INFLATION AND SUPPLY CHAIN
DISRUPTIONS DICTATE A NEW REALITY

Creating a CFO/CPO Strategic Partnership

The unprecedented stress that the current market developments places on business, strengthens our long-held belief that the Finance and Procurement functions should form a strategic power team within any company.

Procurement is at the forefront of market developments regarding strategic and operational cost drivers. These insights should be structurally integrated in the financial target setting and planning.

Moreover, when a company's supply and cost objectives and market reality are transparent and aligned between finance and procurement, significant savings can be unlocked, innovations created and business continuity guaranteed.

In this paper, we share some of our insights on fundamentals to help achieve that goal.

WHO IS ACCOUNTABLE?

In short, it should be a team effort.

A company's financial objectives come from the top and filter down. Therefore, in an ideal world, its procurement strategy would be aligned with the longterm business strategy.

That, however, is not always the case. In fact, there is often a fundamental lack of spending visibility in many companies. Exacerbated by the number of decision influencers, the case for strategic integration becomes clear.

Procurement managers need to think like a CFO. They need to be profit-oriented, risk-aware and aligned with the company strategy.

When is it difficult for a CPO to have a strong grip on financial performance?

- A lack of IT tools that make financial KPIs on spend and savings measurable.
- Playing a secondary role in planning cycles, they are unable to contribute to the setting of targets and the understanding of cost developments.
- No formal procurement responsibility to contribute towards measurement and results.
- Weak integration of procurement reporting and processes into corporate financial structures.
- A disconnect from finance operations in day-today procurement activities.
- Weak communication between procurement leadership and the executive team.

CAN WE SET OBJECTIVES TOGETHER?

Without setting clear and measurable goals, you cannot judge an activity plan to be either a success or a failure. That is no different in Procurement. After all, a large number of its objectives are financial.

Here are a few questions to keep in mind while you set those objectives:

- Has the CFO defined specific spend budgets for the various departments/divisions?
- Are these linked to cost reduction targets? What is their rationale?
- Are these targets operationalised with procurement in a concrete and detailed plan of action on price down versus cost down measures?
- Who is accountable for the final result?

Input from both end-users and subject matter experts (such as IT or ingredients) is crucial for setting realistic goals and receiving a broad team buy-in from the outset.

And as with all strategic plans, target achievement requires reaffirming the message repeatedly!

IS OUR SPEND VISIBLE AND MANAGED?

Before taking stock of saving potential, a company needs to be aware of its actual spending.

That sounds a lot easier on paper than it is in practice. Why is that?

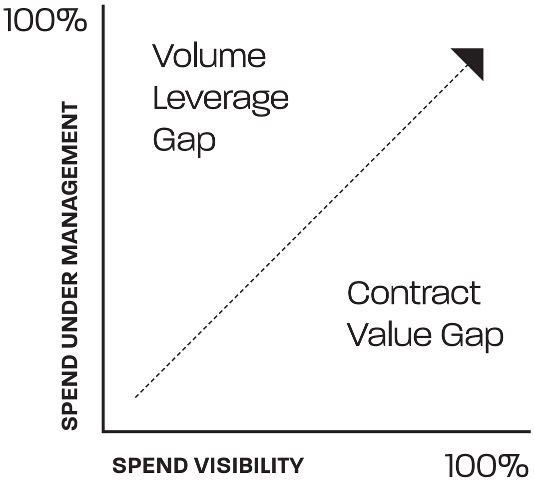
To have a complete overview of spend, a company needs to make sure:

- It has a logical taxonomy of cost accounts and cost centres (transparency).
- This is fully implemented across all departments, divisions and geographic locations throughout the organisation (consistency).
- It is applied to all external spend (compliance).
- It is applied in an administratively correct and comprehensive way (accuracy).

In procurement, an early indicator for successful cost management is ‘spend under management’. Its definition depends on the levels of maturity and ambition of an organisation.

However, for our exercise here we describe it as the share of total expenses that passes through the procurement organisation, at least administratively.


DATA ANALYTICS
Q1
Q2
Jan. Feb. Mar. Apr. May. Jun. Jul. Aug. Sep. Oct. Nov. Dec.
WORLDWIDE DELIVERY



Further on the experience curve comes spend:

- being embedded in a source-to-pay process (negotiation)
- being embedded in a vendor contract (compliance)
- being measured and analysed by procurement in pre-set intervals (monitoring).

