

# Developing the super supplier

Advanced collaborative relationships are still rare, but they offer real competitive advantage – and CPOs should be leading the search

by Corey Billington, Carlos Cordon and Tom Vollmann

**D**oes your company collaborate with its suppliers? Almost everyone will respond affirmatively to this question, but what exactly does “collaboration” mean? Based on our interactions with many companies, we see that collaboration needs to be clearly defined, with each specific customer-supplier relationship placed in a particular category. The categories are differentiated in terms of working relationships, performance metrics, inter-firm communications, managerial attitudes and fundamental objectives. In this article, we show how a few companies have pushed the envelope of collaboration, the benefits that have been achieved, the necessary changes in procurement, the imperatives for other parts of the organisation, and the implications for the CPO.

Let us start with the ultimate example of collaboration – the “super-collaborative” or “super-supplier” relationship. The fundamental objective for this category is set so high that there can be no doubt about the differences in working relationships, performance metrics, inter-firm communications and managerial attitudes. The purpose may be expressed as follows: “Our firm, working jointly with this supplier firm, will double the value/cost produced through our collaborative efforts and we will both obtain competitive advantage.”

Over a six-year period in the 1990s, Honda of America achieved significant payoffs by developing a few super-collab-

orative relationships. While the consumer price index rose by about 11 per cent during this period, one of Honda’s biggest competitors was able to control its costs of incoming materials, which rose by only 7 per cent. By having super-collaborative relationships, Honda was able to *reduce* costs by 19 per cent during the same period. The net gain over its competitor was therefore approximately 26 per cent (see figure 1, page 18).

Honda illustrates how creating and sustaining super-collaborative relationships can result in benefits that vastly outweigh the typical arm’s-length customer-supplier combative relationships. It is a good example of how super collaboration can bring significant cost-reduction benefits and aid market share through forging links with a few key suppliers and cultivating these relationships to produce breakthrough results.

So how *did* Honda of America achieve these results? We often hear firms talking about collaboration, supplier partnerships and so on, but these terms are, at best, largely empty and, at worst, another form of hardball negotiation. Building a super-supplier relationship requires a great deal of effort on the part of both the supplier and the customer, with joint efforts devoted to the processes that support their relationship. There are relatively few companies that focus on those key customer-supplier relationships that can make a competitive difference.

Over the past decade the automotive industry has best illustrated how using super-supplier relationships can result in



major gains over competitors. Specifically, Japanese car makers Honda and Toyota have used super-collaborative relationships to overtake their main American competitors Ford and General Motors. Culturally, the Japanese develop their supplier relationships in a different way than their western counterparts, often nurturing long-term relationships with key suppliers with which they develop joint respect and admiration. These relationships are based on shared trust, honesty, integrity and an objective focus on results.

In addition to the cultural issues and shared values, a super-collaborative relationship often includes a dramatic reduction in risk for the supplier, resulting in far better capacity utilisation. If, in essence, a customer buys a significant portion of the supplier's capacity – say, one shift – then the two firms can work together to greatly increase the productivity in that capacity. There need not be holes in the capacity waiting for orders; batch sizes, transport and synchronised lean manufacturing can be obtained. The cultural issues are necessary, but the payoffs come from much more highly co-ordinated actions, with minimal transactions and close coupling of the detailed operations in the customer-supplier relationship.

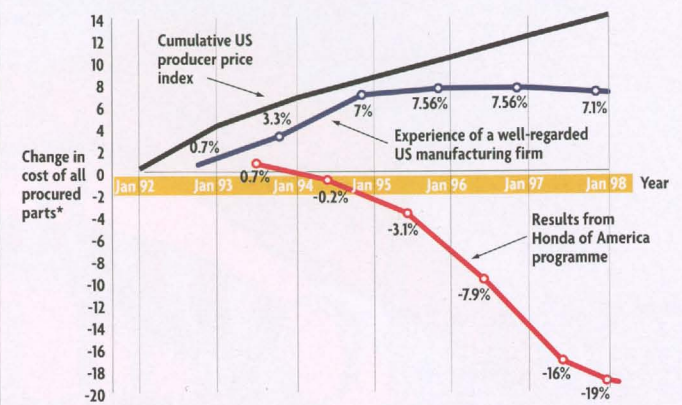
Perhaps a major reason why the concept has worked so well in the automotive industry is that its suppliers produce as much as 70 per cent of the value of the vehicle. In addition to cost, the quality and functionality of the vehicle are largely determined through collaboration.

