The Metrics of Public Procurement: Part 1

By Ash Bedi

The way government selects and analyzes procurement metrics is often not aligned with measuring value or desired outcomes. We see it again and again in Government Accountability Office reports, or in comments from industry, but telling someone what's wrong only takes them so far.

It's a vital topic for leaders overseeing or managing procurement spending, and we commend the efforts being taken by federal agencies and the White House to develop key metrics, and we hope our work will help improve on those metrics already selected. What we will outline in this series is just a starting point for what we hope will be an engaging discussion on this topic.

Our goal ultimately is to help develop the right procurement metrics for the entire public sector. We start by introducing our initial take on metrics based on our expertise having worked across the public and private sectors.

Our starting point is also based on a review of a diverse set of reports on procurement metrics from some well-known and respected places including the Institute of Supply Management (the private sector's premier best practices and research organization for procurement), and governments of the UK and Australia, who have generally been on the leading edge of public procurement. Our goal is to use this as a starting point for a discussion on how to improve the metrics used in public procurement.

WHY METRICS MATTER

Why care about procurement metrics at all? First of all, as the most famous management expert of our time William Edwards Deming said, "you can't manage what you can't measure." Very simply, we need metrics to better gauge procurement's contribution to helping achieve desired outcomes and effectiveness of spending.

METRICS START WITH AN UNDERSTANDING OF DESIRED OUTCOMES

Metrics should not be about just measuring activity (e.g. how many transactions processed, how many personnel trained). These are important. But more important is the need to link activity to ultimate outcomes (e.g. providing healthcare to uninsured at a lower cost).

In other words, what are we trying to achieve in terms of outcomes and what are the actions that get us there.? With this in mind, we present an introduction to procurement metrics organized along four areas. These four areas are in many ways linked to the "procurement value levers" we've discussed elsewhere. We will expand on each of these areas in a subsequent article.

METRICS AREA 1 – MANAGING TOTAL COST

One of the primary goals of any procurement is to manage total cost. This is not just about money. It is also about measuring effectiveness in terms of outcomes – if you have to keep spending over and over to achieve the same outcome, your total cost goes up. Overall, these metrics measure how well an organization is applying various leading practices in managing cost such as achieving better prices, managing specifications, managing demand etc.

METRICS AREA 2 – MANAGING AND ENGAGING SUPPLIERS

This area is focused on measuring how well an organization is engaging, managing and collaborating with suppliers in terms of meaningfully engaging suppliers, achieving socio-economic objectives, and managing supplier performance.

METRICS AREA 3 – MANAGING INTERNAL OPERATIONS AND CUSTOMER SATISFACTION

Efficiency and customer satisfaction is the focus of this metrics area. Examples include measuring cycle time, internal procurement function costs and of course internal customer satisfaction with the procurement function.

METRICS AREA 4 – MANAGING THE WORKFORCE

Here, we focus on acquiring, retaining and developing leadership and broader talent with the required qualifications. This of course is a topic high on the mind of anyone focused on government procurement. We similarly believe this is the key to building a world-class procurement and acquisition system.

Let's dive deeper into the first set of metrics around "Managing total cost."

MANAGING TOTAL COST IS A FUNDAMENTAL MISSION OF THE PROCUREMENT FUNCTION

In our definition, total cost not only accounts for prices paid, but also other factors that drive costs. A simple example that everyone can relate to is printers. The price of a printer (and improvements in that price from competition for example) is only one factor in gauging cost performance.

Other factors include identifying appropriate specifications for that printer, ensuring that the "need" is consistent with the defined specifications, managing the total number of printers bought, etc. Total cost can be broken into four key components. These components measure how well an organization is applying various leading practices in managing cost and driving savings.

While we discuss these factors today in the context of metrics, any professional can also take these to apply specific actions as they go to market for any product or service. Below we elaborate on each of the four savings metrics of managing total cost.

