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## **Markets & supply chains**

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# Markets & supply chains

## 1. Introduction

There is much talk amongst trade economists of value chains, supply chains and market structure. Market structure refers to a market overall and you will hear terms such as monopoly (where there is only one supplier or where the market share of the main supplier is above, say, 80 per cent), duopoly, (where there are only two suppliers), oligopoly (where the top four suppliers between them control at least 80 per cent of the market), imperfect competition, and oligopsony (where there are a small number of buyers) and monopsony (where there is effectively only one buyer). Each of these has different implications for competitive behaviour but it is likely that you will be working in a sector where there is much freer competition.

When Henry Ford revolutionised the way that cars were made, introducing the first moving assembly lines, and manufacturing all the parts that went into the car, the company built a factory in the Amazon rain forest, planning to grow rubber trees and make tyres<sup>1</sup>. But that venture failed. As businesses have aimed to drive down costs, they have tended to specialise more, and thus might make as few as one component that will ultimately be assembled into a car. A consequence is that many businesses will find themselves as part of a supply chain, in which they are either buying components from other businesses or selling components to other businesses.

A supply chain is a system of organisations, people, activities, information and resources involved in supplying a product or service to a consumer. Supply chain activities involve the transformation of natural resources, raw materials, and components into a finished product that is delivered to the end customer. This is different to a value chain though closely related, which describes the range of activities that takes a product from conception to end use and possibly final disposal, focusing on the value added at each stage.

## 2. Supply chains

It may help you in your marketing and, indeed, in your market research if you understand the supply chain in which your business is situated. Even if you are selling directly to end users, it is more than likely that you are in a supply chain since you are buying in the raw materials or components to make the product that you are selling. You are thus competing to buy your raw materials at a cost that is low enough to be able to sell your final product at a

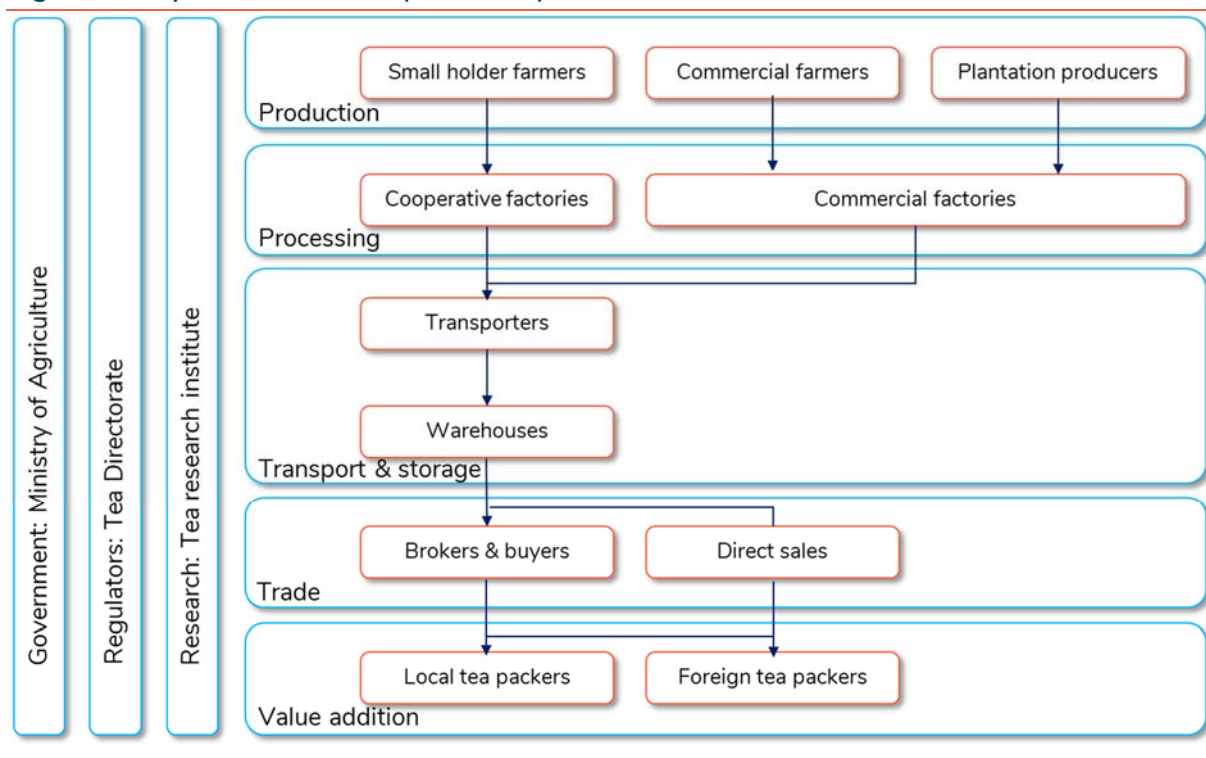
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<sup>1</sup> Economist (2021) Why Ford is leaving Brazil (16 Jan)

