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The CFO's View of Procurement

Work in Progress

November 2009

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Executive Summary

The go-go 1990s, with its fast money and flush credit seeking rapid and steep returns, created the demand for "renaissance" Chief Financial Officers (CFO), who could manage (and market) both the strategic and financial operations of the enterprise. The more sobering decade that followed led directly to the creation and subsequent rise of the Chief Procurement Officer (CPO), who could reduce costs, build internal relationships, and develop strategic suppliers efficiently and effectively. This report looks at the relationship of these two executives through the eyes of the financial and procurement professionals who work for them.

Research Benchmark

Aberdeen's Research Benchmarks provide an in-depth and comprehensive look into process, procedure, methodologies, and technologies with best practice identification and actionable recommendations

Best-in-Class Performance

Aberdeen evaluated 176 finance and procurement professionals in October and November of 2009 to determine the view or perspective that the finance leadership within the average enterprise has of its procurement counterparts. Aberdeen distinguished Best-in-Class enterprises by the following two key performance criteria: percentage of spend under management and the level of contract compliance. Best-in-Class enterprises in this study are notable for their superior performance and for their ability to manage enterprise spend more efficiently and more effectively. They also:

- Reflect (or book) **73% more**, on average, of their identified savings in their budgets
- Have department operating costs that are, on average, **23.6% lower** than their peers

Spend Under Management

The classic measure of procurement's impact upon an enterprise is the percentage of all non-payroll, tax, tariff and fee-related spend that falls under management of this group, what is commonly referred to as ***spend under management***. Aberdeen research has shown that enterprises have been able to achieve a 5% to 20% cost savings for each new dollar of spend brought under management.

Competitive Maturity Assessment

The enterprises enjoying Best-in-Class performance shared several common characteristics with respect to the alignment between procurement and finance particularly in the areas of compliance management and reporting. These top-performing enterprises were:

- **79% more likely** to utilize contract lifecycle management solutions
- **59% more likely** to utilize an automated spend analysis solution

Required Actions

In addition to the specific recommendations in Chapter Three of this report, to achieve Best-in-Class performance, CFOs should:

- Appoint a CPO if one does not exist, then provide a mandate and demand accountability
- Use influence to drive more spend under management of the procurement department
- Identify, define, and track a set of procurement performance metrics that are directly aligned with top enterprise goals

"Our savings process is very informal and we do not have much confidence in it due to procurement's lack of spend visibility and our inability to confirm contract compliance."

~ VP, Finance, Manufacturing Industry, United States

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Chapter One: Benchmarking the Best-in-Class

CPOs: "Best of the Decade"

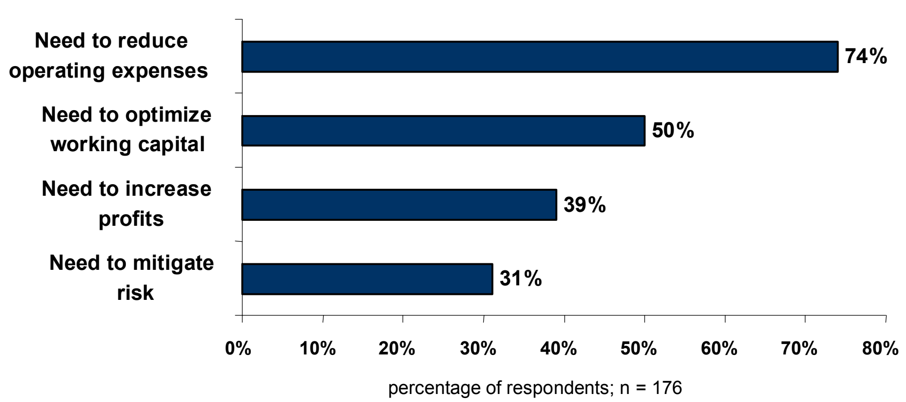
In aggregate, the first decade of the new millennium has been a difficult and sobering one for the citizens of the world. Many bedrock institutions ceased to exist, while certain others hang on for dear life; others still, remain in quiet disrepair. The level of fear, uncertainty, and doubt that has seeped into many aspects of the personal and professional lives of the global worker is a trend unchecked. The unraveling of an earlier age has begun. But the end of *this* age is not the "end of *the* age." And while certain business dynamics and points of reference are forever altered, the global resiliency and strength that were challenged early and often in the 2000s, may yet, define this new chapter.

One business dynamic that has changed significantly, if not dramatically, is the way that the procurement function within many (but not all) enterprises is managed. This decade has witnessed first-hand the broad transformation of the procurement function from tactical back-office department to a strategic function that can deliver strategic value across a wide-range of areas and is worthy of a "C-level" leader. While events in business history have placed procurement at the hub of business process and at the core of business profits, it was not until this decade where the creation and subsequent rise of the Chief Procurement Officer (CPO) began to significantly alter the view of procurement within and beyond the enterprise. But as this report shows (and a decade of Aberdeen research focused on procurement and supply management has shown), procurement is just scratching the surface of what it may some day realize.

CFO & CPO – Aligned on Pressures

Aberdeen's *CPO's Agenda 2009: Smart Strategies for Tough Times* published in April, highlighted the fact that the top pressure on the CPO (**91%**) to reduce costs is at the highest levels in more than a decade.

