

THE POWER OF PURCHASING

PURCHASING CAN BE A STRATEGIC ADVANTAGE, BUT ONLY IF YOUR COMPANY VIEWS IT AS A STRATEGIC FUNCTION

By Tony L. Callahan

The current median home price is at an all-time high and interest rates are rising. If the mounting costs that have plagued our industry during the last four years continue on their current trajectory, the next housing downturn could be sooner than you think. The power of purchasing—the strategic utilization of the purchasing function to assure best quality, minimize cost, mitigate risk, and manage capacity—can help offset this rise.

Maintain quality. Knowing the required quality level for everything purchased is central to a purchasing professional's responsibility. Purchasers know that price should never be prioritized if it means sacrificing quality. If quality level doesn't meet company requirements, you paid too much.

Understanding quality requires good judgment. Consider this: A 2x4 that is defect-free and truly perfect—not a single knot, discoloration, or scratch—could be yours for \$15.92 each (plus freight). Is that a good deal? No. A good purchasing professional assesses the quality requirements of a 2x4 based on its use. The quality standard for a 2x4 stud is, of course, that it's the proper species and grade, is straight, and is in good condition for the application in which it's to be used. By that definition, the cost of a 2x4 stud would be less than \$2.53 each (plus freight). With that definition in mind, a 2x4 that's warped, split, and has excess wane doesn't meet the quality requirements for a stud.

So it goes that purchasing 2x4s that don't meet quality requirements, even at a low price, will result in excessive costs while the framer spends extra time going through the bunk trying to find a good one. If a poor-quality stud is inadvertently used, it will be costly to replace or sister to a 2x4 of acceptable quality. My point: There's a real cost to poor quality.

But it goes both ways. Setting the quality standard for the same 2x4 as knot-free, scratch-free, and of perfect color will result in excessive costs. It's essential that your purchasing team understands the quality requirements of each product and each scope of work for which they're responsible. Undershooting or overshooting the organization's quality requirements can be costly.

Manage costs. The purchasing function can have a tremendous impact on a business's bottom line. If your purchasing department isn't keeping costs in check, it will be tough for your sales department to pick up the slack. Good purchasing professionals view any price increase as if it were coming out of their own pockets. They do extensive due diligence before approving any price increase.

Diligence in keeping costs down takes a certain personality type: one that isn't afraid to ask questions, challenge assumptions, and validate the reasons behind the increase. It's someone who's not hesitant to follow up and follow through. Not everyone is comfortable in that role. A purchasing professional has essentially been given the company checkbook and

has been asked to spend the company's money wisely. He or she needs to be aware that the employer has extended them an enormous amount of trust.

