Creating a Culture of Spend Optimization

While organizations continue to focus on increasing their sales coverage and focus on top-line revenue, procurement still lacks a champion to push its strategic importance. Aberdeen's August 2011 report, Dynamic Procurement: The CPO as Collaborator, Innovator and Strategist notes that 67% of survey respondents point to communication as the most important competency for CPOs and procurement organizations today. Understanding how to communicate procurement’s value, both in an active and passive way, is critical to establishing an organizational culture that can embrace it. Through Aberdeen research, this Analyst Insight looks at what steps CPOs and other procurement leaders must take to create a culture that can go beyond a traditional approach of spend management to spend optimization.

Spend Management versus Spend Optimization

In the past decade, spend management has been the traditional approach that most CPOs and procurement organizations have adopted for improving spend processes. The concept of spend management is one that evolved from a technology perspective when it was realized that purchasing as an organization required a separate and unique set of tools that could set it apart for improving efficiency and gaining deeper insight into spend. Today spend management has expanded into other areas of the supply chain, but its foundation is still focused on controlling spend related to operating costs or Selling, General and Administrative (SGA). It is also evident that the "spend management" concept has taken root across process and technology but lacks in its ability to promote procurement into a strategic role within the organization.

Based on discussions with solution providers and end-users alike, Aberdeen has observed that a trend or evolution of spend management has developed that can be coined as a new concept called “spend optimization.” What makes it different is that spend optimization begins where spend management ends. In other words, where spend management has been focused on improving the performance of the procurement function, spend optimization looks to expand the culture of savings to the rest of the organization through a combination of people, process and technology.

Keeping this expanded concept in mind, this Analyst Insight looks for evidence based on Aberdeen research that points to the current challenges CPOs face in taking a traditional spend management and describes ways for accelerating a transition towards spend optimization.
Changing the Perception of Spend vs. Reality

Aberdeen research consistently reveals that the top pressures related to procurement puts cutting costs at the top of the CPO's agenda. Of course from a spend management perspective procurement’s *modus operandi* is focused on reducing cost and its value is based on how well an organization can source, acquire and pay for goods and services. However as part of the goal of establishing an organization that seeks a spend optimization approach, few organizations have bought into the idea that procurement can become strategic in its ability to identify new revenue or profit opportunities.

Figure 1: Procurement’s Contribution to the Wider Organization

For example, Figure 1 shows 71% of respondents from Aberdeen’s September 2010 report, *From Preservation to Prosperity: The CPO’s Agenda for a New Decade*, indicate that regular achievement of savings targets are procurement’s main contribution to the organization. Survey respondents were also 2.3 times more likely to note the regular achievement of savings targets as procurement’s main contribution to the organization, over the identification of new revenue opportunities.

To get noticed as an agent of change, procurement organizations starting with the CPO need to charter a message beyond a cost centric mindset to one that translates procurement’s contribution as a profit center. To do this CPOs must also develop the ability to become an agent for a frugal culture while finding ways to promote spend optimization within the organization.

Changing Executive Leadership’s Perception

As part of this charter, CPOs also need to involve their superiors. Based on Aberdeen research, executive leadership plays a key role in making this transformation happen and establishing the buy-in that procurement’s value
Creating a Culture of Spend Optimization

is real especially since the CPO does not always have the direct ear of the CEO. For instance, Aberdeen research has found that most organizations today are increasingly aware of the CPO’s role in impacting operational effectiveness. As demonstrated in the *Dynamic Procurement: The CPO as Collaborator, Innovator and Strategist* report, when asked to rank the importance of support for the CPO, 29% considered the CPO role strategic while 36% considered the role very strategic.

**Figure 2: Direct Reporting Relationship of the CPO**

![Diagram showing reporting relationships]

Yet 52% of these same respondents indicated it was critical for the CPO to have support from the executive office for success. In other words, the CPO cannot promote optimization alone given the reporting relationships found in most organizations. Aberdeen's *Dynamic Procurement* report also found that a majority of CPOs report to either the CFO (25%) or the COO (29%) and only 17% reported to the CEO. Thus Figure 2 makes it obvious that for most organizations, procurement leadership reports directly to a C-level executive role rather than having their own seat at the proverbial table. As a result, spend optimization can only become a reality if those in the executive office are willing to help promote the concept.

