



Good Guys or Men in Black

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Despite tremendous corporate belt-tightening across most major industries, it's surprising to see that many small and mid-cap companies continue to fall short of taking full advantage of the vast savings opportunities available to them. The savings potential for companies this size is tremendous and it can be there for the taking. Furthermore, these savings can all be achieved while at the same time reducing the company's operational risk. Skeptical or feeling at risk? You're not alone.

The biggest hurdle facing many small and midsized companies is they tend to focus on key initiatives in the company, but fail to take a systemic look at how they procure goods and services and the related spend and support resources. Often embedded deep within a company's procurement culture are habits and processes that have been in use and passed down through the years. Without conscious effort, like water down the side of a mountain, these processes will evolve and follow the path of least resistance.

What may have been cost effective even a few years ago (and in some cases decades) falls increasingly short today. True cost savings simply cannot be attained by using outdated processes and even worse; such purchasing habits can impose significant hidden operational risks on an organization. So why don't many companies acknowledge this? Oftentimes it's a matter of priorities and focus. When an organization is working to survive through a financial downturn, a systematic review of procuring goods and services is an initiative that may not bubble to the top. Other times it's because the company is just not equipped with the necessary finance, procurement, risk management and legal resources needed to fine tune and take full advantage of the company's purchasing options.

Take, for example the fact that the typical small to midsized company procures outside goods and services on a commoditized basis: it orders 6 widgets, gives specialized vendors narrow specifications and receives multiple quotes to ensure the best price is achieved. Nothing in that process allows for alternative product or service solutions to be introduced or even considered. Worse still, it is the perfect recipe for breeding "vendor creep": the process whereby over time, the company finds itself procuring one-off items from a large number of specialized vendors, none of whom can individually offer meaningful volume discounts to the company. So what can the company's vendors do to assist their client from employing this less than desirable approach? Very little. Their biggest obstacle: overcoming the strong culture and mindset of their customer's front-line managers or purchasing departments.



Sometimes a company is fortunate enough to have a purchasing or “procurement” department. That said, are the resources in these departments truly experts in all expense categories? Do they understand and employ procurement best practices? Do they view all vendors with deep-rooted skepticism and approach each contract negotiation with the view of “the closer a vendor’s margin is to zero the better the deal?” Are they savvy negotiators and do they have a strong background in understanding the business ramifications of key legal terms? Do they effectively govern the agreements they have negotiated (are they getting their bang for the buck)? Typically these procurement organizations possess a good understanding of a few key business areas of an organization and inherit the responsibility for the other areas. Negotiation skills and legal grounding are infinitely variable.

Despite their limitations, many companies continue to rely solely on front line managers and purchasing organizations to manage procurement operations and are reluctant to tap into outside firms that specialize in best practices and procurement transformation. Why? The reason often lies in the perceived threat that such firms pose to these purchasing resources, perceived cost, and the strong effect that such resources can have on senior management’s decisions to turn to outsiders for help.

Having spent most of our careers helping companies drive effective expense savings strategies, we have a deep appreciation for the source of the vulnerability shared by managers and purchasing organizations when approached by outsiders specializing in reducing expenses and transforming procurement operations. They often feel threatened or reluctant for any of the following reasons:

- Certain vendor “relationships” and individual “perks” that some managers may currently enjoy (for having relied on certain vendors for years) could become jeopardized or eliminated;
- Change is difficult: working with a new vendor or process takes people out of their comfort zone (and the only one who embraces change is a wet baby!);
- There is often little to no personal incentive (monetary or political) for managers to significantly reduce their business-line budgets. As is too often the case within companies that have strong corporate cultures, managers: (1) are rarely personally rewarded for achieving budget reductions, (2) often equate the size of their budget to their political capital within an organization; or (3) have the strong opinion that if they don’t spend the entire amount allocated to their budget, they will be hard-pressed to deliver the same results year after year with less resources available to them;
- The most cost-effective solution for a particular expense category may include an outsourced component that involves the termination or “rebadging” of the manager or his direct reports (“rebadging” is a term that describes the process whereby an outsourcing provider agrees to hire certain employees of the client and transfer them to the service provider); or
- If significant savings are achieved, senior management may view their past performance in a negative light because after all, weren’t they expected to find these savings on their own?



Let's switch gears here for a moment; We've outlined the "threats" that outside procurement expertise can pose to a company, let's focus on some of the benefits that a company is often unable to achieve without such assistance. Typically, small to mid-sized companies lack the in-house resources or capabilities to:

- Employ highly effective, procurement best practices that can create significant savings in accelerated periods of time (most companies typically are only able to achieve significant savings on their own by utilizing a resource-intensive and time consuming RFP process);
- Reduce operational risks through the strategic consolidation of best-in class providers (all while achieving optimum cost savings);
- Achieve a true understanding of the landscape of sourcing "solutions" that are currently being offered by best-in-class providers to drive down operational expenses;
- Obtain access to key resources at best-in-class providers, including national account solution teams and professionals that are dedicated to the client's vertical industry; and when an advisory firm is engaged, the provider knows the client is serious about the project they are pursuing and allocates focused pursuit resources and spend accordingly, and
- Employ the appropriate finance, risk management, procurement and legal professionals needed to transform their procurement operations in a cost-efficient manner.

The decision by senior management to engage outside procurement expertise may not necessarily be a popular one, but it is often one that can lead to the transformation of an operation vital to the company as a whole. A simple gauge of the effectiveness of a company's procurement operations can be measured by answering questions similar to those below:

1. How long has it been since competition was formally introduced within the company's multiple expense categories?
2. How many vendors are currently in use within each of the company's expense categories?
3. How competitive is the vendor landscape for each expense category?
4. What are the margins on the goods or services procured for each category?
5. Is the company taking full advantage of all alternative procurement solutions, "private labeled" supplies (vs. "premium branded") or value-based pricing models that best-in-class vendors are currently offering?



Based on responses to the above, it will likely become clear whether a company stands to benefit from outside assistance, and if so, how great that benefit will be. At the very least, companies have found significant value in retaining outside firms to audit the quality of the company's procurement program by establishing a baseline operational risk model for "business-as-usual" in each of the company's expense categories (i.e., identifying what the consequences and risk are with continuing "as is"). It is not uncommon for companies to then find that their current processes have significant inherent risks that can be addressed most effectively with new procurement solutions, thus bringing their operational risk exposure and expenses down simultaneously.

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