38th Board Meeting

2017-2022 Strategic KPI Framework: KPI 12b Performance Target for 2018

For Board Decision

GF/B38/ER13B

The Global Fund

Executive Summary

Context of Key Performance Indicator target proposal

- 2017-2022 Strategic Key Performance Indicator (KPI) Framework was approved by the Board in June 2016 (GF/B35/EDP05)
- KPI targets, as well as interim indicator definitions for KPI 5 and 9c, were approved by the Board in March 2017 (GF/B36/EDP09)
- Target for KPI 12b ‘affordability of health technologies’ is to be set annually
- In November 2017, the Board approved the 2018 performance target for KPI 12b, USD 50 million, and noted that a review of this target was planned for Q1 2018 (GF/B38/DP08)

Proposal for Board Decision

- Based on improved demand visibility and additional analysis of freight & logistics costs, a revised 2018 target for KPI 12b of **USD 122 million** is recommended by the AFC

Board-Approved KPI Definition

KPI 12b Availability of affordable health technologies: b) Affordability

Strategic Vision

Market shaping efforts reduce prices for PRs accessing PPM framework agreements, yielding savings which can be used to support unfunded programmatic needs

Aim of indicator

Measures the Secretariat's effectiveness in increasing the affordability of key medicines and technologies through strategic sourcing.

Reflects achievement of target savings based on tenders conducted and forecast demand, capturing price developments in the market, or mitigating price increases in an environment of rising prices.

Measure

Annual savings achieved through PPM* on a defined set of key products (mature and new)

* Savings achieved via product price reductions; PSA fees; freight /logistics costs, etc.

Limitations & mitigation actions

- ❑ The measure does not capture affordability of products in countries that do not access PPM framework agreements
- ✓ KPIs measuring RSSH achievements will provide information for these countries
- ❑ If considered alone, the indicator could lead to negative incentives for product availability - driving reduced supplier base and reduced investment
- ✓ KPI 12a will be used to control for potential negative effects on availability

KPI 12b Savings calculation methodology

Objective: Aims to measure the cost effectiveness of the strategic sourcing approach

Simplified Methodology*

SAVINGS = (*BASELINE PRICE* – *ACTUAL PRICE*) x *ACTUAL VOLUME*

BASELINE PRICE

Baseline can be set in 3 possible ways depending on the situation, for example:

1. **Default:** Weighted average price (WAP) actually paid during the course of previous contract or defined period (Baseline 1); Utilize previous contract period, unless there has been extension >= 1 year, then use the most recent period average
2. **New product:** Based on the Announced lowest Market Entry Prices (MEP) from vendors (Baseline 2)
3. **Environment of rising prices:** The increased price proposed by a current vendor when establishing a new contract (Cost Avoidance)

* Procurement cost savings are calculated in line with the “Guidelines for sourcing and procurement Savings Reporting” [Included in Annex]

KPI 12b Savings calculation methodology

Simplified Methodology

SAVINGS = (*BASELINE PRICE* – *ACTUAL PRICE*) x *ACTUAL VOLUME*

SAVINGS	BASELINE PRICE	ACTUAL PRICE	ACTUAL VOLUME
Summed up for all products where a baseline price is available (i.e. “comparable products”)	Three options: 1. Weighted average price 2. Market entry price 3. Cost avoidance price	Actual unit price paid for PPM procurements in the performance period	Actual number of packs purchased of the product during the performance period (PO confirmed)

Examples:

- PSA fees, for a given product category

Savings USD 0.28 million = (*PSA fee 2016 4%* – *PSA fee 2017 2.5%*) x *2017 product cost USD 18.8 million*

- Product, for LLIN procured for Tanzania in 2017

Savings USD 3.8 million = (*WAP previous tender period (2014-2015) $3.11* – *Actual Price $2.40*) x *Order quantity 5.3 million nets*

KPI 12b Savings target setting methodology

Simplified Methodology

SAVINGS = (BASELINE PRICE – ACTUAL PRICE) x ACTUAL VOLUME

Target Setting: *The same methodology is used, but with anticipated prices and volumes*

TARGET SAVINGS = (BASELINE PRICE – ***TARGET*** PRICE) x ***PROJECTED*** VOLUME

In following slides, provide disaggregated savings targets, but for proprietary reasons cannot share Target Price or Volumes

For 2018, **weighted average prices** are used to set savings target; baselines depend on the tender cycle

Target price is based on current reference prices and the Secretariat's current estimates of the market situation

Projected volumes come from the aggregated volumes within signed grants

TARGET SAVINGS = (BASELINE PRICE − TARGET PRICE) x PROJECTED VOLUME

KPI 12b Savings target setting methodology

BASELINE PRICE	Dependent on the tender cycle; All core products (ANTMs, ARVs, LLINs) will begin a new cycle in 2018, thus resetting the baseline prices

