

Operations Practice

# How B2B online marketplaces could transform indirect procurement

Complex, indirect spend categories have resisted the trend toward online purchases. But new pressures—and offerings—are reshaping the future of indirect procurement.

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**For people who remember** when consumers first started using digital marketplaces, the realization that the oldest of those platforms are now almost 25 years old can come as a surprise. Even business-to-business platforms have been around for two decades, becoming an almost invisible engine of commerce at many small and medium-sized businesses.

But there's one arena that online marketplaces have yet to penetrate to nearly the same degree: large corporate procurement departments. Concerns about scale, quality, and reliability have made leaders hesitant to change their longstanding reliance on dealing directly with suppliers. This is especially true for the more complicated purchases that fall under the label "indirect spend": everything from IT and telecoms to transportation, professional services, and marketing.

That's starting to change. A new generation of procurement leaders, who have grown up buying online for increasingly complex personal needs, are beginning to wonder whether buying online also makes sense for business. Powerful digital and analytic tools are also contributing to the new mind-set, opening new avenues for procurement departments to generate value in areas outside their traditional focus on transaction management.

Indeed, indirect spending has become a tougher challenge for chief procurement officers (CPOs). Not only is this type of spending growing, but it is also encompassing a widening array of categories—in services as well as goods—as companies become more reliant on third-party providers. Controlling spending, compliance, and risk has become a bigger headache.

Much like online B2C marketplaces, their B2B counterparts offer access to a broad pool of potential vendors operating under a wide range of business models, including not only the obscure and potentially risky operators of the past, but also high-quality, prescreened vendors. And their value to buyers extends much further, to customization, dynamic pricing, and indirect-spend management and control—important factors even for sophisticated procurement

functions. Perhaps most important, they can free procurement teams from time-consuming, often repetitive, transactional work that fails to take full advantage of their more advanced capabilities. When part of a broader procurement system that includes such elements as shared services or digitized sourcing, marketplaces free up procurement teams to place more focus on value-adding activities, such as strategic purchase categories, innovation, and sustainability.

As a relatively new phenomenon, how marketplaces will evolve—and their impact and implications—remains to be seen. What purchasing executives need to understand now is their potential effect on the procurement function and the role of the CPO—and, more broadly, on the supply chain and spot markets. In this early stage, leaders may have fewer answers to guide them, but knowing which questions to ask can help better prepare them to capture maximum strategic advantage.

## **What do B2B marketplaces look like?**

B2B online marketplaces create self-service, digitally-sourced environments where multiple vendors can offer products or services to business customers. As with online B2C sites, B2B marketplaces claim to make it easier to identify the right supplier, improving the customer experience by making transactions simpler and more transparent.

Buyers gain choice, value, and greater efficiencies, while sellers, under pressure themselves to grow revenues, gain access to a broader pool of buyers—without the burden of marketing or (depending on the specific marketplace) the need for dedicated sales, fulfillment, transactional, or logistics functions. When implemented well, marketplace procurement can also facilitate reporting and data analysis.

Bearing in mind that category boundaries are not always sharp, we currently see four types of marketplace. Each is defined by the nature

of its wares and services, as well as by who holds contractual and warranty responsibility for them. For illustration, we include several company names that tend to come up repeatedly in discussions about the sector.

- **Product-focused marketplaces** often focus on commodities like office supplies, furniture and equipment, and packaging. Amazon Business and Alibaba are probably the best-known names, but the category also includes ThomasNet and GlobalSourcesDirect. A variant provides structured services with menu-type offerings, such as maintenance, repair, and operations (MRO) providers.
- **Time-and-materials marketplaces**, which typically offer freight services, travel services, IT and technology, temporary labor, and facilities management. Two well-known examples are SAP Fieldglass and Concur, the expense and travel-management site. Specialty players such as Excess Materials Exchange arguably also fall into this type.
- **Scope-of-work marketplaces** offer services such as marketing, telecoms, utilities, rent and real estate, insurance, and professional services (such as legal and consulting). Examples include Globality, which focuses on digital service-sourcing, and Field Engineer (FE), which sources telecom engineers and technicians.
- **Corporate-spinoff marketplaces**. The final category of marketplaces has evolved from formerly captive platforms that large companies developed for their own supply networks, and have grown to serve other companies as well. InnoCentive, spun off from Eli Lilly, is a prominent example.

