

Using a rapid procurement transformation to generate cash quickly

When time is short, a radical new approach helps procurement leaders find savings fast.

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Faced with slow revenue growth, intensified competition and greater investor focus on cash flow, companies in several sectors have adopted turnaround-like programs to improve bottom-line performance. These programs, such as [corporate turnarounds and restructuring programs](#), seek to deliver maximum cash impact in a minimum period of time. They typically focus strongly on addressing external spend as the fastest, surest, and least painful way to rapidly improve cash flow. Because a focus on external spending produces substantial benefits early in a turnaround program, companies gain strong momentum and time to pursue far more nuanced efforts later on. Procurement is therefore an important focal point for many transformations.

Companies can capture significant value as external spend can typically run from 30 to 70 percent of a company's total expenditure, depending on the industry. In our experience, bottom-line savings of 15 percent are achievable, resulting in a 5 to 10 percent reduction in the overall cost base. Up to half of these savings can be delivered within six months. This impact can be realized without the disruption of FTE reductions or incurring market risks associated with price increases. A rapid external-spend restructuring program provides the additional benefit of building a more commercially aggressive organization for the longer term.

Although many companies have experience with programs to improve procurement performance, companies under cash pressure require a more fit-for-purpose approach to meet their need for rapid cash generation. The aggressive cost reductions needed in turnaround situations require very different measures than traditional procurement improvement program (Exhibit 1).

Exhibit 1**Turnaround programs have very different characteristics than traditional procurement improvement programs.**

Traditional procurement	Turnaround procurement approach
Sourcing programs focus on long-term strategy within the existing procurement process parameters	Turnaround programs inculcate an owner's spend control and profit-driven mind-set; focus is on an accelerated approach for maximizing cash impact
CPO-driven programs empower the procurement teams but lack active CEO or business stakeholder participation	Programs are CEO-owned and jointly driven by the entire top team; CEOs are seen as change leaders and are the catalyst for radical thinking across the organization
Focus is on procurement best practices: "Did you follow the ideal procurement process?"	Focus is on identifying fit-for-purpose levers geared to yielding cash quickly
Continuous improvement plans have quarterly or semiannual reviews	Line-led granular cost impact initiatives have detailed work plans and regular short-interval-tracking mechanisms
Programs track value delivered to the business by the procurement team and negotiate a sign-off	Programs track CFO verified bottom-line impact delivered from spend reduction initiatives

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To succeed, companies must go beyond the usual central procurement-led annual sourcing exercise by making external-spend reduction an overall business a priority for the entire management team. Additionally, executives and staff at all levels of the organization must adopt an owner's mindset, placing a relentless focus on identifying all opportunities for improving operating costs. Companies also require disciplined execution and performance management to ensure value is delivered to the bottom line.

- The distinctiveness of a rapid transformation approach can be expressed through five guiding principles:
- Adopt an owner's mind-set towards external spend
- Ensure active involvement by the CEO and the board
- Identify fit-for-purpose levers that generate cash rapidly
- Use line-led, granular initiatives to drive value
- Establish an unrelenting performance infrastructure to ensure value accretion.

This approach can be deployed in any situation that requires a significant and rapid cost improvement. While the genesis of this approach is in restructuring or turnaround situations, we have found that similar principles can be applied effectively to other, non-turnaround situations where CEOs are looking to pursue significant improvements in the cost base, and are willing to make tough decisions.

1. Adopt an owner's mind-set towards external spend

Employees throughout the organization must adopt an owner's mindset toward controlling spend and generating immediate cash impact. This mindset entails constantly evaluating the full potential behind each spend category, refusing to settle for anything less than this, and continually asking, "What would I do if I owned this business?" Executives and key stakeholders should agree on targets and be incentivized to deliver on these targets as well as related initiatives. Each contract should be assessed through the lens of an investor-owner. The focus should be on the company's sustainability, rather than fairness to suppliers.

