Aberdeen *Group*

The Spend Intelligence Benchmark Report

Turning Data into Action

June 2006

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Executive Summary

As corporate procurement organizations are charged with securing products and services of the best quality and the lowest possible cost, their enterprises are counting on them to be much more than just "order takers." To accomplish that, procurement organizations must develop capabilities in **spend intelligence**. This takes spend analysis a step further, allowing the enterprise to take what it knows from the spend data it has gathered and use it to act on forward-thinking initiatives. In other words, spend intelligence provides *actionable* information.

Spend intelligence helps an organization's efforts to bring more spend under management, a key strategy for chief procurement officers highlighted in the March 2005 Aberdeen report: *The CPO's Agenda: Five Strategies for Procurement Transformation*. The report stated that the success of any supply management program depends largely on its ability to access, organize, and analyze spend data. This a*ccess offers invaluable intelligence on spending patterns, compliance and performance ratings, inventory status, and part attributes*. This, in turn, helps identify savings opportunities, drive compliance, and develop sourcing strategies. This entire process of determining, defining, and executing souring strategies is called spend-under management. Various Aberdeen studies have revealed that enterprises with more spend under management achieve cost and non-cost objectives, such as quality and other metrics.

To gauge how far enterprises have advanced in spend intelligence practices, Aberdeen undertook a benchmark survey of nearly 140 organizations.

Key Business Value Findings

- Best in Class companies excel in spend intelligence through more automation, more frequent spend analysis, and above average spend visibility.

- The key to effective spend intelligence is not just automatically classifying spend information, but performing this crucial process quickly and accurately.

- The top challenges to spend intelligence efforts lie in data quality, data cleansing, and data classification.

- While enterprises' most critical criteria in selecting spend intelligence tools focus heavily on processes, the top criterion addresses user friendliness; enterprises want reporting and analytics tools that are easy to use.

- Enterprises are leaning ─ slightly ─ toward spend intelligence software providers' tools over the offerings of ERP-based solutions and those of e-sourcing and e-procurement vendors.

- Adoption of spend intelligence automation is still in the early phase; 53% of respondents say their enterprises' spend intelligence programs generally revolve around in-house manual services, using spreadsheets.

Implications & Analysis

The "holy grail" of spend intelligence is full and correct auto-classification of spend data, limiting the human intervention to acting on the data (Aberdeen considers Best in Class enterprises as those with at least 81% of spend auto-classified). However, technology can only take an enterprise so far. Accomplishing the goals of spend intelligence begins with what the enterprise does internally via *strategic actions, capabilities,* and *enablers* that enterprises use to respond to the chief pressures, or drivers, of spend intelligence.

Those actions revolve around organization of spend intelligence programs and determining an enterprise's spend analysis and intelligence capabilities before embarking on a spend intelligence program. Specifically, enterprises must consider the following:

- **Securing executive sponsorship**: This is critical for just about any major undertaking, especially one involving an extensive information technology investment. If you don't have a project champion who can make the case to senior executives, find one who can offer the most clout.

- **Building a cross-functional team for enterprise-wide spend intelligence:** Have an intelligence-gathering plan and key stakeholders in place to draw up the goals and expectations of a spend intelligence program.

- **Demonstrating quick hits by assessing spend intelligence opportunities in one or two spend categories:** Showing the results of a small pilot program can help make the case with senior executives.

According to our survey field, half of respondents' enterprises have had spend intelligence programs in place for at least a year, with 19% having had them for at least three years. Of the Best in Class enterprises, 79% have had their programs in place for at least one year, with 21% having established them more than three years ago. Regardless, even enterprises that are not at Best in Class levels or that haven't had longer-standing programs have reported benefits from their spend intelligence undertakings.

So, while longer-standing programs are finding markedly better success in getting a more complete picture of enterprise spend and in "right sizing" their supply bases, all enterprises in the survey are experiencing ─ on average ─ double-digit decreases in the prices of goods and services (13%) and year-over-year cost reductions for all spending (10%). Lowering costs proves to be a strong early indicator of program success. But for the longer term, enterprises need to focus on more than how much they're saving.

The answer lies in "auto classification" of data, especially in how accurately it can classify spend, how "learnable" it is for key users in order to act on the intelligence it generates, and how often it can generate the data an enterprise needs in order to act.

Recommendations for Action

Automation is the lynchpin to a successful spend intelligence program. The goal for a spend intelligence program is the auto-classification of all spend data. Here are Aberdeen's three key recommendations in this report:

1) **Laggard** and **Industry Average** enterprises must drive toward more automation of spend intelligence-gathering processes and standardize those processes at a level with which they're comfortable: company-wide or regionally.

2) A **Best in Class** enterprise must strive for more detailed visibility into spend, with end-to-end spend intelligence software, either all in-house or combined with third-party provider services depending on its intelligence needs. In addition, it should strive for full automation, especially auto-classification of spend data and ensure that data is correct and up to date in the master data system.

3) **All enterprises** must ensure their spend intelligence processes are connected with more and more business processes, such as sourcing, procurement (the obvious choices), contract management, compliance, and supplier performance. They should also *focus* on increased contract compliance as a spend intelligence goal, and utilize any newly cleansed data to determine price variances over time ─ per item and per vendor.

Table of Contents

Table of Contents

Figures

Tables

Chapter One:
Issue at Hand

Gathering data is one thing; taking action based on the data you gather bumps that process up to the next level. As corporate procurement organizations are being charged with securing products and services of the best quality and the lowest possible cost, their enterprises are counting on them to be much more than just buyers. Procurement is becoming an increasingly strategic weapon that must look beyond the purchase orders and invoices in providing more value for the enterprise.

To reach that point, procurement organizations must become more engaged in the gathering of *spend intelligence*. This takes spend analysis a step further, allowing the enterprise to take what it knows from the spend information it has gathered and use it to act on forward-thinking initiatives. Picture spend data at three levels, each more complex than the previous level:

- **The raw data.** For instance, Enterprise XYZ spent $250,000 on office supplies from Vendor A last year, in the second year of a three-year contract in which it provided all of XYZ's office supplies. In the first year, the same amount of supplies cost $235,000 and XYZ's bills for the third and final year will total $260,000.

- **Analysis of the raw data (spend analysis).** XYZ has spent $40,000 more than what it spent in Year 1 of the contract, which is coming up for renewal. In the meantime, senior management had mandated a 5% cut in procurement spend. Essentially, XYZ has paid more each year for the same amount of product and it senses an opportunity to cut spend.

- **Spend intelligence:** As the contract comes up for renewal, XYZ uses the data and its analysis of that data to craft a strategy: The message to Vendor A: "Our spend on office supplies in each of the past two years has exceeded the core inflation rate. Our goal is to spend less on supplies, so we want to work out a different pricing structure that will lower our costs. At the same time, we're putting the contract out to bid to see what the market can offer us."