Figure 1: Top Pressures for CFOs



Source: Aberdeen Group, November 2009

Fast Facts

- √ **78%** of CFOs indicated that procurement has a positive impact on the enterprise's competitive position
- √ Roughly **one-third** of all CPOs report to the CFO (more than twice any other job role)

CFO Top Priority for 2010

"Cash management and liquidity improvement."

~ CFO, Metals Industry, United States

"Invest in procurement, contingent labor, and accounting systems. Develop a best in class operation regarding procurement and align that initiative with finance."

~ CFO, Financial Services Industry, Canada

"Regaining capacity for borrowing."

~ CFO, Utility Industry, Asia-Pacific

"Remaining EBITDA and cash flow positive."

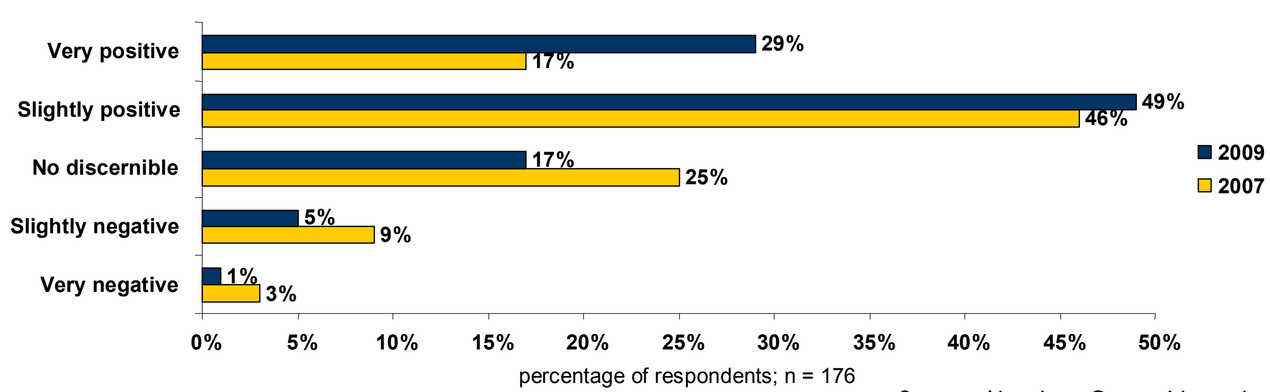
~ CFO Media/Entertainment Industry, United States

In an environment where revenue growth is unlikely if not impossible, enterprises have increasingly focused on what they can, in fact, control. Therefore, it is no surprise that cost containment is also the highest priority for the CFO (**74%**) since the dollars saved improve cash positions and the bottom-line. This situational alignment has worked to the benefit of both the CFO and CPO, as described in the section to follow.

Competitive Positioning

While some enterprises have long utilized procurement strategies and processes to their advantage on the business battlefield, the recent global recession has served to more closely align the goals and objectives of the CFO with those of the CPO. As discussed in the CPO's Agenda 2009: Smart Strategies for Tough Times, two-thirds of procurement executives believe that the economic downturn has positively impacted the role of the CPO within the enterprise research. And, as Figure 2 shows, 78% of CFOs now view the impact that procurement has on the enterprise's competitive position as positive. In fact, CFOs in 2009 are 71% more likely to view the CPO as having a "very positive" impact on competitiveness than a CFO in 2007. One of the clearest examples of this trend has been the increasing number of CEOs and CFOs of publicly traded companies who have highlighted their internal cost / efficiency initiatives (to investors, analysts and the general public) as a top priority and then worked to frame the near-term "success" of their operations in that context. Aberdeen expects this trend to continue into the next decade because despite the muted optimism expressed by many executives that the worst is behind us, the announcement of new cost containment initiatives has been a regular occurrence in the fall of 2009.

Figure 2: Procurement's Impact on Competitiveness



Source: Aberdeen Group, November 2009

The Maturity Class Framework

Aberdeen evaluated 176 finance and procurement professionals in October and November of 2009 to determine the view or perspective that finance leadership within the average enterprise has of its procurement function. Aberdeen distinguished Best-in-Class enterprises by the following two key performance criteria: (1) the percentage of spend under management and (2) contract compliance (% of spend that is compliant to contracts). Spend under management (see sidebar for definition) has been, and will continue to be, a primary metric used by Aberdeen to define and discern Best-in-Class procurement performance from all others. In Aberdeen's view, spend under management is an important metric to utilize because it represents the opportunity that procurement has to impact an enterprise. Certainly, managing a high percentage of spend does not in and of itself guarantee efficient or effective management; but, over years of benchmarking thousands of procurement departments, Aberdeen has identified a high correlation between high percentages of this metric and high performance in other KPIs. Aberdeen research has also shown that the average benefit of bringing one new dollar of spend under the management is between 5% and 20%.

The Cost of Non-Compliance to Contracts

Aberdeen research has shown that the average additional cost for every dollar spent that is not compliant to a supplier contract or agreement is 22%.

Table 1: Top Performers Earn Best-in-Class Status

Definition of Maturity Class	Mean Class Performance
Best-in-Class: Top 20% of aggregate performance scorers	▪ **85%** of spend under management ▪ **81%** contract compliance
Industry Average: Middle 50% of aggregate performance scorers	▪ **59%** of spend under management ▪ **55%** contract compliance
Laggard: Bottom 30% of aggregate performance scorers	▪ **26.7%** of spend under management ▪ **15%** contract compliance

Source: Aberdeen Group, November 2009

The reasons for poor compliance start with an inability to manage or impact enterprise spend but also include an inability to communicate negotiated agreements to key stakeholders and an insufficient technology infrastructure to store and retrieve contracts, as well as and track purchases (and invoices) made against them. One other key inhibitor to effective contract compliance is the fact that, in many enterprises, procurement lacks the respect and mandate to drive supplier implementations and restrict and penalize maverick buying behavior.

