
APPROACHES TO SPEND ANALYSIS AND
SOURCING WITH IMMEDIATE ROI THAT
NO ONE TOLD YOU ABOUT, UNTIL NOW



Enporion, Inc.

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www.enporion.com

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INTRODUCTION

Do you want to do more for your company in the areas of spend analysis and strategic sourcing? Do you need to demonstrate more immediate ROI on your projects?

If so, you're not alone. According to Aberdeen Group, 38% of companies surveyed indicated that leveraging technology for spend analysis is a top strategy. And spend analysis is the foundation for strategic sourcing.

So, why isn't everyone doing it? Many industry professionals have not had the resources nor the budget to invest in spend analysis and sourcing initiatives without an immediate ROI.

This white paper has been written to give you the knowledge of how to use new and different approaches to spend analysis that will not only make better sense to you, but clearly show ways to reap savings benefits faster and with a lower upfront investment. Specifically, it draws the distinctions between the traditional approach used for spend analysis and strategic sourcing and alternative approaches that **deliver comparable savings in a shorter time**.

Take a look at the various approaches to spend analysis and strategic sourcing described in this white paper and look at the attached checklist to determine if your company is a candidate for any of the alternative strategies. By following the steps provided and starting with a select few of them, you'll be on your way to more efficient and cost effective strategic sourcing that will yield quick and meaningful savings.

Enporion, Inc.
302 Knights Run Ave # 950
Tampa, FL 33602
(813) 864-8144
www.enporion.com

WITH BENEFITS LIKE THESE, CAN YOU AFFORD NOT TO IMPROVE SPEND VISIBILITY AND PROCUREMENT EFFICIENCY THROUGH SPEND ANALYSIS?

Spend analysis is the foundation for strategic sourcing and one of the most proven means to achieve cost savings and procurement efficiencies. The intent of this white paper is to describe solutions that can result in a cost-effective path towards spend visibility and strategic sourcing that will yield significant savings and an immediate ROI.

Empirical evidence clearly demonstrates the many benefits of spend analysis and management, including reductions in material and services cost, inventory costs, decreased sourcing cycle times, and improved contract compliance.

According to Aberdeen’s 2007 Spend Analysis Report, the average savings from sourcing efforts after spend analysis is 11.7% for overall spend, and historical savings from indirect, direct, and other categories are shown in the table on the right. Most companies continue to analyze spend data on a sporadic basis, using labor-intensive and time-consuming procedures. Aberdeen research indicates that such activities account for 12% to 15% of the total sourcing cycle, on average, and constitute 30% to 50% of a typical commodity manager's time.¹ (See table at right.) Using spend analysis, enterprises have experienced a 22% reduction in sourcing cycle times overall.²

Category	Savings Potential from Sourcing
Overall Spend	11.7%
Indirect Spend	11.6%
Direct Spend	10.9%
Chemicals	10% - 15%
MRO	7% - 20%
Computer Hardware and Software	7% - 35%
Office Supplies	14% - 18%

Spend analysis improves the ability to actively monitor contract compliance and maverick spending. Without visibility into spend data, it is difficult to ensure that suppliers provide correct pricing, rebates, and volume discounts. Spend data visibility also allows monitoring to ensure that buyers comply with corporate policies and contractual terms for use of preferred suppliers, pricing, payment, and purchase volume commitments. Spend analysis can also help reduce inventory levels and costs. Aberdeen research found that enterprises have been able to reduce total inventory by 20% to 30%, on average, by consolidating and organizing part and material masters. Such master data rationalization efforts helped these companies trim inventory costs by 5% to 50%.²

IF THE BENEFITS ARE SELF EVIDENT, THEN WHY DOESN'T EVERY COMPANY HAVE A SPEND ANALYSIS AND STRATEGIC SOURCING PROGRAM?

