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Stop the Operating Model Pendulum

Technology is rendering the centralized-versus-decentralized debate pointless as organizations need to be both at the same time.

Today's Seemingly Unsolvable Challenges Foreshadow the Operating Model of the Future

For the past couple of decades, procurement leaders have been selling the opportunity for massive benefits, typically based on centralizing a decentralized organization or vice versa. And this very promise, one based on the improbable achievement of reconciling local needs versus central objectives, time and again creates all but certain failure.

> Business users are accustomed to a consumer world where Amazon can meet their needs in a simple, efficient, and cost-effective manner. Yet in the business world, complicated purchasing processes still dominate.

For example, a company's board may want to see 35 percent savings across the enterprise, but the local plant may have unique needs that a central function can't meet. Or perhaps the local people tasked with making purchasing decisions are more loyal to their geographical comrades than they are to the central purchasing authority. In some organizations, this misguided allegiance, where local teams act as independent decision-makers with their own strategies, often works against a CPO's objectives.

This push–pull problem poisons most procurement transformations and can create more inefficiency than the organization began with. So how can a procurement leader hope to influence—or own—decentralized spend?

Guiding Principles of the Future Procurement Operating Model

The future operating model will need to become hyper-focused on customer experience, business acumen, and value creation.

Internal customers want more. Today's business users and suppliers are accustomed to a consumer world where Amazon can meet their needs in a simple, efficient, and cost-effective manner. Yet in the business environment, complicated purchasing processes still dominate. The goal ought to be instead to provide information transparency and seamlessly direct the user to what they need, even if they don't know how to articulate it.

Business needs are not well-understood. Procurement can no longer be a reactive order taker, engaging in simple purchasing requirements and price-only negotiations. Generating savings will not be enough. Tomorrow's procurement organization must bring something compelling to the table, such as intellectual property protection expertise, innovative supply market insights, or advanced supplier collaboration techniques. In other words, the seat at the table is no longer guaranteed; it has to be earned.

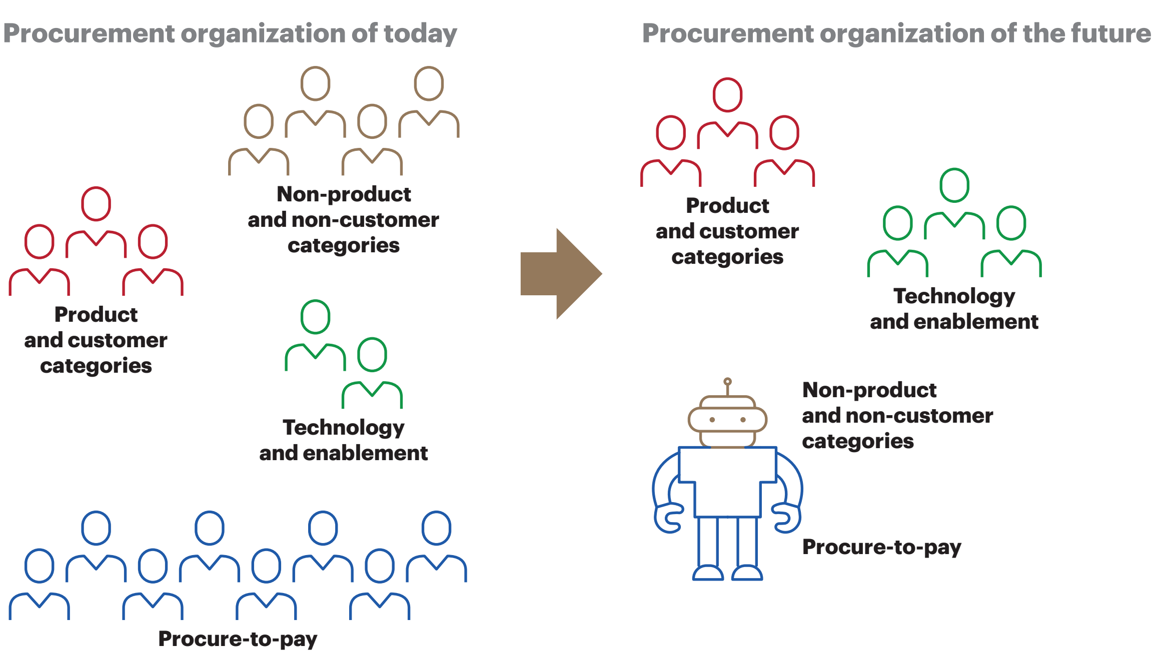
There is too much noise and not enough value creation. Absent meaningful tools, insights, and techniques, procurement functions end up inundated with low-value operational tasks, including ensuring compliance, renegotiating contracts, managing surface-level risks, and dealing with legal compliance—all of which take valuable time away from more impactful work and are being automated.

