LIFE INSURANCE & HEALTH PLAN SOURCING STRATEGY
FOR LATIN AMERICA

MASTER IN BUSINESS ADMINISTRATION

FIELD PROJECT PRESENTED BY:

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**EXECUTIVE SUMMARY**

What is a strategy? Which are the benefits and when do we need to use it?, Which tools should be used and what kind of results can be obtained?

A strategy is Alternative chosen to make happen a desired future, such as achievement of goals, solution to problems and through a careful selection and application of resources to obtain a competitive advantage in productivity in business.

“BMG” is an American company of consumption products founded in 1850 with Worldwide operations. Currently the company has 140,000 employees, having 7,000 in Mexico City. The main products are: Shampoos, Hair Conditioner, Bathroom supplies, tooth paste, etc which can be classified as personal, beauty and health care products.

**Strategic Sourcing area** is focused in Employee Services is responsible to negotiate services related to employee benefits such as: Cars, Insurance cars, Life Insurance, Health Plan, Medical Services, EAP (Employee Assistance Program), Gifts, Employee Transportation, etc.

This project is a “**Sourcing Strategy of Life Insurance and Health Plan for Latin America**“, showing which steps and tools should be followed and used to create and implement the strategy, such as: Market and Industry Analysis, Porter Model, SWOT, Sourcing Choice Model, Theoretical references, internal and external company environments and services specifications and information.

At the end, a sourcing basis for the next 3 years is created, looking for the continuous market evaluation, concluding with new strategic purchasing decisions, such as: Suppliers database reduction, improve commercial relationships, select key insurance companies and brokers, searching process optimization, financial savings, strategic organizations and best practices, globally and across the region.
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1.- Introduction and Background.

"BMG" is an American company of consumption products founded in 1850 with Worldwide operations. Currently the company has 140,000 employees, having 7,000 in Mexico City. The main products are: Shampoos, Hair Conditioner, Bathroom supplies, tooth paste, etc which can be classified as personal, beauty and health care products.

The Company has the Purchasing organization divided in 2 areas: Sourcing and Procurement. The First one is responsible to perform negotiations, evaluate suppliers, make market and industry analysis, competitive bidding, sourcing strategies, create and sign legal contracts and create savings projects.

Procurement is responsible to create purchasing orders, follow up of the payments, purchases and deliveries having direct contact with sourcing confirming the active and approved suppliers.

"BMG" company has manufacturing and commercial operations in the 5 continents. In Latin America the main countries in which Purchasing area needs to be involved are: México, Guatemala, Chile, Brazil, Costa Rica, Argentina, Venezuela, Colombia, Peru and since April 2008 in Panama, as is described in Figure 1.

WORLDWIDE OPERATIONS

Figure 1: BMG Worldwide Operations
2. - **Problem Description.**

Strategic Sourcing area is focused in Employee Services is responsible to negotiate services related to employee benefits such as: Cars, Insurance cars, Life Insurance, Health Plan, Medical Services, EAP (Employee Assistance Program), Gifts, Employee Transportation, etc.

5 Sourcing Resources are responsible of Employee Services Requirements in Latin America: 2 located in the North, 1 in Central and 2 in South Region.

**Employee Services** are restricted to local laws, benefits, taxes and specifications; The Sourcing team is performing local negotiations. If they need to renew the Life Insurance policies for example, of Mexico, they just evaluate in that moment Mexico, evaluating the brokers and insurance companies, but they are not evaluating all the region, performing a market and industry analysis of this service in a regional basis, they are focusing the efforts just in the countries they are located, developing local sourcing interventions not strategic sourcing work.

- The business impact to perform local interventions/ negotiations are as follows:
  - The business is losing leveraging opportunities.
  - The team does not have regional vision and knowledge.
  - Even the resources are located in strategic locations in Latin America, the resources and costs to renew services in every country is high, due every purchasing resource is negotiating the same but in his/her country and not regional bidding process are being performed.
  - Due lot of bidding process are needed, the team is not having control in annual spend, current suppliers and really create a strategic work, just quick interventions to renew the service or satisfy the business need.

These problems are the same in all the Employee Services of Latin America. Due Life Insurance and Health Plan services are the most important of the employee benefits and represents around 31 percent of the spend, the solution to mitigate the problems and create the basis for future negotiations of these services and other employee services, was to create a “**Regional Sourcing Strategy for Life Insurance and Health Plan**”
The objective of this **Sourcing Strategy** is to evaluate tools, methodologies, market trends, innovative concepts, internal commercial situation of “BMG” Latin America including data, agreements and purchasing perspective of **Life Insurance and Health Plans across the region**, that through theoretical and practical approaches allow to create and implement a **Purchasing strategy** knowing the market behavior, internal and external strengths, weaknesses, and opportunities, obtaining better coverage, benefits, hard savings, staff capability, consolidating suppliers relationship and performance, and reinforce the control in the Purchasing Team, delivering sustainable results.

### 3. - Theoretical Reference.

**What is a strategy?** Which are the benefits and when do we need to use it? In the case of “BMG” Purchasing, Which tools should be used and what kind of results can be obtained?

A **strategy** is Alternative chosen to make happen a desired future, such as achievement of goals, solution to problems and through a careful selection and application of resources to obtain a competitive advantage in productivity in business.

Scott-Morton, (1991) views an organization shaped by five main forces: Strategies, Structure, Processes, People and Technology, which has a lot of sense due the companies need these 5 factors to be competitive. In this Project Strategy we will review how these key factors should be considered in order to match in one Purchasing Strategy.

Since 1970 until now, several tools and methodologies have been created and developed in universities and companies in order to join and understand concepts, environmental and economical factors that can be matched providing different visions, creating a strategy to solve specific problems or goals.

For this Sourcing Strategy, strategic tools will be used, such as: **Porter Model** created by Michael Porter, 1979, The Porter Model is also known as "Porter's Five Forces", **SWOT Analysis**, technique that is credited to Albert Humphrey, 1960, **Sourcing Choice Model** developed by different Consulting firms and customized by transnational companies.
The concept of health insurance was proposed in 1694 by Hugh the Elder Chamberlen from the Peter Chamberlen family. In the late 19th century, "accident insurance" began to be available, which operated much like modern disability insurance.\(^1\) This payment model continued until the start of the 20th century in some jurisdictions (like California), where all laws regulating health insurance actually referred to disability insurance.\(^2\)

Accident insurance was first offered in the United States by the Franklin Health Assurance Company of Massachusetts. This firm, founded in 1850, offered insurance against injuries arising from railroad and steamboat accidents. Sixty organizations were offering accident insurance in the US by 1866, but the industry consolidated rapidly soon thereafter. While there were earlier experiments, the origins of sickness coverage in the US effectively date from 1890. The first employer-sponsored group disability policy was issued in 1911.\(^3\)

Before the development of medical expense insurance, patients were expected to pay all other health care costs out of their own pockets, under what is known as the fee-for-service business model. During the middle to late 20th century, traditional disability insurance evolved into modern health insurance programs. Today, most comprehensive private health insurance programs cover the cost of routine, preventive, and emergency health care procedures, and also most prescription drugs, but this was not always the case.

Hospital and medical expense policies were introduced during the first half of the 20th century. During the 1920s, individual hospitals began offering services to individuals on a pre-paid basis, eventually leading to the development of Blue Cross organizations.\(^4\) The predecessors of today's Health Maintenance Organizations (HMOs) originated beginning in 1929, through the 1930s and on during World War II.

### 3.1 PORTER ANALYSIS

The significance to use the Porter Model in this project is to understand according with the market which are the strengths and weakness, that the organization has, confirming if Life
Insurance and Health Plans have substitutes in the market, if there is rivalry, barriers to enter in the market and supplier and buyers power level. **The objective is to define which are the 5 forces involved in the Life Insurance and Health Plan markets, in order to be a key factor in the strategy creation.**

**The Porter’s 5 Forces tool** is a simple but powerful tool for understanding where power lies in a business situation. This is useful, because it helps you understand both the strength of your current competitive position, and the strength of a position you’re looking to move into.

With a clear understanding of where power lies, you can take fair advantage of a situation of **strength**, improve a situation of **weakness**, and avoid taking wrong steps. This makes it an important part of your planning toolkit.

Conventionally, the tool is used to identify whether new products, services or businesses have the potential to be profitable. However it can be very illuminating when used to understand the balance of power in other situations too.

**How to use the tool:**

Five Forces Analysis assumes that there are five important forces that determine competitive power in a situation. The five forces are as follows:

- **Supplier Power:** Here you assess how easy it is for suppliers to drive up prices. This is driven by the number of suppliers of each key input, the uniqueness of their product or service, their strength and control over you, the cost of switching from one to another, and so on. The fewer the supplier choices you have, and the more you need suppliers' help, the more powerful your suppliers are.

- **Buyer Power:** Here you ask yourself how easy it is for buyers to drive prices down. Again, this is driven by the number of buyers, the importance of each individual buyer to your business, the cost to them of switching from your products and services to those of someone else, and so on. If you deal with few, powerful buyers, they are often able to dictate terms to you.

- **Competitive Rivalry:** What is important here is the number and capability of your competitors – if you have many competitors, and they offer equally attractive products and services, then you’ll most likely have little power in the situation. If suppliers and buyers
don’t get a good deal from you, they’ll go elsewhere. On the other hand, if no-one else can
do what you do, then you can often have tremendous strength.

- **Threat of Substitution:** This is affected by the ability of your customers to find a different
way of doing what you do – for example, if you supply a unique software product that
automates an important process, people may substitute by doing the process manually or by
outsourcing it. If substitution is easy and substitution is viable, then this weakens your
power.

- **Threat of New Entry:** Power is also affected by the ability of people to enter your market.
If it costs little in time or money to enter your market and compete effectively, if there are
few economies of scale in place, or if you have little protection for your key technologies,
then new competitors can quickly enter your market and weaken your position. If you have
strong and durable barriers to entry, then you can preserve a favorable position and take
fair advantage of it.

The 5 forces are represented in the **Figure 2:**

![Figure 2 “Porter’s Five Forces”](image-url)
3.2 SWOT ANALYSIS

SWOT analysis will be useful in this project, due to define a Purchasing Strategy is definitively necessary to understand and evaluate external and internal organizational key factors, such as: The Company's Strengths, Weaknesses and Market Opportunities and Threats. SWOT references and detailed explanation is described as follows:

SWOT Analysis is a strategic planning tool used to evaluate the Strengths, Weaknesses, Opportunities, and Threats involved in a project or in a business venture. It involves specifying the objective of the business venture or project and identifying the internal and external factors that are favorable and unfavorable to achieving that objective.

Strategic Use: Orienting SWOTs to an Objective:

If SWOT analysis does not start with defining a desired end state or objective, it runs the risk of being useless. A SWOT analysis may be incorporated into the strategic planning model. The structure of a SWOT analysis is shown in Figure 3.

Strengths: attributes of the organization that are helpful to achieving the objective.

Weaknesses: attributes of the organization that are harmful to achieving the objective.

Opportunities: external conditions that are helpful to achieving the objective.

Threats: external conditions that are harmful to achieving the objective.

Identification of SWOTs is essential because subsequent steps in the process of planning for achievement of the selected objective may be derived from the SWOTs.

Figure 3 “SWOT Analysis”
First, the decision makers have to determine whether the objective is attainable, given the SWOTs. If the objective is NOT attainable a different objective must be selected and the

**Evidence on the Use of SWOT.**

SWOT analysis may limit the strategies considered in the evaluation. "In addition, people who use SWOT might conclude that they have done an adequate job of planning and ignore such sensible things as defining the firm's objectives or calculating ROI for alternate strategies." Findings from Menon, (1999) and Hill and Westbrook, (1997) have shown that SWOT may harm performance. As an alternative to SWOT, J. Scott Armstrong, 1996 describes a 5-step approach alternative that leads to better corporate performance.

