

Changing Perceptions on ERP Strategy

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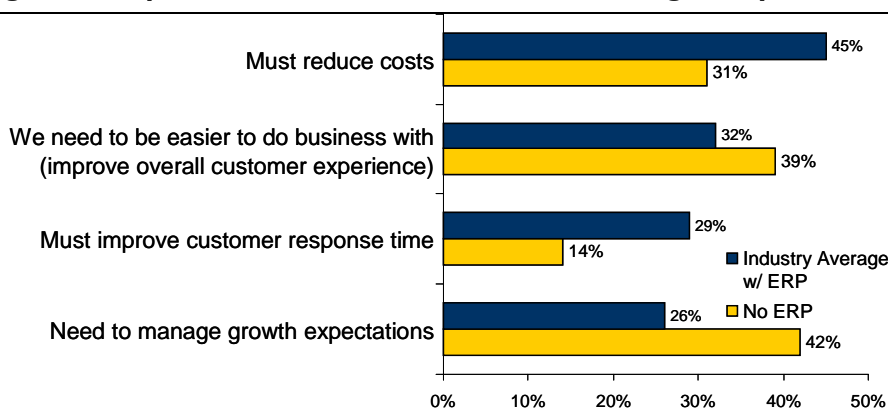
Enterprise Resource Planning (ERP) software is designed to be the system of record for operating and managing a business. But there is still a perception amongst some that ERP is a luxury and a risk in implementation. Even with that, according to Aberdeen's most recent Aberdeen Business Review, almost three quarters of manufacturing companies have some form of ERP. It drops to less than half in other key verticals like retail and healthcare, but is still a significant number.

The key to successful ERP is a strong ERP strategy, not just for implementation, but to keep it operating, growing, and adapting with a company. This Analyst Insight will look at how the changing perception of ERP impacts an ERP strategy. It will also examine how Best-in-Class companies develop and maintain their ERP strategy.

A Perspective on Why Companies use ERP

Before we look at how companies develop an ERP strategy and the perception of ERP, let's look at why companies use ERP to begin with. Figure 1, from Aberdeen's [To ERP or Not to ERP: In Manufacturing, It Isn't Even a Question](#) (March 2011) report, shows what pressures impact the ERP strategy of a manufacturing company. You can see that manufacturing companies with ERP feel a greater pressure to reduce costs, versus companies without ERP being driven by growth and customer issues.

Figure 1: Top Business Pressures for Manufacturing Companies



Percentage of Respondents n=447
Source: Aberdeen Group, March 2011

Now that we know what drives an ERP strategy, let's examine why manufacturing companies don't use ERP. Figure 2, from the same report, shows that the leading reason for not using ERP is because of the fear of the "burden" of the internal effort required to implement.

Analyst Insight

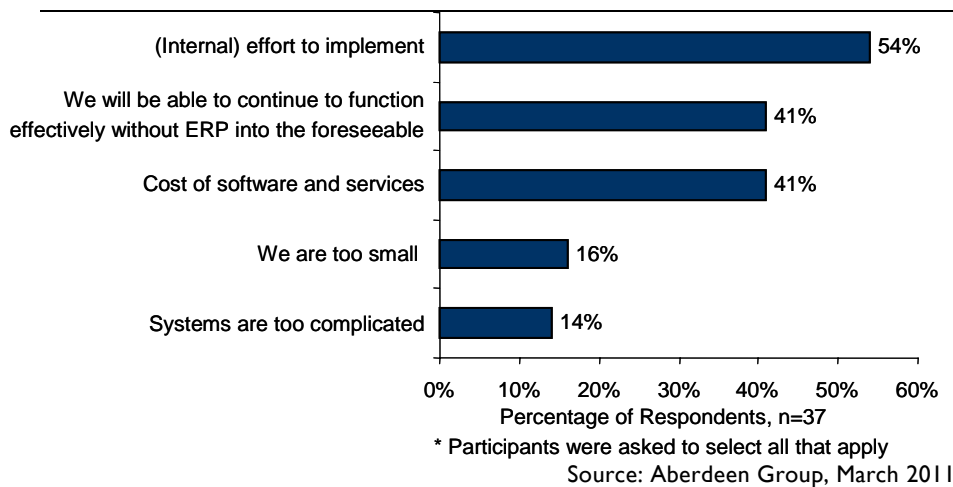
Aberdeen's Insights provide the analyst perspective of the research as drawn from an aggregated view of the research surveys, interviews, and data analysis

Statistics of Companies Without ERP

Companies without ERP tended to be smaller companies. From Aberdeen's [To ERP or Not to ERP: In Manufacturing, It Isn't Even a Question](#) (March 2011) report:

- ✓ 50% were less than \$US 25M compared to 21% of companies with ERP
- ✓ About one third of companies without ERP were between \$US 25M and \$US 100M
- ✓ About one third of companies with ERP were over \$US 250M

Figure 2: Why Haven't You Implemented ERP?



