

# How to Manage Indirect Spend Categories



Imagine you're trapped on a desert island, with limited food supplies. And instead of carefully looking for ways to extract every possible ounce of nutrition and renewable resources from *every scrap of food* in your tiny island larder, you take a bite or two out of, say, 40% of your meals and then throw them away.

That's how many procurement organizations continue to approach indirect spend management, even in today's competitive, data-driven economy.

Indirect spend categories can account for up to 40% of a company's total expenditures—and that number climbs even higher at digital businesses whose indirect procurement occupies the role traditionally filled by direct procurement at more traditional organizations.

And yet, it is old-school cost management, rather than process optimization and value creation, which guides indirect spend management, creating an ever-widening competitive gap into which companies who stay the course may plummet.

In order to avoid this slow starvation, compete effectively, and capture the hidden cost savings and value buried in their supply chains, companies need a new, more

proactive approach to managing their indirect spend categories.

## Overcoming Challenges to Managing Indirect Spend Categories Effectively

The tendency many procurement teams have to place indirect spend management on the back burner is understandable, if regrettable. Using traditional methods, it's more difficult, for example, to draw a straight line between indirect spend categories and profitability (e.g., properly-sourced information technology (IT) services leading to less downtime) than it is to connect business-critical direct procurement materials to the bottom line (e.g., copper and silicon used to manufacture a processor manufacturer's chipsets).

Some of the most commonly used indirect spend categories include:

- Facilities
- Utilities
- Marketing
- Office supplies.
- Technology purchases.
- Human resources.
- Travel
- Outsourced services.

Despite its broad scope, managing indirect procurement represents a very specific set of challenges for organizations, including:

- **Greater complexity.** While direct procurement might include only a few raw materials, indirect spend categories can run the gamut from office supplies to utilities to breakroom snacks to maintenance, repair, and operations (MRO) costs. With such a diverse array of products and suppliers, building an effective indirect category management team and plan requires a much greater breadth and depth of expertise than direct procurement.

In addition, indirect spend is focused internally rather than externally; the goods and services purchased support the entire organization, not just direct materials for production, and often fall under the umbrella of "the

cost of doing business.” Without a clear spend management policy in place and the tools necessary to capture and manage all spend data, it’s all too easy for indirect spend to escape procurement’s control.

Finally, the value and savings created by an efficient and transparent indirect procurement strategy is more difficult for management to see without adequate data management, effective metrics (including key performance indicators, or KPIs) and process optimization. In those circumstances, it’s an uphill climb for procurement professionals to “connect the dots” and so key internal stakeholders such as upper management may not grasp the opportunities at hand.

- **Poorly managed or unmanaged spend.** As they are more difficult to monitor and manage, indirect spend categories may receive only minimal management—or none at all. For companies who don’t have well-developed spend management or category management plans in place for indirect procurement, it’s all too common for maverick spend, invoice fraud, and outright theft to steal value and reduce return on investment (ROI) along with hobbling any hope of truly strategic sourcing.
- **High spend frequency and low spend volume.** Indirect spend purchases vary widely in type, but are generally made frequently, have small individual values, and lower average spend totals than those made in direct categories do.

If the procurement team is still relying on last-gen tech or manual workflows and paper-based processes, it can be extremely difficult to secure optimal pricing and terms from suppliers, or identify and take advantage of opportunities to leverage economies of scale.

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## **Tips for Managing Indirect Spend Categories More Effectively**

In order to capture the overlooked potential savings opportunities offered by indirect spend management, procurement teams need to broaden their paradigm beyond “direct vs. indirect spend.”

A comprehensive approach, where both direct and indirect spend categories are successfully managed in concert with data-driven process optimization, is key.

Implementing such an approach means bringing indirect spend off the back burner and turning up the heat (so to speak) on identifying, measuring, and optimizing cost savings and value.

This is also part of an effective overall digital transformation strategy for procurement, where the focus shifts from cost management to value creation and strategic planning driven by data analytics, artificial intelligence, and automation.

Every company will have its own unique needs when streamlining its indirect spend category management. However, following a few basic tips can help you define your needs and leverage new technologies and tools to meet them.

## **1. Upgrade Your Toolkit**

To liberate the savings and value in their indirect spend categories—and help their parent organizations compete effectively—procurement teams need new tools, including artificial intelligence, data analytics, and process optimization.

These three technologies are absolutely foundational to digital transformation in general and procurement optimization in particular.

Implementing a comprehensive, cloud-based and purpose-built solution such as PLANERGY gives procurement teams a powerful suite of tools required to optimize indirect procurement (and your entire procure-to-pay process).