The Best-in-Class PACE Model

Aberdeen has shown that there is a clear relationship between the pressures companies identify and the actions they take, and their subsequent competitive performance. All participants should examine their prioritized Pressures, Actions, Capabilities, and Enablers (PACE) selections

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and determine whether there are valuable perspectives to be gleaned by comparison with the PACE priorities of Best-in-Class companies (Table2).

Table 2: The Best-in-Class PACE Framework

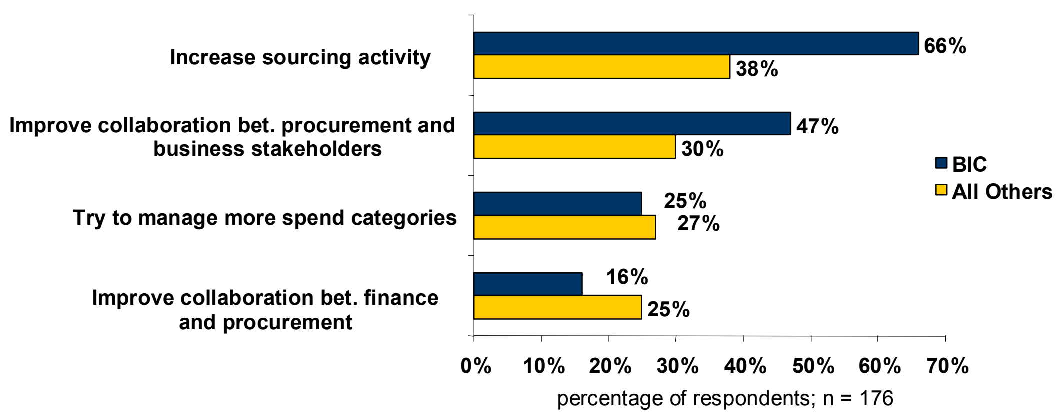
Pressures (Finance)	Actions (Procurement)	Capabilities (Procurement)	Enablers (Procurement)
▪ Need to reduce operating expenses	▪ Increase sourcing activity ▪ Improve collaboration with line of business	▪ Supplier negotiation and contracting ▪ Ability to manage spend ▪ Enterprise-level communication	▪ Spend analysis ▪ Supplier performance measurement ▪ E-procurement ▪ Complex category management solutions (i.e. travel, print, contingent labor)

Source: Aberdeen Group, November 2009

Best-in-Class Strategies

Given the need to reduce costs, it is no surprise to see an increase in sourcing activity tops the list of planned actions to be taken by all procurement departments (Figure 3). The precipitous fall in the price of most commodities and services (from their peaks in the late 2007 – early 2008 timeframe) presented a window of opportunity for enterprises to negotiate new contracts and revisit contracts that had been awarded near the top of the market. As commodity pricing has recovered (i.e. increased), the potential total opportunity to reduce costs has diminished.

Figure 3: CPO Strategic Actions by Maturity Class



Source: Aberdeen Group, November 2009

This means that although re-sourcing categories may continue to deliver savings, the returns from these efforts are likely to be diminishing as markets continue to recover. One of the best opportunities to continue the momentum of a large sourcing initiative is to expand the program's sourcing pipeline with new categories that have never previously been sourced. The

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Best-in-Class that have prioritized sourcing to a greater degree have also made it a priority of much greater magnitude to engage the different budget holders within the business to support the business leader's own cost reduction programs by facilitating more sourcing and identifying other opportunities to drive value.

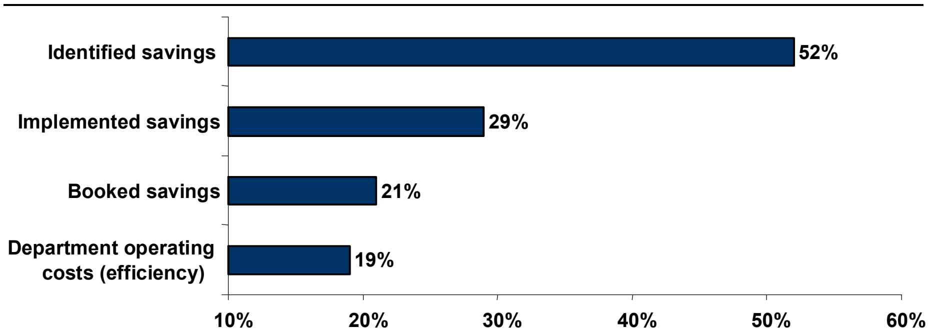
Save First, Ask Questions Later

Despite an ability to drive value and execute against a wide-range of business objectives, deviations on savings measurements are basically the only metrics used by the CFO (Figure 4) to measure the performance of the CPO and the procurement department. The types of savings used by the CFO to measure procurement performance are negotiated savings (**52%**), implemented savings (**29%**) and booked savings (**21%**).

"Our savings process is not formal. It is on an excel spreadsheet, but savings are reported as a value-add function and not removed off business budgets. We get better buy in this way."