If spend analysis does generate significant cost savings and provide procurement efficiencies, then why did a recent Aberdeen report on spend analysis say that “one-third of enterprises do not have a formal program in place to manage spend analysis for the enterprise?” The majority of the companies that have a spend analysis program use manual tools to collect and analyze spend data. Aberdeen stresses that the top action for spend analysis is to adopt technologies to increase spend visibility, and the type of technology recommended is an enterprise-wide, fully automated solution. This enables industry leaders to realize greater cost savings across different areas of enterprise spend.¹

These findings may suggest to readers that spend analysis is out-of-reach for organizations that can't afford to implement an enterprise-wide spend analysis suite with integration into ERP systems and e-

sourcing systems. Price tags of \$100,000 to more than \$500,000 for spend analysis systems⁴ give readers considering these solutions reasons to delay a decision or even take it off the table permanently.

The cost, lack of knowledge and availability of a scalable and customizable spend tool and sourcing services may be a reason for companies not using or even considering spend analysis. If spend analysis conjures images of time-consuming, labor-intensive projects and large unwieldy spreadsheets and databases, then a company-wide spend analysis program will seem like an insurmountable task.

There is a knowledge gap in most procurement departments when it comes to the range of tools and options available for meeting almost any combination of cost, customization, scale, and deployment parameters. The procurement function like other areas in a company has its share of “fires being fought” to keep the supply chain running smoothly. And it is understandable that capable professionals do not prioritize spend visibility and efficiencies of strategic sourcing. When they do raise the priority of spend visibility and strategic sourcing, their efforts in reviewing available tools and professional services are clouded by more urgent daily activities and lack of time to investigate sufficiently.

Multiple sources of spend data is a particularly difficult obstacle to overcome since studies have shown that many large and mid-size organizations have 5 or more sources of spend data. Also, a significant portion of the spend data is either incorrectly categorized or categorized at an incorrect level for detail to be helpful. Another hurdle to starting spend analysis is the lack of resources, either people with the right skill sets and expertise or the necessary tools for a spend analysis project.

The reality is that no matter what your circumstance or need, there **are** solutions available to reap the rewards and benefits of spend analysis, strategic sourcing, and category management. Now, let’s discuss “Traditional Approach” and the new “Alternative Approach” to gaining benefits.

TRADITIONAL APPROACH TO SPEND ANALYSIS AND STRATEGIC SOURCING

The “Traditional Approach” for spend analysis and strategic sourcing most discussed in trade magazines and articles is a resource and time intensive project spanning the course of several months (at least 6 months). The Traditional Approach usually includes significant investments in a spend tool likely involving IT and systems integration with various ERP systems. The strategic sourcing initiative may be conducted in “waves” or phases that may run anywhere from 3 months to 9 months, depending on the size and complexity of the categories being sourced. When a company chooses to go with external partners for spend analysis technology, teams of consultants, and subject matter experts to supplement company procurement resources, results are delivered over a time span of months and at a significant cost. There is no question that this is a proven methodology. However, from a project management and budget perspective, the project as described is a massive undertaking and it is easy to understand why many companies choose not to embark on such a path even with the knowledge of the potential benefits of spend analysis and strategic sourcing. The milestones along the Traditional Approach roadmap described above can be listed as follows:

- Development of procurement and sourcing strategy and implementation plan;
- Implementation of spend analysis solution;
- Train procurement staff in use of new tools, methodologies and reporting;
- Implementation of new processes or organizational changes;
- Launch of sourcing teams targeting first wave of categories;

- Staggered completion of category sourcing initiatives;
- Change management and post-implementation activities;
- Launch additional waves of sourcing categories, etc.

While the Traditional Approach has been proven to be effective, these results are achieved with significant financial and/or human resource commitment. **Consider this, the goals of a robust and repeatable spend analysis and sourcing process can also be achieved by alternative approaches that get to the same destination in a shorter timeframe with a focus on cost effectiveness and time-to-value.**

ALTERNATIVE APPROACHES: MORE AFFORDABLE AND FASTER ROI SPEND ANALYSIS AND STRATEGIC SOURCING

Advanced spend analysis is critical to understanding the current spend in indirect and direct categories. The following sourcing efforts are the key to developing opportunities into cost savings and process efficiencies. Some cost-effective alternatives available for spend analysis and strategic sourcing include:

ONE-TIME SPEND ASSESSMENT SERVICES

Companies with a one-time need with only a few categories of interest or spend, may not be interested in implementing a software suite. The cost-effective option would be to use a spend assessment as a one-time service using an external service provider that can take a “data dump” from a company’s systems and perform an analysis to deliver the insights needed to source these categories in a short timeframe. These insights include vendor consolidation opportunities, category profiles, spend patterns, etc. Where a category or commodity structure is missing, one can be adapted quickly for a company’s needs. The spend assessment may also include customized reporting for the categories of spend or the company’s focus areas.