To instill an owner's mindset, companies must rapidly reset spending behavior throughout the organization, so that there is no appetite for non-critical spend. Deployment of top-down mechanisms—such as demand rationalization, travel restrictions, challenging open purchase orders and opening all contracts for negotiation—should be implemented to prevent any non-critical spend from occurring.

A "spend-control tower" is an effective way to manage indirect spend, as well as contractor and FTE costs and other discretionary spend. The implementation of a control tower typically yields savings of 15 to 30 percent on indirect spend within the first month (see sidebar, "What a spend-control tower can do"). It also sets the stage for [zero-based budgeting](#), which requires a mindset that challenges every dollar in the budget before it is spent. Mindsets must transition from "I will spend every dollar in my budget" to "I have no budget and will only spend where critical."

What a spend-control tower can do

CXOs can make several no-regret moves to generate immediate cash impact from the very first day. The spend-control tower can monitor the progress of these moves. Examples include:

- Stop all discretionary spending (such as "nice-to-have" insurance policies and entertainment)
- Rationalize purchasing cards or credit cards in order to drive more spend onto purchase orders
- Cut (or hire) all contractors with more than one year of service
- Restrict mobile phones paid for by the company
- Tighten the travel policy (such as by prohibiting business class travel or implementing the use of non-flexible fares)
- Sell off obsolete inventory at a discount to generate cash
- De-list long tail vendors to consolidate spend to preferred vendors

2. Ensure active involvement by the CEO and the executive team

Traditionally, procurement programs have been led by the procurement organization, working in tandem with business units to elicit buy-in and

shared commitment to savings targets. In turnarounds, it is critical that the CEO and the top team commit to the importance of external-spend reductions early on and rally the organization around the program. Given that, as noted above, external spend typically accounts for 30 to 70 percent of a company's total expenditure, this topic should be a priority for the CEO.

[CEOs should be seen as their company's change leader](#), responsible for triggering a radical rethinking of the operating model and the company's conventional wisdom (see sidebar, "How one CEO became a change leader"). They must be a role model, leading with actions as well as words – and they can carry out a variety of symbolic actions that demonstrate their commitment to the transformation to the entire organization. Examples include:

- Role modeling cost reduction programs, such as traveling in economy class instead of business class,
- Participating in team review sessions on cost reduction and helping to accelerate decision making,
- Rewarding individuals who have helped the organization achieve significant cost reduction,
- Communicating the transformation's progress and reiterating a personal commitment to the program to the organization on a frequent basis.

How one CEO became a change leader

In one example, the CEO of a mining company role modeled his personal commitment and led the procurement program by:

- Communicating and regularly reinforcing the program's strategic importance to the overall business, which helped achieve buy-in from all key stakeholders,
- Helping to identify and free-up the best and the brightest in the organization to participate in the program,
- Conducting weekly reviews to assess progress, challenge the program team, and rapidly resolve issues (including during his vacation), thereby role modeling the personal commitment that he expected from the team.

The CEO also participated in critical negotiations with key suppliers, including travelling halfway around the world for a key negotiation session. This effort helped achieve superior negotiation outcomes, as well as becoming a strong motivator for the procurement team.

3. Identify fit-for-purpose levers that generate cash rapidly

To maximize the value realized, companies must implement a suite of tools, levers, and capabilities to ensure (see Exhibit 2). Teams should apply technical tools, such as clean-sheet costing and teardowns, to define the maximum potential available. Team members should be encouraged to chase value as if their own money were at stake.

Exhibit 2

A turnaround approach requires considering the full set of modes for each lever to maximize cash savings.

