Logistics Prescription

Merck, UPS distribution contract underscores pharmaceutical industry's logistics needs

UPS landed a significant catch in health care logistics when pharmaceutical giant Merck decided to let the consolidator handle the bulk of its U.S. distribution business.

Drug manufacturers and health product shippers are taking a new look at outsourcing supply chain management, as fierce economic pressures from competition, fuel and transportation price shocks and increased regulation force them to entrust their jealously guarded logistics operations to cost-cutting third-party experts.

UPS has been in the forefront of service providers amassing the equipment, distribution networks and experienced personnel necessary to meet the precise service requirements of health care shippers.

"It has been a gradual education," said Bill Hook, vice president of global strategy for health care logistics at UPS. Many pharmaceutical shippers are wary of third-party logistics providers' ability to comply consistently with government regulations and meet stringent service levels upon which customers' lives may depend. "We kind of built this capacity as part of our strategy but it was not well understood," Hook said.

Merck understands. "UPS offers the healthcare logistics expertise — in shipping, warehousing, order fulfillment and storage — and an existing health care distribution network needed to effectively and efficiently distribute Merck's pharmaceuticals and vaccines in the United States," said Kyra Lindemann, a company spokesperson.

The Merck contract with UPS transfers the lease on two of the drug company's U.S. distribution centers in Atlanta and Reno, Nev., to the package company's Supply Chain Solutions division. "We wanted to focus our attention on where we could get the biggest impact for (Merck)," Hook said, noting that at least 80 percent of Merck's U.S. drug distribution moves through those two facilities.

"Merck previously handled distribution in-house from dedicated warehouses working with a number of transportation service providers," said Lindemann. "The agreement with UPS is part of the company's efforts to reduce costs and focus resources on core drug discovery and development activities."

UPS also persuaded the drug manufacturer to integrate its U.S. distribution with the logistics provider's multi-client warehousing strategy, another leap for health care clients concerned about keeping their often-perishable products segregated and secure from competitors' prying eyes.

"We were quickly able to satisfy them that not only do they get individual attention but that we will meet their standards of control and service," Hook said.

The Merck contract can be seen as vindication of UPS's five-year-old strategy for penetrating the lucrative but reluctant pharmaceutical market. Health care and drug shippers are recognizing a new maturity and hard-won experience among logistics providers who have long sought to win the industry's trust, Hook said.

For UPS the process began in 2004, when the Atlanta-based consolidator started investing in the temperature-controlled warehousing and track and trace technologies, as well as recruiting the skilled labor needed to meet drug company standards.

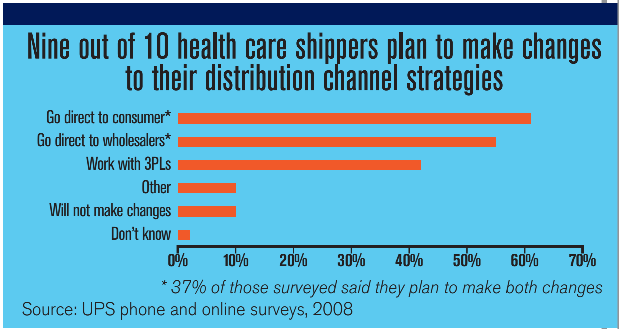
UPS built a 500,000-square foot health care products facility in Louisville, Ky., capable of handling overnight deliveries, and after filling that distribution center, started construction on another nearby.

"The first turning point (to UPS's health care expansion strategy) was when we filled that 500,000-square foot facility at the end of the runway in Louisville," Hook said. "When we bring people through that facility there is always an 'a-ha!' moment at the end."

Today, UPS has a health care compliance team of more than 70 people, a network of 23 U.S. distribution facilities, as well as operations in Canada, and 150,000 square feet in Puerto Rico and 200,000 square feet in the Netherlands set to open this April.

With the Merck warehouses, UPS will operate more than 3.5 million square feet of health care distribution space worldwide.

The market for such facilities and related services is only expected to grow.



Between 26 percent and 54 percent of health care industry executives called themselves very or extremely concerned about their access to growing world markets for their products, according to surveys UPS conducted in 2008.

Multiple incompatible IT systems; myriad government regulations; and varied social and cultural norms across borders have convinced a growing number of these executives of the need for better control of their supply chains.

The UPS surveys indicated health care logistics executives are getting ready to put their money where their products are. Three-fifths of those polled said they expect supply chain spending at their companies to increase in the coming year; the average increase was projected to be 23 percent.

"This is symbolic of a change that is taking place in the industry," Hook said. Like everyone else in this turbulent economy, he said, health care shippers will be looking to cut costs and outsource non-core functions to economize.

BY WILLIAM HOFFMAN