Appraisal and Performance Monitoring of Suppliers

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Welcome to a guide on Supplier Appraisal
1. THE CIPS POSITION
CIPS considers that performance monitoring and assessment of suppliers is a function that is core to P&SM and is in fact a pre-requisite to related activities such as supplier development.

CIPS views, opinions and beliefs are summarised as follows:
• Performance monitoring of suppliers is a fundamental aspect of contract management
• Relationship management is a key skill of P&SM professionals
• P&SM professionals should perceive performance monitoring as a two-way process and be open to feedback and suggestions for improvement from the supplier
• Buyers and suppliers should, as appropriate, jointly measure combined performance towards joint goals
• The monitoring of suppliers' performance should be against that which is agreed in the contract and supporting documentation such as service levels and partnering agreements; and a key objective from the outset should be to aim for continual improvement
• Effective P&SM involves determining the appropriate methods of managing the supply base – different solutions are appropriate for different situations - therefore CIPS cannot be prescriptive about the use of specific measures
• P&SM professionals should also monitor the performance of their main suppliers to ensure they remain familiar with their profiles in terms of growth, market share and financial performance
• P&SM professionals need not undertake the appraisal/assessment of suppliers, or indeed the wider role of contract management. However, they should be responsible for ensuring those who are undertaking the role are properly trained and supported.

2. WHAT ARE THE AIMS AND OBJECTIVES OF THE APPRAISAL AND PERFORMANCE MONITORING OF SUPPLIERS?
At a simplistic level, which may be suitable for suppliers in the non-strategic category, performance can be measured in terms of the following criteria:
• Quality - the percentage of acceptable deliveries in relation to the total number of deliveries received
• Delivery - the percentage of deliveries, delivered on time in relation to the total number of deliveries received
• After-sales service - the time taken in hours/days for queries or problems to be resolved
• Price - the delivered price quoted by a supplier in relation to the lowest delivered price by any one supplier.

A more comprehensive approach could include the following factors:
• An assessment of the level of competence of key personnel within the supplier's organisation
• The capacity of the supplier in terms of physical, intellectual and financial resources, to satisfy the buyer's requirements in full
• Evidence of supplier commitment to the buyer organisation in terms of key areas such as process control, quality control, quality assurance etc
• Evidence of the existence of effective control and information systems
• Full analyses of the suppliers cash resources and financial stability over a reasonable period of time
• A measure of the total acquisition cost (TAC) rather than just price
• A record of the consistency of delivery and quality, preferably with evidence of improvement over time. (Adapted from: R Carter: The Seven Cs of Effective Supplier Evaluation, P&SM, April 1995, pp44-45)

The buying organisation will need to weight each factor according to its importance in the context of circumstances prevailing at the time.

The scope of measurement will depend on:
• value of orders
• time
• criticality of order
• whether it is an ongoing purchase or one-off buy
• factors outside the supplier's control.
An effective strategy for assessing and monitoring suppliers is to approach their current customers with a set of standard questions. These typically will include the following:

1. Have the products or services supplied met the required level in terms of quality and/or delivery time?
2. Has the supplier been able to react speedily and effectively to unscheduled changes in customer requirements?
3. Has the supplier demonstrated a positive attitude when problems have arisen, for instance, in quality standards or delivery arrangements?
4. Is the supplier effective and professional in dealing with sub-contractors?
5. Are you satisfied with the financial standing of the supplier? If not, what particular doubts or reservations do you have?
6. Have you been satisfied with the supplier’s approach to purchasing ethics, as set out in the CIPS ethical code?
7. Does the supplier satisfy current legislation and requirements as far as environmental issues are concerned?
8. Do you have, or would you contemplate having, a partnership agreement with this supplier?
9. Would you recommend this supplier for companies such as ours?
10. May we have your permission to use your company as a reference for our files, either to endorse, or to refrain from, entering into a contractual agreement with this supplier?

Supplier rating and assessment procedures are typically employed when dealing with suppliers who are in a competitive marketplace. Such procedures may be seen as less appropriate or desirable when seen in the context of a partnership relationship or with a monopolistic supplier.