~Director, Procurement Services Industry, Australia

Figure 4: Percentage of CFOs Who Use KPIs to Evaluate CPO Performance



Source: Aberdeen Group, November 2009

More troubling than an almost singular focus on savings (see Analyst Insight at the end of this chapter) as a measure of procurement performance is the lack of standards that exist in the definition of these metrics. Consider:

- **32%** of enterprises have no formal process to measure the savings generated by procurement
- Another **25%** calculate these measures on a case-by-case instance

There are certainly times where ambiguity around performance metric definition and measurement can benefit the person or team being evaluated, but over the long haul, the best way to communicate success and value delivered is to have clearly defined goals and to surpass them. The current gap between the high importance of savings measures and their accuracy must be closed.

The CFO and CPO should work together to develop an enterprise-wide set of savings definitions, procedures to calculate savings, and standard timelines for savings reporting. Aberdeen recommends applying these standards to the three tiers of savings:

- **Identified.** Beyond simple identification of a savings opportunity, this tier of savings is characterized by sourcing activity and negotiated pricing, where savings potential is attainable.
- **Implemented** (or realized). After the contract has been executed, enterprises begin to realize the potential of previously identified savings opportunities. This tier is characterized by purchasing, receiving, invoicing and settlement activity, and ensured by contract compliance and strong end-user adoption.
- **Booked**. Once savings have been realized, they can be recognized or booked in operating budgets and other enterprise-level financial statements. This tier is characterized by close involvement with finance, procurement, and the budget holder.

Aberdeen Insight - Savings: A Riddle Wrapped in an Enigma

While the Aberdeen Global Supply Management (GSM) research team has, at times, in recent years, utilized savings as a contributing determinant of Best-in-Class performance, it has done so with mixed emotions. Not including a performance metric like savings would be somewhat at odds with Aberdeen's research methodology, yet, in the eyes of the GSM team, the use of savings in this regard is a challenge. As discussed above, many enterprises lack a clear definition of savings, additionally the type of savings (implemented versus booked – who should own the budgeting process?) that procurement should be responsible for delivering is another question worthy debate. The next layer of complexity in using savings as a key performance metric is that the opportunity that exists in the marketplace may have more to do with the industry or region of an enterprise than any particular strategy or capability. Additionally, enterprises that are mature, operating at a level of sophistication where current contracts reflect current market pricing, have a smaller opportunity to find additional savings than a greenfield enterprise that has never aggregated spend or sourced a contract through a formal and competitive process. The discussion is just getting started and the fact that total savings from a sourcing project may not be the desired outcome from a sourcing project or supplier relationship has not even been broached (i.e. goals could be supply assurance, innovation, quality, value, growth, or any host or combination of goals). The issue is complex.

continued

Aberdeen Insight - Savings: A Riddle Wrapped in an Enigma

As discussed in many earlier reports and in this chapter, the GSM team has gone through great pains to research and understand the benefits that placing spend under management has on procurement (and overall enterprise) performance. What the research indicates across the results from literally thousands of procurement departments is that the correlation, if not causation, of having a higher percentage of spend under management with improvement in other key procurement metrics like savings, compliance, maverick spend, and operational efficiencies. Aberdeen believes that measuring and tracking spend under management is vital to understanding performance. Aberdeen does not suggest that savings should not be a procurement goal. It should be. But there should be clear definition and context that incorporates the above discussion around the measure. It is less valuable in benchmarking performance, however.

To paraphrase Winston Churchill (again), "savings is the worst measure of procurement performance……. except for all the others." The debate can and should continue.

In the next chapter, we will continue this discussion on the relationship between the CPO and CFO and what the top performers are doing to outperform their peers.

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Chapter Two: Benchmarking Requirements for Success

The CFO's "view" of procurement has improved over the last two years, helped immensely by the CPOs ability to help defend margins by delivering cost reductions. In fact, only **6%** of CFOs now think that their procurement department has a negative impact on competitiveness. Despite this, more than one-quarter of all CFO's gives low marks to their procurement department in the following areas: use of technology to automate processes, financial skills, process visibility and process innovation, enterprise-level reporting, and its impact on product development. In many cases, the low marks reflect an accurate assessment, yet the generally poor, but improving levels of collaboration and communication between the two leaders and their functions play a role. The CFO-CPO relationship remains a work in progress.

Case Study — A Savings Account

The Chief Procurement Officer (CPO) of a large financial services company (one of the top 10 largest U.S.-based financial services companies that includes a large retail banking arm) joined the firm four years ago as the company's first CPO and a plan to move from a decentralized organization to a center-led structure. The procurement function suffered from limited or no controls, poor visibility and a general lack of process and policy standards. While the company understood procurement-generated "savings" conceptually, it lacked any process to track values. "My view was to really focus on savings. They knew how to spell it [savings], but they didn't know what procurement really did or what a successful group could deliver. The language of communication at the time I joined was money so I decided to communicate the value of procurement through savings." The CPO reported to the CFO who provided two or three full-time analysts from the finance team to help develop the organization, set operating guidelines, support a new mandate and then independently track and verify results. The CPO chose to run his department like an independent business and tracked the return on investment that the company had made in his department.

continued

Fast Facts

√ The Best-in-Class manage **73% more spend** than their competitors

√ The Best-in-Class have contract compliance rates that are **70.4% higher** than their competitors

CFO Expectations – Procurement needs to….

