Abstract. Unlike Fortune 500 companies, middle market companies typically have a lower spend and struggle with whether an eSourcing program will be beneficial. Companies with an annual spend of as little as $20 MM have successfully used eSourcing processes to obtain a significant ROI. On the other hand, some companies with an annual spend of $1 billion have not succeeded in eSourcing. This paper addresses the following questions. Is my business suitable for eSourcing? How do I create a successful business case for eSourcing? Do I need to install an ERP system to run a successful eSourcing program? What eSourcing process should I follow? How do I select an eSourcing service provider?

Introduction. We define eSourcing as strategic sourcing using Internet-based tools. Many pieces of traditional strategic sourcing processes such as spend analysis, supply market analysis, RFP development, supplier qualification, supplier negotiations and total cost of ownership analysis can be automated today using Internet-based tools. At least 20+ vendors provide services in this space with different pieces of technology and different levels of service. Most of these vendors can be classified into two general categories: 1) consulting/service focused eSourcing providers and 2) traditional tool providers.

eSourcing vs. Exchanges vs. eProcurement

In addition to eSourcing defined above, CAPS Research (2000) categorizes exchanges and eProcurement as follows:

Exchanges are market creators in which the primary purpose is to bring together many buyers and many suppliers to create a more active and robust market for non-standard or low volume products. The increased information about these products brought about through an exchange should lead to reduced purchase prices and transaction costs as middle market buyers can use suppliers that were previously difficult to find. At the same time, small suppliers will have access to middle market buyers.

Examples of the tools within this category are clearing houses such as those seen with trucking industry. On an Internet clearing site, middle market firms may post less-than-truckload services that they would like to purchase. This benefits both the buyer and seller in that the transportation firm has a way to access new markets and convert a previous less-than-truckload trip into a full truckload so a better rate can be provided. Meanwhile, the middle market buying organization has a means of obtaining transportation for a small shipment at a reduced rate. Many different types of catalogs provide a similar service.
eProcurement is essentially the transaction facilitator. The primary purpose within this category is to reduce transaction costs by improving order efficiency and automating back-end accounts payables and accounts receivables. The outcome is the reduction of costly paperwork and errors and improved inventory management. Typically this is accomplished through a web-based XML technology.

An important note is that eSourcing models are different from exchange models that exist in many industries and attempt to bring buyers and seller together through an open marketplace. Most eSourcing models are buyer-driven and the fees for the services are paid by the buyer and not by the seller.

**eSourcing Opportunity.**

*Is my business suitable for eSourcing?*

The answer to this question depends on the nature of the market and product/service. The attributes of the product and the nature of the market should be analyzed concurrently to determine whether an eSourcing effort will be successful within your organization. Especially important is the extent to which the product is differentiated or commoditized. If the product to be sourced is highly unique, custom designed, and differentiated for which it is difficult to clearly establish the specifications, a different type of eSourcing strategy will be necessary than if the product is an off-the-shelf commodity. As an example, a consumer foods company attempted to buy a unique machine that is designed to pick tomatoes from the vines. The company was only planning on purchasing a couple of these machines, and only a few such manufacturers of these machines existed; therefore, no eSourcing application was appropriate. Meanwhile the same company was purchasing many laptop computers that had standard specifications available from several distributors. Because a high volume of these computers were being purchased, eSourcing was appropriate.

Closely related to the nature of the product is the position of the market. Therefore, before a company implements an eSourcing effort, it should determine if the market of the eSourced product is seller or buyer-centric. A seller-centric market is one in which there are few sellers but many buyers. In such a market the eSourcing approach should be focused on reducing transaction costs rather than price negotiations. Vice-versa in a buyer-centric market, an eSourcing model based on price negotiations is more suitable.

*How do I create a successful business case for eSourcing?*

A successful business case begins with detailed spend analysis. Many middle market companies do not perform such spend analyses due to a lack of a centralized organizational structure and/or lack of proper systems and procedures. Once the spend analysis is complete, the next step is to create the list of potential eSourcing categories. Those items for which there are only a few qualified or qualifiable suppliers should be eliminated from the list as well as those strategic categories for which you would like to continue long-term supplier relationships. For the remaining spend, estimate the savings that can be accomplished using eSourcing for each category, then estimate the resources required to launch a successful eSourcing program. eSourcing service providers such as Global eProcure can assist in providing benchmark data for savings and resources required. This analysis will provide a
backdrop for building a business case. The typical projected ROI for an eSourcing program for the middle market ranges between 8X to 15X.

*Do I need to install an ERP system for successful eSourcing?*

No! While it is helpful to have an ERP system to capture spend data, there are a number of companies that enjoy the high ROI of eSourcing without an ERP system in place. Typically ERP systems capture 40 to 50% of spend and hence, even if these systems are in place, a broader, more detailed spend analysis is still required for a successful eSourcing program.

*What eSourcing process should I follow?*

The eSourcing process requires the following components: detailed spend analysis, supply market analysis, supplier selection and qualification, supplier training, price negotiations, and total cost of ownership analysis. Many of these components can be automated using Internet-based tools, and a good eSourcing service provider will have all of these components in place.

*How do I select a service provider?*

Select a vendor with a background in strategic sourcing rather than in technology, moderate prices, and specializing in the middle market. If an eSourcing service provider appears to be too technology oriented, their customers may suffer from poor spend and supply market analyses – both of which are important factors required for significant savings. Once familiar with the new process, you may consider reducing the service level and continue using just the tool. In our experience, it takes at least one to two years before buyers are able to use the technology and train the suppliers on their own. Also, it is important to ensure that the vendor has longevity, talent, scalable technology, and actual paying customers. If a vendor is providing a free pilot, you should question how long that vendor would be in business. On the other hand, a vendor with great experience providing services to Fortune 500 companies may be too expensive for a middle market organization with the majority of the eSourcing savings going towards vendor fees.

*How do I put a change management effort in place?*

eSourcing requires change management for two different groups: the buying organization and the supplier organization. When discussing the barriers to change and techniques for overcoming them, Daft (1995) notes three organizational barriers and two personal barriers that are pertinent to eSourcing:

**Organizational Barriers**
- Failure to perceive benefits
- Lack of coordination and cooperation
- Incompatible systems

**Personal Barriers**
- Uncertainty Avoidance
- Fear of Loss
The reasons for each of these barriers and potential strategies for overcoming them could be discussed at length. However, the change strategy most frequently advocated for the past thirty years has been communication and education (Strebel, 1996). In addition, a company should make every effort to keep the monetary investment and psychological barriers of a change management effort as low as possible.

An example of reducing the psychic investment is provided by companies focused on the middle market such as Global eProcure and SPS Commerce. When working with their clients, these third party service/technology providers support the change process by offering training and all communication to the suppliers. The main purpose is to assure that both the company employees and the suppliers are well educated so that they will not resist the change.

**Summary.** Most middle market companies have the opportunity of leveraging the Internet to reduce the cost of purchasing. First, the nature of the market must be analyzed so that it is understood whether a buyer-centric or seller-centric market exists for the product. Second, the eSourcing process must be matched with the product/service and market. Because different applications are appropriate for various markets a mismatch may result in lost time and money. Third, a cost-benefit analysis or business case is required upfront and change management processes should be implemented. A vendor with a background in strategic sourcing, focusing on middle markets with moderate price structure is best suited to begin a successful eSourcing program.
REFERENCES

Book references:

Journal or magazine article references:

Web site references:
“eSourcing” CAPS Research. Capsresearch.org