A monopolistic supplier may mean it is the only supplier within a critical distance, or the only supplier who will deal in specific quantities, or with specialised production equipment, and so on. In such cases, the buying organisation may feel that there would be no point in making an assessment of the supplier and from that making demands for improved performance, as they would always have the ultimate threat of removing the supply. However, better knowledge of the supplier may assist the buyer in locating an alternative source, previously thought, for whatever reason, to be unacceptable. Another approach is for both buyer and supplier to undergo some form of assessment, which could lead to ways of reducing the transaction cost between the organisations, to the possible advantage of both parties.

It has been suggested that some form of supplier assessment or monitoring is necessary for most relationships given the lack of trust which often characterises the buyer/supplier relationship. When a buyer is faced with a competitive market, there is contractual trust, ie both parties rely on the word of the contract rather than trusting and communicating with one another. Some form of assessment is necessary to ensure that the incumbent supplier’s performance is in line with, or better than, the market. The next level of trust is competence trust where the buyer organisation trusts the competence of the suppliers but not necessarily the management. The third level of trust is referred to as goodwill trust which is associated with partnerships.

It has been suggested that supplier appraisal and monitoring procedures are not necessary in a true partnership because the organisations totally trust each other’s management to strive for world class performance within their supply chain. Evidence of such appraisal or monitoring in a partnership could, therefore, be indicative of the failure of that partnership. However, it could also be argued that supplier appraisal and monitoring procedures can be undertaken with a view of continuous improvement to both organisations, so it would be to the benefit of the partnership. By analysing other suppliers, the partnership can ensure that it is always the best it can be. It can also be argued that lack of trust is considered by most businessmen as commercial reality. Purchasing managers will wish to avoid an accusation of complacency about the suppliers if the partnership does not live up to expectations.
3 WHY ARE SUPPLIER APPRAISAL AND PERFORMANCE MONITORING NECESSARY?

Suppliers can have a significant impact on the success or failure of the organisation. As a result, one of purchasing’s key activities is securing the best suppliers, in terms of value for money, to operate within the supply chain. Depending on the strategic nature of the product, the buying organisation may be interested in not just their own supplier but in the supplier’s suppliers; this can be seen most clearly in the car industry where supplier tiering is common.

A suggested checklist for existing non-strategic suppliers is as follows:

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If the answer to most of these questions is yes, perhaps it is time to investigate other suppliers to ensure that your non-strategic supplier relationship is indeed the best available situation, and is not just continuing out of habit.

4 WHAT DO WE MEAN BY A GOOD SUPPLIER?

If he is doing his job properly a buyer will need to know what to look for as far as the supplier and his range of products are concerned. To take a random example in Purchasing Management Handbook by Aubrey Grant, the chapter Purchasing Castings highlights what buyers of castings are recommended to look for when assessing suppliers. These are as follows:

- Casting materials (metals)
- Process selection
- Casting design
- Pattern equipment
- Testing
- Equipment selection
- Foundry selection
- Purchasing policy
- Quality routines
- Delivery reliability

Whilst some of these performance measures are specific to the foundry industry (similar industry-specific lists could be drawn up for, say, the catering and motor industries) there are some parameters, such as delivery reliability, which are common to suppliers in most sectors of industry. Thus a generic list of supplier performance criteria might include: quality; delivery; commercial competitiveness and technological competence/expertise. Each may be subdivided further – delivery for instance, comprises aspects such as responsiveness and reliability.

Is age a factor?

Is the length of time a supplier has been in existence a valid criterion for assessing supplier performance?

To take technological competence as an example, the age of the supplier company may be viewed as either maximising or minimising that parameter. It could be argued either that a long-established company is fully conversant with the technology within its particular field and is experienced in applying it, or, alternatively, that a new company has not had time to acquire a high level of technological expertise, but as part of its learning curve is always ready to seek out and employ (if appropriate) the latest technological advances. This accords with common sense and with the perception that long-established companies are by and large content with existing technology and are probably less inclined to be innovative than newer companies are. That said there will inevitably be many exceptions to this general rule as the following three examples illustrate.

Whitechapel Bell Foundry

This is one of the oldest companies in the UK, dating from 1570. The manufacturing technology (including the composition of the bell metal) is old and well-
established, but this is not to say that improvements and refinements in manufacturing techniques have not taken place over the years. These improvements have enabled WBF to establish and enhance its worldwide reputation. WBF has firmly established itself in a niche market and has little if any need to market its services; its customers come from all parts of the world.

