Caravel

LEADING THE WAY IN PROJECTS

Strategic Procurement Projects

Encompassing Bid and Tender Management

Caravel Group – commercially proven expertise for the procurement process

THE SPECIALIST FOR LARGE COMPLEX MULTI-DISCIPLINED PROJECTS

Procurement Projects

Business is all about the buying and selling of products and services. Issuing tenders and bidding for work therefore represents familiar territory for most organisations. However, unfortunately it is often performed badly, resulting in significant loss of stakeholder value for one party or another.

The formal procurement processes are inextricably linked to major projects in industry sectors such as construction, transport, process industries or utilities.

Procurement projects encompass a complex web of processes as customers and suppliers alike strive to derive maximum stakeholder value from an increasingly competitive business environment.

Before a contract can be executed, the purchaser has to manage the requirements specification, tender evaluation, negotiation and finally the contract award.

The other side of the coin sees suppliers faced with requests for tenders/proposals/quotation, solution development, tender submission and contract negotiation/award.

Whatever the procurement project may be, its focus usually rests on the commercial risk management as both parties seek to transfer and treat risk in the procurement process.

The objective therefore is to develop a contractual structure that allows the appropriate transfer and acceptance of risks between the parties, in exchange for fair value. After all, both parties aim to accomplish a successful outcome for their respective stakeholders.

Achieving this goal requires a clear understanding of the underlying concepts and the pitfalls. Organisations with access to the necessary expertise have a distinct advantage over those that don't.

As an expert in major strategic procurement projects, Caravel has the core capabilities to help clients bid for work and manage tenders. We have a strong track record as procurement project partners and have successfully managed large, high-profile procurement projects.

The procurement environment

Procurement projects usually operate within a multifaceted and often multi-organisational environment that demands careful consideration of technical, regulatory and commercial parameters, as well as their respective constraints.

Regulatory issues

The solution specification and preliminary development relies on effective interaction between the parties. However, for probity reasons this also has to be kept under strict control and is especially stringent for large organisations, government agencies and publicly listed companies.

In addition, tenders involving government agencies are bound by a rigorous legal environment involving various legislative acts that support a level playing field.

Transferring knowledge and information

The procurement process involves a significant amount of information/data gathering in addition to formal specifications of requirements. Depending on the nature and size of the procurement, additional knowledge and information may be transferred in one of several ways:

- by means of 'open house' sessions with both parties in attendance
- by allowing tenderers access to information in specially appointed data rooms
- as part of a formal due diligence process
- a mix of the above

Technical constraints

The technical environment can be difficult and multi-faceted, and often requires a systems retrofit, involving the integration with existing systems. It is important to note that Greenfield environments have their own requirements and consequently also carry other types of risks.

Change management

The deployment of new systems usually impacts on operators who need training. This can be of crucial importance as incomplete training may represent a significant threat of incident on the one hand, or complete failure to deploy on the other. These facets can become more complex when linked to an industrially active environment.

Commercial issues

In instances where an organisation introduces new systems, it may interrupt the delivery of existing services or impose a temporary capacity constraint during transition. As a result, the project has to deal with significant commercial constraints. For security management projects, security integrity must be maintained at all times.

Procurement mix

Procurement projects fall into one of three categories:

Product procurement is concerned with features and benefits of a product and may also focus on emotional aspects of product ownership.
Service procurement captures the entire spectrum from professional services at one end, to technical, trade and operational services at the other. The spotlight is on capability and reliability of supply, as well as cost and benefits derived from the services. Value is a key attribute of this procurement.
Product and services represents both of the above with a focus on balance of features and benefits of each.

Dimensions of the procurement exercise

- Funding requirements
- Procurement philosophy and risk profile
- Conditions of tendering / contract
- Tender schedules
- Performance and measurement requirements
- Service level agreement; balanced scorecard
- Evaluation methodology and assessment criteria
- Requirements analysis and specification
- Functional / technical specification
- Governance matters

Procurement strategy and stakeholder value

Organisations traditionally adopt a dual procurement strategy:

1. Identify panels of suppliers that deliver personnel or product at least cost.
2. Identify panels of integrators/outsource partners that are capable of full solution design-build-operate and can accept the transfer of risk.

While this approach is commonly accepted as useful, it can often fail to deliver optimum value as it lacks a mechanism to manage risk and consequently also stakeholder value (as opposed to cost).

After all, the objective is to attain a maximum net value from delivery by minimising the risk of supply.

A typical business case for the purchase of an asset will express this in terms of NPV compared to the expected ROI over the asset lifecycle, conventionally expressed as:

Expected Stakeholder Value = $ invested × ROI per annum over asset life

In reality however, projects often experience scope creep, delays and price increases, all of which diminishes value. Similarly items may be removed from the scope as undeliverable, again resulting in a significant loss of stakeholder value.

