

Creating Strategic Supply Chain Partnerships

A systematic approach for the Oil and Gas industry

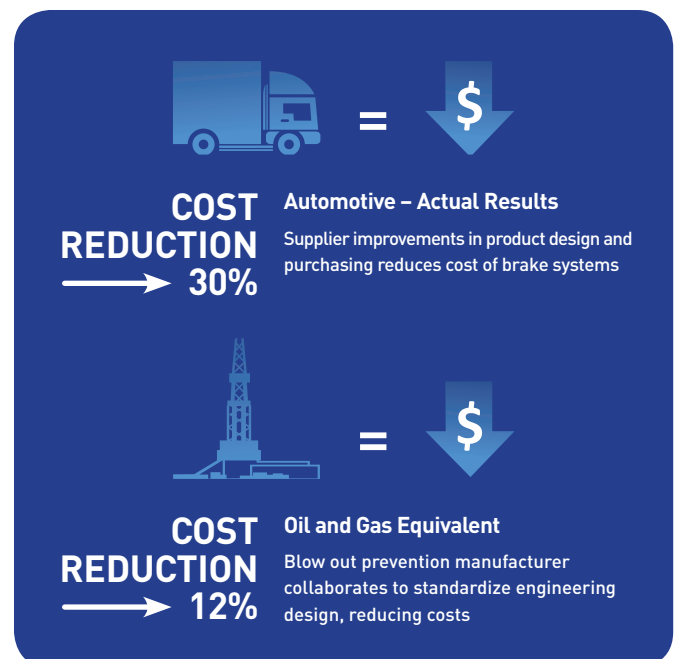
There is an archetypal cycle to how Oil and Gas companies pursue improvements to their Supply Chains. We need to break this cycle.

When oil prices are high, companies and their suppliers of products and services each pursue improvements in their own respective parts of the Supply Chain. When the oil price falls, as it has recently, the word "demand" no longer refers to what E&P companies are consuming but to what they want from their suppliers: price and cost reductions ... now!

The industry needs to find a way out of this cycle. While we recognize that application of best practices in Supply Chain management can drive hundreds of millions of dollars of savings, we believe that in the Oil and Gas industry most of these improvements take place in the silos of customers and suppliers. We believe that there is even more to be realized by instead focusing on the interfaces and partnership opportunities between participants in the Oil and Gas value chain.

Industry Cousins?

The most cited and successful examples of such Supply Chain partnerships – joining the silos of suppliers and customers – come to us from the automobile industry. Toyota and Honda stand out in particular for having reaped huge benefits including significant cost reduction by accomplishing this in their North American operations - and this despite the huge cultural bias against this way of managing the Supply Chain.¹ Yet there are some fundamental similarities between the two industries that lead us to believe that these successes could be achieved in Oil and Gas as well.



What drives this need for a high level of supplier integration in these industries? Capital intensity, long-term planning horizons and an ever increasing level of dependence on key suppliers (in some cases a few vendors may account for up to 70% of product costs) have made the ability to collaborate with one's major suppliers a critical success factor in the

¹See Jeffery Liker and Thomas Choi, "Building Deep Supplier Relationships", Harvard Business Review, December 2004.



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marketplace. Toyota and Honda have been able to lead the curve in costs, quality and innovation in North America through close collaboration and integration with their suppliers - and not just for this quarter or the next, but for the entire product life cycle.

By contrast, upstream Oil and Gas have not taken a systematic approach to Supplier Integration. Sure, E&P companies can point to close cooperation with drilling contractors, cement companies or transport providers – but for most cases the extent of cooperation and sharing of information falls far short of that achieved in the auto industry. Which leads us to ask: Shouldn't we apply this model here as well?

Evolve's Supplier Integration Model

Our model is based on eight fundamental principles of integration between the organization buying goods and

services – and we mean the entire organization – and the company providing them. Your primary objective will probably vary, but be it value stream performance, lower unit costs, reductions in cycle times or improved innovation, it is at the center of your target.

By creating a shared vision with your suppliers, with clear expectations and ways of measuring and managing performance a higher level of understanding is achieved. This together with visibility into and the determination to improve each other's operations and processes, while supported by relationships mapped to the right person at each level you can turn a source of adversity into a source of competitive advantage.

A high level view of this model is illustrated below. **F.1**

We believe that these forms of collaboration are lacking and are in fact applicable to Oil and Gas. By taking a systematic approach the industry can reap similar benefits such as lower costs, reduced cycle time and accelerated innovation.



“Both parties need to be putting something on the table that they wouldn't have done before. Otherwise it's just negotiating or a transaction.”

Oil and Gas Supply Chain Executive
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