The Hidden Treasure in Tail-end Spend

Abstract

Many businesses do not optimize their tail-end spend, and as a result, the cost of invoice processing, combined with purchase and associated costs, often exceeds the value of the invoice itself. However, if CFOs make tail-end spend management a strategic priority, they can effectively improve the bottom line.

Invoices of less than $100,000 value represent 83% of the total invoice volume, whereas 95% of the total invoices have a value of less than $250,000.

Introduction

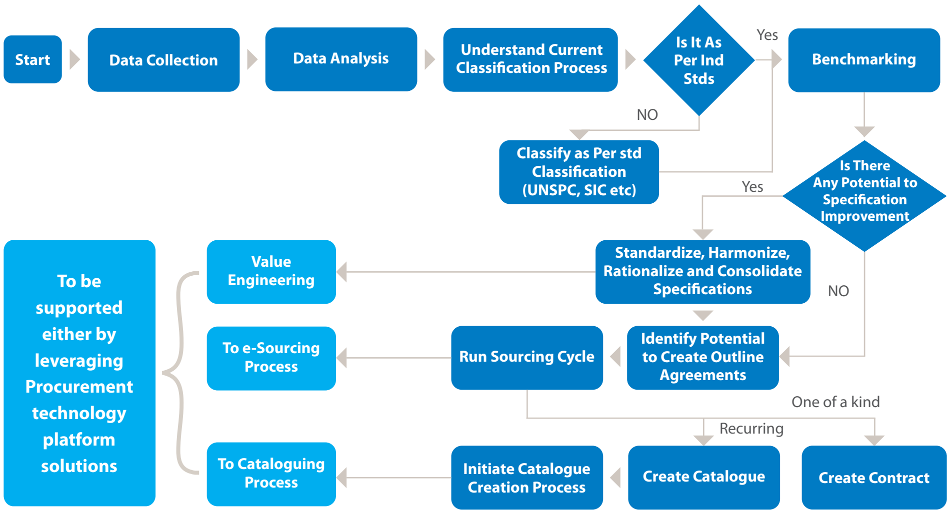
Processing a large number of low value invoices is the reality in most businesses, and results in increased invoice management overheads. Many times, the cost of invoice processing, combined with purchase and associated cost, far exceeds the value of the invoice itself. Further, 60-70% of procurement employees are dedicated to processing these low value invoices. Effectively managing this tail-end spend can save between 30-70%, depending on the industry and project type.

Senior Management's View on Tail-End Spend

In consulting engagements, questions on the need and importance of managing tail-end spends, receive interesting responses from CFOs.

Despite these different views, senior management, especially those in roles with direct P&L ownership, appreciate the need for managing and reducing tail end spend, and are keen on exploring best practices.

Tail-end Spend Management Process: The Key to Success Tail-end spend management requires an effective process partner with industry best practices, such as classification, benchmarking, and cataloguing.



Industry Best Practice for Managing Tail-end Spend

While process deployment is critical, it's equally important that organizations ensure process rigor. Do not skip steps, deviate from standards, implement practices partially, or compromise benchmarked performances.

Instead apply a robust technology platform to value-engineer the process, along with in-scope products and services. This use of technology will ensure right vendor targeting, effective cataloging, requirements aggregation, and competitive negotiation.

Four Approaches for Success with Tail-end Management

In addition to the right process and workflow, success with tail-end spend management requires four customized approaches to suit enterprise specific culture and ethos.

Approach 1: Value engineering to derive maximum value from products and services procured.

To arrive at an accurate definition of value:

- Encourage project and engagement teams to brainstorm and accurately define value metrics.
- Factor-in product, service, and business functionality, combined with associated overheads (procurement and management costs).

Well-strategized e-sourcing can result in significant business value through optimized tail-end spend.

- Reduce the complexity of large valuation exercises that involve a few million dollars by aggregating services into sourcing buckets, engaging with reliable and proven aggregators, and outsourcing the exercise as a managed service to a partner with expertise in the area.

Approach 2: E-sourcing has become the new normal.