ON-GOING SPEND ASSESSMENT, ANALYSIS, AND REPORTING SERVICES

Similar to the “one-time need” case, if your company does not have the resources and/or expertise to implement and conduct on-going spend assessments, a good option is to find an external service provider that can. This solution will be at a fraction of the cost of the software and with little time commitment from in-house resources. Additionally, the assessments will be conducted in a short timeframe that can be customized based on your requirements by spend analysis experts. This approach is also attractive to companies that may want to rely on the external provider while their staff focuses on a different set of priorities. Customized reporting is typically included for the categories and the company’s focus areas.

Spend Tool feature set can drive faster ROI

A major advantage when considering tool features is to get a scalable solution that can be rolled out to small groups and then easily expanded to a large number of users. The ability to get started with a small investment is also consistent with scalability. The benefits of spend analysis need not be “back-end” loaded into a sourcing process. Likewise, ease of use and ability to leverage existing technology platforms and infrastructure are very important. The easier the tool is to use and teach to an extended group of users, the more pervasive its use will be within an organization.

An external service provider can also offer services related to on-going spend analysis in the categories of interest, market intelligence, reporting and analytical services, tracking and monitoring of rebates,

and more. Some of these service providers also happen to provide e-sourcing and e-procurement software solutions and include on-going analysis and reporting as part of the product offering. In other words, there are several avenues available to gain the benefits of these functions in a very cost-effective way without using internal resources that already have a full workload.

OPPORTUNITY ASSESSMENT SERVICES

The quick and cost-effective way to obtain an opportunity assessment on your direct and indirect categories of spend is to use an external service provider who can take your spend data and in a short time develop the opportunity analysis. Using a qualified external service provider will also help you improve your understanding of the savings opportunities because you are leveraging their expertise and market knowledge, as well as that of your own professionals.

LEVERAGING EXISTING CONTRACTS, SOURCED AGREEMENTS, OR GROUP CONTRACTS

Many indirect categories of spend such as Office Supplies, Computers and Peripherals, Safety Supplies, MRO, etc., have limited technical specification requirements. There are service providers that have existing contracts with top suppliers and pricing that reflects a preferred relationship or higher spend base. These are called group contracts or sourced agreements. The transparency in the costs and benefits for joining these contracts makes it an easy decision for the buyer organization. “Piggybacking” on such an existing contract is a very quick way to see immediate savings because these service providers can take your market basket or spend and develop an estimate of savings that will be received by joining the existing contract. The avoided effort of sourcing this spend within the category is an additional bonus. These contracts usually come with associated spend reporting and analysis to monitor and curb maverick spend, as well as providing other process efficiencies.

In addition to providing easy access to savings based on the difference between current prices and negotiated contract pricing, joining an existing contract may also have the added benefit of the category management functions (described below) included with the contract. For smaller companies or for non-core or less critical categories, the included category management function can reduce the resource and time commitment needed to manage the contract and category.

TARGETED CATEGORY SOURCING

Strategic sourcing for direct categories (or indirect categories for that matter) requires the focus of internal procurement resources. This is especially true in the strategy formulation and selection stages for the sourcing process. Internal focus is also critical in the communications and change management (implementation and post-implementation) stages of the sourcing process. External resources can be best leveraged in the “front-end” functions such as spend and market research, as well as in the RFP development, bid analysis, and negotiation phases. **The key to managing the costs associated with the use of professional service providers is in using them in the sourcing process where they are most value-added because of their subject matter expertise in specific categories.**

Category management follows the sourcing effort and some or all of these functions can also be provided by external services providers. Companies should weigh the cost of managing and optimizing spend associated with the sourced categories internally versus the benefits of using external providers.

