Competitive Supplier Development Approaches in State-owned Enterprises (SOE)

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public enterprises
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Global expenditures on infrastructure

South Africa is not alone in investing heavily in infrastructure.

- China is projected to spend over a thousand billion dollars in infrastructure between 2006-2010

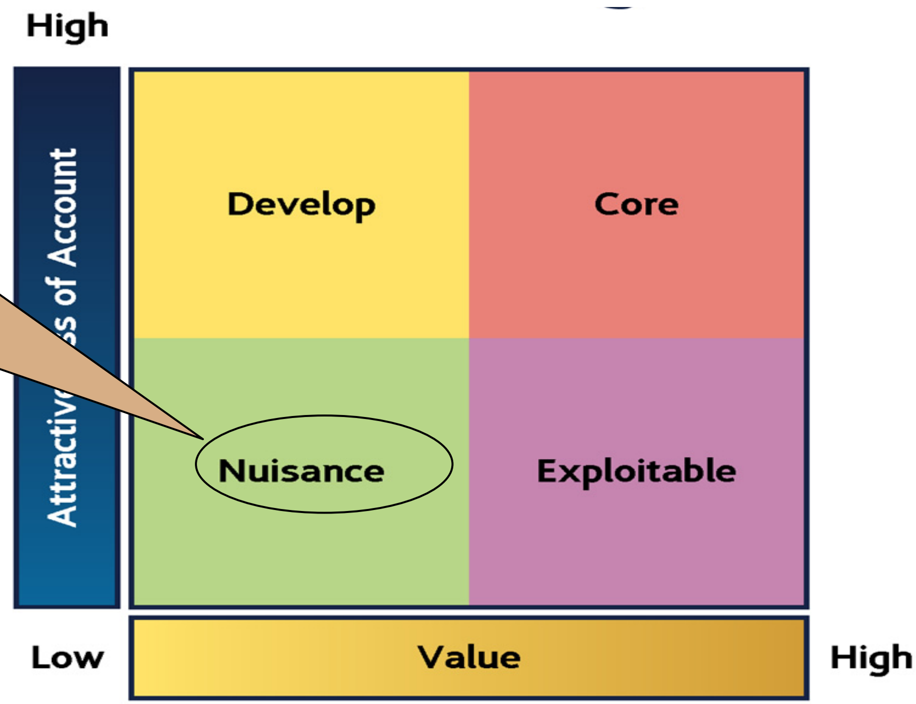
- India's infrastructure expenditure is also increasing dramatically

- Many other countries are investing in new power generation capacity

Supplier power

In this global context, SOE buyers face a significant risk of being seen as a nuisance by leading global suppliers.

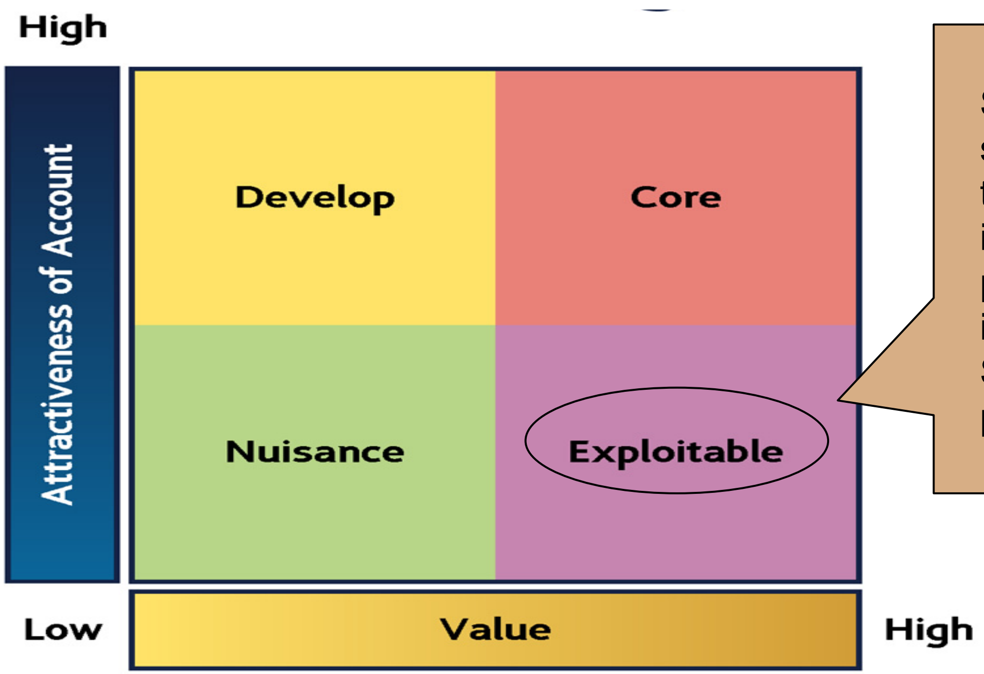
Particularly problematic in strategic requirements areas (high value, core to business)



A procurement strategy merely based on imports has significant risks and may be short-sighted. . .