**Ford**

Turning now to a radically different area of manufacture (the motor industry) - and specifically one company, Ford. Like WBF Ford has global reach even though it has been in existence since for a much shorter time than WBF (the Ford Motor Company came into being in 1903). During the century that it has been in existence the company’s products, with some notable exceptions such as the Edsel saloon, have followed a course of progressive improvement. Customer service has improved dramatically not least because of pressure from the competition even though many of the early players in the US market have long since vanished from the scene.

**Honda**

Whilst the history of Ford is relatively short compared to WBF that of Honda is shorter still (the company dates from 1948). The generally held view is that the Honda range of products are of very high quality, being manufactured in accordance with their well-known emphasis on manufacturing on a zero-defect basis. This philosophy, of course is also applicable to other Japanese companies such as Toyota, Sony or Hitachi.

**5 WHAT ARE THE ADVANTAGES OF ASSESSING/MONITORING SUPPLIER PERFORMANCE?**

1. Any identified weaknesses on the part of the supplier can be addressed or concessions/compensation sought for poor performance.

2. The data may be used to evaluate and compare performance of new suppliers.

3. Measurement can be used as the basis for continuous improvement (kaizen).

4. Measurement on a two-way basis can highlight the buyer's deficiencies, which may be the source of common problems within many supplier relationships.

5. Objective and subjective measurements give an overall picture of the supplier’s/buyer’s performance.

6. Each company gains a better understanding of the constraints, deadlines, potential, etc affecting the relationship.

7. It helps to remove or reduce emotive issues such as personal relationships between buyer and supplier.

**6 WHAT ARE THE DISADVANTAGES?**

1. The time and resources cost of carrying out measurement activities.

2. Assessing only objective or only subjective criteria could lead to skewed results. It is necessary to take account of both.

3. The weightings and the actual scores given to suppliers can be influenced by a biased buyer.

**7 WHAT ARE THE KEY ELEMENTS OF SUPPLIER PERFORMANCE?**

In summary, there are three different aspects to the monitoring of supplier performance post-contract:

1. Gathering factual, and therefore objective, information about their performance such as lead-times from order, quality standards being met, pricing compliance and whatever else is set out in the contract. This type of information can usually be obtained from IT systems within the organisation in the form of management information. With all these aspects, it is good practice to be as consistent as possible in the approach to assessment and performance monitoring.

2. Ascertaining the views and experiences of the customers in respect of service, attitude and response rates for instance (which should be as objective as possible and reflect reality but, inevitably may in some cases be subjective). One way to collect information on performance is by individual interview against a defined set of questions. This can be face to face or on the phone but needs to be interactive so that the interviewer can explore the background when necessary. The P&SM function will have to assess the validity of any subjective remarks. Sometimes commitment is required from customers, such as engineers in the field, to keep records of their experiences of working with a supplier in order that objective factual data can be used. Another way is to undertake customer satisfaction surveys which can be quite short and distributed by email.

3. The supplier’s experience of working with the buying organisation must also be considered in the evaluation, as it might be the case that they are facing unnecessary obstacles, or perhaps are dealing with difficult people.
8 HOW IS SUPPLIER PERFORMANCE ASSESSED?

There are a number of key themes which might be used to assess supplier performance and which might be used as a yardstick for determining whether good practice is being achieved in specific situations. Some examples of such themes (together with their sub-categories) are as follows:

**Product Quality**
- MTBF (Mean Time Between Failure)
- Percentage of incoming rejects (delivery accuracy)
- Warranty claims.

**Service Quality (against agreed SLAs)**
- Call-out time
- Customer service response time
- Performance against agreed delivery lead times.

**Relationship/Account Management**
- Accessibility and responsiveness of account management.

**Commercial**
- Costs are maintained or reduced.

Whilst traditional hard key performance indicators such as those above are obviously important it is advisable also to be aware of the so-called soft ones, frequently encountered in other contexts. These include difficult-to-measure considerations such as ethical issues, professional relationships and cultural fit.