Figure 1 illustrates not only the outcome of a super-supplier relationship, but also the time required to make it a reality. There are no quick fixes in this game, and the shared trust, honesty, integrity and objective focus on results must be maintained over a long time frame, unimpeded by sub-optimal squeezing of carefully chosen key suppliers. The long time frame is, in essence, used for a continuing set of business process re-engineering activities in both the customer and supplier companies, where cost and value are continually enhanced. For example, the vice-president of procurement for Honda of America at the time decided to develop one of its super-supplier relationships in sheet metal parts. After analysing existing suppliers in this area, he approached a small sheet metal company run by two brothers who had the "correct attitude". His criteria were to find a supplier that would be excellent at collaboration, trustworthy and share a mutual motivation for results. He approached the owners and took them into his firm's internal operations, shared best practices and taught them how to develop process engineering techniques, benchmarking and rapid knowledge implementation. They continued to collaborate, share information and provide feedback to one another, which resulted in this supplier becoming one of the

**Corey Billington** ([corey.billington@imd.ch](mailto:corey.billington@imd.ch)) is professor of operations management and procurement, **Carlos Cordon** is professor of operations management, and **Tom Vollmann** is professor emeritus of manufacturing management at IMD in Lausanne, Switzerland. The authors would be interested in hearing your experiences of collaborative relationships

FIGURE 1

### How 'super collaboration' helped Honda of America



\* Over 50% of total automobile cost

SOURCE: RETIRED VP PROCUREMENT, HONDA OF AMERICA

most competitive in the industry. After three years, the supplier had cut the costs of its materials by half, which was significant because it had previously been competitive anyway.

It is important to understand the payoffs to the supplier as well as to the customer. The "super supplier" can sell to its customer partner at cost-plus pricing, while selling to competitors at market prices. Classical economics tells us that the market price is set by the cost structure of the least competitive supplier still able to stay in the industry. The super supplier, being dramatically more productive, will achieve larger profit margins when selling to the competitors of its customer partner.

### Other examples of super collaboration

A multinational provider of products, technologies, solutions and services – which we will refer to as IQ – achieved great benefits through its focus and cultivation of super-collaborative relationships. In one somewhat unusual example it approached a memory supplier that was motivated to work with IQ but whose products did not meet its quality standards. The provider helped this supplier by signing a sourcing contract (again reducing risk for the supplier) and then going into the marketplace to help it find customers that could accept the product with its existing quality levels. Although the quality was below standard for IQ, it was good and improving. As was the case for Honda of America, IQ was able to provide significant engineering and process support to the supplier, leveraging its extensive process knowledge from benchmarking the best suppliers in the market.

In this collaboration, IQ shared results of quality analysis with the supplier and helped it with engineering and quality. Not only did the supplier improve its sales, it was also able to significantly raise the quality standards of its product – to the levels required, in fact, by IQ. In turn, IQ then benefited by being able to take advantage of this supplier's competitive pricing.

ing and adding another acceptable quality source. Moreover, when the market later went short on this product, IQ was able to use its sourcing contract to secure scarce supply, even though it was not using this supplier's products before the shortage occurred.

Another example of strong supplier collaboration is when large retailers such as Wal-Mart select so-called "category captains". At one stage, for instance, Frito-Lay served as the category captain for snack foods at Wal-Mart. In this role, Frito-Lay had access to sales data for all snack foods sold by Wal-Mart, including its competitors'. While the category captain in itself may not develop engineering expertise, the shared data does give competitive advantage to a selected supplier.

Wal-Mart has had category captain relationships with several other firms, including Procter & Gamble, Sara Lee and Hewlett-Packard. Despite its combative reputation, Wal-Mart also works in other kinds of collaborative relationships with key suppliers. For example, Philips Consumer Electronics received advanced information on special sales of competing products, so that it could adjust its own build schedules. The trust built from working effectively in these relationships develops the right culture for further co-operative efforts.

