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INSIDE SUPPLY MANAGEMENT

Cooperation Brings Profitability

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Tapping Into ... Competitive Advantage — Suppliers Yield Innovations

More and more organizations are discovering that suppliers can be used as a strategic source that gives them a true competitive advantage.

Ask virtually any CEO about his or her top corporate priorities, and invariably growth and innovation are at the top of the list. But even at a time when supply management is beginning to gain inroads to the C-suite, few have fully explored the potentially rich territory of their supply chain to reap innovative rewards.

Considering that many times, 50 percent or more of the corporate budget is expended on suppliers, suppliers represent one of the most influential means of creating value and competitive advantage. However, because suppliers have traditionally been seen as "vendors," their potential as innovation partners has often been overlooked, and thus undervalued.

Today, companies can no longer afford to simply adhere to traditional thinking. Supply management must face the ultimate reality that a company cannot cost-cut its way to long-term prosperity. And worse, in numerous instances, wholesale hacking of suppliers has resulted in a severe diminishment of the supply base, leaving fewer options and alternatives. In addition, global competition is forcing companies to recognize that they must double, and even triple, their innovation output if they are to remain competitive. More and more, executives are invariably coming to the conclusion that in a fast-moving, rapidly changing world, the most sustainable source of competitive advantage is collaborative innovation.

Innovation is the most effective strategy for combating competitors with low price structures because it gives rise to a wide range of new options, including new technologies, process improvements, new business models and access to new market opportunities. In short, innovation from the supply base is a strategic initiative that impacts both revenues and profits.

The Battle of Value Chains

As a strategic issue, supply chain innovation should be an executive committee issue, directly faced not only by supply management, but also by marketing, operations and finance. Ultimately, any organization must deal with the fundamental issue of how to deliver value and create competitive advantage in the marketplace. No one company is an isolated element. Each is part of a value chain, which is a systematic approach to examining the development of competitive advantage first written about by M. E. Porter in his book, Competitive Advantage (1980). The chain consists of a series of primary and support activities that create and build value, culminating in the total value delivered by an organization. In the larger scope, winning the competitive game is a question of how to create an entire value chain that is more competitive than that of other rivals. This cannot occur if the relationship with both our suppliers at the sourcing end of the value chain and the customers at the sales end of the chain is adversarial. A collaborative relationship with primary suppliers and customers is essential if innovation is to flow and flourish.

Too many of our current business and economic models are founded on the view that commercial enterprise is based on independent stand-alone organizations. This can be misleading. A new order of thinking must be established that carefully and critically examines the premises of our currently accepted wisdom, and challenges its presumptions.

The importance of new ways of thinking is substantiated in a recent study conducted by The Warren Company's Engines of Innovation group, which concluded that the best companies regarding innovation across business boundaries have undergone a deep rethinking about their core business, which includes the following.

Internal versus inter-organizational business models. The best companies see their business as part of a more interconnected value chain or network and create a strategic system for creating, aligning and managing the creation of value. This involves a very intensive rethinking of what value means to their businesses and to their customers, and is clearly communicated into the supply chain.

Strategic value of suppliers. During the last 50 years, spending on outside suppliers rose from a paltry 20 percent of total organizational expenses, to nearly 70 percent (in some cases, more) of expenses. This fundamental shift has made what is now called "supply chain" a major strategic issue that has not been effectively addressed by scholars or businesses. Too many organizations still treat suppliers as "vendors," reflecting an old-fashioned mentality. The best ones segment their suppliers into at least two categories — strategic suppliers and commodity suppliers, the former receiving special attention for the co-generation of innovation streams.

Power of collaborative innovation. As innovation becomes more pivotal in business decisions, and suppliers more critical to the generation of value, the best companies create more effective strategies, architectures and models for cooperative creativity than what has been relied upon in the past. The best companies recognize that collaborative innovation is one of the most powerful means of creating new ideas that impact revenues as well as expenses. They recognize that differentials in thinking are the primary source of innovation, and this can only come from having a broad series of alliances both internally and externally. Here are some of the areas that can benefit from collaborative efforts:

- **Negotiations and risk management.** Current models for cross-corporate negotiations, contract management and risk management are based on shedding risk, maximizing value for one party while minimizing for the other and managing relationships tactically or transactionally. These methods have a diminished or even negative impact in a fast-moving, interconnected world when applied to both primary suppliers and customers.

- **Revenue impact of suppliers.** The flow of innovation from suppliers can have major impacts on revenue as well as cost for the modern enterprise. A strategic review of this impact is essential. The best companies look deep into their supply base for new ideas, products, technologies, services, solutions and business models that could enlarge their top line. Supply management links with R&D and marketing to explore these possibilities.

- **Impact of critical drivers of competitive advantage.** With the change in the driving forces of competitive advantage, where the traditional drivers based on size, positional or transactional power and financial clout have been superseded by speed, aligned or collaborative power, and innovative agility, a new model of competitive advantage is essential. (For an example, visit www.enginesofinnovation.com.)

Addressing the issue of innovation means creating a much clearer understanding of the nature of innovation than the old adage that "invention is a flower, and innovation is a weed." Fundamentally, there are six types of innovation, each having its own intrinsic value. The six variants each have a vital role to play in the supply base, and companies must be aware of their different strategic impacts in creating competitive advantage:

1) technology invention (for example, patentable);
2) product improvement and design;
3) systems solutions and integration;
4) process improvement;
5) new business models;
6) market extensions; and
7) socio-organizational relationships.

What makes this seven-dimensional model of innovation attractive is that it empowers nontechnical people to engage fully in all but one of the types of innovation.

How the Value Network Beats the Competition

When collaborative innovation networks are pitted head-to-head with legacy supply chain models, the value networks win time after time. It is important to understand why. Our research and operational experience has shown there are a number of reasons, the most important of which is collaboration. A cooperative system enables strategic alignment, flow of innovation, mutual interest and speed of decision-making. These factors eliminate or reduce non-value-added friction costs in the business system, thus enabling greater profitability, long-term planning and investment horizons, integration among network entities and better flow of useful information within the network.

Strong, visionary leadership is required in such a situation, as well as the ability to interact at the senior levels of the members of the value network. But good intentions and eloquent words are insufficient. A powerful system based on collaborative relationship-building best practices, along with powerful championing skills, will be required to make the mind-set shift, the culture shift, the strategic shift and the operational systems shift together to benefit everyone.