



Case Study: Understanding the problem.

Do what you do best, let us do the rest.

NaviSource Banking Solution

Procurement Benchmark

Competition, cost, and global pressures are driving a strategic sourcing echo boom among mid-size enterprises.

Mid-size enterprises have prioritized improvements in strategic sourcing competency and systems as a necessity for survival.

Most mid-size firms will need to build sourcing programs from the ground up, starting with standardizing processes, formalizing group structures, hiring key talent, and adopting supporting technology solutions and services.

Aberdeen's procurement benchmark study found that the typical mid-size enterprise applies disciplined sourcing methods to only a third of total spending. Most rely on ineffective, fragmented, and largely manual procedures to analyze spending, negotiate, collaborate, and manage suppliers. Such inadequacies limit the ability of mid-size enterprises to leverage already diminutive spending volumes, assess supply market opportunities and costs, and drive continuous improvements in supply costs and performance. These factors lead Aberdeen to estimate that inadequate sourcing competencies are costing mid-size firms in the U.S. more than \$134 billion in missed supply savings opportunities annually. With global economic instability and inflation on the horizon, improving sourcing competencies will be a necessity for mid-size enterprises.

Recognizing mid-size enterprises' resource and budget constraints, Aberdeen recommends that they employ the following practices to formalize and improve strategic sourcing operations and performance:

- Develop and enforce standard sourcing procedures company-wide;
- Obtain sourcing and commodity expertise, including consultants;
- Improve access, quality, and analysis of corporate spending;
- Enlist executive support for resources and policy changes; and
- Leverage sourcing management automation to reinforce process standards, improve productivity, and increase negotiation and knowledge sharing capabilities

Mid-size enterprises employing these strategic sourcing techniques report more than four times greater procurement cost savings, better supply performance, and greater profitability than industry peers.

Cost Pressures

Factors driving the surge in strategic sourcing among mid-size firms.

Mid-size enterprises report sustained pressure from competitors, customers, and executives to reduce costs.

New regulatory requirements. New regulatory (e.g., Sarbanes Oxley) and executive requirements demand that mid-size companies improve visibility and control of corporate spending and supply chains.

Rising energy and commodities prices. Increases in oil prices alone have added \$400 billion to the cost of doing business over the past year. Energy price increases are beginning to drive inflation for other commodities.

Globalization. Pressures to source from the lowest cost providers demand improved sourcing and supply management skills.

Supply market instability. Rising energy and commodity prices, competing demand from emerging markets, and changing tariffs require mid-size firms to vigilantly source and ensure supply continuity.

Hail Mary: Fourth and Twenty, Ten Seconds on the Clock

CFO "The 'three bids and a cloud of dust' mentality of old will not sustain us in today's global market. We must be more disciplined and knowledgeable in our sourcing methods if we are to achieve savings and to improve, or even sustain, the current cost line."

Evidence is sourcing deficiencies are having a negative impact on mid-size enterprises. The typical mid-size company only applies disciplined sourcing methods to 30% of total spending.

Most mid-size firms lack the process and commodity expertise and supporting organizational and technology infrastructure to transform sourcing operations.

Sourcing deficiencies put mid-size firms at a cost and competitive disadvantage.

Improvement strategies include making sourcing a corporate initiative, hiring procurement leaders and talent, adopting sourcing automation, and using consultants.

Most mid-size enterprises continue to rely on inadequate, fragmented, and largely manual procedures to analyze spending, and negotiate, collaborate, and manage suppliers. Aberdeen's benchmark identified the following hindrances to sourcing effectiveness at most mid-size firms:

Lack of formal sourcing procedures: More than a third of mid-size enterprises lack formal and written strategic sourcing processes that are used consistently across the company. Another third only use disciplined and formal sourcing methods for their most critical or strategic spend categories.

Lack of sourcing and commodity skills: Mid-size enterprises rated the lack of strategic sourcing process expertise among the top challenges to sourcing transformation at their companies. Respondents reported that their companies lack general strategic sourcing principles as well as domain expertise for key spend categories and supply markets.