NOT EXHAUSTIVE

		Typical modes	Turnaround modes
Supplier levers	Reduce price	<ul style="list-style-type: none"> • Consolidate suppliers and introduce new lower-cost suppliers • Ask existing supplier for discount or switch volume among existing suppliers 	<ul style="list-style-type: none"> • Demand discount/restructure pricing mechanism • Insource rather than contract work and increase/reduce market price exposure • Establish new supply chains
	Change terms	<ul style="list-style-type: none"> • Increase/decrease contract length • Change payment terms • Remove late delivery charges or include, reduce, or remove threshold for a volume rebate 	<ul style="list-style-type: none"> • Ask suppliers to suggest price relief in exchange for changing any contract clause • Exchange warranty liability for cash savings • Increase/reduce take-or-pay or exclusivity • Reduce availability guarantees and inventory holding requirements
Demand levers	Reduce usage	<ul style="list-style-type: none"> • Track individual usage • Control discretionary spend 	<ul style="list-style-type: none"> • Set aggressive targets based on technical limit • Remove dollars from budgets absent of a specific initiative • Impose reduction on usage in short-term to test the limit • Reduce planned duration of maintenance activities • Reduce frequency and extent of maintenance
	Change spec	<ul style="list-style-type: none"> • Reduce number of unique products (SKUs) • Standardize goods/services for purchase • Reduce specifications 	<ul style="list-style-type: none"> • Substitute branded products with supplier unbranded substitutes • Reduce grade of contractors to minimum requirements
Top-down levers	Control system	<ul style="list-style-type: none"> • Remove unwanted suppliers • Raise approval to add new suppliers 	<ul style="list-style-type: none"> • Reduce obsolete inventory holdings and optimize order size and timing • Ban all noncompliant purchase orders and inform all suppliers
	Control process	<ul style="list-style-type: none"> • Reduce spend possible without sign-off • Enforce competitive bidding • Ensure compliance to terms and service levels 	<ul style="list-style-type: none"> • Ban/limit discretionary spend • Enforce purchasing process • Restrict time-sensitive orders

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However, depending on the company's context or the urgency of their requirement for cash, it may be prudent to prioritize speed over maximum value for certain spend categories.

Although it takes 12 to 18 months to realize the full impact of most benefits of such a program, there are a few initiatives that can deliver cash early on (for an example, see sidebar, “Fleet-size rationalization for immediate cash impact”). This short-term impact is invaluable to the bottom line and helps the organization gain confidence in its ability to deliver the turnaround. Short-term wins include:

- Demand rationalization, which can help manage the scope of activities and is effective immediately
- Reopening all contracts for negotiation and creating a deal calendar for upcoming negotiations as a starting point for the team
- Estimating and managing off-contract spend through a spend-control tower. By challenging all purchase requisitions relative to demand, substitution, scope and price levers, a control tower rapidly instills a cost-conscious culture throughout the business.

Teams should also examine the full suite of procurement levers available and evaluate each lever to determine its applicability and suitability.

Fleet-size rationalization for immediate cash impact

A healthcare company undergoing a rapid transformation to improve its financial position targeted opportunities that would rapidly generate cash. The company had a fleet of more than 100 vehicles, which the staff used to travel between multiple office locations in a city and for work-related callouts. Maintaining the fleet entailed significant operational and capital expenses.

The fleet comprised a mix of owned and leased vehicles. Leased vehicles came from a single provider, with all ongoing expenses included in the monthly lease cost. The fleet was designed to meet peak demand.

The procurement team, in collaboration with business units, reviewed fleet spend to identify cost reduction opportunities with immediate cash impact. Three key cost-reduction levers were identified:

- Demand management, which included managing vehicle utilization and aligning the type of vehicles in the fleet with their intended use
- Canceling all new and replacement orders for vehicles
- Implementing strict process controls, which ensured better availability of vehicles during periods of peak demand.

The improvements from the vehicle rationalization initiative resulted in an immediate reduction in fleet expenses of 20 percent. The team put in place KPIs to help sustain these improvements.

4. Use line-led, granular initiatives to drive value

To maximize the value delivered by procurement in a turnaround situation, it is critical to create a granular set of initiatives that have stretch targets and well-defined owners. This consolidated list of initiatives, consisting of hundreds of initiatives with improvement value and delivery timelines developed by the procurement and business stakeholders, forms the bankable plan against which the entire organization is accountable. The upfront development of this bankable plan must promote four critical success factors:

- A granular set of initiatives, all expected to entail strategic supplier negotiations that correspond to individual contracts ideally
- Stretch targets for all initiatives, requiring procurement leaders to tell bold stories and challenge targets
- Ownership of initiatives by contract owners, not category managers. Contract owners deliver the value, while receiving guidance from category managers
- Setting granular, trackable milestones to ensure feedback on the progress of delivering the pipeline of initiatives. It is also crucial to involve business units at this stage of the planning process, to ensure they are part of the journey from the beginning and support the eventual delivery of cash.

