Analyse This:

Procurement Metrics That Matter

The Hackett Group
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Principal and Global Procurement Advisory Practice Leader

Zycus
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VP Corporate Development
Evaluation How-to:

Why?

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5. Scroll to Description
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Analyze This:
Procurement Metrics That Matter

Speakers:
Richard Waugh
Zycus Inc.

Chris Sawchuk
The Hackett Group
Comprehensive Source-to-Pay Suite

Zycus Source-to-Pay Solutions

- Financial Savings Management
- Spend Analysis
- Strategic Sourcing
- Contract Management
- Supplier Management
- Requisition Processing
- Catalog Management
- Purchase Order Management
- Invoice Management
10. Net Promoter Score
9. Incremental Revenue from Supplier Innovation
8. % Suppliers Accounting for 80% Total Spend
7. Supply Management Resource Allocation
6. Procurement ROI
5. Realized/Implemented Savings
4. Cost of Procurement as % of Spend
3. Procurement Contract Compliance
2. Spend with Line Item Visibility
1. Spend Under Management
**Total Spend** refers to the cost of direct and indirect materials and services purchased (i.e., disbursements) in the year. Expenditures on taxes, employee base salaries & bonuses, charitable contributions, organizational memberships, dividends, securities, interest payments, and stock repurchases should be excluded from the spend amount. The intent is "Sourceable" spend not just "sourced" spend by procurement professionals.

**Spend Influenced** refers to spend in which Procurement has some influence over or is managed and includes spend that is actually sourced by procurement as well as spend that is purchased within the context of the Procurement policy.

**Spend Covered by Formal & Documented Sourcing Strategies** refers to spend for which documented category plans and goals exist. Category plans can include, but would not be limited to: approach related to geographic sources of supply, business process sourcing decisions, recommendations related to goods and services that require multiple suppliers vs. sole sourcing, and "buy splits" among the targeted supply base to mitigate assurance of supply risks, and recommendation related to alternative sources of supply.

**Spend Sourced by Procurement Professional** refers to spend which the procurement organization led or was involved in the process of supplier selection and pricing.

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**Metric #1: Spend Under Management**

<table>
<thead>
<tr>
<th></th>
<th>World Class</th>
<th>Non-WC</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total Spend</strong></td>
<td>96%</td>
<td>69%</td>
</tr>
<tr>
<td><strong>Spend Influenced</strong></td>
<td>87%</td>
<td>55%</td>
</tr>
<tr>
<td><strong>Spend Covered by Formal &amp; Documented Sourcing Strategies</strong></td>
<td>85%</td>
<td>66%</td>
</tr>
</tbody>
</table>

Hackett Procurement Benchmark, 2014
**Metric #1: Spend Under Management**

**Calculation**
Spend Actively Sourced/Managed by Procurement
Total Purchased Goods and Services - Non-discretionary, e.g. Taxes

**Value**
Measures Procurement Control and influence; Potential Savings Pipeline

**Technology Enabler(s)**
Spend Analysis, eSourcing

**Caveats**
- Spend Under Management Does Not Equal Identified or Realized Savings
- 100% SUM May Not be Attainable or Desirable
- Relevant Benchmarks Vary Widely by Industry

**Selected Industry Benchmarks**

<table>
<thead>
<tr>
<th>Industry</th>
<th>% SUM</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aerospace &amp; Defense</td>
<td>93.00%</td>
</tr>
<tr>
<td>Automotive &amp; Transport</td>
<td>93.08%</td>
</tr>
<tr>
<td>Chemical Manufacturing</td>
<td>77.70%</td>
</tr>
<tr>
<td>Engineering &amp; Construction</td>
<td>85.47%</td>
</tr>
<tr>
<td>Financial Services</td>
<td>63.86%</td>
</tr>
<tr>
<td>Industrial Manufacturing</td>
<td>85.18%</td>
</tr>
<tr>
<td>Metals &amp; Mining</td>
<td>83.61%</td>
</tr>
<tr>
<td>Petroleum</td>
<td>81.66%</td>
</tr>
<tr>
<td>Utilities</td>
<td>67.91%</td>
</tr>
</tbody>
</table>

*Source: 2013 CAPS Research Cross-Industry Benchmarks*
Metric #2: Spend with Line Item Visibility

The ability to view spend data by supplier on a global basis...

