



THE FUTURE OF PROCUREMENT FOR PHARMA OPERATIONS

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AT MANY PHARMACEUTICAL companies, procurement is long overdue for a major upgrade. The COVID-19 crisis creates an urgent need, as well as a unique opportunity, to ensure that the procurement function can optimize risks and costs in effectively supplying technical operations (TechOps).

To achieve and sustain step-change improvements, companies need a carefully sequenced, self-funded transformation approach. Gaining greater visibility into spending lays the foundation for improving the management of categories and suppliers as well as optimizing expenditures on indirect categories. To fully unlock the opportunities, companies must build the enabling capabilities related to people, systems, and digital analytics.

These improvements provide the basis for a strategic collaboration in which procurement teams take a seat at the table with business and finance teams to proactively manage costs across the life cycle of products.

It's Time for a New Procurement Paradigm

Procurement functions are playing a pivotal role in getting pharma companies through the COVID-19 crisis. The pandemic has created unprecedented supply chain uncertainty, disrupted manufacturing operations, and complicated demand forecasting. The challenges for supply chain continuity and supplier risk management are likely to continue for the foreseeable future. And they come on top of other issues that pharma companies have been coping with in recent years, including higher pressure to reduce costs, more intense regulatory scrutiny, and faster cycles for product launch. At the same time, however, the crisis has opened a window of opportunity to decrease spending and fundamentally rethink the role of TechOps procurement.

Some pharma companies have started to improve the procurement capabilities that support TechOps, mainly by deploying digital technology, but most are still far from matching their peers in consumer goods and other adjacent industries. For a variety

of reasons, pharma firms have been reluctant to radically upgrade procurement. Once a company selects a product platform, its costs are generally locked in throughout the product life cycle. This makes it hard to change the approach to procuring products in specific categories and managing suppliers. If a company does make changes to its supply chain, it may need to address regulatory compliance issues and adjust quality requirements—which, again, creates obstacles to doing things differently.

Decentralized decision making and siloed perspectives on costs can also impede a company’s ability to make fundamental changes. Similarly, the supplier network is typically fragmented and has grown organically without an eye toward enterprise-level costs. The network is managed decentrally, often on the basis of undocumented knowledge held within subgroups of managers.

The time has come for pharma to overcome these obstacles to change. For solutions, companies can look to the approaches that other industries have already successfully applied to optimize costs and minimize risks in the supply chain.

