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E-Sourcing & E-Auctions in Procurement Operations: An Effective & Expedient Approach

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Abstract: ***Today's world is the world of high demand and supply. Where firms or organizations are seeking ways to fulfil those demands and productive & effective supply chain. Supply chain professional are thinking, analysing, executing and creating strategies about how to compete in a much more better way. This has further motivated many organizations to adopt efficient strategies in order to enhance cost efficiency, supply chain processes and finally efficient and productive results. Now, here new & recent concept came into picture called as E-Auctions & E-Sourcing. An E-Auction is a well-known e-Sourcing concept. E-Auctions work by putting a plunging pressure on the charges by introducing competition into the procurement process and determining the bidding winner - the firm to whom the contract is to be awarded In this paper we will introduce the benefits of E-Sourcing & E-Auctions and issues, challenges in the same area.***

Keywords: E-Sourcing, E-Auction, Sourcing, Auction

1. Introduction

E-Auctions were started to be used in early 90s. This popularity was the result of the focus on pricing and the insight of purchasing organisations and departments who are inviting many suppliers to bid competitively in an online auction would reduce the price. That is what their thought process was. Thus, the early e-Auctions were designed as 'open descending price-only events'.

However, instead of generating low costs the price-focus of e-Auctions alienated suppliers, especially in industries in which suppliers could be differentiated in terms of quality, reliability, delivery times etc. In addition, buyers often incurred considerably higher costs when dealing with an e-Auction winner. Quickly, companies realised that the price-only focus was limiting the potential for growth and the popularity of e-Auctions, and the industry moved away from the price-focused approach.

Auctions have been around for centuries. People with goods wanted an efficient way to sell those goods to people who wanted those goods. For many people, the memory of an auction involves a fast-tongued auctioneer belting out numbers to a loosely organized crowd. Historically, the highest level of technology used for an auction involved plugging a microphone into a wall.

Then someone realized that the Internet could be more than a paperless catalogue. The Internet could be used to expand the universe of potential buyers for any one item. It could be used by buyers to compare goods more efficiently and accurately. Anyone could enjoy an auction from a comfortable seat unencumbered by time or location.

The online auction proved to be a great application of technology for those wishing to sell products. Traditionally, the auction represented the seller and involved one seller to many buyers. Auctions helped drive up prices for the seller

But what about those people wishing to buy goods and services? Fortunately, technology worked equally well for buyers, especially buyers working on behalf of a professional organization. Now auctions could be used to represent the buyer and help drive prices down.

Over the years, various auction formats were devised and executed, including the most well-known format, the reverse auction. Rather than having one seller with many buyers, a reverse auction involved one buyer with many sellers. Sellers placed decreasing bids on a set of goods or services and followed the same set of rules.[1]

Depending upon the requirement and industry patterns e-auctions are fragmented into the below piece as –

Sealed Bid Auction - In a sealed bid reverse auction, sellers have a few days (and possibly weeks) to submit one best and final bid. Bidders never have any knowledge of what the other sellers are bidding. This is dramatically different from a standard reverse auction, where each bidder knows exactly how he compares to other bidders; they have a shorter time frame to place a quote, and can reduce their price as often as they want within the time limitations, unless the parameters stipulate that only a single, “best and final offer” be submitted.

Reserve Price Reverse Auction - In a reserve price reverse auction, the buyer establishes a “reserve price”, the maximum amount the buyer will pay for the good or service. It can also be called a “qualification price”. If the bidding does not reach the “reserve price”, the buyer is not obligated to award the business based on the results of the auction. Once the reserve price is met, the buyer is obligated to award the business to a participating supplier.

Forward Auction - With forward auctions, bids increase in value rather than decrease in value. There are situations where this type of auction format would be appropriate. An example would be when the Sourcing Team wants to sell or liquidate assets.

Fixed Price Auction - The buyer establishes a buyout price at which the buyer can simply buy the item being auctioned

and end the auction. Variations support a minimum bid that will be accepted and bidders will be prevented from going below this bid. The first bidder(s) to reach this bid win(s) the auction.

English Auction - English auctions are probably the most common type of auction format. Users bid the highest price they are willing to pay for an item and bidding activity stops when the auction duration is complete. The item is sold to the highest bidder at their bid price. Conversely, sellers bid the lowest price they are willing to sell an item for and bidding activity stops when the auction duration is complete. The item is bought from the lowest bidder at their bid price.