While an ERP implementation can require some effort, it can be successful and pay back whatever effort is expended. To be successful, an ERP implementation must adhere to certain criteria:

- Managed by a cross-functional team from operations, finance, and Information Technology (IT)
- Implementation results are measured including Return-on-Investment (ROI) and operational impact
- Closely aligned with the industry and able to grow as a company changes to meet demand

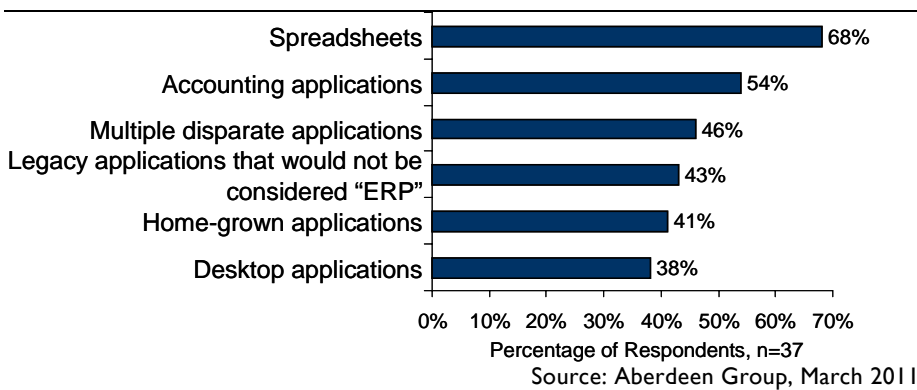
Some businesses feel that they can continue to function effectively without ERP. Those companies' leadership typically feel that since they are relatively small and still growing, they can't take the time to slow down and implement an ERP system. But ERP can help emerging companies track this growth, making sure that nothing gets lost in the cracks. There are many scalable ERP solutions that smaller businesses are implementing in order to fuel their growth. Aberdeen's [ERP in SME: Fueling Growth and Profits](#) report explored the ways in which smaller businesses are employing ERP.

So if a company doesn't have ERP, what are they using? Figure 3, from Aberdeen's [To ERP or Not to ERP: In Manufacturing It Isn't Even a Question](#) (March 2011) report, shows what most people would assume; a combination of spreadsheets, accounting software, homegrown applications, and older business software.

“The entire company relies on the data in the ERP system and could not survive without it.”

~ Steve Crow, Executive VP,
Life Tech, Inc.

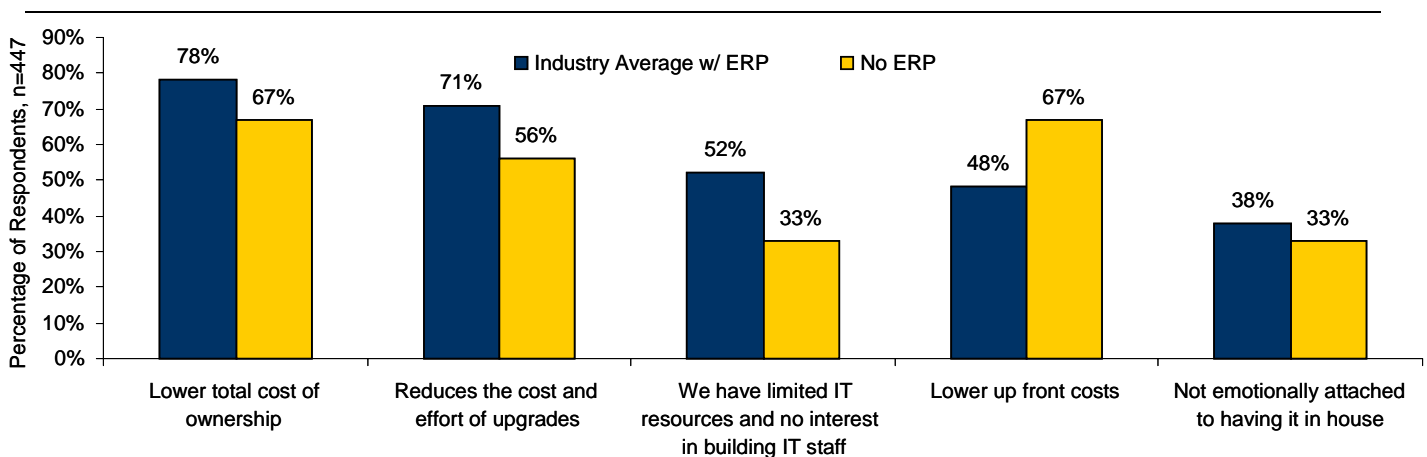
Figure 3: What are You Using Instead of ERP?