Of course, this is a simple example, but you can see the clear contrasts among the three levels. The spend intelligence step highlights the action an organization can take after gathering and analyzing the data.

Spend intelligence helps an organization's efforts to bring more spend under procurement management, a key strategy for chief procurement officers highlighted in the March 2005 Aberdeen report: *The CPO's Agenda: Five Strategies for Procurement Transformation*.

The report stated that the success of any supply management program depends largely on its ability to access, organize, and analyze spend data. *Access to timely, accurate, complete, and detailed spend data offers invaluable intelligence on spending patterns, compliance and performance ratings, inventory status, and part attributes*. This, in turn, helps identify savings opportunities, drive compliance, and develop sourcing strategies.

Pressures behind Spend Intelligence

The key factors behind formal spend intelligence programs reflect those that drive enterprise efforts to transform their procurement, sourcing, and supply chain teams into strategic weapons (Figure 1): **Save money** and **control spend**. But the top three factors also address the importance of having the right processes in place to execute and refine a spend intelligence program.

Figure 1: Top Factors Driving Adoption of Formal Spend Intelligence Programs
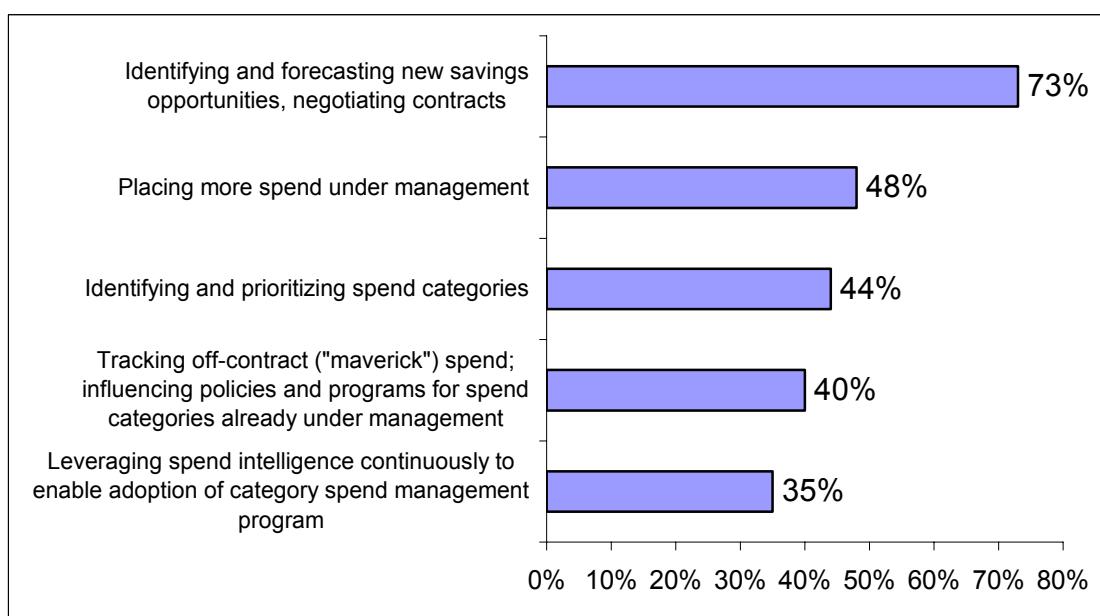
Contrast these top three factors with the five in Figure 2. These factors, which focused heavily on gathering information, were high spend intelligence priorities a mere two years ago, but are now secondary to the factors listed in Figure 1. This indicates how far spend intelligence has advanced as a corporate discipline in that span.

Chapter Three will analyze how enterprises are combating those pressures ─ through strategy, processes, and technology ─ and the practices that leading, or Best in Class, enterprises are undertaking.

Figure 2: Lesser Factors Driving Adoption of Spend Intelligence Programs

Identifying top suppliers of goods or services	15%
Identifying top commodities - current or future	9%
Decreasing sourcing cycle time	6%
Identifying top sites for spend	3%
Determining M&A synergy	2%
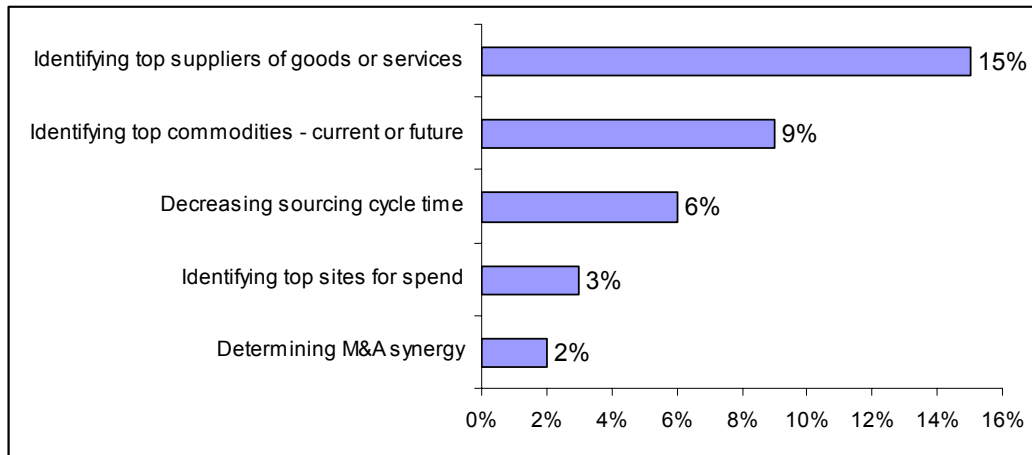
Source: Aberdeen*Group*, June 2006

Processes and Automation

To achieve the maximum results from spend intelligence programs, Aberdeen advocates *enterprise-wide processes facilitated by broad-based automation*. As Chapter Two will point out, most enterprises have a long way to go to reach that level. For instance:

- Only 9% of the 139 survey respondents have fully automated spend intelligence process automation using common company-wide systems.

- Only 23% have spend intelligence processes that are standardized and aligned company-wide.

So, while spend intelligence programs have been in place for more than a year in about half the enterprises represented in the Aberdeen survey, most of the rest have either launched theirs within the past year or are planning programs. Yet, to respond to the chief drivers of spend intelligence, enterprises must examine their internal processes and determine where automation can complement them to achieve the goals of their programs.

Altogether, the drivers lay the foundation for Aberdeen's spend intelligence PACE Framework, which indicates corporate behavior in this area (See PACE Key). These factors, or pressures, are what drive enterprises to ease these pressures through strategic actions, internal capabilities (business process competencies), and technological enablers.

> **PACE Key — For more detailed description, see Appendix A**
>
> *Aberdeen applies a methodology to benchmark research that evaluates the business pressures, actions, capabilities, and enablers (PACE) that indicate corporate behavior in specific business processes. These terms are defined as follows:*
>
> ***Pressures —*** external forces that impact an organization's market position, competitiveness, or business operations
>
> ***Actions —*** the strategic approaches that an organization takes in response to industry pressures
>
> ***Capabilities —*** the business process competencies required to execute corporate strategy
>
> ***Enablers —*** the key functionality of technology solutions required to support the organization's enabling business practices

Chapter Two:
Key Business Value Findings

Key Takeaways

- Best in Class companies excel in spend intelligence through more automation, more frequent spend analysis, and above average spend visibility.

