Revealing the Secrets of Best-in-Class Procurement Organizations

Denali Group

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INDIRECT SPEND MANAGEMENT
BENCHMARKING STUDY

October 2016
ABOUT THE STUDY

Focused primarily on INDIRECT SPEND in companies across North America.

The purpose is to identify best practices and trends in INDIRECT SPEND MANAGEMENT, as well as to quantify key operational metrics for comparison of participants.

Most metrics and practices were organized along 3 PRIMARY THEMES:

1. VALUE CREATION - Those practices and metrics relating to Indirect Procurement's ability to generate value to the organization.
2. OPERATIONAL EXCELLENCE - Those practices and metrics relating to Procurement's ability to operate an efficient and cost-effective operation relating to Indirect Procurement.
3. STRATEGIES FOR GROWTH - Trends and anticipated changes in the Indirect Procurement landscape going forward.

OVER 50* QUANTITATIVE & QUALITATIVE BENCHMARKS & PRACTICE POINTS WERE EVALUATED.

* Only participants have access to the full range benchmarks.
TABLE OF CONTENTS

ABOUT THE PARTICIPANTS
THE INDIRECT SPEND MANAGEMENT SPACE
CREATING VALUE BENCHMARKS
OPERATIONAL EXCELLENCE BENCHMARKS
FUTURE TRENDS

4
5
8
15
23
ABOUT THE PARTICIPANTS

31 PARTICIPANTS across 9 INDUSTRIES

INDIRECT SPEND
[Averages 15% of revenue]

REVENUE
LOW: $61M
AVERAGE: $2.6B
HIGH: $20.5B

EMPLOYEES
LOW: 1,000
AVERAGE: 17,858
HIGH: 73,000

$10.6B
LOW: $120M
AVERAGE: $75B
HIGH: $10.6B

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Indirect Spend Management Space

For the purposes of this study, Indirect Spend includes:
- Professional Services
- Marketing & Advertising
- Facilities Services
- IT Hardware & Services
- (Top Five) and...
- Utilities
- Travel
- Office/General Supplies
- HR Related Services
- Fleet
- MRO

Historically, Procurement organizations have focused mostly on Direct Spend, leaving much of Indirect Spend to be managed by internal stakeholders.

Now, many companies have Dedicated Teams focused specifically on Indirect Procurement.

Indirect Spend
1. Spend on materials and services that do not go into a company’s finished product.
2. Spend that is purchased for consumption or use by internal stakeholders, as opposed to direct spend, which is ultimately consumed by the external customer.

Trends
1. Spend Increase
Indirect spend is increasing due to increased outsourcing and use of contract resources, which drives more spend into indirect service categories.

2. Focus on Indirect Spend
More companies are focusing on indirect spend than they did 3+ years ago.

3. Procurement Technology
Advances in procurement technology are helping procurement organizations gain control and visibility over indirect spend.
KEY FINDINGS

TOP CATEGORIES OF SPEND include:

- IT HARDWARE & SERVICES
- FACILITIES SERVICES
- CAPITAL GOODS
- PROFESSIONAL SERVICES
- MARKETING & ADVERTISING

$2.6B

The average participant spends $2.6B per year on indirect spend, with 85% actively managed by procurement, utilizing 4,225 suppliers.

INDIRECT PROCUREMENT COSTS (ON AVERAGE)

0.9 cents per INDIRECT DOLLAR spent

ON AVERAGE

PARTICIPANTS SAVED 9% of total indirect spend annually

PARTICIPANTS RETURN 12.3X their cost in savings each year
SPEND DISTRIBUTION BY INDIRECT SPEND CATEGORY

- Professional Services (17%)
- Marketing & Advertising (17%)
- Capital Goods (14%)
- Other (13%)
- Facilities Services (12%)
- IT Hardware & Services (12%)
- MRO (5%)
- Travel (4%)
- HR (2%)
- Logistics (2%)
- Fleet (1%)
- Utilities (<1%)
- Office Supplies & Furniture (<1%)
Creating Value Benchmarks
What Can You Do?

