THE IMPACT OF **INDIRECT SPEND** ON **WORKING CAPITAL**

TOOLS AND STRATEGIES TO IMPROVE VISIBILITY AND BETTER MANAGE PURCHASING

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MOST SENIOR FINANCE EXECUTIVES BELIEVE that they have a fairly solid grasp on their company's indirect spend, which includes office supplies, professional services, warehouse management services, and other expenditures that keep the business running. After all, they are the fiscal monitors of their organizations.

In reality, there are often expenditures that fall outside of the normal procurement processes — sometimes referred to as "dark purchasing." Most of the dark purchasing occurs in the indirect spend category, and the lack of attention to this purchasing "channel" adds to the challenge of optimizing working capital.

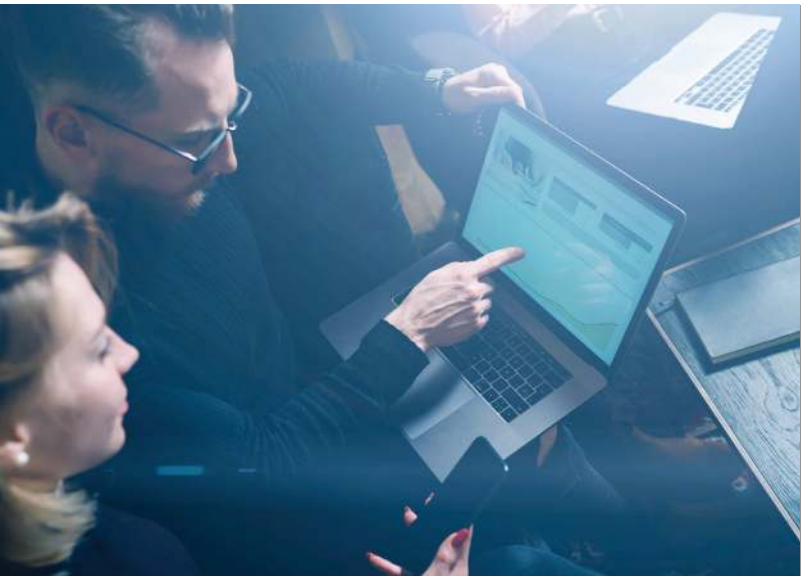
While many companies seek to gain greater governance and better insight into purchasing trends, the fact is that a billion-dollar company will waste about $15 million annually due to a lack of control over its procurement processes, according to Accenture's *Getting a Grip on Tail Spend* report.

This white paper explores ways to improve working capital efficiency by gaining control over indirect spend. Topics include:

- **Signs that your indirect spend processes are harming your working capital position**
- **Identifying the "hidden" expenses and developing a plan to avoid them**
- **How consolidated data and processes can reduce companies' spend management discrepancies and streamline processes**
- **Leveraging vendor relationships to save money without relying on yearly rebates**
- **A look to the future of indirect spend strategies**

THE LINK BETWEEN INDIRECT SPEND AND WORKING CAPITAL

ONE-QUARTER OF RESPONDENTS to The Hackett Group's *2018 Key Issues Study* say that deepening procurement's influence on complex indirect spend categories is a critically important driving value beyond sourcing. Better working capital management is an important goal of deploying more efficient procurement processes.



There are a number of telltale signs that the inability to effectively manage indirect spend is impacting your organization's working capital management, but among the most disconcerting is not knowing how much is being spent and having an incomplete forecast of future outlays. "If you don't have a good handle on what you are spending, and don't have a clear idea as to what you'll be spending in the future, you don't have a good grasp of your working capital," said Sean Bliss, Vice President of Business Development, Indirect Spend and Material Handling for Corcentric, a leading provider of procurement and finance solutions.

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Finance chiefs may be under the impression that their company is spending a small amount in one area, for example, and will budget for those expenses accordingly. However, when they dig in to the numbers, they're spending more — sometimes tens of thousands of dollars more — than they thought they were, Bliss noted.

Vendor rebates can also be at the root of unexpected spending. There is a tendency to focus on quarterly or annual rebates when negotiating with vendors, rather than on upfront pricing, a strategy that can encourage overspending to achieve higher rebates. "In this scenario, you end up focusing on supplier incentives, which is good for the supplier, rather than what's important to your business," Bliss said.

Whatever the cause, poor indirect spend management results in ineffective working capital management and the inability to fund future initiatives to grow the business. "You need enough working capital on hand to take advantage of opportunities as they arise and to be innovative," Bliss noted.

BRING SPENDING OUT OF THE SHADOWS

EVEN AT COMPANIES WITH TIGHT CONTROLS over their indirect spend, there will inevitably be expenses that bypass the normal procurement process. These "hidden" expenses often require more resources to process, as they are less likely to rely on digitized documentation that allows for greater accuracy and agility with suppliers and vendors.

"Expenses that fall outside of the normal channel can be fragmented across hundreds of suppliers and involve a disproportionate amount of time and resources to manage," according to Bliss.