- The top challenges to spend intelligence efforts lie in data quality, data cleansing, and data classification.

- While enterprises' most critical criteria in selecting spend intelligence tools focus heavily on processes, the top criterion addresses user friendliness; enterprises want reporting and analytics tools that are easy to use.

- Enterprises are leaning — slightly — toward best-of-breed solution providers for spend intelligence tools, over the offerings of ERP-based solutions and those of e-sourcing and e-procurement vendors.

- Adoption of spend intelligence automation is still in the early phase; 53% of respondents say their enterprises' spend intelligence programs generally revolve around in-house manual services, using spreadsheets.

What are the characteristics of Best in Class enterprises when it comes to spend intelligence? The distinguishing factors are breadth of processes, spend visibility, the use of technology in executing spend intelligence programs, and how frequently they conduct spend analysis activities (Table 1). The Best in Class distinguish themselves from Industry Average and Laggard enterprises with *higher degrees of automation, process standardization at either a regional or company-wide level, frequent (quarterly or better) spend analysis,* and *above-average spend visibility at a category or commodity level.*

To determine Best in Class companies in this survey as part of Aberdeen's Competitive Framework (See *Competitive Framework Key*), we asked respondents about the accuracy of their enterprises' auto-classification capabilities; or, how much spend is classified automatically, without human intervention, through current processes. Aberdeen determined that accuracy in Best in Class organizations measures at least 81%. The accuracy range for Industry Average enterprises is 51% to 80%; for Laggards, it's 50% or less.

Program longevity can also be a help. Sixty percent of Best in Class represented in the survey have had spend intelligence programs in place from one to three years. Another 30% have been working with them for more than three years (Figure 3).

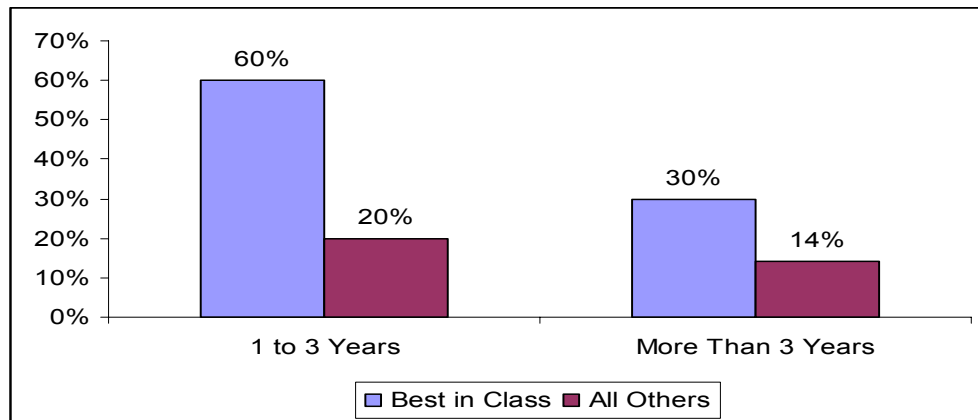| Competitive Framework Key |
|---|
| The Aberdeen Competitive Framework defines enterprises as falling into one of the three following levels of practices and performance: |
| *Laggards* —practices that are significantly behind the average of the industry |
| *Industry Average* —practices that represent the average or norm |
| *Best in Class* —practices that are the best currently being employed and significantly superior to the industry norm |

Figure 3: Spend Intelligence Program Longevity

Source: Aberdeen*Group*, June 2006

Table 1: Aberdeen's Competitive Framework for Spend Intelligence

|	Laggards	Industry Average	Best in Class
Process	For most, spend intelligence processes are mostly ad hoc or non-existent; many are still manual. And, most spend analysis is conducted either monthly, quarterly, annually, or ad hoc	Spend intelligence processes are either partially or fully automated; spend analysis is generally conducted annually or more frequently	Spend intelligence processes are either partially or fully automated; spend analysis is generally conducted quarterly or more frequently
Organization	For most, spend intelligence processes vary by individual site or there are no formal processes, mostly the latter	For most, spend intelligence processes vary by individual site or there are no formal processes	For most, spend intelligence processes are standardized at the regional level or company-wide
Knowledge	Most have category- or commodity-level visibility into most company spend, but many have either supplier-level (baseline) visibility or visibility across enterprise	Category- or commodity-level visibility into most company spend	Above average spend visibility at category or commodity level
Technology	Spend intelligence services are manual and in-house (using spreadsheets); data cleansing is manual and services-based, with use of Excel and Access tools	Spend intelligence services either manual and in-house or hosted spend classification with Web reporting access; data cleansing is manual, services-based, or hosted in some fashion, possibly with in-house infrastructure	Most are automated with in-house or third-party software, or a combination of both.

Source: Aberdeen*Group*, June 2006

Process and Automation

Aberdeen believes a centralized process that covers the entire enterprise is an important step to placing as much spend under procurement organization management as possible and gaining more detailed visibility into spend. It's no small wonder, then, that most Best in Class enterprises have processes that are standardized either company-wide or by geographic region. By contrast, only 21% of all other companies in the Aberdeen survey ─ less than half of the Best in Class ─ claim this level of standardization (Figure 4).

Figure 4: Process Scope ─ Best in Class vs. Other Enterprises
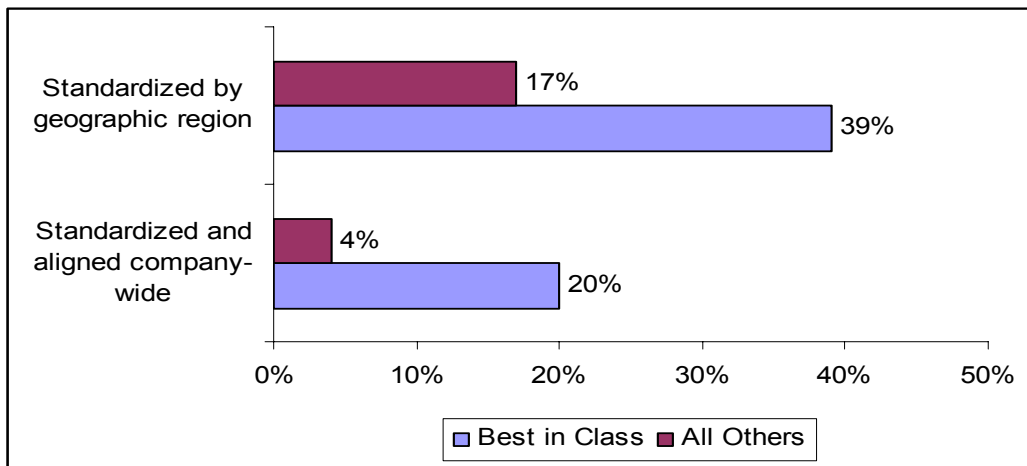
Source: Aberdeen*Group*, June 2006

Automation can help shorten processing times by providing needed information quickly enough for the enterprise to act. Such a capability is becoming increasingly important in a more fast-paced global economy. Here, 94% of the Best in Class have at least partial automation, compared with 74% of all other enterprises (Figure 5).