...correlates with higher spend cost reductions and more effective supply base rationalization

<table>
<thead>
<tr>
<th>Spend Cost Reduction as a Percent of Spend</th>
<th>Suppliers per Billion of spend</th>
</tr>
</thead>
<tbody>
<tr>
<td>Significant 2.9%</td>
<td>Significant ≈4K</td>
</tr>
<tr>
<td>None/Limited 2.4%</td>
<td>None/Limited ≈6K</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>World-Class</th>
<th>Peer Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>89%</td>
<td>42%</td>
</tr>
<tr>
<td>11%</td>
<td>56%</td>
</tr>
</tbody>
</table>

Significant amount of information available company-wide
Limited amount of information available company-wide
No company level data available

Source: 2013 Hackett Procurement Benchmarking Database

Calculation
Spend Classified at Line Item Level
Total Purchased Goods and Services

Value
Gain Insights for Effective Sourcing

Technology Enabler(s)
Spend Analysis

Caveats
- Must Provide Sufficiently Granular Classification
- 100% Line Item Visibility May Not Be Attainable - or Desirable
**Metric #3: Procurement Contract Compliance**

**Calculation**
Managed Spend on Contract with Approved Supplier
Spend Under Management

**Value**
Monitors Compliant Purchasing

**Technology Enabler(s)**
eSourcing, P2P, Contract Management, Spend Analysis

**Caveats**
- Requires Integrated Suite of Tools
- Must Also Address Supplier Compliance with Pricing/Terms

**Benchmark**

<table>
<thead>
<tr>
<th>Benchmark</th>
<th>Laggards</th>
<th>Average</th>
<th>Best-in-Class</th>
</tr>
</thead>
<tbody>
<tr>
<td>Procurement Contract Compliance</td>
<td>11%</td>
<td>30%</td>
<td>78%</td>
</tr>
</tbody>
</table>

Source: Aberdeen Group
Metric #4  Cost of Procurement as % of Spend

<table>
<thead>
<tr>
<th>Company</th>
<th>Procurement as % Spend 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Acme Inc.</td>
<td>0.90%</td>
</tr>
<tr>
<td>Industrial Mfg.</td>
<td>1.06%</td>
</tr>
<tr>
<td>World Class Hackett</td>
<td>0.60%</td>
</tr>
</tbody>
</table>

**Calculation**
Procurement Labor, Benefits, Outsourcing, and Technology
Total Purchased Goods and Services

**Value**
Tracks Procurement Efficiency

**Technology Enabler(s)**
Spend Analysis

**Caveats**
- Higher Procurement Costs Do Not Equal Higher Savings
- Relevant Benchmarks Vary Widely by Industry

**World-class Procurement Organizations Continue Their Efficiency Gains, But at What Price?**
In 2013, world-class procurement organizations reduced their labor, outsourcing and technology costs by 1.6%; the peer group, by 3.0%. Over the years, cost-reduction efforts have been successful, but these have come at a price. Today, these organizations are running extremely lean – perhaps too lean. World-class procurement’s challenges are compounded by their diminishing ability to reduce spend and avoid purchase costs, down sharply in 2014. This represents a 17.3% decline, returning annual savings levels to only slightly above pre-recession benchmarks.

