Supplier Performance Management: It’s More Than a Scorecard, It’s a Strategy

Published 17 June 2020 - ID G00716070 - 16 min read

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Initiatives: Direct Material Sourcing and Supply Chain Services

Chief procurement officers have a fundamental responsibility to monitor and improve the performance of their supply base. This research provides an outline of the key elements needed to build a robust supplier performance evaluation process.

Overview

Key Challenges

- Implementing a best-in-class supplier performance management (SPM) program is a resource-intensive activity that can be prohibitive to deploy with a large supplier population.

- Metrics used to measure supplier performance are often operationally focused and don’t always reflect the full value provided by suppliers in supporting broader business goals.

- Supplier performance ratings are often disconnected from internal processes and sourcing strategies. Unclear rewards — or consequences — linked to the performance management process will minimize the relevance of this strategy to both buyers and suppliers alike.

- Supplier feedback is rarely included in the performance assessment process, making it a one-way conversation that does not encourage supplier collaboration.

Recommendations

Chief procurement officers (CPOs) responsible for direct material sourcing and looking to track and improve supplier performance should:

- Use supplier segmentation to identify the type of performance metrics to use according to the supplier’s criticality to the business and where performance improvements will yield the greatest value.

- Incorporate metrics that support your company’s goals and values, such as innovation, responsiveness and risk, to capture the full value delivered by your suppliers — do not use operational metrics only.

- Design effective scorecards to communicate performance expectations, set priorities and drive continuous improvements, not just to measure for its own sake.
Introduction

One of the most common questions Gartner gets from companies looking to measure supplier performance is, “What metrics should we include in our supplier scorecard?” Although companies ask this question for the right reasons, there’s a great deal more to managing supplier performance than just implementing a scorecard. According to Gartner’s research, improving the performance of existing suppliers is among the top critical tactics that procurement must use to deliver value to the business. ¹

To ensure that suppliers’ performance aligns with company goals, suppliers should be measured beyond traditional operational metrics, such as on-time delivery, quality and cost savings. While these metrics are fundamental, there are several other aspects that buying organizations value, and these should also be included in the suppliers’ performance assessment. These range from measuring suppliers’ innovation capabilities and their ability to support new product introductions, to other aspects such as the quality of the relationship and responsiveness of their service team. Incorporating these value-oriented metrics helps companies move from being reactive, looking only at history, to being predictive and future-focused.

This research provides the key steps needed to develop a best-in-class SPM strategy and how it can be used to improve supplier relationships and mitigate supplier risks (see Figure 1).

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**Figure 1: Four Steps to an Effective SPM Program**

1. **Select**
   - Suppliers to Measure

2. **Define**
   - Value-Oriented Metrics

3. **Measure**
   - Using Effective Scorecards

4. **Reward**
   - Performance

Source: Gartner
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Analysis

Implementing a formalized supplier performance management program is a major step that, if done correctly, will enable companies to clearly and objectively measure their suppliers’ ability to
deliver value across a broad range of priorities. One of the main barriers companies struggle to overcome in their quest to develop collaborative supplier relationships is multiple versions of the truth regarding a supplier’s performance. Different stakeholders have different needs from the supply base, and without visibility and agreement on how suppliers are performing, it can be difficult to get stakeholders’ support to execute effective supplier development strategies.

Unfortunately, companies often implement SPM as a forced ranking exercise, mainly focused on operational metrics and replacing supposedly low-performing suppliers with little knowledge or regard for actual root causes or capabilities. Some of the most typical reasons for a failed attempt at implementing an SPM program are:

- Trying to measure as many suppliers as possible, forcing companies to narrow their assessment to operational metrics that can be pulled from an ERP system.
- Failing to identify suppliers where improved performance can have the greatest impact for the organization.
- Attempting to use a “one-size-fits-all” approach to measure all suppliers.
- Using metrics that reflect the needs of a limited group of stakeholders.
- Providing no transparency to the supply base on what metrics are being utilized or what criteria are being used to measure performance.
- Failing to incorporate the supplier’s feedback to identify changes the buying organization needs to make to fix problems that could be adversely affecting the supplier’s performance.