The measures, objectives and targets used in the monitoring of suppliers’ performance must reflect those that were agreed when the contract was let. That is why it is important to specify a commitment to continuous improvement at the outset. It would be unfair to the supplier to suddenly introduce a range of measures after the contract had begun – however if such an introduction mid term through the contract is unavoidable then it should be negotiated and agreed in a professional manner and not merely imposed on the supplier in an arbitrary fashion.

CIPS believes that suppliers should always be asked to continually improve their contract performance. However, incentives are required for the supplier to reflect improvement in costs or to give more for the same price. Competition and the possible loss of business may well be an incentive. However where the supplier is aware that there is little risk of that (in a genuine sole-source situation for instance) things may be very different.

There is arguably another reason for doing it, in that over time the market and the needs of the customer can change and these needs need to be taken into account. An example might be the closure of a distribution terminal because of the construction of a new road which means that an operation could be serviced from some other terminal.

**Supplier Visits**

These are an important element both in the initial appraisal and also in the post-contract performance monitoring process.

The following is a checklist of those areas requiring particular attention by staff of the purchasing department when they carry out such visits.

**Personal attitudes**
The state of morale in the supplier’s workplace is obviously of importance. Much can be gleaned from:
- Whether any employee dissatisfaction appears to be present
- The level of interest in customer service shown by supervisory staff
- The level of energy displayed
- Whether manpower is being used effectively, with everyone busy.

**The condition of the manufacturing equipment**
Dirty and poorly maintained equipment tells its own story. Conversely, sophisticated and innovative equipment betokens an organisation which is au fait with the latest technological advances.

**Quality control**

Evidence of effective QC procedures is, obviously, a good sign.

**Housekeeping**

A plant which is orderly and clean in its general appearance is indicative of careful planning and control by management.

**Expertise of technical staff**

Conversations with these employees will reveal their level of knowledge of the latest developments and expected future trends within the industry.

(taken from Purchasing and Supply Chain Management, by CK Lysons and B Farrington)

9 HOW IS THE PERFORMANCE OF KEY SUPPLIERS ASSESSED?

Key suppliers of high value and high risk goods and services (outsourced service providers for instance) demand close performance monitoring and this is where most resources should be employed. This might involve monthly meetings where performance is discussed, issues resolved and new targets set as appropriate. CIPS encourages P&SM professionals to hold feedback meetings with suppliers at suppliers’ premises so enabling them to assess efficiency levels on the supplier’s home ground. The situation may however
be somewhat different for outsourced services such as cleaning or catering. In this case the meeting should be held where it facilitates inspection of the problem areas. This approach also ensures that members of the outsourcing contractor’s senior management team are present.

Suppliers providing goods and services on security/bottleneck type goods and services in those which are relatively low value but of significant importance to the organisation for whatever reason, need regular monitoring. In some cases supplier failure can result in significant financial loss to the business, or even failure. The final and in many ways, the most straightforward significant category of spend is leverage ie high value/volume and low risk. The usual method of monitoring the performance of such suppliers is to hold quarterly meetings in which feedback from both parties is reviewed.

However, it is not just term contracts that need monitoring; suppliers of capital equipment who provide maintenance services should also be monitored. This is to ensure that their service is consistent with what was agreed at the outset, and indeed that the performance of the equipment meets the customer’s expectations.

10 PERFORMANCE MONITORING OF SUPPLIERS AND ITS FIT WITHIN P&SM

For the purposes of this document the term suppliers includes contractors for works and services as well as supplies; the term performance monitoring means measuring a supplier’s ability to comply with, and preferably exceed, their contractual obligations ie monitoring post-contract.

CIPS believes that supplier appraisal/ performance monitoring is a fundamental element within contract management and supplier development (the latter topic is covered in a separate CIPS practice guide). Contract management includes activities of a buyer during a contract period to ensure that the seller fulfills all his obligations under the contract.

At the start of a contract there is inevitably a degree of risk and uncertainty for the parties involved. As the contract proceeds both parties learn from experience and the risk begins to diminish as the original contract assumptions come to be tested. For these reasons it is important to hold regular review meetings where both parties ask how they can make the contract perform better. Hence the need for monitoring and measurement of performance against that agreed in the contract as well as its supporting service level descriptions and other documentation such as partnering agreements. These meetings should be two-way, with both parties learning from each other. Thus the buying organisation needs to seek the supplier’s comments as to how well they are carrying out their side of the contract, for example, to check whether all information is being provided on a timely basis.

