

- **Outcome Measures**

- Measure results delivered by suppliers
- Reduce costs and improve quality of, sourcing and supplier selection decisions
- Guide supplier investment decisions
- Guide SRM investment decisions

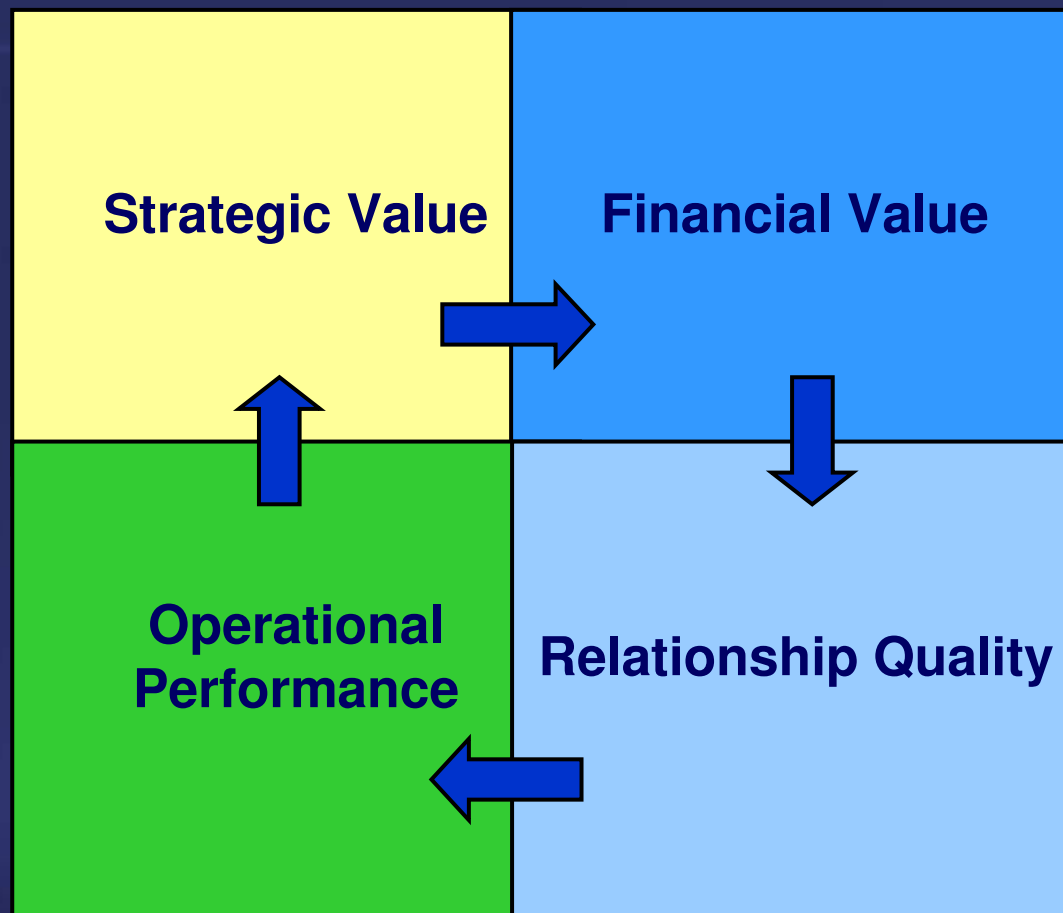
- **Value of Outcomes**

- Validate importance and value of outcomes in relation to the company's business strategies

Evaluating the value of a supplier partnership requires metrics beyond Operational Performance

- **Operational Performance** – traditional area of emphasis
- **Strategic Value** – tying metrics to align with a company's strategies (i.e. geographical expansion)
- **Financial Value** – tying Operational and Strategic metrics to Financial value. This requires the development of metrics to measure results of strategic partnership activities and innovation, which is not always easy to do (i.e. revenue)
- **Relationship Quality** – important to be able to measure the quality of relationships with suppliers to drive better business results (i.e. ease of doing business)

A Total Value Scorecard integrates all four areas of measurement to fully leverage the value of the partnership



Organizational Alignment

- **Organizational Alignment is critical for a strong SRM program to drive alignment and buy-in**
- **Communication materials and schedules need to be developed for stakeholders**
- **A Communication strategy determines and outlines the best methods to educate the organization on SRM and its potential value to the organization**
- **Relationship Manager needs to be appointed**



Opportunity Areas Possible Through SRM

- **Provide leading edge technology**
- **Advance innovation**
- **Reduce material costs**
 - Harmonize specifications
 - Improved material quality
- **Reduce or avoid capital spending**
 - Improve equipment effectiveness
 - Improve equipment capability and efficiency
 - Lever low cost country assets
- **Improve energy efficiency**
- **Streamline internal processes**
- **Reduce transportation and storage costs**



Innovation - Product Enhancements

What was done?