Therefore the formula for net stakeholder value really is:

Net Stakeholder Value = Expected Value – Lost value

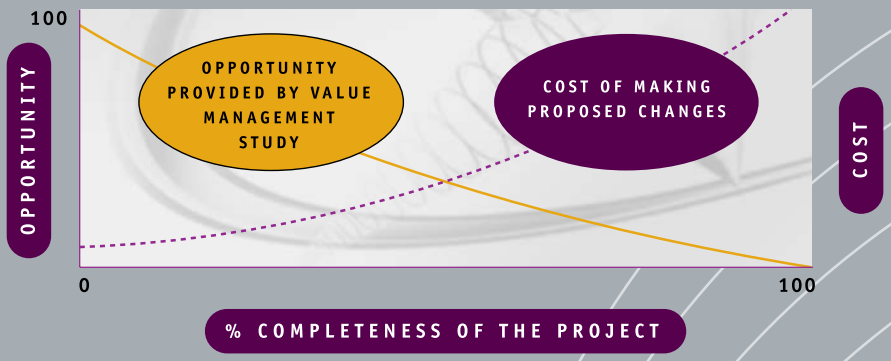
Purchaser value is optimised by suppliers that are specialists in their field; this especially applies to the discipline of project management.

Protecting the value of your project

In order to ensure a maximum net stakeholder value from the delivery, the procurement process needs to consider value management principles.

Value management establishes the loss of value through scope creep and clearly identifies items that may represent a disproportionately high cost by comparison to the low value they add to the project.

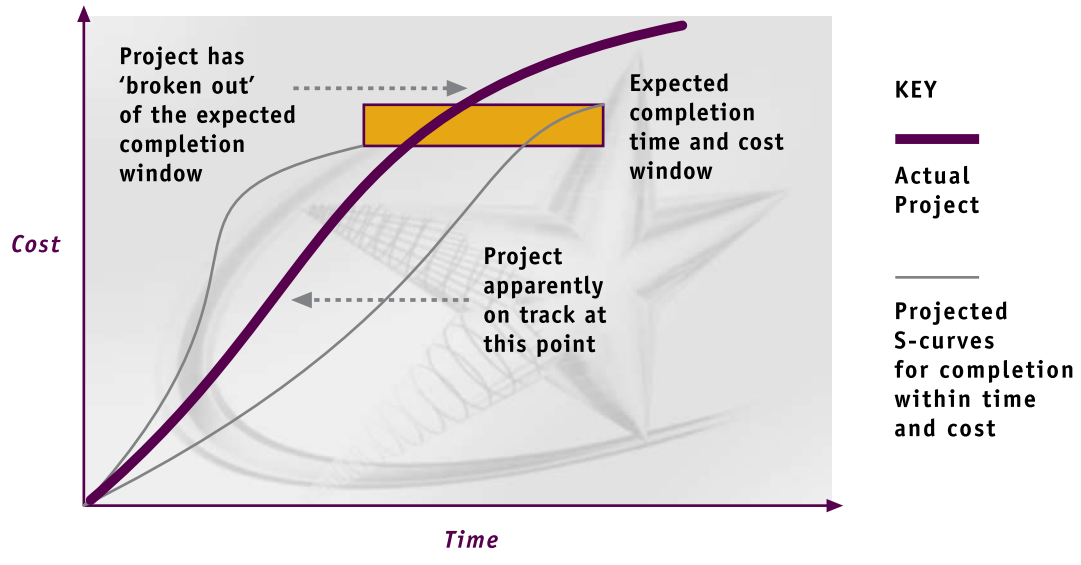
It is important to note that while value management is an important tool for eliminating items of low stakeholder value from the project, it is unable to fully address stakeholder value issues. The root cause of most lost stakeholder value in project delivery, namely poor project management/governance at all levels by all parties, remains unfettered by value management principles. Regardless of the terminology, the real focus of value management is, in fact, on cost.



The breakout phenomenon - controlling supplier contract value

In order to determine the true progress of a project of deliverables, appropriate tools have to be deployed to determine whether or not the project is on track to be completed within the expected time and cost window, and whether suppliers should be paid.

Caravel has adopted the earned value technique which places a value on the work delivered against time, and compares this with the baseline project plan. This is plotted against the minimum/maximum expected time and cost positions within which a project is likely to be completed. The graph reliably detects projects that appear to be on track, yet are actually about to 'break out'.



The paradox of cost and value

It should be considered that the definition of *cost* and *value* is largely context based and depends on the frame of reference. The concept of earned value, for instance, represents stakeholder value for the supplier while it constitutes a cost for the purchaser.