So how does super collaboration take place? And how does one create and manage it? We think it is helpful to divide or segment collaboration into four distinct levels. There is often an evolution and choice process for which supplier relations to improve. Moving from one level to the next requires definitive changes, which are most profound in the case of super collaboration.

## LEVELS OF COLLABORATION

Just as in market segmentation, where specific customers or customer groups are identified for specific treatment, suppliers need to be similarly segmented in terms of the degree of collaboration, and the subsequent differences in the approaches to be used. One size does not fit all.

We see four levels of collaboration between firms and suppliers, from no collaboration to very high levels of collaboration where a firm actively invests in the success of the supplier and its competitive position. We term this "super collaboration", since the firm is actively helping its supplier to be better than the competition in exchange for preferential treatment.

● **Combative:** This is the classic purchasing approach where procurement uses combative negotiations to get results. The main emphasis is on playing "hardball" with suppliers to bring down prices or leverage vendor reductions. These relationships use no collaboration and are always the best source for a quick fix when bottom-line results need to be doctored: simply demand lower prices and let the suppliers cope with the consequences. But as supply chains become more global and fragmented, the returns from this approach are diminishing, while the hidden costs are becoming more visible. While bottom-line issues and cost savings are a fact of life, heavy-handed negotiations fracture supplier relationships. Zero-sum

approaches of this kind mean that suppliers have no incentive to proactively help increase value/cost. Neither are innovative ideas likely to be shared with those customers perceived as solely interested in price-cutting (although suppliers tell us that such customers are often not interested in new ideas). The bottom line is that combative negotiation can help to achieve competitive costs, which avoid competitive *disadvantage*, but rarely bring competitive *advantage* to your organisation.

But let us be clear, combative negotiation is not to be abandoned as a procurement method. Many supplier relationships *should* be combative. If the items are not critical to the customer, and the customer is not the major customer for the supplier, why not try to get the best possible deal? Our message is that this approach needs to be applied to a carefully chosen supplier segment. If "price take down" is the only measure that procurement is being graded on, then combative negotiation will be the default approach, used with all suppliers. And if procurement staff are frequently rotated in their jobs, the organisation has little ability to develop long-term relationships, so short-term results dominate. Typically, most supplier relationships become combative. It is critical not to let all supplier relationships become combative, and to select carefully those that should receive different treatment.

● **Co-operative:** Possibly the majority of procurement relationships can be described as co-operative, with each side striving for supply chain co-operation. These relationships typically exist as an ongoing joint business exchange for goods and services and rarely go beyond the goal of mutually acceptable working terms. Shared costs in the supply chain relationship are discussed and understood. The customer works with the supplier to reduce these costs, as well as managing inventories and overall quality control. In addition, sales, response and transaction data are shared so that each party can operate effectively and efficiently.

● **Partnership:** These make up a small percentage of customer-supplier relationships. In this dynamic the emphasis is for each party to create mutual benefit rather than trying to gain primary control of the relationship or to focus on price reductions. This extends the co-operative relationship and normally attempts to maximise the overall value of it. Through the joint collaboration created in partnerships, each party aids the other in developing and/or leveraging their joint intellectual property – maximising the value of the relationship. Unlike a co-operative relationship, which focuses primarily on price and transactional costs, a partnership can support increased productivity and joint product development. A partnership takes time to develop and must have continuous and honest communication so that a deep level of trust can be built and so that each partner will commit to long-term goals. There will be fewer price-based negotiations but greater emphasis on jointly prospecting for new competencies, ideas and technologies to enhance the joint relationship and the customer product portfolio. >>

● **Super collaborative:** Although we have used this term and "super supplier" interchangeably, the former term is the better one: it is not about suppliers becoming some form of goliath, it is the joint relationship that counts – both firms truly collaborating. Some companies spend a great deal of money on procurement engineering and benchmarking to create excellent "should cost" or "absolute best cost" models.