These criticisms are addressed to an old version of SWOT analysis that precedes the SWOT analysis described above under the heading "Strategic and Creative Use of S.W.O.T. Analysis." This old version did not require that SWOT's be derived from an agreed upon objective. Examples of SWOT analyses that do not state an objective are provided below under "Human Resources" and "Marketing."

**Internal and external factors:**

The aim of any SWOT analysis is to identify the key internal and external factors that are important to achieving the objective. SWOT analysis groups key pieces of information into two main categories:

**Internal factors** – The strengths and weaknesses internal to the organization.

**External factors** – The opportunities and threats presented by the external environment.

The internal factors may be viewed as strengths or weaknesses depending upon their impact on the organization's objectives. What may represent strengths with respect to one objective may be weaknesses for another objective. The factors may include all of the 4P's; as well as personnel, finance, manufacturing capabilities, and so on. The external factors may include macroeconomic matters, technological change, legislation, and socio-cultural changes, as well as changes in the marketplace or competitive position. The results are often presented in the form of a matrix.
It is prudent not to eliminate too quickly any candidate SWOT entry. The importance of individual SWOTs will be revealed by the value of the strategies it generates. A SWOT item that produces valuable strategies is important. A SWOT item that generates no strategies is not important.

**Avoiding Errors:**

Opportunities external to the company are often confused with strengths internal to the company. They should be kept separate.

SWOTs are sometimes confused with possible strategies. SWOTs are descriptions of conditions, while possible strategies define actions. This error is made especially with reference to opportunity analysis. To avoid this error, it may be useful to think of opportunities as "auspicious conditions".

**Examples of SWOTs factor:**

**Strengths and weaknesses**

- Resources: financial, intellectual, location
- Cost advantages from proprietary know-how and/or location
- Creativity (ability to develop new products)
- Valuable intangible assets: intellectual capital
- Competitive capabilities
- Effective recruitment of talented individuals
- Competitive Advantage

**Opportunities and threats**

- Expansion or down-sizing of competitors
- Market trends
- Economic conditions
- Expectations of stakeholders
- Technology
• Public expectations
• Changes in markets
• Global Influences

Use of SWOT Analysis:

The usefulness of SWOT analysis is not limited to profit-seeking organizations. SWOT analysis may be used in any decision-making situation when a desired end-state (objective) has been defined.

3.3 Sourcing Strategy Basics

Some companies have separated in the last decade their Purchasing areas approaches. In some transnational companies the payments and general follow up, Purchasing orders creation and explanations are responsibility or Procurement staff. Negotiations, Vendors selection, savings projects, contracts and commercial agreements and purchasing strategies creation are responsibility of Sourcing strategic team.

In this project we have been reviewing what a business strategy is. Due the objective of this project is to create a Purchasing strategy, below you can find more reference of how this information can be useful and transformed for market trends and purchases point of view, providing more perspective and a Sourcing strategy can be created.

According with Jack Ryan, 2008, The purpose of a strategy is to provide direction, or a blueprint, to deliver competitive advantage. It requires a clear understanding of what we want to accomplish via the strategy (e.g. the business needs) and our own and the opponent(s) weaknesses and strengths. While it needs to include specific tactics to be implemented, it is broader than a tactic because it provides the structure and foundation of why that tactic should work. If the tactic is not successful, it provides a framework for analysis of the root cause, and potential alternative tactics. We may learn that our basic understanding and therefore strategy was flawed, but we would obviously hope that would be far less frequent than an update of tactics. That is why a strategy should last for several years if the fundamentals of the game (in our case, market) remain unchanged.

There are several implications that need to be considered to for to create a sourcing strategy:
Don’t underestimate the importance of determining the business needs, which is how your customer defines winning. This process is part of the Linking skill area, and I recommend you look at that fundamental skill concurrently, or minimally before you have to write an actual strategy. Referring to the military references above- in many cases the reason a battle strategy failed was because the combatant was not clear on what was considered “winning”.

We have limited resources and cannot do everything. While there are many business objectives that need to stay under control, they need not all be covered in your strategy. It should represent a few real choices of action that leverage our relative strength or a competitor’s weakness.

This first requires a real understanding of those strengths and weaknesses; superficial strategies are neither long standing, nor do they make the business as successful as it could have been.

Strategy choices are specific. If you are the largest customer, then “leverage scale” is not a strategic choice. Scale is a strength, and you need to decide how best to leverage it. That may be via approaching the market globally when everyone else is regional, or it may allow you to consolidate volume with a few suppliers that give them greater scale, and therefore lower cost than anyone else in the market, that they can pass on to us. But you need to have thought through how you will use a strength that will be difficult for others to immediately implement.

The most important and interesting strategies are always where we do not have an advantage today. The point of doing this work is not to continue to play to a stalemate, or worse yet, lose. If the rules of the game are not working in our favor, you need to think through how to change the game. You are part of the largest consumer products company in the world: there is a way.

Strategy is about making choices. This Current Best Approach (CBA) provides a fairly detailed review of potential questions to ask oneself. The intent is to sequentially consider each Element using only those parts of each Element that are relevant to the situation or item being purchased. Choose the aspects of each Essential Element that apply to the item being sourced.
The keys to a successful strategy are analytical thought, creativity, and action, not answering every question. Use the map on page 2 as the guide through the process and the rest of the document for reference/explanation/coaching.

**When Used:** Any external sourcing strategy for Global, Regional, or Local purchase of materials, services, or equipment. If the item is important enough to warrant a strategy, this thinking framework should be used to develop that strategy. To note, the CSA guidelines require that 70% of the spend of any audited group be covered by a Sourcing Strategy. This CBA is also relevant for assessing external options in make vs. buy decisions.

**Who Uses:** People who purchase items (goods and services) for the company; individuals or teams/netsworks buying the item for which a strategy is needed; or cross-functional sourcing teams which need to collaborate in developing external supply strategies.

**Who is the Customer:** There are typically four customers—Purchases Management in the Spend Pool organization involved; Business Unit Management when the item is of critical importance to a Business Unit; the Purchases organization to onboard new people; and other functional people who will interact with the supply base. The strategy provides the rationale for strategic direction and tactical executions.

**Benefit:** A standard thought process that lays out the steps in developing a strong Purchasing strategy looking out three or more years. The thought process leads to a clear assessment of the situation enabling the design of an effective “game changing” strategy. The CBA also provides guidance on documentation of the resulting strategy.

**Prerequisite:** The ability to use several other Purchases skills is important in using this CBA to develop sourcing strategies. The skills of Linking company needs to supplier industry capability, Leveraging, Industry Analysis, Supplier Analysis, Economic Analysis (Benchmarking, Forecasting, Cost Modeling), and Competitive Analysis are all used in constructing a strategy. The skills of Competitive Bidding, Negotiation (both internally and with suppliers), Supplier Relationship Management, and Commercial Agreements are often used in executing a strategy.
A “Strategic Sourcing Skill and Analysis” has eight essential elements to be considered according with Jack Ryan P&G, 2008, and at the end can be used in a purchase strategy. The elements description is as follows:

**PURCHASING SOURCING STRATEGY SKILL**

**EIGHT ESSENTIAL ELEMENTS CBA**

The Purchasing Sourcing Strategy Development CBA (Current Best Approach) provides an analytical thought process and framework for Purchasing strategy formulation and execution. The eight Essential Elements provide a logical approach for putting together a supply strategy. The Essential Elements outline the key aspects that need to be considered in developing Purchasing Sourcing Strategies.

**OBJECTIVE:** Plan and leverage our presence in material, service, capital/current expense, etc. markets to deliver against our business needs and develop competitive advantage now and in the future.

**PRINCIPLES**

1. **Strategies are long-term, with periodic renewal.**

   Purchasing Sourcing Strategies are strategic plans that focus on long-range efforts (three-plus years out) and contain enough flexibility to work regardless of foreseeable market fluctuations and routine levels of change expected over such a time frame. Strategies are renewed periodically (every 24 months or when major changes occur in either business strategies or commodity/service/equipment markets or when the results are not being delivered as anticipated). They are to be documented in writing.

   Purchasing strategies also apply to major one-time purchases. In this case, the strategy addresses supplier selection and the approach to be taken with that supplier.
2. **Purchasing strategies are done for all major externally-sourced items.**

Purchasing Sourcing Strategies are prepared for externally-sourced items that are needed in the business. This business need can be measured in many ways, including cost/spend, quality, sales volume, profitability, innovation, localization, supplier diversity, speed-to-market, responsiveness, risk management, supply availability, product performance, and service reliability to both internal and external customers. It is important to recognize that the decision not to have a Purchasing strategy is a strategic choice, and that CSA’s require that 70% of the spending in any audited unit must be covered via a sourcing strategy.

Purchasing strategy is also a key element in outsourcing (make vs. buy) decision making. The external supply option needs to be assessed from a long-term perspective vis-à-vis internal manufacture or service performance with regard to reliability, quality, capital/resource intensiveness, cost, speed, responsiveness, technology life, supplier diversity, etc.

3. **Strategy scope reflects the level of leveraging that adds value.**

External Sourcing Strategies will be formulated at the highest level of leveraging scope that adds meaningful value. Strategy scope within the company can be Global, cross-Business Unit, Regional, Local, and within Business Unit, depending on the impact of scale on the results that are attainable for the item being sourced. Strategies make choices that are right for the Company, within the scope of the strategy. At the same time, it is important that strategies seek to meet the needs of all participating Business Units over time. If one Unit consistently “loses,” the strategy is insufficient and will need to be modified. Leveraging can also reach outside BMG by aggregating volume with suppliers or customers, forming consortiums with buyers from other industries, or outsourcing our purchases to companies that buy for a range of customers. The key is proactively managing these relationships instead of just letting the other parties do the work without clear accountability.
4. **Strategies are both data and judgment based. Agreements must be honored.**

Strategies will be built from a combination of data analysis—internal and external—plus informed judgment based on market and internal knowledge. If concerns or disagreements arise over a proposed strategy, they will be openly resolved using data whenever it is available. It is not acceptable to agree to a strategy and then execute differently.

5. **Strategy rigor is determined by the complexity and size of the purchased item.**

Strategies will be constructed with the level of detail (rigor) appropriate to the complexity and relative importance of the item being sourced. This allows the length and detail of the written strategy to be tailored to the business situation involved.

6. **Strategies must be executed to deliver results.**

The reason strategies are developed is to deliver results from the supplier relationships and commercial agreements that flow out of the strategies. Therefore, strategies must be executed if they are to deliver results. This execution takes the form of tactical actions with suppliers and internal BMG organizations. The results of these actions must be measured to ensure they are as intended. Alignment across organizations (Geographies, Functions, Disciplines, Businesses) is critical to success and should be secured early in the strategy development process.

**Purchasing Strategy Skill Essential Elements**

There are eight Essential Elements that make up the CBA for developing Purchasing Sourcing Strategies. They are:

A. **Data Analysis Phase**

   1. Assessment of Business Needs and Capabilities
   2. Assessment of the Supplier Industry/End-User Market
3. Macroeconomic and Cost Analysis

B. **Strategy Development Phase**

4. Desired Results

5. Sourcing Choice Model/SWOT Analysis

6. Statement of Strategy

7. Tactical Planning and Execution

C. **Approval and Renewal Phase**

8. Documentation and Renewal

A. **Data Analysis Phase:** This phase focuses on gathering and analyzing data from the company, the industry, suppliers that make the item (goods and services), and the broad macroeconomic situation. It provides the baseline data from which strategy and tactics will be developed. It is a comprehensive environment scan, both internal and external.

1. **Essential Element 1**

**Assessment of Business Needs and Capabilities**

This element is critical to a successful strategy because it uses the linking skill to translate business needs into actionable requirements of the supply base to meet those needs. It also uses linking to understand the Business Unit’s capability to impact the supply base. The internal alignment process begins with this Element. Involve other Business Unit functions in this assessment so that their input and knowledge is well understood and integrated into the strategy process.

**Business Need Linking**

Inventory? Local currency content? What is the Go-to-Market Strategy? Speed-to-market? What are the Business Unit’s goals? How does what you buy impact those goals? Are there important Corporate objectives? Supplier Diversity? Sustainability?