Spreadsheets are typically the internal reporting method of choice for most small manufacturing companies and could be considered the biggest competitor that any ERP vendor faces. Spreadsheets are easy to use, almost universally available, and can be emailed to anyone with another spreadsheet application. In fact, most ERP applications assume that users will continue to use the data from the ERP system as exported spreadsheet files. But spreadsheets do not easily roll up, standardize processes, nor allow any type of collaboration. That is where companies must graduate to an ERP system.

Also note from Figure 2 that 41% of those manufacturing companies without ERP feel that the cost of software and services is too high. Because of this, one area of interest for companies concerned about the upfront cost of ERP is SaaS, also known as cloud deployment. Aberdeen's [SaaS ERP: Trends and Observations 2010](#) report found that 39% of respondents were willing to consider SaaS as a deployment model for their ERP, a 70% increase over the previous year. Seventy-nine percent (78%) of these respondents are willing to do so because of the lower total cost of ownership (Figure 4).

Figure 4: What Factors into a SaaS Decision

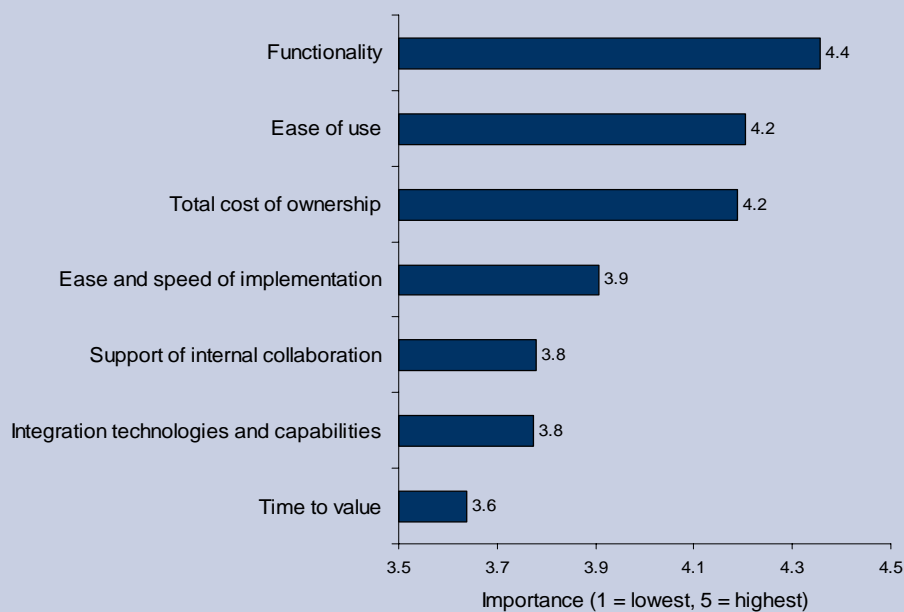


But even with that interest level, SaaS still remains at less than 10% of all deployments of ERP. Users should consider SaaS as another deployment method, but only as an option along with on-premise and hosted. Choosing a multi-deployment capable ERP is important in many circumstances so a company has the ability to choose whichever deployment option fits its environment.

Aberdeen Insights — Selection of an ERP

Seeing the impact that a good ERP strategy has on a company's performance, you can understand the critical nature of the selection process. Aberdeen's January 2011 document, [Economy 2011: Back on Track for Growth?](#) highlights the typical selection criteria and rates the importance to potential ERP users.