## The implications of online B2B marketplaces

Online B2B marketplaces offer several general benefits to business. Notable are greater transparency in product, service, and supplier availability—as well as in pricing and purchasing

terms. Hours and time zones are irrelevant, making marketplaces truly global. And, perhaps most significantly, they provide CPOs with the means to offload the tactical, often repetitive work that dominates procurement (especially in indirect categories), improving their management so they can focus on more strategic activities.

On the other side of the coin, sellers also benefit from marketplaces, gaining access to new customers, visibility into the market's pricing structures, and features and services they might not have otherwise been able to afford, such as lower shipping costs and better marketing analytics. Ultimately, marketplaces promise broader economic impact, expanding opportunities for smaller vendors.

Let's take a closer look at the details of what online B2B marketplaces can potentially offer CPOs.

### Greater vendor choice, one-stop shopping.

Price transparency gives buyers greater awareness of supplier options, increasing competition among suppliers and creating opportunities for large purchasers to replicate (or even increase) the scale advantages that they have long negotiated through spot purchases via traditional channels. Accordingly, online marketplaces could enable purchasers to consolidate their vendor rosters. The global procurement manager of a major automotive original-equipment manufacturer (OEM) recently told us, "I'm glad our CPOs pushed the marketplace idea for indirect procurement. It has increased our competitiveness, both in unit prices and in our choice of suppliers—and it has expanded our knowledge of suppliers and markets. Our results have been so positive that the company is now considering scaling our program to include some of our direct-spend items."

### Faster and cheaper delivery.

As with B2C sites, online B2B marketplaces often provide faster throughput times, thanks to advanced IT and logistics capabilities. Their scale also enables them to offer highly competitive shipping rates, which may be better than those negotiated directly under existing contracts.

**Savings.**

Depending on their industry, companies typically spend 15–30 percent of revenue on indirect spending, so the opportunities for savings are high—especially for those industries with the highest ratios of indirect to total spend. Public-sector organizations are likely to be among the biggest winners: their spending is generally more fragmented than that of private sector companies, and their internal resources for procurement are often more limited.

**Integration into the source-to-pay process.**

For large enterprises, marketplaces' ability to plug into companies' entire source-to-pay (S2P) process is among their most powerful characteristics. By integrating with customers' third-party purchasing systems, marketplaces automate, digitize, and simplify sourcing. Integration can ensure that purchase orders are issued at the right price and in the correct quantities. It can also simplify negotiation and contract management—and streamline accounting, reporting, tracking, and control.

**Managing spending and compliance.**

Advanced-analytics capabilities can help companies control indirect spend more flexibly than longstanding tactics, such as allowing purchases only from a very narrow selection of catalogues. Additionally, transaction histories and dashboards with centralized data can be made accessible to those with procurement or budgetary responsibility. As a result, even if spending initially rises because of the lower friction that B2B marketplaces offer compared to their traditional counterparts, a more accessible and transparent paper trail makes it easier to retake control. Spending thresholds become easier to establish and reinforce, for example by adopting purchase cards for below-threshold purchases—eliminating purchase-order paperwork for procurement teams, while still allowing spending to be monitored. Finally, marketplaces can adapt the old limited-catalogue model, setting up “preferred” and “restricted” vendors and categories to aid customers in controlling indirect (and especially rogue) spend.

Sidebar

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**How marketplaces can solve the headaches associated with long-tail spend**

*Long-tail spending is inefficient and often hard to control.* On average, some 20 percent of indirect spend is allocated among 80 percent of the vendor list, creating significant inefficiencies for procurement departments. Marketplaces allow buyers to consolidate purchases under one roof. The greater visibility they offer enables companies to gain control over rogue spend, thus reducing risk and improving compliance.

*Long-tail products are hard to procure because of scant pricing or product information.* Marketplaces provide price transparency. This, along with product-detail pages, enables buyers to make more informed choices and to comparison shop without having to search all over the internet.

*Long-tail purchases can be time-consuming.* Marketplaces can ease the management of long-tail procurement—particularly for catalog-type purchases—by providing auto-replenishment.

*Long-tail purchases are largely (or completely) unmanaged—and more costly than they need be.* Long-tail purchases are typically not negotiated. Instead, people often buy the same products over and over at current market prices, without ever locking in a set price. The savings from marketplace buying can be substantial over time, especially considering the aggregate impact.