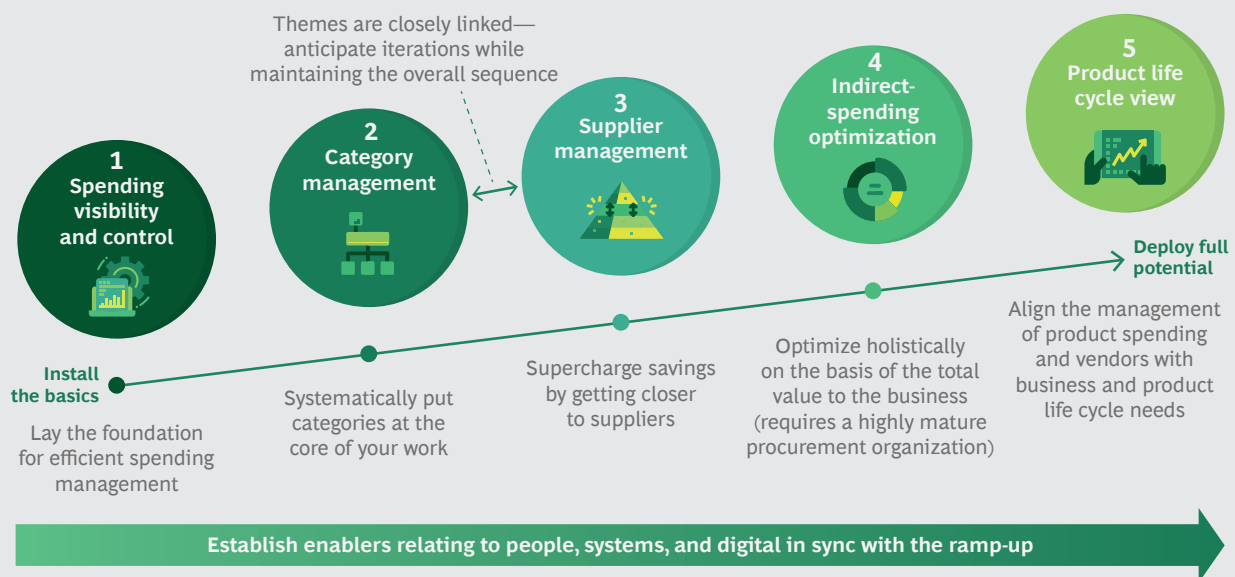
Five Transformation Themes

To transform TechOps procurement, a pharma company needs to address five themes: spending visibility and control, category management, supplier management, indirect-spending optimization, and product life cycle cost view. Considering the complexities and challenges associated with each of these themes, a systematic ramp-up is crucial to gradually achieve higher maturity. (See Exhibit 1.) This is facilitated by applying the Pareto principle—taking a tiered approach that focuses first on the small number of topics that offer the lion’s share of the improvement opportunities.

1. SPENDING VISIBILITY AND CONTROL

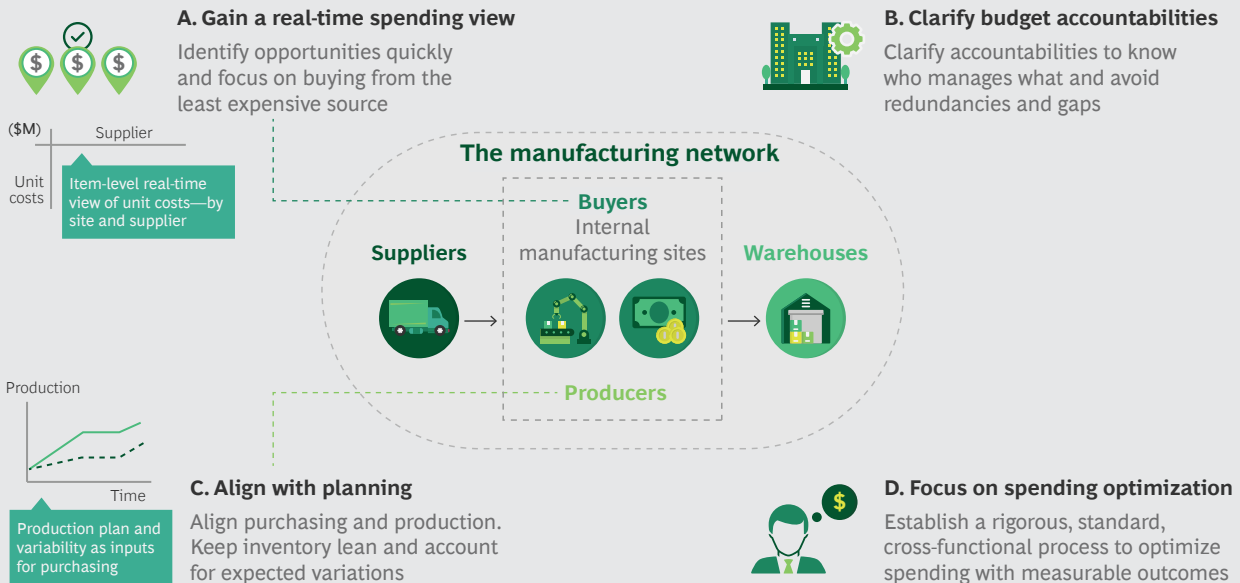
The COVID-19 pandemic underscores the need for transparency and speed in procurement organizations. Companies must respond and adjust instantaneously to the crisis and associated changes in global supply chains. They can use a real-time view of spending to readily assess item-level information on unit costs by site and supplier. (See Exhibit 2.) This provides a baseline for identifying opportunities to save costs or leverage procurement synergies across the manufacturing network. Compa-

EXHIBIT 1 | Five Themes for a Sequential Transformation



Source: BCG.

