

Understanding Supply Markets and Competition



Supply market analysis assists procurement planning and on-going management of supply arrangements by identifying structure of the market, behaviours, supply chain, barriers to market entry, environmental factors, ethical considerations, the buyer's value in the market (Queensland Government)



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Introduction

Effective procurement requires that P&SM; professionals approach their roles with a high-level view of supply markets and the competitive factors that affect these markets (Monczka et al., 2009).

Porter's (1985) five forces analysis can provide a useful framework for understanding these issues:

1. degree of competition: a high degree can create more options for buyers and suppliers, with factors including speed of industry growth, capacity utilisation, exit barriers, product differences, switching costs and diversity of competitors;
2. threat of new entrants: for example, low-cost-country manufacturers such as China are eroding the competitiveness of traditional industries in the west;
3. threat of substitute products and services: as an example, new sets of growing composites, thermosets and carbon fibres are replacing traditional elements such as steel;
4. the power of buyers: increasing power is leveraged over suppliers in the market when buyers consolidate specifications and industry standards emerge
5. the power of suppliers: fewer suppliers in a market increase the power levels among these individual suppliers.

On a practical level at least three categories of information should be considered when undertaking a market research on suppliers (Monczka et al., 2009). First, the information on total annual purchase volumes deriving from a spend analysis, where spend analysis refers to an integrated internal spend data and external supplier and market data. Spend analysis applies analytical and benchmarking techniques in order to identify risks and opportunities for performance improvements and savings (RAND, 2004).

Second, information obtained from interviews with stakeholders to determine their forecasted requirements. If, for instance, the annual purchase volume for the previous year was £10m there is a need to determine whether this figure will fluctuate up or down next year based on the predicted work volume. Interviews might also be useful to ascertain details of sourcing elements missing from the previous year's figure. Finally, external market research data can identify information on key suppliers, available capacity, technology trends, price and cost data and trends, technical requirements, or environmental and regulatory issues (Monczka et al., 2009).

Definition

Understanding supply markets and competition is imperative for strategic sourcing, which refers to "satisfying an organisation's needs from markets via the proactive and planned analysis of supply markets and the selection of suppliers, with the objective of delivering solutions to meet pre-determined and agreed organisational needs" (CIPS Australia. How Do We Measure Up?).

Successful Application

When undertaking market research on suppliers, and as part of strategic approach to sourcing, procurement teams should conduct a detailed analysis of the marketplace and identify how best to meet forecasted demand (e.g. using information from a spend analysis and stakeholder interviews) against the market conditions predicted for the upcoming year (Monczka et al.,

2009). A supplier analysis generally entails establishing benchmarks through industry databases, issuing requests for information, conducting value chain analysis, and undertaking supplier research to identify specific capabilities and the financial health of key suppliers in the existing supply base or of potential suppliers (Monczka et al., 2009).

Steps to Successful Application

- Ascertain true category spend using spend analysis.
- Collect market data to understand what is happening in the marketplace, as well as what internal customer requirements are. Use various sources, including trade journals and annual supplier reports.
- Analyse the data. Category teams can employ various data representation tools to illustrate and explain the current situation (e.g. Porter's Five Forces analysis, SWOT analysis, or supplier analysis).

Monczka et al. (2009); Pandit and Marmanis (2008)

Hints and Tips

- Make market intelligence a part of organisational learning: organisations need to encourage buyers and P&SM; professionals to develop a market-focused attitude and awareness. This may require extensive training. Also, management must implement policies and practices that support these attitudes and behaviours (Wright et al., 2009).
- Regularly review legislative developments that might have an impact on the methods of collecting competitor information. Use this information to update existing policies or to formulate new ones (Rouach and Santi, 2001).
- Make employees fully aware of the company's policy on 'black information' and unethical/illegal methods of collecting competitor information. Focus on 'white' (e.g. open-source databases, newspapers, the Internet) and 'grey' (e.g. visiting tradeshow, in-house competitor publications) information (Rouach and Santi, 2001).

Potential Advantages

- Using Porter's five forces tool to understand supply markets and competition is not difficult and can provide a solid information to aid with strategic sourcing and the development of general P&SM; strategies (Monczka et al., 2009).
- Market data collected for the assessment of supply markets and competition can be 'triangulated' to provide more robust information for forecasting and decision-making. Triangulation refers to combining different types of data collected from multiple sources to obtain a more rounded, holistic picture (Monczka et al., 2009).
- Spend analysis, used as part of the market research process on suppliers, reveals targets of opportunity where adapting purchasing practices can significantly enhance performance and generate savings (RAND, 2004).