Figure 5: Degree of Process Automation for Spend Intelligence

Source: Aberdeen*Group*, June 2006
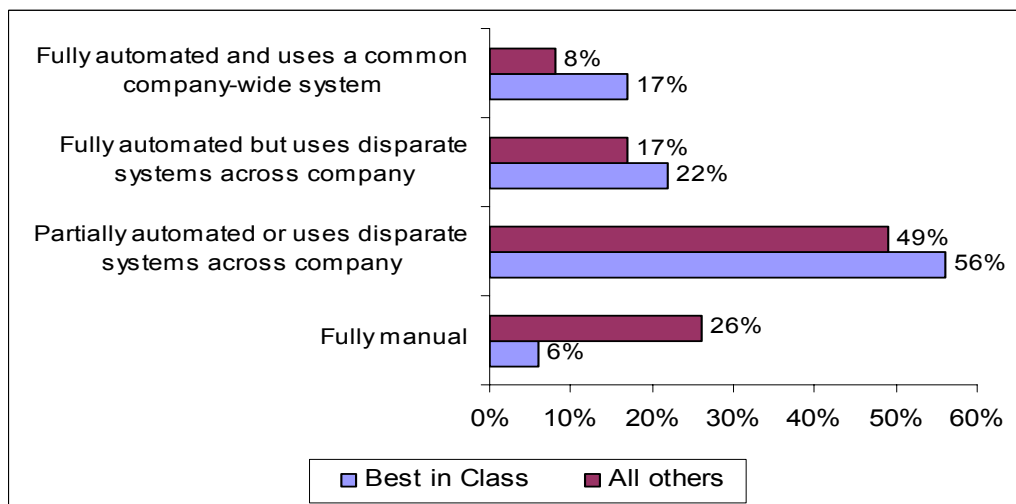
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In fact, procurement executives interviewed for the March 2005 Aberdeen report, *The CPO's Agenda*, believe enterprises should leverage technology to accelerate center-led procurement. That, in turn, helps move the organization to standardized, company-wide procurement processes.

However, most enterprises are conducting their spend intelligence programs without the full benefit of automation, at least beyond desktop tools such as Microsoft Excel and Access. The highest technological level for spend intelligence is in-house, end-to-end software behind the firewall, and includes a data store, auto-classification capabilities, and analytics. Our survey found that only 9% of respondents' organizations are at this level (Figure 6). However, having a complete system in-house is not necessarily the best option for every enterprise. It could work for any of the following reasons:

- Your organization measures daily or more frequently;

- Ease of data extraction;

- Your enterprise is dealing in and analyzing data on commodity items, such as gold, oil, precious metals, and agricultural products such as wheat.

Figure 6: Current State of Spend Intelligence
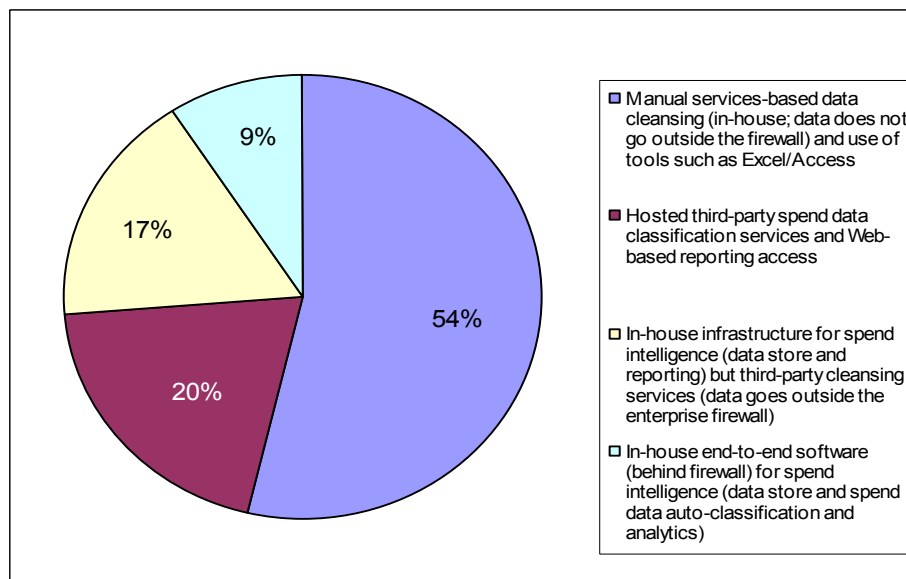
Source: Aberdeen*Group*, June 2006

The Data Problem

The success of any supply management program depends largely on its ability to access, organize, and analyze spend data. In *The CPO's Agenda* report, procurement executives cited this as the most important strategy for increasing spend under management. Access to timely, accurate, complete, and detailed spend data offers invaluable intelligence on spending patterns, compliance and performance ratings, inventory status, and part attributes. This insight helps identify savings opportunities, drive compliance, and develop sourcing strategies. Accurate spend data can also arm procurement executives with the facts needed to secure the necessary budget and policy changes to drive supply manage-

ment initiatives. However, more than a year after that report was published, enterprises have targeted data quality ─ or rather, the lack of it ─ and intense manual data cleansing as the main impediments to successful spend intelligence efforts. In fact, efforts to convert data into actionable intelligence dominate the list of the top four challenges to spend intelligence efforts (Figure 7).

Figure 7: Top Four Challenges to Spend Intelligence Efforts
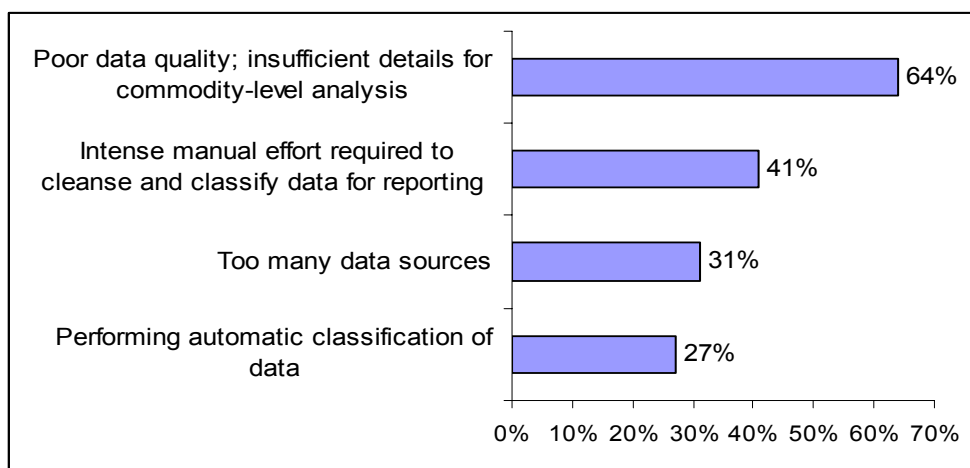
Source: Aberdeen*Group*, June 2006

Survey respondents were asked to rate the level of importance in eight areas of spend intelligence on a scale of 1 (non-important) to 5 (very important). The respondents placed a high importance on such spend intelligence processes as *data classification, data cleansing, data extraction*, and *analysis*. While many organizations and executives place a high importance on reporting, it only placed fifth out of the eight areas (Table 2).