Source: The Hackett Group, 2014
Poll Question #1

Which of the following statements is most true about your current procurement organization

A. Cost of procurement declining – realized savings declining
B. Cost of procurement declining – realized savings flat or increasing
C. Cost of procurement flat or increasing – realized savings declining
D. Cost of procurement flat or increasing – realized savings flat or increasing
**Metric #5: Realized/Implemented Savings**

**Total Spend Cost Savings**

Total spend cost savings (_reduction and avoidance) as a percent of annual spend

The Hackett Group Procurement Benchmark-2014

<table>
<thead>
<tr>
<th>Year</th>
<th>Non World Class</th>
<th>World Class</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>2.13%</td>
<td>4.94%</td>
</tr>
<tr>
<td>2006</td>
<td>2.73%</td>
<td>5.54%</td>
</tr>
<tr>
<td>2007</td>
<td>2.30%</td>
<td>4.40%</td>
</tr>
<tr>
<td>2008</td>
<td>2.29%</td>
<td>5.25%</td>
</tr>
<tr>
<td>2009</td>
<td>2.00%</td>
<td>4.80%</td>
</tr>
<tr>
<td>2010</td>
<td>3.06%</td>
<td>7.04%</td>
</tr>
<tr>
<td>2011</td>
<td>3.39%</td>
<td>7.68%</td>
</tr>
<tr>
<td>2012</td>
<td>2.19%</td>
<td>7.56%</td>
</tr>
<tr>
<td>2013</td>
<td>2.93%</td>
<td>6.46%</td>
</tr>
<tr>
<td>2014</td>
<td>2.97%</td>
<td>5.34%</td>
</tr>
</tbody>
</table>

**Calculation**

Total Spend Cost Savings (Reduction and Avoidance) / Total Annual Spend

**Value**

Measures Actual P&L Impact of Realized Savings

**Technology Enabler(s)**

Financial Savings Management

**Caveats**

- Savings Definitions Matter: Reduction, Avoidance – Both?
- Actual/Realized Savings Relies on Business Compliance/Finance Validation
- Most Mature Organizations May Experience “Law of Diminishing Returns”
Calculation
Total Spend Savings Implemented
Procurement Labor, Benefits, Outsourcing, and Technology

Value
Justifies Investment in Procurement Organization

Technology Enabler(s)
Financial Savings Management

Caveats
- Only Actual/Implemented Savings Qualify
- Relevant Benchmarks Vary Widely by Industry/Organizational Maturity

Source: The Hackett Group, 2014
### Metric #7: Supply Management Resource Allocation

#### Number of FTEs per US$ billion of spend

- **Peer Group**: 59.5 FTEs
- **World-Class**: 43.6 FTEs

#### Number of procurement FTEs focused on supply risk

- **Top Quartile**: 13 FTEs
- **Median**: 4.5 FTEs
- **Bottom Quartile**: 2 FTEs

**Note:** The results also showed a median of 1.1 FTEs per $1B in spend and 1.2 FTEs per 1,000 suppliers.

**Calculation**

\[
\text{# Procurement FTEs Strategic} \div \text{Total Procurement FTEs}
\]

**Value**

Measure Focus on Highest Value Activities

**Technology Enabler(s)**

Supplier Management

**Caveats**

- Full S2P Process Automation Enables Shift to Strategic
- May Also Require Change of Skill Set Mix
How are your procurement organization resources (FTEs) allocated between strategic and tactical activities?

a) Below 15% Strategic
b) 15-30% Strategic
c) 30 - 50% Strategic
d) 50-70% Strategic
e) 70-85% Strategic
f) Above 85% Strategic
Metric #8 % Suppliers Accounting for 80% Total Spend

Suppliers per Billion Spend

Source: The Hackett Group Procurement Benchmark-2014

Calculation
$1B Spend
Spend per Active Supplier
Value
Measures Supplier Leverage and Collaboration Opportunities

Technology Enabler(s)
Supplier Management, Spend Analysis

Caveats
- Higher Productivity May Not Be Goal, e.g. Target Fewer Not More Strategic Suppliers per FTE
- Calculation Depends on Accuracy of Supplier Master and Spend Data
What is the incremental revenue increase arising from supplier innovation efforts facilitated by Procurement (measured as a percent of total reported enterprise revenue)?

