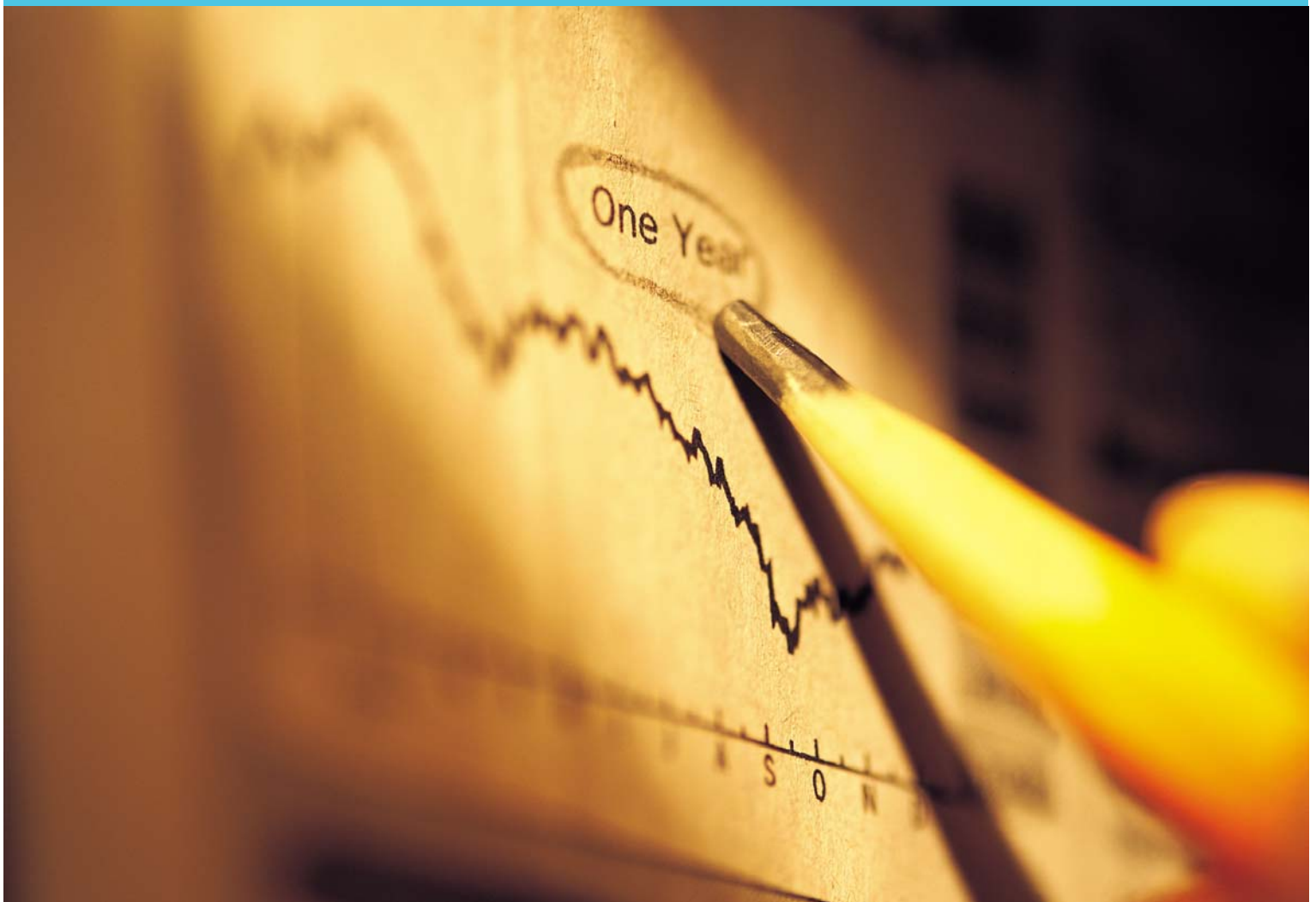# Key Performance Indicators for Responsible Sourcing

A Beyond Monitoring Trends Report

Cody Sisco, Manager, BSR
Blythe Chorn, Associate, BSR

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Responsible sourcing practices have reached an inflection point. Leading companies are evolving their responsible sourcing programs from an approach based on policing compliance to one that goes beyond monitoring to drive continuous improvement through strong supplier management systems and brand-supplier partnerships. Brands are seeking to develop clear goals and metrics aligned around desired supply chain outcomes.

Indicators and metrics are an essential tool for companies to demonstrate the value of responsible sourcing both internally and externally. However, even companies with established compliance approaches, including those that are moving to an approach based on the four Beyond Monitoring pillars (see Figure 1 next page), remain challenged to implement measurement and evaluation systems to track the implementation and impact of their programs. The lack of common standards for evaluating the successes of responsible sourcing threatens to inhibit the further development and wider adoption of responsible sourcing practices.