Details of baseline prices that will be used for 2018 savings target & result calculations

Category	Baseline price 2017	Baseline price 2018
ARV	WAP 2013.07-2014.06	H1 (Q1 & Q2): WAP 2013.07-2014.06 H2 (Q3 & Q4): WAP 2015.01-2018.06
ANTM	WAP 2014.07-2016.12	WAP 2017
LLIN	WAP 2014.01-2015.12	WAP 2016-2017
RDT	WAP 2016	WAP 2017
Non-core products	WAP 2016	WAP 2017
Freight	WAP 2016	WAP 2017
PSA fees	2016 fee %	2017 fee %

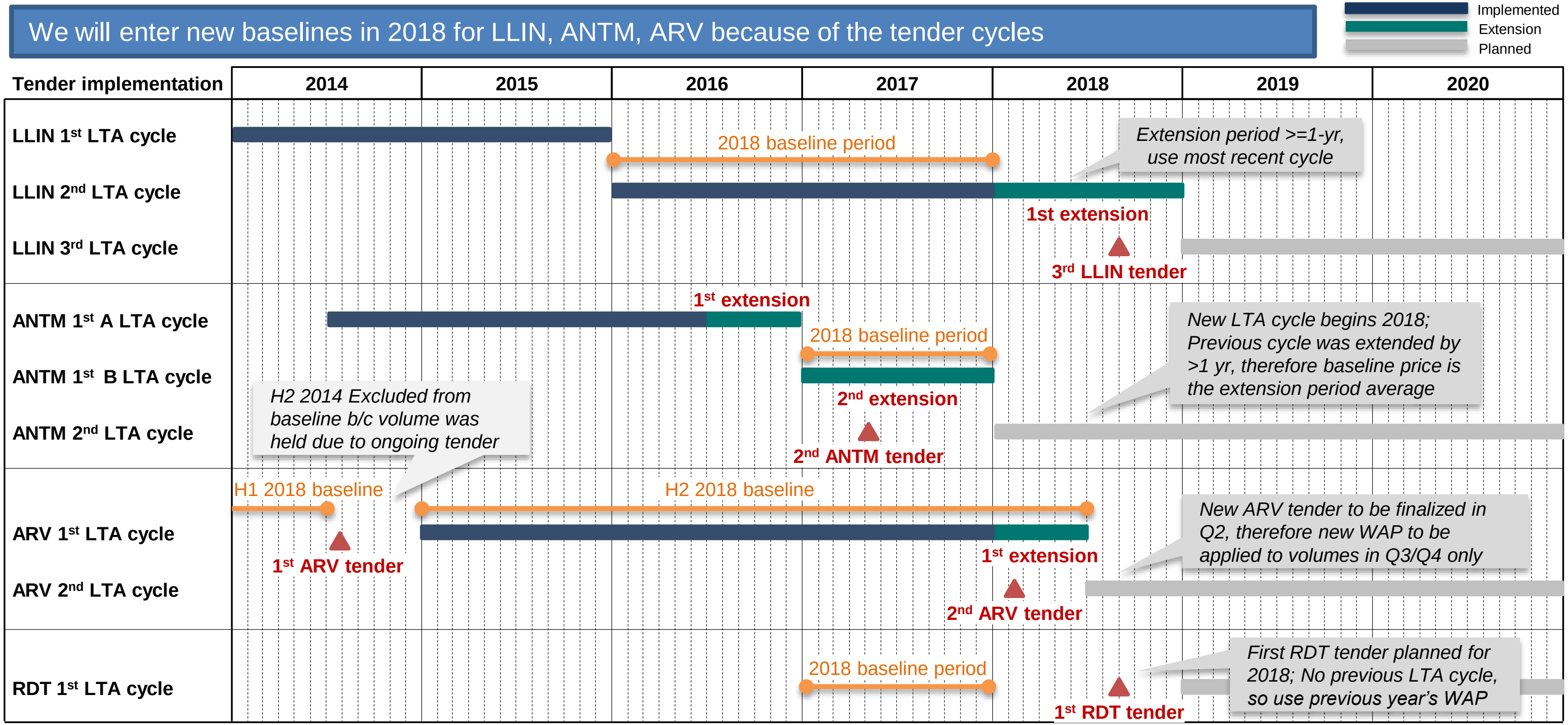
Details of tender cycles included in following slide

TARGET SAVINGS = (BASELINE PRICE – TARGET PRICE) x PROJECTED VOLUME

BASELINE PRICE

Weighted average prices used for comparison purposes are reliant on the tender cycle

We will enter new baselines in 2018 for LLIN, ANTM, ARV because of the tender cycles



