



**Five Strategies To Impact  
Working Capital:  
Procurement's Role In  
Driving Performance**

AN EMPTORIS POINT OF VIEW

Emptoris, Inc.  
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## The Panel

The panelists participating in the development of the “Five Strategies for CFOs” included **Vincent Donargo**, Senior Vice President, Chief Accounting Officer and Controller with Brightpoint, Inc.; **Robert A. Rudzki**, co-author of the book “*Straight to the Bottom Line*” who has held various executive management positions in Finance, Accounting and Procurement; Kirit Pandit, author of “*Spend Analysis: The Window into Strategic Sourcing*” and consultant who has implemented numerous spend programs at *Global 2000* companies; **Anuj Saxena**, author of the book, “*Enterprise Contract Management: A Practical Guide to Successfully Implementing an ECM Solution*” and a Project Executive with IBM Global Business Services; and **Kris Timmermans**, the Managing Partner, Global Sourcing & Procurement practice with Accenture. **John Belchers**, who has served as CFO at four publicly-traded companies including Gensym Corporation and Microprose, Inc., and currently serves as CFO at Emptoris, Inc., also contributed to the discussion. The panel discussion was sponsored by Emptoris, a leading provider of enterprise spend and contract management software.

# The Five Strategies

Current economic conditions and a tight credit market are driving CFOs to step-up efforts to preserve cash, control spending and reduce costs. In parallel, there are increased risks associated with cash management, supplier and vendor failures, and fluctuating costs. As stated by Robert A. Rudzki, author of the book *Straight to the Bottom Line*, "There are too many examples of companies that have tried the 'quick and dirty' approach to cost reduction, only to find that their wins were not sustainable over time." Financial managers need to think strategically to ensure meaningful, effective action with sustainable results.

To this end, Emptoris, a leading provider of spend and contract management solutions, assembled a panel of financial and business consulting experts that have worked and consulted with leading *Fortune 1000* companies and asked them to offer their advice on actions to take to gain greater control over spending and to lower costs in the current economic environment.

The panel examined current trends in cash management, cost reduction and technology, and considered the "lessons learned" from the last economic downturn and recovery. The panel included senior financial executives from *Global 2000* companies, leading business and financial consultants, as well as several book authors who have written about financial management and technology. The group focused on examining strategies for cash optimization, cost reduction and risk management, among other areas.

At the conclusion of the sessions, the panel developed "Five Strategies for Immediate and Sustainable Impact on Working Capital and the Bottom Line." These strategies are detailed below:

1. **Securing and Preserving Cash:** Leveraging Often Overlooked Opportunities in *Accounts Payable* and *Inventory Management*
2. **Getting Costs Down:** Procurement Excellence as a Key Factor in Reducing Costs in a Sustainable Manner
3. **Reducing Risks in a Risky Environment:** Developing and Managing Key Risk Indicators (KRIs)
4. **Getting True Visibility Into Corporate Spending:** *Fortune 1000* Companies Often Operate in the Dark
5. **Stopping a Thousand Leaks:** A Commitment to Active Compliance Can Impact the Bottom Line

*"The current economic environment presents a number of challenges, but also presents opportunities. This is a time when companies often reshape their processes and focus on areas within their control, such as spending and working capital management. As we adapt to become more efficient, it's important that the strategies we implement today will be sustainable and lead to a stronger company tomorrow,"*

*Vincent Donargo, Senior Vice President, Chief Accounting Officer and Controller with Brightpoint, Inc.*

## **1. Securing and Preserving Cash – Opportunities in Accounts Payable and Inventory Are Largely Untapped**

Financial experts emphasize, this is not just a recession, it's a recession with an underlying credit crisis. As a result, companies are working overtime to secure access to capital and preserve their cash on hand. Companies are particularly focused on reducing working capital requirements to minimize reliance on bank borrowing. Experts point to the timing of accounts payable and accounts receivable as a significant area where cash can be taken out of the system. Further, the panel said that efforts in the areas of reducing salary/labor costs and controlling employee benefit costs tend to be "well tapped" or mature efforts at Global 2000 companies; whereas the opportunities for cash savings and preservation in accounts payable and inventory management are largely untapped or unfulfilled.

A quick analysis of a company's DPO, days payable outstanding, in comparison with industry peers, often reveals a high potential to reduce working capital requirements and preserve cash. Take a manufacturing company, per every billion of spend there is typically \$50 million of extra spending on expedited accounts payable. For a \$10 billion company that is potentially \$500 million in cash preservation just in accounts payable.

Managing payment terms with suppliers is often handled on a supplier by supplier basis, creating an opportunity to centrally manage the process. According to industry experts, many trading partners are open to modify payment terms, specifically where the modification involves discounts for early payment. Advanced procurement organizations are making payment terms part of their Request for Proposal process, and are pleased with their supplier responses.

Spend analysis and contract management technologies can help with cash management. Having clear visibility to contract terms can uncover untapped opportunities for negotiation, or could reveal differences between the contractual terms and what is actually being invoiced. Detailed analysis of your company's spend is imperative to identify the areas to target to address payment terms.

## **2. Getting Costs Down – Sustainability is Key, Procurement Excellence Holds Significant Opportunity**

In classic financial management courses, the professor will tell you that to enhance shareholder value you must achieve returns on invested capital greater than your company's cost of capital. The best-performing companies, and the best stocks over time, tend to be those that have ROIC greater than their corporate cost of capital.

The flip side of the equation is more sobering. When your ROIC is less than your cost of capital, the lifeblood of your firm is draining away – you are among the walking wounded. How fast your firm dies will depend on how much of a shortfall exists between ROIC and cost of capital, and

how much you have in financial reserves to fund that shortfall. In the absence of ROIC improving, the firm inevitably disappears.

