



Advancing • Procurement • Performance

Thoughts

Procurement Performance Management

A perspective to advancing spend analysis solutions

By Fabrice Saporito, CEO, Sievo



Procurement is the art and science that orchestrates cross functional decisions in relation to organization's external purchases with the ultimate objective to increase overall value. This definition of the procurement discipline may not be too widespread, but gone are the days when purchasing professionals were primarily considered as "paper pushers". What is also certain is that many organizations would agree that this definition may well be their ultimate goal.

By examining this definition closely one will identify a number of traits that they may have yet to observe in their own organization. The artistic connotation comes to balance the more analytical characteristics of the function for its role of cross- functional orchestrator. Being at the centre of a cross functional dilemma does require more than just analytical skills to support a decision; true change management and leadership capabilities are necessary and are easier to associate with art than hard core mathematics. The definition of orchestrator also stresses the fact that purchasing does not decide but rather gets everyone converging towards an optimal choice that will benefit the company as a whole. What this also suggests, is that purchasing ought to ensure optimal trade- offs between such parameters as cost, quality and risks which will eventually result in greater shareholder value.

By observing that most organizations are not quite there and to establish a path towards such aspiration requires taking stock of the current state of purchasing. By reading the literature and assessing trends discussed within practitioners, procurement seems very much to be focused on finding ways to create more savings for their organizations to better face today's economic realities. So managing their spend is very much where they are and getting a better understanding of what is being bought is very much the focus.

Managing complexity

Cyrus F. Freidheim, Jr., former Vice Chairman with management consulting firm Booz Allen & Hamilton, wrote back in 1998 a book called "The Trillion Dollar Enterprise". In his book he argues that companies will eventually reach gigantic sizes by leveraging all forms of structural and collaborative approaches and in doing so transform the way business is conducted. What was considered as foresight at the time is now a reality as companies operate more and more globally with operations spreading multiple continents evolving dynamically in ever more complex ecosystems. Supply chains are global and understanding what is bought by who at what price and where, is often the first step to take spend under proper management.

Add to this picture the structural changes that companies are undergoing through divestments and acquisitions and you will very quickly realize that taking spend under management is a true moving target that requires great agility. And whilst ERP system and data warehouses are very powerful, they require extensive efforts to quickly identify and capture synergies that M&A activities often promise at the onset of the deal.

Spend Analysis solutions have offered a specific answer to this problem by allowing companies to quickly consolidate spend data from multiple sources and offering a very accurate picture of external purchases in record time. By leveraging artificial intelligence vendors in the space claim the ability to offer continuous automated classification of companies spend with the most complex systems landscapes. Their value proposition is to eliminate the efforts of extensive baseline exercises generally undertaken by management consultants and purchasing managers at a fraction of the cost and to help companies save a lot of money. The offer seems indeed very attractive and with such proposition they have very quickly become an essential component of





the purchasing toolkit.

The devil is in the detail

Armed with their new tool, the purchasing community got however somewhat distracted and lost track of the ultimate objective they were mandated for: namely creating value for the organization as a whole. But “the devil is in the details”; and indeed the more you get into the details, the more you lose sight of the big picture making the exercise more of a transactional mission than a truly strategic. Spend analysis is about analysis and analysis is the essential tool for strategy formulation from where tactics and transactions are eventually derived. So how did this happen?

Our own assessment would like to suggest that the power of technology has been abused to blinding the organization from the essential. Fully automated spend classification is in theory a wonderful advantage limiting requirement for human intervention, but in doing so it also prevents companies from identifying non compliance and strategic divergences at the source. And therefore we would rather advocate a semi- automated approach that alerts procurement professionals when the issues arise, offering them the opportunity to solve the issues prior damages are done as opposed to discovering non compliance post event.

Strategy is also about focusing on what matters and as such aiming at classifying more than 80% of the spend at the lowest levels of details may further distract the limited resources purchasing has available for orchestrating cross functional programs. And although such an exercise might be automated and would generate spend visibility without much efforts, in doing so it may distract people who suddenly end up spending much of their efforts on the 20% of the spend, curious to look for the needle in a hay stack.

