

BENEFITS

of Vendor Consolidation

in the

NEW HEALTHCARE ECONOMY



WHITE PAPER

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EXECUTIVE SUMMARY

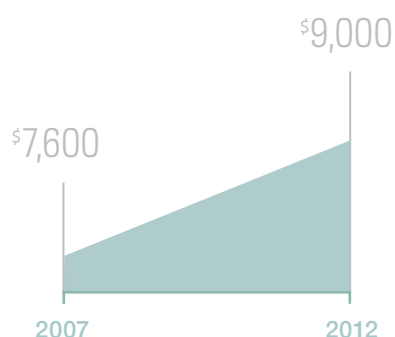
The healthcare industry is facing unprecedented change. Between healthcare reform, growing cost of supplies, and rapid expansion of technology, healthcare organizations must transform to meet the challenges head-on.

When the supply chain strategy is directly aligned to this mission, it becomes a strategic asset that helps healthcare organizations drive toward a brighter future for employees and patients alike.

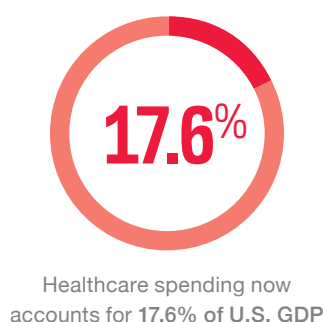
Healthcare reform has brought with it major coverage expansions, increasing demand for healthcare, and new requirements and regulations. The effects on the healthcare industry have been dramatic. Between 2007 and 2012, there was a massive increase in healthcare costs per person — from around \$7,600 to \$9,000.ⁱ Healthcare spending now accounts for 17.6% of U.S. GDP and is expected to reach 19.8% by 2020.ⁱⁱ

Expenses continue to grow for manufacturers and distributors of medical and surgical supplies. Margins continue to shrink as fuel cost fluctuates and raw materials costs increase. Add to this the fact that, when healthcare organizations' budgets get tight, supply typically gets cut before personnel, and vendors are put in increasingly tough positions.

Healthcare cost per person:



Percent of U.S. GDP:



by **2020**

it's expected to reach

19.8%



Technology is rapidly expanding, bringing with it life-saving developments, as well as products and services that enable healthcare organizations to streamline operations and provide higher-quality services to patients. But this technology comes at a price — and it does have a shelf life. With the federal government mandating certain technology investments, and aging IT systems requiring updating and replacement, technology is as much a burden as a blessing to healthcare organizations.

Through these challenges, healthcare organizations are innovating and evolving to ensure their life-saving services are available to those who need them. Yet, many organizations neglect to see that the supply chain can have a direct effect on the bottom line.

Smart healthcare organizations are focusing on solving supply chain issues to decrease costs and improve efficiency. The majority of supply chain leaders and hospital C-suite executives agree that better supply chain management leads to improved patient safety, increased revenue, and better quality of care.^{III} In fact, supply chain leaders enjoy 20% to 50% lower supply chain costs^{IV} than average performers.

The ongoing UPS Pain in the Chain Survey^V has become a standard gauge of supply chain health for the healthcare industry. The results of the 2015 survey revealed that cost management is still a significant supply chain issue.

In this white paper, you will learn the most pressing issues facing the healthcare supply chain today, and how consolidating vendors can be a huge step forward toward transformative change.

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WHAT'S AILING THE SUPPLY CHAIN

Supply chain costs are the second largest, and fastest growing, operational expenses within healthcare organizations. In fact, supply chain represents 40% to 45% of total hospital operating expenses.^{IV} Between the cost of products and the labor, and overhead to manage them, it's easy to see how big an impact the supply chain can have on healthcare organizations.

According to the UPS survey, the top challenges to managing supply chain costs include:

Rapid business growth: Healthcare reform has driven increased demand for healthcare services by an ever-growing number of consumers.

Fluctuating fuel and raw materials costs: As gas prices ebb and flow, it becomes more difficult for healthcare organizations to predict and budget for supply transportation costs. The increasing cost of raw materials, such as resin, latex and paper/pulp, are hitting suppliers hard — and their customers are bearing that burden more and more.

Increasing regulatory requirements: Products must meet not only the healthcare organization's specifications, but also the government's requirements — which are expanding with healthcare reform.

New market expansion: Also thanks to healthcare reform, a new population of customers now has easier access to healthcare — but those customers also now have a wide variety of options. Capturing and serving these new markets poses unique challenges within healthcare supply chains.

Investments in technology, including addressing aging IT systems: As new technology arises in both patient care and healthcare operations, and as the federal government mandates increased investments in electronic records, healthcare organizations face important decisions. Aging IT systems are also a concern, as updating and replacing them adds cost to the supply chain.