It is vital that the buyer keeps managing the supplier and deals with problems as and when they arise. If a supplier begins to suffer financial strain in discharging his obligations then, commercial nature being what it is, the supplier will begin making behind-the-scenes cutbacks, irrespective of what may or may not be specified in the actual contract. The key is to address problems when they are still minor and therefore easier to resolve.

There are many contractual relationships with suppliers where it is more important to agree joint goals and jointly measure performance against these goals – rather than the buyer simply monitoring the supplier’s performance. This requires transparency and a sharing, as appropriate, of business goals. This type of relationship allows for the supplier to monitor performance if a suitable process of validation is in place.

Relationship management is part of the performance monitoring process. It is a key skill for the buyer and can be summarised as the pro-active development of particular relationships with suppliers. A managed relationship is one in which both parties are sufficiently intimate that they each know how the other will react; the relationship is predictable. The purpose of investing in a relationship with a supplier is to improve the supplier’s performance in fulfilling the needs of the buying organisation. CIPS has produced a separate practice guide on this related subject.

Any activities ought to be on a prioritised basis as the benefits realised need to be proportional to the degree of effort expended by both parties. Performance monitoring can be a time-consuming task and so the effort and methods should be proportionate to the value and importance of the contract. CIPS believes that effective P&SM involves determining the appropriate methods of managing the supply base. Different solutions are appropriate for different situations. Although not always appropriate, supplier reduction programmes have helped in the management of the supply base and are particularly beneficial in respect of monitoring suppliers.

CIPS believes that a further purpose in undertaking supplier assessment/ performance monitoring is to provide an opportunity for the supplier to propose changes in the behaviour/approach of the buyer in order to enable them (the supplier) to improve their performance. For example there may be different solutions open to the buyer which could be value adding.

Assessing and monitoring the performance of suppliers is a key aspect of P&SM but one which can easily be under-resourced and neglected. When performance monitoring is undertaken post-contract, the purpose is twofold:
a) to ensure that the supplier is meeting the performance criteria eg service levels and quality, laid down in the contract.
b) to identify room for improvement.
The object of performance monitoring is to improve performance of all parties involved in the contract; it should not be seen as a way of attacking the supplier. Both parties have to perform and learn to measure each other and provide feedback.

11 WHAT ARE THE RESPONSIBILITIES OF THE BUYER?
As stated above, CIPS recommends the practice of ensuring that performance criteria are an explicit part of the contract so that both parties are fully aware of what is required of them post-award.

Although monitoring performance of suppliers should be directed and managed by the P&SM function, it need not necessarily be carried out by them. CIPS believes it to be of critical importance that whoever carries out performance monitoring (and especially the review meeting with suppliers) is properly trained and supported by the P&SM department. This is particularly important when the payment mechanism in the contractual arrangement is contingent on supplier performance. It should be borne in mind that it is the technical people, who may well not appreciate commercial nuances, that need to be encouraged to carry out the monitoring process.

In the event that a supplier consistently fails to meet the requirements of the contract, and does not respond to feedback or suggestions, then the remedies set out in the contract must be brought into play.

Since performance monitoring should lead to continual improvement from suppliers, most suppliers would expect a long-term business relationship with the client. This may involve contracts of several years duration, with options to extend for further periods if the supplier’s performance is satisfactory.

A further consideration is that monitoring suppliers should not just be about their day-to-day performance as viewed by their trading partners, but also in their performance as a business. CIPS strongly encourages P&SM professionals to monitor the performance of their main suppliers, for example, in terms of their growth, market share and financial standing in order that the buyer remains aware of the profile of his key suppliers. In the case of particularly key suppliers – regular meetings with their directors on strategy and future policy and prospects is important with perhaps P&SM professionals being present to provide a common thread. This however assumes the companies who are party to the contract are of similar size. The reality may be different so that the buyer in an SME for instance will almost certainly have a different perspective to that enjoyed by a global supplier.