EXHIBIT 2 | Promote Spending Visibility and Control



Source: BCG.

nies also need insights on future demand (over the short, medium, and long term) so that they can optimize contract terms, quantities ordered, frozen horizon periods, and vendor-managed inventory.

To drive scale and efficiency across the network, the procurement organization needs a clear structure for decision making and rules on decisions rights related to buying and spending. This clarity is especially valuable to address the complexity of decentralized site-level purchasing.

Procurement organizations that reach a high maturity level for spending visibility and control can create tremendous value. And, because these improvements do not alter the related manufacturing processes, a company can capture this value without the need for lengthy regulatory reviews.

2. CATEGORY MANAGEMENT

Procurement functions should fundamentally rethink how they implement category management in TechOps. By transitioning to an approach based on segmentation, maturity, and opportunities, the organization can manage the complexities entailed in achieving output targets. This helps the

company identify early savings—such as quick reductions in indirect spending—that can be applied to fund the subsequent journey.

Categories differ with regard to the effort or lead time required for a change. For example, in some cases, changes in secondary packaging might be simpler than getting regulatory approval to change an excipient or sourced active pharmaceutical ingredient (API). But, rather than considering one category at a time, procurement functions should group them into segments on the basis of clearly articulated priorities. Procurement teams can then consider each category's maturity in order to focus on where changes can yield the greatest benefits. Finally, by prioritizing according to the size of the spending under consideration, the organization can identify and pursue the most valuable opportunities first.

This approach to category management provides a robust foundation for realizing savings through supplier management, which is the natural next step and closely linked. A successful procurement organization seamlessly iterates its activities in both areas.

3. SUPPLIER MANAGEMENT

Supplier management is not a new concept, but many procurement functions fail to maximize its impact because they do not implement it rigorously. To manage relationships effectively, an organization should consider four segments of suppliers:

- **Enterprise.** This group comprises the company's top three to five suppliers. The company typically has close, longstanding partnerships with these vendors that are crucial to maintain sales and profitability. To manage these relationships, the head of TechOps should engage with the supplier's C-suite executives on top priorities and opportunities for collaboration and knowledge sharing. The parties should conduct regularly scheduled meetings to discuss the overall partnership and identify areas of focus. Key joint efforts could include, for example, codevelopment of products and coinvestment in capabilities.
- **Strategic.** These vendors are the next level of 10 to 20 suppliers with which the company has a stable, collaborative connection and mutual interests. A middle manager in TechOps should sponsor the relationship. As with the enterprise suppliers, the parties should conduct regular dialogues to discuss collaborations. They should also track a set of metrics to ensure that the joint projects are scalable. Key topics that parties can team up to manage include specifications (for example, through standardization), demand (such as via vendor-managed inventory), innovation, and cash flow.
- **Core.** This tier is composed of suppliers (typically 30 to 40) that the company purchases from regularly but does not view as key long-term partners. Supplier management staff in TechOps can manage these connections using standardized processes. The key to driving value is to monitor vendor performance using tangible metrics, such as on-time and in-full delivery and right-first-time delivery.

- **Extended Core.** The lowest tier consists of vendors with which the company conducts infrequent and mostly low-volume business. The supplier management staff can deal with these relationships on an ad hoc basis.

4. INDIRECT-SPENDING OPTIMIZATION

Addressing indirect spending in TechOps—not only for quick savings but also holistically—is difficult. Indirect spending is often not well managed because business teams make decisions without input from procurement groups. To oversee spending effectively, companies need to consider two options.

The first is for business and procurement teams to agree on a new working model in which they make purchasing decisions jointly from the outset (such as when outsourcing or offshoring).