With support from Novo Nordisk and Beyond Monitoring members, BSR undertook this research study to better understand the current state of responsible sourcing metrics and to identify how measurement and evaluation practices should evolve to better account for the value of responsible sourcing programs.

Key Findings

Our research revealed a number of key findings about existing metrics as well as the systems that impact the processes of goal setting and evaluation:

» **Setting goals and key performance indicators for supply chain sustainability remains a work in progress**

Most brands are focusing on evaluating suppliers and tracking the implementation of their programs.[1] Measurements of benefits to suppliers and value for brands are underdeveloped, and the few companies that are reporting substantively or comprehensively about their responsible sourcing programs focus on qualitative program descriptions and challenges, rather than outcomes or value.[2]

» **Public reporting is still largely focused on the negative**

Although companies are internally moving away from policing suppliers for lack of compliance, most externally reported indicators remain focused on situations of system failure. For example, many brands measure and report numbers of non-compliances by issue and number of contracts terminated. Measures of positive value are underdeveloped.

Project Methodology

BSR conducted an online survey to better understand metrics and indicators in supplier performance and implementation level, brand program implementation, and value for brands and for suppliers.

BSR sent survey invitations to responsible sourcing contacts at corporate members of BSR's Beyond Monitoring Working Group and other companies with 'best practices' in sustainable supply chain management from a variety of industries. In addition, BSR conducted phone interviews to gather company input in lieu of survey responses and to clarify survey responses. A total of 14 companies' responses are included in this analysis.

BSR also conducted interviews with individuals from two investment analysts and two non-governmental organizations that are active on supply chain labor standards. Participants in the research are kept anonymous by their request.

For more information on the Beyond Monitoring Working Group, visit: www.bsr.org/beyond-monitoring

» **Internal uses and audiences for metrics are unclear**

Companies are still in the process of integrating sustainability factors into sourcing processes and decisions internally. As companies experiment with different kinds of balanced scorecards, risk assessments, and rating systems, the types of data needed to inform sourcing decisions continue to evolve. For example, only five of 14 companies reported that they use and are satisfied with their supplier scorecards.

» **Information management and information technology (IT) infrastructure are critical limitations to program measurement**

Most company responses indicated that IT resources were a key barrier. The challenges cited include limited visibility/information kept in silos, limited ability to manipulate and analyze data, and the high cost of improving IT capabilities.

» **NGOs and investors interviewed describe an unsystematic approach to responsible sourcing metrics and the need for transparency into companies' supply chains and processes**

Both the investors and the activists interviewed suggested that the lack of consistent reporting around audit programs and results has hampered analysis and delayed progress in creating more sophisticated program metrics. For example, the investors interviewed are concerned that companies are not sufficiently managing their supply chain responsibility – both from a security of supply standpoint and from a reputation risk management perspective. There is a gap between what investors and NGOs expect and what companies are considering, which indicates more discussion is needed.

Summary of Findings by Metric Category

BSR investigated the metrics and indicators for implementation and value being used in three areas: 1) Evaluation of suppliers' performance and implementation level, 2) Measurement of brands' implementation of responsible sourcing programs and 3) Value of responsible sourcing to brands and suppliers. Table 1 below presents our findings in each of these areas.

Table 1. Key Findings by Metric Category

Evaluation Category	Findings	Sample Metrics
Supplier performance and implementation level	» There is an ongoing transition to evaluate suppliers based on positive measurements of performance and management capability in order to enable planning for continuous improvement (rather than identification of non-compliances). Positive measurements are typically company-specific supplier ratings schemes that use a range of methods, including assigning points (1 to 100), grades (A-B-C-D), or color coded categories (red, yellow, green) based mainly on audits, but sometimes incorporating other criteria, e.g. management systems, participation in training, leadership activities, etc. » Our interviews indicate an increasing focus on evaluation of suppliers' management systems as the key lever for ensuring sustained performance improvements by suppliers, but the criteria for evaluating management systems continue to evolve.	» Average # of days since last assessment » Findings from audits: # of non-conformances identified in assessments by category (ethics, labor, etc.) and by type (excessive working hours) » % of strategic suppliers enrolled in and "placed out" of continuous improvement programs » # of suppliers that participate in training programs

Brand program implementation	» Companies are beginning to set high level goals for responsible sourcing, such as placing a specific percentage of their spend (or volume) with the highest rated suppliers, and companies are working to identify how to cascade these goals throughout sourcing organizations. » Respondents acknowledged that supplier implementation metrics need to become an integral part of sourcing decisions and brand-supplier business relationships. Training of internal business partners is a commonly used indicator of program implementation.	» % of strategic suppliers provided with guidance or other types of intervention » # of procurement and technical staff trained » Correlation of procurement spend and supplier ratings » # of engagements with external stakeholders
Value of responsible sourcing for companies and suppliers	» This category remains a work in progress. Only one company indicated that it measures the value of the responsible sourcing to the business. In this case it is the company's ability to manage responsible sourcing demands on behalf of its customers that comprises the value to the brand—evaluation is based on meeting the customer requirements, rather than an estimation of the program's value to the companies' business.	» % of terminations » # of assessments funded by suppliers or co-funded with other brands » % change per annum in quality complaints and delivery delays » # of suppliers that implement their own new sustainability management systems

