



What is Procurement Cost Reduction and Procurement Outsourcing (PO)? How Can PO Affect You and Your Organization?

PO #1: Procurement Outsourcing – A Cost Reduction Solution for Companies

Procurement Outsourcing Introduction

This procurement outsourcing series outlines what procurement is, what outsourcing is, why procurement outsourcing is growing rapidly among companies around the globe, what the benefits are, the risks, and why more companies are and will utilize procurement outsourcing to solve a range of challenges, with cost reduction as one of the top reasons.

Net Margins and Costs are hurting Companies

Many companies have not been able to increase revenue, credit is harder to come by for expansion, employees have been downsized to cut costs (less people are doing more work), global competition has increased, raw materials are expected to increase and the bottom line for companies are not what they used to be.

Procurement Outsourcing provides solutions and answers

Because of these challenges and realities, companies are looking for ways to innovate, with many of these companies trying to figure out how to stay in business. Even though there are some risks, procurement outsourcing is a viable means to helping companies, with cost reduction being the largest substantiated reason. A few of the many benefits are Compliance; Cost savings; Efficiency improvement; and Overall performance.

Who are some of the larger Procurement Outsourcing Firms?

With companies like IBM, Accenture, General Electric, and Xerox in the procurement outsourcing business, and others getting into the market, this shows a definite need, provided solutions, growth, and opportunity.

Choose Procurement Outsourcing

As this report will show, procurement outsourcing is growing, companies are becoming more aware of the benefits and risks, the outcomes have been documented and substantiated, and these results are helping company bottom lines. With procurement outsourcing, companies are becoming more competitive, companies are focusing on what they do best, and most importantly, more companies are staying in business.

Procurement Outsourcing

Many companies do not know what procurement outsourcing is and why it is becoming a vital part of their operations. It was only in the 1990's AT Kearney started procurement outsourcing



and began selling procurement outsourcing consulting services. Since then, procurement outsourcing is gaining momentum.

The main reason for procurement outsourcing started was due to the cost reduction that took place. As procurement outsourcing has continued to mature, cost reduction has increased and continues to be the main reason companies continue to outsource their procurement. Before a company even understands the procurement, outsourcing benefits, procurement outsourcing needs to be understood, and why it should become a part of a company's regular operating procedure.

What is Procurement Outsourcing?

Procurement outsourcing is the action of a company outsourcing their procurement functions, with the acquisition of goods and services, through a third party. This does not mean that the company loses control, but it utilizes third party services. The outsourced procurement can mean cost reduction, improved efficiency, improved compliance, and enhanced performance. Procurement outsourcing can involve some or all the company's staff, technology, systems, and vendor management or everything can be directed by the procurement outsourcing firm for the company (Sigaria, Ltd., Procurement Leaders).

PO #2: Procurement Outsourcing Equals Sustainable Cost Reduction Cost Reduction and Benefits

With cost reduction being one of the main driving factors for companies, procurement outsourcing helps meet this need. Even with economic upturns in certain industries and geographical areas, profit margins will remain low, and global competition will continue to increase. In addition, raw materials costs have increased and are expected to continue increasing, and the world economy will continue to affect more nations, companies, and people. With companies spending more than half on their external goods and services for every dollar earned there is a lot of costs to be reduced (Aberdeen Group, Accenture, and PurchasingData.com).

Other Procurement Outsourcing Benefits

In addition, many companies lack internal staff or no staff to conduct the necessary procurement processes to manage their goods and services. Because of this companies are leaving billions and billions of dollars on the table. For many smaller companies, they cannot afford a purchasing department or at best, they have one person who buys for the company, so little or no cost reduction, vendor negotiation, contracts, and price analysis take place. For



larger companies one department does not know what the other departments are doing, leading to increased cost and inefficient goods and services management.

Large Company Outcome Example

One large company example, with annual revenues of more than \$5 billion, had overrun cost, budget problems, compliance issues, little communication, and supply problems. With 252 purchasing personnel across their entire operations and more than \$1 billion per year spend for goods and services, their procurement outsourcing had a lot of potential opportunity for procurement outsourcing. What was the outcome? Centralized procurement, better communications, increased production at each location, cost reduction of more than \$50 million per year within two years, staff focus for core competencies, expansion of certain areas, closing of other areas that were a drain on the company's resources, and streamlined purchasing personnel across the organization for greater outcomes in all areas of each region. (ATS)

Small Company Outcome Example

Even small organizations can be helped with their bottom-line costs, efficiency, and best value. We have served many small organizations from \$1M to \$50M gross revenues with great outcomes. Most organizations of this size do not have a procurement department, most do not have a head of purchasing, and most only have one buyer. More than this, the ISM and NAPM in the U.S. conducted a survey and found that most organizations of this size are not conducting bidding, RFPs, and negotiation processes to gain best value.