People – a fundamental aspect of real procurement value

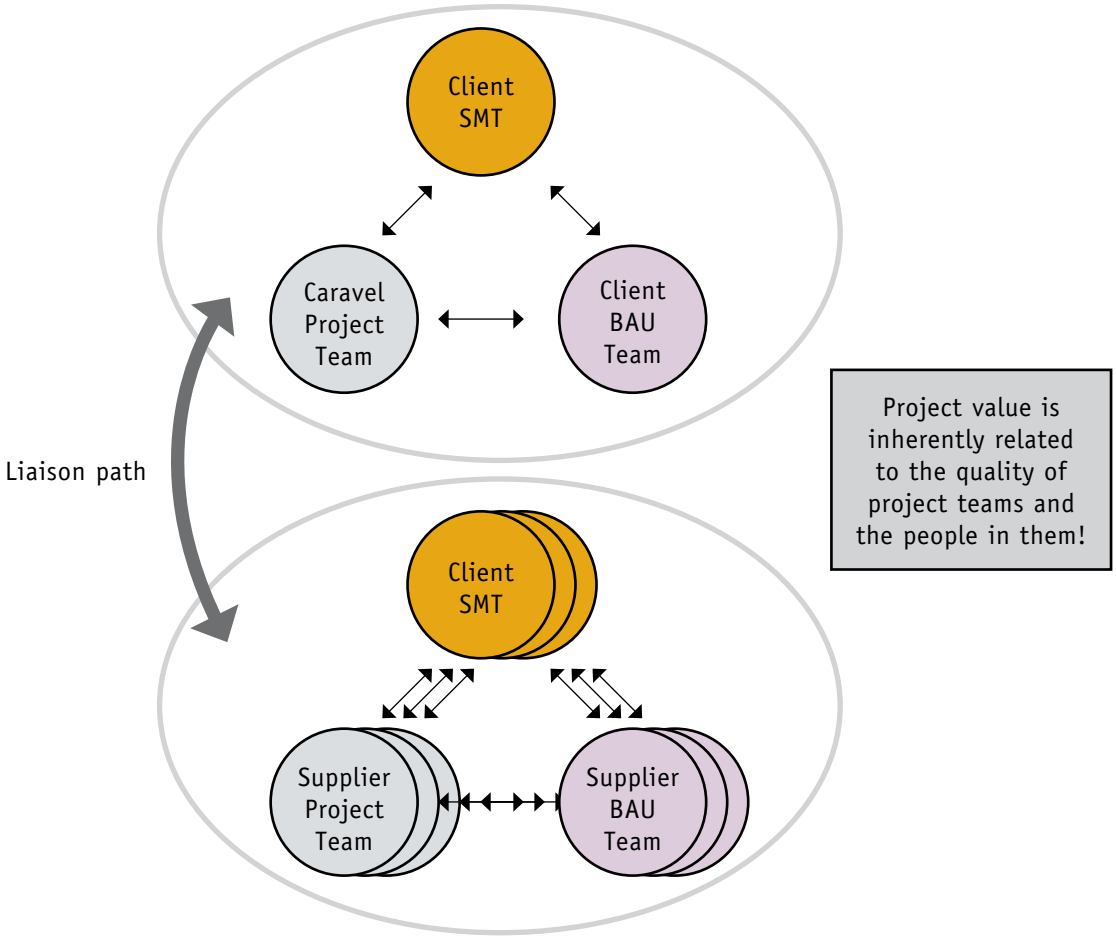
For suppliers and purchasers alike, the procurement process represents a project to be delivered.

As an expert in project delivery, Caravel has identified that the most important factor driving project stakeholder value, is the performance of the project team.

It is a matter of fact that people are the root cause for lost project value through ineffective project delivery.

Optimal project value can only be achieved by effective teams. However, forming an effective project team is a job for specialists and must address:

- The project team leadership;
- The specialist project firm responsible for the project delivery methods, tools and associated collateral;
- The purchasing organisation's leadership, senior management team, line managers and project governance capabilities summarized as project management maturity;
- The supplying organisation's leadership, senior management team, line managers and project governance capabilities summarised as project management maturity.



Risky Business

Procurement risk in context

A common procurement situation – the delivery of an asset – comprises three parties; a *purchaser*, a *supplier* and an *operator*. All of these introduce their own risks to the procurement process.

- The purchaser, whose objective is to derive revenue from the process, introduces procurement risks.
- The supplier introduces risks related to the building and delivery of assets.
- The operator enters the equation with significant operational risk.

It is absolutely vital for the health of a procurement contract that all risks are assessed as early as possible. Failing to do so, can have costly and significant repercussions for the duration of the contract and beyond.

When unanticipated effects take priority

For a procurement process to be rewarded with success, it needs to focus beyond the provision of products and services at the right price. It is imperative to consider the central aspect of commercial risk which often pervades projects and drives the loss of stakeholder value during deployment. In many cases this can make price or cost considerations a second order effect. Risks and costs of deployment, by contrast, essentially drive stakeholder value and therefore assume the first order effect.

In many instances, project risks are poorly understood by project partners and, in due course, inappropriately transferred in a misguided effort to minimise commercial risks. All too often project delivery contracts are let to non-specialist parties. However, since the project delivery cost clearly represents a second order effect – compared to stakeholder value with its associated first order effect – it seems incongruent to treat projects with substandard project delivery capability.