The higher the share of spend under management, the higher the level of insights, control and, thus, improvements. A spend under management share of 70-90 % is a high target to aim for. Still, many companies do not even reach 30%. Clearly, without precise knowledge of expense details, there cannot be any target setting, let alone monitoring.
Any arrangement between procurement and finance will be based on flawed information.

Obviously, the highest potential for cost reduction is reached with the best possible combination of visibility and management. This principle can be applied to overall spending or a specific expense category. So, let's say that a company's visibility of its travel expenses is high due to a good expense management tool but poorly managed from a commercial and compliance perspective. Procurement value is lost (value gap).

On the other hand, procurement might have the perfect contract management process in place. But if it is ignored by end-users, part of the spend volume cannot be leveraged in full (leverage gap).

DO WE HAVE THE RIGHT TOOLS AND PROCESSES?

The starting point of any successful cost management exercise is a well-functioning procure-to-pay (P2P) process.

All expenses must at least be documented (if not approved) through a purchase order. The majority of companies already have this in place. But, in general, there is still a significant improvement potential in terms of:

- Ensuring that the generated data is accurate and complete
- Leveraging data as a basis for target setting, monitoring and analysis
- Improving cost category strategies and vendor management.

CFOs and CPOs should jointly be revisiting their supporting IT infrastructure. They will then often realise that we are only at the beginning of a dramatic transformation in operational procurement. Accounts payable tasks, which are today carried out manually, will become a fully automated process.

E-procurement developments to follow:

- AI and robotic process automation will drive P2P processes
- Self-guided buying through multi-vendor catalogue platforms
- Analytics will offer a significant competitive advantage
- Procurement as a third-party service will grow in relevance as a flexible outsourcing alternative
- Blockchain technology will become part of the procurement infrastructure.

DO WE HAVE EFFECTIVE OPEX POLICIES?

We should not overlook where business operating expenses originate in the organisation.

Who are the 'end-users'? Within which guardrails are they buying?

From fleet and travel expenses to office supplies, telecommunication and factory consumables, all expenses must comply with standards set internally.

These standards can range from unwritten rules to policies formally agreed by top management. But even when policies are in place, the CFO should not be complacent. Procurement can play an important supporting role here as an agent of change.

Set clear standards and policies, as you do for raw materials. Travel expenses are only reimbursable when booked through the company's web portal. Define a limited catalogue for office supplies and stick to it.

Managing expectations upfront can save a lot of time and energy.

ARE WE FACING REALITY? REPORTING ACTUAL SAVINGS

Savings are only savings when they have a tangible and measurable effect on the bottom line. It is the responsibility of Procurement management to ensure this happens.