"Establish standardized methods of procurement. Centralize sourcing. Develop policies & procedures regarding spend, outside of T&E."

~ CFO, Financial Services Industry, Canada

"Create cross-functional teams and become involved in the budgeting process in order bring to light what is planned to be purchased."

~ CFO, Manufacturing Industry, United States

"Strengthen its team via acquisition of quality experienced individuals

~ VP, Finance, Metals Industry, Ecuador

Case Study — A Savings Account

The CFO and CPO also utilized three operating principles as it related to savings:

1. **Establishing financial rigor** by holding the finance team accountable for savings calculations
2. **Regular reporting and monitoring** by using a procurement savings database to capture project level results and present an enterprise-level view of year-to-date savings
3. **CFO sign-off** which was just that – the CFO needs to sign off on all final savings values

With CFO alignment and a small technology budget, the CPO proceeded to invest in an e-sourcing application and began an aggressive e-sourcing campaign that delivered savings totaling in the hundreds of millions of dollars over his first three years in the role.

Competitive Assessment

Aberdeen Group analyzed the aggregated metrics of surveyed companies to determine whether their performance ranked as Best-in-Class, Industry Average, or Laggard. In addition to having common performance levels, each class also shared characteristics in five key categories: (1) **process** (the approaches they take to execute daily procurement operations); (2) **organization** (corporate focus and collaboration among stakeholders, such as procurement and finance); (3) **knowledge management** (contextualizing spend data and exposing it to key internal stakeholders); (4) **technology** (the selection of the appropriate procurement, finance and sourcing tools and the effective deployment of those tools); and (5) **performance management** (the ability of the organization to measure its procurement and financial results to improve its business). These characteristics (identified in Table 3) serve as a guideline for best practices, and correlate directly with Best-in-Class performance across the key metrics. These metrics represent the percentage of CFOs who rate the capabilities below as "Above Average" (respondents selecting "Good" or "Excellent" instead of "Average" or "Poor")

Table 3: The Competitive Framework

	Best-in-Class	Average	Laggards
Process	Supplier negotiation and contracting		
	79%	71%	67%
	Total cost / spend management		
	69%	61%	54%
	Process efficiency and standardization		
	56%	46%	44%

	Best-in-Class	Average	Laggards
Organization	Enterprise-level communication		
	60%	47%	33%
	Positive impact on product development / innovation through internal collaboration		
	47%	28%	28%
Knowledge	Visibility into procurement and sourcing processes		
	50%	37%	33%
Technology	Technology enablers currently in use:		
	▪ 81% spend analysis ▪ 65% e-procurement ▪ 58% BI / financial analytics ▪ 59% specialty service procurement application	▪ 53% spend analysis ▪ 50% e-procurement ▪ 38% BI / financial analytics ▪ 59% specialty service procurement application	▪ 48% spend analysis ▪ 42% e-procurement ▪ 38% BI / financial analytics ▪ 59% specialty service procurement application
Performance	Performance-tracking capabilities in use:		
	▪ 69% supplier performance measurement ▪ 53% procurement corporate performance management ▪ 50% SOX compliance / tracking solution	▪ 51% supplier performance measurement ▪ 38% procurement corporate performance management ▪ 26% SOX compliance / tracking solution	▪ 39% supplier performance measurement ▪ 18% procurement corporate performance management ▪ 33% SOX compliance / tracking solution

Source: Aberdeen Group, November 2009

"To support finance activities, we are implementing a procure to pay process merging A/P and Purchasing under Procurement Services and renegotiating every major contract for cost savings."

~ CPO, Higher Education Institution, United States

Capabilities and Enablers

Best-in-Class enterprises have leveraged a series of process, organization, knowledge management and performance-tracking capabilities, as detailed in Table 3, to effectively drive superior performance across the scope of key procurement and sourcing metrics. These organizations have also utilized a core set of procurement, sourcing, analytical and financial solutions to complement their performance and drive considerable value across the enterprise.

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Process: Sourcing and Spend Management

The very core of a Best-in-Class procurement organization is a strong grasp on basic process management principles and a team equipped to execute them. Supplier negotiation and contracting (nearly 80%) sits at the nucleus of a classic procurement skills matrix. For the modern procurement department these capabilities include the identification of the best sourcing opportunities and an ability to structure and communicate these opportunities to the suitable market and negotiating a final contract that optimizes value for the enterprise. With the need for an increase in sourcing volumes, these capabilities help the Best-in-Class source a wider range of categories to greater result.

As discussed in Chapter One, spend under management provides a string indication of maturity within a procurement department and impact beyond it. With control over total cost and spend management (nearly 70%), top-performing enterprises are readily able to direct the consistent flow of procurement spending within the company and are afforded superior visibility into corporate spending, thus ensuring better opportunities for savings.

Organization: Communication

If change management is a classic pitfall to a software deployment, the communication gap that exists between some CPOs and CFOs remains the largest bridge to cross. Poor communication between these two leaders and their departments is a direct cause for a lack of alignment on goals and objectives or ambiguity around performance metric definition and results. For the overall enterprise to run on all cylinders, the procurement and finance teams should actively communicate with each other in regards to insight into corporate spending, potential roadblocks for negotiations, and the status of implemented / booked savings. Best-in-Class enterprises are nearly 43% more likely than all other enterprises to have above average enterprise-level communication. If the average procurement department manages 57% of total enterprise spend, that means there is an opportunity to go after the other 43%. Having an ability to clearly articulate the value proposition for budget holders and functional peers to work with procurement can provide great returns in driving more spend under management.