An effective SPM program will provide a communication channel with the supply base that promotes trust and transparency. This will give suppliers clear guidance on what they’re being measured on, what scoring criteria are being used and what it takes to be a preferred supplier. It will also encourage a culture of continuous improvement with both parties closely collaborating to address performance gaps. Finally, SPM will enable better alignment between procurement leaders and internal stakeholders by ensuring that their voices are represented in the assessment of suppliers’ performance. This is particularly important when hard metrics alone are insufficient to show whether the supplier is doing a good job or not.

Use Supplier Segmentation to Identify the Group of Suppliers Where Performance Improvements Will Yield the Greatest Value

Monitoring supplier performance can be time-consuming, as an effective SPM strategy will include not only operational, quantitative metrics but also nonoperational metrics that are qualitative in nature. Tracking these metrics consistently will require data, management time, resources and input from internal stakeholders. This helps to ensure that stakeholder needs are represented in the process; however, it is time-consuming and not scalable in organizations where there are hundreds, if not thousands, of suppliers.
Effort and resources spent on managing suppliers’ performance should be proportionate to the value and importance of the supplier. All suppliers cannot be measured equally, especially when there's a large supply base. For this reason, it is critical to identify the group of suppliers where an active performance management approach may yield the highest benefit to the organization. To do this, use the output of your supplier segmentation strategy and start by focusing on strategic suppliers first (see “How to Design an Effective Supplier Segmentation Strategy”). As the SPM program evolves, consider adding other critical suppliers to the program.

Digital technologies can help the supplier performance assessment process, with some tools having the capability to capture operational data from internal systems, launch internal surveys to collect qualitative ratings from stakeholders and can even provide a portal for suppliers to self-assess themselves. While these technologies help simplify the process, there is still significant manual work required. Therefore, a differentiated approach is used, where companies differentiate the type, complexity and breadth of metrics used to assess suppliers based on their criticality to the business.

Metrics used to measure supplier performance will vary, depending on the types of suppliers being evaluated, as shown in Figure 2. For example, when measuring strategic suppliers, where joint value and stronger collaboration are pursued, growth capabilities, such as supplier innovation, risk management and cultural alignment are quite relevant, and therefore, should be part of the performance assessment. In contrast, when measuring the performance of nonstrategic but critical suppliers, innovation or cultural alignment may become less relevant.

**Figure 2: Key Metrics to Consider by Supplier Segment**
The purpose of formalizing a SPM program is not to cover as many suppliers as possible. Rather, its main objective is to proactively manage and drive performance improvements of the business’s most critical suppliers. While it may be tempting to start from the bottom and measure the performance of a larger number of suppliers, procurement leaders should instead start from the top, focusing on suppliers where performance improvements can yield the greatest benefits.

Managing performance and driving continuous improvement with a critical few suppliers have significantly more impact than tracking operational metrics with a larger supply base. This doesn’t mean that the performance of transactional suppliers is unimportant. However, due to the resources needed to implement an effective SPM program, transactional suppliers are often managed in a reactive way, primarily focused on operational metrics.

Define Supplier Metrics That Encourage Innovation and Partnering, Including Aspects Beyond Operational Performance

Supplier performance is often defined as the supplier’s ability to deliver on time and with the required quality specifications. Delivery and quality metrics are critical; however, they represent only the minimum expectations from the supply base that conform to contractual commitments. They are backward-looking metrics that do not provide enough insight into the supplier’s future performance, nor do they reflect other aspects also valued by buying organizations, such as service levels, risk management or innovation. Simply put, measuring supplier performance only in terms of cost and delivery or quality is a narrow approach that doesn’t fully reflect the overall value and capabilities of the supply base.