Insufficient systems infrastructures: More than 80% of mid-market enterprises use a hodgepodge of homegrown sourcing automation "solutions" and offline communications to facilitate negotiations and manage sourcing projects. Most supplier negotiations occur either face-to-face or via e-mail or phone. The homegrown solutions primarily consist of word-processing or spreadsheet-based RFX templates and analytics. Such inadequate and dissociated "systems" limit the feasible number of suppliers evaluated, diminish productivity, elongate sourcing cycles, and stifle knowledge transfer.

Adding to these challenges, mid-size enterprises often lack the spending clout to aggressively negotiate the best pricing and terms with suppliers, making it even more imperative that mid-size firms capitalize on every dollar and advantage. Such inadequate sourcing competencies limit the ability of mid-size enterprises to leverage already diminutive spending volumes, assess supply market opportunities and costs, and drive continuous improvements in supply costs and performance.

Strategic Sourcing: A Necessity for Survival

Strategic sourcing offers the largest and most direct opportunity to address challenges. Aberdeen defines strategic sourcing as the process of identifying, evaluating, negotiating, and configuring the optimal mix of products, sources, and services to support supply chain and other business objectives at the lowest total cost.

When managed effectively, strategic sourcing can dramatically improve cost structures, operational performance, and product quality. It can also shrink time-to-market cycles and improve an enterprise's ability to exploit market changes and respond more efficiently to global customer demand.

While there are a myriad of strategic sourcing approaches, the primary goals are similar:

Select the combination of products, services, and sources that offers the lowest total cost solution. Total cost is the sum of multiple price and non-price factors, such as research, process, quality, delivery, support, billing, reporting and warranty terms. Modeling and understanding the total cost of a supplier, product, or program is fundamental to effective sourcing. Such insights can determine true cost.

Ensure sourcing decisions support supply chain and business objectives. Sourcing decisions made without regard to how they will impact other areas of the enterprise or supply chain are at risk of not achieving intended results, or failing altogether. Sourcing strategies must be aligned with supply chain and business initiatives to ensure sufficient supply to support requirements and optimize cost and performance.

Enhance and institutionalize knowledge and proven sourcing methodologies across the enterprise. To be successful, a strategic sourcing program must incorporate standard procedures and metrics. It must also provide an environment that fosters continuous improvement. Such an environment requires supply management professionals to have timely access to spending, commodity, and market information and to utilize (and continually enhance) standard sourcing methodologies.

Obstacles: Planned Responses to Strategic Sourcing Challenges

While the motivation for strategic sourcing improvements is clear, the roadway to success will be long and arduous. In fact, more than half of mid-size firms are "uncertain how to begin a strategic sourcing initiative," and nearly 40% of benchmark participants lack any formal sourcing or procurement organizations.

Challenges to improvements include internal resistance to standardizing and centralizing sourcing procedures, poor visibility into spending data, and a general lack of strategic sourcing and category management competence within the enterprise. Many mid-size firms also report difficulties in securing sufficient budget and resources to acquire and deploy sourcing automation.

Mid-size firms have prioritized the following strategies to overcome these challenges:

Secure executive support for strategic sourcing and automation investments. Executive authority is the most critical component for a successful strategy.

Recruit a proven procurement executive to lead the development of a strategic sourcing organization and program.

Upskill the procurement team by outsourcing, process, and category expertise.

Mid-size firms are also looking for technical skills and experience with sourcing and procurement automation. These findings echo a previous Aberdeen study, which found that procurement executives planned to add commodity experts and technology managers to their teams. This has proven difficult as deep domain expertise is expensive and quite rare leading to an increased awareness and interest in outsourcing solutions.

Adopt sourcing automation to improve leverage across the enterprise, process standardization, productivity, spend visibility and control.

Use consultants to develop and accelerate competence and programs.

Key Sourcing

Automation will be key to enterprises. procurement transformation plans.

Procurement automation investments have been tactical to date.

Future investments will look to drive more intelligent operations and to leverage and integrate disparate applications.