English auctions also allow the buyer/seller to specify a reserve price below which the item will not be sold.

Dutch Auction - The buyer solicits bids for a Lot consisting of multiple units of the same item. Each seller can bid on part of the Lot at a fixed price (per unit). When the auction is over, the buyer pays the highest successful bid price. For example, if a buyer wanted to buy 10 units, and buyer A offered to provide 5 units @ $75, buyer B offered to provide 3 units @ $80, buyer C offered to provide 6 units @ $90, and buyer D offered to provide all 10 units @ 95, then the buyer would buy 5 units from buyer A, 3 units from buyer B, and 2 units from buyer C at a cost of $90 each for a total of $900.

Yankee Auction - Similar to the Dutch auction, the buyer solicits bids for a Lot consisting of multiple units of the same item. Each seller can bid on part of the Lot at a fixed price (per unit). When the auction is over, the buyer takes the lowest priced bids, in ascending order, until a full Lot is reached. For example, if a buyer wanted to buy 10 units, and buyer A again offered to provide 5 units @ $75, buyer B offered to provide 3 units @ $80, buyer C offered to provide 6 units @ $90, and buyer D offered to provide all 10 units @ 95, then the buyer would buy 5 units from buyer A (at $375), 3 units from buyer B (at $240), and 2 units from buyer C (at $180) for a total cost of $795.

2. Gains / Benefits in E-Auctions

E-Auctions are increasingly common in the B2B world, with many organisations seeing this as an effective way to lower the costs of purchasing products.

Advantages for Buyers - An e-Auction provides, organizations, Firms, companies, procurement professionals with the most competitively prices for their preferred products, pitching in suppliers directly against one another to see who can offer the lowest prices whether through online portal or website. It also streamlines the procurement process and saves time, as each supplier is not required to submit a full proposal, whosoever is complaint or commercially adequate, will only be participating in e-auctions.

Advantages for Suppliers - Reverse auctions are generally open, enabling smaller or less well known businesses to compete in the e-Auction process. This can also allow suppliers to compete in new sectors. A winning bid can lead to more business, as most buyers will look to source their 'non-core' products from their existing supplier.

Market Transparency - An electronic reverse auction with multiple, qualified bidders can be used to flush out the true market price of the auctioned items. Furthermore, this information can be used as the basis for real-time benchmarks for future sourcing projects. Auctions spark healthy competition, which can help all participants understand the true market value and identify areas where they need improvement. A buyer benefits by knowing true – often lower – costs. Suppliers benefit by knowing the market rate so they can review their own business or pricing model.

Decreased Error Rate - Since the sellers enter their own bids, there is less chance of human error during bid transcription and importation into a common bid file. The ability to run preliminary price rounds and the ease of online editing all serve to help catch mistakes and clarify requirements before the auction commences.

Simplified Apples-to-Apples Comparisons - Since all the submitted bids are in a common format contained within a single tool, the buyer can more easily make an easy apples-to-apples comparison, even with Dutch, Yankee, or other reverse auction variants.

Increased Buying Reach - Unlike traditional auctions that limit a buyer to the suppliers who can converge to a common location and time, electronic reverse auctions give a buyer access to a global supply base, including suppliers in low cost countries.

Unifying Force for Process Improvement - An electronic auction is one of the cornerstones of an efficient, executable, strategic sourcing process. It enables Sourcing Teams to streamline purchasing processes by creating standard formats for purchasing across any spend category. Electronic reverse auctions simplify bid collection, bid comparison and centralize relevant data in a central location for easy query and display. This reduces cycle time, decreases the chance for human error, and provides a solid foundation for award analysis and optimization.

Auctions encourage high cost producers to increase their emphasis on the identification and elimination of process waste, an effort that sometimes leads to revolutionary improvements and significant cost reductions in the long term.

Cycle Time Reductions - Online auctions can be coordinated in a manner of days and conducted in an hour – shaving weeks from the traditional offline process. Furthermore, auctions force key players to focus and make decisions in a timely manner. They also accelerate awards, and this benefits all participants who want to grow sales faster.

More Time for High Value Activities - The drastic reduction in data collection efforts and cycle time leave more time for high value activities such as spend analysis, strategy selection, and award optimization.

Direct Cost Reductions - Successful reverse auctions immediately reduce the cost of acquisition (that would otherwise be paid) for each item successfully auctioned.