## Buyer beware

Buying online can be a risky proposition: the transaction is impersonal, and buyers cannot be certain they will get everything they ordered, or that the quality (especially for a first-time purchase) will meet their needs and expectations. In an automated environment, can procurement managers be sure they will get the same level of service they would get with a direct vendor relationship—in logistics, billing, credit policies, and refund and exchange policies? Global purchases come with additional risks in all of these areas. These are no small concerns; a single glitch can cause inconvenience at best, and at worst, impair the buyer's ability to deliver its product or service to customers.

B2B online marketplaces follow one of two accountability models. In the broker model, the marketplace connects buyers and vendors, but offers limited, if any, warranties or responsibility for the transaction as buyers transact and contract directly with vendors. In the single-vendor model, the marketplace contracts with the buyer to act as a single vendor and bears responsibility for delivering the products and services as promised. The marketplace holds agreements with all of its vendors, in effect acting as agent.

Generally speaking, e-catalogs follow the broker model, as do vendors of complex, more customized (or high-value) services, such as insurance and facilities maintenance. Scope-of-work marketplaces, which encompass professional services, generally follow the single-vendor model. In some cases—for example, where the vendor is only a distributor—the warranty may lie with the OEM. Or if the marketplace itself is the actual vendor of a given category, it is the guarantor.

## The features CPOs should seek

To attract buyers, marketplaces need to attract quality vendors. To do so, they need to promise a bigger customer base than vendors could otherwise secure on their own. Marketplaces must also provide a user experience that is above and beyond what buyers get from dealing with individual vendors. By “user experience,” we mean not simply the scale of offerings or the

range of amenities and features, but the total experience: how interactive it is; how much buyers enjoy shopping; how indispensable the marketplace becomes to them; and how valuable it is in helping them perform their work and accomplish their goals.

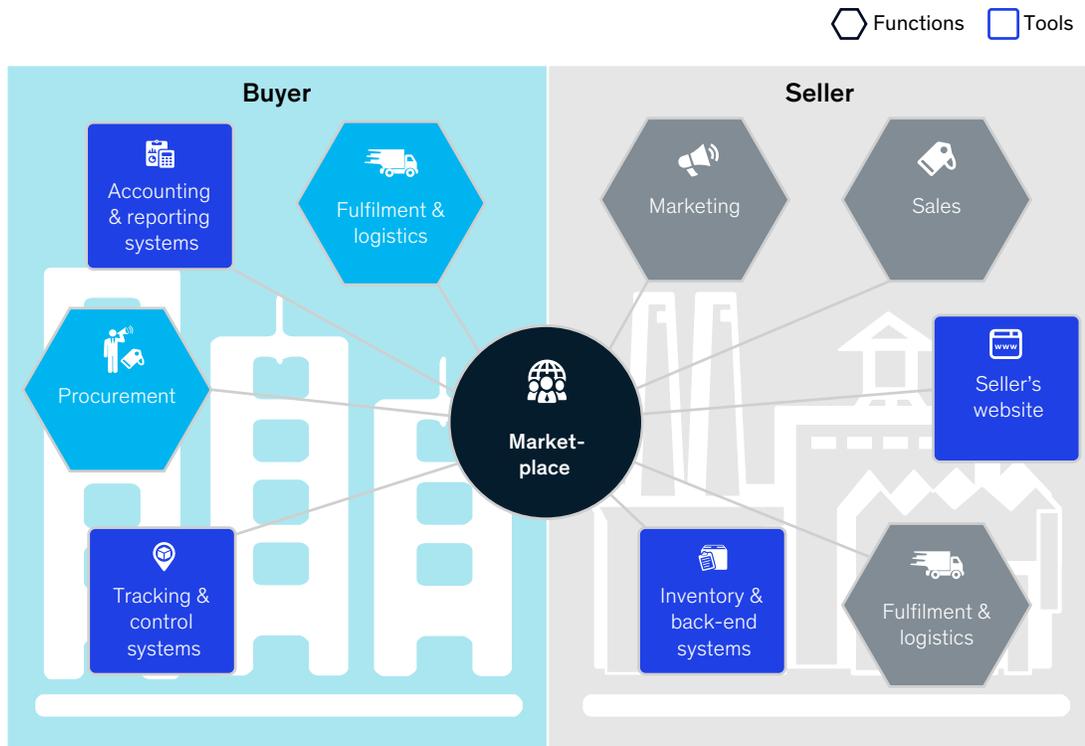
Which features are deemed most attractive will depend on the size of the buyer. For example, integration—the ability of the marketplace's customer-relationship-management system to tie into the customer's S2P system (linking ultimately to its ERP platform)—will be more attractive to large enterprises. For smaller buyers, integration means the ability to coordinate the seller's e-commerce site and back-end information with the buyer's fulfillment, logistics, and tracking. It can include owning the technology feed from the seller's warehouse in order to sync inventory and organize orders (Exhibit 1).

