



Business Consulting Services

Business Transformation Outsourcing (BTO)

Procurement Services:

What is BTO Procurement and how can it impact Services Procurement?

Jim Kalina

IBM Global Procurement Services

Business Transformation Outsourcing



Agenda

- **Introduction**
- **What is Business Transformation Outsourcing (BTO)?**
- Benefits of BTO Procurement
- Potential impact on Services Procurement
- Summary

What is Business Transformation Outsourcing?

Delivering improved business results through continuous strategic change and the operation and transformation of the client's business processes, applications, and infrastructure measured against business outcomes.

Focus on core business

Innovate and improve vs. cost cutting

Increase flexibility to adapt quickly

Improve decision support

Speed time to benefits

Reduce costs

Reduce barriers to change

Business Process

Outsourcing targets reducing tactical costs and investment in non-core processes

Business Transformation

Outsourcing addresses the full scope of a client's tactical and strategic needs and seeks to transform existing processes to best-in class

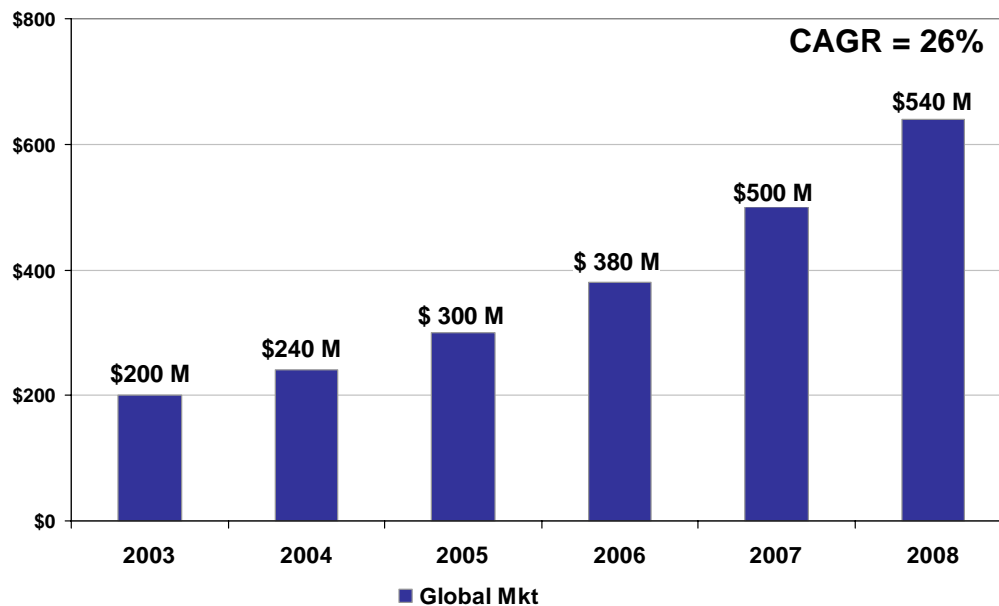
Business Transformation Outsourcing solution areas

| Customer Care | Human Resources | Finance & Administration | Procurement |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>Business Processes</p> <ul style="list-style-type: none"> ▪ Customer Care ▪ Order management ▪ eCommerce ▪ Services after Sales ▪ Warranty Service ▪ Field Service management ▪ Billing & Payments ▪ Customer analytics ▪ Call center operations | <p>Business Processes</p> <ul style="list-style-type: none"> ▪ Web enabled self-service portal and contact center ▪ HR Process redesign, subject matter experts ▪ Staffing, Recruiting, benefits, Org Development, Training, Education ▪ Expense acctg, payroll ▪ Data and Analytics ▪ Vendor aggregation and management | <p>Business Processes</p> <ul style="list-style-type: none"> ▪ Cost Accounting ▪ JE Processing ▪ AP/AR ▪ Fixed Assets ▪ Project Accounting ▪ Inter-company Billing ▪ Credit & Collections ▪ Cash Application ▪ Internal/External Financial Reporting ▪ General Accounting ▪ Budget and Forecasting | <p>Business Processes</p> <ul style="list-style-type: none"> ▪ Strategic Sourcing ▪ Supplier Catalog Enablement ▪ Supplier Relationship Management ▪ Indirect-Direct Purchasing ▪ Contract Management ▪ End-User Support ▪ Offshore Sourcing |

NelsonHall 2004 analysis highlighted the relative immaturity of the procurement BPO marketplace and the expected strong growth

Global Procurement BPO Market Revenue

NelsonHall, 2004



- *Current size of the procurement BPO market is small with **few standalone outsourcing contracts**. Much of the current procurement activity is **embedded in other forms as outsourcing** such as technology purchases with desktop services and temporary staff procurement within HR outsourcing.*
- *Procurement BPO is therefore an **immature marketplace** which presents providers with an **opportunity to develop market share**.*
- ***Acceleration of growth** anticipated from 2006 onwards, **once early adopter phase complete**.*

NelsonHall

Source: "Targeting Procurement Outsourcing.", NelsonHall, 2004

NelsonHall suggests a number of factors that will be important as the procurement BPO market matures