Though there has been progress in addressing healthcare supply chain cost issues, the change has been slow in coming. Inefficient manual processes, dirty data, lack of visibility, and poor business intelligence continue to plague the supply chain.

The supply chain has traditionally been seen as a necessary but secondary function, primarily responsible for buying and delivering inventory. It's time to stop viewing supply chain management as a back-of-the-house function. Bringing the healthcare supply chain to the forefront can drive significant change in healthcare costs.

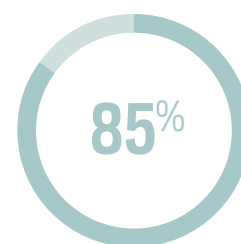


DRIVING COSTS OUT OF THE HEALTHCARE SUPPLY CHAIN

As healthcare organizations seek solutions to the challenges of healthcare reform, increasing demand and declining reimbursements, it's becoming clearer just how much impact the supply chain has. Just \$1 reduction in operating expenses can impact the healthcare supply chain as much as \$1,000 worth of new revenue.^{vii} With U.S. healthcare spending hitting \$3.1 trillion in 2014^{viii}, this is a compelling business case for transforming the healthcare supply chain.

A survey conducted by Cardinal Health^{ix} found that 85% of hospitals are either planning to or are currently working to implement solutions that reduce waste and cost in the supply chain.

The UPS study shows that the top three greatest opportunities for this are:



Percent of hospitals that are planning or currently working on reducing waste & cost

1

Optimizing transportation costs: Overpayment for transportation and shipping services is a common problem in healthcare supply chains. Consolidating shipments and using transportation companies who are optimized are effective ways to cut transportation costs.

2

Gaining better inventory visibility: Sixty percent of hospital C-suite executives reported unnecessary transportation fees because they didn't have the right products on hand when they were needed.ⁱⁱⁱ Processes and applications that enable healthcare organizations to track inventory, monitor and manage supply chain events, and view orders and shipments in real time can create more efficiency and drive down costs.

3

Consolidating the total number of transportation providers: Using fewer transportation providers gives healthcare organizations more control and leverage, improves efficiencies, and makes it easier to manage and track shipments.

The number one thing healthcare organizations can do right now to take huge strides toward transformational change is to consolidate vendors.

ENABLING TRANSFORMATIVE CHANGE BY CONSOLIDATING VENDORS

There are nearly 5,300 acute-care hospitals in the U.S., each of which has hundreds or even thousands of vendors.^x This complexity not only adds inefficiencies to the supply chain, but it leaves little leverage to negotiate cost and service.

Building better relationships with a chosen few vendors is an effective way to drive costs out of the healthcare supply chain. Supply chain managers should choose suppliers that they trust, and minimize the total number of vendors for the most cost management benefit.

There are six major benefits of consolidating vendors:

1

Working with a smaller list of vendors makes

companies more efficient: When organizations work with many suppliers who do the same things, redundancies add up and efficiency declines. Consolidating vendors helps solve this problem.

Fewer staff members are needed to manage vendors, and less time is spent searching for information in different systems. This enables healthcare organizations to repurpose staff to focus on more strategic initiatives. It also drives consistency in information management, and more uniform policies around data retention, archiving and disposal.

Working with fewer vendors also makes it easier to manage and track orders, and can even improve management of inventory levels. Considering that \$5 billion is wasted every year on expired, lost or wasted product,^{xi} this can have a huge impact on the healthcare organization's bottom line. Supply chain managers will have better control of overstocking and understocking, which will reduce instances of expired supplies and excess fees.



Hospitals lose about
\$5BILLION per year
on expired or wasted products

\$ = \$100,000,000

2

Easier to secure high quality products at lower prices:

Rather than purchasing similar items from many vendors, consolidating vendors increases organizations' purchasing power and allows them to get higher quality products at the best prices. Stronger relationships with fewer vendors incentivizes competition.

With the rise in the price of raw materials, healthcare organizations are feeling the burden of cost increases — but with a strong relationship with select vendors, supply chain managers have more power to influence how that burden gets distributed. Fewer vendors receive higher order volumes, which in turn incentivizes more reasonable pricing and better discount packages to keep the healthcare organization's business.

3

Improved quality of service: When healthcare organizations choose to work with fewer, more carefully selected vendors, the relationship grows to be based on mutual trust and cooperation. Forming alliances with best-in-class vendors creates strategic partnerships in which information is shared more easily and inventory production and management get streamlined. This information sharing is key to preempting costly overstocking and risky understocking.

Also, supply chain managers have closer relationships with their vendors when they consolidate, which only benefits both parties. When supply chain managers are able to tap into suppliers' unique knowledge, the healthcare organization can become an easier, less expensive customer to serve — which lowers vendors' selling, general and administrative costs, and in turn encourages vendors to share the savings.