Knowledge Management

Visibility is often considered the cornerstone of a successful procurement organization; visibility into not only corporate spending but also all procurement processes (50%) have assisted Best-in-Class enterprises in driving performance through their strategic mix of technology enablers and internal tactics. If compliance or savings are lagging, these enterprises have the visibility in place to restructure the processes behind the performance to optimize their plan of attack.

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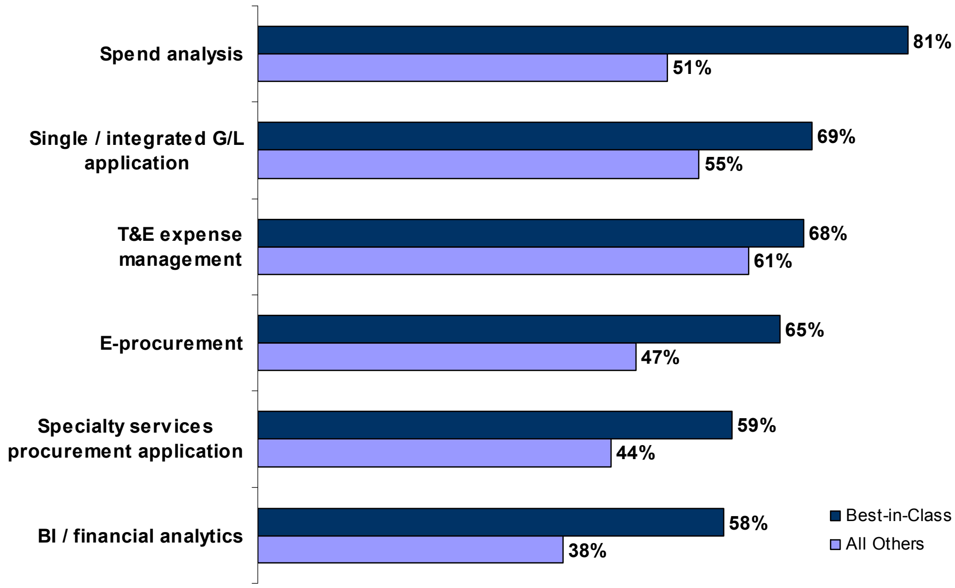
Technology

As with their process, organizational and knowledge management capabilities, Best-in-Class enterprises have leveraged technology solutions to propel their superior performance (Figure 5).

Figure 5: Best-in-Class Technology Utilization



Source: Aberdeen Group, November 2009

Top-performing organizations have leveraged a set of enablers across the scope of both the procurement and finance functions. Utilization of these solutions has assisted in driving enterprise-level visibility, higher rates of spend under management and contract compliance, and consistent implementation of identified cost savings from sourcing efforts:

- Spend analysis, as shown in the *Spend Analysis: Transforming Data Into Value* report, has been linked to a sharp increase in procurement performance. Through spend analysis and its associated processes (data cleansing, enrichment and reporting), Best-in-Class organizations (81%) are able to 'slice-and-dice' their spend data (culled from both procurement and financial systems) to uncover spending trends / patterns and identify opportunities for savings, as well as arming the sourcing force with deep-level information for contract negotiations. Use of a business intelligence / financial analysis system (58%) has also assisted these top performers in optimizing their procurement approach through data-driven strategies.
- A single, integrated general ledger application (nearly 70%) can provide real-time access to accounting information and assist both the finance and procurement organizations with unique reports that can be leveraged for educational efforts. This centralized application

can also be utilized to implement and book savings information as a means of booking them for future budgeting.

- Specialty service procurement solutions (nearly 60%) have assisted Best-in-Class enterprises in tackling some of the complex categories of spend that typically elude the modern procurement eye. These categories, which include contingent labor, T&E, print / print services, strategic meetings and real estate / facilities manage, often require a varied set of processes, policies and sourcing methods. Specialty service procurement solutions are specifically built for these complex areas of spending and can drive value (in terms of savings and compliance) from categories that do not often fit within the scheme of distinctive indirect or direct spending.

Performance Management

Performance measurement is a common trait of Best-in-Class enterprises; a failure to track the several key metrics within the procurement organization often results in poor bottom-line growth and the destruction of the finance / procurement relationship. Best-in-Class enterprises have actively tracked the performance of both their suppliers (69%) and contracts (50%) to better manage their spending and drive more dollars to the bottom-line.

Although supplier performance measurement is a key method in ensuring that the supplier base adheres to contract rules and appropriately mitigates supply risk, tracking SOX compliance is a chief contributor in pushing savings from an identified level to fully-booked and hitting the bottom-line.