Its success depends on taking a holistic view of the various aspects of the sourcing process:

- Accurate classification of products and services
- Industry benchmarking
- Appropriate spend aggregation comprising standard RFX
- Negotiation and contracting processes

Approach 3: Electronic catalogs of suppliers, products, and services within the procurement system enable two essential factors for tail-end optimization:

- Effective standardization
- Aggregation of tail-end line items and categories

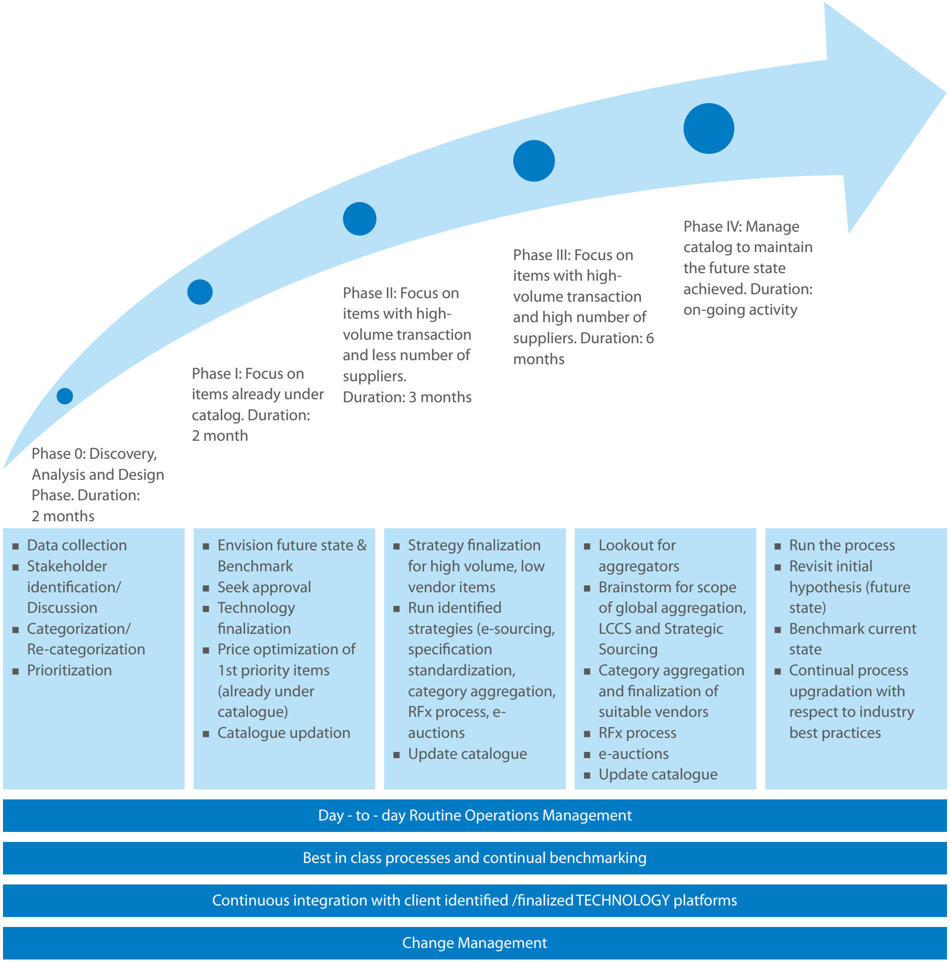
Companies with over 70% catalog penetration enjoy optimized turnaround time, greater accuracy, and improved stakeholder satisfaction level.

It is important to ensure clean and accurate catalogs, with minimal duplicate items. Besides optimizing the cost of catalog maintenance, efficient catalog management results in overall savings of 2-5% from the current level, with scope for further improvement.

Approach 4: P-cards come in handy for low value spends where contracting is not possible due to system complexities such as one-of-a-kind spending, spending by traveling employees, and low value emergency spot buys. When implemented after proper analysis, P-cards improve process transparency, reduce discretionary spend, facilitate accurate and speedy reconciliation, streamline payment processes, and significantly reduce processing cost.

Phased Implementation and Maturity Roadmap

In typical cases, the analysis and strategizing period of the tail-end management process ranges from two to three months, whereas the implementation, depending on the business context and complexities, takes five to six months.



Implementation Roadmap and Maturity States for Electronic Cataloging

Case Study: Financial Organization Optimizes Tail-end, Saves One Million

A large US-based BFSI organization began its tail-end optimization journey by identifying problems in its data classification and spend management strategy.