The remaining features, many of which benefit buyers and sellers equally, span the sourcing-to-procurement path.

- **Robust product and service offerings**, including detailed product information and technical specs that facilitate product comparison and purchasing.
- **Transparent and dynamic pricing** to help teams buy smarter and compare prices, so they can negotiate more effectively.
- **Ordering and fulfillment data**, including the customer's purchase history, shopping or wish lists, and other preferences is not only convenient for customers; it also gives vendors and the marketplace valuable data to help improve customer experience.
- **Financial services**, including financing for buyers, and insurance and tax-management services for sellers.
- **Payment options**, which include multiple forms of payment, open purchase orders, and stored account data, are especially important for e-catalog marketplaces.

Exhibit 1

## Integrating B2B marketplaces into procurement systems creates powerful benefits for buyers as well as sellers.



Giving customers a choice of currencies for payment ensures greater global reach.

- *High-quality logistics*, such as negotiated shipping rates that most vendors cannot match on their own. Cost-effective and speedy logistics with advanced tracking capabilities are a critical competitive feature, particularly in commodity categories.
- *Returns and refunds*, which marketplaces can process promptly, thanks to their fulfillment, payment, and logistics systems.

### The impact on CPOs and the procurement function

As demand grows, the breadth of product and service categories available on B2B marketplaces will expand dramatically, in turn making them more attractive to procurement teams. Over the next

three to five years, we expect a marked rise in the proportion of indirect purchases managed via marketplaces. In effect, indirect procurement will increasingly become platform management—a shift that will require teams to tailor their indirect-procurement strategies more carefully.

The resultant streamlining of many procurement activities and processes will likely have a profound impact on the role of the CPO and the procurement function. With less time spent vetting vendors, chasing down transactions, coping with paperwork, reining in rogue spend, and ensuring compliance, procurement teams will be able to devote more of their energies to higher-value work, such as researching new and better materials, and unearthing promising marketplaces (Exhibit 2).

As more services become available through online platforms, the procurement function will initially focus on three roles: finding marketplaces that

Exhibit 2

**A new way of working for the procurement team**



offer the required specialty services from high-quality providers; maintaining vendor relationships; and—perhaps most important of all—managing risk. For example, the rapid increase in tech spending by non-IT business units suggests that IT services might be an important category for marketplaces, particularly for controlling quality. Industry analysts project that by 2021, indirect spending will be led and directed by tech-procurement people at up to 60 percent of large enterprises.

Procurement leaders can further protect their organizations by following a comprehensive supplier-management approach, especially one that incorporates a range of standard and ad hoc performance indicators. That’s a substantial improvement over single-vendor models, and allows

buyers to explore new avenues for performance evaluation—such as designing simple user-feedback scores for each vendor or even each transaction.

Over time, procurement officers’ primary role of tough negotiator, rule enforcer, and smart sourcer will shift to that of “developer”; supporting marketplace creation by shaping the source of supply according to their company’s needs. This might include creating internal marketplaces that feature preapproved vendors, allowing local managers to access services without having to go through the requisition process each time.

Whether for products or services, procurement’s more strategic role might also include developing

digital road maps to optimize the S2P chain, or innovative collaborations with suppliers. CPOs will find more creative uses for and approaches to marketplaces as they continue to evolve; indeed, the dynamic among buyers, sellers, and marketplaces will fuel the evolution of each entity.

### **Will marketplaces really take off?**

For all their advantages, the unbridled growth of online B2B marketplaces is far from guaranteed. Product-focused marketplaces could have difficulty gaining a foothold. Large buyers may be less interested in expanding choices than in managing spend through their usual tactics. Or they may insist on having their own personalized catalog with special pricing. And while general pricing discounts could certainly be negotiable initially, the economics might be difficult for marketplaces and their vendors to maintain over time. Vendors with low margins may have little wiggle room to afford the cost of participation, although ultimately—and especially for commodity sellers—they may find few alternatives.