SOE and supplier industries

While local suppliers, coming from a history of unpredictable demand and imports have an opportunistic attitude to SOE relationships.



Suppliers focused on short term gain, rather than long term investment and productivity improvement despite SOE purchasing power.

Although the SOE's wield market power, it does not mean they will be seen as customers of choice. . .

Advantages of competitive supplier development to SOE

In the current context of huge global demand for infrastructure and shortages of certain items, SOE have a commercial interest in the development of internationally competitive local supply industries, in order to secure supply and reduce costs.

Other potential advantages to SOE of securing local supply:

- decreased forex related risks or premiums
- proximity of suppliers (particularly for services and fast moving items):
  - speed of delivery
  - lower inventory requirements
  - improved access to skills
  - cluster advantages, eg collaboration, innovation around local requirements
  - greater responsiveness

A key caveat - price premiums

Price premiums could crowd-out investment amongst SOE's customers while encouraging unsustainable investment amongst SOE suppliers.

Price premiums paid to suppliers for local content

increased costs

Increase in prices charged by SOEs for services

Crowding out of investment in customer industries – negates goal of increasing growth and job creation

→ The objective must be to build the competitiveness (in terms of quality, cost and responsiveness) of local supply industries, not to pursue local content at all costs.

The importance of procurement

The essence of the CSDP is to procure in such a way as to create a conducive environment for investment in supplier industries.

Why is procurement so important?

- The more coherent the customer, the more coherent the supplier
- The competitiveness of the buyer is inextricably linked to the competitiveness of its suppliers
- Investment decisions are based on assessment of future demand → short-term planning by the customer will lead to short-term planning by suppliers
- Better long-term planning and standardisation can create the economies of scale required for investment in supply industries
- The quality of supply industries depends significantly on the quality of major buyers' demand planning and the quality of major buyers' management of procurement processes and supplier relationships
- The development of internationally competitive exporting capital equipment industries associated with the mining industry provides an example of the potential effect of long-term collaborative relationships between buyers and suppliers

Supplier Development Plans

Under the CSDP Transnet, Eskom and PBMR have produced plans to develop their local supply base, based on an assessment of opportunities and constraints. These plans have been approved by government.

The Supplier Development Plan

- Capital and operational expenditure analysis (all tiers)
- Supplier industry and supply market analysis (local and global supply and demand, strengths and weaknesses, threats and opportunities)
- Identify focus areas for leveraging expenditure to promote industry development, at all stages of the value chain
- Targets for increasing competitiveness, capacity and capability of the local supply base
- Set Key Performance Indicators and delivery milestones
- Incremental approach
- Updated periodically

The plans should help to mobilise investment in supplier industries.

LEVELS OF INTERVENTION

The supplier industry development plans focuses on intermediate manufacturing capabilities.

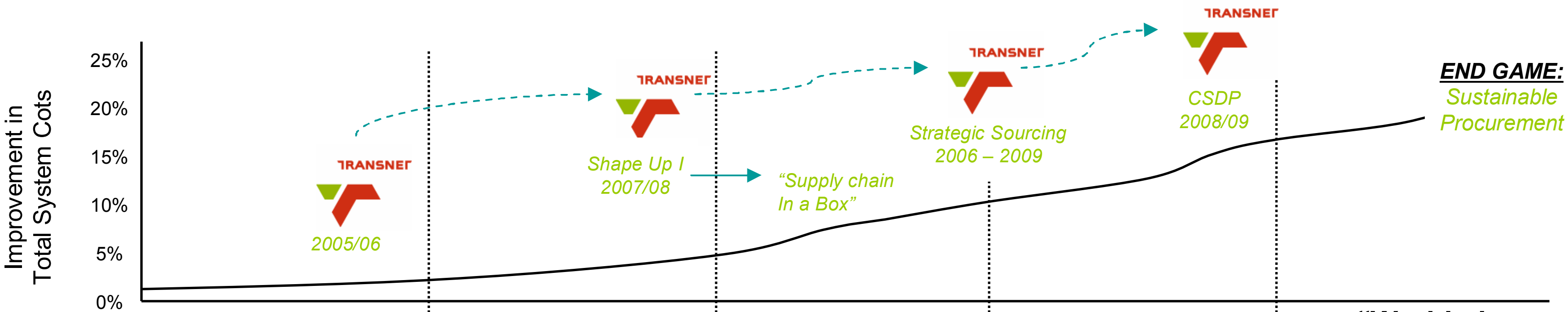
Level	Examples	Intervention requirements
Globally leading (Technology Innovator - OEM)	• Ultra heavy forging • Pipe milling	• Government driven investments for strategic economic purposes – not commercially viable in short to medium-term
Advanced (Technology Adopter)	• ASME III production facility • High voltage switchgear	• Commercially viable but high complexity – government investment in specialised skills and technologies to enable investment
Intermediate (Manufacture to spec)	• Pipe prefabrication • Gas cycle system	• Investment requirements within capability of company balance sheets, but clear medium-term commitment required
Shallow (Resource Processing)	• Construction • Structural steel	• Within current industry capability • Sufficient notice required and information sharing to enable capacity expansion

