

Raising the World-Class Bar in Procurement Through Digital Transformation

By Laura Gibbons, Christopher S. Sawchuk and Srinivasa Rao Dabbera

Executive Summary

World-class procurement organizations remain highly focused on achieving optimal performance. The Hackett Group's 2018 analysis of its procurement benchmarking database quantified the performance advantage of these organizations, which include 21% lower labor costs and 29% fewer full-time equivalent staff than more typical organizations (i.e., the peer group). Technology has always played an important role in enabling world-class performance, but procurement is now at an inflection point: World-class organizations can continue to reduce costs by embracing digital technology, while the peer group can leverage the same technology to catch up faster at less cost.

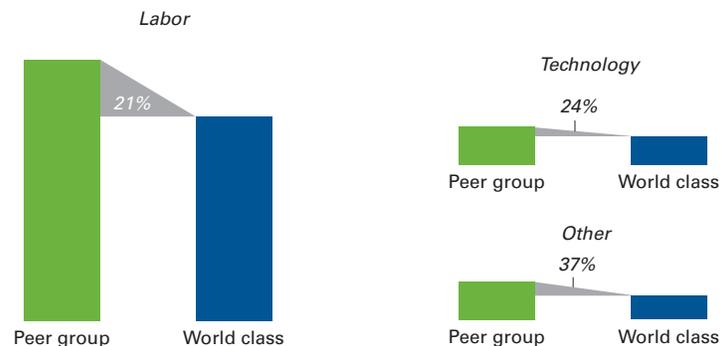
The World-Class Performance Advantage

World-class procurement organizations outperform more typical companies in our benchmark and research database (which in our empirical methodology we designate as the "peer group") on two important dimensions:

1. They are more efficient, operating with 21% lower labor cost (Fig. 1).
2. They are more effective at delivering services to internal and external customers, requiring 29% fewer full-time equivalents (FTEs) to do so (Fig. 2).

As for the first point, by standardizing and automating routine tasks, they lower the cost of many activities. As regards the second, the world-class group continues to significantly outperform the peer group in service delivery productivity. In combination, for a typical company with \$10 billion in revenue, attaining world-class performance in procurement represents as much as \$6 million in potential savings annually.

FIG. 1 Procurement cost as a percentage of annual spend



Source: The Hackett Group, 2018

Digital transformation defined

The Hackett Group defines business services digital transformation as “improving customer experiences, operational efficiency and agility by fundamentally changing the way business services are delivered, using digital technologies as the enabler of holistic transformation.”

Digital transformation differs from previous approaches to technology-enabled change in the following ways:

- Digital transformation creates new ways of doing things:** In the past, technology-enabled change was mainly aimed at replacing manual processes and making them faster and more efficient. While the push to reduce cost and increase efficiency is ongoing, as we move into the digital era, technologies like predictive analytics, social media, robotic process automation (RPA) and artificial intelligence (AI) are not only changing the speed and efficiency of processes but creating entirely new avenues for doing things.
- Digital transformation is customer-centric:** Past technology-driven transformations automated processes within and between enterprises. In contrast, digital transformation uses technology to engage internal and external customers through interactive cloud-based tools and portals to provide better service to stakeholders, and to leverage big data and predictive analytics for better, faster insight.
- Digital transformation increases the velocity of change:** Not only have the speed and nature of technological change accelerated as new types and combinations of technologies are launched at a fast pace, but the speed of adoption has also risen dramatically. Today, companies pilot and adopt new tools in a matter of weeks and months, not years