Figure 5: Top Selection Criteria for ERP



Source: Aberdeen Group, January 2011

Continued

Aberdeen Insights — Selection of an ERP

As You can see from Figure 5, actual software cost is of lesser importance than other criteria. Functions and ease of use are at the top, but basically, regardless of the cost, companies are saying if I can't use it effectively, no price will be low enough. Looking just below functions and ease of use criteria is Total Cost of Ownership (TCO). TCO is made of the following criteria:

- Implementation effort and cost
- Software cost
- Integration costs
- Maintenance and support costs

The first three components of TCO are in the top seven criteria shown in Figure 5. So in the end, even though fit to function and usability are the top two criteria, TCO or one of its key components makes up four of the top seven.

ERP in Use and at its Best

Table 1, from Aberdeen’s [*To ERP or Not to ERP: In Manufacturing, It Isn't Even a Question*](#) (March 2011) report, shows a comparison of operating metrics for manufacturing companies using and not using ERP. When comparing the performance of companies that have already implemented ERP with those that have yet to, it is clear that ERP is helping these manufacturers to perform better. Companies that have yet to implement ERP consistently perform below the Industry Average. Using ERP, manufacturing companies are improving their inventory accuracy, experiencing faster month-close completions, and delivering more product or services complete and on-time. It is, of course, impossible to measure the reduction in inventory levels as a result of ERP in those businesses that have yet to implement ERP, but the Industry Average of those that have ERP are reducing their inventory by 11%.

Table 1: Performance of Those Manufacturing Companies With ERP vs. Those Without

Definition of Maturity Class	Mean Class Performance
Best-in-Class: Top 20% of aggregate performance scorers	<ul style="list-style-type: none"> ▪ 22% reduction in inventory levels ▪ 97% inventory accuracy ▪ 3.4 days to close a month ▪ 98% complete and on-time delivery
Industry Average: Middle 50% of aggregate performance scorers	<ul style="list-style-type: none"> ▪ 11% reduction in inventory levels ▪ 94% inventory accuracy ▪ 5.3 days to close a month ▪ 93% complete and on-time deliver
No ERP	<ul style="list-style-type: none"> ▪ 90% inventory accuracy ▪ 6.5 days to close a month ▪ 89% complete and on-time delivery

Research Methodology

In the [*To ERP or Not to ERP: In Manufacturing It Isn't Even a Question*](#) (March 2011) report, Aberdeen defines Best-in-Class as the top 20% of performers in the following operational metrics related to ERP:

- ✓ Time to close books
- ✓ Internal schedule compliance
- ✓ Complete and on-time shipments
- ✓ Inventory accuracy

Source: Aberdeen Group, March 2011

Table 2, from *ERP in Manufacturing 2010: Measuring Business Benefit and Time to Value* (June 2010) report, shows the significant impact that ERP has on the operating performance of a manufacturing company. Best-in-Class companies see almost a 20% reduction in overall costs, not to mention the significant improvement in other operating parameters. Even Laggard companies that had ERP implementations at the bottom of the maturity model see about 5% improvements in cost along with improvement in other parameters.

Table 2: Business Benefits Achieved from ERP

Benefit from ERP	Best-in-Class	Industry Average	Laggard
Reduction in operating costs	20%	13%	5%
Reduction in administrative costs	18%	10%	4%
Reduction in inventory	22%	11%	3%
Improvement in internal schedule compliance	18%	12%	7%
Improvement in complete and on-time shipments	17%	13%	5%

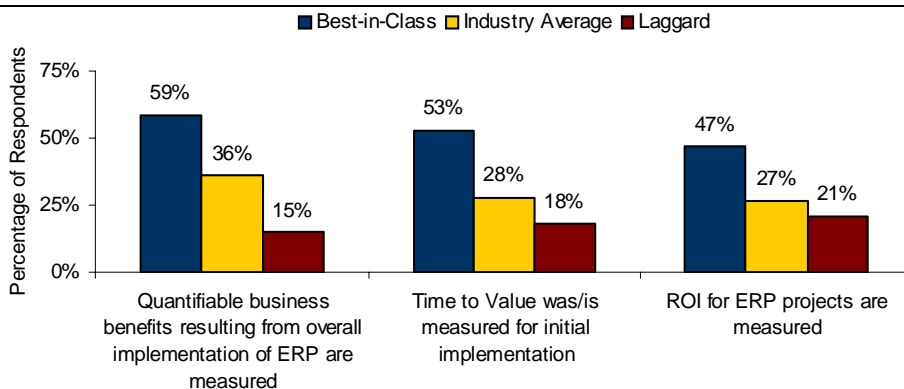
Source: Aberdeen Group, June 2010

So, between Table 1 and Table 2, it is clear that even a bad ERP implementation is better than no ERP implementation.