Table 2: Importance of Capabilities in Spend Intelligence Processes

PROCESS	Avg. Rating of Importance (1-5 Scale) ALL RESPONDENTS
Data Classification	**4.32**
Data Cleansing	**4.25**
Analysis (slice/dice, power user capabilities)	**4.14**
Data Extraction	**4.10**
Reporting (preformatted reports overall)	**3.87**
Turnaround Time	**3.79**
Supplier Content	**3.72**
Reporting (dashboard)	**3.57**

Source: Aberdeen*Group*, June 2006

The respondents were also asked to rank their capabilities in each area, with the same numeric criteria (1 being very poor, 5 being very strong). In a side-by-side comparison with Best in Class performers (Table 3); we found a large gap among the areas regarding data (classification, cleansing and extraction) of approximately 30%, with Best in Class companies exceeding the full survey field.

Table 3: Current Capabilities in Your Spend Intelligence Processes

PROCESS	Avg. Ranking of Capability (1-5 Scale) ALL RESPONDENTS	Avg. Ranking of Capability (1-5 Scale) BEST IN CLASS
Data extraction	3.23	4.22
Data classification	3.01	3.89
Data cleansing	2.61	3.39
Supplier content	2.98	3.47
Turnaround time	2.68	3.44
Reporting (preformatted reports overall)	2.87	3.28
Analysis (slice/dice, power-user capabilities)	2.99	3.17
Reporting - dashboard	2.44	3.00

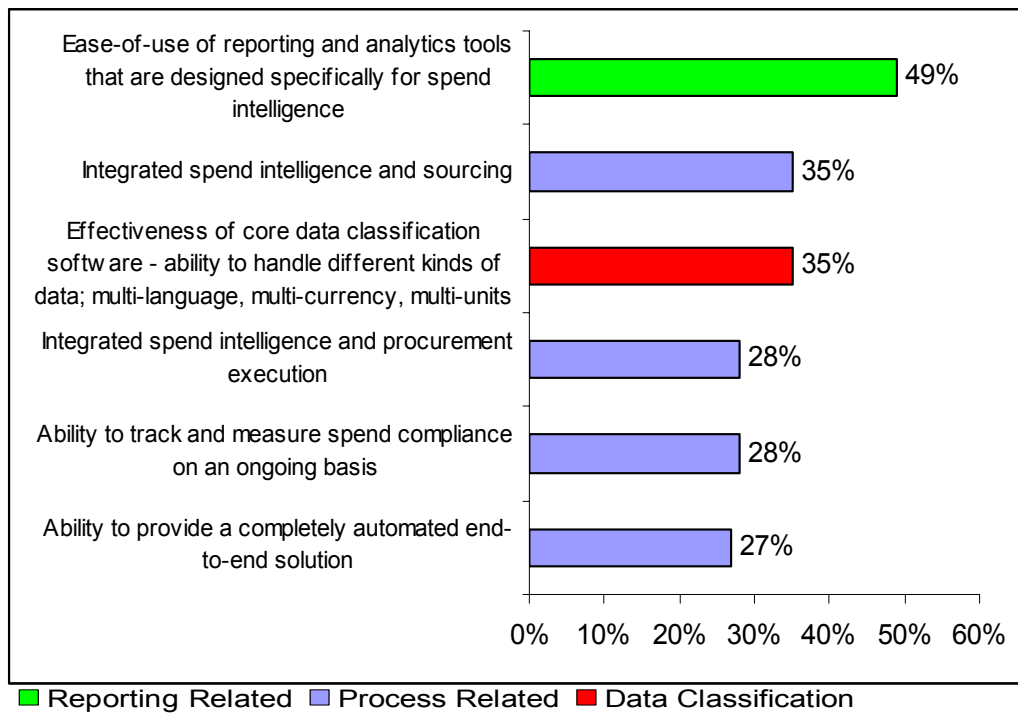Source: Aberdeen*Group*, June 2006

So, when enterprises are looking for spend intelligence tools, these capabilities are high on their lists of criteria (Figure 8), especially when it comes to user friendliness (green bar) and process improvements (blue bars). And, effectiveness of the core data classification software in its ability to handle different kids of data, such as language, currency, and units of measure ranks high (red bar). While a completely automated, end-to-end solution would be the most optimal for spend intelligence efforts, only 27% of respondents cite that as a critical selection criteria. But it ranks slightly higher as a priority among Best in Class enterprises.

Technology Options

No vendor has the ultimate solution in the spend intelligence area. The best vendor for an enterprise must be determined by such factors as number of data sources, level of data cleansing required, and reporting requirements. So, it's not surprising that no one vendor can claim dominance in this sector and, according to our survey, no one appears to be in a position to claim the "leading provider" moniker. And, because the spend intelligence market itself is so new, best-of-breed spend intelligence solution providers did not show up high when respondents answered this question.

Figure 8: Critical Selection Criteria for Spend Intelligence Solutions

Source: Aberdeen*Group*, June 2006

However, when respondents were asked which type of solution their enterprises would consider primarily, spend intelligence software providers' products came out ahead of ERP-based tools and e-sourcing and e-procurement providers (Figure 9). Even most enterprises that use ERP giants SAP and Oracle for spend analysis today are looking in other directions for their spend intelligence tools.