Adoption plans for mid-size enterprises include:

Greater interest in broader sourcing project management and collaborative and optimization-based negotiation capabilities, rather than the priced-based reverse auctions that fueled the first wave of online sourcing. Part of this motivation can be attributed to the fact that many mid-size firms lack the buying clout to mandate and capitalize on reverse auctions, particularly in tightening supply markets.

Broader adoption of a new shared application delivery model that provides sourcing functionality to multiple clients from a single and centrally hosted application instance. Aberdeen's report, On Demand Supply Management Benchmark found that more than 50% of mid-market firms will deploy sourcing and procurement solutions in this shared mode (a.k.a., On Demand or Software as a Service (SaaS)) within the next 24 months. The study also found that sourcing automation deployed in a shared mode can be implemented within weeks, deliver full payback within six months, and offer solution and maintenance costs half those of installed software.

Prioritization for sourcing application to effectively integrate with execution, and compliance solutions. Having learned from the compliance challenges of early adopters, mid-size firms list the ability to integrate with or deliver contract management and procurement execution (as well as ERP systems) as critical criteria they will use to select their sourcing solution providers.

Increased reliance on third-party consultants to help define strategic sourcing processes and train internal employees on commodity costing models, sourcing automation tactics, and category and supply market assessments.

Procurement as Strategic Partner

Enterprises continue to rely on procurement to reduce costs and ensure supply quality and availability. However, procurement organizations are playing an increasingly important role in creating value for the enterprise in the form of new revenue opportunities, improved profitability, and competitive differentiation.

Globalization, outsourcing, regulatory compliance, and shifting dynamics have advanced procurement as a discipline and a contributor to enterprise value. In addition to cost and supply control, procurement is increasingly playing key roles in market expansion, product innovation, and compliance.

Standardizing procurement procedures and systems, managing supply risk, maintaining top talent, and driving compliance are chief challenges to procurement transformation.

Ninety-percent of executives report that procurement's role in strategic operations has increased dramatically over the past five years. This shift has been accelerated by:

Globalization. Looking to drive more cost-effective, competitive, and global supply chains, enterprises are leveraging procurement to identify low cost and reliable sources of supply from low cost producers.

Outsourcing: With businesses transitioning under performing assets and processes to external partners, the need to devise effective strategies and systems to assess, contract, and govern supply relationships has increased exponentially. Procurement's role in strategic operations has increased dramatically over the past five years, with procurement contributing to market expansion, product innovation, and compliance.

Regulatory compliance. New regulatory mandates for improved financial reporting and controls (e.g., Sarbanes-Oxley Act) have increased requirements for procurement to adopt strategies and systems to improve visibility and control of spending and contractual commitments. Requirements for environmentally responsible products (e.g., RoHS, WEEE) spawned similar demands for procurement to control product content and identify alternative materials and sources.

Procurement automation. Early sourcing and acquisition-to-requisition-to-pay-to-consumption technologies enabled enterprises to leverage competitive negotiation environments and process efficiencies. Automation also extended sourcing and procurement processes to the enterprise and increased visibility and expectations for procurement results.

Changing supply market dynamics: Rising energy and transportation prices and curtailing of supplier inventories and production capacity have elevated the importance of establishing and maintaining stable and efficient supply lines.

Executive Support

It is imperative to enlist executive support for resources and policy changes. Best-in-class performers cited garnering the support of top brass - particularly the CFO and SVP of supply chain - as the leading contributor to their success. Executive support is critical for securing the requisite budget and resources to augment staff and fund sourcing automation investments. Executive backing is also critical to drive mandates and policy changes to ensure business unit support and accountability for strategic sourcing and cost savings, as well as compliance goals and guidelines.

In fact, a recent Aberdeen benchmark of 100 CFOs found that companies with the best-performing procurement operations shared the following attributes:

The finance organization provides dedicated resources to procurement or participates as a core member of sourcing teams.

The companies use formal, preferably multi-year, procurement plans to project, audit, and validate procurement savings.

Financial systems are positioned to complement purchasing applications to improve visibility and compliance.