Taken together, these principles enable procurement to direct their capabilities and resources to their primary purpose: translating supplier value into product and customer value with a bottom-line impact. Organizations will need to think digital first but with the mind-set that even though digital will have a profound impact, the focus needs to be on enhancing talent and optimizing how the organization can best serve the business.

Building Blocks

Organizations that opt for the reimagined procurement operating model can expect a much smaller function. However, we don't expect the cost of the function to decrease in proportion since the new model will require upskilled professionals and will need to invest and maintain the relevant technology, all of which are likely to keep costs relatively neutral to today's levels. The new organization will require different and more advanced capabilities, such as deep category and product expertise and strong stakeholder engagement skills, coupled with digital architecture know-how, to drive AI-enabled self-service and automation—a job for whole-brain thinkers. In addition, the technology setup will require advanced technical skills coupled with procurement knowledge in a structure that is drastically different from today (see figure 1).

Figure 1
Procurement organizations will downsize and change their structure



Source: A.T. Kearney analysis

The design of the future operating model will be constructed with three building blocks:

Category alignment

Procurement functions need to evaluate categories as either integral or non-integral to the product offering or customer proposition that the business produces (see figure 2). Today, direct and indirect categories are managed with the same broad resourcing approach, with indirect categories typically being the source of the greater tactical volume of effort (and therefore requiring larger teams), but both essentially given equal attention and effort. In the future, the focus will be on providing a deep sustained understanding of the supply market only for categories that are integral to the product offering or customer proposition. For these categories, including commodities, procurement will continue to be the connector between the business and the supply market, and a broader and more sophisticated set of levers will continue to be required to extract the full value. For categories that are not integral to the product or customer offer, some of which might be less complex and less sophisticated, procurement will primarily focus on putting the right supply options in place, enabled by technology for self-service by end users.

Figure 2
The future procurement operating model will have two buckets of categories

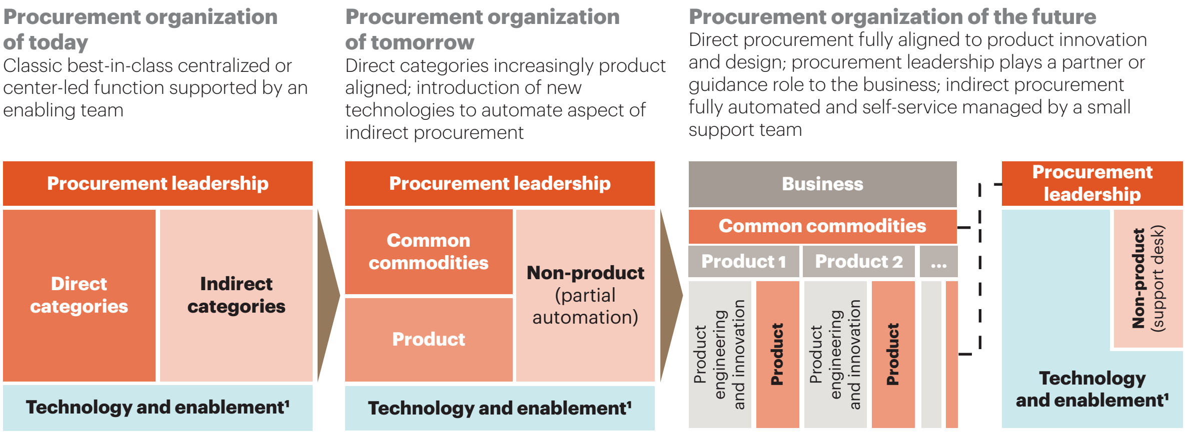
Categories integral to the product offer	Categories not integral to the product offer
• Varies by industry but usually includes all directs, packaging, marketing, and other spend that directly impacts the offer	• Varies by industry but usually includes most indirect categories including facilities, professionals services, repairs, and transport
• Operating model aligned to products • Procurement activity integrated in product development or innovation teams to improve the offer	• Operating model aligned to user communities • Procurement activity focused on supporting users to buy solutions to meet their needs
Procurement role predominantly • Providing high-value commercial input—orchestrating supply and demand power • Obtaining the right behavior from suppliers—managing relationships well	**Procurement role predominantly** • Ensuring technological enablement in place—so that users or stakeholders can self-serve as much as possible • End-to-end orchestration—ensuring that the processes and enablement work, including the data analytics to make decisions