The most concerning factor though is the fact that most of these solutions tend to focus on price rather than the drivers of cost. Purchasing choices are complex: they ought to balance the requirements of multiple stakeholders with market realities and strategic choices. This means that whilst an internal price benchmarking analysis may show an opportunity on what appears to be a similar product or service, it can by no means be interpreted as a saving that can be made. There may be legitimate reasons for why such differences exist which we believe are embedded within business and sourcing strategies. So limiting oneself to a price analysis without using a proper procurement performance driver tree that assesses the drivers of costs is a shortcut one should rather not engage in.

A roadmap to muscle up spend analysis

In order to create value, spend analysis solutions have to come of age, and in doing so they ought to take a strategic cross- functional view of organizational realities. At Sievo, we call this strategic crossfunctional approach: Procurement Performance Management. In essence Procurement Performance Management (or PPM) is offering much of what Spend Analysis solutions do, but with more depth whilst adding much more breadth by going beyond what spend analysis do.

Depth

PPM reaches more depth in multiple ways starting by taking a procurement performance driver based approach to analyzing the spend. So it is not anymore about price only, but really the drivers of costs. Indeed, revealing price levels without truly understanding the underlying drivers of price is ignoring strategic choices that organizations have made to meet specific needs. For example, an innovation focused organization that makes high gross margins on their products



may have decided to increase the number of suppliers they buy strategic materials from in order to a) reduce the risk the risk that a sole supplier goes bust and takes the business down or b) invite competition from new suppliers and push the innovation envelope further. In doing so, such companies will likely increase price of end products due to a more fragmented supplier base, but they will also considerably reduce risk and increase innovation capabilities. And besides, the likely price increase might not be felt on the company's bottom line due to the very high gross margins.

Depth, is also about addressing the typical tradeoffs that purchasing makes to get better prices, namely payment terms and inbound inventories. Finally it takes account of market dynamics by offering a window on risks assessment be it financial (driven by commodity market prices) or operational (driven by supply chains and single sourcing decisions as the example above highlights).

Breadth

Providing breadth is taking such solutions all the way from analysis to planning and controlling, taking stock of actual cross- functional strategies and measuring financial and non financial impact of these choices.

Spend analysis highlights opportunities or hypotheses for creating value that ought to be tested by cross- functional teams. This is where category strategies are being formulated with the support of multiple functions that play specific roles in the process. Monitoring the role of each other and ensuring that improvement programs deliver results is of utmost importance to avoid great ideas to die. It is also the basis of commitments for creating value for the company, value which can be translated into budgets.

But having commitments in place is not a guarantee for success. Indeed, ensuring that such great ideas truly deliver results require an element of controlling that would offer transparency to cross functional teams on the actual implementation of such strategies. Controlling is not about policing, but rather a guardian of value execution without which captains of "Trillion Dollar Ships" would be left in the dark.

And providing such guidance is not about stating the obvious, i.e. telling that we are not where we should be, but rather providing an in depth explanation: "Captain we are not at the position we were supposed to be at, but we identified the cause: one of our engines was running slow and we added more grease for it to speed up and we are now back on track".

By overlaying breadth with depth that procurement performance drivers offer, organizations will eventually be able to identify sources of strategic misfits and value leakage, making PPM a truly actionable tool for companies willing to advance procurement performance.

To conclude

Organizations ought to think about their spend analysis in a strategic way and avoid the "Procurement Rabbit Hole" as described in an article for CPO Agenda me and my friend Hugh Baker co- wrote when advising with Booz & Co. Companies make choices for a reason. Respecting and supporting the implementation of these choices cross- functionally is what matters to breaking up silos and become an "organizational maestro".



Advancing • Procurement • Performance

About the author

Fabrice Saporito is the Chief Executive Officer of Sievo, a leading Procurement Performance Management software firm. Prior joining Sievo, Fabrice was advising clients in Europe, Middle East and the United States of America on strategy and operational issues with The Boston Consulting Group and Booz & Company. Fabrice holds is a Graduate from the French Grandes Ecoles and Harvard Business School. Besides “Thoughts”, his writing has been published in multiple media including CPO Agenda, Strategy + Business, Executive Magazine and CEO Middle East. He can be reached at fabrice.saporito@sievo.com

About Sievo

Sievo is a leading Procurement Performance Management software firm. Established late 2003 in Helsinki, Sievo serves clients around the world and offers integrated spend analysis, planning and controlling solutions to advance procurement performance.

Sievo Oy

Kaisaniemenkatu 2 B
00100 Helsinki
Finland
Tel. +358 20 789 0340
Fax. +358 20 789 0341
www.sievo.com