Supplier performance will have a direct impact on multiple internal groups; however, many sourcing and procurement organizations reach out to only a small group of stakeholders when developing scorecards, assessing performance and reviewing supplier development plans. When SPM occurs in this type of vacuum, the lack of alignment between the suppliers’ assessment and the needs and requirements of the business will result in missed opportunities, higher costs and increased risks. To avoid this, for example, food manufacturer Kellogg’s uses an internal survey to request input from internal stakeholders when scoring suppliers across different aspects. 2

An effective SPM program will provide an objective assessment of suppliers’ performance that becomes a key factor to consider when defining future sourcing strategies. For this reason, leading procurement organizations recognize that there is much more to supplier performance than delivery and quality, and therefore, expand the range of metrics they use to answer a simple question for selected suppliers:

“How well does this supplier meet the current and future needs of our business?”
Answering this question requires procurement leaders to look beyond their own set of metrics and functional priorities and reach out to other internal stakeholders to understand how this group of suppliers impacts their objectives. These stakeholders will play a critical role in defining the supplier metrics that reflect their priorities and in defining the scoring criteria that must be used for each metric. Including metrics that fall outside procurement’s traditional focus on cost, quality and delivery into suppliers’ performance assessments is one of the many ways supply chain leaders in procurement can further engage and align with their internal stakeholders’ needs (see Figure 3).

**Figure 3: Key Supplier Performance Metrics**

When looking to define metrics and key performance indicators for strategic suppliers, make sure they encourage innovation and partnering. Developing a win-win relationship of trust and shared accountability can be done only if one side is not trying to win at the other’s expense. Metrics and corresponding criteria used to measure suppliers’ performance must accomplish the following:

- Support the end-to-end supply chain strategy for achieving overall revenue growth, profit and other company goals.
- Align with how the (ultimate) end customer measures the organization’s ability to serve it, including areas such as responsiveness, efficiency or agility.
- Drive the right behavior and support better decisions.
Emphasize continuous improvement.

Be mutually agreed.

Expanding the set of metrics beyond traditional ones of cost, quality and delivery, and including other nonoperational metrics, allows procurement leaders to move from being reactive (looking only at history) to being predictive and future-focused. Use metrics that track risk management, supplier innovation and the quality of the relationship between both organizations. Table 1 highlights a few industry examples of the different metrics used to measure supplier performance.

<table>
<thead>
<tr>
<th>Metric</th>
<th>Conagra Brands</th>
<th>GE Appliances</th>
<th>General Motors</th>
<th>Schneider Electric</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operational</td>
<td>Delivery</td>
<td>Quality</td>
<td>Quality</td>
<td>Cost productivity</td>
</tr>
<tr>
<td></td>
<td>Quality</td>
<td>Delivery</td>
<td>Program launch</td>
<td>Competitiveness</td>
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<tr>
<td></td>
<td>Lead time</td>
<td>Productivity</td>
<td>Total enterprise cost</td>
<td>Quality</td>
</tr>
<tr>
<td></td>
<td>Cost productivity</td>
<td>and cost out</td>
<td>Supply chain delivery</td>
<td>Delivery</td>
</tr>
<tr>
<td>Nonoperational</td>
<td>Innovation</td>
<td>Environmental, health and safety (EHS)</td>
<td>Innovation and engineering</td>
<td>Innovation</td>
</tr>
<tr>
<td></td>
<td>New product launch</td>
<td>Customer service</td>
<td>Transparency</td>
<td>Sustainability</td>
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<tr>
<td></td>
<td>Enabling technology</td>
<td>Technology and innovation</td>
<td>Communication and responsiveness</td>
<td>Responsiveness</td>
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<td></td>
<td>Working capital reduction</td>
<td>Program management and Execution</td>
<td>Total enterprise approach</td>
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<tr>
<td></td>
<td>Sustainability</td>
<td>Finance and payment terms</td>
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<td></td>
<td>Account management</td>
<td>Agreement terms and conditions</td>
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Deploy Scorecards to Convey Performance Expectations and Set Priorities, Not Just Measure; Incentivize High-Performing Suppliers

Supplier scorecards are one of the most common tools used to manage suppliers’ performance. However, many companies use them exclusively for scoring suppliers, thereby failing to leverage the scorecards’ full potential as a communication tool that should be used to define goals, set priorities and promote a culture of continuous improvement (see “Supplier Performance Scorecard and Assessment Tool”).