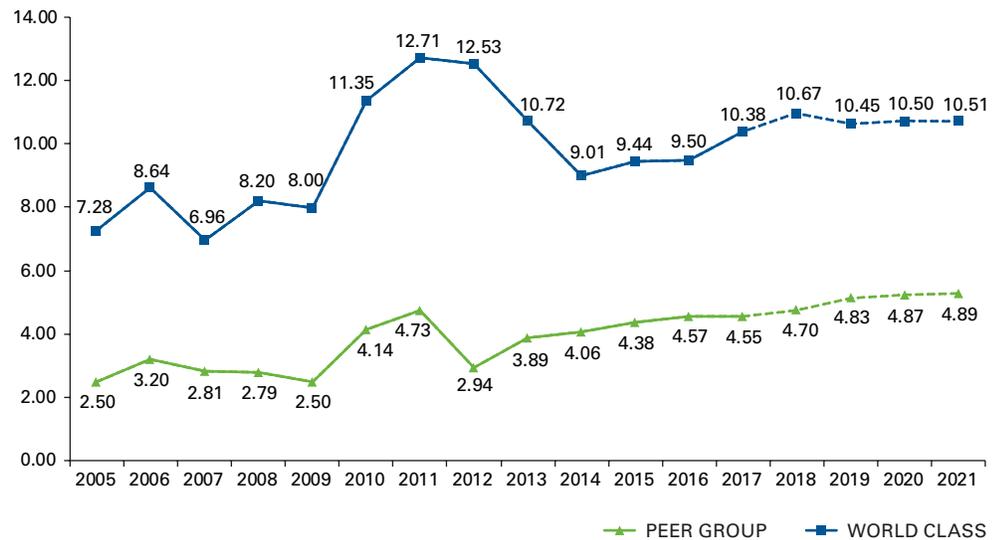
FIG. 2 FTEs per US\$ billion of spend



Source: : The Hackett Group, 2018

World-class procurement groups also have a significantly higher ROI (i.e., the ratio of total savings generated by procurement to its total operating cost) – a 10.7X payback on investment in procurement, compared to 4.7X for peer-group companies (Fig. 3). However, even the world-class group is losing ground. Cost reductions and savings are forecasted to level out in coming years, making it necessary to find new ways to continue to unearth value.

FIG. 3 The ROI of world-class procurement

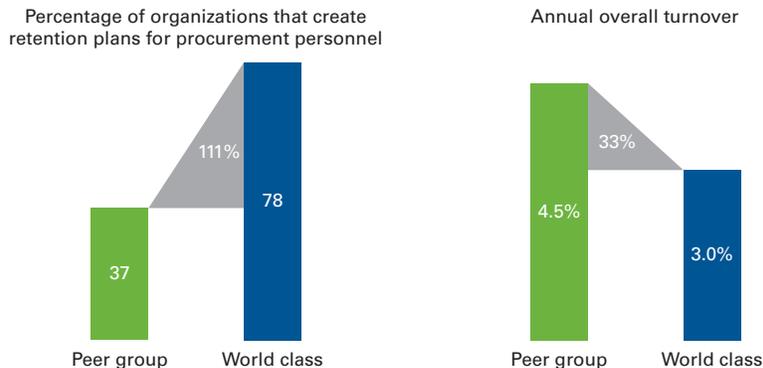


Source: The Hackett Group, 2018

In addition to a higher ROI, world-class organizations are more effective than the peer group in how they operate and deliver services. For example, the percentage of transactions requiring post-issuance activity (to resolve discrepancies in areas like order quantity, quality and pricing) is often two to three times less. Fewer errors means higher-quality process execution across the board. These differences have real bottom-line impact: The high number of transactions for some processes and the cost to correct errors brings the cost gap between world-class and peer organizations into the millions of dollars.

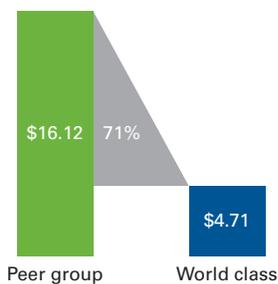
Also, the higher degree of talent-retention planning and lower turnover rates illustrate the ability of world-class procurement to influence business performance (Fig. 4). This is a sign of organizational health, in that people are being developed and given opportunities for professional growth. A benefit of lower turnover is the retention of organizational knowledge. Plus, higher retention not only saves costs but shows that world-class organizations are better at fitting new hires with job requirements and delivering an employee experience that matches the expectations of recent joiners.

FIG. 4 Retention planning and turnover levels



Source: The Hackett Group, 2018

FIG. 5 Cost per order



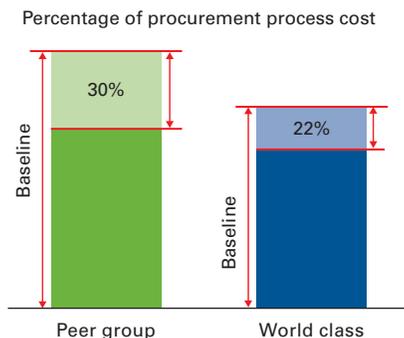
Source: The Hackett Group, 2018

The Digital Transformation Imperative

Cloud-based infrastructure and applications, virtual business and technology networks, and business analytics are converging with employees and consumers who are increasingly comfortable with new mobile technologies and business models. This has created tremendous opportunities for procurement organizations to apply digital technologies to transform service delivery. Increasingly, digital technology is the platform for delivering a whole new class of services, such as predictive analytics to guide decisions. Moreover, digitally enabled processes reduce errors and make information easier to access. In fact, companies that have invested in digital technologies are 56% more likely to be viewed as a valued business partner.