- **Greater emphasis on full-service BPO** rather than stand-alone consultancy and application hosting services
- Focus will continue on **indirect spend** with some manufacturing MRO being outsourced.
- Focus on management of a **wide range of indirect goods and services**.
- Process management will include increasing emphasis on supplier management, settlement and fulfillment
- **Improved access to goods and services** will increase in importance alongside cost reduction
- **Procurement BPO Contracts will continue to be standalone**; back-office multi-process contracts still some way off though vendors will develop multi-process shared service center capability
- Delivery capabilities will be shared across clients
- **Providers demonstrating operational excellence combined with sustained cost savings will emerge as leaders in the marketplace**

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Market forces demand that companies operate with ever more speed, agility and cost-effectiveness

Industry Drivers

Low-growth macro-economic environment

Complex, empowered consumers

Intense global competition

Need for innovation

Strategic Imperatives

Re-focus on core business

Respond to the Customer

Re-align the Enterprise

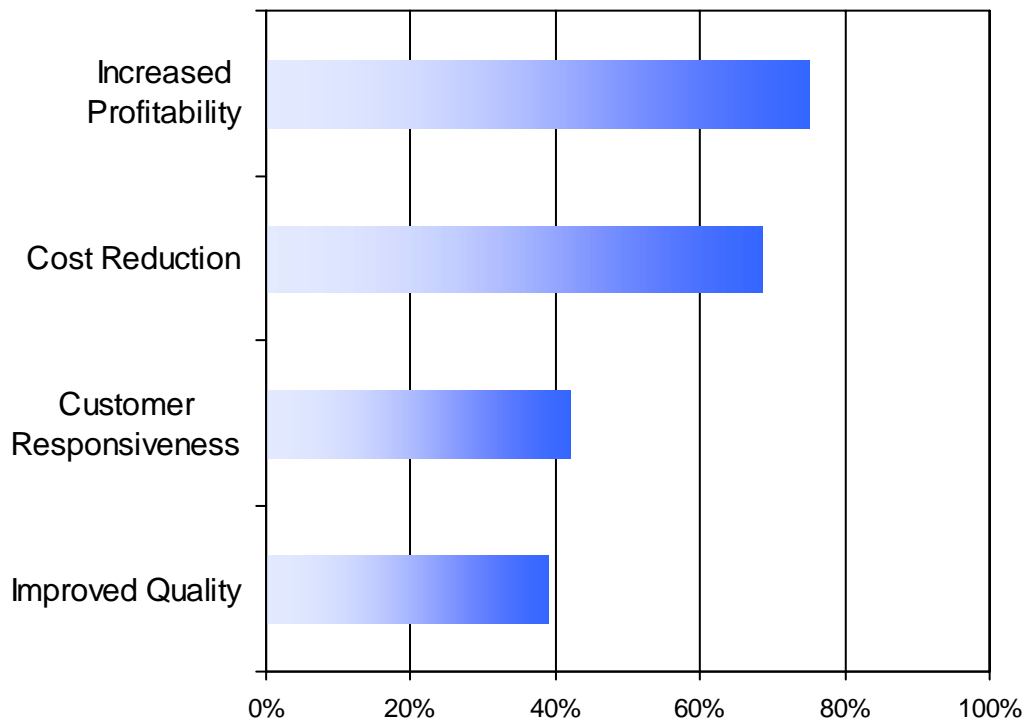
Operating Requirements

- **Respond faster** to increasing consumer demands, customer needs, and competitive threats
- **Operate with greater agility**, managing a flexible value network that brings the right capabilities to the right place at the right time
- **Aggressively manage costs** to counter price/margin pressures and maintain competitiveness

Supply chain executives:

Reducing procurement costs to support improved profitability

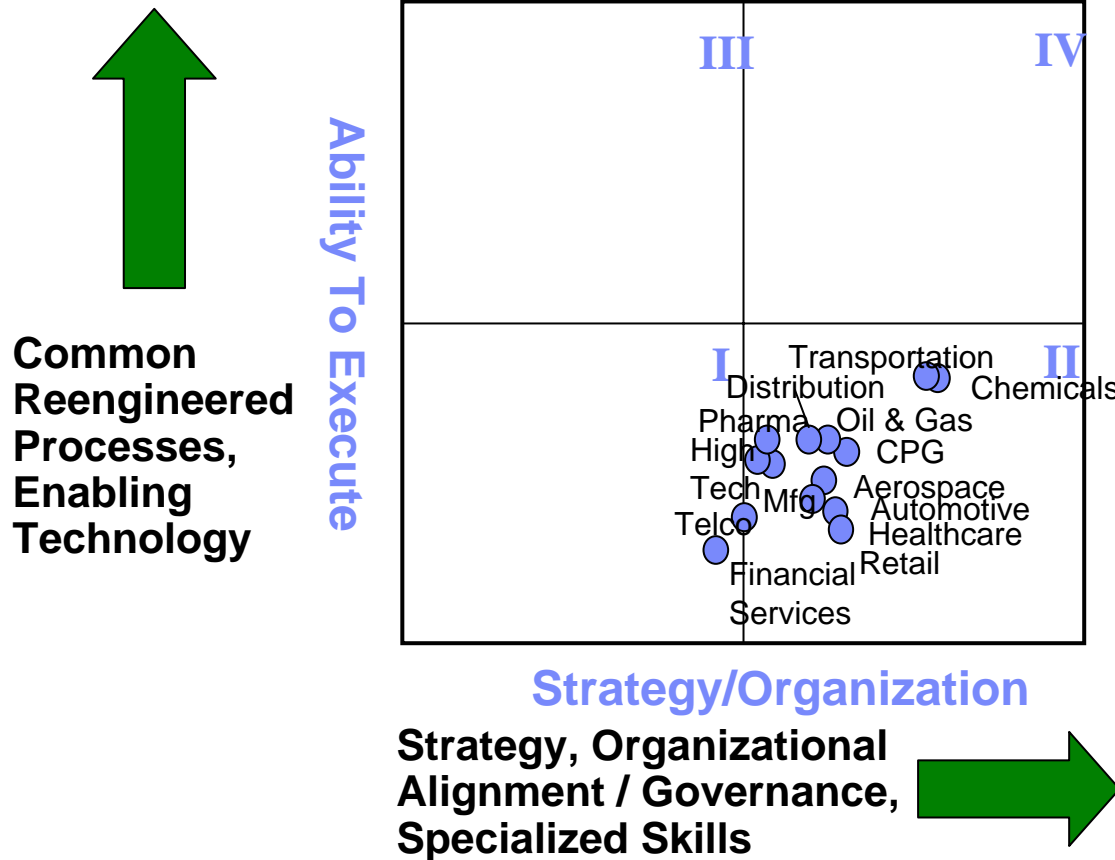
Top Objectives for Procurement



Bottom line profitability

- **Three out of four of Supply Chain executives believe their top priority for procurement is supporting bottom line company profitability**
- **Cost reduction is viewed as nearly twice as important as other priorities**

Although the importance of transforming procurement has been recognized there are execution challenges



Procurement Challenges

- Pressure to **cut costs**
- **Lacking basic information** about spend
- **“Maverick” purchases** mean lost leverage
- Too many suppliers
- Processes **paperwork intensive** – only 11% on-line spending on average
- Lacking **specialized sourcing skills**
- Operation in **high cost locations**
- **Managing change**

Organizations continue to struggle with internal constraints that hinder their ability to meet these challenges

Management Complexity

Managers are struggling to satisfy complex new business requirements all across their enterprises, value networks, and global markets.

Organizational Fragmentation

Product, functional, and geographic silos exacerbate operating inefficiencies and prevent firms from responding to market needs in a consistent way.

Rigid Cost Structure and Asset Base

Resources and capital are committed to continued operation and maintenance of slow-growth, low-value business activities.

Stretched thin

Slow to adapt

Inefficient

Distracted

Inflexible IT Infrastructure

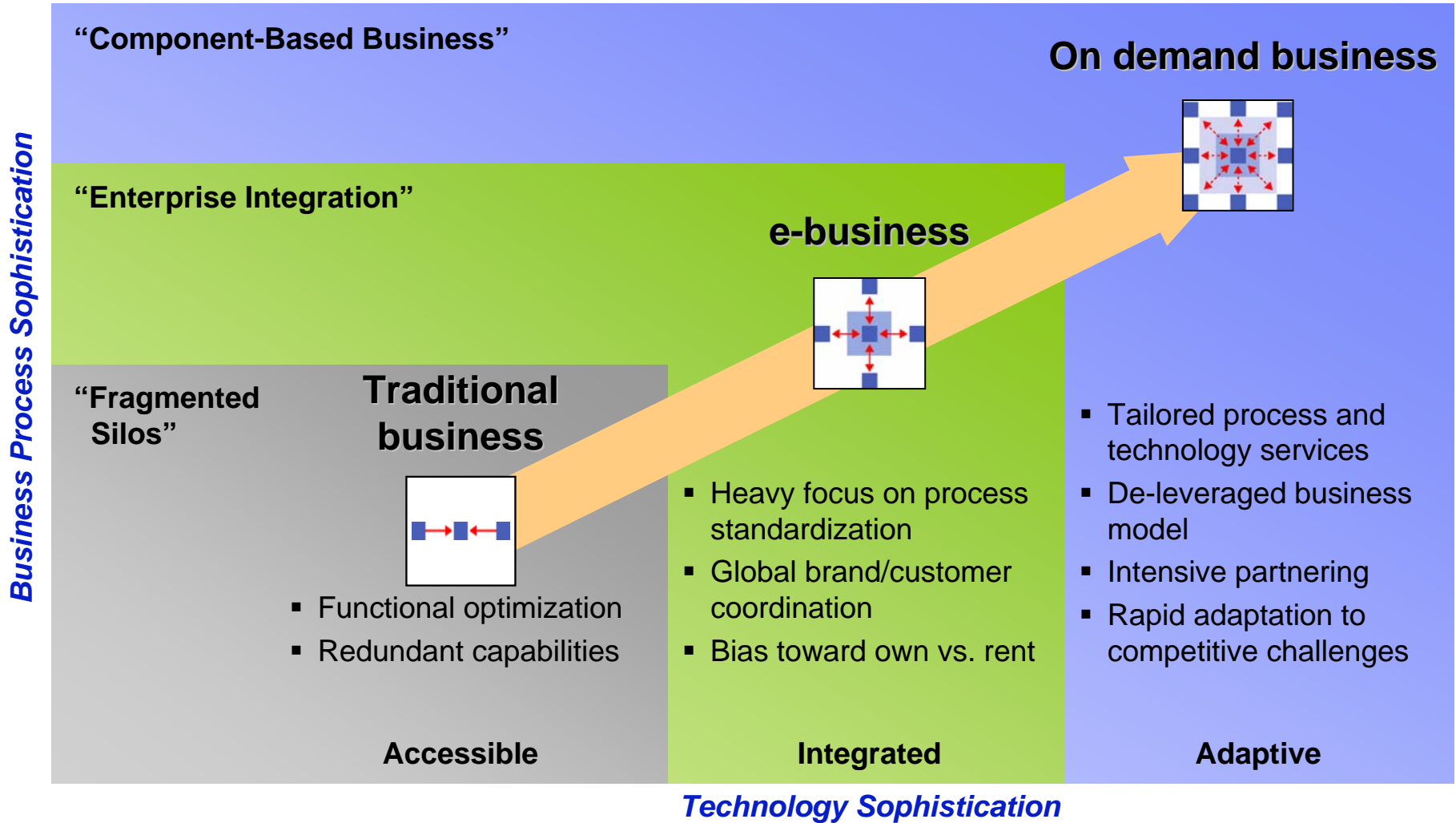
The technology environment is overly complex and serves to inhibit – rather than enable – the deployment of new capabilities.