TARGET SAVINGS = (BASELINE PRICE − TARGET PRICE) x PROJECTED VOLUME

Proposed 2018 target

Current target	USD 50m
Proposed target	**USD 122m**

Based on improved demand visibility and clearer timelines for the ARV tender, an updated 2018 savings target of **USD 122 million** is recommended by the AFC

Detail of proposed target

Category	Target Savings USD (millions)	Price assumptions
ARV	106	Majority of savings achieved in H1 2018 while still using WAP 2013.07-2014.06. Since H1 2018 is the first 6 month extension of ARV 2015-2017 implementation, the same baseline as 2017 will be applied. Price projections based on current reference price and trend.
ANTM	6	Implementation of ANTM procurement strategy (2017)
LLIN	8	Theoretical WAP price for 2018 based on the annual performance review
RDT	0	Procurement strategy will be launched in 2018, it is not appropriate to preempt the tender result
Non-core	0	a. Procurement strategy for all non-core products will be incorporated into the upcoming PSA strategy. Not possible to make savings price projections in advance of tender. b. Freight & logistics strategy also to be aligned to PSA strategy, however there are saving opportunities to be further identified through the annual review with PSA.
Freight	2	
PSA fees	0	
Total	***122m***	

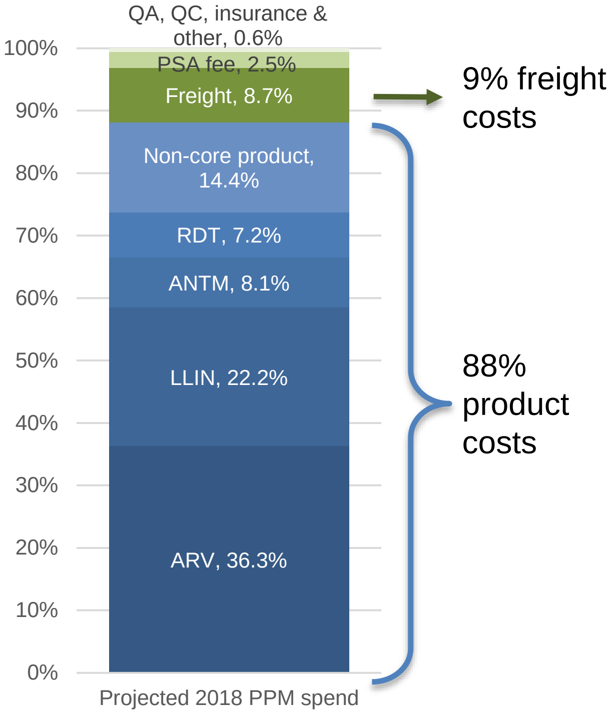
Proposed 2018 target

FAQ: New dolutegravir-containing first-line ART regimen (TLD)

- Antiretroviral medicines have been the main driver for cost savings in the past two years, with the price of 1st line regimens decreasing 42% since 2014. USD 144 million in savings from ARVs was achieved in 2017.
- TLD is being introduced as a more robust regimen than the current preferred Efavirenz based version
- The volume guarantee price of USD 75 per person per year (USD 6.25 per pack) negotiated by CHAI with two manufacturers is due to come into force in April 2018
- The PPM reference price at the end 2017 for both TLE and TLD was already at USD 6.25, so we do not anticipate any financing or procurement barriers to uptake of the new regimen. Product uptake will therefore be dependent on country transition plans, including readiness in terms of registration of new product and utilization of existing stocks
- Indicative future pricing will be confirmed in Q3 2018 after completion of the Global Fund ARV tender

Proposed 2018 target

FAQ: Freight & logistic savings



- Freight & logistics account for 9% of projected 2018 PPM spend with the health products accounting for 88%
- Freight & logistics costs are closely tied to fuel costs and the global economic cycle; if the global economy is stable, projection of freight costs is possible
- In 2018, we expect up to USD 2 million in savings from PFSCM as it continues to implement its long-term agreements under its 'multiple freight forwarder strategy'
- 82% of 2017 shipments (for ARV, ANTM, RDT & IRS) were sea and/or ground freighted. Of the 18% air freighted, analysis indicates that 46% of these shipments were due to ordering patterns & late orders. The Secretariat is actively working to improve demand forecast accuracy to minimize the unnecessary use of air freight
- IDA is currently excluded from freight savings analysis as 73% of their volumes are bed nets which are all sea freighted; and the 3-yr bed-net cycle and spot tender approach based on a wide range of delivery destinations makes the total freight cost difficult to compare
- Future Freight & Logistic strategy will be incorporated into the overall PSA strategy which will be launched in 2018, with full implementation 2019 onward