A commercial imbalance of negotiating power inevitably leads to an inappropriate transfer of risk that ignores the core capabilities of the parties, resulting in significant loss in stakeholder value.

While service or product providers are often all too keen to accept risk in order to win a contract, this rarely bodes well for the project at large. After all, the conventional process typically fails to consider whether or not the party that owns the risk is also sufficiently equipped to remediate its consequences, should they occur.

The potential for severe and expensive mitigation can often dwarf the initial project cost, obliterate any project stakeholder value and add additional layers of legal complexity.

A meaningful approach to commercial risk management

Project risk is a major hurdle to overcome; nevertheless it must be accepted as a fact of life. The basic premise for project risk applies - it has to be first identified, then treated, removed or transferred.

In a procurement situation this requires timely interaction between the parties so that they clearly understand the extent of deployment and operational or commercial risks. Rather than be offloaded by the purchaser as a matter of course, the risks should be transferred to the party best able to treat and manage them, in exchange for fair value.

This is a fundamental requirement for a successful procurement process, yet is rarely addressed before the final contract, usually at the expense of project success.

The ideal scenario involves meaningful interaction between the parties so that everybody clearly understands the extent of deployment and operational risks.

The procurement philosophy has to acknowledge that the party best able to manage a risk should also own it. This avoids the common scenario of risks being bundled and transferred to a party unable to treat or remediate them.

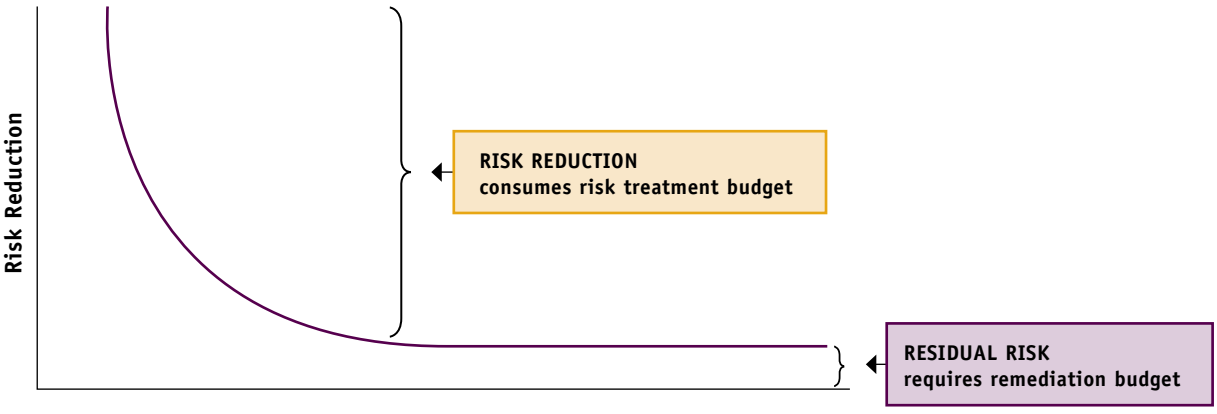
Addressing risks in the budget

The transfer of risk goes hand in hand with negotiations over the fair exchange of value to accompany the risk.

It is vital to establish and allocate an appropriate risk treatment budget that reflects the distribution of identified risks and the parties' capability of dealing with those risks.

And because risks can never be reduced to zero, the project team also needs to establish a risk remediation budget as part of the procurement process.

Cost of Risk Treatments



A residual risk remediation budget needs to be included in the procurement plan funding.

Funding requirements

Large transport and utility procurement projects often feature finance or funding components as part of the deal. In these cases it is common to form an Alliance that includes investment bankers, or Public Private Partnerships in the case of large public sector procurement.

It should be noted that Alliances are also increasingly used as an effective vehicle for sharing risks and rewards. They also serve to minimise existing risks by virtue of the involvement of specialist businesses. Thus, Alliancing is consistent with the message that "the party that owns the risk should treat it".

Typical funding structures at a glance:

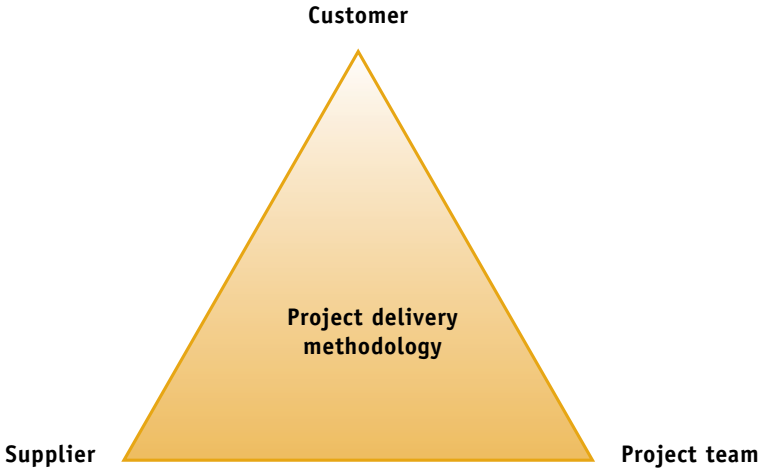
	Strength	Weakness
Public-Private Partnership	• Funding provided externally • Powerful partnerships • Single lead supplier	• Made up of multiple, smaller teams from different suppliers – leads to high risk of loss of stakeholder value • Constant tension between supplier and customer • Highly visible failures • Must meet hurdle rates
Alliance	• Shared gain and pain • Alignment of outcomes • Win-win • Profit and overhead generally at risk for supplier • Significantly increased potential for innovation as the Alliance is based on win-win outcomes	• Resource intensive • Relies on a level of trust and disclosure not normally available in a conventional contract • Owner and Alliance partner share some of the risk
Outsource	• If handled correctly provides significant ability to increase delivery capability • Tax effective • Potential for innovation	• If wrong procurement approach selected will lead to significant loss of stakeholder value • Risks generally not transferred or considered
In-source	• Generally considered the least risk since outcomes are directly under management control • Ability to apply trusted resources to solving the delivery problem	• Business-as-usual suffers • Portfolio of projects does not align with business program • Reduced potential for innovation
Conventional procurement	• Tried and trusted • Most management in comfort zone • Works well for simple procurement tasks	• Does not treat risks well • Procurement approach often at odds with deriving maximum stakeholder value

Spotlight on Methodology

An appropriate project delivery methodology applied to the procurement project is invaluable, and a basic premise of project success.

It is the glue that binds the customer, supplier and project team.

Organisations readily point to their “project management methodology” as evidence that this requirement is met.



However, upon closer inspection, it usually turns out to be a “project progress monitoring methodology”. While it includes checklists and spreadsheets for typical project lifecycle steps - from development and funding through to project initiation, execution and close out - it fails to address core project delivery and implementation methods. Similarly, the procurement itself is a project but it is often reduced to a series of “gate” steps that ensure financial accountability without addressing the outcomes.

The result is a project that is run at the whim of the project manager who may, or may not, adopt PMI approved methods with appropriate breakdown structures. More importantly however, the project manager cannot capitalise from proprietary proven methods and approaches that a specialist project management business adopts.

Industry statistics demonstrate the adverse impact of this scenario with a 35% failure rate attributed to inadequate project delivery management. When combined with the 35% failure rate due to poor project governance by senior management team and line managers, this suggests that around 70% of projects will fail. These figures, which include the supplier organisation project senior management team and line management deficiencies, may rise further if the supplier organisation’s project capabilities are deficient.

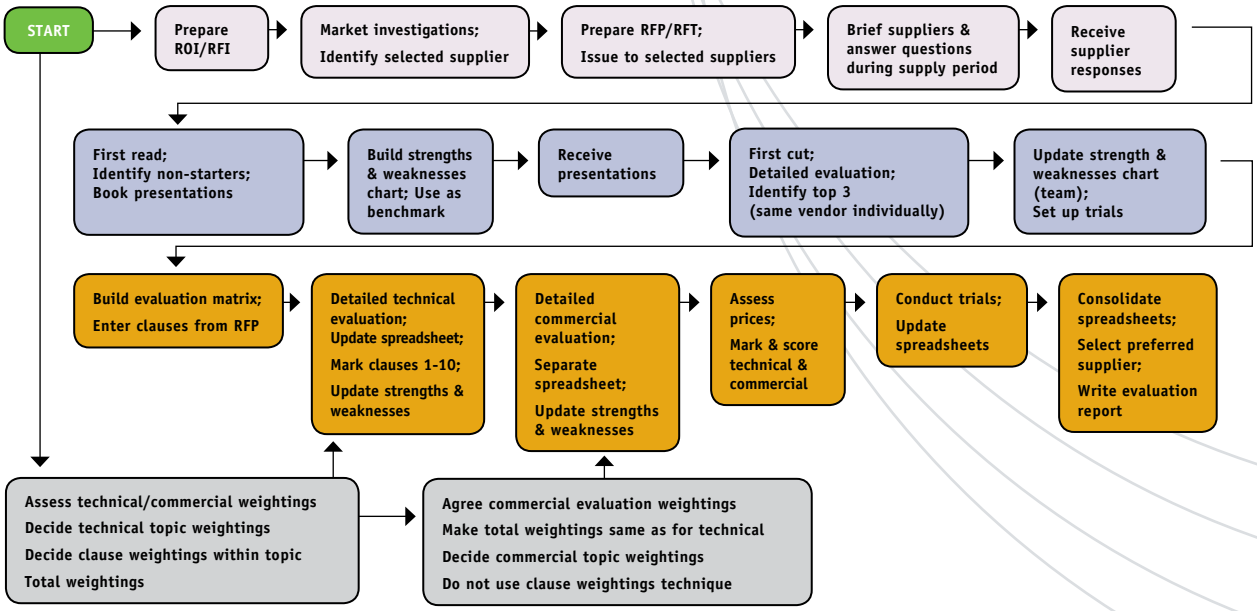
Managing Tenders

It is important to establish commercial parameters and consider specific matters that add clarity and stakeholder value to the tender process.