When designing supplier scorecards, start by defining what you are trying to accomplish with the group of suppliers selected and include metrics that will help drive these suppliers toward specified goals. Too often, companies measure suppliers only in the areas where data is easily available, not on the desired behavior they want to see in the suppliers. Good scorecards should expose problems and give companies the tools necessary to steer desired behaviors. Consider the following principles when deploying scorecards:

- **Transparency is key**: Believe it or not, many companies fail to share performance data with their suppliers. Scorecards without transparency and visibility are worthless in achieving companies’ goals. Suppliers and contract manufacturers need to know how they are doing individually and compared to others. They must have a clear understanding of not just what they are being measured on but also the details behind the scoring criteria.

- **Scorecards should drive the desired behavior**: The different metrics included in the scorecard should be weighted to reflect those areas that are most relevant to your organization. Suppliers will use these relative weights to interpret your objectives; therefore, you must make sure your scorecards accurately reflect what you want to accomplish. If pricing is 50% of the score and quality is only 10%, you are telling suppliers that meeting quality standards isn’t as important as cost. Companies that have seen the most success in this area are those that use the same metrics for all their suppliers, but also adjust the assigned weightings and grading criteria based on specific supplier capabilities, category strategy and/or product line.
Support and educate, don’t just monitor: Monitoring without any support, resources, training and capacity-building mechanisms won’t go far toward meeting the company goals. The goal of SPM programs is not only to grade suppliers but also to identify opportunity areas for improvement. Be prepared to assign the necessary resources to ensure that the company acts on these opportunities.

Scoring must come with action. Suppliers that score well must be rewarded; otherwise, there is no incentive for them to improve performance. Participation, active engagement and supporting broader business goals are a supplier’s ticket to many benefits they might otherwise think they’re entitled to. To incentivize your suppliers, build a list of rewards you would be willing to offer top-performing suppliers that have great value to them, but little to no cost to you. Use the rewards listed in Table 2 as a starting point and engage with your sourcing and procurement team to identify any other ideas that suppliers may value.

Table 2: Rewarding Top-Performing Suppliers

<table>
<thead>
<tr>
<th>Visibility and Recognition</th>
<th>Revenue and Margin Growth</th>
<th>Joint Business Development and Others</th>
</tr>
</thead>
<tbody>
<tr>
<td>Invitation to supplier summit</td>
<td>Higher-volume participation or exclusivity</td>
<td>Supplier development and staff training (lean, quality, sustainability, etc.)</td>
</tr>
<tr>
<td>Supplier awards</td>
<td>First access to new electronic request for quotation (eRFQ) opportunities</td>
<td>Extend employee discounts to suppliers</td>
</tr>
<tr>
<td>Access to senior leadership</td>
<td>Connect them with other business units</td>
<td>Share with supplier market data</td>
</tr>
<tr>
<td>Participate in supplier innovation days</td>
<td>Expedited qualification process</td>
<td>Co-branding opportunities</td>
</tr>
<tr>
<td>Give testimonial suppliers can leverage in marketing materials</td>
<td>Extend subtier pricing to suppliers</td>
<td>Offer dynamic discounts</td>
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<tr>
<td></td>
<td>Longer-term agreement payment terms</td>
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</tr>
<tr>
<td></td>
<td>Access to better financing rates in supply chain finance programs</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Gain-sharing agreements</td>
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</tr>
</tbody>
</table>

Source: Gartner
Similarly, ensure you are defining clear consequences for underperforming suppliers. It is always easier to work with underperforming suppliers — instead of replacing them — to identify root cause and areas where buying organizations may help them develop their capabilities to improve. However, there will be cases where performance is consistently below expectations; therefore, other actions, such as limiting exposure to new business opportunities or even loss of business volume, will be required. It is critical that procurement leaders incorporate supplier performance ratings into their sourcing strategies to influence their decisions. Failing to do so might lead to underperforming suppliers winning incremental business or being exited when poor performance was beyond their control, which renders the goals of the SPM program useless.