We served one organization and helped them reduce costs in three areas reducing costs by more than \$3 Million in one year, developed a procurement department for them, created the best practices and SOPs for sustainability, centralized their software, helped them hire a Purchasing Director and two buyers, and increased their revenue.

There are many things that can be done with Procurement Outsourcing for most organizations, whether small, medium, or large.

With all types of companies and organizations there is a greater opportunity to increase the percentage savings. Many of these companies listed below have some type of procurement department and the procurement process is already taking place.

ATS' experience has brought about many different outcomes for savings when goods and services have been outsourced with our procurement techniques.



Almost All Goods and Services can be Outsourced

Procurement outsourcing covers all goods and services in companies. Some example areas are Office supplies; Computers; Paper; Toner; Fencing; Electricity; Natural gas; Landscaping; Property management; Maintenance; HVAC; Software; Information Technologies; Payroll; Accounting; Legal; Flooring; Fencing; Asphalt; Credit; Banking; Cement; Steel; Financing; Fleet automobiles and trucks; Human resources; Signs; Print; Telecom; Cellular; and many other areas. The bottom line of procurement outsourcing is that if the good and service can be outsourced through a third party (the procurement outsourcing company) providing cost reduction, more compliance, more efficiency and production, and an opportunity to the company to focus on their core competencies, the procurement outsourcing model works well.

PO #3: Procurement Outsourcing Market

What is the Market?

Everest Research Institute, a well-known global consulting and research firm, has successfully predicted continued growth in procurement outsourcing and will continue to grow. It looks good for procurement outsourcing firms, because it is a managed service and performance-based model, which companies are starting to see as a partner relationship. (Everest Research Institute, Everest Group)

IBM one of the largest procurement outsourcing leaders stated, “Challenging economic times and intense global competition have placed increased pressure on company balance sheets. More than ever before, businesses are refocusing on core activities and carefully managing cash. By natural extension, this has led to detailed scrutiny of procurement spending with suppliers—which can equal as much as half of a company’s annual revenue. As pressures continue to mount, businesses must ensure that they are realizing the optimum values from their procurement spend or they may find themselves at a competitive disadvantage.”

Companies can only reduce so many staff positions to reduce costs, increase revenue so much in a down turned economy, and compete in a highly competitive global market with low net margins. Where do companies find more capital and resources? They find it by reducing costs with the goods and services they are already purchasing, thus the increased demand in procurement outsourcing and projected growth.

This has proven to be true and procurement outsourcing continues to be a best in practice solution for many companies and continues to grow.



Future Growth

The Aberdeen Group Report, one of America's premier business management research groups, stated that one of the biggest growth areas in Business Process Outsourcing will be procurement outsourcing. This has proven to be true.

This study, which included many companies in a variety of industries found that internal purchasing departments are increasingly seeking the involvement of third-party experts to leverage their abilities to drive down costs. In fact, 40% of the organizations surveyed indicated that they would be outsourcing all or part of their procurement functions in the next two years.

The top four reasons cited for why these companies would engage in procurement outsourcing were:

- 45% pressures to lower procurement transaction costs.
- 41% increased global competition.
- 36% need to gain access to improved pricing.
- 34% pressures to re-focus personnel on more strategic activities.

From 2007 through now, even despite the global economic downturn, less buyers, conservatism, financial and credit problems, procurement outsourcing continued to grow.

What is Causing Procurement Outsourcing to Grow?

The future is bright and profitable for procurement outsourcing, as companies continue to look for ways to improve performance, bolster bottom line revenues, and lower operating costs. As this industry continues to grow, the traditional functions like fleet maintenance, payroll processing, legal services, and local delivery continue to be expanded. Other areas that had never been outsourced are taking place in record growth, such as recruiting, hiring and human resource management functions. In all reality, anything and everything is being outsourced, because companies continue to refine their missions and business models looking for cheaper, better, and faster.

PO #4: Procurement Outsourcing Benefits

There are Many Benefits to Procurement Outsourcing

There are many benefits that can occur from procurement outsourcing. Some of them are:

- Reduced costs and increased quality.
- Centralized procurement.
- Provide needed goods and/or services.



- New market development.
- Just-In-Time Inventory (JIT).
- Increased supply chain efficiency.
- Best value and remain competitive.
- Government compliance.
- Supplier performance improvement.
- Support day-to-day buying activity.
- Policy/Procedure creation, implementation, validation.
- Transaction automation and processing.
- Focus to core competencies.
- Strong end-user to provider relationship developed.
- Lower procurement related labor costs.
- Overall procurement performance improved.
- Greater control, reporting, and vendor compliance.
- Organization and internal cost performance.
- Data for benchmark analysis, goals, and results.
- Procurement personnel training.
- Hedges future increase of raw materials.
- Procurement department creation and implementation.