Key challenges looking forward into 2018/19

- **Unknown demand and late submission of orders**: Unknown demand creates missed opportunities for leveraging volumes that could otherwise result in lower pricing and savings. Late orders from PRs as a result of poor planning or shifts between donor funding sources contribute to increased reliance on suppliers with short lead times, irrespective of price considerations, combined with potentially higher costs in freight (air freight). Opportunities to place advance orders are constrained by country-customized labelling requests for a substantive proportion of the volumes procured.
- **Decline in ACT volumes**: Demand for the Private Sector Co-payment Mechanism for ACTs (CPM) has been declining over time and in 2018 will be only one fifth of the 2017 level. This decrease has largely not been transferred to public sector channels funded by the Global Fund and greater volumes may be needed to sustain sufficient procurement leverage.
- **Transition to new dolutegravir-containing ART regimens**: Unforeseen rapid transition of multiple countries with too short notice and inadequate supply security may result in supply-side constraints.
- **Harmonization of specifications**: Non-standard specifications contribute to missed opportunities for efficiencies and product spend would also be classified as “non-comparable” and thus excluded from savings calculations if the same product specifications were not purchased in the baseline period (167 million product spend was excluded in 2017 savings calculation as non-comparable).
- **Non-core products**: Negative savings are reported on a wide range of non-core products linked to low visibility on demand, low volumes and spend, and fragmented markets.

ANNEX: KPI 12b - Guidelines for sourcing and procurement Savings Reporting

Version 1.0

Key principles

Objectives

It is the objective of these guidelines to lay out roles and responsibilities, definitions and key processes of the sourcing and procurement department savings reporting.

Governance

The Sourcing and Procurement department is the owner of these guidelines while Strategic Controlling team acts as the custodian.

Change requests should be forwarded to Strategic Controlling Team for alignment. Where all participants are in favor of the changes, the updated guideline is then presented by Strategic Controlling Team to the Management Executive Committee for final approval.

Definition of Procurement Savings

A **cost saving** is defined as a **reduction** against a **baseline** resulting in a **potential spend reduction.**

The following baselines qualify for productivity savings and be used in most appropriate situation:

- Baseline 1 – Weighted average price (WAP) during the course of previous contract or defined period.
- Baseline 2 – Announced lowest Market Entry Price (MEP) for single or multiple vendors
- Cost Avoidance Baseline - The reduction or elimination of a price increase with the current vendor during the course of new contract

In order for a baseline to be valid, all of the following pre-conditions must be met:

- Cost savings realized are as a result of Procurement's pro-active contribution
- The baseline was validated by strategic controlling team according agreed methodology

Baseline 1

Baseline 1 Unit Price – Weighted Average Price (WAP) during the term of framework contract or defined period.

The basic calculation is:

$$\text{(Baseline 1 Unit Price - Unit Price}_{\text{Current Year}}\text{) x Volume}_{\text{PO confirmed in Current Year}}$$

Note:

1. **Weighted average price (WAP)** can be amended aiming to align the product specification in order to capture the procurement impact.
2. If there is no existing long term agreement in place, we can calculate the **Weighted Average Price (WAP)** base on transactional data in the **defined period,** the period should not be short than 12months.

Future year forecasted saving calculation is:

$$Total\ Forecasted\ saving = \sum_{n=1}^{\infty}\left(\text{Baseline 1 Unit Price} - \text{Forecasted WAP Year}_n\right) * \text{Expected Volume of Year}_n\Big)$$

Baseline 2

Baseline 2 Unit Price – Announced lowest Market Entry Price (MEP)

<u>The basic calculation is:</u>

Single Vendor:

$$(\text{Announced lowest MEP by acceptable vendor} - \text{Final Contract Price}) * \text{Volume}_{\text{PO confirmed in Current Year}}$$

Multiple Vendors:

$$(\text{WAP of announced MEP by acceptable vendors} - \text{Final WAP}) * \text{Volume}_{\text{PO confirmed in Current Year}}$$

<u>Forecasted saving calculation is:</u>

$$Total\ Forecasted\ saving = \sum_{n=1}^{\infty} \left(\text{Baseline 2 Unit Price} - \text{Forecasted MEP Year}_n\right) * \text{Expected Volume of Year}_n\Big)$$

Cost avoidance

Applies to cost reductions above baseline and against budget baseline

1 **Cost avoidance – The reduction or elimination of a price increase with the current manufacturer during the course of new contract**

The basic calculation is:

(Proposed Price Increase or Contractually Agreed Price – Final Negotiated Price) x (Respective actual volume during the year)

2 **Cost avoidance – Reduction vs budget baseline**

The basic calculation is:

Total Cost Allocated According to Budget Baseline of CY – Actual Total Cost of CY

Note: in order for Proposed Price Increase to be used as a baseline, 2 pre-conditions must be met:

- The baseline is tightly documented (a documented audit trail supporting the calculation of the baseline is available)
- The baseline calculation/savings are signed off by strategic controlling team