competitive price. Figure 1 shows a very simplified supply chain for the tea sector. As it happens, this is based on an example from Kenya, but it is very similar to the tea sector in countries such as India.

Farmers, whether subsistence or commercial, grow tea. Already you can see that key links have been omitted in that the farmers may need to buy seed and will almost certainly buy in fertiliser and pesticide. The tea is harvested and then sent to factories for processing, which may require bringing in extra labour to do the harvesting and transport firms may be needed to take the tea leaves to the factory. After that initial processing, the tea is transported and stored until it is sold, via brokers, or the tea auction or direct to buyers. It may well then be transported again, perhaps to a foreign destination, and then more value is added through packing into small quantities for sale to consumers. As well as the key steps set out in the figure, many of the businesses will additionally be buying in supplies or consumables including electric power, packaging materials, marketing services, advertising services, etc. The whole market is likely to be impacted by legislation and regulation and, in some markets, a levy to fund sector wide research.

**Figure 1: Simplified value chain (Tea sector)**



Academics undertake much research to understand supply chains; governments all want to improve the efficiency of supply chains. We do not need to worry about any of that. All that is necessary is that you understand where you fit in your own supply chain and consider the implications for your business. If the cost of your material rises, what impact will that have on the price that you need to charge your customers? What about rises in cost in other goods and consumables? If there is suddenly a shortage of paper, say, or another peripheral

but important item, what impact will that have on your business? How closely do you work with the immediate link in the chain behind or ahead of you, say, to improve the design, or reduce the cost, or improve the quality?

But, perhaps most important of all, understanding the supply chain can help you think about where you currently fit and where you might fit in the future. Is there scope, for example, to jump a link in the chain? Can you buy materials from further back in the chain? Or, if you are supplying businesses, can you add more value yourself and sell further forward along the chain? Will that improve your profitability? Indeed, one of the big changes brought about by the internet is the increased ability of customers and suppliers to find each other without having to work through intermediaries.

Here are some questions to consider about your market, your supply chain and the impact of the external environment on both:

- What is the nature and scale of the demand? (How many buyers are there in the market place? What is their concentration? What volume or value do they purchase? How do they undertake their procurement? Is there a desire for individual project contracts or for longer term supply arrangements? Does this present opportunities to enter a market?) See PROFIT factsheet on *Researching the market* for more detail on how to answer these questions.
- What is the distribution of power among your rivals? (How many sellers are there in the market place? What is their concentration? How important is price? Is there scope for differentiation through better quality?) See PROFIT factsheet on *Considering market forces* for more detail on how to answer these questions.
- Are there barriers to entry or exit into the market? (Are you susceptible to competition from new entrants? What is the scope to innovate? Will that help you to position yourself as better than the competition?)
- Have you considered how government rules and regulations impact the market? (Can you use these to your advantage?)
- Do you have good relationships with suppliers and customers? (Is there scope to do something on a small scale as way of developing new relationships that might lead to more business in due course? Does your offer allow other businesses in the supply chain to see themselves fulfilling a different role?) See PROFIT factsheet on *Market entry options*.



### Next steps

Think through the following questions to explore opportunities that may arise out of your position in the supply chain: Where do you fit in your supply chain? Can you exploit your position to advantage, especially if you are to trade with another country? Is there scope for disintermediation? Is there scope to offer more specialist products to a narrower range of customers? Or less specialist products to a wider range of customers?

### 3. Conclusion

It is not essential to understand where you fit into a supply chain, especially if your customers are consumers, but it will help if you do understand, and will be especially helpful if you are selling to business customers and those customers will be adding further value before selling on whatever they have bought from you. If you are selling services, then being clear about how the service supports those in a particular supply chain may help you win more customers in the same segment of the market.

### 4. Further information

New, S (2010) The transparent supply chain, *Harvard Business Review* (Oct)

PROFIT factsheets:

- Researching the market
- Considering market forces
- Market entry options

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