How do you bring hidden spending out of the shadows? Bliss suggests a simple first step: Examine a year's worth of spending and sort the expenses from highest to lowest dollar amount. In a typical procurement environment, 80 percent of spending is being done with the top 100 or so vendors through established procurement processes. This exercise will shine a light on the other 20 percent, which includes one-off or under-the-radar expenses that can be better managed or consolidated among various offices.

Bliss noted that it is virtually impossible to put every expense through an established procurement pipeline, but significantly reducing the amount of spending outside of the normal process can yield significant results. According to a September 2016 report from *Supply Chain Quarterly,* companies can save up to 25 percent by eliminating dark purchasing with tools to improve control and visibility.

PROCUREMENT LEADERS CAN HELP **REDUCE COSTS BY 7 PERCENT ON AVERAGE** BY MORE EFFECTIVELY HANDLING TAIL SPEND.

— THE HACKETT GROUP

The Hackett Group estimates that by more effectively managing tail spend — which it defines as purchases that are too small, too infrequent, or not strategic enough to go through a full strategic sourcing process — procurement leaders can help reduce costs by 7 percent on average. Managing tail spend is a way for procurement to increase its influence on, or involvement in, the company's purchasing.

"Categories where you have a lot of suppliers indicate that these areas are not well sourced and reflect buying at the last minute, rather than making more considered purchases. These are areas of opportunity."
Marisa Brown, Senior Principal Research Lead, Supply Chain Management for APQC, a non-profit benchmarking organization, emphasized that companies need to develop policies to curtail maverick spending and enforce the penalties for going outside of the standard procurement processes.

According to APQC's research, only 43 percent of organizations have extensively documented consequences for applying noncompliant sourcing processes. In addition, only 41 percent enforce the consequences to a very great extent. "It's unfortunate that more organizations don't enforce these consequences. Those that take this essential step have lower costs and need fewer employees for procurement," said Brown.

LEVERAGING AUTOMATION TO IMPROVE DATA AND VENDOR RELATIONSHIPS

MORE THAN THREE-QUARTERS (76 percent) of organizations ranked measuring and managing procurement performance and business value as high/critical in importance, according to The Hackett Group's *2018 Key Issues Survey.* However, only slightly more than half (56 percent) believe they have the ability to address the challenge.

While resources are tight, automating as much of the procurement process as possible is essential to improving working capital management. Rogue spending takes much more time to manage, as there are no established invoicing and payment processes (unlike those that would normally be applied to purchases that go through the standard procurement channels).

Unwieldy procurement processes cost time and money. Processing multiple payments to multiple suppliers multiple times in a billing period diverts resources from more strategic activities. "Automation enhances visibility, and if you've got visibility, you can make determinations regarding demand and do a better job of budgeting," said Reggie Peterson, Director, Indirect Supply Programs, Corcentric.

Without visibility into spending, there is no ability to control it. A company may be buying office supplies from several different vendors across many different locations, but if there is not clear visibility to the line-item data associated with these purchases, finance doesn't have insight into organization-wide spending. The result: a lack of data to negotiate volume discounts, and money left on the table.

Data ultimately bolsters an organization's ability to negotiate better upfront pricing with vendors, rather than relying on year-end rebates. "Regular reviews and meetings with vendors open up communication and highlight the value of the relationship beyond rebate incentives," Corcentric's Peterson added.

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CONCLUSION: **DON'T DERAIL CASH MANAGEMENT PLANS WITH POOR INDIRECT SPEND MANAGEMENT**

No matter how adept your organization is at purchasing, there will always be a segment of the indirect spend category that doesn't flow through the normal procurement process. The challenge is to minimize the rogue spending by funneling as much as possible through approved vendors and established workflows.

More tightly controlled indirect spend will result in a healthier balance sheet, providing the company with sufficient working capital to invest in the future and rapidly respond to changes in the marketplace.

There are always challenges to reining in indirect spending. It can be difficult to identify spending that occurs outside of the standard procurement workflow, which leads to less accurate cash forecasts due to unexpected expenses. One major hurdle is that many organizations have yet to invest in the tools to improve their indirect spend management. According to a recent AmeriQuest survey, 71 percent of organizations surveyed lack an e-procurement solution.

Clearly, there are opportunities to strengthen and automate the procurement process in ways that will have a positive effect on the company's cash position. The move toward robotics and artificial intelligence to complete many routine tasks is just the beginning of the digital transformation that is underway, and CFOs are poised to lead the charge.

KEY TAKEAWAYS:

- Organizations that don't get a handle on their indirect spend experience significant waste in terms of resources and lost opportunities to consolidate purchases, putting their ability to fund future projects at risk.
- Automation provides visibility into indirect spending, enabling organizations to leverage their relationships with vendors beyond seeking year-end discounts.
- Progressive CFOs recognize that a collaborative, automated effort to streamline indirect spend can boost their cash position and help them broaden their scope of influence among business unit and firm management.

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ABOUT CORCENTRIC

Corcentric is a leading provider of procurement and finance solutions that transform how companies purchase, pay, and get paid. Corcentric's procurement, accounts payable, and accounts receivable solutions empower companies to spend smarter, optimize cash flow, and drive profitability. Since 1996, more than 6,000 customers from the middle market to the Fortune 1000 have used Corcentric to unlock new potential within their enterprise.

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