Over 80% of the company's 8,000 vendors, with an average spend of less than USD 10,000, accounted for only $16 million or 2%, of in-scope spend. With only 175 vendors under the tail-end tracking scope, the organization’s CPO needed to drive operational improvement.

The company’s optimization initiative included 5 steps:

1. Create a cross functional team for various business units to participate.
2. Conduct a value engineering exercise to aggregate high value line items and classify tail-end spend across 12 categories.
3. Implement an RFX process to identify potential vendors who are ready to aggregate as per the company's spend structure design, and view the spend as a managed service.

By optimizing tail-end spend, the company saved over USD 1 million on a spend base of USD 300 million.

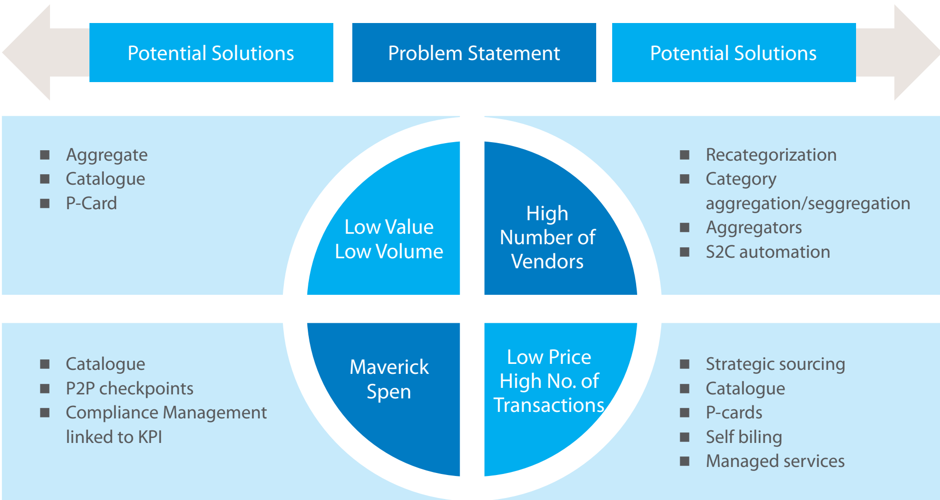
Companies need to avoid the one-size-fit-all approach, and instead start with a business-specific, customized tail spend strategy.

4. Negotiate lot rates based on an appropriate lotting strategy and implement RFP processes.
5. Deploy self and vendor managed electronic catalogs and outsource catalog management.

The organization’s spend management coverage now includes tail-end spends, bringing USD 200 million under direct spend management. By reducing its transaction count by over 50%, the company reduced its total cost of operations by over 25%.

An Implementation Framework for Your Business

Most businesses treat tail-end spend optimization as just another cost optimization exercise. However, given its unique nature, tail-end spend management requires differential treatment, and customized strategies.



Potential Solutions for Various Business Situations

Enhancing the Bottom Line: Benefits of Optimizing Tail-end Spend

TCS’ implementation experience shows that there is a clear and strong case for tail-end spend management:

- Reduce discretionary spend (15-20%) and transaction count (45-55%)
- Improve aggregation with 20-30% reduction in vendor count, resulting in efficient vendor management
- Reduce errors by 60-70% with effective automation
- Create time for strategic thinking and enterprise value creation activities

- Increase operational efficiency and profitability by 7-12%
- Improve transparency across processes, operations, and stakeholders, with e-auctions and standardization

Conclusion: The Road Ahead

Tail-end spend optimization is not just a onetime exercise. It's important for businesses to keep pace with evolving industry standards and benchmarks. While your company focuses on the 20% strategic suppliers that make up 80% of your spend, optimizing the balance 20% that goes to 80% of your suppliers is equally important. Therefore, despite its low value, large volume nature, tail end spend management must be part of your business' strategic agenda.

About The Author

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A part of Tata Consultancy Services' (TCS') Global Consulting Practice (GCP), Chand K Raina (CK) is a supply chain management (SCM) expert with over 14 years of experience. He has worked with clients across industries and geographies, designing, developing and deploying SCM practices.

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