Cultural Resistance

Traditional attitudes and management practices conflict with the need for rapid, insight-driven decision-making and execution.

Source: IBM Institute for Business Value analysis

Companies can transform themselves to what IBM calls an “On Demand” business to achieve market leadership



This transformation starts by recognizing which components of business bring differentiating value

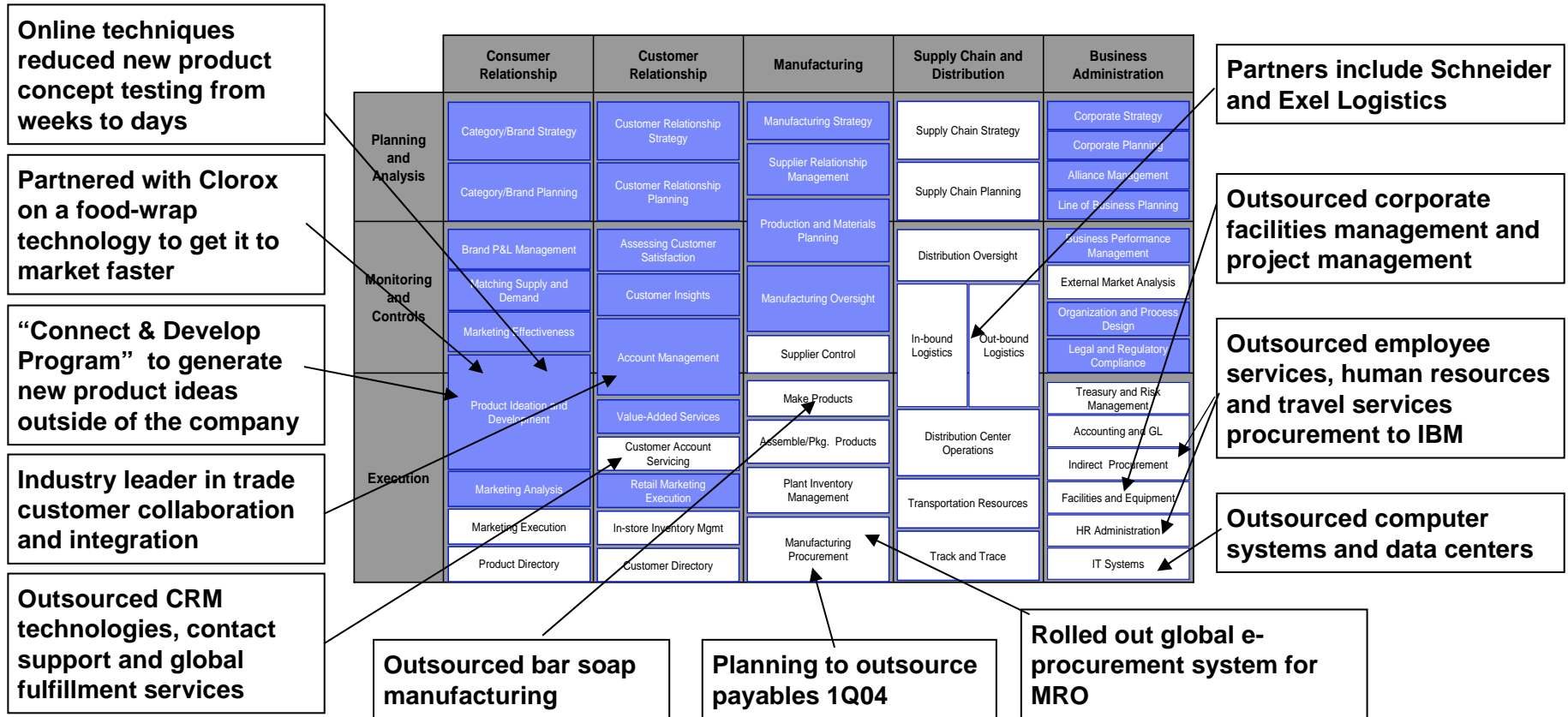
Illustrative

| | Consumer Relationship | Customer Relationship | Manufacturing | Supply Chain and Distribution | Business Administration |
|--------------------------------|----------------------------------|---------------------------------|-----------------------------------|--------------------------------|------------------------------------------|
| Planning and Analysis | Category/Brand Strategy | Customer Relationship Strategy | Manufacturing Strategy | Supply Chain Strategy | Corporate Strategy |
| | Category/Brand Planning | Customer Relationship Planning | Supplier Relationship Management | Supply Chain Planning | Corporate Planning |
| Monitoring and Controls | Brand P&L Management | Assessing Customer Satisfaction | Production and Materials Planning | Distribution Oversight | Business Performance Management |
| | Matching Supply and Demand | Customer Insights | Manufacturing Oversight | | In-bound Logistics Out-bound Logistics |
| | Marketing Effectiveness | Account Management | Supplier Control | Distribution Center Operations | |
| | Product Ideation and Development | Value-Added Services | Make Products | | Transportation Resources |
| Execution | Marketing Analysis | Customer Account Servicing | Assemble/Pkg. Products | Track and Trace | Treasury and Risk Management |
| | Marketing Execution | Retail Marketing Execution | Plant Inventory Management | | Accounting and GL |
| | Product Directory | In-store Inventory Mgmt | Manufacturing Procurement | Indirect Procurement | |
| | | Customer Directory | | Facilities and Equipment | |
| | | | | HR Administration | |
| | | | IT Systems | | |

 = Differentiators = Non-differentiators

For example, P&G is actively off-loading non-strategic activities and re-investing in its core business

Recent Examples of P&G Strategic Initiatives



■ = Differentiators □ = Non-differentiators

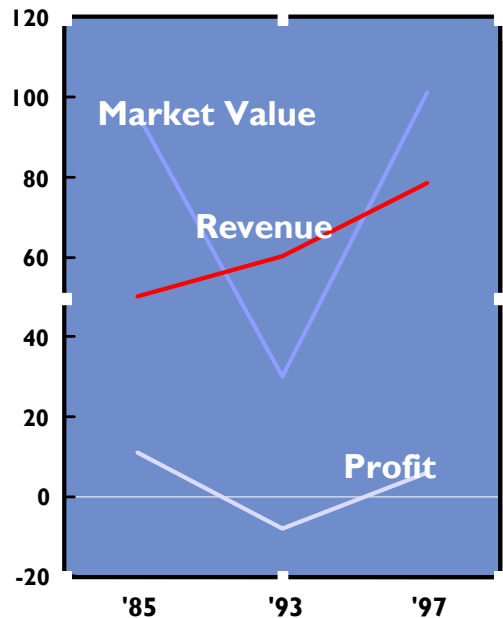