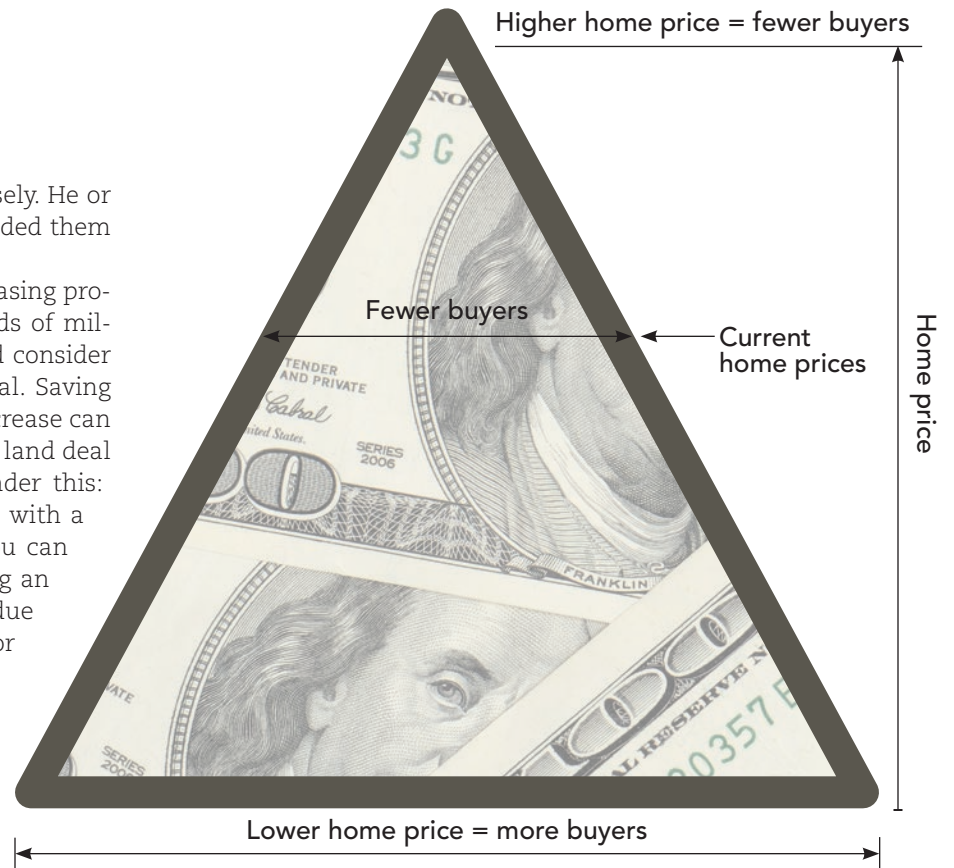
Depending on the size of the organization, purchasing professionals control hundreds of thousands, hundreds of millions, or even billions of dollars. Companies should consider this when hiring their next purchasing professional. Saving even a few percentage points or avoiding a price increase can mean the difference between making a prospective land deal work or not. Purchasing professionals should ponder this: The next time you're very busy and are presented with a cost increase, which you're tempted to take so you can move onto the next task, remember that approving an increase is far more difficult if you haven't done due diligence and if you see yourself as the one paying for the increase. This is how your employer would want you to see it.

Mitigate risk. Purchasing needs to leverage the organization's spend so it can be competitive in the marketplace, with no sacrifice of safety, quality, or capacity. Sometimes it means single-sourcing a given material, supplier, or trade category. Other times it means expanding the material specs, suppliers, or trade base. Purchasing demands constant evaluation and, when needed, corrective action to mitigate risk.

Mitigating risk requires a dynamic approach. What kind of financial shape are your current suppliers in? Does the supplier tend to take on more work than it can perform within the required time frame? Risks vary depending on the housing cycle. In a boom phase, capacity is front of mind. In a down cycle, trade longevity is a greater concern.

Expand capacity. Purchasing must ensure that it has enough capacity within each material and trade category to be certain the organization can meet its customer commitments. That requires strategically working with trades to develop additional capacity and identifying new sources of capacity where needed. To do this well requires extra effort. Get out of the office to meet with trades in the field. Drive competitive jobsites to scope out new sources of supply. Attend local home building events and network with other industry professionals outside of purchasing.

Identify and develop trades. Good purchasing professionals know that safety, quality, cost, and cycle time are important. They understand the need for strategic relationships with manufacturers, distributors, and trades. They forge relationships with companies that give more than just lip service to safety, that work to keep quality high and costs low, are involved in a builder's new product development projects, provide open-book cost transparency, work jointly to lower costs, engage in joint initiatives to improve safety on the jobsite, and



Climbing prices are shutting out some potential buyers, but savvy purchasing can help offset pressures exerted by market conditions.

meet schedules by doing whatever it takes. Every purchasing pro wants to work with strategic manufacturers, distributors, and trades like these. You probably know of at least one, but sadly, they're few and far between.

Each situation is unique. Some purchasers make the mistake of treating every trade as a partner, even when they're not. Others err on the side of treating every trade as suspect, even when they're not. Savvy purchasing pros know the difference, and they know how to manage each situation. They also understand that a critical part of their job is to find and develop strategic trades. This requires qualifying new trades, working with construction to onboard them, and doing everything possible to make the new trade successful. Savvy purchasers don't fall into the trap of thinking there's only one brand of material that will work or only one trade that can install it.

It's no wonder that companies are upping compensation packages to attract the best purchasing talent. Purchasing has a big impact on the organization's success. A good purchasing pro who can maintain quality, minimize costs, mitigate risks, and adjust capacity as needed can produce results that are in excess of 10 times the cost to employ him or her. **PB**

Tony L. Callahan, CPSM, CSCP, has worked in the home building industry for nearly two decades.