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The New CPO



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THE CHANGING ROLE OF THE CPO

Purchasing used to be a boring function that most companies took for granted; it involved a lot of transactional work and tedious repetition—important activities for day-to-day or even moment-to-moment operations, but not critical to the organization’s overall planning and financial performance.

Anyone with basic negotiating skills could manage procurement, it was often said; deeper strategic thinking and serious deal making took place elsewhere. For a nine-to-five, it wasn’t a bad way to eke out a living. For an ambitious businessperson, however, purchasing was nothing but a dead end.

But that’s all changed. The growth in outsourcing, the drive for efficiency, and the dramatic cost savings that can be delivered by well-managed supply chains and pricing analytics have transformed purchasing into a strategic function in many companies. The best of them now view procurement as a potential asset, one that is as important as research, product design, finance, and marketing. These companies realize that many of the questions

that executives must answer correctly to succeed in today’s commercial environment are intimately and directly linked to purchasing: What work should we farm out? What work should we keep? With what companies should we partner? How many suppliers should we have? What should our relationship be with our suppliers? All of these strategic questions now fall squarely on the desk of the chief procurement officer.

Of course, recognizing that the procurement department is not the career backwater it was once considered and capturing the significant strategic and financial value embedded in this function are two different things. Indeed, to profit from an elevated respect for procurement, many companies will have to undo decades of bad habits in the recruitment, training, and devel-

opment of their purchasing professionals. No longer can they afford to place competent but unimaginative people in these jobs. Nor can they afford to ignore their current procurement staffers by offering them few chances of advancement and neglecting their skills.

Hiring the merely good is not enough for organizations that want to build world-class purchasing departments. Instead, they must make stellar appointments—filling the senior procurement jobs with people who can become tomorrow’s top corporate leaders. Managerial talent of this caliber doesn’t develop by accident. Businesses hone executive abilities by identifying and encouraging promising individuals and providing them with the right opportunities over years, even decades.

Slowly but inexorably, the programs that are needed to develop top purchasing executives are being implemented at more and more

organizations. In fact, procurement managers themselves evince a budding sense of optimism about their prospects, a sharp change from prior, gloomier assessments. In a recent Booz & Company survey of 100 CPOs and supply chain management leaders, 66 percent of respondents said the CPO will play a larger role in setting business strategy in the next five to 10 years, and 44 percent of respondents said activities in the purchasing department will be a top priority (see Exhibit 1). The general conviction in the executive suite seems to be, as one respondent put it, “Procurement needs to be more strategic—closer to the CEO agenda.”

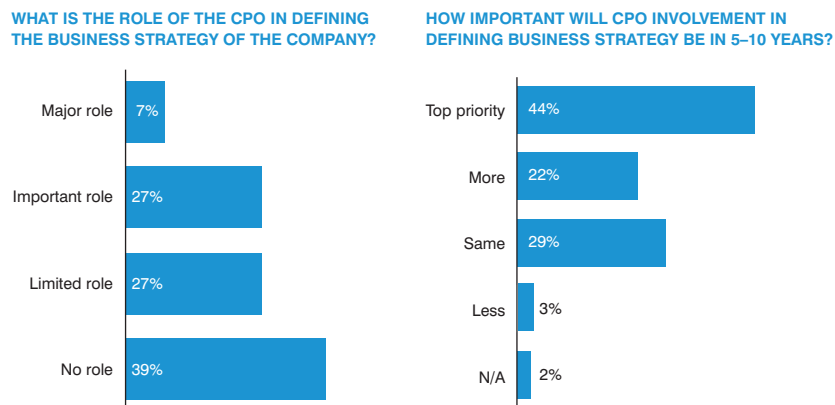
This suggests that although it will continue to be important for the purchasing professional to have functional expertise enabling him or her to get the best deal on paper clips (as well as to leverage more value from the entire supply base), strategic capabilities, political savvy, and leadership talent are increasingly

important priorities and prerequisites for CPOs. In fact, our survey revealed that 46 percent of senior purchasing executives believe that strategic understanding and overall business sense will be the most important traits for purchasing managers in the future. Meanwhile, two traditional measures of purchasing professionals’ functional expertise—their ability to manage supplier networks and their understanding of the products or services they are buying—weren’t rated as the top priority by even 5 percent of respondents (see Exhibit 2). The challenge for tomorrow’s procurement officers, noted one CPO, will be “setting the strategic agenda through growth and innovation.”