**Supply Chain Design.** Responsiveness/localization requirements? Flexibility requirements (late-stage differentiation)? Cost requirements? Capacity requirements? Role of 3rd parties?

**Technical Strategy.** What is the technology strategy for the material, service, or equipment? Where in its life cycle are we? Does this item’s life cycle impact other purchased items (substitutes, replacements, etc.)? What is the innovation rate for this item?

**Volume Projections.** What are the year-by-year volume forecasts out three or more years? Does demand vary significantly within a year? How does that impact the supply capacity and cost? What are the underlying business assumptions that drive the volume projections? Are they risk adjusted? How will we supply the upcoming Sales and Operation Plan (S&OP) volumes while preparing for any changes projected in future years? How do Business Unit CDSN or Responsiveness objectives affect supply planning?

**Innovation Considerations.** Is this a developmental material/equipment or a new service requirement? What initiative/project is it tied to? Are there intellectual property considerations—what is the intellectual property strategy—patent rights, licensing, JDA/CDA? What is the development timeline? Speed-to-market? Will the item’s development impact the volume of currently used items? Are there information security considerations in this situation?

**Quality/Reliability/Information Considerations.** What are our quality requirements? How is the item used? How does it impact product or BMG work process performance? What level of reliability and customer service is necessary for those who use the item? What level of administrative, information, and communications interface is needed? What are the logistics requirements?

**Cost/Cash Flow Considerations.** What is the forecasted cost? Target cost? Inventory/cash flow needs? Is this a major spend item? **Current Cost Benchmark**—what do we pay for this item across BMG? Why are there differences?
Potential Acquisitions, Divestitures by BMG, or Outsourcing. How will usage be impacted? Will existing agreements remain valid? For how long? Are there supplier relationship implications, cost implications?

Multiple Business Units. Is the item used in more than one Business Unit? Are the specifications common? If not, could they be? Are there commonalities between the Business Unit needs? Differences? How do their volume projections add up? How should the Business Units organize to collaborate (single BU buys for all, a team, etc.)?

Effective Business Continuity Planning that enables us to have contingency plans in place to cover our needs in the event that a supply disruption or serious emergency strikes the business.

Business Capabilities Linking

Importance of the item to the Business Unit. This point looks at the strategic importance of the item to help assess whether significant resources ought to be spent to support sourcing the material. It looks at two dimensions, economic size ($ volume) and risk/complexity potential. The importance of the item or service in a company is shown in Figure 4.

![Figure 4 “Service Economic Size”](image)

Large Volume, High Risk/Complexity requires high commercial, technical, and operational resource allocation. Large Volume, Low Risk/Complexity requires high commercial resource allocation and will need to justify technical or operational resources, typically based on economic (savings) potential. Small Volume, High Risk/Complexity requires high commercial, technical, and operational resources to manage/eliminate the risk and complexity. Small Volume, Low Risk/Complexity requires reduction/elimination of resource allocation.
Functional Capabilities across the Business Unit

**Resources.** Can adequate, knowledgeable Company resources be dedicated to working on the sourcing strategy execution for this purchased item?

**Cross-Functional Alignment.** Is there strong cross-functional interaction that can form the basis for alignment to action?

**Commercial/Purchasing.** What resources can Purchases dedicate to the sourcing work? Do we have experience? Are we knowledgeable about the market?

**Technical.** Do we understand how the item works and is made? How will we apply it to our products or services? Do we have technical resources available for qualifications, quality improvement, specification simplification/standardization, integration of the supplier with BMG systems, etc.?

**Financial.** Are we prepared to invest financial resources (people, money) to improve results from the sourcing of this item?

**Logistics.** Is our Material Supply Management system strong? Flexible? Reliable? For non-material items, are the internal customers of the service or equipment capable of integrating with the service supplier or operating the equipment involved?

**Information Technology.** Is there IT support for supply base communication and collaboration? Are connections made via the Supplier Portal or ERP-to-ERP connectivity and are hardware, software and bandwidth infrastructures in place and common across the Business Unit?

**Cross-Business Unit Alignment.** If this is a cross-BU sourced item, are the above-mentioned functional capabilities available in each relevant BU? There may be differences across the Business Units with regard to the level of capability. How do we reconcile these differences?

**Transactional.** Do we have clear links across the purchase to payment cycle (P2P) including order originators, purchasing, receiving, accounts payable, Treasury/banks and suppliers.
Operational Capability to deal with the supply base:

**Commercial/Purchasing.** Are we a major buyer of the item? A desired customer? Do we have productive relationships with any suppliers of the item? Are we capable of collaborating with other companies or across our Business Units to create consortiums?

**Financial.** What are the economic goals/constraints which must be met (NPV, ROR, financial risk, cost, etc.)? Is investment a barrier to change?

**Technical.** Do we technically understand how the item works and is made? Are there regulatory or safety risks? Do we have a strong intellectual property position?

**Logistics/Operations.** How complex/long is the logistics pipeline? How intricate is the service integration with BMG systems/people? How does this material affect the responsiveness goals of the Business Units? Is the supply local, regional or global?

**e-Connectivity.** Can our information systems easily link with suppliers? Are they transparent to adding a new supplier or a barrier to change? Are we Web capable? Are the suppliers? Are our internal organizations aligned on a preferred method of communications (e.g., Internet) or are there functionally specific preferences (Internet, EDI, phones and faxes)? Should we mandate the way we want suppliers to connect with BMG (internet/e-mail vs. phone and fax) and if you do decide what type of connectivity you want, recognize e-mail/websites are not a replacement for human interaction.

**Alignment.** Are the various Functions or Business Units communicating the same message?

**Complexity.** Is the Company use of this item complex, requiring precise integration? Is the make-up of the item complex? Is the project that uses it complex? Can this complexity be reduced? How does the complexity impact the level of expertise needed by the company and the supplier?

**Responsiveness.** What is our target leadtime? What is our target Material Supply Time? Speed-to-market goal? Customer responsiveness goals? Initiative timing? How much time do we have to take action with the supplier?
2. **Essential Element 2**

**Assessment of Supplier Industry/End-User Market**

This element is critical to a successful strategy because it assesses the market forces and relationships that translate into the industry’s capability to supply what is necessary to meet our business need. It assesses the industry, its projected supply/demand balance, the suppliers in the industry, their relationships to BMG, to each other, and to our competition’s position in this market.

**Industry Analysis using the Porter Model**

The real purpose of this analysis is to come to some conclusions about the industry and how it can be influenced by our strategy.

Assessment of Porter’s five forces, including an outlook assessment of these forces in the future. It is vital that the analysis penetrates to understand what the underlying drivers of the Porter forces are.

1. Threat of new entrants.

2. Bargaining power of the supplier’s feedstock and product input suppliers (includes materials, labor, copyrights, third-party patents, R&D costs, etc.). This is key to understanding the complete supply chain for the item being purchased. Should BMG source the feed stocks?

   Should the company and/or our supplier join consortia, should we combine our volume with theirs?

3. Rivalry of existing companies competing with each other in the industry. Is there open competition, cartels, collaboration between competitors?

4. Threat of substitute products or services.

Bargaining power of the suppliers’ customers including, and beyond, BMG. This includes knowledge about the other buyers—are they forming consortia that have more scale than the company and more power vis-à-vis the industry? Do other industries have more leverage than
our industry with this supply base? Do other customers really drive events in the market/industry?

What are the impacts of e-business on the industry? Are there viable e-exchanges in this industry? Should they be considered as a "sixth Porter model force" if they do have significant influence? Do certain suppliers have private exchanges or web portals that draw their customers? Is that part of their "power level"?

What is the impact of supplier localization and diversity on the industry? Analysis of what these forces mean to our sourcing strategy. This is the key output of the Porter Analysis. It requires us to understand the underlying drivers of each force and how they influence industry and individual supplier behavior. Can we influence the forces to change them, or must we react to them?

**Industry Supply/Demand Analysis**

What is the demand forecasted for this industry? What key customer groups make up this demand? Why is their demand forecasted to move the way it is?


Is the item expected to be in loose, balanced, or tight supply? How will that impact our sourcing approach?

Are the feed stocks/cost inputs to this item driven by market supply/demand? If so, are they expected to impact material supply? How many tiers back in the supply chain?

Are there viable local/diversity suppliers in the industry? If so, what needs to be true for BMG to leverage their capabilities?

**Supplier Analysis**

Cross-functional alignment needs to be built and reinforced in this step. It is important to involve the appropriate organizations in conducting this analysis—especially internal customers of the supply base.
What is our current relationship (if any) with each supplier we are considering?

Strategic (both parties are engaged in creating joint value),

Essential (relationship is based on longer-term collaboration),

Competitive (relationship is used primarily to deliver short-term results), or

Emerging (relationship is new and/or developing

Is the relationship healthy and meeting expectations? Do the various Business Unit functions view the supplier relationship in the same way or are there differences? How do we reach internal alignment on these perspectives?

What are the strengths and weaknesses of each supplier’s key business units and overall?

Management and strategy.- What are the supplier’s core competencies? Who are the key decision makers? Do we know them? The corporate and business unit strategies—does the company as a customer fit into that strategy?

Financials.- Cost structure (labor, logistics costs, depreciation, etc.). Profit center design (by plant, geography, business unit, what?) Debt levels. Cash flow/profitability.

**Supplier base including vertical integration.**

Research and development capability.- Technical competencies? Scale-up ability? Innovative service development?

**Information technology.** Are they Web capable? willing to collaborate? Able to handle transactions, volume planning and logistics electronically with high reliability? Do they belong to exchanges? Have their own web portals? Can they afford electronic connectivity tools? Have ERP to ERP connections with suppliers and customers? Can they provide second tier diversity spending?

**Customer base.** Any of our competitors? Are our competitors key customers of this supplier? Do they have strategic relationships with our competition?
Is the item we want to buy in a core/strategic business for the supplier? How does it fit with the supplier’s other businesses? Is there potential for divestiture?

What is management’s view of the company? Does the company buy other items from this supplier? What relationships exist on those items?

What are the supplier’s manufacturing, distribution, service office locations, and how do they mesh with the company using locations? Does it matter? Are they well run? Will their capabilities impact our ability to meet Business Unit responsiveness goals, either positively or negatively?

Customer service reputation good? Bad? Why? Do they have a Business Continuity Plan? Is it reasonable?

**Supplier Measurement.** How is the current supply base performing?

Cost—price plus non-acquisition costs (freight, duty, storage, etc.).

Cash flow—inventory, payment terms, capital investment capability, debt rating.

Quality—statistical process control measures, complaints, cost of quality, BMG user’s input.

Logistics—MRPII reliability measures (on time, correct quantity, etc.), MSM assessment of supplier daily interaction, internal company customer assessment of supplier service and interaction.

Innovation—intellectual property, research and development track record, exclusivity terms, etc.

Market intelligence—information about the industry market, its suppliers and customers.

Speed/Time—leadtimes, response times, innovation/investment timelines, scale-up timelines.

Transactional administration—invoice accuracy, electronic interfaces, etc.

**Supplier’s Supply Chain Power Mapping.** Understand the supplier’s supply chain. Where does the power in that chain lie? Is the supplier a key player or is part of their supply chain really where the power lies? Does this power structure shift with market conditions over time? If
your direct supplier is not the “power” in the chain, should the company establish contact with the power player(s)? In concert with your supplier or independently?

**Competitive Analysis**

Often other functions can be of real help in this step.

Review use of this item by our competitors. Which products/businesses use it, approximate volumes, using locations? Specifications, quality requirements. Which suppliers, which plants, what is their relationship?

**Estimate of cost**—volume scale, logistical pipeline local or import, specification implications, feedstock implications, currency.

Purchasing approach (centralized/decentralized, Global/Local, competitive or alliance, supply chain linkages, etc.).

Developmental approach: use of material in products, patent positions, unique supplier competency use, copyrights, etc.