Potential Disadvantages

- Trade consultants can be contracted to conduct market research on suppliers but these services are usually very costly (Monczka et al., 2009).
- Even if the company contracts a market research firm to collect information, data must still be processed internally and integrated with other data so that it they are relevant and capable of being easily communicated to stakeholders (Monczka et al., 2009).
- Secondary data used in supplier market research may be outdated and therefore fail to provide the specific information required (Monczka et al., 2009).

Performance Monitoring

- Strategic alignment: measure of visibility of a formally documented procurement strategy/percentage of objectives linked to business strategy/percentage of procurement time spent on global and enterprise-wide focus (CIPS Australia. How Do We Measure Up?).
- Spend under management: a traditional measure of procurement's impact on a company is the percentage of all non-payroll related spend falling under management of this group (Bartolini and Dwyer, 2008).
- Porter's industry analysis: can be used to develop appropriate benchmark measures to position the company against competitors. Measure of profitability is a basic starting point (Porter, 2008).

Case Studies

- Recent research shows that by 2015, outsourcing of business services to China will more than double in value to US\$9.5-\$10b (£6-£6.3b). The research forecasted that cost arbitrage will remain favourable over the next 13- 14 years, which will enable companies adopt a relatively long-term strategy on offshoring (Supply Management, 2011b).
- Companies who establish the link between information on spend and information on categories to enhance purchasing increase savings by 67%, achieve 25% more spend under control, and improve contract compliance by 11% more than those failing to make the link (Bartolini and Dwyer, 2008).
- GlaxoSmithKline (GSK), a leading pharmaceutical manufacturer and R&D, on average has an annual return of 5,451% from its sourcing programmes. The company recognises that by raising visibility and control in sourcing, suppliers can be held more accountable, better terms and conditions can be negotiated and the learning process can be channelled across the supply base (Pandit and Marmanis, 2008).

Further Reading/References

CIPS Source Downloads

- CIPS Australia & Portland Group: Strategic procurement benchmarking survey report
- CIPS: Anti-competitive practices
- CIPS Australia: Dealing with monopolistic & distorted supply markets
- CIPS Australia: From strategy to practice: Making procurement strategies work in the real world
- CIPS: Managing purchasing & supply management resourcing & competencies

Web Resources

- Supply market analysis kburl.me/peaaau
- Competition and supply chain innovation kburl.me/jzxrl
- Porter's five forces article kburl.me/egzwwk
- Competition Commission examines the big supermarkets kburl.me/jo6ym
- Understanding supply kburl.me/oiapn

Books

- Useful guidance on strategic sourcing and spend analysis.
- Information on supply market research.
- Step-by-step guidance on strategic sourcing and market analysis.
- Handbook on supply market intelligence.
- Strategic supply chain management.

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Video

Interview with Michael Porter: The five competitive forces that shape strategy
https://www.youtube.com/watch?v=mYF2_FBCvXw

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Video

Cisco agile supply chain

https://www.youtube.com/watch?feature=player_embedded&v=nbWalgv3f7s

CIPS Group Easton House, Easton on the Hill, Stamford, Lincolnshire, PE9 3NZ, United Kingdom
T +44 (0)1780 756777 F +44 (0)1780 751610 E info@cips.org

CIPS Africa Ground Floor, Building B, 48 Sovereign Drive, Route 21 Corporate Park, Irene X30, Centurion, Pretoria, South Africa
T +27 (0)12 345 6177 F +27 (0)12 345 3309 E infosasa@cips.org.za

CIPS Australasia Level 8, 520 Collins Street, Melbourne, Victoria 3000, Australia
T 1300 765 142/+61 (0)3 9629 6000 F 1300 765 143/+61 (0)3 9620 5488 E info@cipsa.com.au

CIPS Middle East & North Africa Office 1703, The Fairmont Hotel, Sheikh Zayed Road, PO Box 49042, Dubai, United Arab Emirates
T +971 (0)4 327 7348 F +971 (0)4 332 5541 E mena.enquiries@cips.org



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