Segmentation

What Is Supplier Segmentation?

Supplier segmentation is the process of categorising suppliers based on their **strategic importance**, **risk**, **spend**, and **relationship value** to the organisation.

It helps determine **how much attention, management effort, and governance** each supplier should receive.

In Contract and Supplier Management (CSM), supplier segmentation ensures that **resources are allocated appropriately** — high-value or high-risk suppliers receive more oversight and collaboration, while low-value suppliers are managed more efficiently.

Why Supplier Segmentation Matters in Contract Management

Benefit	Description
Improved Governance	Helps prioritise contract performance reviews, audits, and renewals.
Risk Mitigation	Identifies critical suppliers where failures could disrupt operations.
Performance Management	Enables differentiated Key Performance Indicators (KPIs) and Service Level Agreements (SLAs), based on supplier tier.
Relationship Management	Supports collaboration and innovation with strategic suppliers.
Efficiency	Prevents over-managing low-value suppliers.

Supplier Segmentation Model - Kraljic Matrix

A Kraljic Matrix is a tool commonly used in procurement teams to segment suppliers based on **supply risk** and **profit impact**:

Quadrant	Example	Contract Management Approach
Strategic (High risk / High impact)	Critical IT	Partnership model, detailed performance reviews, joint development
Leverage (Low risk / High impact)	Major office supplies	Competitive sourcing, standardised SLAs
Bottleneck (High risk / Minimal impact)	Specialised maintenance supplier	Risk mitigation, dual sourcing, contingency planning
Routine (Low risk / Low impact)	Cleaning services	Simplified contracts, efficiency focus

There is a **Kraljic Matrix tool** available for you to use which can be found at the bottom of this page.

How to Implement Supplier Segmentation in Contract Management

Open or close

Step 1: Gather Data

- Spend analysis (annual spend per supplier)
- Risk assessment (financial, operational, reputational)
- Business dependency and strategic relevance
- Contract complexity and length

Step 2: Define Segmentation Criteria

There are tools to support you when performing contract and supplier segmentation e.g. Kraljic Matrix , risk assessment, spend analysis etc.

When defining segmentation criteria, Organisations should consider a combination of financial, operational, risk, and policy-related factors:

Contract Value and Spend Profile

- Total contract value (annual and whole-life cost)

- Spend concentration (single supplier vs multiple suppliers)
- Impact on budget if costs increase or savings are not achieved

Purpose: Supports prioritisation of high-value contracts for enhanced oversight and benchmarking.

Criticality of the Goods or Services

- Impact on statutory duties and public service delivery
- Consequences of service failure or interruption
- Degree of substitutability or availability of alternative suppliers

Purpose: Identifies contracts requiring robust performance and continuity management.

Risk Profile

- Financial stability of the supplier
- Complexity of delivery or reliance on subcontractors
- Health, safety, information security, or safeguarding risks
- Reputational risk to the contracting authority

Purpose: Aligns with risk-based governance and internal control requirements.

Market Conditions and Supply Chain Resilience

- Level of market competition
- Supplier dependency or monopoly positions
- Supply chain fragility or geopolitical risk

Purpose: Informs engagement strategy and contingency planning**.**

Performance and Compliance History

- Delivery against KPIs and service levels
- Contractual compliance and issue frequency
- Responsiveness to improvement actions

Purpose: Enables differentiation between stable suppliers and those requiring closer management.

Policy and Strategic Importance

- Contribution to National Outcomes
- Community Benefits delivery
- Fair Work First compliance
- Climate change, sustainability, and net zero commitments

Purpose: Ensures alignment with Scottish Government policy priorities and Scottish Procurement Policy Notes (SPPNs).

Contract Complexity

- Degree of specification flexibility
- Change frequency and variation levels
- Contract duration and extension options

Purpose: Identifies contracts requiring specialist commercial or legal oversight.

Example dimensions:

- Annual spend
- Business criticality
- Risk exposure
- Performance history
- Innovation potential

Step 3: Classify Suppliers

Use the Kraljic Matrix to assign each supplier to a category (e.g. Strategic, Leverage, Bottleneck and Routine)

Step 4: Tailor Contract Management Activities

Align contract management intensity to supplier category:

- **Strategic:** Ensure effective contract delivery and supplier performance, risk management and maximisation of supplier and market development opportunities.
- **Leverage:** Ensure continuity of supply, value for money, risk management and supplier performance. Seek supplier development where possible. Retain/gain market knowledge
- **Bottleneck:** Ensure continuity of supply, value for money, risk management and supplier performance. Seek supplier development where possible. Retain/gain market knowledge
- **Routine:** Ensure continuity of supply and risk awareness

Step 5: Monitor and Review

- Reassess segmentation twice a year or when major changes occur
- Track supplier performance KPIs and risk indicators

The Kraljic Matrix – Supply Management Positions Template, which can be found at the bottom of the page, allows you to record all CSM activities for each segment. There are some examples pre-populated in this document which can be deleted/amended as required and to suit your organisation.

The output from the Resource Planning Tool can be input into this tool. This document helps you segment your contract portfolio into four categories (Leverage, Strategic, Bottleneck, Routine). This will allow your organisation to record the extent of work involved in managing each category. This includes frequency of performance review meetings and frequency of Management Information, etc.

There is a natural tendency to over-estimate the work required and it is important to avoid this by being as pragmatic as possible. It is worthwhile comparing/collaborating with a similar organisation which has a more mature CSM operation. Especially where an organisation lacks the experienced managerial staff required to make informed judgements. This collaboration will allow your organisation to benefit from the mature organisation's experience You should factor in distortions such as the learning curve they experienced on the journey towards

maturity.

Checklist

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Supplier Segmentation Key Considerations

- Involve **stakeholders** (finance, operations, risk) in segmentation decisions
- Keep segmentation **dynamic** — update as business strategy or as markets evolve
- Use segmentation to inform **contract renewal decisions**
- Avoid segmentation based solely on contract value
- Ensure segmentation does not disadvantage SMEs unfairly
- Use segmentation to **inform management activity**, not to alter contract terms
- Ensure escalation routes are clear for higher-segment contracts

Any documents you need are listed below

Kraljic Matrix Tool

(file type: xlsx)

Kraljic Matrix - Supply Positions Template

(file type: docx)