

# Guide to Completing a Spend Analysis

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## What is a Spend Analysis?

Spend analysis is the process of collecting, cleansing, classifying and analysing expenditure data from all sources within the organisation (i.e. purchasing cards, invoice purchasing and eProcurement systems, etc.). The process analyses the current, past and forecasted expenditures to allow visibility of data by supplier, by commodity or service, and by groups within the organisation. Spend analysis can be used to make future management decisions by providing answers to such questions as:

- What was bought?
- When was it bought?
- Where was it purchased?
- How many suppliers were used?
- How much was spent on each item?
- How much was paid for each item.

## Why do a Spend Analysis?

Spend Analysis should be the foundation on which sourcing initiatives are based on. It creates an understanding of the spend structure. Organisations need to gain insight into how much money is being spent on what types of services or products.

Spend analysis also helps an organisation find new areas of savings that previously went untapped, as well as it allows an organisation to hold onto past areas of savings that they have already negotiated. This is a valuable tool for the Chief Procurement Officer or equivalent to gain insight into what to buy and from whom and it helps them realise savings promised by past sourcing efforts.

There are three core areas of spend analysis:

- Identify and Collect Spend Data
- Cleanse Group and Categorise Spend Data
- Analyse Spend Data.

Spend analysis is often viewed as part of a larger domain known as Spend Management which incorporates spend analysis, category management and strategic sourcing.

## How is Spend Analysis done?

### Identify and Collect Spend Data

The first step is to extract data from existing systems of the business (such as Accounts Payable, Purchasing Cards and Purchase Order systems).

The next step is to examine the completeness of spend data and identify the accuracy of the existing chart or accounts structure.

Finally examine the type and usefulness of the classifications and determine if the existing items can be consolidated or replaced if underused both at the category and supplier levels.

### Cleanse, Group, and Categorise Spend Data

Once data is collected, it should be cleansed to remove any duplicates or errors, grouped, and categorised.

Grouping and categorizing spend data should be done by adopting an internal classification system or by adopting an industry-standard classification scheme like using the UNSPSC codes (The United Nations Standard Products and Services Codes).

Higher-level detail of spend at the category or supplier level is the first step in grouping and categorizing spend data. Examples include: categorizing goods and services that are being acquired; determining how many suppliers are being used for specific categories; and how much the organisation is spending on specific categories, in total and with each supplier.

It is important to remember that at this stage some of the data generated may or may not be mapped to categories depending on internal classification given to a system e.g. the spend on “tapes and bandages” might be classified as miscellaneous. However, it may be possible to classify this spend either against a category named “Maintenance” or “MRO” (Maintenance, Repairs & Operations). Mapping spend to categories is important. Item level detail of spend data enables a precise view of spending with each supplier and for each commodity on an organisational, departmental, project and buyer basis.

## Analyse Spend Data

The analysis should assess whether the current procurement structure, processes, and roles are adequate to support a more strategic approach to acquiring goods and services (for example: whether the organisation could provide more effective, coordinated management of high-dollar, high-volume categories of goods, services, and suppliers on an on-going basis).

With the implementation of regular Spend Analysis, procurement officers should aim to use the data to:

### Benefits of using a spend Analysis

When done correctly, Spend Analysis allows an organisation to identify opportunities to leverage buying power, reduce costs, improve operational performance and provide better management and oversight of suppliers, while improving relationships with internal and external stakeholders.

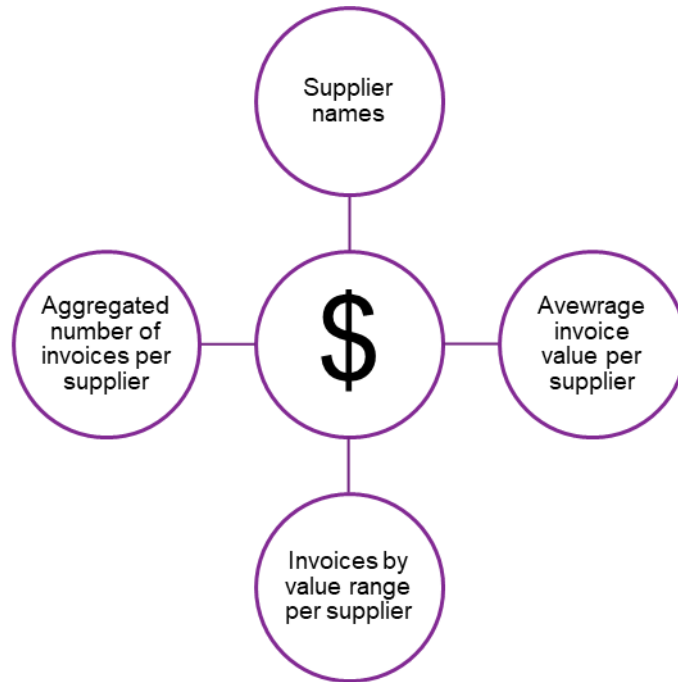
Below is some further guidance and models for practical approaches to:

- Invoice reduction
- Supplier consolidation
- Achieving improved negotiated terms
- Category rationalisation/extension
- Contract compliance
- Co-operation with other organisations