These models and the procurement engineering knowledge used to build them may be used to obtain better pricing, but this will have limited value if done in a combative fashion. Instead, if the results of the absolute best cost models (best practices) are provided to a single supplier, that supplier, working closely with the customer, can make the necessary improvements to achieve the best cost – profitably. Correctly managed, the supplier gains significant competitive advantage by adopting this unbiased competitive intelligence, insights and engineering expertise and using it against its competition. The challenge is to ensure that, as in the examples of Honda of America and IQ described earlier, this also creates competitive advantage for the buyer.

When a firm commits to actively helping a supplier win in its market, a much higher level of collaboration is developed. Such relationships are rare, although more are forming as success stories and measured results are publicised. However, they remain far from being a standard procurement practice.

The customer focus for super collaboration requires a commitment from the entire firm to create significant competitive advantage for the selected supplier, and vice versa. In return for sharing relative process costs and insights, the supplier agrees to give the buying firm preferential treatment in the form of competitive advantage. One procurement executive described this as "I make them king and they make me happy".

Figure 2 is a summary of the four types of collaboration, in terms of the implications for the customer firm. As it shows, the payoffs are much higher from more collaborative forms of procurement, but the difficulties in implementation are much higher as well. It is important that firms see these four relationship types as choices that need to be deliberately made. More critically, once made they imply differentiated ways of working, performance metrics, inter-firm and intra-firm communications, attitudes and managerial support. They may also require very different people in the procurement organisation.

Figure 3 carries the distinction between collaboration levels further, showing that the segments get smaller as one increases the degree of collaboration. There is only time to work with a very few suppliers at the super-collaboration level.

**Creating a 'super-collaborative' relationship**

So what are the implications of all this for the CPO? What does a company need to do to create more collaborative relationships? How should one start on the road to super col-

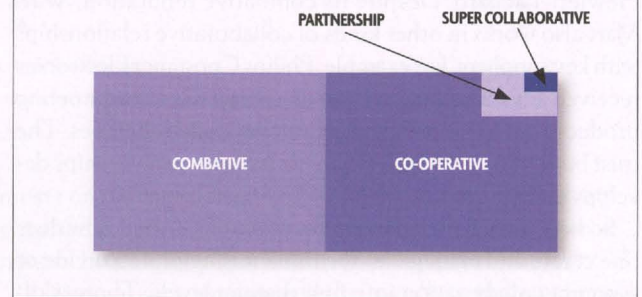
FIGURE 2

**Levels of collaboration**

PROCUREMENT STYLE	COMBATIVE	CO-OPERATIVE	PARTNERSHIP	SUPER COLLABORATIVE
BENEFIT TO FIRM	Lower price	Costs lower	Incremental value	Competitive advantage
COMPETITIVE ADVANTAGE	Rare	Possible	Likely	Significant
LIKELIHOOD	Most typical	Common	Difficult to sustain	Difficult to form

FIGURE 3

**Typical mix of collaborative relationships**



laboration? What are the imperatives in procurement – and in other parts of the company?

It is best to start this journey with only one supplier. The procurement organisation should be able to single out the best supplier with which to create this type of relationship. Procurement professionals will need to analyse which supplier is best suited for super collaboration, if any, and which could generate the benefits needed if efforts were put into joint working. In addition, with which supplier can they generate the mutual trust to reciprocate significant preferential treatment? Next, they will have to work diligently to form a relationship that can bear long-term pressure and scrutiny, and create a system of continuous measurement. A delicate balance must be reached here, as the supplier and the buyer will be exchanging sensitive market information necessary for them to attain their goals of higher productivity and creating competitive advantage.

This checklist outlines activities that a firm should have completed before starting a super-collaborative relationship:

- Procurement has a strategy, measures and a charter for competitive advantage that goes beyond "price take down".
- A spend category has been identified where a market opportunity exists to have a super-collaborative relationship.
- All functions in both organisations are committed to the long-term relationship.
- A structure has been organised that will continuously evaluate, communicate and improve the super-collaborative relationship. It will handle the continuous communication and alignment internally and with the supplier organisation.

Super-collaborative relationships require diplomacy and will be impossible to create and maintain without a consistent, long-term and collaborative mindset. This will require choosing appropriate procurement professionals to carry out this association since the goals, objectives, tactics, and even language used will be quite different than in typical procurement relationships. One does not "manage" the super-supplier relationship any more than one "manages" the relationship with a spouse. Occasionally, each organisation will appoint ombudsmen or relationship managers to safeguard the relationship.