The Best Keep on Doing It

But once again, it's not just about the final metrics and implementations. It's about a company setting itself up to continue to perform with an organization that is built to operate an ERP system at its best. Many times, it starts out at just being able to measure what success is. Figure 6, from *ERP in Manufacturing 2010: Measuring Business Benefit and Time to Value* (June 2010) report, shows how Best-in-Class manufacturing companies continue to measure and monitor their ERP system, as well as its use.

Figure 6: Measuring ERP's Impact



Source: Aberdeen Group, June 2010

As we can see, Best-in-Class manufacturing companies are over twice as likely to have measuring capabilities in place for ERP implementations. As the ERP strategy is ongoing, those same companies are also almost twice as likely to have a measurable ROI for ongoing ERP enhancements.

Research Methodology (cont.)

In the *ERP in Manufacturing 2010: Measuring Business Benefit and Time to Value* (June 2010) report, Aberdeen defines Best-in-Class as the top 20% of performers in the following operational metrics related to ERP:

- √ 22% reduction in inventory levels
- √ 97% inventory accuracy
- √ 3.4 days to close a month
- √ 96% manufacturing schedule compliance
- √ 98% complete and on-time shipments

Research Methodology (cont.)

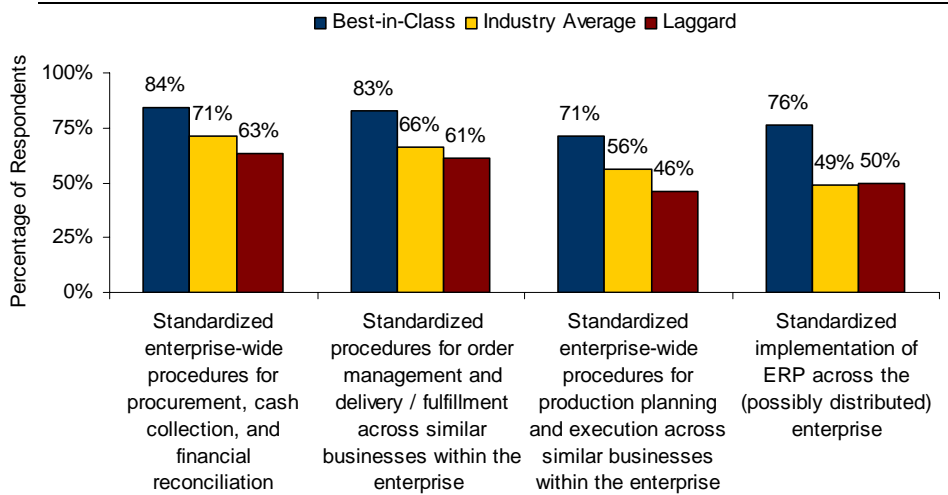
The Aberdeen Maturity-Class Framework defines enterprises as falling into one of the following three levels of practices and performance:

- √ Best-in-Class (20%) — Practices that are the best currently being employed and are significantly superior to the Industry Average, and result in the top industry performance.
- √ Industry Average (50%) — Practices that represent the average or norm, and result in average industry performance.
- √ Laggards (30%) — Practices that are significantly behind the average of the industry, and result in below average performance.

*No ERP — For this report, we also have a category defined as no ERP

Another key capability that a Best-in-Class manufacturing company has over other companies is to standardize key business processes. Figure 7 shows this in detail.

Figure 7: Standard Process Capabilities



Source: Aberdeen Group, June 2010, n = 445

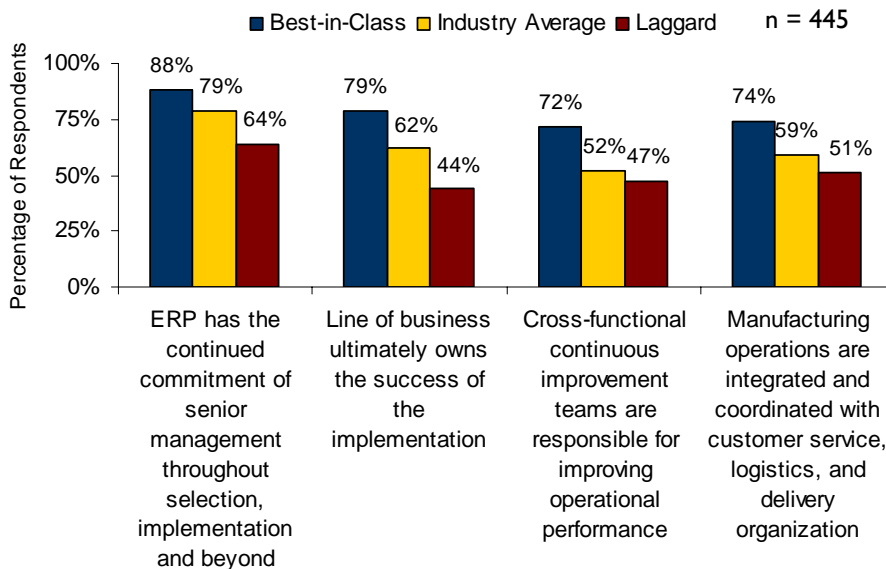
“Since the recession, the ERP has given us the ability to write reports to analyze the data in new ways we wouldn’t have been able to.”