ROIC is typically defined as earnings of the business, divided by the capital invested in the business.

When you increase profits, that improves ROIC, and it also improves cash flow. When you improve capital utilization, that improves ROIC and cash flow. When you improve both profits and capital utilization, you create a powerful compounding effect on both ROIC and cash flow.

Obviously, then, ROIC is dependent on the profits of a business, in relation to the assets invested in the business. As we'll see shortly, advanced procurement can have an enormous positive impact on all elements of the ROIC equation.

With regard to the top-line of the income statement - the revenue line - success with customers is often heavily influenced by the effectiveness of your supply chain. How well do your suppliers work in tandem with your own organization? Getting the supply side in good shape can help to grow revenues and change the competitive dynamics in your favor. Just imagine the impact on your business if you could make it to market with new products months - if not years - ahead of your competition, and with a lower cost structure.

With regard to costs, in most companies more than 50% of the cost structure relates to procurement and supply chain costs. In spite of that importance, most senior executives don't know where to start to dramatically reduce those costs and improve their bottom line on a sustainable basis.

And, with regard to the assets invested in the business, advanced procurement and supply management – working with the supply base - can have a significant impact on working capital levels, and on capital projects, thereby favorably impacting ROIC.

### **3. Reducing Risks in a Risky Environment – Developing and Managing Key Risk Indicators (KRIs)**

In the last 20 years, world-class procurement departments have adopted new, powerful processes and tools – to unlock and create new shareholder value, to accelerate change, and to create powerful supply chains that their competitors are now trying to catch up with.

So, what are the key strategies that you need to know in order to add value to your bottom line?

When it comes to improving margins and profits, procurement can have an impact through initiatives that favorably impact revenues – and other initiatives that directly target costs of the business.

For example, on the revenue enhancement side, more companies are beginning to realize the value of working collaboratively with suppliers on innovation, and on reducing the cycle time from product concept through delivering that new product to the marketplace.

With regard to costs, world class companies view all areas of spend as being within the scope of modern procurement practices (i.e. no sacred cows), and pay particular attention to reducing maverick spend and ensuring compliance with negotiated contracts.

When it comes to improving the capital intensity of the business, procurement can have an impact through initiatives that favorably impact working capital – and initiatives that impact the total investment in capital assets.

For example, payments terms offer enormous opportunity to add value and financial flexibility, by negotiating longer “net” terms, plus attractive discount options if you elect to pay early. Similarly, inventory programs offer the opportunity to free up significant working capital, and so-called “asset recovery” initiatives offer a disciplined approach to realizing value from underutilized or idle plant and equipment.

To summarize the framework we have discussed so far, advanced procurement – if given the right role, the right tools and adequate resources – can directly impact all four strategic drivers of ROIC.

## **4 Getting Real Time Visibility Into Corporate Spending – Fortune 1000 Companies Operate in the Dark without Spend Visibility**

Just a fraction of Fortune 1000 companies have current, accurate visibility into their spending. Experts say the first step to better managing corporate finances is to have clear, accurate, and current spend visibility. Good spend visibility enables smarter strategies for cash management and cost reduction. The good news is, gaining global enterprise visibility into spending is much easier now than it was even a few years ago. With software programs or outsourced aggregation of data, companies can get a current, enterprise-wide view into spending detailed by category and operations. For relatively minimal costs, it is realistic today to have monthly spend visibility company-wide.

Companies have long been shackled by the dispersed and disparate nature of their spend data. It's stuck in dozens of different systems and departments around the globe. However, today there are software tools and outsourced processes that can be used to give a current, consolidated view of spending. Leading spend analysis software technologies can aggregate data from over two dozen different systems, including every major ERP platform, and can analyze and drill down on spending along dozens of different dimensions including by commodity, cost center, GL account, geography, time, payment terms, and more.

“How can you control spending when you don’t even know what you’re spending? Most Fortune 1000 companies do not have a 360-degree real time view into their spending. The average CEO, CFO and CPO are typically looking at division or departmental spend data which is often badly out-dated. It’s their dirty little secret,” said Kirit Pandit, author of “Spend Analysis: The Window into Strategic Sourcing.”

## **5. Stopping a Thousand Leaks – A Commitment to Active Compliance Can Impact the Bottom Line**

Although great gains have been made in controlling and even reducing costs in recent years, particularly with the application of technology, outsourcing and Low Cost Country Sourcing (LCCS), there is still significant leakage and wasteful spending at the average Global 2000 company. One of the biggest areas of loss for companies is in non-compliance to existing contracts. Whether it’s enforcing negotiated pricing, realizing quantity discounts or ensuring quality standards and associated penalties and discounts, spend and contract compliance becomes even more essential in a recessionary environment.

Companies often do a solid job of identifying savings opportunities, however it is in regulating and enforcing compliance to those savings where they often breakdown. Technologies such as contract management software can help companies proactively enforce and ensure compliance. Anuj Saxena, author of the book, “Enterprise Contract Management: A Practical Guide to Successfully Implementing an ECM Solution” and a Project Executive with IBM Global Business Services, notes that the application of technology takes an impossible task and makes it manageable.” Spend analysis helps with identifying savings opportunities, sourcing software with getting reduced prices in those categories, and contract software with enforcing spend guidelines and savings. Such a holistic approach that can reap significant new savings.

## For Additional Information:

For further information on this topic, we recommend reading, *"Surviving and Thriving in an Economic Downturn With World Class Supply Management,"* a white paper developed by Robert Rudzki. Written from the perspective of the executive office, this white paper explains how world class supply management can directly drive improvements in a company's return on invested capital (ROIC) and earnings per share (EPS). This paper along with a number of other resources is available for free download on [www.emptoris.com](http://www.emptoris.com) in the "Library".



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