How do our competitors use e-commerce (aggregation, ERP integration, web portals, exchanges, etc.) for this item? Are they members of buying consortia? Are they Web-based? Do they share scheduling information across multiple supply chain tiers?

Assessment of our advantages/disadvantages vs. competition

Economics, Supply availability/quality standards, Supplier influence/leverage, Time (leadtimes, development time, expansion time), Efficiency (e-commerce, resource allocation, etc.), e-Connectivity (IT infrastructure, planning and invoicing systems, etc.), Supplier Diversity/Localization

If the competitor does not use this item, what do they substitute for it? Implications of the substitute (economics, performance, time, supply, etc).

3. **Essential Element 3**

**Macroeconomic and Cost Analysis**
This element focuses on **non-market based** factors that impact cost and supply/demand. There are two major types of factors:

(1) **macroeconomics** that drive governmental, broad trade and currency movement, and

(2) **structural costs** that determine industry and supplier break-even points. They include company costs (overheads, R&D costs, yields, productivity, etc.) and non-acquisition cost factors. These are the “constants” around which market forces move.

**Macroeconomics**: The PEST model shown in Figure 5 provides a good tool to guide your thinking about broad external factors that influence the materials/services you are sourcing:

<table>
<thead>
<tr>
<th>POLITICAL</th>
<th>ECONOMIC</th>
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<tbody>
<tr>
<td>Environmental/sustainability issues</td>
<td>Consumer economic situation/trends</td>
</tr>
<tr>
<td>Current/future legislation</td>
<td>Market and trade cycles</td>
</tr>
<tr>
<td>Government policies</td>
<td>Distribution trends</td>
</tr>
<tr>
<td>Trading polices</td>
<td>Interest/exchange rates</td>
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<tr>
<td>Petroleum prices</td>
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<thead>
<tr>
<th>SOCIAL</th>
<th>TECHNOLOGICAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Consumer buying patterns</td>
<td>Maturity of technology</td>
</tr>
<tr>
<td>Major events or influences</td>
<td>Replacement technologies</td>
</tr>
<tr>
<td>Demographics</td>
<td>Technology legislation</td>
</tr>
<tr>
<td>Law changes affecting social factors</td>
<td>Access, licensing, patent, intellectual property issues</td>
</tr>
</tbody>
</table>

*Figure 5 “PEST Model”*
Cost Structure Analysis

What drives cost in the industry? R&D, capital, feedstocks, labor, etc.? What are key cost factors of the product/service you are sourcing? Will administrative or research costs be the key driver? Production costs? Logistical movement? What are the projections for the cost of these factors over the coming months/years? What drives the Administrative (overhead) or Research cost areas (headcount, capital investment, intellectual property cost, sales and marketing, etc.)?

What drives the Production cost areas (material, capital depreciation, labor, yields, scrap, information systems, warranty costs, etc.)? What are the technologies that drive the cost to produce or deliver the item (goods or services)?

Are there significant differences in the cost structure of different suppliers in the industry?

B. The Strategy Development Phase: This phase is pivotal. It defines the commercial goals that the strategy and its tactics must deliver. These goals and the information from the Data Analysis Phase are used to develop the strategy and the tactical plan to execute the strategy. The reason for the strategy is to deliver the results necessary for the business—this phase defines all this.

4. Essential Element 4

Desired Results

This element describes the success criteria, in terms of business results, that the strategy needs to deliver. It looks at both longer term (three-plus years) strategic results, as well as nearer term (3-12 month) tactical results necessary to deliver what the business needs.

Involving business leadership and other internal stakeholders in the development of these success criteria is a key step toward getting the necessary support for the strategy and tactics that emerge from the CBA process.

Strategic Desired Results: There are three types of strategic results—quantitative, relative, and work process/system improvements. Choose only those that are relevant for the item being
sourced. Strategic results ought to be stretch targets that clearly relate to the needs and goals of the business.

**Quantitative Results** are specific numerical or physical results that are determined by three mechanisms.

They need to be communicated in a format/terminology consistent with that used in the Business Unit.

**Loss Analysis**—An analysis of the difference in total cost (not just price) between the internal BMG Global benchmark and the costs of all non-benchmark using locations. This total provides the maximum savings potential (waste elimination) for the item at the point in time that the strategy is being developed. Refer to the Best Value Sourcing models and Total Supply Chain Cost Calculator. A second approach is the use of “Should Cost Analysis” to calculate the theoretical lowest cost to produce the item in question. This becomes the benchmark against which current cost is compared to determine the “loss.”

**Innovation/Time Analysis**—An analysis of the level of innovation, time-to-market, and consumer value of the Company product that uses the item being sourced. It includes (1) innovation of the new item (material, service, equipment design, etc.) and the initiative that contains/uses the new item, (2) the timeline to develop, test, and expand the new product or service that contains the innovation, (3) the quantity necessary to support the Company’s expansion plans, and (4) the target cost of the item and/or initiative to ensure strong consumer value. A Loss Analysis technique (time mapping) can effectively be used to measure time loss and understand true lead times.

**Opportunity Analysis**—An analysis of the business-building potential of the Company initiative that depends upon the item being sourced. This is particularly applicable to marketing service purchases and purchases that support new product initiatives designed to increase Net Outside Sales via volume or pricing increases or responsiveness initiatives.
Relative Results are measures versus another position in the market. They are sometimes difficult to measure precisely. They are often based on judgment, competitive/market analysis and intelligence, and published industry indices.

Competitive Advantage—An assessment, usually an educated guess, of how the company cost/intellectual capital/performance quality compares to that of our competition. The measures are cost, proprietary/exclusivity of performance, and product or service quality relative to competition—all of which drive consumer value.

Versus Market—An assessment of how the company cost and availability compares to the general market for the item. If we are a large buyer, we should see lower cost. If we are a preferred buyer, we should see greater availability in tight markets. Our goal is to beat the market, not just ride along the market flow—costs below market, increases less than/later than the market, decreases larger than/faster than the market.

Versus Forecast—An assessment of the company results (usually cost or time) versus that forecasted by the Purchasing, Finance, or project organization.

Work Process/System Results are measures that track the development or significant improvement of systems that allow us to buy better value. Examples include material simplification, volume forecasting systems, administrative effort reduction, supplier quality assessment systems, electronic purchasing, and other “how the work is done” approaches. The goal is to be more effective and efficient. Loss analysis of people effort is an effective approach in this area.

Tactical Desired Results: These are the goals set for each near-term sourcing intervention that is part of a longer term strategy. They are nearly always quantitative in nature and need to be met or exceeded to have the tactical intervention considered successful. These objectives should be Specific (a particular cost or volume), Measurable, Attainable (yet stretching), Reliable (deliverable), and Time-bound (SMART). Over time, the sum of these quantitative measures must move us directionally toward the longer range goals of the strategy. They are decided upon as part of Essential Element 7, Tactical Planning and Execution.
5. **Essential Element 5**

**SOURCING CHOICE MODEL**

Once you have analyzed both the internal and external conditions that influence the item you are sourcing, you need to re-evaluate the strategic importance of the item which you reviewed from an internal standpoint in the Assessment of Business Needs and Capabilities. External factors provide further insight into the risks and complexities of the item. The Sourcing Choice Model shown in Figure 6 uses a 2X2 matrix to choose whether to in or outsource the procurement of this item or some blend of the two (e.g., do in-house strategy, outsource tactics/transactions).

<table>
<thead>
<tr>
<th>Risk/Complexity</th>
<th>Voluntary Bottleneck</th>
<th>Strategic Differentiator</th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>II</td>
<td>IV</td>
</tr>
<tr>
<td></td>
<td>Manage, Grow or Exit</td>
<td>Alliance, Collaborate, Leverage</td>
</tr>
<tr>
<td>Low</td>
<td>I</td>
<td>III</td>
</tr>
<tr>
<td></td>
<td>Outsource or discontinue, increase efficiency</td>
<td>Competition, Maintain multiple suppliers</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Volume /Cost</th>
<th>Risky Bottleneck</th>
<th>Strategic Differentiator</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
<td></td>
<td></td>
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<tr>
<td>High</td>
<td></td>
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</tbody>
</table>

**Figure 6  "Sourcing Choice Model"**

**I - Non-Critical:** low volume, risk and complexity

The questions to ask here are: How can we dramatically reduce the time and effort we spend here, yet ensure we get what we want at the best price to deliver low total cost and low cash flow?
Outsource to a third party purchaser (e.g. contract buyers, distributors) to aggregate our small volume with other buyers with monitored success criteria.

**II - Risky Bottleneck:** low volume, high risk and complexity

This is the **worst** place to be. Volume is not enough to deliver alliance level economic returns for a supplier and the resources necessary to manage the risk simply increases the cost. The key questions here are: Can we reduce the risk? Can we simplify the item or its use? Can we grow its volume? Can we exit the use of this item?

It is extremely risky to outsource these items without positive responses to the questions above. It is key to develop an effective management system to monitor these items, which can be very strategic when they fail, yet are not important when they work.

**III - Financially Competitive:** high volume, low risk, complexity

These items are strategic because of their economic importance and size. To win, we must use our market knowledge to acquire these items below market by leveraging their size and simplicity. E-commerce makes this even more imperative because of the aggregation and consortium possibilities it opens to us and our competitors.

Use competition and put the infrastructure necessary to leverage competition in place—simple specs, rapid qualification procedures, rapid decision making.

Aggregation/consortium with others to leverage larger volumes (Decide if the company volume will transfer your advantage to the other players thus reducing our scale advantage).

Incremental volume discount seeking.

**IV - Strategic Differentiator:** high volume, high risk/complexity.

These items add the unique difference that drives the business. They can be proprietary performance drivers, major risk sources, or unique features that draw customers/consumers. These items must be both leveraged and managed to deliver value (benefit/cost).
Model dynamics: This model is dynamic, not static. Items can shift quadrants due to BMG actions, supplier actions, or external market forces (competitors, macroeconomics). It is extremely risky to just assume an item will always stay in its quadrant. Sometimes our strategy involves moving the item from one quadrant to another (e.g., Strategic Differentiator to Financially Competitive, or Risky Bottleneck to Non-Critical, etc.).

6. **Essential Element 6**

**Statement of Strategy**

This element uses the results of the SWOT Analysis and the Desired Results element to determine a strategy platform that addresses the key factors regarding the item being sourced by creating a limited number of strategy planks that look out three-plus years and are designed to deliver the necessary business results. Strategy is the set of choices (planks) that define BMG’s strategic purchasing approach to the item in question. It is not the selection of a particular tool. (E.g., the strategy of leveraging multiple suppliers’ excess capacity might be executed by the selection of the inquiry tool as a tactical choice in the next element of the CBA.)

It is critical to forge the cross-functional agreement and commitment to the strategy in this element. This can take the form of involving other organizations in the development of the strategy planks, up-front review of the SWOT Analysis for input prior to the strategy development, or prompt review of the strategy for input/agreement after this element. Since cross-functional involvement began in the Data Analysis phase, this should build on that.

**Time frame.** Strategy planks need to have a forward time horizon of three-plus years. The planks need to be broad enough to deal with normal business fluctuation and contingency planning, yet focused enough to set a long-term direction. This is a balance.

**Choices.** The number of strategy planks should be limited to allow focus. If too many planks are developed, it increases the dilution of effort and the risk of not executing the full strategy. The SWOT Analysis may expose many potential strategy plank options. The Strategy Development element requires prioritization of those most critical to the delivery of ongoing
business results. Developing strategy requires choices about what not to do, as well as what to do. More than three or four planks can be very difficult to execute.

Potential Areas of Intervention. Typically, strategic planks fall into six general types of interventions. All six are rarely found in a single strategy.

(1) Market Intervention. Defines choices made in the market for the item to be sourced. Examples include single vs. multiple suppliers, competitive vs. collaborative approaches toward suppliers, make vs. buy, localization, supplier diversity, purchase of feedstocks, encouragement of additional capacity, Global vs. Regional vs. Local sourcing or a mix of the three. E-procurement offers the opportunity to use the Web to find new suppliers, provide scheduling transparency, exchange information, collaborate, manage competitive bidding (auctions and inquiries, etc.)