Source: Sykes Enterprises Press Release, 30 Jun 03; Business Week, 7 Jul 03; Oster Dow Jones Select, 17 Jun 03; PR Newswire, 17 Jun 03; Fast Company, Sept 03; <http://www.ecom-ohio.org>, July 2002; Company web sites

According to Nelson Hall, corporate cost reduction is the primary driver of procurement outsourcing

- **Need to improve a company's bottom line through reduction of expenditures on indirect goods and services** (usually as part of a corporate cost reduction initiative)
- **Speed to achieving results while managing risk / distraction** is critical
- Recognized **transformation obstacles** to achieving procurement effectiveness
 - Lack of information about indirect spend
 - Lack of specialized category sourcing expertise
 - Need to improve compliance management across organization
 - Desire to consolidate procurement function into shared services operation
 - Need for global support
 - Avoid need for additional investment in infrastructure or applications
 - Failure of previous investments to realize full value or expected ROI
 - Improve services delivery (quality / speed)
- Reducing procurement **personnel** is typically **not a major motivator**

IBM's own successful procurement transformation began in the 1990's

Our "near death" experience in the early 1990's...



| Measure | \$US Billions | | | |
|-------------|---------------|----------|-----------|--------------------|
| | 1990 | 1991 | 1992 | 1993 |
| Revenues | 69 | 65 | 65 | 63 |
| Earnings | 6 | 3 | -5 | -8 |
| Cash Flow | 5 | 1 | 2 | -3 |
| Debt | 20 | 27 | 29 | 31 |
| Bond Rating | AA+ | AA+ | AA+ | A |
| Stock Price | (high of) 117 | (EOY) 95 | (EOY) 50 | (low of) 41 |

... was a catalyst for change



NO. 1

We decided not to die

KEEPING IBM TOGETHER

Did the world need a company like IBM anymore? In the early 1990s, our way of computing and our way of working with customers had fallen out of vogue, and we were on a fast track to being dismantled, from within.

Then, in the spring of 1993, new leadership brought a new vision—and a surprising decision. IBM would stay together. We believed niche players weren't the future. In fact, breaking up the company would have been the end of everything IBM stood for.

CONTINUED →

We invested in procurement and achieved dramatic results which helped fuel our turn around