- Purchasing organisations need to establish the context of the supply and explain business requirements and objectives.
- Similarly, scope breadth, scope complexity and inherent commercial risks must be established and discussed at an early stage.
- Boundary diagrams coupled with volume metrics are used to help describe the scope of activity.
- A thoroughly strategic approach should be adopted to address matters of funding and risk.
- Service Level Agreements and Balanced Scorecards are used as a strategic planning and measurement tool to describe the desired performance criteria requirement.
- The organisation needs to adopt appropriate techniques to manage the selection process with "open house" sessions for disclosure and formal interviews which include only people responsible for the project delivery (rather than sales people).
- As part of supply management, it is important to establish the techniques that will be used to drive prices down and performance up over time.

To determine whether or not benefits are being derived from a project, its value is usually assessed at the beginning i.e. during the development stage, and then at completion. However, the value lost during deployment or execution is rarely considered which delivers an incomplete picture of the actual project value to an organisation.

Caravel's tender management methodology



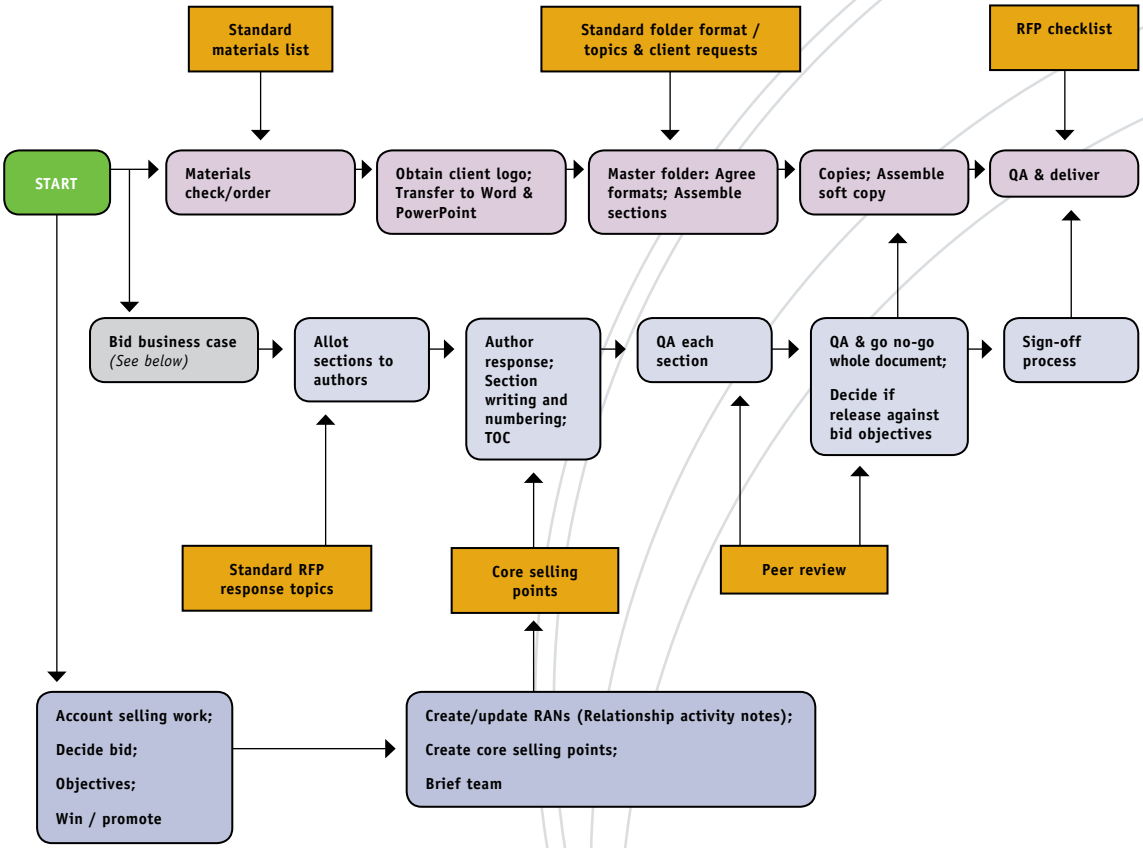
Caravel's approach considers the total cost of ownership (TCO) as well as the total value of ownership (TVO).