Untangling even the most labyrinthine indirect procurement supply chain is much easier with:

- Complete data transparency and full integration with all applications, including your existing enterprise resource planning (ERP) solution, office suites, marketing software, etc.
- Process automation and robust internal controls support the capture of all transactions, help streamline verifications and approvals, and make it easier to measure supplier performance and compliance.
- An end to maverick spend and invoice fraud.
- Advanced supplier relationship management tools that can help you

identify your best suppliers, consolidate spend to leverage economies of scale, etc. For example, outsourcing IT services, Internet hosting, and Website hosting to a single provider may allow your team to secure significant savings while still having a contingency plan in place with secondary suppliers.

- Simplified inventory management and support for advanced AI-powered procurement processes such as automatic reordering when low levels are detected.
- Support for KPIs and other metrics that can help you target specific savings opportunities for each spend category. Monitoring contract compliance, service level agreements, etc. can provide greater strength at the negotiation table and also reveal opportunities to partner with preferred suppliers for new materials, standardization of products, and more.
- Advanced analysis and reporting tools that make it easier to move away from basic cost reductions and toward a total cost of ownership (TCO) and ROI model that provides clear connections between indirect spend management and value creation.

## **2. Update Your Strategy**

With a centralized eProcurement solution in place, you can establish new protocols and sourcing strategies built around SAM: Spend management, Automation, and Metrics.

SAM helps procurement teams tame their indirect spend by ensuring it is fully visible, fully automated, and carefully monitored and analyzed.

Proactively managing indirect spend data supports continuous improvement initiatives and helps teams draw connections between that improvement and organizational goals such as profitability and competitive advantage for internal stakeholders.

SAM relies on advanced analytics and process management. Connecting indirect spending with generated value is much simpler when you follow a basic three-step approach.

1. A detailed spend analysis is the essential first step. A detailed breakdown

of indirect spend will provide you with a transparent and complete view of spend across indirect spend categories. This will make it much easier to identify areas in need of immediate improvement, streamline your indirect spend categories while maintaining strategic redundancies, and select your preferred indirect suppliers based on their capabilities and performance record.

2. Using the insights revealed by your spend analysis, you can establish and implement best practices for category management. Following these practices is especially important in managing indirect spend, as the diversity and number of suppliers requires category managers to have both high expertise and the information they need to put it to proper use.
3. Armed with both a clear picture of your current spend and a plan for streamlining your indirect spend categories, you can develop and implement an indirect spend management plan as part of your overall spend management strategy. Metrics play a key role here, as they provide benchmarks for demonstrable improvements, value creation, and cost savings. They also help you establish a baseline for strategic sourcing and process improvements you'd like to make in the next iteration of your spend cycle.

Those same metrics can help you “slice and dice” your indirect spend management categories in important ways.

For example, categories where scalability and cost savings are the primary concerns might provide the greatest value if outsourced entirely.

On the other hand, business-critical processes with the potential to provide value in multiple dimensions (e.g., greater operational efficiency and agility, product innovation, improved compliance, etc.) if properly optimized may be better off sourced to a specialty vendor whose systems can be tightly integrated with your own.

### **3. Make Agility, Sustainability, and Resilience Your Watchwords**

In an uncertain global economy, companies who invest the necessary resources in building agile, sustainable, and resilient supply chains are the ones best equipped

to endure and overcome powerful (and in some cases, unprecedented) business disruptors.

Agility is as much a mindset as it is a strategy. As with digital transformation technologies, agility is more of a paradigm shift than it is a mere operational adjustment.

Collaborative, creative, and transparent, agile procurement teams focus on continuous improvement, proactive problem solving, and connecting value as directly to their workflows and processes as possible.

Agility improves supplier relationship management through communication and collaboration. And provides the flexibility required to pursue opportunities for growth and innovation with key partners while still providing the resources and contingencies required to protect business continuity.

Sustainability, too, is critical to better indirect spend management. Properly implemented, sustainable procurement practices generate hard value through reduced costs, potential opportunities for product innovation, and greater versatility in the face of disruption.

But they also generate soft value through reputational improvements, a smaller environmental footprint, and a larger market share with key demographics.

Finally, ensuring your indirect procurement prioritizes supply chain resilience will help keep the Internet connected and your break room coffee machine perking—as well as your website online, the lights on at your manufacturing facilities, and your remote teams collaborating across time zones and business units.

Resiliency in indirect procurement helps teams minimize their risk exposure and protect business continuity, and helps build the strong supplier relationships that can prove invaluable in a crisis.

## **Free the Value and Savings Hidden in Your Indirect Spend**

Don't starve your company of potential value with poorly managed indirect spend.

Invest in data management tools and update your indirect spend management strategy to craft a supply chain that's streamlined, agile, and resilient.

With a proactive and strategic approach, you can untangle your indirect spend supply chain and ensure every dollar spent in every category is generating an optimal ROI for your business—along with strategic insights and process improvements that provide lasting value and support for organizational goals.

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