Technology costs per procurement FTE in world-class organizations is typically higher than in the peer group, reflecting greater investments in areas such as process automation. These in turn deliver productivity advantages. For example, the cost per order at world-class procurement groups is 69% lower than that of the peer group (Fig. 5). More important, extensive use of automation allows procurement staff to devote a greater part of their day to talent development and activities that boost business performance.

FIG. 6 Process cost reduction attributed to digital transformation



Source: The Hackett Group, 2018

Raising the Bar on Performance

Delving into our 2018 benchmark database, we calculated the savings benefit that world-class procurement organizations have over the peer group. We found that digital transformation enables typical procurement organizations to reduce process costs by 30%, and world-class procurement organizations by 22%. This means that digital transformation can more than close the cost gap between the two comparison groups (Fig. 6), implying that even world-class procurement organizations are not operating at the lowest achievable cost level.

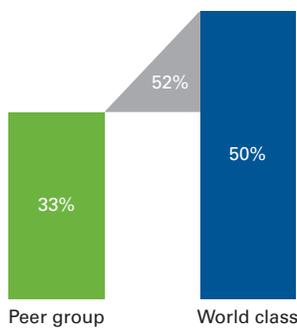
Although achieving world-class performance can take five or more years, companies are likely to see marked improvements after just two years. Those that continuously pursue change have much to gain. First, new technologies will dramatically accelerate the pace at which the peer group can approach world-class performance levels. Second, new digital tools will enable world-class procurement organizations to further improve their performance (measured by cost) by at least 22%, allowing them to break through a cost plateau that has lasted for several years.

While digital transformation will create huge opportunities for performance improvement, this is not to say companies can abandon their ERPs and technology landscape rationalizations. Nor will technology alone deliver these results. The new procurement transformation model relies on technology to lead the way, but it must fit within a larger strategy, one based on a well-designed service delivery model that includes not just technology but processes, information, talent and organization redesign. The new digital technologies (e.g., cloud, mobile, RPA, analytics) at its core will allow procurement to significantly accelerate headcount reductions. It may use the resulting savings to fund more technology investment, while redeploying or hiring new resources for higher-value activities.

Six Digital Accelerators

Below are the top imperatives for improving procurement’s performance and supporting the business strategy over the long term.

FIG. 7 Percentage of procurement organizations with formal SLAs for internal customers



Source: The Hackett Group, 2018

Accelerator #1: Digital engagement

World-class organizations are service-oriented and customer-centric in their approach to procurement delivery. They actively measure the results of their efforts through formal service level agreements for internal customers (Fig. 7).

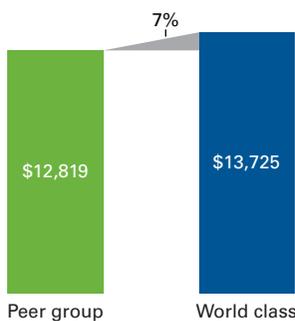
The result is a far better customer experience, leading to higher digital engagement levels. Self-service is a prime example of the difference this approach can make. Most self-service is designed to render processes more efficient, rather than enable the user to be more productive. World-class procurement organizations report high usage of both employee and manager self-service, largely because they create these offerings with the customer experience in mind.

Accelerator #2: Robotic process automation

RPA has made a quick entry onto the agenda of procurement and purchase-to-pay organizations to perform routine activities without human intervention. In procurement, 38% of companies are currently in the piloting stage, indicating rapid adoption. Assuming widespread adoption of RPA continues, many procurement organizations believe it will become one of the areas with the greatest impact on the way their work gets done in the next decade.

It is not the specific business process that determines a good candidate for RPA, but rather the characteristics of the process, such as the need for data extraction, enrichment and validation. Activities requiring integration of multiple screens as well as self-service inquiry resolution are also ripe for RPA. The key is that RPA is best deployed in a stable environment where no changes to processes are on the horizon.

FIG. 8 Annual technology cost per FTE



Source: The Hackett Group, 2018

Accelerator #3: Analytics-driven insight

The hallmarks of information-centric, world-class procurement organizations are the presence of a sophisticated information/data architecture that makes effective data analysis possible; planning and analysis capability that is dynamic and information-driven; and performance measurement that is aligned with the business.