- Commercialization of Snack-n-Serve - a patented packaging system with an innovative re-close feature
- Launched in Jun'05

What was different?

- Supplier involvement from the beginning
- Primary supplier worked with their supplier and included Kraft
- Seamless, open information sharing on all aspects, including cost
- Business accepted initial cost increase, with an aggressive plan for Next Generation reduced cost

What resulted?

- Consumer benefits: re-sealability, ease of opening and increased product freshness
- High level of consumer praise, >200 in 10 months (1 SKU)
- 5% incremental growth for CA! Chewy
- 1 patent granted; 5 addl. applications pending
- Exclusivity in perpetuity for the cookie category



SRM Scorecard

- | | |
|--|---|
| - Use suppliers' expertise and resources earlier | ✓ |
| - Move to non-prescriptive approach | ✓ |
| - Clarify roles, responsibilities and upfront | ✓ |
| - Enforce Go/NoGo disciplined decision making | ✓ |
| - Align expectations with joint metrics | |

Innovation - New Market Entry

What was done:

- SRM Collaborative partnership was developed with packaging material supplier
- Several innovation sessions were held in Brazil, Mexico, Argentina, and Costa Rica
- Alignment was gained and joint business planning was achieved between top management at Kraft and Supplier
- Multi-country/plant scorecard was implemented in Latin America

What was different?

- Great focus on Kraft innovation needs; greater level of information sharing
- Cost-in-use model to support plants
- In-house quality/planning/pre-print support

What resulted?

- New products introduced
- Development of affordable packaging formats to enable Kraft to enter and better compete in the NE Brazilian market



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Innovation - Improve Competitive Edge



What was done?

- Collaborative joint development and commercial framework has resulted in new joint and Kraft patent filings
- Joint developments resulted in new high foaming creamer in coffee mixes that can meet competitive threat globally

What was different?

- Ensuring good cross functional alignment from the start paved the way
- Joint development agreement with 2-way confidentiality
- Significant capital investment by supplier on Kraft's behalf
- Commitment to purchase for 5 yrs (longer than usual)
- Joint development resulted in jointly owned patents (pending)
- 'On the spot' rule for decision-making in cross-functional Steering Team sped-up the process

What resulted?

- Improved product in market in UK/FR/Germany
- 4 patents pending (2 joint and 2 Kraft owned)
- Rights of exclusivity for Kraft and preferential access to supplier capacity
- Right of first refusal to new technology innovations

Coffee Mixes

13mm foam
height



25mm foam
height



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Leading-edge Technology

What was done?

- Introduction of Fast Franks: Delivering on consumer convenience with a quick and easy to use product that creates a warm, fresh bun in the microwave
- First time a hot dog and bun packaged together with shelf life > 10 days

What was different?

- Supplier involvement from the beginning: Oscar Mayer invited supplier to join their Fast Franks development team
- Supplier shared technology, to translate the concept into a marketplace reality
- Combining the tray from supplier and the proprietary dough technology from Kraft made the product a success and protected it from competitors

What resulted?

- Launched nationwide in the USA, Oscar Mayer Fast Franks are available in 2 SKU's
- Consumer benefits of soft and warm bun texture without over drying or wet spots in an easy to open packaging
- Delivery of a fresh bun with long shelf life (75 – 90 days)



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Transportation & Storage Cost Reduction



What was done?

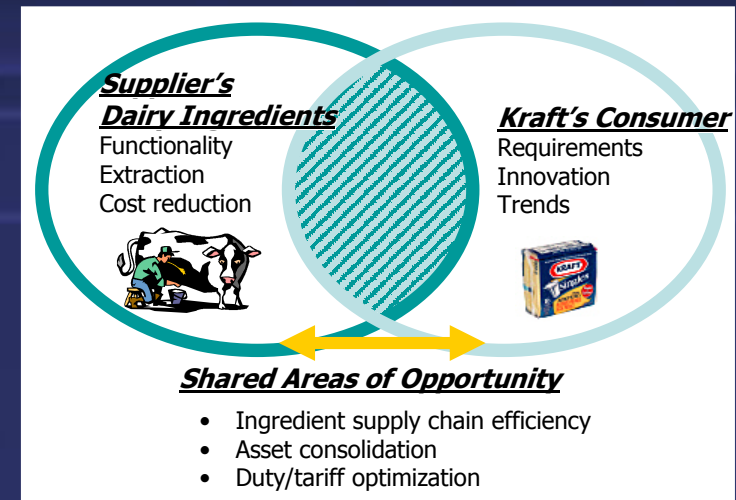
- Kraft/Supplier team targeted supply chain simplification as a key value generating opportunity
- Goal was to eliminate redundant costs and working capital

What was different?