(2) Technical Intervention. Defines technical choices with commercial implications for the delivery of business results. Examples include material simplification vs. development of new specifications, intellectual property approaches, qualification of substitute materials/services, product formulas and processes that provide flexibility, information technology/Internet technology options, invention and commercialization of new items, etc.

(3) Cost Structure Intervention. Defines efforts to impact the underlying cost structure of the item. Examples include waste elimination efforts, tariff reduction lobbying efforts, yield improvement, labor reduction/automation, overhead cost reduction, etc. (Sometimes cost structure interventions also require technical interventions.) Should-Cost and Target-Cost analysis can be valuable tools in this intervention as can the use of e-connectivity to reduce supplier transaction costs.

Supplier Relationship Intervention. Defines efforts to leverage or build upon an existing relationship with a supplier. If the relationship is cooperative or collaborative, perhaps we can extend this cooperation to new areas or a new aspect of the business. Similarly, if the relationship is adversarial or competitive, can you manage or direct that energy a different way so that a good business result occurs? Are there individuals in that company who can help (or hurt) our ability to use this intervention?
Sometimes we have the desire to change a relationship significantly—i.e. take a Competitively Based Incumbent relationship to a Strategic Business Alliance or Preferred Supplier relationship. This kind of change is very difficult to execute—it takes time (sometimes even years), resource/time investment and internal alignment across functions to successfully accomplish. It also requires mutuality—that is, both sides want to make the change. If both sides do not want to change it will probably not happen regardless of how much the other one wants it. Supplier relationship is almost always a given—part of the Analysis Phase of this CBA—and always a tactic because doing business with a supplier requires managing the relationship. To be strategic, this intervention requires influencing the supplier to significantly shift its resources/approach from the status quo.

In some cases, there is no existing supplier relationship (new item or supplier). While the choice of a desired supplier relationship via the sourcing strategy is important, without any history with the supplier, the relationship will need to be built not just assumed. This choice dictates how we initially resource and approach the relationship, but ultimately the relationship will be determined by our experience with the new supplier. A desired relationship should not be assumed to be true, especially with new suppliers.

**Company Internal Work Process Intervention.** Defines efforts that change how BMG does the work relating to the item being sourced. These are changes we must make to our internal systems. Examples may be volume forecast system changes, SAP compatibility work, qualification system changes, pooling of like items into a family to be purchased together, outsourcing the work, etc. Success is normally a binary measure—yes/no—and a productivity or speed measure. Use of IT tools, Intra/Internet capabilities, mining our own SAP data, and Web-delivered outside knowledge are all ways to change our internal work processes.

**STRATEGIC INTERVENTION/SOURCING CHOICES IMPACT MODEL**

In Essential Element Number 5, you categorized the material or service you are sourcing into one of four quadrants. The following **Figure 7**, adapted from the *Gillette Gemstone Model*, provides some guidance on the relative impact of any of these strategic interventions normally have on a particular Sourcing Quadrant.
**Strategic Intervention Option**

<table>
<thead>
<tr>
<th>Strategic Intervention Option</th>
<th>Sourcing Choices Model Quadrant</th>
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<tbody>
<tr>
<td></td>
<td>Non-Critical</td>
</tr>
<tr>
<td>Market Intervention</td>
<td>HIGH</td>
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<tr>
<td>Technical Intervention</td>
<td>LOW</td>
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<tr>
<td>Cost Structure Intervention</td>
<td>MEDIUM</td>
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<tr>
<td>Supplier Relationship Intervention</td>
<td>MEDIUM</td>
</tr>
<tr>
<td>Internal Work Process Intervention</td>
<td>MEDIUM</td>
</tr>
</tbody>
</table>

**Figure 7 “Strategic Intervention Option”**

**Cost/Benefit Assessment.** Once interventions have tentatively been chosen, consider the resources necessary to execute the strategy planks.

Resources include organizational items (people, time, travel budget, opportunity costs of not doing other work). It also includes tangible resources like up-front cash/capital outlays, short-term premium costs, higher inventories, and ongoing cost premiums.

Risk assessment is also relevant. What is the degree of difficulty of the intervention? Do the odds of success, size of the gain, and resource investment warrant the choice?
Payback. How important is the gain? Will it outweigh the investment? Financial analysis (risk, NPV, etc.) is an excellent measure.

Having completed this cost/benefit risk assessment, make a final choice of the strategy interventions.

Documentation of the Strategy. Write a statement of the strategy that includes each of the planks that make it up, and the rationale for each plank. (See Essential Element 8 for guidance on the finished documentation)

Alignment. Once documented, the strategy, with its rationale and any necessary supporting data (e.g., the SWOT or Porter Analysis, Loss Analysis benchmark data, etc.) needs to be reviewed for alignment with the internal decision makers (Purchases management, critical stakeholders).

7. **Essential Element 7**

**Tactical Planning and Execution**

This element takes the strategies developed in the previous element and lays out the near-term (3-12 month) tactical choices and the detailed operational action plans necessary to deliver the strategy results. This element also includes the actual execution of these plans, which often represents the bulk of the work time necessary to deliver the desired results.

Cross-functional agreement, support, and resourcing of this work is often critical to successful execution. The alignment of other involved functions and stakeholders to the tactical plan needs to be agreed to BEFORE you begin execution. If you are not sure you have this alignment, it is highly important that you delay implementation with suppliers until you have the support necessary to have a right to succeed. The speed and transparency of the sourcing tool drives the urgency and level of upfront cross-functional alignment and prompt action; e.g., e-auctions allow all suppliers to see how much the company gives up if we do not quickly qualify a new low-bid supplier, a traditional inquiry is less transparent, so losing suppliers do not know how much we leave behind by not picking the low bidder.
Key Tactical Steps

Set Quantitative Goals (as described in Desired Results). These will be the near-term success criteria. Consider the long-term results trend you are seeking, as well as the near-term market conditions, Company business needs (cost forecasts, profit forecasts, new product initiatives, etc.).

Tool Selection: Based on the strategy, select the appropriate tools/approaches to deliver results. These are the key tactics (e.g., inquiry, negotiation, auction, particular commercial or intellectual property agreement, supply chain waste elimination, etc.). A rationale why these tactics were chosen is often valuable.

Supplier Relationship Management: Based on the strategy, ensure the appropriate supplier relationship is in place or actively being worked to support the strategy. Supplier relationship management is critical to successful execution of both tactics and strategy.

Integration of Tool Use with Supplier Relationships: Assess how each potential supplier will react to the tools selected. Tailor the approach so it is effective with each supplier based on the type and health of the current relationship and the desired future relationship. If the relationship and tool are not consistent, reconsider the tool selection or re-evaluate the strategy to include a Supplier Relationship intervention. Example: use of auction on a Strategic Alliance partner’s business should cause you to stop and question either the tool or the relationship because auctions often require the use of significant competition and can cause more emotion than traditional tools due to its transparency and time pressure.

Supplier Operational Capability Assessment. For each new potential supplier location:

Current/incumbent supplier locations should have already been assessed as part of the supplier analysis and measurement parts of Element 2 (Assessment of Supplier Industry/End User Market).

Is the local supplier management team strong? Customer-focused? Improvement capable? Is the organization strong? Non-union/union, depth, capability, etc.

What level of investment is this facility willing to put into improvements that impact our business? Are they collaborative with customers? With BMG in particular?

What level of support does this facility receive from central technology and support service groups? Do we pay for what we use, or is it an overhead burden?

**Timing of the Intervention.** Decide when to intervene, taking items like contract expiration, market conditions, urgency of business need, and supplier relationship trend into consideration.

**Determine the type of Commercial Agreement** and necessary terms and conditions BMG must have for the supply of this item.

**Operational Action Plan**

Sequence the specific actions that must take place to execute the tactical choices: What steps and events must take place? When and where should they take place? Who must do them (Responsibility Chart)? This includes confirming the agreement to resource the work by all Functions involved. How will the steps be completed (approach)?

Take the Actions and award the business to the selected supplier(s). The allocation of business should ALWAYS be documented in writing via a recommendation for the approval of the appropriate Purchases Management.

**Transaction Mapping.** Once the business is awarded and the commercial terms of the deal concluded, it is vital that these terms be translated into an order which can effectively be administered in SAP. This is called “Transaction Mapping”. Without effective transaction mapping the Purchase to Payment (P2P) cycle can be seriously disrupted, resulting in delayed or erroneous payments to suppliers. Part of the Operational Action Plan must be to complete the transfer of money for the service or material rendered by the supplier.

**Documentation and Renewal Phase:** This phase describes (1) the minimum documentation necessary for a strategy, and (2) the requirements for both strategy and tactic
renewal. Markets and cost structures in commerce are dynamic—they will change. Therefore, renewal of our strategies and tactics is extremely important and **must** be done.

8. **Essential Element 8**

**Documentation and Renewal**

**Documentation:** All strategies should be documented in writing and approved by the appropriate Business Unit Management (typically Purchases Management but sometimes General Management or other key Internal Functional Management, depending upon the level of cross-functional action that must be taken).

**4.- SOLUTION AND PROJECT DESCRIPTION THAT WILL BE DELIVERED TO THE COMPANY.**

**DESCRIPTION:**

The Project that was delivered to the company at the end of March 2008, was a structured document not bigger than 25 pages (required by the company), which contains a Regional Purchasing Strategy of Life Insurance and Health Plan, confirming with is the market trend after a market and industry analysis of Latin America, current suppliers and brokers in the region, current suppliers and Purchasing resources geographic coverage, current costs and trends, external and internal environment including Strengths, Weaknesses, Opportunities, Threats, in which part of the Sourcing Choice Model are located these services, according with the complexity and volume for the company, confirming leveraging opportunities, which strategy should be followed, tactics, risks and implementation plan.

The Project documents delivered to the company contains the following topics:

I. Objective

II. Theoretical Reference.

III. General Overview. Current situation of Life Insurance and Health Plan negotiations, annual spend, current insurance companies and brokers, service specifications
   - A. Internal Environment Scan.
   - B. Suppliers & Annual Spend.
   - C. Insurance Specifications.
IV. Market / Industry Overview.
- External Environment Scan.
- Medical Costs Trend.
- Suppliers (Brokers) Rank.
- Porter Model.
- SWOT.
- Sourcing Choice Model.

V. Business Needs.

VI. Desired Results.

VII. Statement of the strategy.

VIII Strategy Planks.

IX. Risks.

X. References.

**COMPANY SOLUTION:**

I. OBJECTIVE:

The objective of this Sourcing Strategy is to evaluate Tools, methodologies, market trends, innovative concepts, internal commercial situation of "BMG company" in Latin America including data, agreements and purchasing perspective of Life Insurance and Health Plans across the region, that through theoretical and practical approaches allow to create and implement a Purchasing strategy knowing the market behavior, internal and external strengths, weaknesses, and opportunities, obtaining better coverage, benefits, hard savings, staff capability, consolidating suppliers relationship and performance, and reinforce the control in the Purchasing Team, delivering sustainable results.

II. THEORETICAL REFERENCE.

What is an strategy? Which are the benefits and when do we need to use it? In the case of BMG Purchasing, Which tools should be used and what kind of results can be obtained?
A strategy is an alternative chosen to make happen a desired future, such as achievement of goals, solution to problems and through a careful selection and application of resources to obtain a competitive advantage in productivity in business.

Scott-Morton, (1991), views an organization shaped by five main forces: Strategies, Structure, Processes, People and Technology, which has a lot of sense due the companies need these 5 factors to be competitive. In this Project Strategy we will review how these key factors should be considered in order to match in one Purchasing Strategy.

Since 1970 until now, several tools and methodologies have been created and developed in universities and companies in order to join and understand concepts, environmental and economical factors that can be matched providing different visions, creating an strategy to solve specific problems or goals.

