Marketplaces: Contract Procurement and the Role of Advocacy

The B2B online market represents a tremendous opportunity — $1.8 trillion in 2003 according to Forrester. Not surprisingly, competition is intensifying in many segments. In markets that are evolving the fastest, various models have emerged. However, they only address spot functionality within the procurement value chain. Creating solutions for contract purchasing — and implementing the specific functionality required to do so — will become essential for capturing value in many industries. In turn, online marketplaces will find it difficult to remain neutral as increasing demands for functionality are better met through advocacy.

Across industries, contenders are vying for influence over which business models will succeed (e.g. advocacy v neutrality). Even within an industry, some players offer multiple marketplace models such as auctions, reverse auctions and basic RFP/RFQ (i.e. CheMatch, Covalex).
Successful e-marketplaces will facilitate functionality across all seven components of the procurement value chain.

Procurement Process

Needs Assessment	Vendor Management	Order Management	Inventory Logistics	Payment	Measuring/ Monitoring	Customer Service
• Conduct data gathering • Research industry environment • Conduct benchmarking • Develop product specifications • Determine goods required and budget • Set policy (who can order, budget)	• Identify vendors • Develop RFP templates • Send out RFP to vendors • Analyse bids • Conduct negotiations • Sign contract • Determine preferred vendors	• Identify necessity of ordering • Fill out requisition – gain approval • Generate order • Transmit order to vendor • Receive confirmation • Track order	• Arrange delivery • Arrange for inspection, authenticatior • Trace lost/ delayed items • Route items to internal customer • Confirm receipt • Update inventory	• Receive invoice • Verify invoice with GL/AP • Authorize payment • Transmit payment • Receive payment confirmation • Integrate payment with financial system	• Create spending reports • Review reports and assess compliance with budget and policy • Follow-up with non-compliant business units	•Detect problem orders •Communicate with vendors •Return item •Receive replace-ment

Four of these areas — order management, inventory logistics, payment and customer service — are particularly crucial for both spot and contract purchasing. Current exchanges address only a portion of these core procurement elements. However, the next generation of marketplaces will incorporate additional spot functionality.

Contracting is the dominant form of transaction in many industries. Up to 60 percent of the volume in some industrial and commodity markets is under long-term contracts with pre-negotiated prices, according to Morgan Stanley Dean Witter. And many firms cite contracts as their primary means of managing eCommerce risk, according to Forrester. These needs are best met by enhanced functionality around contract procurement.

Contract functionality will emerge as a part of a bundled procurement offering. Complex products that compete along multiple dimensions and products that have service agreements require contracting to ensure a specific, comprehensive and clear agreement. Until the derivatives market becomes comprehensive enough to cover the product price risks for mid-to-small markets and businesses, buyers and sellers will want contract protection from price fluctuations. Contracting allows fixed pricing, a series of price changes, or even hybrid agreements with fixed and variable components. Declining cycle time expectations require timely delivery of critical production inputs. Contract terms that can be included to address this need are delivery schedules and late penalties. Lack of company reputation in many neutral exchanges creates an additional layer of default risk for which marketplaces rarely insure. Contracts allow for the stipulation of contingencies and provide a stronger basis for legal recourse. Finally, relationship-specific investments — such as those involved with systems integrations — require the long-term commitments that contracts can solidify.

Three areas of the procurement value chain — needs assessment, vendor management and measuring/monitoring — are particularly important for contract purchasing. Most e-marketplaces largely ignore the significance of this space. And those that attempt RFP/RFQ processes are extremely limited in offering value beyond request submission (e.g. analysis).

Enhanced functionality should be provided in all three areas critical to contract procurement. Activities such as data gathering and benchmarking can be automated. Electronic questionnaires could be sent to conduct preliminary interviews. Analysis tools could aid decision-making by presenting formatted data in summaries and hybrid scenarios. Three-way negotiations could take place online, facilitating multiple constituency management. Finally, compliance can be monitored with rules engines that submit email follow-up to non-compliant units.

In order to capitalize on the benefits of increased functionality, e-marketplaces will find it difficult to remain neutral. Some neutral marketplaces will evolve towards a buy-side orientation. In the process, they will move from providing high-level industry information to determining user requirements, developing specification, benchmarking and analysing bids. Functionality will grow from trade facilitation to formulating recommendations. E-marketplaces will evolve from intermediators to procurement service providers.

On the sell-side, formerly neutral marketplaces will advance from the same high-level information publishing to create market tools for forecasting demand and analysing probability of bid acceptance. They will develop recommendations around specification packages and optimised pricing. They will provide basic customer relationship management functions. And in offering this enhanced functionality, e-marketplaces will predominately advocate in order to remain effective.

Ed Chen, Sept 2000