Spend Analysis: Visibility for Intelligent Decision-making

Spend analysis has gradually become the top process in the procurement executive’s toolbox, placing itself in the top-tier of functionalities alongside e-sourcing, e-procurement and strategic sourcing solutions. Aberdeen research over the last half-decade has chronicled the rise of spend analysis and its true value within the procurement organization. Spend analysis, and the resulting intelligence gleaned from a deep-dive view into corporate spend data, has enabled sourcing groups to uncover opportunities for savings and has given the CFO a strategic advantage by utilizing this information for future forecasting and budgeting.

Spend Analysis: Improving Spend Visibility for Over a Decade

Spend analysis programs have historically been created, executed and leveraged to achieve one major objective: improving visibility to corporate spending. As Figure 1 details, the vast majority (70%) of organizations across the globe have seen an increase in spend visibility as a direct result of the spend analysis function and its associated processes.

Figure 1: Increase in Spend Visibility as a Result of Spend Analysis

The modern spend analysis program consists of various processes, all of which contribute to an overall increase in spend visibility. These processes include: extraction of spend data from multiple internal systems (general ledger, ERP, financial systems, etc.), cleansing and classification of spend data, enrichment of spend data, and analysis / reporting of spend data. The final phase of the program, analysis / reporting, is where companies see the most

Source: Aberdeen Group, July 2010
value derived from spend analysis technology and systems. Procurement and financial execs can "slice-and-dice" their corporate spend data any number of ways, including by supplier, category, date, business unit, etc. to effectively gain intelligence over purchased items (both direct and indirect). This information can be translated into true intelligence, which can arm the strategic sourcing team when negotiating contracts with key suppliers.

**Who is Using Spend Analysis?**

Spend analysis has traditionally been utilized as a procurement and sourcing-focused tool, as its analysis / reporting capabilities are a critical driver for supplier negotiations and achieving cost savings. However, recent Aberdeen research has found that although the Chief Procurement Officer and his / her sourcing staff are the primary users of spend analysis programs / systems, the CFO and associated financial positions are also beginning to see the value of spend analysis (Figure 2).

**Figure 2: Users of Spend Analysis Systems**


Source: Aberdeen Group, July 2010

The CPO's office (66%) has been the primary user of spend analysis over the last decade; as detailed in the *Spend Analysis: Transforming Data Into Value* benchmark study (September 2009), spend "intelligence" is a key component in filling the sourcing pipeline, negotiating deals with suppliers, and identifying areas / opportunities for savings.

Complex category management has become just as critical a procurement aspect as direct materials management; complex categories, such as contingent labor, Travel and Entertainment (T&E), facilities, and strategic meetings, often entail myriad sets of contracts with a vast array of suppliers and vendors. Spend analysis can assist category managers (64%) in consolidating spending, right-sizing their supplier base, and having real-time visibility into spending against budgets for these categories.
Although financial analysts (32%) and CFOs (28%) have been slow to adopt spend analysis as a go-to tool, there is inherent value for the ones already leaning on this classic procurement process. The notion of “savings” has evolved from a strict procurement metric into the financial performance arena, and with a consistent focus on bolstering the bottom-line, CFOs and their teams will rely on spend analysis systems to achieve those cost savings. Savings erosion, which encompasses post-sourcing price changes and logistical / supply risk issues, is also a concern for the finance team, and the CFO must utilize spend analysis as a means of mitigating supply risk factors (and key market pressures) by leveraging the data culled from spend analysis systems.

**Spend Analysis Automation and Integration**

Spend analysis solutions, as further explained later in this document, are often a crucial component of the overall success of a spend analysis program. Recent Aberdeen research has discovered that in selecting a spend analysis solution, companies are focused on integration of the procurement and sourcing processes with an automated spend analysis system (Figure 3).

**Figure 3: Criteria for Spend Analysis Solution Selection**

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<thead>
<tr>
<th>Criteria</th>
<th>Percentage of Respondents, n = 250</th>
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</thead>
<tbody>
<tr>
<td>Integration of spend analysis and sourcing program</td>
<td>44%</td>
</tr>
<tr>
<td>Integration of spend analysis and procurement execution</td>
<td>40%</td>
</tr>
<tr>
<td>Ease-of-use of reporting / analytics tools</td>
<td>32%</td>
</tr>
<tr>
<td>Completely automated end-to-end solution</td>
<td>22%</td>
</tr>
<tr>
<td>Ability to track / measure compliance</td>
<td>20%</td>
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Integration with sourcing (44%) and procurement execution (40%) are the two most critical aspects reviewed by companies when selecting an automated spend analysis solution. Spend analysis is the true link between intelligence and execution, thus third-party solutions must offer a means of extending the data culled and analyzed from their systems into active processes for strategic sourcing and overall procurement management.
**Spend Analysis Automation**

A critical linchpin in the spend analysis program is process automation; unlike other business areas (such as expense management and accounts payable / invoice-processing), manual methods of spend analysis do not involve stacks of paper. Instead, manual spend analysis refers to a lack of repeatable processes that are not automated and require users to push along each step within the greater spend analysis system.