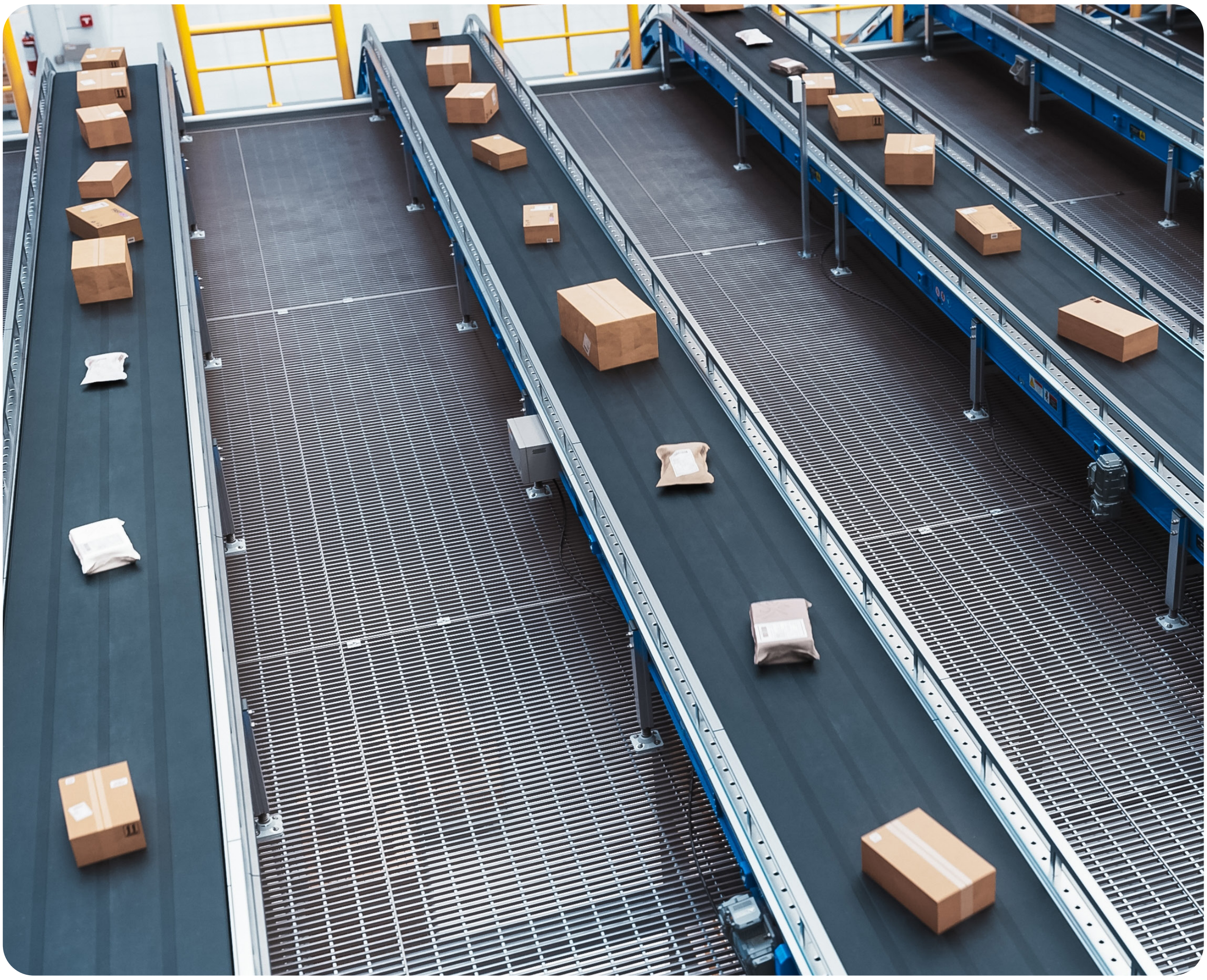
You should have these key actions discussed by management:

- Agree on baseline spending and reference prices in advance
- Always apply the total cost of ownership (TCO) principle and do not ignore any relevant costs made through the ordering and consumption process
- Don't report on identified savings only. They mean nothing. It is all about achieved cost reductions
- Make savings sustainable. Create rolling saving plans. Fill the savings pipeline
- Implement savings dashboards from a category bottom-up aggregation
- Saving milestones are to be monitored and steered against in case of underachievement
- Deviations are to be met by alternative strategies and action in time.

Today, it is our belief that the procurement function covers more than cost savings only.

But business operating cost and working capital reduction, being two of the most tangible contributions to corporate (financial) performance, deserve to be managed professionally.

That will only happen when the CFO and CPO talk and agree on the best way forward.



AGENDA TOPICS FOR YOUR NEXT CFO/CPO MEETING

Ownership:

- Agree on who is responsible for the actual saving result
- Are cost-saving accountabilities clearly defined between ourselves?
- Is the executive board on the same page?

Target Setting:

- Do clear savings and business continuity targets exist within our organisation?
- Are they broken down into actionable departmental clusters?
- Does procurement have a clear role in long-term sustainable saving planning?

Spend Under Management:

- Have we set targets for spend visibility and spend under management?
- How do we make sure these are achieved in reality?
- What category spend deserves priority to be actively managed next?
  How will we implement this?

Tools and Processes:

- Does our ERP system sufficiently support our ambitions of managed cost reduction?
- Are we aware of the latest available market solutions?
- Do we understand if and how cloud-based S2P/P2P tools could close the gap?

Policies:

- Is our top 80% spend governed by clear procurement policies?
- Are these policies well documented, owned, communicated and endorsed?
- What are our ambitions to cover the other 20%?

Reporting:

- Do we have a robust saving reporting process in place?
- Are savings traceable in our financial reporting?
- Are saving achievements incentivised by top management?

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