\$5+ Billion cost and expense savings last year

95% of global buying is conducted electronically

maverick buying reduced from **50%+**

to less than **0.2%**

employee satisfaction increased from **40%**

to **82%**

35,000 suppliers connected with IBM via the web

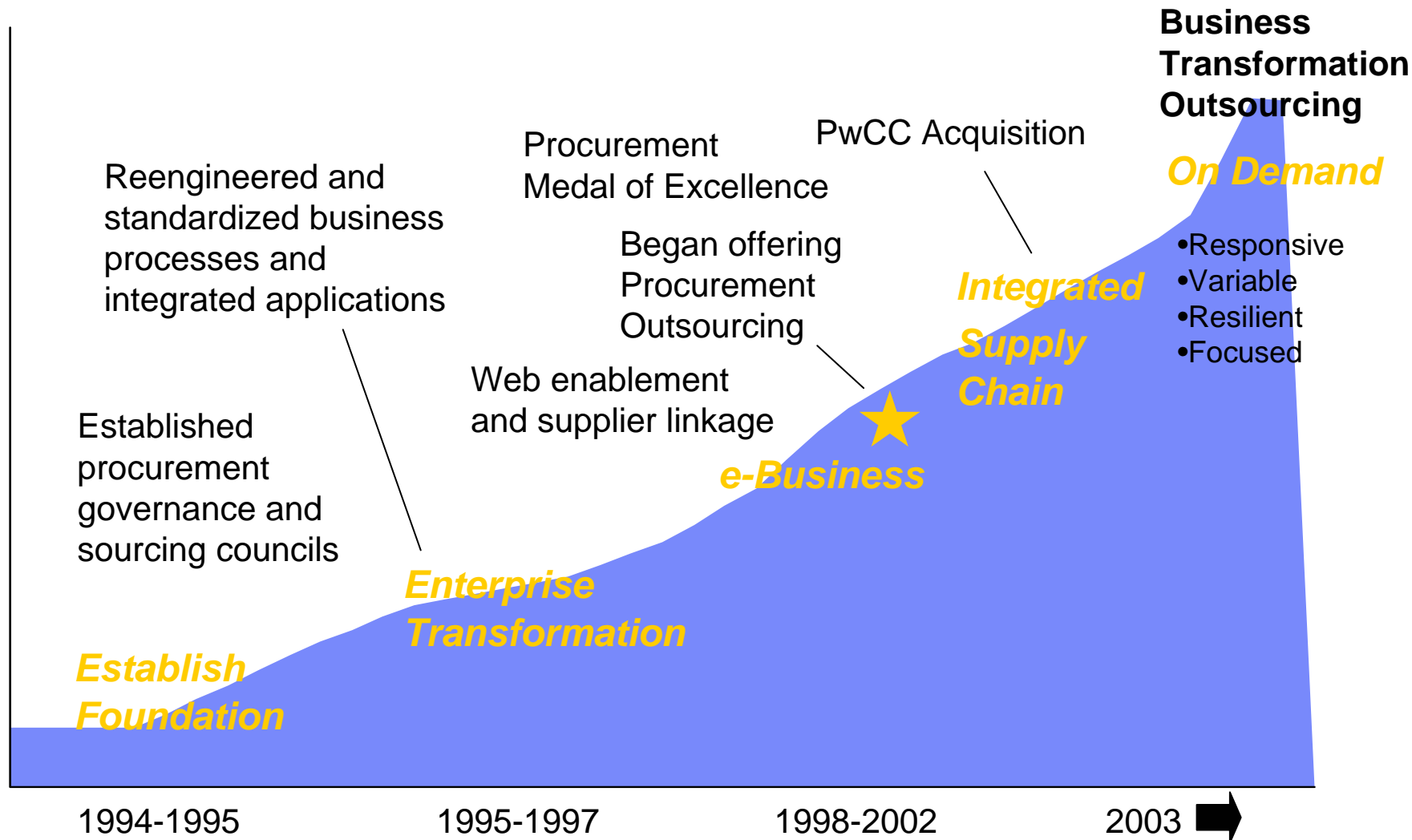
96% of purchasing transactions “hands-free”

Time from requisition to supplier order placement reduced from

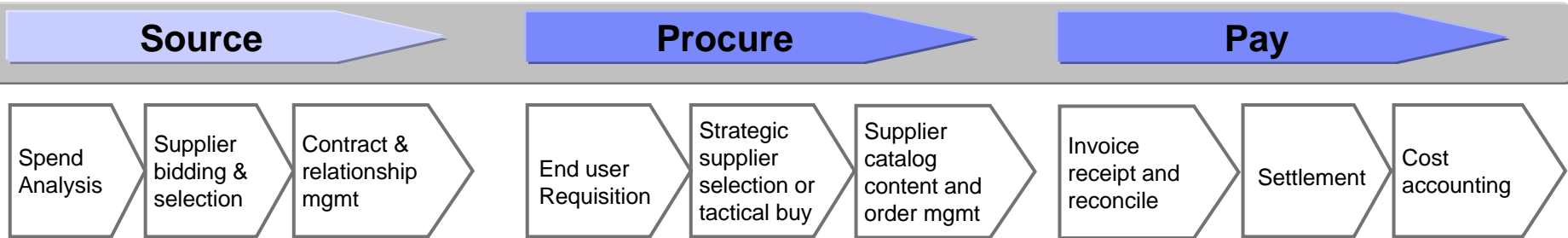
2-3 weeks to **just hours**

\$438M saved with e-procurement

We've continued the journey to "On Demand" and clients became interested in leveraging IBM's investment



As you evaluate BTO providers, one element to consider is the platform they will utilize to manage your procurement