~ Leonard Hartka, IT Director,
Sun Automation Group

Standardization is fairly high across the board in Best-in-Class manufacturing companies. But once you move away from the cash management processes, other companies start to drop off in areas like delivery and planning. And not only does standardizing processes help the process itself, but it makes it easier to apply ERP as a productivity tool in those processes. So the best companies are setting themselves up to be even more successful as ERP expands within their organizations.

One other key area to examine that impacts an ERP strategy is a company’s organization around ERP and its operation. It is not to say that a company needs to completely reorganize itself to use an ERP system, but rather as Figure 8 shows, to have commitment at a senior level to make ERP the primary operating systems.

Figure 8: Organizational Capabilities



Source: Aberdeen Group, June 2010

Also, making the business leaders own the final success of the ERP strategy and system is a significant difference between Best-in-Class manufacturing companies and Laggards. One other area of note where Best-in-Class companies out perform all others is in continuous improvement. Best-in-Class companies recognize that cross-functional teams are a key to continuous improvement. While not necessarily tied directly to an ERP strategy, it does show that Best-in-Class manufacturing companies recognize the need for internal collaboration for success.

ERP Strategy Beyond Implementation

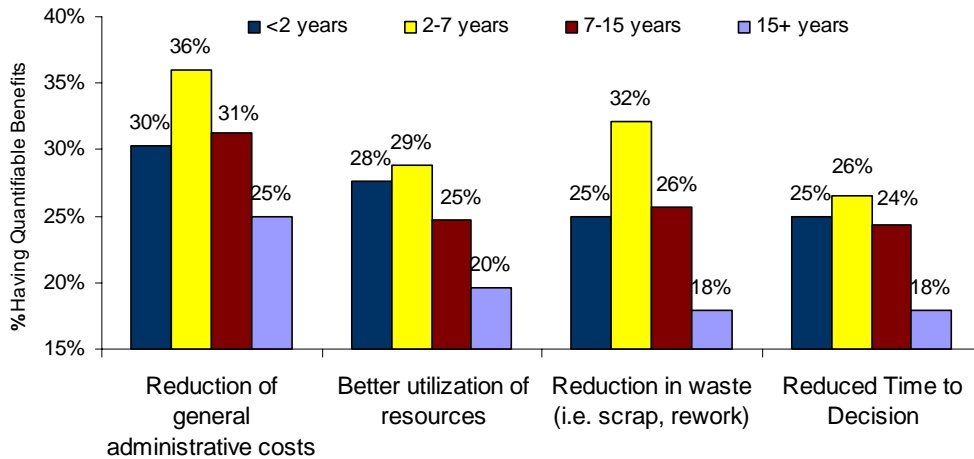
A critical part of any ERP strategy is keeping the ERP current and relevant. An ERP strategy that lags behind current operational needs can quickly lead to operational issues. The *Aging ERP: When Old ERP is Too Old* (May 2011) report found that there are distinct differences in operational benefits depending on the age of a system (Figure 9).

You can quickly see that the benefits form a fairly obvious bell curve with ERP systems between two and seven years old forming an ERP sweet spot. As an example, let's take a quick look at administrative costs. Companies with ERP systems between two and seven-years old have almost 30% more reduction in costs than companies with systems older than 15 years. There is even a 15% difference with systems that are between 7 and 15 years old.

"We measure the success of our ERP implementation by the amount of time we spend creating each component of our business: quote, order, job, PO, invoice. We also consider the ease of tracking jobs, accounting information, inventory control, and purchased components. The final factor is time spent maintaining, training, and procedural-izing the system and the personnel required to use the system."