Benefits of online auctions – Suppliers - There are also benefits for suppliers who participate in online auctions. There are numerous success stories discussing how supplier organizations grew their business globally through their participation in online auctions.

Less time to complete - Since this process helps the buyers be more efficient, the suppliers will receive more information, receive it faster, and benefit from a quicker award decision.

3. Difficulties / Issues in E-Auctions

Disadvantages for buyers - The principal issue with an e-Auction is that it is usually based solely on price, and does not factor in other criteria like service levels, delivery or quality. Whilst these can be incorporated into the e-Auction process, price is the overall driving factor. The buyer may discover that the lowest bid is not the one with the highest quality products or does not meet the required standards of delivery or customer service.

The e-Auction usually centres on a 'core list' of essential everyday products, rather than focusing on the complete range of products that the buyer may source from the winning supplier throughout the contract. Overall the buyer may find that the costs of monitoring and managing the project outweigh the benefits.

Disadvantages for suppliers - Suppliers that are determined to win the reverse auction may place a bid that is too low for their business. As well as the cost of the product, suppliers need to factor in the cost of servicing the contract, from delivery to invoicing. Vendors may find that winning a bid could result in them making a loss on the contract.

Overall we can see that the e-Auction has pros and cons for both buyer and supplier. The e-Auction is a very effective way of optimising procurement, but it is based on price. Both parties must look at the overall costs of the contract to ensure it provides value too.

Stakeholder politics and policies - To be successful, all stakeholders should be committed to the auction process. Otherwise, an auction project may end prematurely and possibly lead to animosity among all parties. Be aware that many stakeholders have "emotional" attachments to incumbent suppliers and to informal or formal "partnership" agreements. Many stakeholders generally dislike e-Auctions, most likely due to misconceptions or previous failures. Additionally, no one likes to be labelled as callous and many people feel that auctions and head-to-head competition are mean-spirited, especially to long-standing suppliers who have delivered high quality goods and services over time.

Success Enabler: Stakeholder education and participation - In order to get all stakeholders to participate and accept the auction, the Sourcing Team may need to spend time educating the stakeholder community on how e-Auctions improve organizational efficiency and cost-effectiveness as well as individual job responsibilities. Additionally, they should be kept informed throughout the entire process so they do not feel things are happening without their knowledge. It is also important to insist on all communication happening through one centralized location (such as an online forum) to ensure "preferred" vendors are not privy to information other did not receive. This also assists in removing some of the challenges around "emotional attachments" to incumbent suppliers.

Internal Barrier: Hidden Costs - The supply and utilization dynamics must be well understood before an item is put up to bid on an auction. If there would be a significant cost for switching suppliers, or if utilization costs vary across the supply base due to differences in quality, then these costs must be considered before an item is put up for bid. Also, a commitment to supplier diversification or minority suppliers might add cost above and beyond the lowest cost award without these commitments and these costs also need to be understood.

Success Enabler: Uncover true costs - The key to getting past this barrier is active stakeholder participation to understand the true costs of using current or new suppliers and senior management commitments to diversification or minority suppliers and other commitments that might increase cost. Many organizations conduct internal RFIs to root out key issues and costs. Some companies go directly to the incumbent supplier because the supplier has the current specifications, prices and volumes.

Internal Barriers: Technology - Online reverse auctions use sophisticated software platforms that utilize the convenience of the World Wide Web. Though these platforms are stable and have been thoroughly tested, there is always a chance that during the event the platform could fail, access to the Internet is disrupted causing one or more suppliers to lose connectivity or the suppliers' own computers could fail.

Success Enabler: Redundancy plans - To minimize the potential adverse effects resulting from disrupted systems, choose a platform that is capable of detecting if supplier(s) lose connectivity. If all suppliers lose connectivity, make sure there is a backup plan. Additionally, build in redundancy for accepting supplier bids via proxy bidding processes. A proxy bidding process should be developed in advance and proxy bidders trained and on call. Many e-Sourcing vendors can also provide this service.

4. Conclusion

As compared to the Traditional negotiation, e-sourcing is a much better approach in terms of documentation, project management, and evaluation, tracking data, timelines and delivery. On the same side it has been observed that e-sourcing has certain issues as well but those issues can be addressed. And on the same side issues are specifically pertaining to industries and their process.

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