Category Management Tools Guidance Notes

The document outlines category management with information on how CIPS category management tools can help you to segment spend into areas which contain similar or related products enabling focus opportunities for consolidation and efficiency.

This knowledge paper is supportive of Procurement professionals operating at operational level of the CIPS Global Standard

CIPS members can record one CPD hour
CIPS Category Management Tools Guidance Notes

A Category management strategy enables procurement professionals to focus their time and conduct market analysis to fully leverage their negotiations and correctly manage their suppliers in alignment with the corporate objectives. You can also access further category management guidance here.

This document will cover the following models which CIPS members can be downloaded here.

Tools

1. Direct Vs Indirect Spend
2. Category Management Cycle
3. Capex Vs Opex
4. Kraljic Product Positioning Matrix
5. Category Management Template
1. Direct Vs Indirect Spend

Use this model to help understand the difference between direct and indirect costs within procurement and as an aid within category management.

In practice this model can be used to separate the products or services for which a procurement department is responsible. By using this model as a guide to distinguish between different types of costs and how they are linked to the end product or service, a buyer can then allocate the correct resources to each procurement and develop a relationship that suits the need.

For example if a category manager is responsible for the procurement of raw materials to make meals for a hospital, they could separate their costs as the physical food stuff being direct costs and the reusable packaging that the raw materials arrives in, along with other products for the hospital café as indirect.

The disadvantage of this model is that some products or services may be both direct and indirect. It is not always possible to place a procurement solely in one area of the diagram.
2. Category Management Cycle

Follow this CIPS category management cycle to help you define a category management process. To view the CIPS interactive tool click here.

- **Initiate** - Start by defining the categories that procurement will manage: this can be done by using the Direct and Indirect model as a starting point or a guide.

- **Prepare** - Once the categories are defined, visions need to be established so that the buyer or category manager is able to manage the category in alignment with the corporate vision. For example, if the corporate vision is to support local business to develop the local economy, the buyers need to create a vision to use suppliers within close proximity.

- **Prioritise** - Objectives need to be set as part of the process to achieve the vision. Objectives for the local economy, for example, could be to source 50% of direct cost products from suppliers in the same county, state or region within 5 years. Objectives set should always be SMART for ease of measuring the results.

- **Define** - The strategies that should be set as the next part of the process need to reflect the objectives. A strategy for this example could be to contact all suppliers within a 50 mile radius and invite them to tender for all indirect cost related contracts.

- **Implement** - Once the strategies are agreed and approved by senior management, the category manager needs to work with the stakeholders to gain buy in. The strategies need to be supported by everyone to ensure their effectiveness.

- **Maintain** - To help ensure that the strategies are implemented and the objectives are achieved, the category manager can set Key Performance Indicators (KPI) or Service Level Agreements (SLA) which can then be monitored to evaluate performance. A KPI could be to sign three strategic product or service contracts with local suppliers within one year. As per objectives, KPIs and SLAs should aim to be SMART.

- **Improve** - At regular intervals, and the timing of such intervals depends on the nature of the industry, the categories should be reviewed. Procurement is a constantly evolving function so it may be that a category that was relevant at the start of a period becomes obsolete, non-critical or moves from direct to indirect. The reviewing process is important to ensure that categories are always relevant and in keeping with the overall corporate vision.
3. CAPEX Vs OPEX

Use this model to gauge an understanding of which procurements are capital purchases (CAPEX) and which are operational purchases (OPEX).

Some procurement departments manage their categories of spend by separating capital and operational purchases.

This model is an aid to help understand which type of products fit in which category.

A CAPEX item, usually a one-off purchase, is something that is integral to the organisation such as a building, a piece of machinery or some land where a new development may be planned i.e. a green field site which has planning permission for a new hospital to be built would be a CAPEX item to the organisation that bought the land.

An OPEX item is a product or service that is related to the operational function. So in relation to the hospital land, an OPEX item would be the bricks, roofing or labour purchases.

CAPEX items are usually tangible but in the current technological era things such as websites and electronic systems can be classified as CAPEX.
4. Kraljic – Product Positioning Matrix

This model is a tool to help categorise products or services against their level of risk in relation to supply and financial.

The four quadrants of this model identify the importance of the product or service.

- The **strategic quadrant** represents procurements that are critical to the organisation. Products or services within this area require a high level of attention from buyers to ensure that supply is continuous. Failure of supply of these products or services in their correct specification would cause critical problems for an organisation. Relationships between buyers and suppliers of strategic items should be collaborative at the very minimum.

  Using the hospital example, staple dietary requirements from the direct cost category would fall into the strategic quadrant i.e. butter, rice or bread

- **Leverage items** are products or services that cost a large amount but where there are many suppliers from which to choose. CAPEX purchases usually belong in this category. Relationships with suppliers are not as important as in the strategic quadrant.

  An example of a leverage item would be a large digital screen at the entrance of the hospital to display adverts. The item will be of high value but there will be lots of competition in the market.

- Products or services that belong in the **routine quadrant** are usually low value and are available from many suppliers. The market structure of items that belong in this quadrant is likely to be perfect competition.

  An example of a routine item in a hospital could be the hand sanitizer used on the wards. There is an abundance of suppliers that can provide this and the cost is quite low.

  Relationships with the suppliers of routine products do not require much resource and buyers regularly change suppliers to secure an improved cost.

- Items within the **bottleneck** quadrant have a low financial value to the organisation but are not available from many suppliers.

  Within a hospital a bottleneck service could be the removal of any used needles. Whilst this service is relatively low in cost, there are not many suppliers that can offer it but without the service the hospital could not function.
The limitations of this model are that some items can fit into various quadrants if they are used in a variety of end products. Using this model as an aid to category management should include cross-functional work across all buyers to ensure that, where necessary, products or services are grouped together to achieve optimum value.

This theory can be further complimented by the use of the Supplier Preferencing model. The model can be overlaid to show how the suppliers view buyers of each category of product – Kraljic/Preferencing overlay.

The relationship classification model further aids the understanding of how buyers and suppliers view each other and the type of style in which their business should be managed.

You can also download an editable version of the Kraljic matrix to plot your own products and services in the four boxes.
5. **Category Management Template**

Use this template in conjunction with the category management process model and the category management cycle to devise, manage and monitor categories.

When populated this template can be used as part of the whole category management process from the division of the category and what products/services belong within it to the final part of the process where lessons are learned during the reviewing of KPIs and SLAs.