Figure 9: Types of Spend Intelligence Solutions Enterprises Will Consider
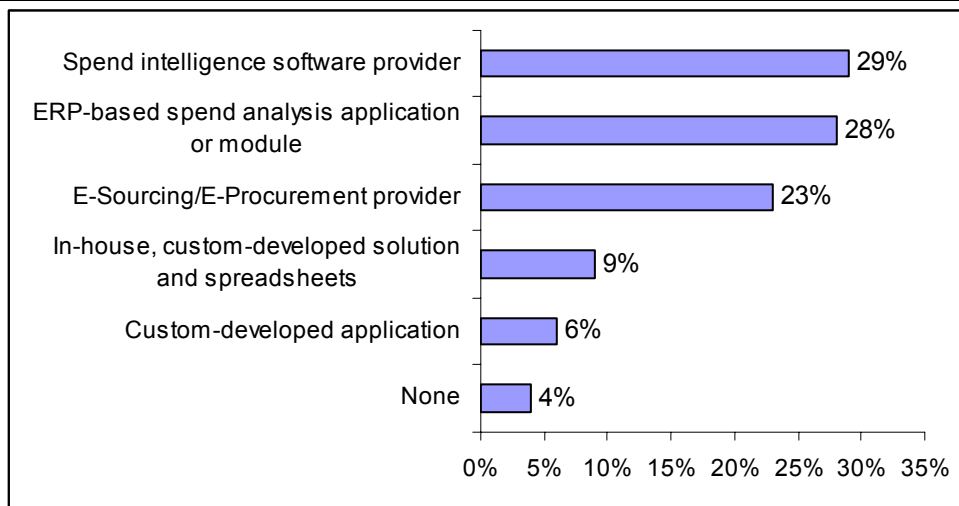
Source: Aberdeen*Group*, June 2006

Some enterprises will integrate their spend intelligence tools into their ERP systems. For instance, a large high technology company with a major vendor's ERP system used a best-of-breed provider's solution to cleanse and classify spend data. While the ERP system handles about 80% of the company's purchase orders, the spend intelligence solution helped classify $30 million in "miscellaneous" spend into 140 categories, providing better visibility into spend. After the cleansing, *no* spend amount was categorized as "miscellaneous." This is significant since no action can be taken on miscellaneous spend, but the new set of 140 categories can be allocated to organizations or individuals who can act on and react to the data.

Chapter Three:
Implications & Analysis

- The "holy grail" of spend intelligence is full and correct auto-classification of spend data. Enterprises should strive to take as much human intervention out of the spend intelligence process as possible.

- The key strategic actions in driving a robust spend intelligence program center around measuring the current state of your spend analysis program, securing executive buy-in, and "testing" the potential by assessing opportunities in one or two spend categories.

- The payoffs from successful spend intelligence start with bringing more spend under procurement management and increased contract compliance. Enterprises are also reducing sourcing cycles as well as the number of purchased items.

In 2004, *spend analysis* efforts focused on gathering of information that enterprises could use as a first step toward gaining control of their supply bases and their spend. Today, *spend intelligence* is allowing these enterprises to push the envelope on spend analysis, expand visibility into spend and the supplier contracts that lie behind the spend, and identify targets for category spend management programs to isolate certain spend areas needing special attention.

Pressures, Actions, Capabilities, and Enablers (PACE)

The "holy grail" of spend intelligence is full and correct auto-classification of spend data, limiting the human intervention to acting on the data. However, technology can only take an enterprise so far. Accomplishing the goals of spend intelligence begins with what the enterprise does internally. Table 4 highlights the prioritized *actions, capabilities,* and *enablers* that enterprises use to respond to the chief pressures, or drivers, of spend intelligence.

Those actions revolve around organization of spend intelligence programs and determining the enterprise's spend analysis and intelligence capabilities before embarking on a spend intelligence program. Specifically, enterprises must consider the following:

- **Securing executive sponsorship**: This is critical for just about any major undertaking, especially one involving an extensive information technology investment. If you don't have a project champion who can make the case to senior executives, find one who can offer the most clout.

- **Building a cross-functional team for enterprise-wide spend intelligence:** Have an intelligence-gathering plan and key stakeholders in place to draw up the goals and expectations of a spend intelligence program.

- **Demonstrating quick hits by assessing spend intelligence opportunities in one or two spend categories:** Showing the results of a small pilot program can help make the case with senior executives.

Table 4: PACE Framework for Spend Intelligence

Prioritized Pressures	Prioritized Actions	Prioritized Capabilities	Prioritized Enablers
Identifying and forecasting new savings opportunities (within spend categories) and negotiating contracts	Demonstrate quick hits by assessing opportunities in one or two categories and tactical sourcing	* Standardize processes company-wide to gather the data necessary to choose savings targets * Make sure category managers are among the high-end users of spend intelligence tools	Move away from manual methods of gathering data (e.g., spreadsheets) and automate more functionality that also allows for role-based access
Placing more spend under management	* Secure executive sponsorship * Build a cross-functional team or committee for enterprise-wide spend intelligence	Standardize spend intelligence processes in some fashion (e.g., by region or company-wide) to suit goals	Software that covers the breadth of processes for spend intelligence, including data store, spend data auto-classification and analytics, and that integrates with the rest of the spend management process
Identifying and prioritizing top spend categories	Create a baseline for spend intelligence by identifying data sources, current state of data quality, and computing a "state of visibility"	Have category- or commodity-level visibility into spend to meet or exceed what you need to know	Strive for complete automation across disparate systems or - preferably - company-wide
Tracking off-contract ("maverick") spend, and influencing policies and programs for spend categories already under management	* Secure executive sponsorship * Build a business case for investments in spend intelligence infrastructure	Conduct spend analysis monthly or more frequently	Best-of-breed software or tools within your ERP system that span the enterprise and provide auto-classification of spend data and reporting with exception management
Leveraging spend intelligence continuously to enable adoption of a category management program	Demonstrate quick hits by assessing opportunities in one or two categories and tactical sourcing	* Standardize and align spend intelligence processes company-wide to facilitate decision-making * Have category- or commodity-level visibility into spend to meet or exceed what you need to know	In-house end-to-end software (behind the firewall) for spend intelligence (data store and spend data auto-classification and analytics)

Source: Aberdeen*Group*, June 2006

- **Building a business case for investing in a spend intelligence infrastructure:** Here, demonstrate where the enterprise can gain more visibility into spend and contract management through a technology investment program, where it can find both short- and long-term savings opportunities.

- **Creating a baseline for spend intelligence by identifying data sources, current state of data quality, and computing a "state of visibility":** Show how the returns from a spend intelligence program can grow as the enterprise gains more experience with it.

The Payoffs of More Robust Spend Intelligence

According to our survey field, half of respondents' enterprises have had spend intelligence programs in place for at least a year, with 19% having had them for at least three years. Of the Best in Class enterprises, 79% have had their programs in place for at least one year, with 21% having established them more than three years ago. Regardless, even enterprises that are not at Best in Class levels or that haven't had longer-standing programs have reported benefits from their spend intelligence undertakings (Table 5).

Table 5: Spend Intelligence KPI Results

KPI	All Respondents	Programs in Place for at Least 3 Years
Percentage of Enterprise Spend under Management	37%	49%
Reduced Sourcing Cycles by %	19%	25%
Reduction in Overall Number of Purchased Items by %	10%	15%
Contract Compliance Rates	31%	35%

Source: Aberdeen*Group*, June 2006

So, while longer-standing programs are finding markedly better success in getting a more complete picture of enterprise spend and in "right sizing" their supply bases, all enterprises in the survey are experiencing ─ on average ─ double-digit decreases in the prices of goods and services (13%) and year-over-year cost reductions for all spending (10%). Lowering costs proves to be a strong early indicator of program success. But for the longer term, enterprises need to focus on more than how much they're saving.