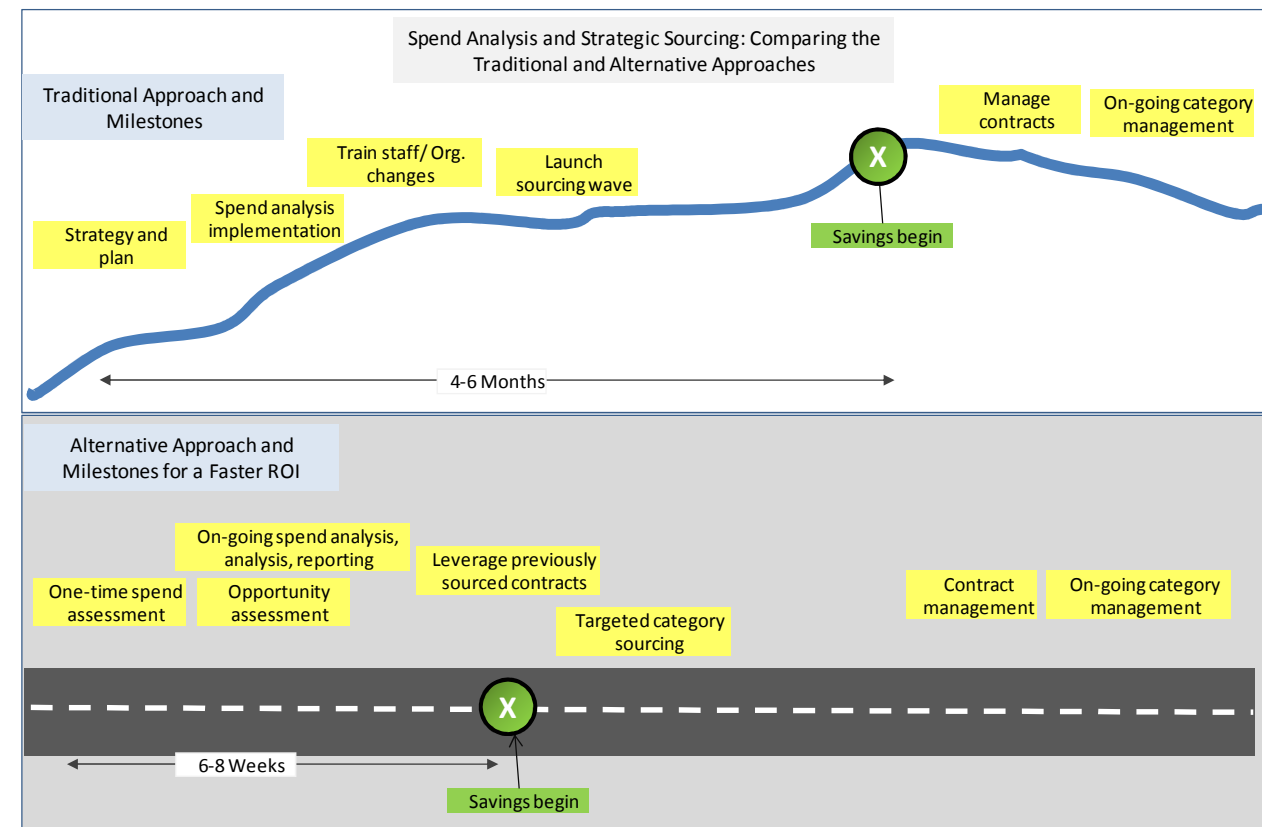
Category management typically includes:

- Raw material and commodity analysis, including tracking of pricing and market conditions;
- Supplier performance measurements, including price accuracy, delivery performance, product quality, and order accuracy;
- Supplier market analysis, including tracking of market conditions and significant news (bankruptcies, strikes, mergers, etc.);
- Risk mitigation planning.

CONTRACT MANAGEMENT

The last phase of a strategic sourcing process includes the contract implementation and embedding changes from the sourcing process. This includes monitoring the terms and conditions of the contractual agreement and tracking rebates, payment terms, escalation clauses, etc. After contracts for materials and services are created, contract compliance management software enables organizations to create, store, edit and manage any type of business contract to ensure transaction compliance for the terms agreed to in those contracts. These tools offer the flexibility of an automated contract assistant to create contracts, based on business processes, or the use of templates for standard agreements. Such software automates and standardizes significant portions of the resource intensive work of crafting contract language, including standard terms and clauses and providing a highly dynamic and flexible central repository that allows for easy storage, retrieval and information management.

