Innovating Tail Spend Management
An opportunity to improve P&L and working capital

Tail spend is traditionally considered the weak link of spend management. This is mainly because purchases in the tail account for only one-fifth of total spend but constitute the vast majority of its volume. With innovative solutions becoming available in the market, it’s easier to enhance tail spend management and transparency without any increase in effort. This leads to P&L savings ranging from 5% to 20% of total spend in scope.
Introduction

To improve working capital, many organizations have taken measures to improve their cash balance, including: leading and lagging, enforcing collection policies and delaying payments to critical suppliers, lowering safety stock levels and selling AR positions to factoring companies. These measures require constant vigilance by management; as soon as focus slips, working capital values decline immediately.

The market for procurement and sourcing technology is rapidly evolving. Digital and analytics capabilities are providing more sustainable opportunities for organizations to improve cash management. Procurement technology is being modernized through virtual assistants, cloud-based business intelligence tools and catalogue solutions (including marketplaces). As part of this digital revolution, all major Procure-to-Pay software vendors have integrated guided buying and self-service into their technology. This innovative procurement approach gives organizations two important benefits:

1. An increased independence for its users in procuring goods, which subsequently decreases pressure on procurement organizations.

2. The realization of financial benefits typical of open market economic models.

The rise of B2B marketplaces

The rise of B2B marketplaces and consolidators is a critical enabler for the optimization of tail spend management. Marketplaces are defined as virtual catalogs through which organizations can procure goods, ideally in a self-service manner. Examples of marketplace platforms are Amazon Business, Alibaba.com and eBay Business Supply, all B2B-focused.

These players provide catalogs that cluster many vendors in one place, from where organizations can buy mostly commodity products. More niche players, such as Corlido, SDI International and Candex, provide controlled catalogs that can cover a wider spectrum of procurement spend.

These niche players offer the opportunity to consolidate multiple vendors in dedicated and company-specific catalogs. As consolidators offer a higher degree of customization and control, these can be particularly useful for services-related spend or the procurement of specialized and high-risk products.

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<th>Criteria</th>
<th>Marketplaces^1</th>
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^1 The capabilities assessment of marketplaces and consolidators is to be considered indicative and may vary per specific solution
At the moment, there is no single dominant global player in the B2B marketplace arena, with each big player focusing on a specific geographical scope.

Tail spend opportunities

Tail spend is generally defined as the amount of money that an organization spends on purchases that make up approximately 80% of transactions but only 20% of total spend volume. As this characteristic suggests, tail spend transactions are mainly low-value, and often one-off purchases, which go out to a wide array of suppliers.

The efforts required to manage such high volume, combined with its lack of strategic importance, make tail spend a perfect candidate for being de-prioritized by procurement organizations. However, the same characteristics that lead tail spend to be considered procurement noise also hint at opportunities to optimize it.

There are multiple ways to improve tail spend. Examples include: streamlining processes (including process automation); rationalizing the number of suppliers; and adopting stringent policies. All these measures can be effective in improving tail spend, but they often require constant vigilance in order to retain control. Catalogs or other automated buying channels enable procurement teams to move certain categories from unmanaged to managed spend, leading to more sustainable and significant savings.
Next to improved user experience, there are financial improvement opportunities. Benefits unleashed by marketplaces and consolidators fall into the following categories:

**Vendor Management avoidance**
By transitioning a multitude of vendors to a single marketplace, total costs related to vendor management decrease.

**Manual PO process avoidance**
With a fully automatic PR/PO creation process for procurement through marketplaces, costs related to manual processing of Purchase Requests and Orders are avoided.

**Finance cost avoidance**
For purchases made through Marketplace invoices are submitted electronically, which leads to a simplified invoice handling for the Finance organization. Adoption of Ghost Cards for payment may further simplify the process.

**Purchase pricing competitiveness**
Marketplaces usage lead to more competitive pricing, either through an open market environment (virtual marketplaces) or through continuous market screening (non-virtual marketplaces).

**Procurement cost avoidance**
Certain procurement activities are shifted from procurement to marketplaces, leading to a decreased effort of the procurement organization.

**Rebates**
In case purchases are made through credit cards, rebates of approximately 1% of the spend are generated.

**Working Capital**
Standardization of payment terms for tail spend may lead to extended average payment terms.

From a working capital perspective, tail spend is often characterized by non-standardized and short payment terms: marketplaces and consolidators can support the standardization and the extension of payment terms, with positive effects on Days Payable Outstanding (DPO).

**How to start?**

How do you benefit from these innovative solutions? And how do you decide what is the preferred buying channel for your products and services? The first step of tail spend management is classifying spend categories based on spend value and risk.

After such categorization, it is easy to identify the right approach to each quadrant of the “spend allocation model”. The bottom left quadrant is the ideal target for a transition to marketplaces and consolidators, along with a part of the spend considered high-volume. Some of the high-risk spend can also be considered as candidates for such a transition under specific circumstances.

This open marketplace concept goes against traditional procurement practices (negotiating and enforcing strategic supply agreements for higher-value spend categories), which makes some procurement organizations hesitant to adopt these innovative approaches. Buy-in from the organization leadership is therefore a critical success criterion.

It helps to start with low-impact categories and have the concept grow into the organization. Typical and widely-adopted examples of such low-risk categories include: office supplies, MRO parts and basic facilities maintenance services. Most of the transactions in these categories are products or services low in both value and risk. These will provide the best testing ground. Once organizations are used to this concept and have proven its value, it can be more easily expanded to other categories.
Tail spend in the future

Thanks to the development of digital technologies, companies have the opportunity to create more value. B2B marketplaces are evolving quickly. Players like Alibaba and Amazon for Business are currently expanding their geographical scope and increasing the variety of products and services they offer. In addition, they are moving their focus from small and medium businesses to larger organizations. Niche consolidators, on the other hand, are also expanding their grasp and enhancing their offers.

These developments will give a big impetus to the professionalization of tail spend management. An increasing number of organizations have already started leveraging these solutions for improving P&L and working capital. We predict that more than 20% of B2B transactions will be procured through marketplace and/or consolidator solutions by 2025, potentially being expanded widely outside the tail spend category.
More information?

Want to know more about modernizing tail spend management? We are happy to help. Please contact Yvonne Daas or Pietro Moradei.

Contributors: Soumen Mukerji, Menno Boekhorst, Diana Taborda, Kevin Lalchand

Contact us:

Yvonne Daas
Partner
Mobile: +31 (0)6 1098 0167
Email: ydaas@deloitte.nl

Pietro Moradei
Manager
Mobile: +31 (0)6 5755 6148
Email: pmoradei@deloitte.nl