Determine interventions

The plans also determine what procurement managers and others can do about marginally competitive areas.

Diagnose Market Failure	Possible SOE Intervention	Possible Govt Intervention
Lack of competition or competitiveness	Negotiate directly with global supplier for FDI, unbundle contracts, link competitiveness improvement to contracts, establish collaborative buyer-supplier relationships eg joint R&D and innovation	Competition Commission, Legislation, support to marginal local suppliers (eg quality, competitiveness, technology support), access to finance, tariff adjustment
Lack of economies of scale	Standardise designs and specs, long term contracts, bundling, collaborate with other buyers	Investment incentives, loans, feasibility studies
Lack of Information	Improve planning, smooth demand, communicate (supplier forums), supplier benchmarking	Establish databases, feasibility studies, research, supplier benchmarking
Lack of coordination across supply chain	Collaborate, collaborative buyer/ supplier relationships	Collaboration incentives, support for cluster coordination
Externality (e.g. skills)	Incorporate skills development into tender, collaborate	Skills development incentives, skills development coordination, cluster coordination

In order to implement the CSDP, SOE need to move far up the procurement evolution path.



Theme	***"Serve the Factory"***	***"Lowest Unit Cost"***	***"Coordinated Purchasing"***	***"Cross-functional Purchasing"***	***"World-class Procurement /Supply Base Mgmt."***
Organisational Form (Process)	• At factories/ departments only • Reports to plant / department manager or lower	• Purchasing departments at BU level • Professional Purchasing	• Centralised purchasing or loose cross-unit coordination - Procurement Committee	• Center-led with execution in BUs • Extensive use of cross-functional teams	• Cross-functional supplier development teams • Co-located suppliers
Key Skills (People)	• Clerical • Logistics	• Cost analysis • Negotiation	• National Contracts • Procurement database	• Supplier development • Cross-functional problem solving	• Selection of suppliers • Relationship design • Improve supplier capabilities
Technology Used	• Fax • Phone	• EDI, fax • e-mail • Analysis programs	• Database • eSourcing • eProcurement	• ERP integration • EFT, self invoicing	• CPFR
Sample Activity	• Identify Suppliers • Expedite orders	• Managing bidding • Cost Analysis	• Work with internal users to get compliance • Develop corporate olicies	• Supplier certification • Make vs. buy decisions • Challenge specifications • Total system cost analysis	• Identify areas where supplier partnerships apply • Collaborate on advanced technology with suppliers • Continue improvement measures of supplier performance

Procurement capacity building in the SOE

A major procurement capacity building programme for participating SOE has therefore been put in place.

The Institutes of Southern African Procurement Academy (ISAPA)

- Collaboration between the Institute of Procurement and Supply South Africa and the international Chartered Institute for Procurement and Supply

- ISAPA now being implemented in Transnet:
    - involves 'professionalisation' of procurement within Transnet
    - procurement staff offered training leading to internationally recognised qualifications
    - procurement qualifications being linked to procurement career paths
    - includes on-the-job training and mentoring
    - includes socio-economic context (CSDP and BBBEE)

- ISAPA currently in testing phase in Eskom

DPE, the dti, DST DoL, DOE, Eskom and Transnet also working together to put in place support initiatives to assistsuppliers to respond to SOE demand:

- **Technical skills**
- **Supplier technology, quality and process benchmarking with UNIDO**

Something to think about

Companies or government bodies which are monopolies in their sector determine the quality of their supplier industries through the quality of their planning and the management of their procurement processes and supplier relationships.