~ CEO, Small Tooling and Machinery for the Packaging Industry

Figure 9: Benefits from ERP Implementation by Age of ERP



Source: Aberdeen Group, May 2011

What is also interesting is that systems that are within the first two years of implementation are also lagging behind the systems that have been in-place for two to seven years. It is most likely that new systems are still rolling out and users are still becoming familiar with the use of the system. Systems more than seven years old are going to be based on older software infrastructure and possibly hardware, but users are typically very comfortable with the system. Systems older than 15 years are usually going to suffer from lack of integration and modern programming tools.

This is most likely a result of a combination of things:

- Age of the software infrastructure
- Lack of available modules
- Lack of support for the ERP system
- Aging hardware
- Lack of integration capabilities

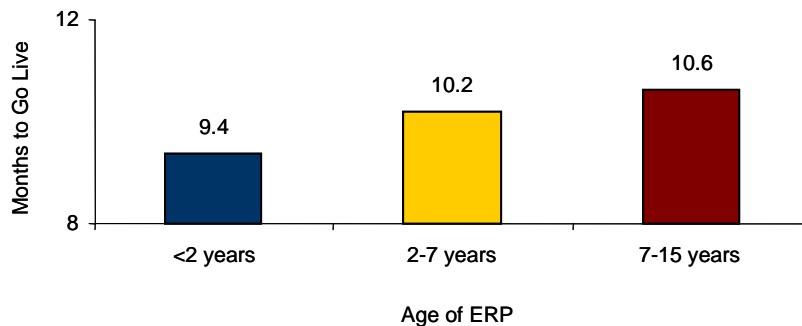
This doesn't mean that older systems can't be integrated and tied to other business systems, but it can cause ongoing integration work that is not supported with any automation features from the vendor (if the vendor still exists).

An area of distinction that may cloud some companies' decision-making around ERP strategies is time to get the system up and running. Figure 10 shows that newer systems take 30% less time from install to operation than older systems.

“We use a system that requires very little customization and can be supported remotely. Our older accounting systems require expensive onsite support.”

~ Andy Schmidt, IT Director,
Sun-Maid Growers

Figure 10: Time from Install to Operation



"We replaced our old and heavily customized system with an up-to-date system and saw immediate improvements in operations cost and processing time."

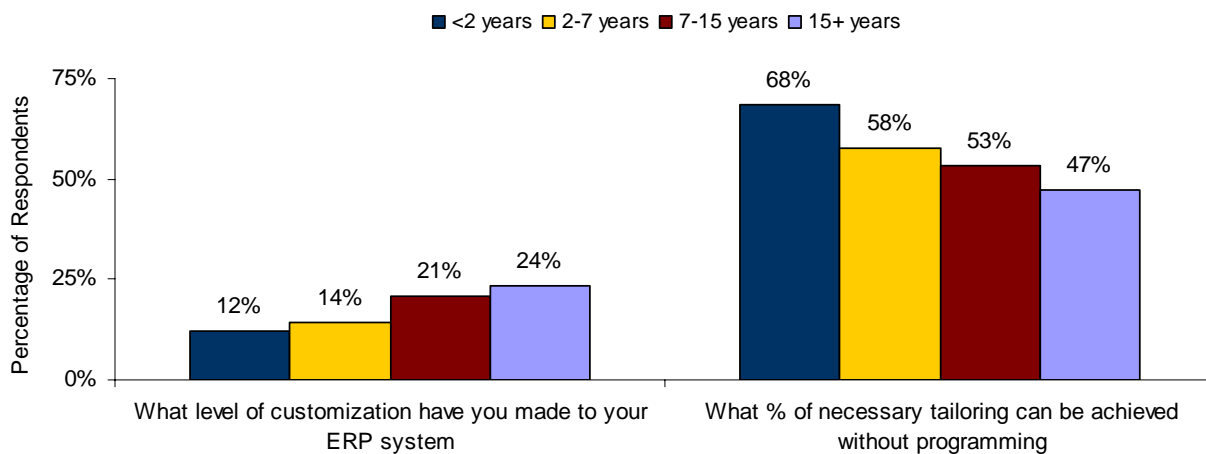
~ Patrick Scanlon, Director,
EOC LLP

Source: Aberdeen Group, May 2011

Figure 10 also gives a good view into how ERP implementations have progressively improved from an effort standpoint over the last 15 to 20 years. It shows that ERP vendors, user companies, and implementation partners have become progressively better at getting ERP up and running effectively.