For this Sourcing Strategy, strategic tools will be used, such as: Porter Model created by Michael Porter, 1979, SWOT Analysis, technique that is credited to Albert Humphrey,1960 and Sourcing Choice Model developed by different Consulting firms and customized different transnational companies.

The concept of health insurance was proposed in 1694 by Hugh the Elder Chamberlen from the Peter Chamberlen family. In the late 19th century, "accident insurance" began to be available, which operated much like modern disability insurance. This payment model continued until the start of the 20th century in some jurisdictions (like California), where all laws regulating health insurance actually referred to disability insurance.

Accident insurance was first offered in the United States by the Franklin Health Assurance Company of Massachusetts. This firm, founded in 1850, offered insurance against injuries arising from railroad and steamboat accidents. Sixty organizations were offering accident insurance in the US by 1866, but the industry consolidated rapidly soon thereafter. While there were earlier experiments, the origins of sickness coverage in the US effectively date from 1890. The first employer-sponsored group disability policy was issued in 1911.

Before the development of medical expense insurance, patients were expected to pay all other health care costs out of their own pockets, under what is known as the fee-for-service business model. During the middle to late 20th century, traditional disability insurance evolved into modern health insurance programs. Today, most comprehensive private health insurance
programs cover the cost of routine, preventive, and emergency health care procedures, and also most prescription drugs, but this was not always the case.

**Hospital and medical expense policies** were introduced during the first half of the 20th century. During the 1920s, individual hospitals began offering services to individuals on a pre-paid basis, eventually leading to the development of Blue Cross organizations. The predecessors of today's Health Maintenance Organizations (HMOs) originated beginning in 1929, through the 1930s and on during World War II.

**BACKGROUND.**

**III. GENERAL OVERVIEW.**

This Sourcing Strategy covers Latin America “Life Insurance and Health Plan services”, which are part of SR&A Employee Services spend pool and are used in all BMG sites across the different Business Units regionally. The strategy will be valid for the next 2 years if no major changes occur internally or in the market.

Usually these insurances services are required and managed in MDO locations (General Offices of each country), although in some cases, HR of each plan select the insurance coverage and confirm the business needs. The BMG locations that require Life Insurance and Health Plan are: Mexico, Costa Rica, Guatemala, Brazil, Argentina, Chile, Peru, Panama, Colombia and Venezuela.

To get a better understanding of these sub-spend pools, a brief definition and description

- **Life Insurance Definition:** Insurance to be paid to a beneficiary when the insured dies.
- **Health Plan Definition:** Health insurance provides coverage for medicine, visits to the doctor or emergency room, hospital stays and other medical expenses. Policies differ in what they cover, the size of the deductible and/or co-payment, limits of coverage and the options for treatment available to the policy holder.
A. INTERNAL ENVIRONMENT SCAN.
Every year Life Insurance and Health Plan services must be renewed in all the LA Countries (Mexico, Costa Rica, Guatemala, Peru, Colombia, Venezuela, Chile, Argentina and Brazil. Since April 08 Panama will be part of “BMG” sites that requires these services).

**Life Insurance and Health Plans** services are managed by Brokers hired by BMG in each country of the region. Their responsibilities are to evaluate the insurances markets and insurance companies in order to recommend the best alternatives to BMG, searching the best value, coverage, benefits and handling the day to day policies administration work.

Having ten LA Countries that required these services, we have 12 different brokers, handling 20 services (10 Health Plans and 10 Life Insurances). This is the result of local decision and purchasing interventions, loosing leverage opportunities.

B. Suppliers & annual spend.
The current suppliers used in the region for Health Plan or/and Life Insurance services are as follows:

**Brokers:** During 2007-2008 the company has 11 brokers in Latin America: Brokers I, II, III, IV, V, VI, VII, VIII, IX, X, XI and XII.

**Insurance Companies:** During 2007-2008 the company has 10 insurance companies in Latin America: A, B, C, D, E, F, G, H, I, J and K.

**ANNUAL SPEND.**
The annual expenditure of Life Insurance and Health Plans in Latin America in year (Dec06-Dec07 was U$11MM (eleven million of dollars) (Health Plan U$9MM and Life Insurance U$1MM).

Information regarding Latin America spend, brokers and insurance companies is confirmed in the following charts.
HEALTH PLAN 2007:
Just Costa Rica has a full BMG self founded administration, Mexico, Venezuela and Brazil have the basic plan self founded and the extended coverage managed by an insurance company.

The data is shown in Figure 8 "Health Plan"

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Mexico</td>
<td>$ 4.00</td>
<td>BROKER I</td>
<td>A</td>
<td>July 2007</td>
<td>Self administered the first US$5M, then Insurance company</td>
</tr>
<tr>
<td>Costa Rica</td>
<td>$ 0.40</td>
<td>BROKER II</td>
<td>None</td>
<td>July 2007</td>
<td>Self founded administration</td>
</tr>
<tr>
<td>Guatemala</td>
<td>$ 0.30</td>
<td>BROKER III</td>
<td>B</td>
<td>June 2007</td>
<td>Insurance Company</td>
</tr>
<tr>
<td>Panama</td>
<td>TBD April 08</td>
<td>BROKER IV</td>
<td>C</td>
<td>April 2008</td>
<td>Insurance Company</td>
</tr>
<tr>
<td>Peru</td>
<td>$ 0.20</td>
<td>BROKER V</td>
<td>D</td>
<td>June 2007</td>
<td>Insurance Company</td>
</tr>
<tr>
<td>Colombia</td>
<td>$ 0.20</td>
<td>BROKER VI</td>
<td>E</td>
<td>Jan 2008</td>
<td>Insurance Company</td>
</tr>
<tr>
<td>Venezuela</td>
<td>$ 0.40</td>
<td>BROKER VII</td>
<td>F</td>
<td>JULY 2007</td>
<td>administraton + Insurance Company</td>
</tr>
<tr>
<td>Chile</td>
<td>$ 0.30</td>
<td>BROKER VIII</td>
<td>G</td>
<td>February 2008</td>
<td>Insurance Company</td>
</tr>
<tr>
<td>Argentina</td>
<td>$ 0.20</td>
<td>BROKER IX</td>
<td>H</td>
<td>July 2007</td>
<td>Insurance Company</td>
</tr>
<tr>
<td>Brazil</td>
<td>$ 4.00</td>
<td>BROKER X</td>
<td>I / J</td>
<td>November 2007 and December 2007</td>
<td>Basic Plan self founded administraton + Insurance Company</td>
</tr>
<tr>
<td></td>
<td>$ 10.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Figure 8 "BMG Health Plan"

LIFE INSURANCE 2007:
Almost all the Life Insurance or Health Plan service need to be renewed in June-July of every year. Just Costa Rica has a self founded administration for Life Insurance services, all the other countries are covered by insurance companies. It is shown in Figure 9 as follows:
C. Insurance Specifications:

Usually in Latin America, BMG has the following Life and Health Insurance specifications (average information):

**Life Insurance:**

- 24 months of salary.
- Double payment in case of accidental death.
- Disability coverage.

**Health Plan: BASIC PLAN:**

Coverage until US$300,000.

The plan should include Hospitals, emergency care, maternity and cares related, surgery and cares related.
Dental analysis not obligatory, good to have it.
Should not exclude AIDS.
International coverage.
Employee co-payment in medical appointments.

**UNLIMITED COVERAGE** - Extension of basic plan.

### IV. MARKET / INDUSTRY OVERVIEW

#### A. EXTERNAL ENVIRONMENT SCAN.

**Latin America** - Overall almost 95% of the insurance companies have local presence, nevertheless the insurances brokers have more regional participations, mainly by geographic blocks (La North, LA Central, LA Andean and LA South).

According with Watson Wyatt in WASHINGTON, D.C. during February, 2008 – **Medical cost increases for employers throughout the world are expected to accelerate over the next five years**, according to a poll of insurance companies conducted by Watson Wyatt Worldwide, a leading global consulting firm. The poll also found that, in a vast majority of countries, medical cost increases are outpacing the general rate of inflation.

Nearly three-fourths (71 percent) of respondents expect higher or significantly higher medical cost trends over the next five years. Additionally, more than eight of 10 (81 percent) report that medical costs are eclipsing the general rate of inflation in their country. The results are based on a Watson Wyatt survey of 85 insurance companies that provide medical insurance to employers throughout Asia, Africa, Europe and the Americas.

“Rising medical costs have rapidly become a global issue that reaches far beyond the United States and other developed economies,” said Francis Coleman, a senior international health care benefits consultant with Watson Wyatt. “Many of the factors causing U.S. employers to experience significant increases in their health care costs — such as increased utilization, expensive medical technology and an aging population — are having comparable effects throughout the world.”
Insurance companies in Asia and Africa are expecting double-digit increases in employer medical costs in 2008, with the exception of companies in Hong Kong and Singapore, according to the poll. The same is true in Latin America, except for Brazil and Chile, where costs are expected to increase by around 7 percent. In Europe, most insurers – except those in Italy – are projecting increases in the single digits, although respondents in all European countries said they expect higher trends over the next five years.

Following you can find a brief description of Health & Life Insurance Policies and basic concepts in the market:

- **Health Maintenance Organization (HMO)** An HMO is a type of managed health care system. A group of doctors and other medical professionals offer care through the HMO for a flat monthly rate with no deductibles. However, only visits to professionals within the HMO network are covered by the policy. All visits, prescriptions and other care must be cleared by the HMO in order to be covered. Your primary physician within the HMO will handle referrals.

- **Preferred Provider Organization (PPO)** A PPO is similar to an HMO, but care is paid for as it is received instead of in advance in the form of a scheduled fee. PPOs may also offer more flexibility by allowing for visits to out-of-network professionals at a greater expense to the policy holder. Visits within the network require only the payment of a small fee. There is often a deductible for out-of-network expenses and a higher co-payment. You will have a primary physician within the network who will handle referrals to specialists that will be covered by the PPO. After any visit, you must submit a claim and you will be reimbursed for the visit minus your co-payment.

- **Fee-For-Service (FFS)** FFS plans (also called indemnity plans) allow for visits to any medical professionals. These plans are extremely flexible, allowing you to make most of the decisions about your personal care. After the visit, you pay the bill and then submit a claim to the insurance company for reimbursement. The only limitations are that services provided must be specified in the policy in order for a claim to be accepted. These plans fall outside the label of managed care, and the result is higher deductibles and co-payments.
Medicare. Medicare is a federal program which provides health insurance for qualified individuals over the age of 65. Enrolled individuals must pay deductibles and co-payments, but much of their medical costs are covered by the program. Medicare is less comprehensive than the above programs, but it is an important source of post-retirement health care.

Medicare is divided into three parts. Part A covers hospital bills, Part B covers doctor bills, and Part C provides the option to choose from a package of health care plans. The individual enroll as soon as is qualified because, at that time, the individual can receive coverage even if have health problems. Later the individual may no longer qualify, so this free period is very important.

COBRA and HIPAA. COBRA is a federal program that allows employees to remain on their company health plans for up to 18 months after leaving the employer by paying insurance premiums out of pocket. The system is designed to prevent people who are between jobs from experiencing a lapse in coverage.

HIPAA is an Act of Congress that gives people the right to insurance coverage from any provider as long as they have been covered by a group policy in the previous 63 days. Even people with serious illnesses must receive coverage from any carrier if they can pay the premium costs, which are not regulated by HIPAA.

Premium: The amount the policy-holder pays to the health plan each month to purchase health coverage.

Deductible: The amount that the policy-holder must pay out-of-pocket before the health plan pays its share. For example, a policy-holder might have to pay a $500 deductible per year, before any of their health care is covered by the health plan. It may take several doctor's visits or prescription refills before the policy-holder reaches the deductible and the health plan starts to pay for care.

Copayment: The amount that the policy-holder must pay out of pocket before the health plan pays for a particular visit or service. For example, a policy-holder might pay a $45 copayment for a doctor's visit, or to obtain a prescription. A copayment must be paid each time a particular service is obtained.