12 HOW CAN SUCCESS BE ENSURED?
The prospect of success can be maximised, if not guaranteed, if the following recommendations are borne in mind:

1 The time and resources put into measurement must be commensurate with any benefit realised.

2 Time and resources are also affected by simplicity of systems for measuring performance. A system easily understood by suppliers and buyers alike is less likely to be viewed with suspicion.

3 Performance measurement is a useful tool, but it is just that, a tool. A buyer’s own perception of the relationship is equally important, especially if the measurement exercise has not been able to cover a significant factor.

4 The weightings applied to the measurement criteria must reflect the needs (and perhaps changing needs) of the organisation. If the organisation uses Just-In-Time techniques, then delivery will probably require a higher weighting than, say, price.

5 Measurement criteria should, as a minimum, be discussed with the suppliers prior to implementation. In this way, any criteria outside the supplier’s control or unfair additions can be identified. The suppliers may have useful additions to make to the list. It also helps the supplier to improve performance if the supplier is aware of what is being measured and thus what is important to the purchaser.

6 The use of existing information for measurement purposes will avoid expense and time. Such information can be goods received notes (what and when supplied), rejections (quality of goods supplied) and quotations (deviation from original price/cost).

7 Depicting suppliers’ performance in graph format in a prominent position within the organisation:

• provides information at a glance
• prevents information becoming buried in tables
• emphasises the importance that the organisation places on suppliers’ performance
• provides evidence of continuous improvement, or otherwise
• allows visiting suppliers to rate themselves against others.

8 Both buyer and supplier organisations should be deriving benefit from the vendor rating exercise. In this way, both organisations will look for ways to improve the relationship and supply chain, rather than the
exercise degenerating into apportioning blame or a series of excuses for poor performance. Measurement will become a motivating factor rather than a chore which has to be endured.

9 The buying organisation should set up a recognition and reward system. In this way, there is visual and loud acknowledgement of outstanding supplier performance. Recognition and reward can be in the form of annual supplier awards, letters of praise from the CEOs of the buying organisation, which can be displayed prominently in the supplier’s foyer, as well as sharing of profits, or closer ties such as a partnership.

13 WHAT ARE THE MAIN REASONS FOR FAILURE?
1 Often the measurement procedure is not used consistently, which in turn eliminates any ongoing benefits.

2 Failure by the buying organisation to feedback the results of its measurement to the suppliers in order to allow them to implement changes.

3 Failure by the buying organisation to take on board the comments made by suppliers after receiving feedback on the results.

4 Suppliers not being consulted when the measurement criteria to be included in the assessment is determined. This can result in unrealistic or ambiguous criteria.

5 Suppliers not being informed of the measurement criteria and required standards until after the assessment process has been completed.

6 Suppliers viewing the measurement process as simply an excuse to rationalise the supplier base, rather than an ongoing improvement exercise for both parties.

7 Over-complicated measurement criteria, which do not correspond to the level of benefit derived.

8 Inflexible weightings applied to all of the criteria for all of the suppliers. There should be a different weighting applied according to the strategic importance of the supply. The Kraljic Matrix Box can be used for dividing procurement into strategic, leverage, routine and bottleneck categories.

9 Communication lines being shut as soon as problems arise. If the supplier feels comfortable in immediately discussing potential problems, then any difficulties can be avoided or minimised.

14 REFERENCES
Books
Most purchasing textbooks contain a section or chapter on supplier appraisal and performance monitoring.
Titles include:
- Purchasing and Supply Chain Management
  C.K. Lysons and B. Farrington
  2006
- Measuring Procurement Performance
  R. Carter and J. Leech
  2002
- Managing External Suppliers
  B. Hughes
  2001
- Supplier Appraisal (a title in the CIPS ‘How To’ series)
  C. Lysons
  CIPS 2002
- R. Russil
  Purchasing Power: Your Suppliers; Your Profits
  1997
Articles
Numerous articles on supplier performance assessment and monitoring, many of a case study nature, may be accessed through the Archive Search section of the Supply Management website - www.supplymanagement.com

The annual conferences of IPSERA (International Purchasing and Supply Education and Research Association) have featured papers of a more academic nature. The website is www.ipsera.org

Websites
www.nao.org.uk
www.crownagents.com
www.bipsolutions.com
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