Companies determined to develop a new generation of corporate procurement leaders—while maintaining a competitive supply chain—should take five steps in particular:

1. *Recruit from top schools.* The bad news is that, by and large, companies

Exhibit 1
CPO Role in Business Strategy



Source: Booz & Company

have not bothered to seek out the best and the brightest for purchasing; most recruiting has historically been internal. The result, of course, was a self-fulfilling prophecy: Second-tier candidates couldn't raise purchasing to a strategic competence, and their underperformance seemed to justify the function's relegation to a supporting role. If procurement is to achieve its promise, companies must seek out top performers to fill these jobs.

The good news is that the level and quality of purchasing talent is rising. Responding to the new demand, some top business and industrial management schools have added purchasing to their curriculum. For example, Helsinki University of Technology, a forward-thinking business school whose students consistently beat their European and American peers in international business case competitions, recently added a purchasing and supply management curriculum within its industrial management major. The

university developed the innovative course of study with the support of leading Finnish corporations.

2. Pay a competitive salary. The growing corporate realization of the enormous business impact that procurement can create has stimulated healthy increases in the earnings of procurement and supply chain professionals. The magazine *Purchasing* reported in December 2007 that on average, U.S. purchasing professionals earned US\$84,611, up from \$64,300 in 2002—a 30 percent increase in five years. In the United Kingdom, purchasing directors' compensation rose steeply as well—to £76,000 (\$157,000) in 2007, up a full 14 percent from the year before, according to a survey conducted by the Chartered Institute of Purchasing and Supply and compensation experts the Croner Company.

Underpaying for purchasing executives in such an environment is a penny-wise, pound-foolish strategy. Worse, an insistence on clinging to old

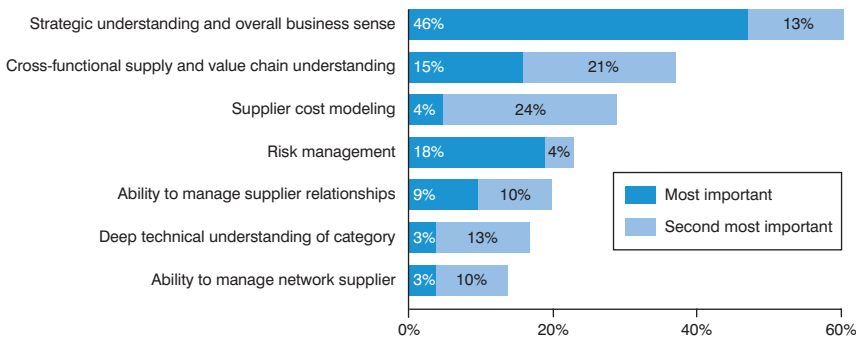
pay scales—that is, not paying purchasing executives on par with other top managers—will simply ensure that the company hires the same old kinds of individuals, only worse.

3. Rotate functional assignments. It is essential to the development of future purchasing leaders that they obtain the widest possible training and experience within the organization. Leading corporations already routinely move executive candidates from one job to another to broaden their knowledge of overall operations. At IBM, for example, the most promising purchasing employees may spend a few years in finance, market intelligence, or even global services before being shifted back to supplier management. Similarly, Nokia's procurement rotation plan gives its purchasing staff a taste of what it's like to deal with different types of expenditures or categories of supplies and services.