Managing Bid Projects

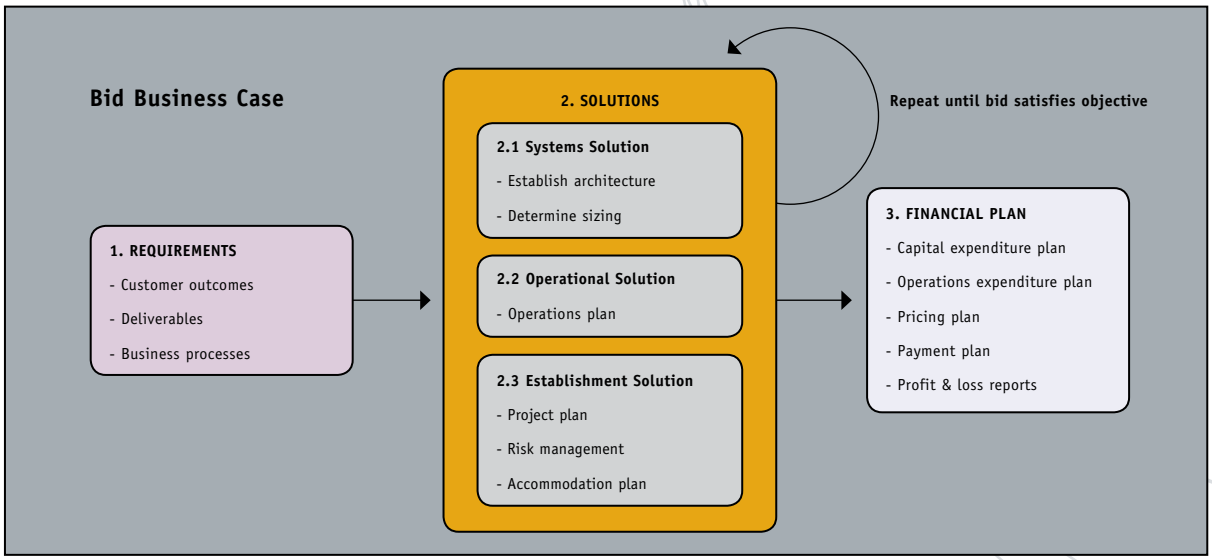
Suppliers have to address a number of vital aspects as part of the procurement process.

- The requirements analysis and mechanisms to resolve ambiguity need to be established.
- Clearly state why the bid is being pursued, and confirm that the organisation has the capability and resources to deliver it.
- Establish a business case for the bid (opportunity qualification) and ensure that the proposed supply is consistent with the business.
- Cost of bidding and internal governance and approval steps need to be established and approved.
- Establish a bid management team that is committed to the supplier's bid process and adheres to it.
- Client relationship model needs to be decided, consistent with the type of supply.
- Solution development is pivotal to the supply and needs to cover all aspects of analysis, design, build, deploy, operate, maintain, and support as necessary.
- Sub-supplier acquisition, contracts and management solution.
- The contract administration needs to manage plans and documentation and keep track of critical dates and triggers.
- Risk management and risk sharing through back-to-back arrangements; assigning the correct ownership of risk and stakeholder value as outlined earlier. Negotiation matters especially in terms of risk acceptance/avoidance.
- Pricing matters with viable relevant options where these exist.
- Confidentiality is paramount - loose lips break deals.