There is a significant correlation between the visibility to spend and adherence to contracts. As spend visibility increases, adherence to contracts increases as well.

In order to increase your return on the cost of procurement, increase the percentage of spend under management, as well as percent of spend that is contract compliant.

Furthermore, communication is critical. Procurement is no longer a simple gatekeeper to purchasing activity. Our experience finds that open discussions with business units explaining procurement policies, available contracts, and prospective benefits of purchasing on-contract enable true compliance.
Despite the increasing amount of outsourcing activities, participants still purchase the majority of indirect materials and services from the North American regions.
Participants realized an average of 9% savings on total indirect spend, 5% of which can be characterized as hard savings.
The top 5 categories for average savings were: IT, Marketing, Facilities, Professional Services, and Fleet.
Participants agreed that Competitive Bidding and Preferred Vendor Policies returned most value in support of Procurement activity.
The top 3 initiatives for creating value included Category Management, Supplier Consolidation and Demand Management.

<table>
<thead>
<tr>
<th>Initiative</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Category management / strategy development</td>
<td>89%</td>
</tr>
<tr>
<td>Supplier consolidation</td>
<td>89%</td>
</tr>
<tr>
<td>Demand management</td>
<td>78%</td>
</tr>
<tr>
<td>Use of total cost method in sourcing projects</td>
<td>78%</td>
</tr>
<tr>
<td>Product standardization</td>
<td>61%</td>
</tr>
<tr>
<td>Value engineering</td>
<td>44%</td>
</tr>
<tr>
<td>Use of artificial intelligence or automation robotics</td>
<td>17%</td>
</tr>
<tr>
<td>Purchasing re-manufactured, refurbished or rebuilt</td>
<td>17%</td>
</tr>
<tr>
<td>Investment in advanced big data analytics</td>
<td>17%</td>
</tr>
<tr>
<td>Use of generic products</td>
<td>6%</td>
</tr>
<tr>
<td>Purchasing products with less packaging</td>
<td>6%</td>
</tr>
</tbody>
</table>
The vast majority of respondents are investing in Spend and Supplier Management tools over the next 1-2 years.
IT, Facilities and General Supplies/Services were the top 3 categories controlled by Procurement

- **74%** - IT Hardware & Services
- **72%** - Facilities Management
- **72%** - General Supplies & Services
- **68%** - MRO
- **68%** - Logistics
- **58%** - Travel Management
- **56%** - Professional Services
- **55%** - Marketing & Advertising
- **53%** - HR Related Services
- **51%** - Fleet
- **49%** - Capital Goods
- **43%** - Utilities

Metric is defined as the Percentage of Spend, by Category, under management. Denali Group defines “Spend Under Management” as spend that is covered by a sourcing plan and routinely sourced, contracted, and controlled.
Active Suppliers per Million Dollars of Indirect Spend

Number of Suppliers with 80% of Indirect Spend

What Can You Do?
Not all metrics are created equal. Pick the top 5 metrics that truly move the needle of supplier management. Define each metric, establish a baseline, and identify targets based on industry benchmarks. Set-up monthly review meetings to track progress and corrective actions.

We recommend assessing metrics such as: Total suppliers; Total active suppliers; Total active suppliers per 1 million dollars of indirect spend; Total suppliers with 80% of indirect spend; and Indirect spend with “strategic suppliers” as a percentage of total spend.
The average managed spend per allocated resource is $70M
What Can You Do?

Implementing an **eProcurement System** is a great way to reduce PO processing costs. Reducing manual touch points will lead to a **reduction in errors and rework**.

Although, it is important to keep in mind that choosing a solution that isn’t a good fit for your organization can lead to low user adoption and increased costs.
45% of respondents currently incorporate a self-serve electronic environment into their procurement operation.