Source: A.T. Kearney analysis

Business alignment

Ensuring the required level of business alignment and interaction to become an integral part of product development and business operations will likely leave procurement professionals sitting closely within the product teams they serve. Most center-led organizations today operate in centralized procurement teams that are separated from the business with alignment driven by either transactional activities or category-specific sourcing events. In the future, this alignment will happen on an ongoing basis (see figure 3 on page 4). This will unlock the strategic value of procurement in product and service development and continuous improvement that was lost without an ongoing business connection. Levers that are becoming more prevalent, such a

Figure 3
Procurement will become integrated into product teams



¹ Enablement powered through artificial intelligence
Source: A.T. Kearney analysis

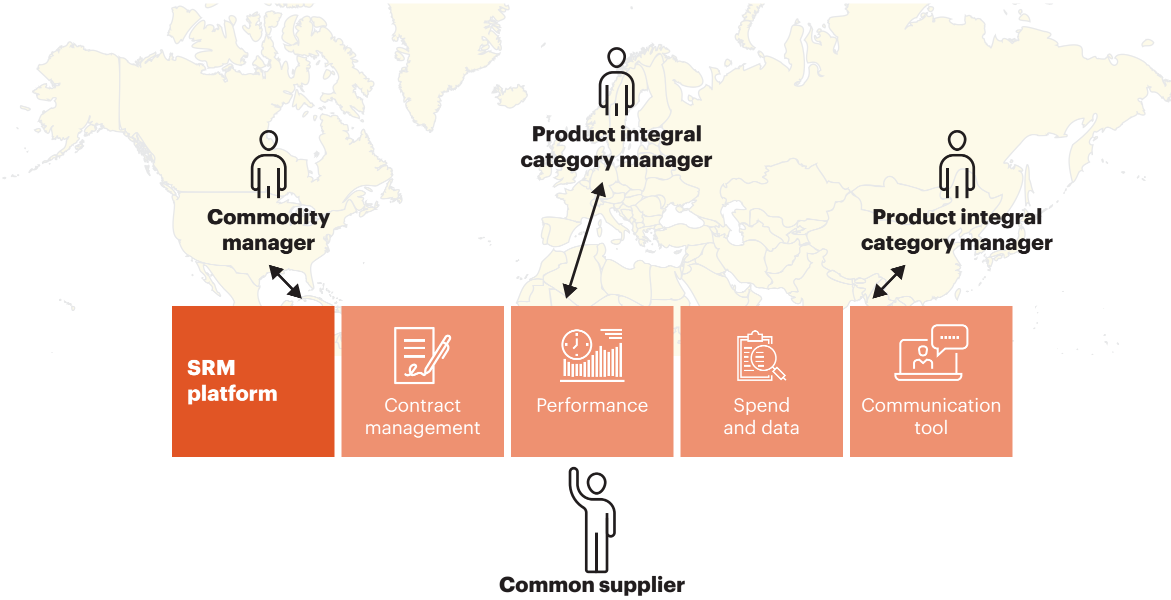
value reengineering and supplier-driven innovation, will become the norm as the procurement mandate grows—and with it, the opportunities that can be pursued. The question of procurement centralization then becomes secondary and will be driven by the nature of the overall business model.

Supplier alignment

Technology will form the link with the supply market, enabling procurement to maintain the leverage gained through centralized relationships without necessarily being structured around supplier engagement. Historically, even though best practices have been driven by adequate supplier segmentation and focus on key strategic suppliers, supplier leverage has often come from consolidating volume into large agreements with tight global governance of supplier relationships. In this model, physical interaction has been a major driver of the structure of procurement activity around these key supplier relationships, typically detached from real alignment with the business stakeholder on how to capture value from those supplier relationships. And yet, if technology eliminates the need for physical proximity, it opens up all kinds of new possibilities for managing the interaction with suppliers and the business.

In the future, supplier segmentation will still be a crucial driver of interaction models, and although procurement will continue to be the main connector with suppliers, technology will enable a different kind of intimacy both with suppliers and with the business while also supporting and enabling global relationships and a broader supply market (see figure 4 on page 5). The focus will shift from tactical contract compliance and performance management, which will be automated and readily available, to true value-creating interactions with suppliers in alignment with business stakeholders. This will include not only joint value programs with strategic suppliers, but also management of ecosystems in sync with the business to drive end-to-end product and service innovation. In this new battleground, procurement needs to be measured for its ability to assure that supplier relationships deliver the right value for its business partners.