**Calculation**
Revenue Improvement from Supplier Innovation
Total Purchased Goods and Services

**Value**
Quantifies Procurement Delivered value from Supplier Collaboration

**Technology Enabler(s)**
Supplier Management

**Caveats**
- Emerging Metric – Finance Validation Key
- Must Be Able to Document Improvement Attributable to Procurement Involvement

Source: The Hackett Group Procurement Benchmark, 2014
Metric #10 Net Promoter Score

**Calculation**
% of Promoters - % of Detractors

**Value**
Gauges Internal Customer Satisfaction

**Technology Enabler(s)**
Survey Tools

**Caveats**
- Focus on Performance Trend vs. Raw Score
- Root Cause Analysis Needed for Unfavorable Scores
Procurement Operations Dashboard

**COST PROCUREMENT AS % SPEND**

- 1.20%
- 1.06%
- 0.90%
- 0.60%
- 0.60%
- 0.00%

**ACME INC 2013**

- WORLD CLASS HACKETT BENCHMARK 2013
- INDUSTRIAL MFG. CAPS BENCHMARK 2013

**PROCUREMENT OPERATIONS DASHBOARD**

**SAVINGS**

- SAVINGS TARGET FOR 2014
- YTD ACTUAL
- YTD FORECAST

**PROCUREMENT ROI**

- 12.00%
- 10.72%
- 10.00%
- 8.00%
- 6.00%
- 6.73%
- 5.25%
- 4.00%
- 2.00%
- 0.00%

**ACME INC 2013**

- WORLD CLASS HACKETT BENCHMARK 2013
- MFG. CAPS BENCHMARK 2013

**NET PROMOTER SCORE**

- DETRACTORS
- PASSIVE
- PROMOTERS

**NET PROMOTER SCORE = % OF PROMOTERS - % OF DETRACTORS**
Supplier Management Dashboard

Procurement Resource Allocation

- Strategic: 44%
- Operational: 40%

CAPS Industrial Mfg. Benchmark 2013

ACME Inc. 2014

Supplier Innovation

- Centro Inc: 20
- Flowcontrol: 37.5
- SMC Pneumatics: 62.5
- Tri-State Valve: 62.5

Average of Key Performance Indicator (KPI) Score

Suppliers Accounting for 80% of Total Spend

Spend Split in % & Savings Potential

- Savings Potential %
- Spend With Remaining Suppliers
- Spend With Top 20 Suppliers

Savings Potential:

- Paint: 55%
- Plasticize: 57%
- Inorganic: 75%
- Petroleum: 70%
- Packaging: 58%
Poll Question #3

Which of the Following is the #1 Metric That Matters Most to Your Organization?

a) % Suppliers Accounting for 80% Total Spend
b) Cost of Procurement as % of Spend
c) Incremental Revenue from Supplier Innovation
d) Net Promoter Score
e) Procurement Contract Compliance
f) Procurement ROI
g) Realized/Implemented Savings
h) Spend Under Management
i) Spend with Line Item Visibility
j) Supply Management Resource Allocation
analyze this.
by richard waugh

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analytics + insight = procurement performance

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✓ All F&B, Cocktails
✓ Entertainment & Evening Beach Party
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Session #WS08

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Today's Presenters

Richard Waugh  
VP Corporate Development  
Zycus Inc.

Richard has an extensive background in B2B E-Commerce. He helped launch GE's Trading Process Network (TPN), the first on-line Marketplace for Sourcing and Procurement. He was also Co-Founder of B2eMarkets, one of the first SaaS (Software as a Service) Sourcing Suite providers and later covered the Supply Management market as an Industry Analyst for the Aberdeen Group.

Chris Sawchuk  
Principal & Global Procurement Advisory Practice Leader  
The Hackett Group

Chris Sawchuk has over 17 years of experience in supply management, working directly with Fortune 500 and midsized firms around the globe and in a variety of industries to improve all aspects of procurement, including process redesign, technology enablement, operations strategy planning, organizational change and strategic sourcing. He is a regular contributor to business publications, a frequent presenter at industry events, and co-author of ePurchasingPlus. He has been recognized by Supply & Demand Chain Executive magazine as one of its “Pros to Know.”
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