4

Bill payment process becomes clearer, reducing soft costs and improving credit rating:

Working with fewer vendors also makes bill payment processes simpler and more efficient. This in turn reduces soft costs (such as order management, shipment tracking and invoice paying) and improves the organization's credit rating because there are fewer credit lines and less opportunity for credit issues. Fewer orders are placed, leading to fewer invoices to manage and less time waiting for payment approval.

5

Consolidating shipments cuts transportation costs:

The costs of getting supplies into the warehouse decrease with vendor consolidation as well. Fewer, more optimized shipments from the same suppliers lower the per-unit freight costs. Consolidated shipments also mean fewer shipments received, and more efficiencies when it comes time to unload and shelve products.

6

Pressure manufacturers and distributors to innovate their products and service models:

Healthcare organizations gain leverage when they consolidate vendors, and innovation becomes a differentiator when deciding which vendors to choose.

Vendors that respond with innovation to the changes in the healthcare industry become welcome partners. Those that bring original solutions help healthcare organizations provide better patient care and support the business strategy, and those that improve the quality of their products cost healthcare organizations less money and hassle in returns. Vendors that invest in solutions that enhance service help supply chains become more efficient and cost-effective.

As supply chain managers choose top-quality, highly innovative vendors to work with, the relationship becomes one of collaboration, and new solutions emerge. Vendors not chosen are forced to innovate to get in the running.

CHOOSING THE RIGHT VENDORS TO AVOID RISK & SEIZE THE BENEFITS OF CONSOLIDATION

It's clear that consolidating vendors gives healthcare supply chains leverage, lowers costs and creates efficiencies. The first step, however, is to choose the right vendors.

Evaluate and qualify existing vendors

Not all vendors are created equal. Some will quickly stand out when you begin looking through your vendor list. Cost is only one of the factors that matter when deciding which vendors to choose.

Consider the following when evaluating your existing list of vendors:

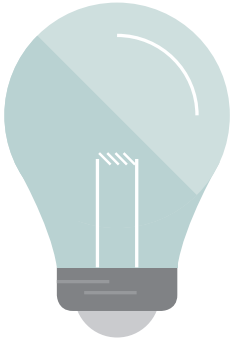
- Your existing relationship with them and their relationship with the entire supply chain organization — from warehousing to accounting.
- The efficiency and effectiveness of their processes, and if any of their processes clash with your organization's policies and procedures.
- Delivery performance, including ease of ordering, timeliness, packaging quality and shipping rates.
- The hard and soft costs of the relationship. Hard costs are expenses related to physical assets — e.g., inventory and equipment. Soft costs include expenses that aren't easily included on a company's balance sheet — e.g., approval time, writing checks, and redundancies in roles and responsibilities.

Select vendors that have shown dedication to servicing the account in the best manner possible

Supplies play a critical role in delivering patient care and in enabling healthcare organizations to operate more efficiently and cost-effectively. Vendors play a large part in this, and those chosen should support the greater strategic mission of the supply chain by making it their mission to provide the best service.

In other words, vendors with a track record of high-quality service should be shortlisted.





Select vendors who are already innovating

Healthcare organizations can tap into supplier innovation to support business strategy and streamline supply chain management. For example, vendors who provide tools that enable supply chains to gain inventory visibility and reduce costs are more likely to move the needle toward a more streamlined supply chain and become long-term strategic partners.

Supply chains benefit from innovative collaboration with vendors. New products and processes come from this trust-based relationship, and efficiencies are realized on both sides.

Office Depot's financial benchmarks reporting is a perfect example of vendor innovation that can impact healthcare supply chains. These reports allow healthcare organizations

to compare the Cost per Staffed Bed (CSB) and Cost per Full Time Employee (FTE) to identify inefficiencies across departments.

Most importantly, vendors should be viewed as partners — not adversaries — to ensure a positive relationship and secure the most cost savings. The efficiencies created by consolidating vendors not only help supply chains create transformative change within healthcare organizations, they help those organizations avoid the risks that overcomplicated systems/processes and disparate policies produce.

When part of an overall healthcare centralization strategy, consolidating vendors enables healthcare organizations to standardize policies, make processes and costs more consistent and repurpose staff to focus on more strategic initiatives.

Supply chains benefit from innovative collaboration with vendors ... Office Depot's financial benchmarks reporting is a perfect example of vendor innovation that can impact healthcare supply chains.

CONCLUSION

Pressuring vendors to lower their prices won't produce the supply chain improvement effects that building better relationships with vendors will. But no matter the skill level and efficiency of your supply chain, it's impossible to build great relationships with a long list of vendors.

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Consolidating vendors simplifies the supply chain, making transformative change much more possible. It will enable supply chain management to have a strategic role in strengthening the healthcare industry to provide the highest quality patient care and withstand the challenges ahead.



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