World-class procurement organizations spend 7% more on technology per FTE (Fig. 8) and invest a greater proportion of their budget than the peer group on systems and tools to enable analytics capability. Without an advanced information management capability, agility is impossible. Agile operations require a “sensory” system that monitors external conditions, plus analytical capabilities that comprehend this data within the business context. This flow of feedback information is the basis for business decision-making.

Accelerator #4: Modern digital architecture

Results from recent Hackett Group research on the benefits of various software tools are encouraging. In the case of supplier discovery software, the top benefit found was a reduction of up to 31% in the time it takes to find and qualify a new supplier. This is due to the use of system-recommended suppliers based on pre-defined criteria and preferences; faster searches based on specific documentation; product and service requirements; and having access to rankings and feedback about suppliers from other companies.

The research also documented the benefits of e-sourcing software, including the ability to reduce overall cycle time by 30% by using standard templates to reduce data-collection errors. The reported benefits of contract lifecycle management (CLM) software include reducing the amount of time required to find a contract by 52%, trimming the number of lapsed contracts by 39%, and increasing the use of standard terms and conditions to ensure compliance.

Accelerator #5: Digital workforce enablement

Procurement can leverage modes of communication that appeal to a new generation of workers to create a culture of collaboration and speed up work processes. For example, many world-class organizations have launched social media initiatives and other web-centric spaces to facilitate broad communication. Tools such as Yammer, a Facebook-like application designed for use within a single organization, let users crowdsource answers and obtain information, often faster than via traditional means such as phone calls or email.

Accelerator #6: Cognitive computing

Cognitive computing and artificial intelligence (which seek to mimic the way the human brain works) are in their nascent stages but are starting to help some procurement organizations run models, make predictions and analyze large data sets. For example, a consumer goods company has been relying on a cognitive tool used by a third party to gather data from social networks worldwide to make predictions about potential trouble spots. The tool looks for the number and frequency of posts based on certain keywords; then, using cognitive computing, calculates an intensity level for each topic and combines historical data to predict the likelihood of specific events (e.g., a coup or economic slowdown) to help the company optimize its sourcing decisions.

Getting Started With Digital Transformation

Traditionally, procurement transformations began with process redesign, and only later identified the right technologies to enable the new processes. Digital transformation turns this model on its head by first looking for opportunities to use new technologies. Then they are used to create new processes that are customer-centric and efficient, and permit step changes in performance.

Rather than undertaking a single, giant transformation project, digital adopters start with individual, well-defined initiatives. They look at areas where there are opportunities for improvement and select technologies that can bring about change, such as cost savings and new sources of revenue.

To succeed, procurement organizations must embrace the principle of continuous improvement. They must be ready to fail and try again. Digital technologies evolve quickly, so what may not work today may work tomorrow. Companies must continuously scan the market for new ideas and solutions to test, implement and scale, before moving on to another area in need of improvement. Stasis is not an option.

About the Advisors

Laura Gibbons

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Ms. Gibbons has industry and consulting experience in areas such as purchase-to-pay, strategic sourcing, payment strategies, manufacturing operations, economic impact analysis, and organizational and process design. She previously worked in The Hackett Group's Strategy & Operations consulting practice, where she specialized in sourcing, procurement and supply chain. Before joining The Hackett Group, Ms. Gibbons served as Strategy & Operations Associate at Groupon.

Christopher S. Sawchuk

Principal & Global Procurement Advisory Practice Leader



Mr. Sawchuk has over 20 years of experience in supply management, working directly with Fortune 500 and mid-sized companies around the globe and in a variety of industries to improve all aspects of supply management, including process redesign, technology enablement, operations strategy planning, organizational change and strategic sourcing. Mr. Sawchuk specializes in working directly with CPOs to help define a long-term strategy. He has been recognized by *Supply & Demand Chain Executive* magazine as one of its "Pros to Know." Mr. Sawchuk's background includes engineering and operations roles with both United Technologies and IBM.

Srinivasa Rao Dabbera

Director, Quantitative Analysis



Mr. Dabbera has over 15 years of experience in business analytics applications and quantitative research. In addition to managing the company's quantitative analysis team, Mr. Dabbera's primary responsibilities include converting, analyzing and interpreting data from benchmarking surveys, performance studies and other research into insights that are applied to solve clients' process and performance challenges. He works closely with The Hackett Group's benchmarking, advisory and research teams to respond to inquiries from members. His experience spans across the general and administrative domain. Previously, Mr. Dabbera held a variety of analyst roles with a leading market research company and management consulting company.

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