Developing 'Fit-for Purpose' Buyer-Supplier Relationships: Beyond Partnership – Alternative Supplier Relationship Types

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Abstract. Over the past 10 to 15 years, the conventional wisdom within the purchasing and supply field has been that the development of collaborative relationships represents best practice purchasing and supply management. It is the contention of the authors, however, that this view is misguided and that managers need to adopt a fit-for purpose approach. For some purchases, a collaborative relationship is not necessary. On other occasions, the power relationship between the buyer and supplier means that the incentives required for a collaborative relationship are not present. This article sets out the different types of supplier relationships that exist in business markets and briefly discusses the factors that managers might consider when making relationship selection decisions.

Introduction. Over the past 10 to 15 years, the academic field of purchasing and supply management has developed significantly. The discipline can now claim to possess a credible body of work. However, one of the less impressive aspects of the discipline's development has been its treatment of supplier relationship management. It is fair to say that over the last 10 to 15 years conventional wisdom has stated that the development of collaborative relationships represents best practice purchasing and supply. It is the view of the authors that this view is misguided and that managers need to adopt a fit-for-purpose approach to the issue.

In our view, the underlying reason why this conventional wisdom emerged was the epistemological approach adopted by a number of purchasing and supply academics. Adopting an empiricist approach, various writers observed the successes of collaboration in certain industrial circumstances and took the view that such successful practice could be replicated elsewhere. As a result, what emerged to guide practitioners in the area of supplier relationship management was a series of tools taken or adapted from a number of what were believed to be exemplar companies. In our view, what practitioners actually required of academics was the development of a theoretical framework, developed initially from first principles and then tested empirically.

Whilst the danger of adopting an empiricist approach to model building in the social sciences is the risk that what works in one context might not work in another, in the supplier relationship management arena another problem has been encountered. This was that the researchers observing exemplar companies, such as Toyota, in our view, misunderstood what they saw. They assumed that as Toyota and its suppliers were working collaboratively it meant that they were also acting in a non-adversarial manner. This was not the case.

Whilst Toyota and its suppliers were engaged in all sorts of joint development projects, aimed at enhancing design and innovation and reducing waste, there was no question as to which party was obtaining the greatest benefits from the collaboration – Toyota. Toyota was working with its suppliers to increase the surplus value (that is, the gap between the supplier's costs and the buyer's utility) being generated in its transactions, but was then appropriating most of that value. Why was Toyota able to do this? It is very simple. It was because Toyota was dominant over most of its suppliers.

The merit of this example is that it allows us to question the assumption that managers face a choice between the bad old ways of adversarial, arm's length relationships and the new, best practice ways of non-adversarial, collaborative relationships. It allows us to see that such a choice is a false dichotomy. It is perfectly possible, for example, for relationships to be adversarial and collaborative.

In an attempt to make a contribution to the debate over supplier relationship management, we built two models. The first, descriptive, model identifies the potential, generic supplier relationship types that exist in business markets. Having identified the potential relationship types, we then developed a further model that consisted of the factors that drive which of these relationship types is eventually adopted in transactions between buyers and suppliers. Both of these models are discussed in the remainder of the article.

Generic Supplier Relationship Management Types. As was suggested in the Toyota example discussed above, we believe that in order to understand supplier relationship management, and in order to be able to identify the types of relationships that can be found in business markets, we need to view relationships as consisting of two main dimensions. These dimensions are the way of working between the two parties and the way in which the surplus value created in the relationship is shared between the two parties.

In terms of the way of working, we can crudely divide working methods into a choice between a collaborative way of working and an arm's-length way of working. By an arm's-length way of working, we mean that the two parties engage in very little contact during the relationship, beyond the exchange of the basic commercial information – what is to be supplied, at what price, by what date, etc – that needs to be exchanged in order for a transaction to take place. Such a level of interaction will often be highly appropriate when the transaction involves the supply of basic 'off-the-shelf' goods and services.

A collaborative way of working is where the level of interaction is higher and the relationship involves the creation of additional surplus value through some form of innovation or waste reduction. The different ways that buyers and suppliers can collaborate has been codified in a recent article by Cannon and Perrault (1999). They identify four categories of buyer-supplier interaction: product / process information exchange, operational linkages, co-operative norms and relationship-specific adaptations.

Supply relationships, therefore, fall somewhere on a continuum between arm's length and collaborative. Clearly, the more a buyer and a supplier engages in the categories of activities Cannon and Perreault have classified for us, the closer towards the collaborative end of the continuum the relationship is. This then constitutes the first of the two main supplier relationship dimensions.

The second dimension of a supplier relationship is the division of surplus value. This dimension can be explained with reference to basic economics. As was mentioned earlier, the term *surplus value* refers to the difference in a transaction between the supplier's costs and the buyer's utility function. A supplier is not expected to go into business if there is no prospect of making a profit. Therefore, included in its costs is a reasonable profit margin, something economists refer to as 'normal profits'. The buyer's utility function, meanwhile, is determined by the extent to which it values the product. If the product in question is priced beyond its utility then it will exit the market. The importance of these two points is that they bound the transaction within a certain terrain. That terrain is referred to as the surplus value.