**Changing Procurement from Within**

Similar to the idea of spend management, the transformation to spend optimization must also begin within the procurement organization itself. To take on the task CPOs need to also help prepare their team with the right tools and knowledge that can help translate the value of procurement to peers such as finance, HR, IT, and the supply chain.

However, many procurement organizations today are ill-equipped in their own ability to meet this challenge from the top down. Aberdeen research in *Dynamic Procurement* identified that the top barrier for a procurement organization to better align the procurement strategy with organizational objectives is the lack of appropriate skills or knowledge, as noted by 47% of

“We had no procurement systems. We had no procurement process. Literally, when people wanted to buy things, they would write it on a napkin from lunch, a piece of paper from the printer and drop it off to the accounts payable person and say “Would you please buy this and make sure it gets paid?” And that’s clearly not a sustainable process for a fast, rapidly growing company, so I took the opportunity at that point in time to go look for procurement solutions that would help us add some process, make it easy to use for our particular customers – meaning, the rest of the departments.”

~ CFO, Pandora Media

Source: Aberdeen Group, August 2011
respondents. Moreover, the top two staffing challenges for the procurement organization was the need for people with different job skills (64%) and the need for people with a more formal education (41%).

Figure 3: Formal Training in the Procurement Organization

Looking at the perspective of the skills that are lacking, Figure 3 demonstrates some of the widest gaps between Best-in-Class and all other organizations. The figure shows Best-in-Class organizations are ahead of their peers in traditional procurement areas, such as understanding the importance of commodity/category and the ability to work with legal contracts. Yet even Best-in-Class organizations demonstrate a need to increase training in areas that relate to the wider business functions such as finance, product development and sales.

To develop the right procurement team, Aberdeen research suggests recruiting new talent focused on broader business backgrounds gained through formal education (i.e. MBA, CPA). Finding talent outside of procurement will assist the procurement team’s efforts to broaden skill sets for better understanding the needs of the wider organization and developing the right message to cater to them based on this knowledge. Developing a wider range of skills outside of procurement also encourages and improves cross-functional coordination. This coordination is required between the procurement organization and other teams being led by the executive core by being able to speak the same language (e.g. Finance, Supply Chain, HR, Product Development, etc.). Dynamic Procurement identified that 75% of Best-in-Class organizations demonstrate this capability compared to 59% for all other organization.

Focusing on Center-Led Procurement

Another key step in spend optimization is having the CPO attempt to centralize control of policies and procedures that can be a challenge based
on the history of the organization. Whether through mergers or acquisitions, organizations often inherit separate procurement cultures that do not share a common core culture. Many purchasing organizations are also unable to create a consistent flow for procurement decisions or processes paramount for achieving spend optimization. For instance according to the November 2010 Aberdeen report, *Effective E-procurement: Assessing Options for the New Economic Normal*, a little more than half (53%) of organizations using a decentralized model can demonstrate standardized procurement processes such as the need to purchase and requisition approval, compared to 80% of the Best-in-Class. Furthermore, CPOs may even be fighting an uphill battle with business units demonstrating a higher likelihood to have their own objectives achieved locally. *Dynamic Procurement* found that only 8% of Best-in-Class companies use some type of decentralized model, compared to 25% for all other organizations.

In comparison to a decentralized model, centralized procurement can promote greater efficiency for establishing procedures and can prevent such dysfunctions. However, even complete centralization is not always practical or desirable. For example, central purchasing organizations may lack the knowledge of local supply markets and consumption patterns and prevent the identification and realization of savings opportunities.

**Figure 4: Organizational Approaches for Procurement**

Due to these challenges in both decentralized and centralized approaches, many leading organizations have adopted a hybrid model known as "center-led." Reasons for this are based on the flexibility it provides. Data collected in the *Dynamic Procurement* report shows Best-in-Class organizations are pointing to the center-led model as a differentiator from their peers in its ability to quickly integrate acquisitions and more readily bring distributed locations under management. Moreover in a typical "center-led model," areas like sourcing and buying power are managed from the top down.

**Best-in-Class Definition**

For the report, *Effective E-procurement: Assessing Options for the New Economic Normal*, the Best-in-Class were determined using the following metrics:

- Days to On-Board a New Supplier for Goods
- Days to On-Board a new supplier for Services
- Purchase Orders compliant with Existing Contracts

"To get users to actually use the e-procurement tool I think we would have to use some sort of mandate just to get them to test the system. We're currently live on our corporate campus and we're about to go live in a bunch of plants all over the world so we don't have it everywhere yet and we're still trying to decide how we want to push it out. But the thing is that as soon as they actually get into the system they tend to love it. It's not something that's non-user friendly or anything like that, it's just that change is bad and change is scary which prevents people from wanting to do it. And if we say, this change is coming and you need to be a part of it and they test it out and they realize love it and everyone we've shown it to loves it – they just have to see the system."