Large companies will be important to online marketplaces in achieving critical mass. Yet some companies might be reluctant to cast off longstanding relationships with suppliers and distributors, especially those that are able to match the capabilities of marketplaces while still offering substantial value. For sensitive, complex (non-commodity) purchases, such as for IT or professional services, CPOs might be wary of an automated and impersonal approach. In some purchase categories, such as travel, CPOs might be able to secure more competitive pricing and greater flexibility from agencies rather than platforms.

Finally, but not least, a simple, straightforward user experience is crucial. Some companies may be discouraged by the complexity of getting their existing sourcing applications to work with marketplace systems. Still, no company can, or should, put off a digitization effort for their procurement function. There are a number of steps they can take to move forward successfully and with minimum risk.

### **How will marketplaces evolve?**

Just as the growth of B2B marketplaces will reshape the procurement function and the role of the CPO, so, too, will procurement influence the evolution of marketplaces. We envision CPOs eventually partnering with the marketplace to find goods and services, forming buyers' consortia among peers, and even developing entire ecosystems with suppliers and peers that more effectively serve companies' needs (Exhibit 3).

How might these changes play out among the three archetypes?

For product-placed platforms, which deal primarily with commodity products, the field will likely tilt toward consolidation, with smaller players finding it increasingly difficult to compete against big entities. At the other end of the spectrum, scope-of-work marketplaces seem primed to succeed as niche providers that serve specialized markets like marketing and legal services, especially for more commoditized activities. Time-and-materials marketplaces will probably feature more competition.

Another likely scenario is the emergence of procurement-as-a-service. For smaller companies that lack a formal procurement function and procurement expertise, procurement-as-a-service would help offload the lion's share of procurement activities to a marketplace, thus saving money while improving results. Marketplaces would gain in multiple ways, including having access to the demand-planning needs of a whole new segment of buyers.

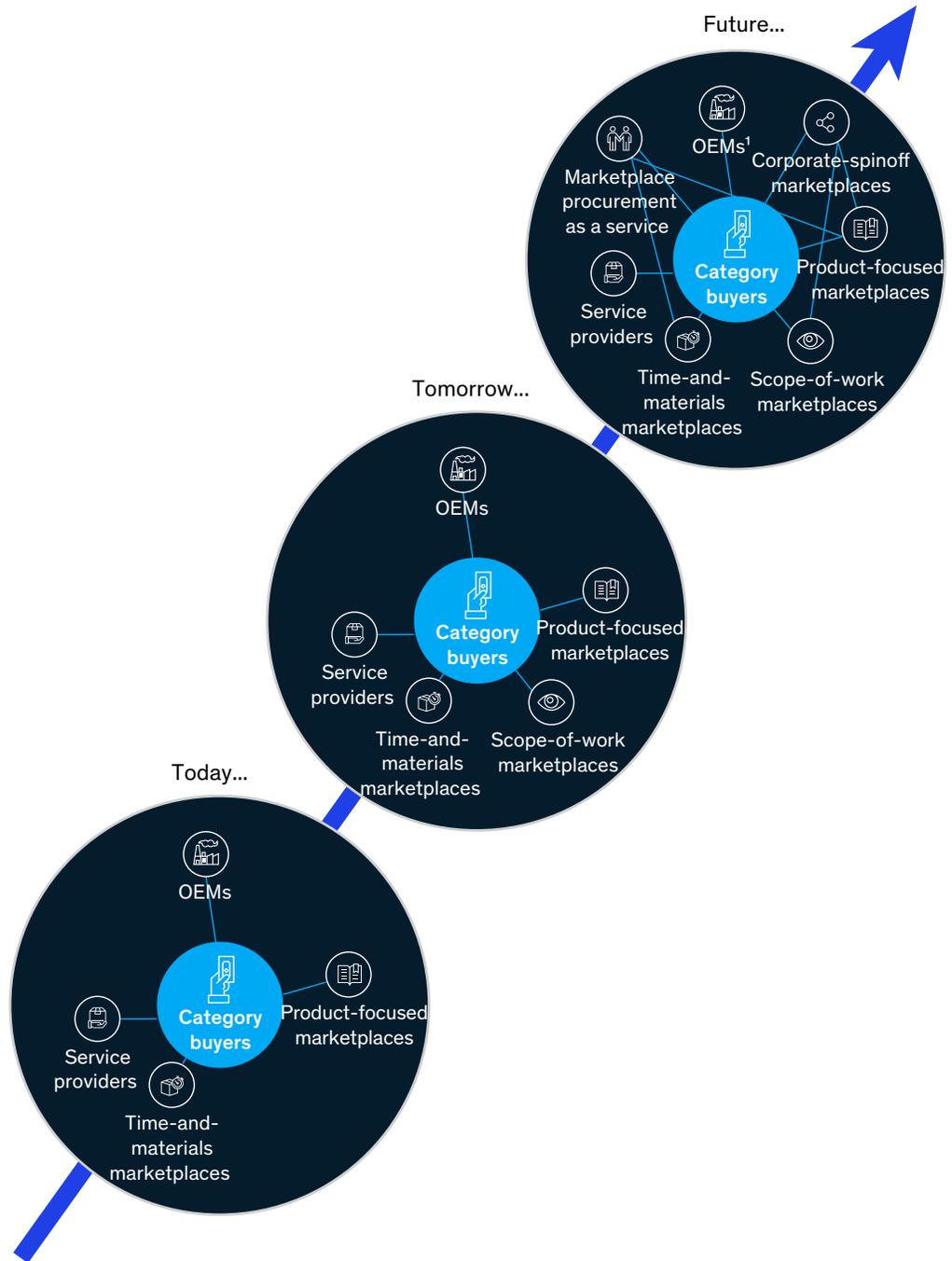
These dynamics can propel marketplaces forward, increasing competitiveness and enabling agility in the procurement organization as it delivers more value to the company.

