Industry Report

Is Supplier Consolidation a Good Strategy in Emerging Markets?

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Supplier consolidation is one of the strategies followed by organisations to source effectively. As the supply market is developing in emerging countries, buyers are looking out for opportunities to consolidate. Supply base for lab supplies in emerging markets is fragmented, hence, in order to consolidate supplier base, buyers are following indirect sourcing model through hybrid contract for sourcing lab supplies. This article provides an overview of the trend in sourcing lab supplies in emerging markets. It analyses if supplier consolidation is a feasible strategy in emerging markets to achieve the objectives of procurement team.

Supplier Consolidation – the road ahead

Low cost country sourcing and supplier consolidation are the two major approaches followed by the major pharmaceutical companies to be more efficient and achieve cost savings from procurement viewpoint.

Emerging countries are definitely acting as low cost sources for procurement of laboratory supplies; however, the supply market is highly fragmented in these countries posing a challenge to the consolidation approach.

Supplier consolidation would be a strategy to adopt where the market is consolidated and has major suppliers with complete capabilities. Supply market in emerging countries is fragmented and comprises of small sized companies as against suppliers such as Thermo Fisher or Sigma Aldrich in developed markets.

Hence, in order to support the procurement team to save cost and to leverage the opportunities in emerging markets, supplier consolidation as a suitable approach is in question.

Current Scenario – Shifting to Emerging Markets

Suppliers are moving to emerging markets to manufacture supplies at less cost while buyers are setting up procurement offices there to source and procure at low cost.

Suppliers

To cut down the raw material cost, logistics cost (which is incurred in shipping the raw materials for supplies to US and Europe for manufacturing) and leverage the low cost of labour in emerging nations, major suppliers are moving their production units to countries like China and India.

Import of lab supplies from emerging countries to developed countries is expected to increase significantly in the next 3-5 years driven by entry of major suppliers (Thermo Fisher, VWR and Agilent) into countries, like China and India by setting up their manufacturing plants, to obtain 20-25% savings on manufacturing costs.

For instance, China has rich source of raw materials and their government is providing allowances for the foreign manufacturers who are setting their bases in china. This provides ample opportunities for the suppliers to set up manufacturing bases in China. Lower cost of investments and lesser lead times are few other reasons for the major lab supplies manufacturers to choose countries like China.

Buyers

The big pharmaceutical companies who have entered the emerging markets are sourcing locally from the regional suppliers to meet the local needs. Buyers from developed countries are also trying to leverage on the low cost of materials in emerging countries by importing supplies in order to enhance their cost savings.

In the developed markets, buyers have already consolidated their supply base and source lab supplies from few major suppliers. On the contrary, in emerging markets like China and India, buyers are procuring from multiple suppliers which include a mix of global and local suppliers.

Shift from Direct to Indirect Sourcing Model to Attain Supply consolidation

Traditionally, bigger companies used to source from multiple local suppliers or from global suppliers directly; however, nowadays global suppliers are acting as intermediates or channel partners between the buyer and local suppliers to support supplier consolidation. Supplier consolidation will provide better opportunities for negotiations by leveraging the economies of scale and reduces the total cost of procurement. It also reduces the transaction cost and administration cost. Interference of these intermediates also validates the quality and ensures the supply of right quantity.
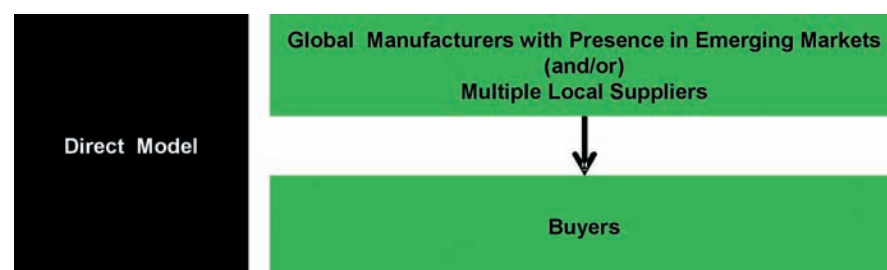

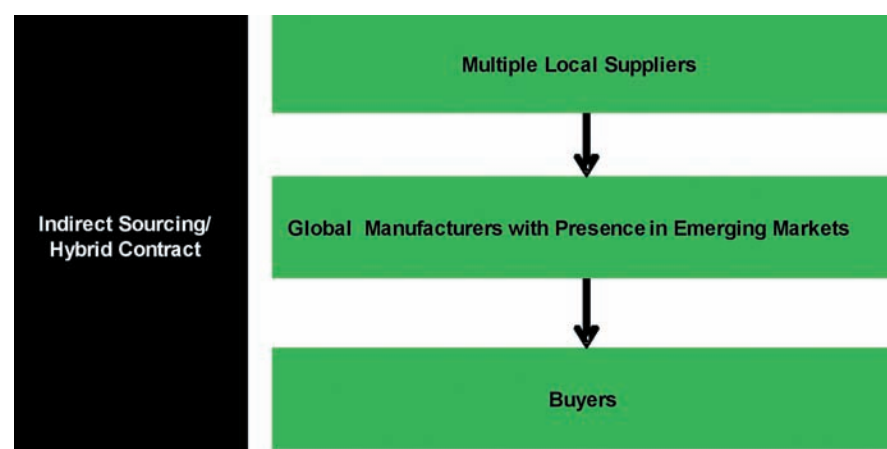
Figure 1. Direct/Traditional sourcing model

Figure 2. Indirect sourcing model

Draw Back in Indirect Model?

Supplier consolidation is achieved through indirect model, however, it seems that some cost saving is achieved, whereas the buyer ends up paying it to the intermediaries. The margin charged by the intermediaries or channel partners to keep up the quality parameter of the supplies is higher or almost equal to the cost saved.

Conclusion

The indirect model appears to support supplier consolidation and help companies save cost but at the end the buyer does not get the desired value. A comparative analysis of the cost involved in direct vs. indirect model considering the time value of money, would help buyers in meeting their actual targets. On the other hand, buyers can effectively negotiate with the intermediaries to reduce the margins to a win-win situation.

Currently, buyers are slowly changing their engagement models and are engaging directly with local suppliers as the benefits of direct engagement exceed that of consolidation. Supplier consolidation could only save the transaction and administration cost, which is trivial as compared to the total cost which gets absorbed as margins to the intermediaries. Hence, buyers prefer the local suppliers for the lab supplies spend by bypassing the major suppliers in the emerging markets.

About Author

Hareesh Reddy Kalavakunta is a research analyst with the Lab Equipment and Maintenance domain. His professional role comprises of efficient project execution, along with authoring white papers and articles. He has 15 months of experience in market research in the field of lab equipment, supplies and PPE.

References

http://www.nextlevelpurchasing.com/articles/supplier-consolidation.html

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