**Request and Incorporate Supplier Feedback to Identify What Needs to Happen on Both Sides of the Relationship in Order to Improve**

A formalized SPM program has many advantages as it helps to align internal stakeholders in establishing one source of truth regarding suppliers’ performance. However, one of the greatest, but often overlooked, benefits of SPM is enabling a two-way communication channel with the supply base. Leading organizations work with their suppliers to identify opportunity areas where changes might be needed on the buyer’s side to improve the supplier’s performance. For example, a supplier with a poor on-time delivery score might be struggling due to constant last-minute changes from the buying organization, with purchase orders being placed outside the standard lead time. In contrast, a supplier scoring low on risk management metrics may be the result of a lack of resources from the buying organization to qualify a secondary production facility.

Supplier performance should be managed in the spirit of continuous improvement; therefore, it is critical to encourage suppliers to provide feedback on what needs to happen on both sides of the relationship in order to improve performance. To do this, a CPO from an industrial manufacturer of gas turbines used a simple method to encourage supplier feedback. She decided to start all quarterly business reviews with strategic suppliers by asking them two simple questions: “How are we performing as a customer?” and “What do we need to do to improve?” By making this change and acting on the supplier feedback received, she was able to establish credibility and get suppliers to jointly collaborate in performance improvements.

Higher-maturity organizations take this even further, implementing formalized supplier feedback surveys or even establishing what is commonly referred to as “reverse scorecards,” where suppliers are expected to provide feedback on metrics being used to gauge their performance. For example, in 2015, General Motors (GM) improved its SPM program by launching a 360-degree survey, requesting suppliers to rate it as a buyer using the same performance categories that GM was using to rate them. This allowed GM to establish a continuous feedback loop with its key suppliers that helps to identify improvement opportunities for both organizations (see “Use Supplier Satisfaction Surveys to Become a Customer of Choice”).

Managing and developing suppliers must be institutionalized as an ongoing process to drive continuous improvement for your organization and its suppliers. This requires the right leadership
and attitude to incentivize suppliers as well as provide ongoing education and training and a
greater degree of data transparency.

Evidence

1 Gartner’s Future of Supply Chain, 2018, n = 275.
2 “Video: Supplier Management Excellence at Kellogg’s — Fostering and Measuring Value.”
3 “SPARK 2019: Conagra | Supplier Performance Management,” Scout.
4 “Video: Engaging Suppliers to Align, Inspire and Deliver.”
5 “Video: Driving Better Supplier Engagement at General Motors.”
6 “Video: Reinventing Supplier Collaboration at Schneider Electric.”

Document Revision History
Supplier Performance Management: It’s More Than a Scorecard, It’s a Strategy - 7 August 2018

Recommended by the Author

Use Supplier Satisfaction Surveys to Become a Customer of Choice
Follow Gartner’s 4-Step Framework to Implement an Effective Supplier Relationship Management Program
Key Success Factors to Assess Your Supplier Relationship Management Program
Merlin (Automated Supplier Scorecard Platform)
How to Navigate the Fragmented Supplier Management Solutions Market

Recommended For You

Best Practices for Privileged Access Management Through the Four Pillars of PAM
Evaluate These Factors in a Global Manufacturing Site Selection Activity
HR Business Partner Career Diagnostic
Toolkit: Assess National and Organizational Attributes in Addition to Costs for Global Manufacturing Site Selection
Supply Chain Brief: Expand Capacity Planning Beyond Manufacturing for Feasible and Optimized Supply Plans