Savings are realized much sooner using the Alternative Approaches to Strategic Sourcing



CONCLUSION

Spend analysis is a critical first step in any strategic sourcing initiative and to ensure that you are effectively and efficiently managing your spend on an ongoing basis. If resource and budget concerns are a roadblock to tapping the benefits of spend analysis, strategic sourcing and related processes, especially when thinking of only the Traditional Approach, then this paper described several Alternative Approaches to bypass those challenges. The key reasons a company should consider non-Traditional approaches is to drive faster ROI while reaping the benefits of spend analysis and strategic sourcing as shown in the graphic above. Furthermore, a hybrid approach is also common, where a company chooses some services and processes done in the Traditional Approach and others using alternative approaches. It is important to the elements of a roadmap as described in this paper to reach the goals of cost reductions and process efficiency using highly cost-effective techniques that can be customized for a company's circumstances and environment.

Appendix "A" Checklist: Are you a Candidate for Cost-Effective Solutions?

Cost-effective solutions	You might be a candidate if...
<i>One-time spend assessment using external services provider</i>	<ul style="list-style-type: none"> ✓ Your need is a one-time need, or ✓ You only have a few categories of interest or spend, or ✓ There is an interest and need for customized reporting.
<i>On-going spend assessment using external services provider</i>	<ul style="list-style-type: none"> ✓ You do not have the resources, expertise, or interest to conduct on-going spend assessments, or ✓ Your internal staff is focused on a different set of priorities, or ✓ You have an on-going need for customized spend reporting.
<i>Opportunity assessment utilizing external service provider</i>	<ul style="list-style-type: none"> ✓ You are not sure where to begin to focus your attention, or ✓ You want to leverage the expertise and market knowledge of the service provider for categories where you may have limited market knowledge, or ✓ You want a quick high-level evaluation of potential direct and indirect categories and savings opportunities.
<i>Leverage existing Contracts, sourced agreements, or group contracts from external provider</i>	<ul style="list-style-type: none"> ✓ Your spend is not large enough to obtain the best pricing from suppliers, or ✓ You want to reduce or eliminate the time and effort put forth by your internal staff in sourcing some indirect (or direct) categories of spend, or ✓ You wish to benefit from the category management, on-going analysis, and reporting services that may be included with the sourced contract, or ✓ Your internal staff has limited information or knowledge of the latest pricing, market trends, etc. of certain categories, or ✓ You are interested in quick savings in some non-core categories while your staff focuses on the categories of strategic interest, or ✓ The net cost savings and process efficiencies from joining an existing sourced contract matches or exceeds what you may be able to achieve internally.
<i>Targeted category sourcing services</i>	<ul style="list-style-type: none"> ✓ Internal resources are at a premium and there are other competing priorities, or ✓ You decide to use external service providers in portions of the sourcing process where they are most value-added because of their subject matter expertise, or ✓ Services providers may be able to drive processes such as spend and market research, RFP development, bid analysis and negotiations to completion in a more timely and efficient manner.
<i>Contract management</i>	<ul style="list-style-type: none"> ✓ Your current process for managing contracts is paper-based and inefficient, or ✓ You manually create, store, and edit any type of business contract to ensure transaction compliance for the terms agreed to in those contracts, or ✓ You are interested in the cost-effectiveness and flexibility of having an automated contract assistant to build contracts, based on business processes, or the use of templates for standard agreements, or ✓ You are interested in automation and standardization of significant portions of resource intensive work of crafting contract language, terms and clauses, or ✓ You are want a highly dynamic and flexible central repository allowing easy storage, retrieval and information management.

SOURCES

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2. *Aberdeen Group, Spend Data Management: Unlocking Value Across the Extended Enterprise, November 2003*
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Enporion, Inc.
302 Knights Run Ave # 950
Tampa, FL 33602
(813) 864-8144
www.enporion.com