Aberdeen Insight — Plugging the Savings Leaks

In the realm of procurement, the sourcing process is where the savings rubber hits the road, for it is during the award and negotiation of new contracts that the identification of savings (or cost reductions) from earlier period's spend occurs. But the sourcing process (i.e. definition of requirements, developing a bid package, identifying and qualifying suppliers, etc.) requires a different set of skills than those required to implement a new supplier or contract. Aberdeen research has shown that procurement departments fail to implement **roughly 15% to 25%** of the savings that are identified at the time of contract award. Some of this "leakage" occurs for acceptable reasons - changes in requirements (or specifications) or changes in demand as examples. A larger portion of the leakage is based upon a failure to comprehensively implement the supplier contract and ensure that stakeholders buy against it. There can be shared blame for this failure, but it is one for which procurement should be held accountable. And one that procurement should guard against with effective processes, tools, and policies that fall under the control of procurement.

continued

Aberdeen Insight — Plugging the Savings Leaks

The savings gap increases dramatically when we consider the percentage of identified savings that are "booked" (savings that are reflected in budgets) in an enterprise's financials. The average enterprise books **38.2%** of the identified or negotiated savings that procurement identifies. Best-in-Class enterprises that have tighter coordination and controls established between the CFO and CPO capture **73% more** of this savings on their books than their competitors.

As discussed in the 2007 version of this report, which findings are still relevant today, "The traditional view places blame for the gap between implemented and booked savings squarely on the shoulders of procurement. But this is a significant and fundamental issue that must be revisited and challenged. Procurement's role should be to deliver savings to the enterprise. If a line of business chooses to deploy the savings to drive other goals that does not make implemented savings any less real. Just as it would be absurd to expect the head of a business unit or general manager to defer to procurement's judgment above all else on the management of its business and key initiatives in the next 12 months, it makes little sense to involve the CPO in a protracted discussion around how to reallocate savings."

Chapter Three: Required Actions

Given the expansion of duties and responsibilities for the average CFO, a sub-optimal procurement operation is and should be a large "black mark" on the CFO's scorecard. Developing a Best-in-Class procurement operations program requires competence, diligence, and patience. Whether a company is trying to move its performance in from Laggard to Industry Average, or Industry Average to Best-in-Class, the following actions will help improve the working relationship of the Chief Financial Officer and the Chief Procurement Officer as well as drive performance improvements:

Laggard Steps to Success

1. **Immediately begin to collaborate and start measuring (and reporting) regularly on procurement performance KPIs.** Measuring the activity and results across procurement operations is a great starting point. Measuring the impact of those metrics is a great next step. Once the initial measurements are in place, review them regularly and refine as needed. Over time, it may become clear that other metrics or definitions are needed. Avoid measures like cost avoidance that cannot be quantified in an absolutely unambiguous way.

- **Establish a plan to drive regular, formal and informal communication between procurement and finance.** The more comfortable each department is with the other, the more readily opportunities that sit unexploited today will begin to emerge. Ensure that the entire dialogue is not focused on performance and performance measurement. Involve constituents from each function in each other's staff/department meetings. Rotate resources and seek projects that can combine members of both teams. The CFO and CPO should also be included in the plan and meet on a regular timetable (i.e. monthly or bi-monthly)

Industry Average Steps to Success

- **Close the technology and business process gap around contract compliance.** Policies and procedures must be solidly in place before an enterprise can be truly effective at managing and improving compliance. Solutions, like contract lifecycle management, that provide enterprise-level visibility and directly support compliance policies are a critical step towards operating efficiency.
- **Use data from procurement metrics to educate internal and external stakeholders.** Help employees understand the impact of their behavior on the enterprise. They will be much more likely to support something that they understand. Data can also help garner additional support from executive management on the value of certain initiatives, particularly if the CFO has signed off on the

Fast Facts

√ The Best-in-Class book **73.2%** more of their identified savings than their competitors

√ The Best-in-Class operate their departments **23.6% more efficiently** than their competitors

Savings Tiers

Identified: Beyond simple identification of a savings opportunity, this tier of savings is characterized by sourcing activity and negotiated pricing, where savings potential is attainable.

Implemented (or realized): After the contract has been executed, enterprises begin to realize the potential of previously identified savings opportunities. This tier is characterized by purchasing, receiving, invoicing, and settlement activity and ensured by contract compliance and strong end-user adoption.

Booked: Once savings have been realized, they can be recognized or booked in operating budgets and other enterprise-level financial statements. This tier is characterized by close involvement with finance, procurement, and the budget holder.

importance of these metrics and their definition. Additionally, sharing key data with suppliers to let them know where they are with relation to performance and compliance from your perspective will serve to improve their performance and reduce your risk.

- **Get the CFO to champion a major procurement initiative each year.** Procurement departments that fail to realize their potential are often constrained by a lack of mandate. The heft and visibility that the CFO can add to major procurement program can reap extraordinary rewards and is time well spent.

"Procurement saving measurement is based on the commodity index tracked monthly. For our commodities, the purchase price is always affected by the global price movements of oil and metals. Therefore, the total cost of our buy is reviewed with our suppliers on a monthly basis. Finance is involved the foreign exchange rate and bank interest rates that will affect the true cost of commodity material.

~ VP, Procurement, Consumer Electronics, Korea

Best-in-Class Steps to Success

- **Involve members of finance and procurement on compliance audits.** Collaborate on the audit process and seek to understand the causes behind non-compliant behavior, then work together to establish policies that drive the desired behavior. Develop a joint strategy to clearly communicate them and monitor them on a go-forward basis. Communicate any improvements from this program to the CPO and CFO on a regular basis.
- **Cascade performance objectives from the enterprise to the procurement department and its staff.** The clearest driver of employee behavior is compensation. Aligning the procurement department and staff's performance goals with the enterprise will go a long way towards driving engagement and dialogue and the development of a clear mechanism to assign accountability for performance.
- **Challenge the view (if it exists) that it is procurement's responsibility to negotiate budget reductions with the line of business**. Once savings have been achieved, it should not fall to procurement to establish how this real benefit should be allocated across the enterprise, but rather to the line of business and / or finance. Placing procurement in this "line of fire" can potentially put it at odds with the group that it is trying to support and engage on future projects. Finance should own this process and lead the discussion.