Rotation programs not only create new opportunities for the individual

Exhibit 2
The Importance of Future Capabilities

WHICH TWO OF THE FOLLOWING CAPABILITIES DO YOU BELIEVE WILL BE MOST IMPORTANT FOR PURCHASING PROFESSIONALS IN THE FUTURE?



Source: Booz & Company

procurement executives but also benefit the company. Two- to three-year rotations infuse fresh blood and new ideas into the top purchasing ranks, prevent the development of counterproductive personal relationships between buyers and suppliers, and reduce the risk that bottlenecks will arise from relying on a limited number of experts who specialize in buying an even smaller number of products and services.

4. Revise and expand training. The training required to function effectively as a purchasing officer is much more complex than it was just a few years ago, because it must include both traditional purchasing expertise and broader financial and managerial skills.

Procurement professionals still need such core skills as negotiation techniques, supplier market analysis, and cost modeling, but training programs involving these once-basic skills often require revision as the field of purchasing becomes more advanced and challenging. For example, traditional cost modeling involved little more than short-term analysis of commodities markets to lock in prices over perhaps a three- to 12-month period. But these days that's only the beginning. CPOs

now must be adept at macroeconomics and have wider corporate finance skills to manage futures, puts and calls, fixed contracts, and other strategies and instruments that are designed to cover purchases over many years. CPOs increasingly need the financial acuity to accurately forecast supplier prices 24 months out or more so they can make better decisions about long-term contracts for oil and other commodities or the raw materials that should be used in their company's manufacturing processes and products.

In some industries, such as the airline industry, the last few years have demonstrated that the cost management of a key commodity like fuel oil can sometimes be the key not just to profitability but also to corporate survival. For example, with long-term hedging of more than 80 percent of its energy costs, Southwest Airlines avoided the turbulence many airlines suffered when jet fuel prices nearly tripled between 2002 and 2005.

To help develop the broad areas of expertise that procurement officers need to thrive in the new purchasing environment, companies should turn again to top business schools for general management training.

5. Create career paths for purchasing talent. Ironically, although capabilities training is an investment that yields a higher return in the short term, it's also one that carries a greater risk to the department. Equipped with a wider array of skills and more expertise, purchasing professionals will find it easier than ever to leave their companies for better opportunities—and high industry turnover rates suggest that these budding executives aren't shy about taking advantage of new offers.

To prevent such a brain drain and ensure that companies and individuals are capturing the full potential of their purchasing talent, it is essential that companies offer concrete and compelling career paths for procurement professionals. To determine which procurement executives deserve special treatment, human resources departments should build into performance appraisals and measurement the new set of skills needed by purchasing managers, such as a higher degree of financial acumen and finely honed strategic thinking. Moreover, the company must reward procurement officers who meet certain cost and delivery targets with greater compensation.

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The purchasing department should be viewed as a training ground for senior corporate positions. If the anecdotal evidence is any indication, the best senior purchasing officers are fully capable of filling those spots. For instance, Richard Purcell, former Microsoft CPO, is now chief executive officer of the Corporate Privacy Group, a consultancy on business privacy practices. And Pekka Ojanpää, after only a year as CPO at Kemira Oyj, the leading chemical supplier to the pulp and paper industry, was named president of its Kemira Specialty division. In February 2008, he was named president of Kemira Water.

Some might argue that thinking of well-trained and innovative purchasing managers as indispensable talent

assets is a short-term phenomenon that will generate only a modicum of real change within most organizations before it disappears. But we see the rising need and desire for highly skilled purchasing professionals as a lagging indicator in the long-term trend of supply chain revolution. Over the past 30 years, business thinkers have become increasingly aware of the crucial role that the supply chain plays in corporate success. Yet even as they realized that the supply chain was a profit engine, executives and purchasing professionals alike remained oddly unaware of the purchasing department's contribution to the efficiency of that engine. It is time for both smart companies and smart purchasing professionals to adopt a new perspective.

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