It is imperative that the guardians of the super-collaborative relationship follow the "agreed rules of engagement" and are able to receive feedback and constructive criticism. An open and trusting rapport must exist, along with a joint focus on how working together can make each party more competitive. Firms will have to resist the temptation to fall back into combative behaviours when their super-collaborative suppliers are making high profits (from their competitors). Indeed, this is when you should actually be applauding their efforts, because they are making life harder for your competition.

Besides the opportunity to increase profits, the CPO's firm becomes another set of eyes and ears for the supplier and can contribute ways to cut costs, greatly increase productivity and eliminate waste. Normally, the relationship is judged using absolute best cost models where the goal is to supply goods or services at the best possible cost regardless of the current market price. We are not talking here about corporate espionage – though some critics may consider this to be the case – but by the CPO's firm creating competitive advantage through a long-term commitment by continuously providing unique feedback and insights that may be impossible for the supplier to obtain on its own.

### Three tenets for super-collaborative success

Once their company is ready for a super-collaborative relationship, a CPO must know that they have the means, motives and opportunity to venture forward. But how will you know if your organisation is ready for super collaboration? There are three essential tenets:

- **Means:** procurement has the competencies within its organisation to handle a super-collaborative relationship, is focused on competitive advantage and has decided on a measure of success that will illustrate this.
- **Motive:** strategic intent must exist and the gain from competitive advantage should be a motivator for each party to the collaborative relationship.
- **Opportunity:** there must be an appropriate market and supplier to form a super-collaborative relationship. An opportunity must exist for this relationship to produce a result that makes the investment of time and resources worthwhile.

It is essential to have a constant focus on objective and fact-based benchmarking using tools similar to the absolute best cost models described above. The ultimate goal for each side

of the relationship is to strive to create significant competitive advantage to an absolute measure, not a relative one.

Once a super-collaborative relationship is formed, the classic metrics associated with traditional suppliers no longer apply. Super collaboration must have outstanding results, since the effort and investment go beyond that required of any other procurement relationship. The relationship's metrics need to focus not only on the overall improvement of the supply chain or maximising value creation, but also on what competitive advantage each affiliate has created for their own organisation through their joint efforts.

Every process and activity at the supplier and at the customer needs to be constantly benchmarked and subjected to critical review. Improvements in other companies, industries and fields should be examined and best-in-class processes surveyed and used. The rate of improvement and value created should be continually measured. One approach is to establish "half-life" measures. If, for example, the time to deliver an order is two days, how long does it take to reduce it by 50 per cent? How long does it take to reduce the cash-to-cash cycle in the relationship by half? The key is to develop those metrics that most influence the joint effectiveness of the super-collaborative relationship.

Super-collaborative operations will improve classic productivity measures and each affiliate must commit to an ever-evolving set of metrics that develop and exploit gains and valuable learning brought by their counterpart. The super-collaborative supplier may use its new competencies with other customers – certainly those that relate to internal processes. As the partner, the interest is in having your supplier be a most effective provider of goods and services to others as well, but for the competitors to pay much higher prices. Of course, there will need to be open dialogue as to what acquired learning and initiatives can be used with other customers and suppliers. However, setting strict limitations on this joint material should be discouraged, as the focus should be on enhancing each other's market position and creating competitive advantage.

So, if super-collaborative relationships can yield such compelling results, why isn't every company racing to form one so that it can outpace its competitors? Simply put, it takes an empowered procurement function and devoted strategic effort over a long period of time. These relationships take long-term commitment and focus to grow and entire organisations must buy in and support the effort. Most firms have a difficult time committing to internal initiatives, so long-haul external collaborative relationships may be out of their comfort zone. Additionally, relying on procurement as a broker and facilitator of competitive advantage may be difficult for firms to accept. Over time, the procurement function must evolve and be endorsed to be a significant part of the firm's competitive advantage. The CPO will need to ensure that his or her team has the right skills to make this happen.

Correctly done, the commitment and energy invested can provide significant results that would be impossible for a firm to accomplish on its own. ■