Caravel's bid management methodology



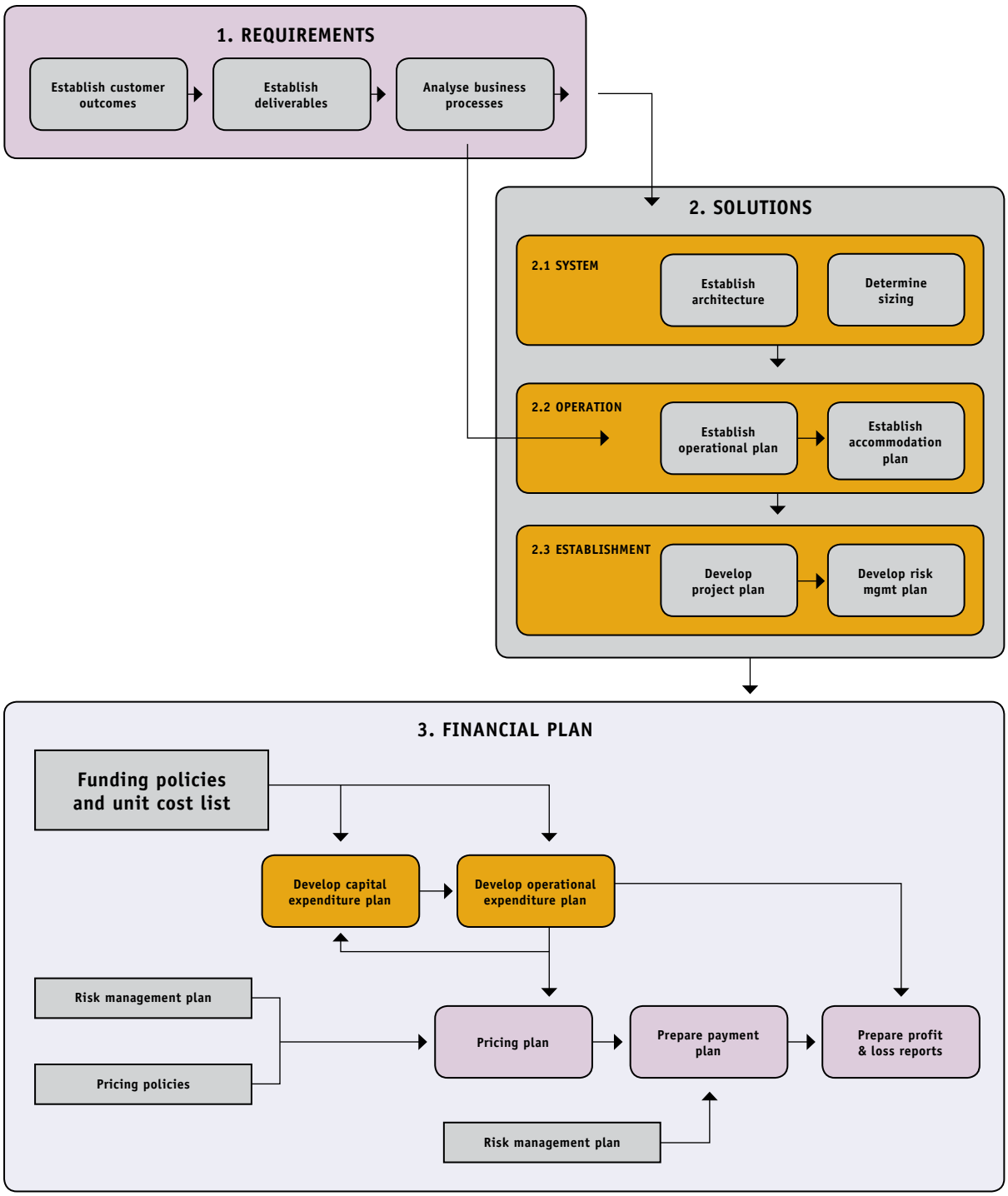
The Caravel bid management approach ensures that bids are constructed logically and with control points targeted at removing unacceptable risk (tendering risk, commercial risk or technical risk) from the bid. The level of acceptable risk will vary from organisation to organisation and from bid to bid.



The development of the bid business case is a key element of the risk reduction process. This ensures that the commercial viability of the bid is thoroughly assessed and approved before delivering the response.

Bid business case process

The bid business case process follows logical steps to build the solution around the business need and to then merge this with the financial costs and funding approaches. The output of this process is a robust business model that can be used for sensitivity analysis and “what if” modelling (particularly around the risk elements of the project).



The profit and loss for the bid will determine the final tendering approach based on the viability of the project. Combined with analyses of the risk using sensitivity analysis or other tools, the bid manager and the bid approval team will be well positioned to make a decision on the viability or otherwise of the proposed bid.

The Caravel approach to procurement projects is driven by the premise of maximising stakeholder value. This applies equally to the procurement or bid management process.

The procurement approach selected has a significant effect on how much value is at risk. If the procurement approach is not considered early in the procurement planning phase this can lead to the potential loss of all value (and in some cases create negative value) at the end of the process. This is readily supported by the fact that 50% of projects still fail to meet their objectives.

Caravel can achieve a 90% success rate on project delivery including procurement projects through the selection of the most appropriate procurement approach.

And since the engagement of Caravel represents a procurement in itself, we welcome the opportunity to demonstrate how we deliver our services at a price and performance level that optimises stakeholder value.

Please refer to our service specification brochures for more options related to the procurement of Caravel's services.

Caravel
LEADING THE WAY IN PROJECTS

Caravel's range of project services

As a leader in projects, Caravel offers a range of specialised consultative and implementation services that span the entire life cycle of a project from inception, through implementation to final hand-over. Caravel adds value at every point along the way through project management services for:

Strategic Management of Projects
Core services include:
- Multi-project Management
- Organisational Resource Management
- Value Management
- Project Feasibility Studies
- Critical Chain Modelling
- Organisational Project Management Maturity Assessment

Project Assurance
Core services include:
- Project Governance
- Project Audits
- Project Health Checks
- Recovering Troubled Projects
- Project Risk Assessments
- Post-implementation Review
- Mentoring and Training

Project Planning and Execution
Change Implementation
Business Process Innovation
Business Partnering
Enterprise Management Solutions

Operational Management Centres
Core services include:
- Customer Contact Centres
- Service Management Centres
- Operational Control Centres
- Mission Critical Moves

Safety Critical Projects
Bid and Tender Management
P³MO™ Project Management Office (PMO)
Security Management Projects

Caravel can tailor a range of industry-specific services to suit the exact needs of your organisation.

Please refer to our website for your nearest Caravel office: www.caravelgroup.com