Having identified the concept of surplus value, we now need to explain the factors behind how it is shared between the two parties. For us the major factor is buyer-supplier power (Cox et al 2000; Cox et al, 2002; Cox et al, 2003). By combining insights provided by sociology and industrial and institutional economics, it has been shown that buyer-supplier relationships can be characterised by one of four generic power positions. These are buyer dominance, supplier dominance, buyer-supplier independence and buyer-supplier interdependence. How the surplus value is shared is related to which of these four power positions pertains.

Where the buyer is dominant the buyer takes all of the surplus value. This is also the case where there is a situation of independence. The reason why the buyer is able to take all of the surplus value is that in both situations there is a competitive market. In a situation of interdependence - i.e. both parties are highly reliant on each other - the surplus value is shared, as the two parties are both able to negotiate from a position of relative strength. Finally, where the relationship is characterised by supplier dominance the supplier takes either a majority of the surplus value or all of it. Which of these occurs will depend on whether the supplier is able to price discriminate. If the supplier is unable to price discriminate, it may well be that an individual buyer's utility function is still in excess of the price being charged by the supplier.

The situations described above all relate to an arm's-length relationship and the surplus value that is created by the supplier's standard offering. However, we can also model the division of surplus value when the relationship between the buyer and supplier is collaborative. In economic terms, the reason why a buyer and a supplier enter into a collaborative relationship is to either reduce the supplier's costs or increase the buyer's utility.

For example, a buyer and a supplier could decide to undertake an exercise of process activity mapping. Having mapped out the process, they may decide that there is considerable waste in the process that can be easily eradicated. This action will reduce the supplier's costs and increase the amount of surplus value. Alternatively, a process activity mapping exercise could cause the two parties to realise that an adaptation to the configuration of the supplier's product would allow the buyer to simplify its own production process, thus reducing its own costs of production. If this was the case, this innovation would increase the buyer's utility function for the product. If this increase in the buyer's utility was greater than the increase in the supplier's costs caused by the adaptation then there will also be an increase in the amount of surplus value.

However, under our assumptions, even if there has been collaboration between the two parties that has led to an increase in the amount of surplus value, there is still the question of how that surplus value is divided. Under our assumptions, the fact that the two parties have collaborated does not change the fact that the buyer-supplier power relation will determine how that increased surplus value is divided.

Having discussed the two main dimensions of supplier relationships, it is now possible to present our model of the generic relationship types to be found in business markets (Cox, 1999; Cox et al, 2000). This is shown in Figure 1. As can be seen, we have identified six generic types. These come from the three possible divisions of surplus value and the two different ways of working.

Figure 1. Generic Supplier Relationship Management Types

Buyer-Skewed Adversarial Arm's-Length	**Buyer-Skewed Adversarial Collaboration**
Non-Adversarial Arm's-Length	**Non-Adversarial Collaboration**
Supplier-Skewed Adversarial Arm's-Length	**Supplier-Skewed Non-Adversarial Collaboration**

Making Supplier Relationship Choices. It needs to be recognised that all that this first model does is set out the generic relationship types that can be found in business markets. It does not tell managers what type of relationship to adopt in the particular circumstances he or she faces. To do this the manager needs to consider a number of questions. These questions are the basis of the second of the two models we have developed.

Managers need to ask the following. First, what are the likely benefits from collaboration? Second, what will be the cost to the firm of the collaborative activities? Third, what is the probability of the collaborative activity being successfully executed? Fourth, what is the power relationship with the supplier and how will this impact (a) whether the supplier will be interested in collaborating and, if it is, (b) the way in which the surplus value created will be divided? (Watson et al, 2003; Cox et al, 2003).

Having considered these factors the purchasing manager will be able to assess whether it is desirable or possible to enter into a collaborative relationship with a supplier and will know which of the two parties is likely to dominate the exchange. This assessment will see the relationship being positioned in one of the six boxes in the above matrix, as will all assessments of all buyer-supplier transactions.

Conclusion. We have set out in this article six generic supplier relationship types. We have also argued that none of these six types of supplier relationship represents 'best practice'. Many academics disagree with this and argue that non-adversarial collaborative relationships constitute a superior form. In our judgement, such a view is misguided for three main reasons. First, collaborative relationships are not always necessary because of the nature of the transaction. Second, it is perfectly possible to have a collaborative relationship with a supplier over which you are dominant. Indeed, we would argue that collaboration is much easier when you are dominant. Third, collaborative arrangements with suppliers are not always possible. There are many occasions when the incentive structure within a relationship is such that the supplier has no interest in dedicating scarce management resources to it. This will often be the case in situations of supplier dominance. In such situations there is very little the buyer can do about it.

Therefore, rather than thinking in terms of a best practice relationship style, managers should understand the alternative types that exist in business markets and assess which of these are desirable and / or possible in the circumstance in question (Cox et al, 2004).

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