### **Four things every CPO needs to consider**

B2B marketplaces are not just about going online. Positioning the organization to make the most of them will require a concerted effort. We've identified four important actions CPOs can take, not necessarily in order (and some in parallel):

Exhibit 3

**Indirect-spend ecosystems are likely to become more complex and interconnected.**



<sup>1</sup>Original-equipment manufacturers

***Assess your current indirect spend and processes.***

How mature is your procurement organization? How does your spend break down by category, and what percentage could potentially fall within the three B2B marketplace types? Identify the shortcomings or pain points in your current procurement effort. How might your near-term and longer-term procurement needs be served as the online marketplace landscape develops?

***Run small-scale pilots.*** Start by buying in those categories that you can readily monitor to measure impact. If possible, test all four archetypes to get a feel for how they work and how they compare to your traditional channels. Recognize that if a pilot doesn't immediately yield results (such as savings or an expanded supplier base), that doesn't necessarily mean marketplaces aren't right for your organization. Success will depend on many factors, including which categories you choose to buy via marketplaces, what resources you have in place to support the shift (more on that below), and how responsive individual marketplaces are to customer needs.

***Envision your next-generation procurement organization and the value it could potentially deliver.*** What kind of efficiency could you realize that could be redeployed in more value-generating activities? How much could the ability to source contingent labor via online marketplaces accelerate your speed-to-market or improve customer response times? Could you quantify the benefits of accelerating the flow of inbound goods and services on your organization's productivity? Consider the compounded savings and efficiencies of locking in prices across a broader range of categories on a yearly basis.

Each organization's strategy will depend to a great extent on the nature of its indirect spend—how commoditized it is, and how much value would be at stake if much of it were outsourced.

***Determine the resources you'll need.*** Is your current technology up to the task? If not, what will your organization need to do to get your technology systems and digital capabilities in order? What competencies will your procurement team need to manage marketplace procurement most effectively? And, what kind of talent will you need to perform the more strategic, value-adding work?

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At this stage, it's hard to foresee how far and how fast B2B online marketplaces will develop. As with many things digital, once there is a critical mass of users, the playing field can explode. The biggest payoff will come to those who approach this new channel not merely in terms of transactional convenience, but as a strategic opportunity.

CPOs who lay the groundwork now—by doing their homework, investigating new categories and new ways they can serve the organization's needs, and anticipating the systems and talent they'll need—will be ahead of the game. By elevating the role of the procurement function, they have the potential to not only capture savings and preserve resources, but to help their organization achieve competitive advantage in new ways—and even unleash new opportunities.

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