### Steps used for Invoice reduction

- Seeking monthly invoices from some suppliers
- Identifying categories/suppliers where invoice volume problems occur
- Moving suppliers to purchasing card (If purchasing cards are used by the organisation)

**Figure 1: Invoice Reduction**



### Steps used for Supplier consolidation

- Identify and eliminate small spend suppliers e.g. less than \$1000 per year
- Identify and eliminate small transaction suppliers e.g. less than one per year
- Identify groups/departments using a lot of “one time” suppliers
- Identify the categories with a lot of small suppliers in them

**Figure 2: Supplier Consolidation**



## Steps used to improve negotiations of terms/rates with suppliers

- Identify suppliers with highest spend and who within the organisation they supply
- Identify other suppliers in the same category as the top tier suppliers. Apply a Pareto analysis (80/20 rule) to identify how many suppliers fit into your top 80 percentile in that category
- Benchmark rates across departments/areas to identify variations in rates
- Understand how much the top tier suppliers rely on the organisation's business
- Based on the analysis negotiate better rates with suppliers

**Figure 3:** Terms in the Top Tier



## Steps for Category rationalisation/extension

- Identify suppliers enjoying a relative monopoly of supply to the organisation
- Identify categories that could be aggregated to rationalise suppliers and drive costs and prices down
- Identify contracts coming up for renewal where the supplier base is rationalised or extended

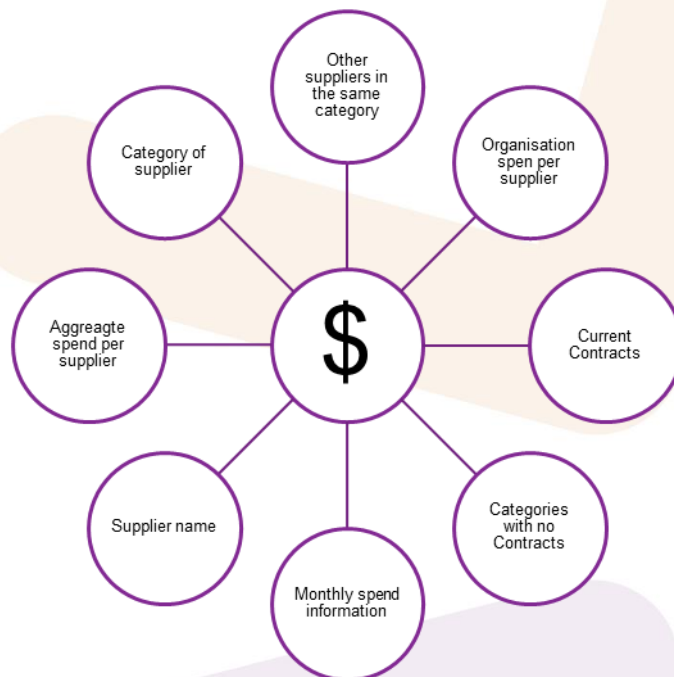
Figure 4: Category Rationalisation/Extension



### Steps for Contract compliance

- Identify groups in the organisation that are not using the preferred/contracted supplier in a given category
- Identify categories of spend that are not contracted
- Introduce monitoring/controls to limit non-contract spend

Figure 5: Contract Compliance



## Steps for Cooperation (aggregation with other organisations)

(Where there are opportunities to collaborate with other health services or other groups within the organisation)

- Identify suppliers already shared and how much is spent with those suppliers
- Identify shared categories with the greatest spend/greatest number of suppliers
- Identify and align contract end dates to enable collaboration

**Figure 6:** Aggregation with other Organisations or Groups



## Create Repeatable Processes (Automation)

Excellence in spend data management requires that spend data extraction, classification, enhancement, and analysis activities be supported by automation and services that can streamline existing procedures and make spending analysis a repeatable process.

Creating a repeatable process may require directly licensing automated data cleansing and classification software or engaging consultants or other service providers that leverage such solutions to deliver a ready-made or turnkey spend data management service.

Organisations should seek to incorporate the knowledge of internal sourcing and commodity experts into the automated system through the use of software engine rules and self-learning capabilities.

Procurement Officers should seek to generate automated monthly reports of the most current spend data to ensure that the most current spend position of the organization is being considered in new procurements.

## Summary

The above Spend Analysis information provides us with category taxonomy and forecast knowledge-base that can be reviewed from time to time to inform the procurement process and strategy of the organisation.

Spend analysis provides the data required as a basis for developing the organisation's procurement strategy. Refer to the Guide to Procurement Strategic Analysis for further details.

Analysing spend will help an organisation to:

- Rationalise and categorise their supplier base and focus on those suppliers that offer the best value. In some cases, it can also identify other important variables, other than just price, such as cooperation and development
- Build key metrics for all spend categories to monitor progress and ensure success in realising the cost saving targets and sourcing opportunities. By tracking actual savings procurement can demonstrate benefits of a strategic approach
- Understand spend patterns, demand information and clear purchasing requirements to improve suppliers election and contract negotiation.

## More information

Related documents and templates are available on the HSV website.

## Disclaimer

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