Cost of Requisition-to-Order Cycle

A study by Aberdeen measured the costs of the requisition-to-order cycle in many companies. What they found through procurement outsourcing was lower costs through lower transaction costs, as well as from lower absolute costs on the items purchased. Before outsourcing the cost was \$33.00 – after outsourcing, the cost was \$14.15 – a savings of more than 57% in staff resource costs.

Aberdeen’s research found that for each dollar of spend brought under outside procurement management, companies were able to realize cost savings of between 5% and 20%. Keep in mind that this is an average, with larger companies. With smaller and medium-sized companies, there is a greater opportunity to increase the percentage savings.

PO #5: What should companies expect overall in the future?

What is the future market for Procurement Outsourcing?

“Many people are tired of hearing about how terrible things were ...,” as Mark Toon, CEO of EquaTerra, points out in the latest article in Supply Chain & Logistics. His prediction came true



from “surviving the downturn to succeeding in the upturn.” Keep in mind that procurement outsourcing affects goods, services, services, labor, personnel, available resources and currency, sources, suppliers, technology, and many other areas in a company. The expectations became as follows:

- Global Sourcing – increased growth due to main desire of reducing costs.
- Social Media – companies need to have policies in place to maximize “their positive impact” (the image of a company affects pricing, talent, and communications, which all works with procurement).
- Talent Acquisition and Retention – salary increase for highest performing talent (talent and team increase revenue and better spend management in most cases).
- Optimization and Renegotiation – to deliver optimum value from company internal processes and existing suppliers’ investments are being made.
- Flexibility – companies are making commercial arrangements to be able to cope with unpredictable demands (there are a lot of changes from markets, demand, credit, natural disasters, energy, and other unpredictable situations).
- Procurement outsourcing – more companies are looking at and moving forward with procurement outsourcing because it is maturing, it is growing, it is the fastest growing outsourcing segment, and many are achieving double digit savings.

PO #6: Companies Starting to Understand Procurement Outsourcing **Understanding Procurement Outsourcing**

One of the biggest factors causing procurement outsourcing to grow and continue to grow is an understanding of the benefits. Companies are beginning to see that there are more positive than negative impacts from procurement outsourcing. The fear of a company losing control by utilizing procurement outsourcing in their company is fading away. Companies are seeing smarter buying, reduced costs, and continued control of their company. In other words, procurement outsourcing enhances companies and supports their core competencies. Procurement Outsourcing continues to grow in demand.

The amount of procurement outsourcing deals and sourcing deals have grown steadily over the last several years, according to Global Services/Equaterra.

Steady Growth

Who are some of the larger procurement outsourcing firms?

Besides IBM, Accenture, and others, others have and are emerging in the marketplace of procurement outsourcing. This includes General Electric / Genpact and Xerox and many others.



Other companies are getting involved in providing procurement outsourcing because of the need for companies to reduce their costs due to leaner net margins and global competition.

What are some of the risks?

Even though there are risks, a report conducted by AMR research, found that buyers will increase their activities by a ratio of five to one for their near-shoring sourcing. (Purchasing, Page 23). What this means is that companies are choosing Mexico as their number one choice, with Canada in second, and Brazil in third, with Eastern Europe as a potential sourcing location.

The AMR report found the biggest supply chain risks to be:

- Lower consumer spending.
- Supplier product quality failures.
- Volatile energy costs.
- IP infringement.
- Regulatory compliance.

One of the biggest areas of risk for procurement outsourcing, according to Pratibha Verma of Global Services, is “Despite the expansion of procurement outsourcing, the continued lack of standard deal terms suggest that market is still not yet ‘mature’ and yet has a number of risks in it.”

PO #7: Who are companies choosing to conduct their procurement outsourcing? Procurement Outsourcing Growing and in Demand

In conclusion, procurement outsourcing is in its infancy, is not understood by many companies for the benefits it brings, and the fear of losing control is a key factor in whether a company engages in the process. There are also some risks because of the current economy and quickly changing global market with lower consumer spending, product quality, energy cost volatility, compliance, and IP infringement.

On the other side, because of the economic downturn, low net margins, lack of credit, and cost reduction needed by companies, procurement outsourcing has become a viable solution. For this very reason, procurement outsourcing is being reviewed and utilized increasingly because of the cost reduction and savings that occur. With companies able to reduce costs from five to more than 20 percent for goods and services, this makes a significant difference to a company’s bottom line.



ATS has averaged more than 28% of average savings, \$534,000 cost reduction per procurement cost reduction project, in 98% of engaged procurement cost reduction clients.

Because of the necessity for companies to survive and reduce costs, procurement outsourcing has grown over the last few years and continues to become more the norm! With procurement outsourcing, companies can focus on what they do best, retain more money for their bottom line, and gain all the benefits of those goods and services outsourced. Procurement outsourcing helps all involved in procurement outsourcing come out ahead – the company needing the outsourcing, the third-party company conducting and managing the outsourcing, and the vendor/supplier who provides the goods and services.

How are You Maximizing Procurement Outsourcing for Your Organization?

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