Another area around ERP strategy that is consistent in our research and in discussions with user companies is about customization. Figure 11 shows the correlation between the age of a system and the amount and ability to make non-customized changes to the system.

Figure 11: Customization and Tailoring of the ERP System

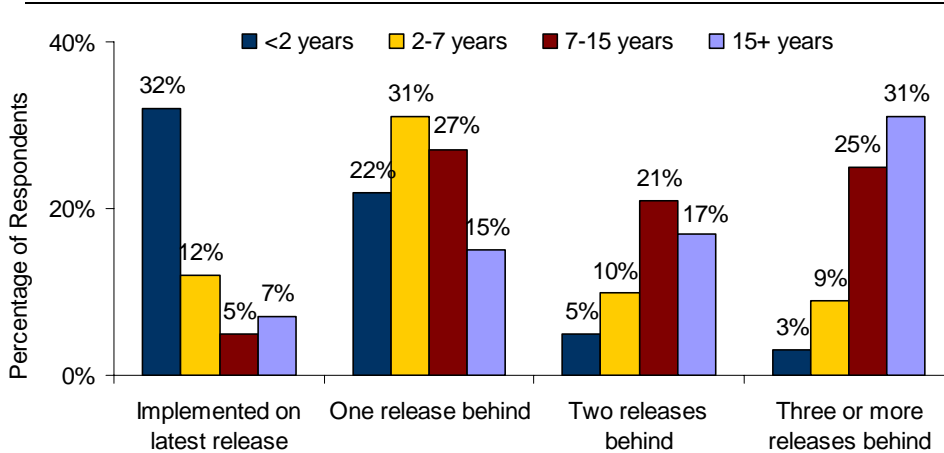


Source: Aberdeen Group, May 2011

The oldest ERP systems have twice as much customization as the newest systems. Figure 11 also shows one of the reasons for this situation. The oldest ERP systems are almost 40% less likely to be able to tailor their system without programming. This leads to higher IT support costs and more difficult system upgrades.

In fact Figure 12 shows that the oldest systems are 10 times more likely to be more than three releases behind on upgrades. The newest systems, as one would expect, are over twice as likely to be current or only one release behind over the oldest systems.

Figure 12: Version Status for ERP System



Source: Aberdeen Group, May 2011

So an ongoing ERP strategy that keeps your ERP system current is a key aspect of any company's ERP success. But an ERP strategy in place that, from the start, keeps growth and ability to change at the forefront is important.

Key Takeaways

Looking at how companies develop an ERP strategy, even if that strategy is to not have an ERP strategy, points to several criteria for having a Best-in-Class ERP:

- Have a cross functional team that develops and maintains an ERP strategy. Seventy-four percent (74%) of Best-in-Class companies used cross functional teams to select and manage the ERP implementation.
- Look at ERP strategy as the means to standardize and streamline your business processes. As we have shown, 84% of Best-in-Class companies using ERP have standardized cash processes, while only a third of companies without ERP have done that.
- Have an ERP strategy that focuses on keeping the ERP system current enough to support growth and changes in the market. For example, systems older than 15 years tend to have 30% higher administrative costs associated with them.
- Set your ERP strategy to minimize customization. Only customize what gives you some competitive advantage. Twice as many

How many ERP systems does your company operate?

The [Aging ERP: When Old ERP is Too Old](#) (May 2011) report found that older implementations have more systems do deal with on average.

- √ < 2 years old - 1.7 systems
- √ 2- and 7-years old – 1.9 systems
- √ 7- and 15-years old - 2.0 systems
- √ older than 15 years - 2.9 systems

companies with older systems have customized ERP compared to just over 10% of companies with newer ERP.

- Measure, measure, and measure. Best-in-Class companies are more than twice as likely as all others to measure and continue to measure their ERP performance.

Our research shows that having an ERP strategy in place that not only focuses on system implementation, but ongoing organizational, business process, and system growth, is the strategy Best-in-Class companies are using.

For more information on this or other research topics, please visit www.aberdeen.com.

Related Research

<u>ERP in Manufacturing 2010: Measuring Business Benefit and Time to Value</u> ; June 2010 <u>ERP in SME: Fueling Growth & Profits</u> ; August 2010	<u>SaaS ERP: Trends & Observations 2010</u> ; October 2010 <u>ERP: Is High ROI with Low TCO Possible?</u> ; January 2011 <u>To ERP or Not to ERP: In Manufacturing, It Isn't Even a Question</u> ; March 2011
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