Recommendations

We believe next generation supply chain programs will seek transformational results on working conditions and environmental performance by driving toward ambitious goals in a few key areas. In general, BSR recommends that responsible sourcing key performance indicators should have the following characteristics:

» **Focus on Suppliers' Management Capacity as well as Performance**

While strong performance is the ultimate goal, capacity for independent management of social and environmental issues is crucial for suppliers to take ownership of their sustainability progress. Brands should consider establishing a supplier evaluation scheme that balances performance KPIs with indicators of management capacity – for example, comprehensive supplier rating systems that account for both management systems capability and performance across four issue areas of ethics, labor, health and safety and environment as well as commitment, governance and leadership demonstrated by suppliers. (See Table 2 on page 5.)

» **Build Ownership for Indicators and Metrics Throughout Brands**

KPIs are usually designed at a high-level as overarching goals. They need to be designed though so that responsibility for implementation can be assigned throughout the company and accountability is clear. For example, an indicator on the number of suppliers receiving training can be translated into a target for individual procurement staff. Similarly, more micro-level targets that can be rolled up provide a picture of overall performance. Suggested indicators/metrics:

- **Coverage:** set a target to ensure clear goals for which suppliers will be assessed in detail and by when.

- **Data latency:** setting a measure of how recent supplier assessment data is, e.g. by keeping track of how many days since the most recent assessment at each supplier (or for specific categories of supplier, e.g.

Table 2. Components of a supplier sustainability rating system (sample)

Category	Evaluation Component	Possible Score*
Overall	Commitment	10
	Governance	10
	Leadership	10
	Transparency	15
	Responsible sourcing	15
Ethics	Management Systems	5
	Performance	5
Labor	Management Systems	5
	Performance	5
Health & Safety	Management Systems	5
	Performance	5
Environment	Management Systems	5
	Performance	5
Total Possible		100

* Companies can and should put different weights and priorities on different aspects of supplier management capability depending on companies' specific goals. However, the baselines for rating suppliers' management capabilities are standardized in many cases, e.g. SA 8000, ISO 14000, OHSAS 18000. The main challenges are to transition from finding non-compliance to positive evaluation, ensuring credible validation of data, and providing incentives in areas that will drive continuous improvement.

high risk or strategic suppliers) and setting thresholds or targets to trigger assessments and regular buyer-supplier communication.

- **Cost effectiveness:** setting targets for supplier assessments that are co-funded by other brands or paid for by suppliers.
- **Supplier ownership:** setting targets for the number of strategic suppliers that proactively supply third-party verified assessment data. A sub-metric could also include the number of proactive communications from suppliers to buyers to make the company aware of problems and that steps that are being taken to address them.
- **Internal awareness and training:** track awareness among buyers and other staff of responsible sourcing issues, their roles and responsibilities, desired behaviors, and incentives through formalized training and incentive programs.

» **Establish the Value for Suppliers**

Suppliers will be most motivated if they understand the value created by meeting responsible sourcing requirements for their businesses. Value indicators should therefore be designed for external reporting, and brands should ensure that assessment programs capture metrics that quantify the value of improvements that result from their responsible sourcing programs. Suggested indicators/metrics:

- Impact on quantity or terms of business contracts – Number of contracts issued with highly versus poorly rated suppliers; Differences in price, etc. in contracts issued with highly versus poorly rated suppliers.
- Impact on stability and duration of business relationships – Average length of relationships with highly versus poorly rated suppliers.

» **Demonstrate Program Value Externally**

Stakeholders want to understand the processes through which companies meet their responsible sourcing commitments. Moreover, investors in particular are interested in understanding the impact of social and environmental issues on companies' financial performance and the value derived from responsible sourcing. Potential indicators/metrics:

- Total cost of supply measurements – Including transaction cost, on-time delivery, availability/reliability of supply, etc.
- Risk mitigation measurements – Coverage and data latency of assessments for (strategic) suppliers; Measures taken to reduce risk.
- Supply chain efficiency measurements.

Conclusion

It is clear that for responsible sourcing to advance, methods for evaluating the success and impact of supply chain sustainability programs must continue to evolve. In addition to the well understood barriers such as creating internal alignment around the goals and metrics of responsible sourcing, the deficiencies in IT systems are also a substantial challenge. And while the links between suppliers and brands seems to be improving through increasing brand-supplier communication and collaboration, there is a significant disconnect between brands and investors, with a lack of communication around responsible sourcing practices and how these practices impact risk and value, as well as betweeen brands and NGOs, and how practices impact social and environmental outcomes. As responsible sourcing continues to develop, communication and collaboration among these stakeholders, and transparency in collection and analysis of metrics and indicators, will need to advance.