~ Chief e-Procurement Administrator, Armstrong
through the establishment of centers of excellence. Execution of transaction
intensive activities such as the issuance of purchase orders and invoice
processing are done at the local levels. Based on the benefits, it is clear that
reaching the goal of spend optimization favors a center-led approach to
procurement by providing an easier way to manage disparate locations while
providing the freedom and flexibility of procurement staff to make
purchasing decisions based on local knowledge and regional requirements.

**Evangelizing the Use of E-procurement to End Users**

Broadening the reach of procurement through the CPO, executives, and
wider organizational support are all necessary steps for creating a culture of
spend optimization. However to ultimately translate it into process and
make the message stick, organizations must also adopt the right
technologies to make it a reality. Technology in the form of e-procurement
can have an enormous impact on the procurement transformation to a
strategic function. But hinting at the movie *Field of Dreams*, if you built it, will
they come?

Since the interaction with procurement for most users comes in the form of
technology and not from the CPO, the e-procurement platform becomes
the main channel for communicating procurement’s values and culture.
Furthermore based on global consumer access to recognized consumer
storefronts (i.e. Amazon) and search engines (i.e. Google) combined with
the dissemination of smart phones and tablets, end-users of enterprise
technology are increasingly expecting these same elements at the
workplace. What this suggests is that while past spend management
approaches deploy e-procurement technologies for improving procurement
process, it often stops short of empowering the end-users to embrace the
solution and the optimization concept as their own.

Moreover with the evolution of technology in the cloud framework in
multiple realms, technology today demonstrates that ease of use, anywhere
access and cost effective approaches are all becoming the norm from what
is expected from any form of enterprise technology, and thus must be
considered as part of a core strategy being promoted by procurement
leadership. Therefore when end-users do not understand process or
procedure and/or are reluctant to use e-procurement systems designed for
them to purchase products and services, the end result is a lack of adoption.
This defeats the purpose of the technology investment while negating any
efforts of promoting spend optimization. This is why using the right e-
procurement tool is so critical to changing the organizational mindset of
procurement.
Figure 6: Challenges to Adopting E-procurement

Along these lines Figure 6 demonstrates the top four areas that were most often stated as barriers to using the eProcurement system in the organization. Taken from the data collected from the Aberdeen report, *Effective Procurement* (2010), the top barrier preventing use of eProcurement was user knowledge of system capabilities at 34%, closely followed by system and process alignment at 32% of responding companies.

Furthermore, establishing consistency for business users begins with introducing new processes in the form of the e-procurement initiative. To be successful, end-users must be involved early and frequently be appraised of the goals of the e-procurement system. Doing so prevents alienation of business needs, prevents distrust of the new system and improves procurement policy compliance by closing the backdoor. As a result of such actions, leading procurement organizations demonstrate higher rates of spend under management and reduced rates of maverick spend. For instance in the *Effective Procurement* study, it was found that Best-in-Class averaged 74% spend under management compared to 63% for all others and for off-contract or maverick spend at 14% compared to 23% for all others.

"Our top priority for the procurement organization in 2012 is to ensure business continuity and manage compliance requirements."
~ VP Director of Operations, Global Semiconductor Manufacturer

"If I could change one thing about the procurement organization it would be choosing more educated and experienced staff."
~ Procurement Manager, Iron Ore Pellet Processing/Manufacture
In comparing the Best-in-Class to their peers, the capability gap also shows how the former are more likely to have implemented policies and procedures that prevent the alienation of the end-user base. Figure 7 shows the largest difference in organizational capabilities between Best-in-Class and all other organizations is in the ability to institute measures for adherence to internal policies (67% v. 49%) and the use of established guides to processes for training/onboarding new users of procurement systems (63% v. 41%). The Best-in-Class were also 57% more likely to have consolidated all e-procurement under a common platform, further increasing the chances of user participation while sending a more concise message for improving adoption and for creating an organization that optimizes spend.