Auto Classification

The key for successful spend intelligence lies in "auto classification" of data, especially in how accurately it can classify spend, how "learnable" it is for key users in order to act on the intelligence it generates, and how often it can generate the data an enterprise needs in order to act.

As more data is generated through the use of e-procurement systems and automated direct materials orders within the supply chain, there is a danger of information overload. Most purchasing analysts are busy enough, but as the amount of information to analyze increases, conventional spreadsheets are just not sufficient. Data classification tools, or "auto class" capabilities, provide the intelligence to mine the information, perform automated analysis, and help discover savings opportunities. One example is aggregating multiple AP and e-procurement systems if an enterprise's spend on a certain supplier's

products or services exceeds a threshold that will trigger additional discounts. This "discount-discovery" process is one of many examples in which a proper auto-classification solution can yield a tremendous return on investment.

Other Enabling Technologies

Along with data classification, the spend analysis/spend intelligence field contains four other major processes and technology areas.

Data Extraction

This technology pulls data from various enterprise systems that contain spend and other pertinent data (e.g., ERP, AR/AP, General Ledger). Enterprises that have numerous data sources benefit most from a vendor that emphasizes a strong integration architecture, thus the ability to extract data from different sources. Aberdeen recommends that enterprises ask for references from clients of potential vendors that have strong spend intelligence from the data sources residing in their current environments.

Data Cleansing

The most common example of a data cleansing function is examining spend data extracted from accounts payable and other systems. For example, the vendor IBM could appear as "IBM", "I.B.M.", and "IBM Corp". Without such a conversion, a process known as normalization, IBM would appear as three different vendors, thus causing reduced negotiating leverage. Another example is converting "GALLONS", "Gal", "gallons", and "galons" into "GAL." A global company purchasing gasoline needs to sum up all these disparate units to determine the total number of gallons spent in the U.S., and must also tally the "Liters", and "Litres" purchased internationally. This form of intelligent cleansing, in conjunction with data classification, can provide insight and visibility into (1) the total amount of gasoline purchased in all countries and by all units of measures (gallons, litres); (2) amounts purchased from various vendors; and (3) amounts by location. This level of information can be used to strategically negotiate a contact with a global provider of gasoline. This is an example of how spend analysis and the data cleansing capability provide the insight to reduce costs.

Data Store

A data store can be a conventional "spend data warehouse," modified for the richness of information a data classification system will provide; for example, a deep hierarchy of spend such as "IT" → "IT Hardware" → "Laptops" → "Power Laptops".

Analytics and Reporting

While analytics and reporting can be seen as a commoditized area, it's important since it's the only function visible to executives. Most spend intelligence systems have robust reporting because they use third-party OLAP (online analytical processing) tools and customize them for the specific data model. Here, the better reporting systems offer very easy-to-use and easy-to-configure dashboards, executive roll-ups (high-level views by supplier or location), and very intuitive ways for people from all levels of a company to drill down into details, such as the actual purchase order.

Case Study: Success through Automation

The procurement organization for a large manufacturing company is spending more time and resources on strategic activities, less than a year after adopting a Web-hosted tool that classifies spend data. The tool, installed in July 2005, replaced a largely manual process in which the organization was using some automation via Microsoft Excel, according to the group's manager. One of the group's five full-time employees was responsible strictly for the manual classification of spend data.

As of last March, the procurement group had more than doubled the amount of time it spent on strategic activities and cut the amount of time it had been spending on transactional activities (Figure 10). The procurement group began seeing the payoffs within three months of the installation when it gained the equivalent of one-quarter of a full-time employee's schedule in time savings. As the group gains expertise with the tool, the manager expects to move one of his five full-time employees to more strategic activities.

Figure 10: Automation Helps Procurement Organization Become More Strategic
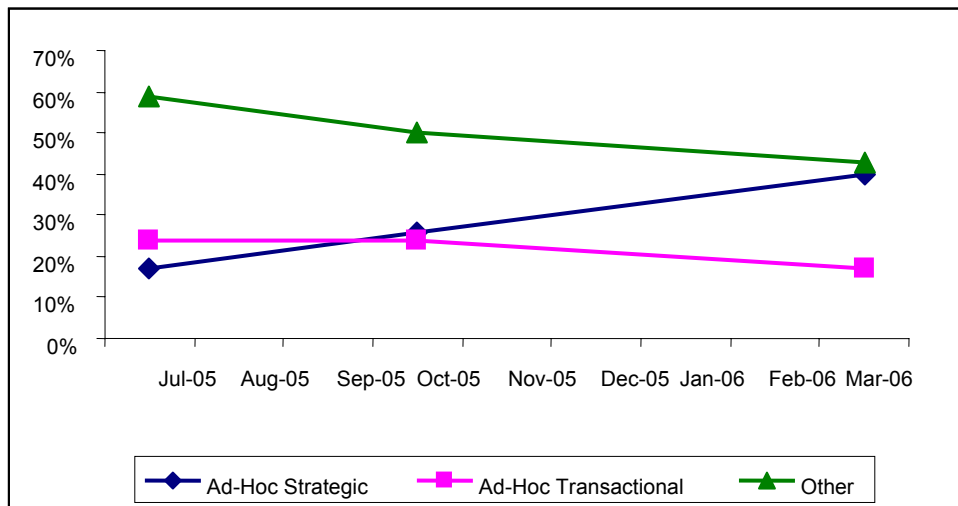
Note: "Other" refers to the following: supplier reviews, spend data, administration, paid time off, training, reporting.

Source: Aberdeen*Group*, June 2006

"We view (the tool) as an advantage for our group," the manager says. "You can pretty much do whatever you want to do."

And if your procurement organization wants to ─or *has* to ─become more strategic, this may be a good example to follow.

Chapter Four:
Recommendations for Action

Key Takeaways

- Automation is the lynchpin to a successful spend intelligence program. The goal for a spend intelligence program is the auto-classification of all spend data.

- Laggard and Industry Average enterprises must drive toward more automation of spend intelligence-gathering processes and standardize those processes at a level with which they're comfortable: company-wide or regionally.

- A Best in Class enterprise must strive for more detailed visibility into spend, with end-to-end spend intelligence software, either all in-house or combined with third-party provider services depending on its intelligence needs.

The ultimate goal for any enterprise spend intelligence program is auto-classification of all spend data. Therefore, automation is the lynchpin to a successful spend intelligence program. How that's done depends on the enterprise's spend intelligence needs. A fully in-house, end-to-end system could be beneficial if it gathers data daily or more frequently, needs easier data extraction, or deals with certain commodities whose prices fluctuate daily (e.g., oil, gold, wheat). Otherwise, third-party providers that offer particular services, such as data cleansing, may be able to relieve the enterprise of a burden if it has more expertise and can do the work cheaper and more efficiently than if the enterprise were to retain it.