Coinsurance: Instead of paying a fixed amount up front (a copayment), the policy-holder must pay a percentage of the total cost. For example, the member might have to pay 20% of the cost of a surgery, while the health plan pays the other 80%. Because there is no upper limit on coinsurance, the policy-holder can end up owing very little, or a significant amount, depending on the actual costs of the services they obtain.
- **Exclusions:** Not all services are covered. The policy-holder is generally expected to pay the full cost of non-covered services out of their own pocket.

- **Coverage limits:** Some health plans only pay for health care up to a certain dollar amount. The policy-holder may be expected to pay any charges in excess of the health plan's maximum payment for a specific service. In addition, some plans have annual or lifetime coverage maximums. In these cases, the health plan will stop payment when they reach the benefit maximum, and the policy-holder must pay all remaining costs.

- **Out-of-pocket maximums:** Similar to coverage limits, except that in this case, the member's payment obligation ends when they reach the out-of-pocket maximum, and the health plan pays all further covered costs. Out-of-pocket maximums can be limited to a specific benefit category (such as prescription drugs) or can apply to all coverage provided during a specific benefit year.

**B. Medical Cost Trends:**

Medical Costs trend is shown in Figure 10.

<table>
<thead>
<tr>
<th>Region</th>
<th>2006</th>
<th>2007</th>
<th>2008 (projected)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Asia and Africa</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>China</td>
<td>15.2%</td>
<td>21.2%</td>
<td>19.6%</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>6.8%</td>
<td>8.8%</td>
<td>9.1%</td>
</tr>
<tr>
<td>Philippines</td>
<td>11.6%</td>
<td>11.4%</td>
<td>11.5%</td>
</tr>
<tr>
<td>Russia</td>
<td>13.3%</td>
<td>13.7%</td>
<td>15.7%</td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>13.3%</td>
<td>13.3%</td>
<td>16.3%</td>
</tr>
<tr>
<td>Singapore</td>
<td>5.5%</td>
<td>6.5%</td>
<td>7.5%</td>
</tr>
<tr>
<td>South Africa</td>
<td>7.4%</td>
<td>10.0%</td>
<td>12.6%</td>
</tr>
<tr>
<td><strong>Europe</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>France</td>
<td>5.6%</td>
<td>6.6%</td>
<td>7.3%</td>
</tr>
<tr>
<td>Italy</td>
<td>5.5%</td>
<td>11.0%</td>
<td>11.3%</td>
</tr>
<tr>
<td>Netherlands</td>
<td>6.0%</td>
<td>5.2%</td>
<td>6.0%</td>
</tr>
</tbody>
</table>
The estimated Medical costs in Latin America for 2008 and 2009, will have an estimated increment around 10-15%.

**C. SUPPLIER RANK (INSURANCE BROKERS)**

According with Brokerage and insurance experts, following you can find an annual global insurance-brokers ranking (2007) by revenues, leading firms' results and strategies. While Marsh and Aon held their respective rankings of one and two, Lockton Cos. Inc. took a big jump in the Top 20 by moving from No. 14 to No. 10 due to its acquisition of Alexander Forbes International Risk Services. However, Aon outranked Marsh in brokerage revenues in 2006.

**1. Marsh & McLennan Cos.**


**www.marshma.com Trading symbol: MMC**

Top Lines: Commercial
Developments in 2006: Results were affected by stock option expense in each segment for the full year. Continued to see restructuring savings and charges under restructuring plans; sold Sedgwick Claims Management Services, Price Forbes (its U.K.-based wholesale brokerage business), and Kroll Security International.

2. Aon Corp.


200 East Randolph St., Chicago, Illinois 60601. Phone: 312-381-1000

www.aon.com  Trading symbol: AOC

Top Lines: Financial services; directors and officers; errors and omissions; commercial property; commercial casualty

Developments in 2006: Aon became the world's No. 1 insurance broker based on broker revenues. Company continued deployment of its global sales database, replacing more than 27 systems around the globe. Made more than $150 million worth of acquisitions.

Strategy for 2007 & 2008: Continue to measure success against operating plan built around three specific objectives: delivering distinctive client value, strengthening Aon's talent and achieving operational excellence. Continue to realize the savings from companywide restructuring program. Continue to rationalize costs while making major investments in the business.

3. Willis Group Holdings Ltd.

Revenues 2006: $2.4 billion/ Revenues 2005: $2.3 billion. Brokerage Revenues 2006: $2.3 billion/ Brokerage Revenues 2005: $2.2 billion

10 Trinity Square, London, United Kingdom. Phone: (44-20) 7488-8111

www.willis.com  Trading symbol: WSH

Top Lines: Commercial; reinsurance; construction; aerospace; energy; financial and executive risks; employee benefits; health care; niche; environmental

Developments in 2006: Held inaugural Investor Day and launched Shaping Our Future, a series of strategic initiatives designed to extend financial leadership. Launched the Willis Quality Index, an initiative to benchmark insurance carriers; completed eight acquisitions with annual revenues
of approximately $30 million. Strategy for 2007, 2008: Deliver breakout growth and performance by growing market share, making acquisitions, using technology as a competitive advantage, and being an Employer of Choice; continue the expansion of a global service client-centric model.

The Gallagher Centre/Two Pierce Place, Itasca, Illinois 60143-3141. Phone: 630-773-3800
www.ajg.com Trading symbol: AJG
Top Lines: Employee benefits; property/casualty insurance markets; risk management
Developments in 2006: AJG continued to address legal/regulatory changes related to contingent commissions; in December it reached an agreement to resolve all claims in a class-action lawsuit pending in the New Jersey Federal District Court—for which the company had reserved costs in 2005. AJG eliminated more than $100 million of investment-related debt from its balance sheet through the sale of two consolidated investments in 2006; at Dec. 31, AJG had no corporate operating related debt. AJG completed 11 acquisitions in 2006. Executive changes included the passing of Chairman Robert E. (Bob) Gallagher in August, and the election of his nephew, President and CEO J. Patrick Gallagher Jr as chairman.Strategy for 2007 & 2008: Gallagher’s Brokerage Service Retail Division anticipates its greatest revenue growth over the next year will continue to come from its niche/practice groups and middle-market accounts, alternative markets such as captives, and through mergers and acquisitions. With 165 acquisitions completed since 1986, AJG management plans to further such growth.

D. PORTER MODEL
The significance to use the Porter Model (shown as Figure 11) in this project is to understand according with the market which are the strengths and weakness, that the organization has, confirming if Life Insurance and Health Plans have substitutes in the market, if there is rivalry, barriers to enter in the market and supplier and buyers power level. The objective is to define which are the 5 forces involved in the Life Insurance and Health Plan markets, in order to be a key factor in the strategy creation.
The LA BMG Porter Model of Life Insurance and Health Plan shows that these are complex services, with high barrier to entry to this market, due to the companies needing enough cash and financial health to be competitive and get good accounts. The biggest brokers have global and regional presence, but almost all insurance companies in LA have local presence. There is a high rivalry between brokers and insurance companies to get big transnational companies as clients, providing some different value add in order to make a difference in the market. The BMG power is their name, financial stability, high global volume, although the regional volume in Latin America is significant as well and the company has leveraging opportunities, causing rivalry between insurance companies and brokers, offering to participate in Life Insurance, Health Plans, and car insurances bidding processes. The suppliers power is that the Life Insurance and Health Plans depend on the employees' deaths and illness statistics and depending on that are the costs involved in the services. Life Insurance and Health Plan do not have
substitutes, the only alternative is to confirm a self fond BMG administration, Which means do not have an insurance company involved in the process, BMG track an specific amount at the beginning of the fiscal year and if any accident happen, this fond covers the expenses and is administrated by the broker.

E. SWOT ANALYSIS

SWOT analysis (shown as Figure 12) will be useful in this project, due to define a Purchasing Strategy is definitively necessary to understand and evaluate external and internal organizational key factors, such as: The Company´s Strengths, Weaknesses and Market Opportunities and Threats. SWOT references and detailed explanation is described as follows:

**SWOT Analysis — Life Insurance and health Plan services**

<table>
<thead>
<tr>
<th>Strengths</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fluent Cash Flow Company.</td>
</tr>
<tr>
<td>Trusty Operations and payments.</td>
</tr>
<tr>
<td>Significant Life Insurance and Health plan volumes.</td>
</tr>
<tr>
<td>BMG brand name.</td>
</tr>
<tr>
<td>Global or regional contracts can be signed.</td>
</tr>
<tr>
<td>Leverage volumes opportunities.</td>
</tr>
<tr>
<td>Current Negotiations with Global Brokers.</td>
</tr>
<tr>
<td>Mainly all the insurance decisions are taking by MDO (General Offices) of each country.</td>
</tr>
<tr>
<td>The employees number across the region has been stable.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Opportunities</th>
</tr>
</thead>
<tbody>
<tr>
<td>The services we required are available in the market.</td>
</tr>
<tr>
<td>Take advantage of our brokers to get more local and regional information and employees statistics.</td>
</tr>
<tr>
<td>Take advantage of our Global RFP.</td>
</tr>
<tr>
<td>Split the brokers volume reducing the numbers of suppliers.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Threats</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exchange rates.</td>
</tr>
<tr>
<td>Inflation.</td>
</tr>
<tr>
<td>The insurance companies has local presence, reducing the possibility to apply regional approaches, although is possible with brokers.</td>
</tr>
<tr>
<td>The insurance costs threat to increase during the next 5 years. Every country has different benefits and obligations.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Weaknesses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Limited resources in the sites and countries to fully support sourcing interventions and with out full spend pool knowledge.</td>
</tr>
</tbody>
</table>

Figure 12 "BMG SWOT Analysis"
The **BMG Life Insurance and Health Plan SWOT Analysis** shows internal and external factors proving visibility of the market. BMG Strengths and Weaknesses. The BMG Strengths are that it has a financial stability, known in the market (Brand name), with global and regional leveraging opportunities due current negotiations or new initiatives. High Global/ regional Annual Volume and all the sites require Life Insurance and Health plan services. The BMG weaknesses are every sites have different benefits and insurance coverage, making more difficult the sourcing work and leveraging, but possible, although Sourcing does not have resources in every country. The Threats are economical changes in the region, such as inflation, law changes. Unfortunately the insurance companies have local presence, reducing the possibility to use them in a regional approach, Nevertheless the possibility reach in the brokers companies, which have in some cases global presence.

**F. SOURCING CHOICE MODEL.**

The objective of the **Sourcing Choice Model** (shown as Figure 13) is to identify according with the volume, complexity and risk of the service evaluated, what kind of category is in the company and depending of that, How should be managed and negotiated.

Life Insurance & Health Plan is a **strategic category**, due the regional volume in Latin America is significant (U$15MM) and is complex because every country has different specifications, laws and Human Resources policies. Having this information the best **Strategic Sourcing Approach** is to search a Volume concentration strategy with the vendors across the region and find the best price, evaluating services, coverage and geographic locations, consolidations commercial relationships with suppliers as business partners.
SOURCING CHOICE MODEL

V. BUSINESS NEEDS.

1. **Service Level/ add value.** Ensure and Improve life insurance and health plan service level, covering the services required under their medical coverage, providing value to our organization, having good geographic coverage, quick response timings and looking for the best benefits for our company.

2. **Reduce suppliers database.** The business need to reduce the entire suppliers database in 30% in 3 years time frame. Ensuring the remaining vendors cover the business needs.

3. **Cost Reduction.** Our savings targets are more aggressive every year. That is one of the reasons we hope our vendors can find the best approach, have updated information and innovative structures to offer better services & value with less costs.

4. **Process Simplification.** Find the way to simplify the negotiations every year, involving less purchasing and human resources, taking advantage of current commercial relationships, understanding and covering the business needs.
5.- **Sub spend pool Control.** To know when the policies need to be renewed, performed market and industry analysis, anticipating risks and implementing new policies, technologies or coverage, having frequent contact and coordination with Human Resources and Finance.