Source-to-Pay Solution Components

e-Sourcing

ERP

Customer Assistance

Data Warehouse

Imaging

IBM Supplier Portal

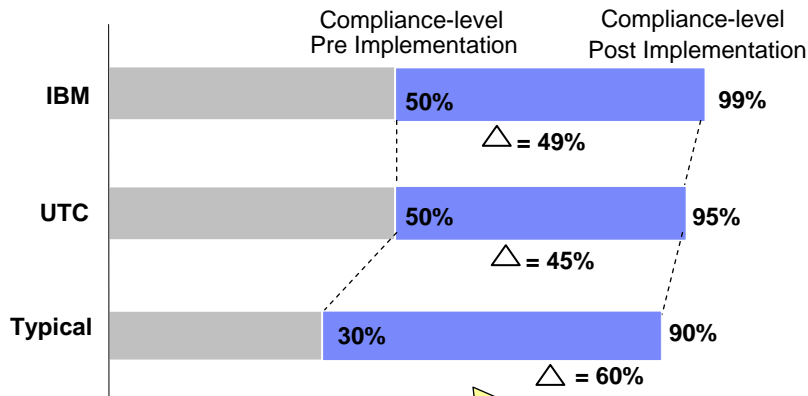
A hosted, multi-client, Source-to-Pay technology platform is an option for companies who require an end-to-end solution but haven't made the investments internally.

Multiple commodity-specific procurement channels must be provided to support 100% spend coverage

| Channel | Process Characteristics | Commodity Characteristics | Sample Commodities |
|---------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------|
| Catalog | <ul style="list-style-type: none"> User selects items on local system; Order is transmitted directly to supplier | <ul style="list-style-type: none"> Low dollar, high volume Strategically sourced Relatively static supplier content | <ul style="list-style-type: none"> Office Supplies Off-the-shelf Software Promotional Items |
| Punch-Out | <ul style="list-style-type: none"> User selects / configures item through supplier site; Order transmitted directly to supplier | <ul style="list-style-type: none"> Large, non-static catalogs Configuration requirements More complex commodities Sophisticated, high volume suppliers | <ul style="list-style-type: none"> Computer / Network Equipment IT Contractors (MSP) Books/Periodicals |
| Contract | <ul style="list-style-type: none"> User references contract terms / pricing / content; Order transmitted directly to supplier | <ul style="list-style-type: none"> Group or individual-specific content Strategically or tactically sourced Does not require supplier content | <ul style="list-style-type: none"> Facilities Maintenance Legal Services |
| Corporate Procurement Card | <ul style="list-style-type: none"> User buys directly from a vendor and charges (where approved) on the Unilever Corporate Procurement Card | <ul style="list-style-type: none"> Low dollar, non-capital Allowed for approved categories and users Highly variable supplier base | <ul style="list-style-type: none"> Maintenance Expenses Meeting / Promotional Expenses |
| Full Buyer (Tactical Buyers) | <ul style="list-style-type: none"> User outlines request for buyer; Buyer sources and transmits order to supplier | <ul style="list-style-type: none"> One-off / custom purchases Non-standard suppliers, terms Fair value determination required | <ul style="list-style-type: none"> Marketing / Advertising Capital Equipment |
| Web Based Payment Request (WPR) | <ul style="list-style-type: none"> User enters data and requests payment upon receipt of supplier invoice | <ul style="list-style-type: none"> Limited strategic sourcing leverage "Sensitive" expenditures Only specified commodities allowed | <ul style="list-style-type: none"> Legal Settlements Regulatory Fees Taxes |
| T&E | <ul style="list-style-type: none"> User requests reimbursement after travel / entertainment completion | <ul style="list-style-type: none"> Employee purchased Booked in advance through corporate travel provider | <ul style="list-style-type: none"> Hotel, air, car Meals / Entertainment HR-related |

The main objective of these end-to-end BTO solutions is to improve compliance to corporate agreements

Contract Compliance Pre and Post Implementation



Companies are typically not able to achieve close to 100% compliance due to insufficient investment in procure-to-pay capabilities.