Increased adoption of procurement automation and increased integration of existing automation investments was a recurring theme among procurement executives. Automation investments were cited as a key component of every major supply management improvement strategy outlined by executives for the next three years. These findings are not surprising. At the tactical level, automation streamlines and removes many of the non-strategic and transactional activities that consume the majority of buyers time, such as order processing, review, and expediting. Automation also allows enterprises to extend procurement processes and intelligence across the enterprise while improving coordination and control of spending and execution. Yet, to date, most procurement automation investments have been tactical in nature, focusing on making existing processes more efficient, such as putting manual requisition-to-pay processes online or using information transparency to create more competitive negotiation environments. These tactical investments were also often disconnected resulting in sub-optimized processes and savings leakage between one application/process area and the next. For example, most e-sourcing users report that their firms have been unable to fully implement savings negotiated online due to insufficient processes and controls to communicate terms and monitor compliance. The lack of a fully integrated solution encompassing early sourcing and acquisition-to-requisition-to-pay-to-consumption technology has, to date, been an impediment to realizing procurement automation potential. To fully implement savings an optimized integration of procurement, requisition, distribution, accounting, project collaboration and asset management is required.

Case Study Enterprises including the Fireman's Fund Insurance Company (FFIC), GlaxoSmithKline, and MetLife are increasingly using automation to extend procurement processes to frontline employees. Each of these companies provides non-procurement personnel a Webbased interface to initiate requests. Category-specific templates guide users through the process of specifying detailed requirements, which are converted into an e- RFX that is either automatically distributed to fulfillment or routed to procurement for further review or action. This requirements gathering process once took weeks; a delay which often led to higher incidences of off-contract (maverick.) buying. These organizations also involve functional and business unit leaders in process evaluation and source selection. Such stakeholder involvement results in greater compliance rates, improved spend and demand visibility, and increased spend under management of the procurement group.

Distinguishing components of full e-sourcing solutions include:

Deep domain expertise for products and services utilizing reverse auction capabilities, and advanced negotiation functionality, including BOM-driven negotiations, multi-line-item negotiations, bundling/unbundling of bids, complex price negotiations, expressive bidding, and internationalization support.

Online requisition capability through a standard web browser, and advanced catalog management.

Integrated distribution that supports advanced receiving capabilities to provide accurate allocation and timely delivery utilizing cyclical processing to reduce freight expenses.

Ability to integrate with multiple accounting systems and support electronic payments, credits, returns and replacements.

Collaboration and project management tools that support cross-functional sourcing and interaction with support and the administration and monitoring of sourcing projects.

Document management and knowledge management functionality that supports sharing and management of sourcing-related documents and schematics and provides a central repository for material, component, part, and market intelligence and supports the management and reuse of sourcing strategies, templates, and process flows.

Asset management for total product life cycle management including product monitoring capabilities to support proactive maintenance or replacement. E-sourcing solution providers are further differentiated by their ability to leverage infrastructure to provide value-added services as business recovery inventory management.

Analytical tools that support spending and cost modeling and analyses. Advanced capabilities include optimization-based analytics to enable massive product aggregation across the enterprise. E-sourcing solution providers are also differentiated by their ability to deliver intelligence on commodities, suppliers, and markets, as well as sourcing expertise, methodologies, and services. Increasingly, providers are augmenting their platforms with spend data classification and analysis, contract compliance, and source/brand performance measurement capabilities.

Center-Led Procurement Organization

In the simplest terms, center-led is organized to leverage enterprise spend, provide centralized sourcing and policies; but allow for decentralized execution at the business unit or region level. When effectively managed this collaborative structure accelerates business unit support, ensures compliance, and drives greater spend under management.