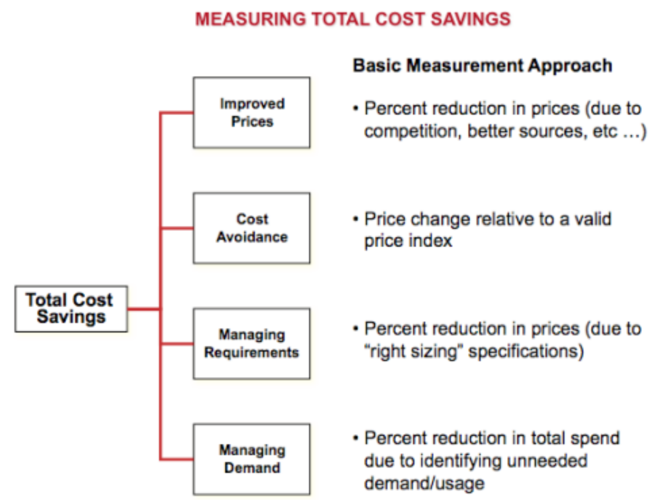
IMPROVED PRICES

Prices paid often grabs all the attention, but the truth is that price may be the most basic and incomplete part of managing total cost. Nonetheless, benchmarking prices paid is an important factor that should be monitored and measured. As we illustrated in our other article, price benchmarking must take into account the context of any purchase including the volume, strategic rationale for supplier, industry conditions. For more on how to improve pricing, you can see our article diving into six proven techniques. In terms of the metrics you need for measuring improved prices, you'll want to employ ones that measure reductions in pricing and the absolute savings achieved as a result.

COST AVOIDANCE

Though sometimes lumped in with improved pricing, cost avoidance is more applicable to products and services where prices tend to increase year over year. The goal here is to measure how well a procurement performed in managing price increases against what the overall market is showing. In other words, if prices are increasing for the market overall, were we able to do better than the market.

A good example of when cost avoidance comes into play is watching the price of oil and similar "commodities" go through inflationary periods. Another example is labor costs for various types of services—we often see year-over-year price increases in these types of spend areas. It's procurement's job to make sure the price increases for our organizations are managed relative to a relevant market index. Or even better,



we want to manage the price increase to be less than a relevant market index. The most helpful metrics to this end are ones that measure whether price increases are favorable relative to previous contract terms and/or relative to a relevant market price index.

MANAGING SPECIFICATIONS

Standardizing specifications across an organization and keeping specs as close to market standards as possible is another way to manage total cost. Both of these are difficult in practice but can yield significant benefit. Metrics for savings due to managing specifications measure how much is saved as a result of identifying alternate, lower-priced products or services to achieve desired mission outcomes.

A couple of examples illustrate the point. One federal agency, for express air and ground shipping needs, increased the "on time" guarantee by 2% above commercial standards. When the suppliers informed the agency of the potential cost increase versus the relative benefit, luckily both the agency and suppliers were able to change the guarantee requirement to the accepted commercial standard, saving both the government and suppliers money.

Another example, different users may require different amounts of memory, speed and overall computing power for their computers, depending on their jobs. By establishing groups of users based on their needs and standardizing around 3 or 4 models, government can work with suppliers to provide higher volumes and other efficiencies.

REDUCTION IN DEMAND

Best way to reduce cost is to not buy something. Seemingly obvious, this is one place where we see a lot of waste and a lot of opportunity. Government organization should be working to measure how much total volume of something they are purchasing and whether it can and is being reduced over time, to match real "needs." Metrics that identify savings from a reduction in demand measure the total savings achieved for eliminating a portion of the demand. In other words, every "unit" reduction in demand represents a 100% savings for that unit! That'll look good on any report.

A common example in the government has been cell phones. One agency, for instance, found thousands of lines that were not being used because users had left the agency. Working with suppliers, they were able to shut down those lines.

WHAT YOU CAN DO TODAY

Regardless of what your organization is buying, you can start today by measuring total cost.

1. Establish clear metrics around total costs, starting with your largest programs and categories.
2. Break down the total costs into its many components, including price and the other factors mentioned in this article.
3. Identify opportunities where factors can be applied.
4. Work with your customers and stakeholders to put an action plan in place.

Stay tuned for more in our metrics series, as we dive into the other metrics areas.