Here are our recommendations for enterprises in each of the three components of Aberdeen's Competitive Framework:

Laggard and Industry Average Steps to Success

1) *Move toward more process automation.* Automation is critical to extracting more detailed, granular data on spend categories and vendors. An enterprise that has manual or partially automated processes should look to automate more.

2) *Strive for broader process standardization.* Aberdeen believes strongly that a centralized organizational and process approach delivers the best results. For the best results in spend intelligence, it's best to get everyone on the same page.

3) *Establish regular, rather than ad hoc, spend analyses.* Regular, programmed intelligence gathering provides more uniform, accurate insight into spend. For best results, aim for quarterly or more frequent analysis.

Best in Class Next Steps

1) *Move toward full automation, especially auto-classification of spend data.* The more spend intelligence "dirty work" you can leave to technology, the more opportunity your procurement organization has to focus on strategic initiatives. Consider third-party hosting of spend intelligence functionality, such as data cleansing, if you believe it can do the job better, if it's not critical to keep in-house, and if your analyses are not conducted daily or more often.

2) *Get as granular as you can on spend visibility.* Best in Class enterprises have above-average visibility at the category or commodity level. The more detail you can gather, the more informed you will be about company spend.

3) *Correct the data at the source.* Many enterprises that perform spend intelligence do not place the corrected information back into master data system (usually the ERP or e-procurement system). Thus, as new transactions occur (generating a new purchase order), the incorrect company name, as an example, needs to be cleansed again. If the master data were corrected, the new purchase order would use the correct company name. Some enterprises, for ease of adoption among users, do not want to change the company name; therefore, another practice is to allow the users to search for the "incorrect" name, but use a "real-time cleanse" during the transaction (requisition) to correct the name. In either case, the new transaction will have the correct information.

Steps to Success for All Enterprises

1) *Look toward vendors that know your industry.* To succeed at spend intelligence, it would help if you were to hook up ─ or at least consider ─ a solution provider that has some familiarity with your industry, especially the processes your procurement organization uses to conduct its work. For instance, the processes in a manufacturing company are different from those of a bank.

2) *Make sure the spend intelligence process is connected with more and more business processes*, such as sourcing, procurement (the obvious choices), contract management, compliance, and supplier performance.

3) *Focus on increased contract compliance as a goal:* One chief objective of a spend intelligence program must be improved contract management, where even Laggard enterprises reported improvements in contract compliance rates. Strong spend visibility can allow an enterprise to capitalize on opportunities to save more, gain favorable terms at renewal time, and find opportunities to consolidate spend.

4) *Utilize the newly cleansed data to determine price variances over time – per item and per vendor*. A strategic item/supplier can be further leveraged by utilizing time-based knowledge.

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Appendix A:
Research Methodology

I n May and June 2006, Aberdeen*Group* examined the spend analysis and spend intelligence goals, processes, experiences, and intentions of nearly 140 enterprises in several industries. Respondents, most of whom came from procurement groups, completed an online survey that included questions designed to determine the following:

- The key factors influencing the development of spend intelligence programs and the strategic actions enterprises were taking to develop those programs;

- The processes, organizational structures, and technology use involved in the generation of spend intelligence;

- Current and planned use of automation to aid these activities; and

- The benefits, if any, that enterprises have derived from spend intelligence initiatives.

Aberdeen supplemented this online survey effort with telephone interviews with select survey respondents, gathering additional information on spend intelligence management strategies, experiences, and results.

The study aimed to identify emerging best practices for spend intelligence and provide a framework by which readers could assess their own spend intelligence capabilities.

Responding enterprises included the following:

- ***Job title/function****:* The research sample included respondents with the following job titles: procurement, supply chain, logistics executive or other business unit manager (38%); director (18%); internal consultant (11%); staff-level professional (10%); senior vice president (8%); CEO, CFO or, other C-level officer (7%), CIO/IT leader (3%); and Other (5%).

- ***Industry****:* The research sample included respondents mostly from manufacturing industries, with representation from the following: automotive (4%), chemicals (6%), construction/architecture/engineering (5%), consumer packaged goods food/beverage, industrial equipment manufacturing, mining/oil/gas, metals and metal products, and pharmaceutical manufacturing (4% each). Others included high technology/software (9%), public sector (8%), health/medical/dental services (8%), utilities (5%), and finance/banking/accounting (4%). Other sectors responding included distribution, education, wholesale, transportation/logistics, retail, and telecommunications services.

- ***Geography****:* Most respondents ─ 65% ─ were from North America. Remaining respondents were from Europe (26), Asia-Pacific (8%), and the Middle East/Africa (1%).

- ***Company size****:* Most of the respondents ─ 62% ─ were from large enterprises (annual revenues above US$1 billion); 27% were from midsize enterprises (annual revenues between $50 million and $1 billion); and 12% were from small businesses (annual revenues of $50 million or less).

Solution providers recognized as sponsors of this report were solicited after the fact and had no substantive influence on the direction of *The Spend Intelligence Benchmark Report*. Their sponsorship has made it possible for Aberdeen*Group* to make these findings available to readers at no charge.

Table 6: PACE Framework

PACE Key
Aberdeen applies a methodology to benchmark research that evaluates the business pressures, actions, capabilities, and enablers (PACE) that indicate corporate behavior in specific business processes. These terms are defined as follows: *Pressures* — external forces that impact an organization's market position, competitiveness, or business operations (e.g., economic, political and regulatory, technology, changing customer preferences, competitive)   *Actions* — the strategic approaches that an organization takes in response to industry pressures (e.g., align the corporate business model to leverage industry opportunities, such as product/service strategy, target markets, financial strategy, go-to-market, and sales strategy)   *Capabilities* — the business process competencies required to execute corporate strategy (e.g., skilled people, brand, market positioning, viable products/services, ecosystem partners, financing)   *Enablers* — the key functionality of technology solutions required to support the organization's enabling business practices (e.g., development platform, applications, network connectivity, user interface, training and support, partner interfaces, data cleansing, and management)

Source: Aberdeen*Group*, June 2006

Table 7: Relationship between PACE and Competitive Framework

PACE and Competitive Framework How They Interact
Aberdeen research indicates that companies that identify the most impactful pressures and take the most transformational and effective actions are most likely to achieve superior performance. The level of competitive performance that a company achieves is strongly determined by the PACE choices that they make and how well they execute.

Source: Aberdeen*Group*, June 2006

Appendix B:
Related Aberdeen Research & Tools

Related Aberdeen research that forms a companion or reference to this report include:

- *The Supplier Enablement Benchmark Report* (March 2006)
- *The Direct Materials Sourcing Benchmark Report* (March 2006)
- *The CPO's Agenda: Strategies for Procurement Transformation* (March 2005)
- *Best Practices in Spending Analysis* (September 2004)

Information on these and any other Aberdeen publications can be found at www.Aberdeen.com.

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