- Detailed supply chain information was shared between Kraft and supplier to develop joint process mapping
- Integrated transportation services to optimize rates, reduce repositioning/dead head costs, and eliminate redundant inventory
- Enabled direct plant shipments from port to Kraft plants for 85% of volume
- Eliminated Kraft buffer warehouse and bypassed supplier buffer for all volume except 15% safety stock held by supplier
- Optimized ingredient packaging systems to minimize direct costs

What resulted?

- Uncovered incremental joint cost saving > \$3MM annually
- Built trusting foundation for further collaboration in other areas, including supply chain restructuring



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Leverage Low Cost Country Assets

What was done?

- Developed North America Application Support Outsourcing Strategy to utilize low cost country (India) assets for legacy system support applications
- Benchmarked with other companies including incumbent supplier to ascertain optimal internal / external ratio along with onsite / offshore mix

What was different?

- Supplier owns day-to-day context work and staff requirement; managing to Service Level Agreement (SLAs)
- Kraft-retained staff manages governance efforts along with high-level Subject Matter Expertise (SME); non-retained Kraft staff redeployed to value-add core work
- Migration from price-only focus to Managed Service Model, including productivity and cost avoidance

What resulted?

- Partnership approach to supporting applications
- Reduced Kraft day-to-day context work
- Leveraged supplier expertise in managing application support
- Several million dollars of saving over 5 years



SRM Scorecard

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Energy Reduction

What was done?

- Implemented a Value card to reflect the total value delivered beyond pricing
- Tracked speed to market and assigned value
- Sustained Energy Reduction Initiative
- Asset reliability program

What was different?

- Moved away from price-only focus to total value, including productivity, cost avoidance and stretching capital
- Supplier has employees at Kraft locations, actively engaged in teams
- Supplier investments made on Kraft's behalf

What resulted?

- Value card is a unique way to measure total performance against goals
- Transformed US contract into a global plain language master terms contract with geographical variations



SRM Scorecard

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Getting Started on SRM

- **Assemble a Cross-functional Task Force**
- **Consult with industry experts**
- **Select key suppliers to pilot your program**
- **Consider technology needed to support your program**

Task Force

An SRM Task Force should include:

- **Representation across all divisions of procurement**
- **Representation from appropriate stakeholders (e.g. R&D, Quality, Manufacturing, Engineering)**
- **Representation across all appropriate regions and/or countries**
- **Organizational development resources to facilitate change management within your organization**

External Expertise

Consider utilizing a consultant to provide:

- **Industry expertise**
- **Proven tools and templates**
- **Team facilitation**
- **Focus**
- **Speed**

Supplier Pilots

Supplier Pilots can be used to:

- **Demonstrate to the organization the “real life” application of SRM work**
- **Apply, refine, validate or further identify best practices, processes & tools**
- **Advance our understanding of performance metrics process**
- **Test and evaluate online performance measurement software/technology**
- **Refine recommended processes to advance supplier relationships**
- **Serve as proving grounds for new ideas developed by the Task Force**

Implementation Expectations

Sponsorship / Staffing

- Ensure have executive level sponsorship
- Focus a dedicated staff to drive the program from design through integration

Legal Protection

- Plan to work through contract/legal position issues to simplifying supplier interactions
 - Intellectual property practices
 - Exclusivity and first-to-market provisions
 - Indemnifications

Change Management

- Assume you will encounter barriers from existing paradigms and/or past practices
- Expect resistance to working with suppliers differently
 - Comfort with sharing/partnering
 - FROM "us vs. them" TO "partnerships"

Likely Current-state Scenarios

- **Supplier decisions have been generally based on price of goods with little attention to total cost or growth**
- **There are likely many ad hoc roles and responsibilities for working with suppliers**
- **Supplier performance metrics are inconsistent, functionally determined and focused on short-term results**
- **It is likely that there is currently only fragmented data that is manually processed via multiple systems, varying by supplier and stakeholder**

Anticipate program development to take time, as it is a culture change and a journey

		Year 1				Year 2				Year 3				Year 4								
Program Development	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Supplier Segmentation Methodology																						
	Design				Implementation																	
SRM Segment Business Processes	Strategic Alliance																					
			Collaborative Relationships																			
					Transactional																	
Supplier Collaboration & Interface IS/IT Tools	Supplier Performance Tracking																					
			Company/Supplier Portal																			
			Supplier Knowledge Mgt Tool																			

Summary

- **SRM equips the Supply Chain with a framework for effectively partnering with suppliers to the mutual benefit of all parties - company, suppliers, customers, consumers and shareholders**
- **While companies will always be mindful of costs, SRM enables a greater focus and drive value beyond cost reduction, particularly focusing on innovation and speed**