**Recommendations**

Aberdeen research referenced in this Analyst Insight makes it apparent that to get noticed as an agent of change in their own rite, procurement leaders must find a way to transform an organization’s DNA and cultural mindset on a number of different levels that include people, process, and technology based approaches. The following are the dynamic approaches recommended for establishing a culture that embraces spend optimization:

- **Be profit-center minded.** Procurement organizations needs to promote the notion that procurement is a value-add to the organization and profit center oriented. For instance, procurement leadership should develop a “what if” scenarios report that can demonstrate procurement’s impact on net income and illustrate how it would have been lower without procurement’s involvement. Showing these types of examples assists in promoting the benefits of procurement and reasons why spend needs to be optimized.

- **Always on the mind of the executive.** Executives need to buy into procurement’s vision of success. This provides two functions: 1. It allows these executives to communicate procurement’s value to their teams and 2. Procurement’s vision of spend optimization is more visible at the executive level.

"Our top priority for the procurement organization in 2012 is to provide a competitive advantage to our company by enhancing business relationships with our partners in order to receive the best quality services that optimizes our spend."

~ Director of Procurement, International Air Transport Assoc.
• **Talent oriented and focused.** Procurement must do a better job at recruiting and marketing the best talent. While traditionally procurement may have been seen as a stepping stone to another function in the past, today procurement is increasingly becoming a desired function by its impact on the commercial viability of an organization. And since procurement touches so many diverse areas such as HR, tax, legal, finance, IT, procurement leaders should recruit from these areas internally to build a stronger organization.

• **Organized through a center-led approach.** Structural deficits in the way procurement has traditionally been organized has often impeded and effort that could create a common culture for understanding its value. Focus should be made on establishing a center-led model based on the ability to promote consistent policy while instilling flexibility of some self-determination at the local level.

• **Leading through innovation and technology.** While organizations too often rely on technology as the panacea to solve organizational issues, technology is the necessary glue that can help centralize procurement processes and close the loop for gaining visibility, increasing spend efficiency and amplifying spend power within the organization. Furthermore technology needs to represent the here and now for end users to want to adopt its use. How this process is executed is critical to the success of a culture that embraces procurement rather than ignores it.

For more information on this or other research topics, please visit www.aberdeen.com.

---

### Related Research

<table>
<thead>
<tr>
<th>Dynamic Procurement: The CPO as Collaborator, Innovator and Strategist</th>
<th>Effective eProcurement: Assessing Options for the &quot;New Economic Normal&quot;</th>
</tr>
</thead>
<tbody>
<tr>
<td>August 2011</td>
<td>November 2010</td>
</tr>
<tr>
<td>The Year of the Supplier: Perspectives on Supplier Management; April 2011</td>
<td>From Preservation to Prosperity: The CPO's Agenda for the New Decade; September 2010</td>
</tr>
<tr>
<td>The State of Strategic Sourcing; March 2011</td>
<td>Spend Analysis: Transforming Data into Value; September 2009</td>
</tr>
<tr>
<td>Bridging the eProcurement Gap through Contract Management; March 2011</td>
<td>The CPO's Agenda 2009: Smart Strategies for Tough Times; April 2009</td>
</tr>
</tbody>
</table>

**Author:** Constantine Limberakis, Senior Research Analyst

Aberdeen Group - Global Supply Management

Email: constantine.limberakis@aberdeen.com | Twitter: @ABG_SpendMngmt

For more than two decades, Aberdeen’s research has been helping corporations worldwide become Best-in-Class. Having benchmarked the performance of more than 644,000 companies, Aberdeen is uniquely positioned to provide organizations with the facts that matter — the facts that enable companies to get ahead and drive results. That's why our research is relied on by more than 2.5 million readers in over 40 countries, 90% of the Fortune 1,000, and 93% of the Technology 500. As a Harte-Hanks Company, Aberdeen’s research provides insight and analysis to the Harte-Hanks community of local, regional, national and international marketing executives. Combined, we help our customers leverage the power of insight to deliver innovative multichannel marketing programs that drive business-changing results. For additional information, visit Aberdeen http://www.aberdeen.com or call (617) 854-5200, or to learn more about Harte-Hanks, call (800) 456-9748 or go to http://www.harte-hanks.com. This document is the result of primary research performed by Aberdeen Group. Aberdeen Group's methodologies provide for objective fact-based research and represent the best analysis available at the time of publication. Unless otherwise noted, the entire contents of this publication are copyrighted by Aberdeen Group, Inc. and may not be reproduced, distributed, archived, or transmitted in any form or by any means without prior written consent by Aberdeen Group, Inc. (2012a)