As Figure 4 details, only 22% of enterprises are currently utilizing fully automated spend analysis systems and processes.

**Figure 4: Automation of Spend Analysis**

![Pie chart showing automation levels: 22% Fully Automated, 45% Partially Automated, 33% Fully Manual, n = 460]

Spend analysis automation isn’t just a means of eradicating arduous data culling / cleansing within Excel spreadsheets; automation enables a repeatable cycle of processes that can adequately (and quickly) extract data, cleanse it, enrich it with real-time supply market information and other key information from internal / external sources, and run detailed analysis reports that will allow sourcing executives to educate their teams and execute more-informed and more strategic decisions in regards to supplier management. The following case study provides an example of how one enterprise did just that by transitioning from manual to automated processes for spend analysis.

**A Lesson from Biotech: Improving Lives and the Bottom Line**

Four years ago, a leading global biotechnology firm was mired in inefficient manual processes that hampered its ability to drive procurement savings. "We had low accuracy in spend classification," notes the firm’s Director of Global Strategic Sourcing. "Our tools were marginal and our category managers were supplementing data manually to generate their plans and initiatives." Lacking a central source of consolidated spend data, the company expended large amounts of effort cleansing and enriching spend data during every reporting cycle. According to the Director, "Because the..."
process took man weeks, we could only do it once a year." But that would soon change.

The firm worked with a solution provider to implement a system to gather information from multiple sources (including ERP as well as travel and procurement cards), which is cleansed of duplicate entries before being transitioned to the next stage of processing. The solution then parses individual data elements, such as supplier name and product description, before using a statistical process to assign specific United Nations Standard Product and Services Code (UNSPSC) classifications - which are then mapped to the firm's own internal material group taxonomy. This information feeds the process of opportunity discovery, and allows for both standard (e.g. spend by supplier, category, etc.) and advanced (ex. dashboards and drill-down) reporting functionality. "To make the solution even more robust and compelling, we use third-party data enrichment services, which provide information on suppliers' financial conditions, diversity classifications, parent-child relationships, and other things we can't get natively from our ERP system," says the Director. But what value has this provided?

"We now have a system that offers us a tremendous amount - say, 10-times more - of data," relates the firm's Director. "This has yielded a perceptible improvement in the quality and sophistication of the analyses that our category managers can accomplish." Not long after implementation, the solution had already made significant headway toward the firm's goal of 90% accuracy in classification, and allowed it to reduce the cycle-time for that classification from weeks down to two days. Commenting on the solution's return-on-investment, the Director noted that within two years of the transition to the new system, his category managers had delivered savings in the millions, "far outweighing our initial investment in the solutions."

The transition process was a collaborative one, with a focus on securing organizational buy-in. "We wanted to go beyond the four walls of the global strategic sourcing department," says the Director. "We wanted to make spend analysis a relevant tool for [our] population at large—especially for our finance organization—so we needed to design a program geared for high adoption." Over time, with an emphasis on review and validation, the collaborative approach led to added confidence in the solution's ability to provide true benefit and support decision-making.

With the implementation behind it, and positive results already achieved, what lies ahead for the firm? There is a push to reduce non-PO spend, as this is more difficult to classify due to a lack of detailed description information, which would be present in a PO. There is also a continued focus on utilizing the automated classification and analysis to unearth savings opportunities. "This is something you will do in perpetuity," according to the Director. "Periodic human drilldowns are needed, not because the model is not performing, but because your business changes, your organization changes - and your sense of the data and how you want to use it changes as well."
An Important First Step

As highlighted in the case study, improving procurement performance through spend analysis is a continuous process. It is also a process with great potential to identify new savings opportunities and help to maximize enterprise profitability. Table 1 shows the improvement-over-time for companies engaging in formal spend analysis programs, along different levels of maturity. Sizable increases between those lacking a program and those even in the early stages highlight potential "low-hanging fruit" - areas where the most immediate impact can be felt. Not surprisingly, visibility and reporting capabilities, along with relationship-building with those responsible for day-to-day sourcing activities show improvements early on. The quality of the data shared improves farther down the line, as additional data sources can be consolidated into a single repository - an area where process improvement and communication alone cannot deliver on spend analysis' full potential. As companies mature, the wealth of available data expands, and reporting functionalities continue to improve, communications can be tailored to provide role- or function-based feedback, easing the road toward collaboration with those outside of the Procurement department.