These line-led initiatives deliver best value when they are grounded in facts, based on solid analyses, and executed through strong collaboration between procurement and business units.

To rapidly capture commercial savings from procurement, companies can establish a “Negotiation Factory”—a systematic and repeatable process for supplier engagement. A negotiation factory empowers negotiation teams with standardized best practice tools such as detailed RFQ pricing templates, best of benchmarking, negotiation scripts, and role plays. By deploying the best procurement resources in the negotiation, businesses can ensure that they maximize the value from all negotiations, instead of just the ones conducted by highly skilled contract owners (see sidebar, “How a negotiation factory enables cross-functional collaboration between procurement and business stakeholders”).

How a negotiation factory enables cross-functional collaboration between procurement and business stakeholders

A mining company has several operational sites within a region and deploys very strict safety measures. The company launched an initiative to reduce the cost of safety inspections and audit services across its sites. These sites used various suppliers, with each site having its own guidelines for service-level requirements. The procurement team had initially targeted a 10 percent reduction based on potential supplier consolidation and rate renegotiation.

The company set up a negotiation factory, with a team consisting of procurement and technical support leaders representing the sites. The team agreed on an aspirational savings target of 30 percent, and systematically assessed all opportunities to reduce cost. In addition to the supplier consolidation and rate reduction savings levers, the team identified incremental value from standardizing services across sites and reducing demand by removing unrequired services. To keep the initiative focused on execution speed, the team developed a detailed milestone plan, which had short-interval tracking in place to prevent any value erosion.

The team leveraged standardized negotiation tools – such as comprehensive RFQ pricing templates and best of benchmarking – to compile and analyze the detailed supplier responses. To prepare for negotiations, the team developed detailed scripts and participated in role-play sessions.

The initiative created a compelling case describing the company's situation and a credible and viable alternative source of supply. Incumbent suppliers took notice, recognizing that they could lose future business unless they were able to reduce prices immediately. Ultimately, one of the company's existing minority suppliers was able to replace the existing majority services vendor by providing a more robust services solution across the sites and reducing current costs by more than 30 percent.

5. Establish an unrelenting performance infrastructure to ensure value accretion

In rapid transformations, close-to-flawless execution is required to ensure success. Disciplined execution requires unrelenting performance tracking. Companies need to develop granular implementation plans and then relentlessly monitor progress against the plan to track bottom-line impact. Each cost reduction initiative should have detailed activities, milestones, owners, and a clear link to value drivers and cash.

Procurement initiatives should be tracked on three levels:

- **Implementation milestones.** Tracking actions and milestones on a weekly basis helps to ensure that initiatives are advancing in accordance with the plan and enables the company to immediately identify and address any roadblocks. Tracking implementation can also reveal opportunities for accelerating delivery.
- **Impact targets.** Tracking changes in the value drivers and KPIs that each initiative is intended to target ensures that initiatives deliver real impact. It also enables rapid intervention in cases where the expected impact is not achieved.
- **Bottom-line results.** Tracking actual bottom-line results ensures that cash is being delivered. Under normal conditions, the company should track bottom-line results monthly;

however, if the company is experiencing a severe cash crunch, it may need to conduct this tracking on a weekly basis through a “cash war room.”

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Reducing external spend to deliver rapid cost improvements should not be regarded as a one-time event. To sustain the impact, a company must fundamentally change how executives and staff at all levels of the organization think about procurement. By adopting these five principles discussed above, companies will begin the process of instilling an owner’s mindset across the organization, breaking down cross-functional barriers, and elevating procurement’s importance as a vital value lever. The first companies to accomplish this transformation will achieve a major competitive advantage through superior bottom-line performance■

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