The second is for the business side to agree to let the procurement function take the lead in making decisions so that procurement can apply its expertise to drive savings. This may require business teams to accept a different, more streamlined service level (such as for capex management).

For either option, the optimization effort benefits from achieving maturity in the first three themes.

Typically, companies can pursue holistic savings in three indirect categories:

- **Capex.** For capital expenditures relating to sites, buildings, and equipment, the aim is to optimize spending on the basis of the total cost of ownership—encompassing design, operations, and decommissioning. A company should consolidate capex requirements and evaluate the return on investment (ROI). Budgets should prioritize capex according to ROI before the company negotiates the terms of arrangements and makes investments.
- **Enterprise-Level Expenditures.** The procurement function should consolidate spending across the company and

identify synergies that allow it to comprehensively reduce costs. Success requires a review of purchasing fragmented across sites. This allows the organization to identify large spending categories—such as those relating to facilities, IT, logistics, utilities, and maintenance, repair, and operations—before it negotiates agreements with suppliers.

- **Spending for Professional Services.** A company needs transparency into its expenditures for services such as for quality control, engineering, regulatory support, and lab and equipment maintenance. It can use the insights as the basis for negotiating master services agreements that cover sites across the enterprise. By aligning service requirements and consolidating budgets across sites, a company can facilitate negotiations with core service providers.

5. PRODUCT LIFE CYCLE COST VIEW

The procurement function should jointly set priorities with the business side for costs and initiatives along the product life cycle. Effective deployment requires a close partnership with the business teams and product lines. The procurement function should participate in product life cycle management to discuss the sourcing and cost strategy at each step, drive the make-versus-buy decisions, and take action on the agreed-upon priorities.

Cost management is the component that has the greatest impact, and is the most complex, in managing the product life cycle. The impact arises from the reduction of lead times enabled by the close partnership. But the complexities involve soft aspects (such as collaboration across functions, including with commercial) and hard aspects (for example, consistent visibility on the cost of goods sold [COGS] and product-level spending).

Sequencing the Transformation Journey

Companies need to take a rigorous approach to sequencing the rollout of the transformation in order to ensure its long-

term sustainability and scalability. (See Exhibit 3.)

Three of the themes—spending visibility and control, category management, and supplier management—are addressed first to provide the foundation for the transformation. They enable the company to realize initial savings in order to fund the subsequent journey, and more important, establish a basis for systematically identifying new opportunities. The timelines for improvement and one-off savings depend on the company's current maturity. With the foundational themes in place, the company can implement indirect spending optimization and the product life cycle view to reach the full potential of its transformation.