Aberdeen Insight — The Next Step

As discussed in *The CPO's Agenda 2009: Smart Strategies for Tough Times* published earlier this year, "CPOs with a firm command of the goals of the larger enterprise, a clear vision and plan focused on supporting or achieving these goals, and an organization well-equipped to execute said plan stand poised and ready to lead their enterprises out of this economic cycle and into the next decade. And, those CPOs that lead and deliver in tough times will gain deserved recognition, they may be duly rewarded, and over time, those with aspirations beyond procurement may reasonably pursue and attain other, more senior roles within the executive ranks."

continued

Aberdeen Insight — The Next Step

Aberdeen believes that the role of CPO is one that should be highly prized and worthy of true executive-level compensation. It should be viewed by people in procurement and expanded supply chain operations as a pinnacle position, a capstone to a wildly successful career. But, there are also CPOs, like those who have given presentations at Aberdeen's CPO Summits that possess the breadth of skills and depth of experience to lead large departments, business units, and entire companies. It is incumbent upon leading CPOs to push their professional envelope and seek their just desserts and seek "higher office." Once empowered beyond the walls of procurement, these former CPOs should continue to invest in the resources that will continue to increase the value that the procurement function delivers to the larger enterprise and build upon a newly started cycle.

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Appendix A: Research Methodology

Between October and November 2009, Aberdeen examined the use, the experiences, and the intentions of more than 170 finance and procurement executives across a wide range of industries.

Aberdeen supplemented this online survey effort with telephone and online interviews with select survey respondents, gathering additional information on the view that the CFO and finance have of procurement.

Responding enterprises included the following:

- *Job title / function:* All of the survey respondents work in the finance (43%) or procurement (57%) departments of their enterprise.
- *Industry:* High technology (12%), manufacturing (7%), financial services (7%), retail (6%), education (6%) and 33 other industries.
- *Geography:* The respondents were from North America (57%), EMEA (30%), and Asia-Pacific (13%).
- *Company size:* Forty-three percent (43%) of respondents were from large enterprises (annual revenues above US $1 billion); 33% were from midsize enterprises (annual revenues between $50 million and $1 billion); and 24% of respondents were from small businesses (annual revenues of $50 million or less).

Solution providers recognized as sponsors of this report had no substantive influence on the direction of this report. Their sponsorship has made it possible for Aberdeen Group to make these findings available to readers at no charge.

Study Focus

Responding finance and procurement executives completed an online survey that included questions designed to determine how the CFO (and other finance executives) view their procurement organization including its:

√ People

√ Process

√ Technology

√ Performance

√ Strengths

√ Weaknesses

√ Opportunities to improve

The study aims to identify best practices for the working relationship between the CFO and CPO and provide a framework by which readers may assess their own management capabilities.

Table 4: The PACE Framework Key

Overview
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, November 2009

Table 5: The Competitive Framework Key

Overview	
The Aberdeen Competitive Framework defines enterprises as falling into one of the following three levels of practices and performance: **Best-in-Class (20%) —** Practices that are the best currently being employed and are significantly superior to the Industry Average, and result in the top industry performance. **Industry Average (50%) —** Practices that represent the average or norm, and result in average industry performance. **Laggards (30%) —** Practices that are significantly behind the average of the industry, and result in below average performance.	In the following categories: **Process —** What is the scope of process standardization? What is the efficiency and effectiveness of this process? **Organization —** How is your company currently organized to manage and optimize this particular process? **Knowledge —** What visibility do you have into key data and intelligence required to manage this process? **Technology —** What level of automation have you used to support this process? How is this automation integrated and aligned? **Performance —** What do you measure? How frequently? What's your actual performance?

Source: Aberdeen Group, November 2009

Table 6: The Relationship Between PACE and the Competitive Framework

PACE and the Competitive Framework – How They Interact
Aberdeen research indicates that companies that identify the most influential 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 those decisions.

Source: Aberdeen Group, November 2009

Appendix B:
Related Aberdeen Research

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

Executive-Based Research

- *The CPO's Agenda 2009: Smart Strategies for Tough Times;* April 2009
- *The CFO's View of Accounts Payable: Cash is King;* February 2009
- *CPO Rising: The CPO's Agenda for 2008;* February 2008
- *The CFO's View of Procurement: Same Page, Different Language;* November 2007

Source-to-Settle Research

- *E-Payables Benchmark 2009: Accounts Payable Rising*; September 2009
- *Procurement Contracts: Real Value, Real Returns*; March 2009
- *Spend Analysis: Pulling Back the Cover on Savings*; October 2008
- *The Advanced Sourcing and Negotiation Benchmark Report: The Art and Science of the Deal;* January 2007
- *The E-Procurement Benchmark Report;* August 2006

Complex Category Research

- *Contract Labor Management: Superior Workforce Strategies for a Demanding Environment*; January 2009
- *T&E Expense Management: Leveraging Data to Drive Performance*; April 2008
- *Strategic Meetings Management: Of MICE (Meetings, Incentives, Conferences and Exhibitions) and Spend*; February 2008

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

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