Figure 4
Integrating procurement with suppliers and the business



Note: SRM is supplier relationship management.
Source: A.T. Kearney analysis

Capability Needs to Increase

If the procurement function has fewer roles and adopts more robust digital tools, then practitioners will need to have a whole host of new skills (see figure 5 on page 6). But more importantly, they will need to be imbued with new traits. In fact, the entire operating model will depend on it. The procurement employee of tomorrow will be a business athlete: savvy and with grit, resilience, creativity, and emotional intelligence. Ideally, he/she/they will also be entrepreneurial, socially responsible, and resilient. Enabled by a flexible, sophisticated operating model, people with these traits can identify strategic opportunities in the supply market. For example, as companies move from physical products to digitally enabled products, simply leveraging the existing system integrator or IT provider will not be enough. Oftentimes, the incumbent SI/IT provider is positioned to choke off or direct digital innovation initiatives. However, a savvy procurement person could look at the digital provider landscape and bring disruptive suppliers into the mix. Moreover, procurement can take the lead in pushing the move from a traditional supplier arrangement (payment for goods or services delivered) to more lucrative and successful joint-venture or alternative funding mechanisms.

This Is Not Just a Decentralized Model

The future operating model will transcend procurement as we have known it. No longer will we debate centralized versus decentralized. Success will be measured by the ability to be nimble, operate efficiently, and expand its influence over the business and the supply base. And these abilities will need to be executed by procurement functions that are smaller and tasked with varied strategic objectives. In other words, the era of the transactional purchasing gatekeeper is over; those activities will be automated. Tomorrow will be about having a high-performing team

Figure 5
Procurement will need to develop a range of new skills

Future role of procurement

	Technology and enablement	Product integral: Demand	Product integral: Advanced SRM
Responsibilities	• Solution engineering • Technology architectures • Deployment and enablement • Performance management • Contract management • Automated sourcing execution • Analytics and insight generation • Benchmarks • Operations (such as sourcing factory)	• Budget control • Spec design and management • Quality management • Total life-cycle management • Value-based sourcing • Collaborative cost reduction • Innovation	• Strategic alliances • Supplier development • Advanced negotiations • Sustainability • Compliance • Risk management
Competency required	• Design thinking • Process engineering • IT architecture experience • Advanced analytics • Change management	• Top-line mind-set • Logic and reasoning • Creative • Analytical, critical thinking • Cross-functional leadership	• Creativity • Intuition • Emotional intelligence • Visual comprehension

Note: SRM is supplier relationship management.
Source: A.T. Kearney analysis

with specialized skills working together to tackle the strategic needs of the enterprise—needs that will become even more crucial as the global economy continues to be shaken by political upheaval and changing demographics.

This approach will strengthen the reputation of the function as a collection of value-adding partners who will improve the overall perceptions of the profession. This will also create opportunities to define varied career paths that can better connect with the business, particularly for the product or service and commodity roles. Thus, the path to becoming a successful business professional will begin with working on a high-performing procurement team. Whether the individual's final destination is finance, product development, sales, or operations, there is no better place to begin than with creating value for the enterprise by strategically influencing the spend.

A Radical Way Forward

The future is bright for procurement functions and professionals who can step up, adapt, and reflect the needs of their business—becoming value-adding trusted partners to key business functions. To do this, procurement must embrace a dramatically different operating model, requiring a radical rethinking of the way CEOs see their procurement function and likely all their back-office functions.

The implications of all of the changes in the function's operating model will be stark:

- Procurement functions will be about a tenth of the size they are today, resourced with highly skilled professionals who collaborate with the business to create value.

- Technology will completely reshape the operating model.
- Indirect procurement functions will largely cease to exist, other than to serve an orchestration role, but will be delivered through self-service marketplaces and intelligent automation.
- Direct and other product and service integral categories will align with products and services or commodities working in direct sync with the business with a flexible project-driven organization.
- Procurement can become more geographically decentralized through human interaction while leveraging a centralized governance and control tower to deploy technology.
- Supplier interaction will be highly strategic and in full sync with the business. Technology will enable truly global supply markets where appropriate.

There is a strategic imperative to do this now. Laggards will not only continue to fall out of step with their competitors from an organizational cost perspective, but also potentially put their organizations at extreme risk through accidental negligence or missed competitive advantage. A high-performing procurement organization, built on a future-based operating model, will solve this problem.

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