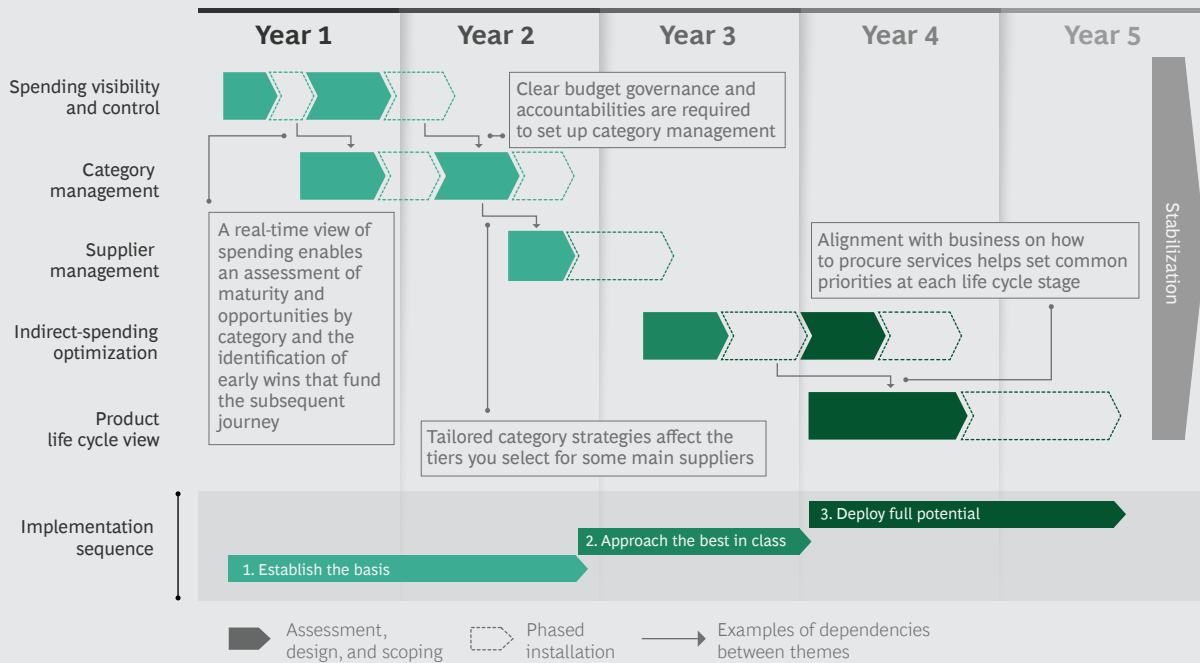
Establishing Enablers

To systematically upskill its procurement organization, a company must put in place the right enablers. And this effort must be synchronized with the development of the five transformation themes in order to ensure success.

Drawing upon BCG's Procurement Excellence framework, we consider three enablers to be essential for a successful transformation of TechOps procurement:

- **People.** The workforce and internal stakeholders in procurement and other TechOps functions must agree on incentives that promote the transformation's goals for value realization (such as cost optimization). Success also requires a smarter approach to collaboration among the business, finance team, and procurement function. Procurement should have a seat at the table with other functions when the company makes key decisions along a product's life cycle. Additionally, the company needs to align the organization structure as well as roles and responsibilities with its new strategy for supplier and category management.
- **Systems.** To enable active and effective management of spending, a company

EXHIBIT 3 | Sequence the Rollout to Promote Sustainability and Scalability



Source: BCG.

Note: Progress on enablers embedded in work on themes (not explicitly shown).

needs to upgrade its enterprise resource planning (ERP) system. A “smart” ERP provides a real-time view of all spending and offers the ability to instantly visualize those expenditures by category and supplier. Additionally, a company should link data related to COGS and the product life cycle stages to the ERP.

- Digital Analytics.** This element is the ultimate enabler, making it possible to realize the potential of people and systems. To empower employees and leverage real-time data systems, a company needs intuitive and highly interactive interfaces. Digital analytics should allow procurement teams to seamlessly switch between or combine real-time views on actual spending, taxonomies, overarching categories, and vendor scoring, among other topics. A company can make the identification of novel opportunities more intuitive by enabling and linking simple analyses of the evolution of COGS and procurement spending over time by product.

Three Imperatives for Getting Started

As it begins its transformation, a company should address three strategic imperatives:

- Review the operating model for TechOps procurement and upgrade it as needed. Ensure that the procurement function has a seat at the table when business and finance leaders discuss product life cycle issues.
- Build the core capabilities required to create value in each of the five transformation themes.
- Ramp up investments in enablers. Develop the relevant talent, gradually improve systems, and pursue the full value potential of digital analytics.

PHARMA COMPANIES THAT lead the way in initiating and scaling up a transformation will gain significant advantages in cost and risk management. Moreover, the benefits of achieving step-change

improvements in TechOps procurement will extend beyond individual companies to the entire pharma industry and the health care ecosystem. Considering the lead time required, companies need to start taking action today in order to

capture the benefits in the years ahead. The COVID-19 crisis has created the motivation and the circumstances to transform TechOps procurement—pharma companies cannot afford to let the opportunity go to waste.

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