Table 1: Increasing Capabilities with Spend Analysis Program Maturity

<table>
<thead>
<tr>
<th></th>
<th>No Program</th>
<th>Less than 1 Year</th>
<th>1 - 3 Years</th>
<th>Over 3 Years</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ability to analyze and develop reports on spend data</td>
<td>14%</td>
<td>26%</td>
<td>48%</td>
<td>64%</td>
</tr>
<tr>
<td>Ability to collect spend data from multiple sources</td>
<td>20%</td>
<td>27%</td>
<td>57%</td>
<td>57%</td>
</tr>
<tr>
<td>Cross-functional coordination with Finance, product, and sourcing groups</td>
<td>28%</td>
<td>30%</td>
<td>42%</td>
<td>53%</td>
</tr>
<tr>
<td>Cross-functional coordination with line of Business and sourcing groups</td>
<td>22%</td>
<td>36%</td>
<td>48%</td>
<td>51%</td>
</tr>
<tr>
<td>Visibility into enterprise-wide spend across all categories (commodities and services)</td>
<td>10%</td>
<td>28%</td>
<td>43%</td>
<td>49%</td>
</tr>
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</table>

Source: Aberdeen Group, July 2010

Of course, capabilities do not improve simply as a function of time. As programs mature, processes are refined - but the technological foundation upon which the programs are built can change as well. As illustrated in Figure 5, adoption levels of specific spend analysis solutions, as well as applications for contract and supplier management, increase as programs mature. Less than one-quarter of firms that have been involved in a spend analysis initiative for three years or more are still using manual (i.e. spreadsheet-based) approaches. This is a logical result, as companies employing spend analysis solutions report greater levels of both identified (8.5% vs. 6.5%) and realized/implemented (7.3% vs. 5.9%) savings from sourcing events, as compared to those who lack this technology. When
combined with supplier and contract management, the benefits expand from simple cost savings to also include areas such as contractual compliance (of both buyers and suppliers), supplier performance measurement, and the enablement of supplier rationalization based on per-supplier volumes, risk characteristics, or other measures that allow Procurement policy to support overall organizational strategy.

Figure 5: Technology Adoption by Program Maturity

![Bar chart showing technology adoption by program maturity](chart.png)

Source: Aberdeen Group, July 2010

Recommended Actions

Spend analysis provides an opportunity for enterprises to produce direct benefits to the bottom line by reducing the costs of purchased goods and services. To begin the journey, interested firms should:

- **Gain an understanding of where their enterprise data resides.** This may include multiple ERP systems, multiple installations of a single ERP across separate business units or locations, e-procurement and Accounts Payable (A/P) applications, among others. This will provide a picture of what data is available, and on what foundation an improvement initiative can be based.

- **After surveying what data is currently available, identify potential avenues for increasing the amount that is captured moving forward.** High levels of non-PO spend may be lessening the value of an e-procurement system, which could be building out a wealth of data for later analysis. Always keep an eye on how current policies and procedures may lead to behavior that can compromise efforts at analysis. Are current rules being enforced to maximize usage of systems that collect spend data? If policies are lax governing the front-end of the purchase process, do
not look past what information may be gleaned from A/P on the back-end.

- **Leverage intelligent sourcing practices to educate themselves.** After taking the steps to understand the current situation (for both processes and technologies), craft a results-oriented Request for Proposal (RFP) to leverage the knowledge of third-party consultants and solution providers to identify potential avenues for improvement. If the processes involved in spend analysis are foreign to current management, utilize this opportunity to learn from those who implement these solutions every day. Providers will not likely provide schematics for data-mapping in an initial response, but in making a business case, they should help shed light on what approaches are best suited for achieving the stated goals. This open-ended approach will help demonstrate each provider’s knowledge, responsiveness, and creativity - three attributes of central importance to an ultimate selection decision.

For more information on this or other research topics, please visit [www.aberdeen.com](http://www.aberdeen.com).

### Related Research

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<td>The CFO’s View of Procurement: Work in Progress: November 2009</td>
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