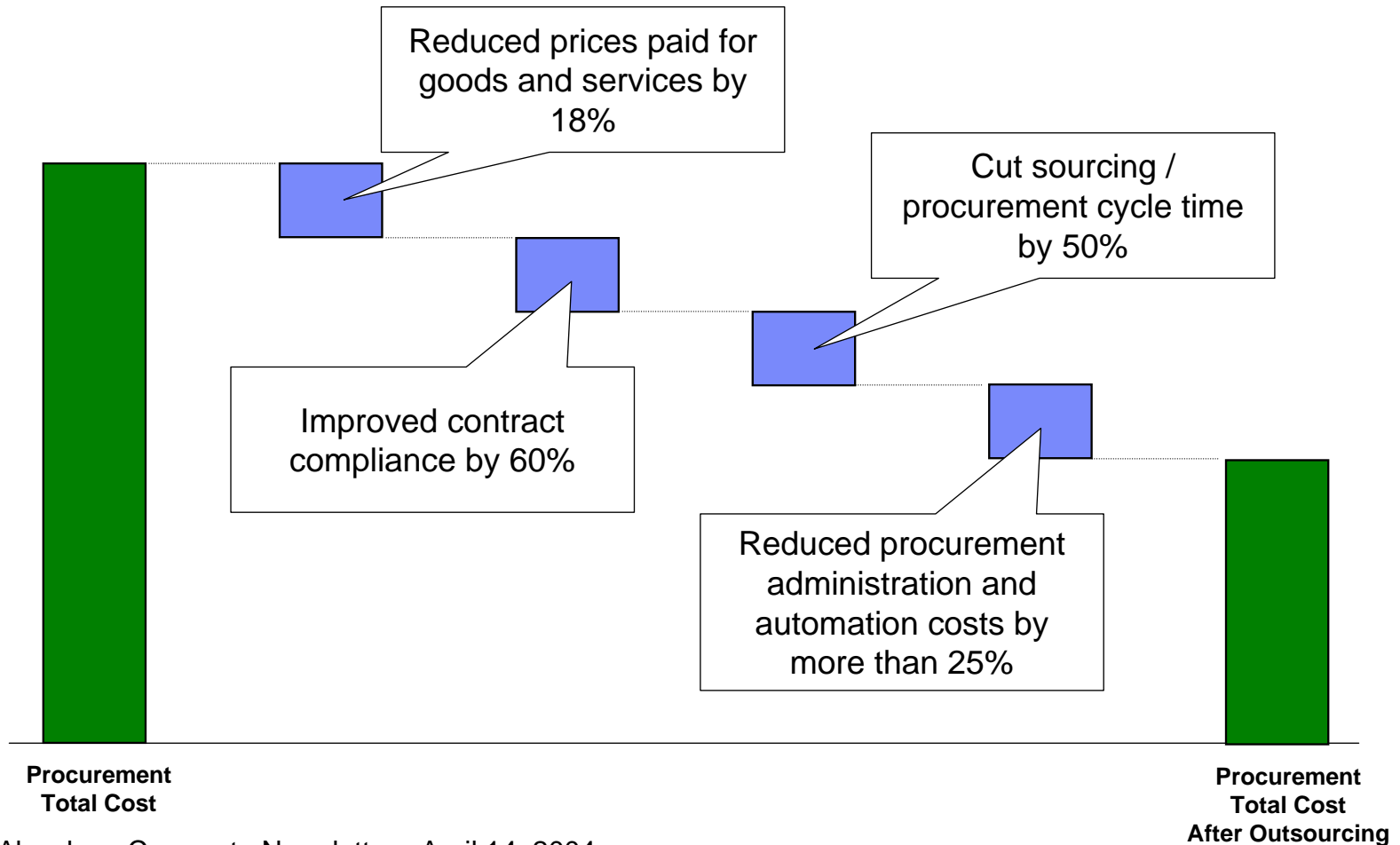
*Compliance = "Goods and services purchased from preferred suppliers at negotiated rates with approved specifications"

How Compliance Is Increased

- 7 different buying channels that enable capture of 100% of company spend
 - Catalog
 - Punch-Out
 - Contract
 - Corporate Procurement Card
 - Full Buyer (Tactical Buyers)
 - Web Based Payment Request (WPR)
 - T&E
- Easy-to-use application front ends that are tailored to business and commodities
- An organization of trained tactical buyers that will actively work on increasing compliance
- Web-based Payment Requests to support 100% spend capture by including non-PO items
- Complete integration of A/P and procurement processes – e.g., automated matching of invoices, receipts and orders, etc
- Ability to implement control policies
- Sophisticated management reporting

According to Aberdeen, procurement Outsourcing is a viable method to improve overall procurement effectiveness

“Procurement Outsourcing Delivers Double-Digit Saving”*



* Source: Aberdeen Corporate Newsletter - April 14, 2004

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With less than 30% of services spend being managed by procurement professionals, something has to change

- Companies are not making the technology investments required to allow you to capture 100% of services spend
- Over 50% of a typical buyers time is spent managing non-value added activities such as data gathering
- Procurement BTO is a trend that, if embraced, could provide the tools required to streamline and capture 100% of services spend with limited investment
- The outsourcing of tactical, non-value added activities such as PO processing and catalog creation would allow buyers more time to invest in internal stakeholders and supplier relationships

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Summary

- The **strategic issue** is how to achieve **procurement effectiveness** either by investing in building capability internally or buying as a service

Procurement Outsourcing can add significant value to services procurement by providing tools to capture 100% of your companies spend and time (through the outsourcing of tactical processing) to allow you to focus on internal customers and their needs.

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IBM brings clear differentiators to the fundamental capabilities that clients look for in selecting a BPO provider

| The Broad Set of Skills To Do BPO Well | | IBM Differentiators |
|----------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Requirements | Description | |
| Deep process understanding | <ul style="list-style-type: none"> Know how the process operates: its workflow, inputs and outputs. Understand how the process links to and impacts the firm's overall business. | <ul style="list-style-type: none"> IBM's award winning Procurement Best in class process expertise with over 70 patents |
| Consulting expertise | <ul style="list-style-type: none"> Benchmark the client operation with industry average. Re-engineer the process. Support the client's change management needs. | <ul style="list-style-type: none"> PwCC acquisition/industry expertise Pioneering BPO provider (UTC) Client references in every industry |
| Broad technical skills | <ul style="list-style-type: none"> Run the underlying apps and technology infrastructure. Upgrade and implement the supporting applications. Handle the integration across systems. | <ul style="list-style-type: none"> #1 services provider for application integration and hosting Investment in BTO platform |
| Operational excellence | <ul style="list-style-type: none"> Manage the processing centers and the staff on a day-to-day basis. Implement the methodology for continuous improvement and cost-cutting. | <ul style="list-style-type: none"> Procurement support in 71 countries Deep strategic sourcing expertise Low cost, global operations centers |
| Financial strength | <ul style="list-style-type: none"> Take over assets and support three-to five-year long contracts. Help the client effectively model the deal and its return. | <ul style="list-style-type: none"> Flexible options with risk share Available IBM financing |

Source: Forrester Research Inc.

IBM capabilities for BTO are unparalleled