Processes Conducted Electronically:
- **Supplier Payments**: 71%
- **Purchase Order**: 67%
- **Invoices**: 66%
- **Request for Proposal**: 53%

Top Initiatives Respondents use to Improve Procurement Efficiency:
- Providing Training Videos/Tutorials for Technology Systems
- Providing Category Specific Training
- Expanding Use of Technology (eSourcing, eInvoicing & Payments, etc.)
- Centralizing the Procurement Organization
- Linking Separate Technology Systems
- Leveraging External Expertise
OUTSOURCING TRENDS

Our survey found a misconception in differentiating Managed Services and Business Process Outsourcing relationships

Key differences between Managed Services and Business Process outsourcing contracts:

• Managed Services take the responsibility of managing a company's people and processes to minimize operational disruption. Outsourcing contracts typically involve processes being managed by new resources, often in a lower cost environment.

• Traditional outsourcing contracts bill based on completed projects or products while a managed service contract is billed based on meeting key Service Level Agreements (SLAs) ensuring quality of services and/or products.

• Managed services provider typically has a niche of industry-specific knowledge or expertise, allowing the provider to implement improvements to lower a company's operating costs and ensure contract profitability.

Outsourceable processes:
FUTURE GROWTH & PLANS (NEXT 1-2 YEARS)
TRENDS IN FUTURE GROWTH (NEXT 1-2 YEARS)

Changes to Size of Indirect Team

- **37%** Anticipate **no change** to the number of allocated resources supporting indirect procurement.
- **26%** Anticipate a **10-25% increase** to the number of allocated resources supporting indirect procurement.

Changes to Level of Indirect Spend

- **16%** Anticipate a **10-25% decrease** in total indirect spend.
- **47%** Anticipate a **+/− 10% change** in total indirect spend.
- **37%** Anticipate a **10-25% increase** in total indirect spend.

Categories to Increase Management

- Professional Services: **82%**
- IT Hardware & Services: **53%**
- Marketing & Advertising: **47%**
- Facilities Management: **53%**
- HR Services: **47%**
TOP 3 PLANNED INITIATIVES (NEXT 1-2 YEARS)

Team
Implement new changes to the team structure
- Increase collaboration with stakeholders across business units
- Increase collaboration with outsourced counterparts
- Centralize procurement functions (direct and indirect)
- Increase the overall size of the team

Category Management
Enhance level of maturity in relation to category management for indirect materials and services
- Benchmarking
- Reporting & Performance Management
- Contract & Supplier Management

Technology
Invest to improve, and/or implement new purchasing and vendor management platforms
- P2P Platforms
- Supplier Relationship Management
- Spend Analytics
- Contract Management
- General Automation of Processes
TOP 3 CHALLENGES (NEXT 1-2 YEARS)

Demand Management
The top challenge facing organizations is understanding Demand Management
- **Improve forecasts** to reduce the amount of unplanned work
- **Advance notice** to new projects and requirements

Cross-Functional Communication
The second-most significant challenge facing organizations is improving cross-functional communication
- **Improve communication** across business units and facilities to promote higher collaboration and leverage sourcing efforts
- **Educate stakeholders** on the role of Procurement and its effect upon the whole organization

Managing Spend Under Contract
The third most significant challenge facing organizations is managing the breadth and complexities of indirect spend and materials
- **Get indirect spend** under contract and subsequently monitor to ensure against maverick spend
- ** Routinely monitor the tail spend (final 20% of spend)**, especially as contract sizes decrease
EXECUTIVE SUMMARY
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Increasing Importance
Indirect Spend Management is becoming increasingly important to Fortune 1000 companies, due to a combination of factors – Growing indirect spend base, more effective tools & technologies, and increased confidence from stakeholders.

Growing Footprint
New spend categories that were traditionally “sacred cows”, such as Professional Services, HR and Marketing, are now commonly managed by Indirect Procurement organizations.

Innovation
Indirect Procurement organizations are continuing to innovate. Top initiatives planned include greater use of formal category management processes, increased use of technology, and continued organizational centralization & collaboration.

Value
With an average return on investment of 12X their cost, Indirect Procurement organizations are becoming a major value contributor, making it a “no-brainer” for companies to provide a great focus on Indirect Procurement.
If you would like to receive the full range of benchmarks, and participate in this benchmarking study, please contact:

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There is no cost to participate, and participants receive a personalized benchmarking comparison report.
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Session #17

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