**VI. DESIRED RESULTS.**

**FINANCIAL RESULTS:**
To obtain U$1.1MM (One point one million dollars) in cost savings (hard savings) over the next 3 Fiscal Years (FY) on a regional level (Latin America). An estimation is to reach U$0.10MM in Life Insurance and U$1MM in Health Plans.

**PROCESS AND PRODUCTIVITY RESULTS:**
- Reduce Supplier database by 30 percent over the next 3 Fiscal Years on a regional level.
- Ensure all the payments are performed through Purchases Orders.
- Improve data accuracy and data control (Purchasing Group, Sub spend pools, sourcing buyer responsible, Preferred Vendor List, etc) supported by PSL (Procurement), working together to accomplish new improvement process, initiatives and projects.

**VII. STATEMENT OF STRATEGY**

Ensure sustainable quality, service level and value added provided in the region, reinforcing the commercial relationship with key suppliers and internal customers, promoting innovation and the best benefits for the organization, applying leveraging and market opportunities.

**VIII. STRATEGY PLANKS**

**PLANK 1: SUB SPEND POOL CONTROL AND RESOURCES PRODUCTIVITY.**

Ensure sub spend pool control via keep searching and confirming updated information and data of current suppliers (brokers and insurance companies), services specifications, annual spends and fees, expiring dates and be able to develop strategic work instead just tactical interventions by country. The internal and external resources should improve their sourcing skills and general productivity.
RATIONALE:
Since Employee services comes from a White Space and almost all its services were managed by Human Resources in the past, including Life Insurance and Health Plans, there is still missing information and data in some countries. Several organizational changes happened in the last 2 years and even the last year (2007), Employee services team has performed a deeply spend pool investigation regarding contracts, expiring dates, annual spends, obligations, current suppliers and brokers, It is necessary to keep working to have updated information, being able to develop sourcing strategies and reduce tactical interventions in the markets, be focused in regional vision and opportunities.

TACTICS: LA Life insurance and Health Plan:

1.- Sourcing Buyers need to keep searching and updating the sub spend pool information (contracts, policies coverage, expiration dates, annual spend and fees, current suppliers).
2.- Keep communication with BMG Global Insurance leaders to know global initiatives and preferred vendors in other regions.
3.- Be focused to ensure the insurance services are being provided, covering internal customers expectations, ensuring the insurance policies are being renewed every year under the best benefits and conditions for the company.

PLANK 2: INTERNAL LEVERAGE & MARKET INTERVENTION AND ANALYSIS.

Drive Costs Savings and Vendors reduction via leveraging volumes, promote competition reducing supplier database across the region. Maximize the value added and services provided by suppliers looking for the best benefits and innovation for our organization.

RATIONALE
Since Life Insurance and Health Plan part of Employee services (ES) are required globally and regionally (Latin America), representing almost 30% of ES LA Strategic Sourcing Team should take advantage of global negotiations in place, at least under insurance brokers scopes due insurance companies have local presence in Latin American markets. Reinforcing the commercial
relationships, looking for the best market value, benefits, coverage, and service level, reducing current rates & fees through leveraging alternatives.

**TACTICS: LA Life insurance and Health Plan:**

1.- Identify, analyze and evaluate the current spend and supply data base in the region.
2.- Evaluate in which countries the brokers and insurance companies have presence.
3.- Leverage volumes, developing a pool of preferred vendors by region or at least by sub regions (LA North, LA Central, LA Andean, LA South).
4.- Share LA potential vendors with Global BMG insurance leaders in order to be aligned and provide an explanation if the potential brokers do not match, confirming the LA reasons, market trends and risks of why the team is recommending other vendors.
5.- The brokers should perform a new market analysis and BMG requirements in order to define if the current insurances cost (life insurance and Health Plan) require insurance companies coverage or BMG can apply a self founded administration managed by our brokers. Cost-Benefits.
6.- Perform regional bidding processes every year, taking advantage of leveraging volumes. The best approach is to homogenize the expiring dates/year, getting annual statistics and perform just one bidding process per year instead of 10 or 20 biddings per country without leveraging even the vendors be the same.

**PRELIMINAR BROKERS ANALYSIS & INVESTIGATION 2008.**

The preliminary regional brokers investigation is shown in **Figure 14.**
AON, Willis Group and Marsh are the broker with better geographic coverage in Latin America, having presence in all the countries, except Marsh without local presence in Guatemala and Costa Rica.

The best approach will be select the best 2 or 3 brokers in the region by sub-regions like: North, Central and South or South and North+Central.

**PLANK 3: PROCESS AND SPEND POOL OPTIMIZATION.**

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Figure 14 “Preliminary Broker Analysis”

**RATIONALE:**

Due tactical interventions have been used instead of Strategic work, the team needs to evaluate and apply technological tools providing automation, facilitating Sourcing approaches, data and information extraction, involving PSL initiatives and tools as well. The ES Team needs to improve
the relationships with PSL, sharing the expectations and scores of both areas, ensuring PSL in handling day to day work and tactical interventions.

**TACTICS: LA Life insurance and Health Plan:**
1.- Identify, analyze and eliminate FI’s payment processes.
2.- Reinforce with internal customers PO (Purchase Orders) applications.
3.- Use BBP /PVL (Preferred Vendor List)
4.- Ensure all the members of the team have access to Sourcing tools as CSTS, One Window, BW, SAP.

**IX. RISKS AND RISKS MANAGEMENT PLAN**

1.- Low involvement of HR management.
**How do we manage it?**
Work with Purchasing Group Managers by clusters (LA North, LA Central, LA Andean, LA South), reinforcing the commitment and benefits between areas and the company. Purchasing & Human Resources Directors are available if the topic requires to be escalated.

2.- Sourcing resources Required /skills/ Frequent ES organizational changes.
**How do we manage it?**
Purchasing Top Management need to evaluate the current LA volume, complexity, staff performance and frequent organizational changes and roles, loosing knowledge and seniority.
The Employee Services Purchases team needs to understand a regional vision is required instead of local approaches and interventions.

**Alignment.** In this part of the project, Purchasing Top Management approves the document.
5. **Company Benefits:**

The company will have different kind of benefits with this project (Purchasing Strategy) and are described as follows:

- **Economics.** - An estimated saving of U$1.1MM (one point one million of dollars) projected in 3 years.

- **Process.** - Business Simplification, evaluating alternatives to reduce the number of suppliers (insurance companies and/or brokers) in the region, which will provide more control in the annual spend, coverage, specifications, improve the commercial relationships with the suppliers, increasing the leveraging opportunities.

- **Strategic.** - Regional Vision in a strategic point of view, reducing the tactic interventions, analyzing the market, industry and trends, which are the basis for the next 2 years consolidating the Employee Services Purchases, being the basis of other services strategies.

- **Internal Control.** - This regional strategy is aligned with BMG procedures and internal policies be part of internal and external audits, providing more control in the information, taking better decisions.

6. **Next Steps:**

6.1 **Implementation Plan:**

The implementation plan is start in May 08 defining which will be the best approach with the best 3 brokers in the region and renew the Life Insurance and Health Plan policies in July 2008.

It will be a continuous process, keep evaluating the market and the industry across the region.

The strategy part has been concluded, the implementation phase should start since April 08 concluding in July 2008.
6.2 Implementation Staff:

The Implementation Plan and Staff is shown in Figure 15.

Figure 15 “Implementation Plan and Staff”

The Latin America Purchasing team will be responsible to perform and manage the strategy creation and implementation. Due the strategic phase is concluded, every sourcing buyer located in North, Central and South Latin America should start the implementation phase since April 2008 to conclude the negotiations and changes in July 2008.
7.- Project Quality.

**7.1 Results VS objectives:**

The obtained results are aligned with the initial objectives, which basically was perform a market and industry analysis, performing a deep understanding of the internal and external company environment. The results were properly achieved on time and with the information and conclusions that the company sponsor wanted.

**7.2 Action Plan Accomplishments.**

The due dates targets defined since the beginning of the Project and activities, were achieved on time. The strategic phase was concluded finishing the following activities:

- Market and Industry analysis.
- Theoretical references.
- Internal and external company environments.
- Purchasing Strategy and tactics planks created.
- Potential brokers were analyzed and a new supplier selection was recommended, nevertheless a full investigation should be continue and implemented in the next months.

**7.3 Benefits VS Expected Results by the Sponsor.**

The benefits exceeded the sponsor expectations due can provide savings. The sponsor willing was to have a formal purchasing strategy of Life Insurance and Health Plan services across the region, if as a result of this analysis a hard savings or cost avoidance can be obtained after the suppliers change or sourcing negotiations are extra expectations. The BMG Director and Group Manager are excited to implement the strategy and more because is the first of employee services purchases. The idea is that Strategic Sourcing really create sourcing strategies evaluating the market, company situation and trends and not just perform purchasing interventions, negotiating local services and individual volumes.
8. **Experience and observations.**

The experience has been heartening, developing professional skills and knowledge. The project shows theoretical and professional information and guidelines confirming which are the best Sourcing practices and steps to create a Purchasing strategy.

The experience helped to really understand the market and industry across the region. Due day to day work, very simple tasks or activities can be performed but due work load, the professionals do not do it, although is essential information that can provide several benefits to the company.

This project demonstrates how regional purchases can be performed and managed. This example is that even the Purchasing Manager is located in Mexico and the sourcing buyers in key Latin American countries; it is possible and can be a success project.

The observations are that not all the projects can be done using only professional skills or academic knowledge, it must be a combination between these 2 concepts and knowledge, and putting together what have we been learning in these years, having theoretical reference and support.

In the real life, the most difficult thing in the projects is to know which people should be involved, how the information should be requested and plan the timings, knowing that not all the areas work in the same way that ours, some can immediately provide information and data and others not. In this case, Purchasing works a lot with Human Resources and Finance, but using other tools as SAP (ERP), Business Warehouse and intranet can be very useful to obtain basic information or data to take decisions or having basic information, how should we plan the project, resources and timings.

This project should not be measured for the pages number, in the real life we know that we must be direct to the point and abbreviate the information in order to cause interest and the people really read it.
This is the project of the whole Mastery in which can fully be applied knowledge and professional interests, due the student has a sponsor and have a direct impact to the companies, a deep analysis needs to be performed. The student needs to plan their tasks, where to search and which information is relevant and which not. I thinks is not value added just copy information or deliver 200 pages if it can be summarized in 50 or if the theoretical reference is too much and is not relevant to the professional project or companies expectations.

In this kind of project the most valuable information is to know the current company situation, market trends, which opportunities we have, how we can take advantages of the resources and how the projects can be implemented comparing costs and benefits.

9. CONCLUSIONS.

The project is a value added for the company, being the base for future strategic purchases. It is a combination of theoretical and professional knowledge. It is very interesting because nowadays the word “strategy” is very popular, is used in articles, subjects, company areas but just a few knows exactly which are the responsibilities or activities to be performed.

As was confirmed at the beginning of this project, The strategic sourcing area is responsible to evaluate the markets, technologies, trends and have a deep understanding of the services, materials and how important are for the company, defining the next steps and negotiation approaches, even is quite difficult to perform a regional strategy being located in Mexico, the solution is to create networking and teamwork being able to understand the different markets.

This project is very important for the company with immediately application. After analyzed the market, industry, potential vendors, costs trends, internal and external environment, we can conclude a leveraging strategy can be used, performing a deep analysis of suppliers and geographic coverage. For sure the company can select just 3 brokers in the region, improving commercial relationships, processes, control and get savings.

This is a great opportunity to mix academic and professional knowledge, getting the information and conclusions to the real life.
10. **Notes and References.**

1. Howstuffworks: How Health Insurance Works
Encarta: Health Insurance

2. See California Insurance Code Section 106 (defining disability insurance). In 2001, the California Legislature added subdivision (b), which defines "health insurance" as "an individual or group disability insurance policy that provides coverage for hospital, medical, or surgical benefits."


http://en.wikipedia.org/wiki/Health_insurance
http://www.businessinsurance.com/cgi-bin/news.pl?id=12202