Unfortunately, transitioning to a center-led procurement organization is a challenging proposition. In fact, procurement executives cited company-wide alignment and standardization of procurement procedures and systems as their top challenge. Unless effectively managed, centralizing source-to-pay processes can actually break the process, leading to longer cycle times, increased opportunities for errors, and even higher costs. Centralization efforts often meet resistance from business units and sites that are unwilling to relinquish local supply relationships and process controls. The goal is to establish a balanced organizational alignment that enables the enterprise to realize the benefits of leverage and efficiencies of central and shared processes, resources, and infrastructure while still supporting the unique requirements of each business unit and geographic location. Many procurement leaders have approached this center-led structure by establishing cross-functional sourcing and commodity groups with representation from all geographies, business units, and functions.

Case Study In an attempt to improve its spending leverage and operational efficiencies in the face of rising energy prices, Sun Chemical, began a phased approach to centralizing its procurement organization. With support from its CEO, Sun piloted a centralized procurement organization, targeting a discrete group of materials and spend that were common to multiple divisions. The trial organized commodity leaders from Sun's European divisions into a central team that consolidated spending volumes, adopted lower priced commodity variants, and employed advanced total cost models. The cost and performance savings were so dramatic that Sun moved to establish a central global procurement organization within a year. This new matrixed group includes:

- Global category teams responsible for setting strategy and sourcing each of Sun's 21 spending categories.
- Regional purchasing leaders responsible for implementing and driving compliance with global category contracts within their regions within the context of local requirements and regulatory conditions.
- Supply chain managers responsible for linking supply to sales and operations planning and global warehousing and distribution.

A center of expertise provides a central knowledge base for skills training, supply market research, supplier intelligence, and sourcing methodologies. Procurement executives identified the following strategies for improving the strategic role and effectiveness of procurement:

- Leverage technology to accelerate center-led procurement. Web-based automation empowers an enterprise to extend acquisition-to-requisition-to-pay-to-consumption activities to the desktops of frontline employees while enforcing compliance with standard procedures and contract compliance. Advanced workflow capabilities embedded within these tools can also provide the flexibility to configure unique processes or controls at the divisional or local level. In fact, many enterprises, such as Corning, Inc. and ExxonMobil view automation as a key enabler for transitioning to a center-led organization and enterprise-wide process standardization and controls.
- Establish common goals: To foster procurement transformation and support across business units, procurement leaders have set multi-year commodity plans that are

mapped closely to the financial and performance goals of the business. These plans include details on the organizational structures, services, and commodity strategies; and provide projections for their financial and operational impact. Unfortunately, fewer than half of all procurement organizations use formal, multi-year plans. Instead, most rely on one-year plans. And 16% of companies lack any formal procurement plan at all.

Increase Spend Under Management

Increasing spend under management is a top initiative for procurement executives.

Future efforts will focus on gaining control of complex services spending.

Key strategies for getting more spend under management include improving access and accuracy of spend data, marketing procurements value, securing policy support, improving contract visibility, and leveraging industry benchmarks. A key measure of any procurement organization's success is the amount of total enterprise spend it has under management. Aberdeen defines spend under management as the portion of corporate expenditures that are sourced and controlled by the procurement organization. The advantages of having spend under management is to ensure maximum spending leverage and the application of consistent and best practice market diligence, costing, negotiation, and compliance methods to each spending category. Spend managed outside the procurement group typically results in suboptimal market vetting, and higher prices and management costs.

Findings from the CFOs Agenda corroborated previous Aberdeen benchmarks which found that the average procurement group has about 60% of its company's spend under its direct management. By comparison, best-in-class procurement organizations manage more than 80% of their company's spending, on average. This delta is not insignificant, considering that enterprises have been able to achieve a 5% to 20% cost savings for each new dollar of spend brought under management of the procurement organization.

Considering these factors, it is not surprising that procurement executives have made increasing spend under management one of their top three initiatives. These executives will focus on expanding the volume and breadth of spend under management of the procurement group. Services are viewed as top categories for improvements. These plans echo Aberdeen's ongoing benchmarking of services procurement practices.

Spend categories lending themselves to integrated management through procurement automation.

1. Transportation/logistics
2. Capital equipment/machinery
3. MRO supplies
4. Office equipment & furniture
5. Fleet management & operations
6. IT equipment and software
7. Maintenance services
8. Print services

NaviSource Solutions Group
800-233-5573 x2