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## **CONDUCTING SUCCESSFUL SUPPLIER NEGOTIATIONS**

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Negotiations is not an art or special gift that only certain individuals possess. Successful negotiations are the result of executing a solid, thorough process - "doing the homework"

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## Conducting Successful Supplier Negotiations

In our recent whitepaper entitled Keys to Success in Conducting a Request for Proposal Process, we covered the full range of activities in the Request for Proposal (RFP) process including negotiations. This whitepaper dives further into the negotiations process, quite possibly the most critical step towards creating successful supplier relationships.

It's a common perception that negotiation is an "art", executed by individuals with certain skills and characteristics. Well, that's how a lot of negotiations are conducted, sort of a game where winning is based on the "magic touch" of the negotiator. In reality, that approach rarely gets you to the optimal result and much is left on the table.

The good news is that successful negotiation is a process, that if followed will get you to the optimal result or very close to it, one which anyone can execute. You don't need to be a negotiation guru.

The objective of the negotiation process is to get the best deal the supplier is willing to offer. It is an important step in the RFP process. No matter how well you conducted the RFP, and no matter what resulted from the feedback process or a reverse auction you may have conducted, you don't know what the supplier is really prepared to give. Only the supplier knows that.

So, what is that process? The following chart shows it at a high level:

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### Elements Of A Successful Negotiation Process

Information	Preparation	Execution
<ul style="list-style-type: none"><li>• RFP results and analysis</li><li>• Supplier feedback results</li><li>• Reverse auction results</li><li>• Cost modeling</li></ul>	<ul style="list-style-type: none"><li>• Quantitative/economic negotiation items</li><li>• Qualitative/non-economic negotiation items</li><li>• Value analysis of items – to you, to the supplier</li><li>• Assessment of supplier likely positions</li><li>• Negotiation targets</li><li>• Documented plan</li><li>• Defined team roles</li><li>• Negotiation meeting objectives</li></ul>	<ul style="list-style-type: none"><li>• Strategy</li><li>• Dynamics</li><li>• Understanding of "Dos and Don'ts" for success</li><li>• Document</li></ul>

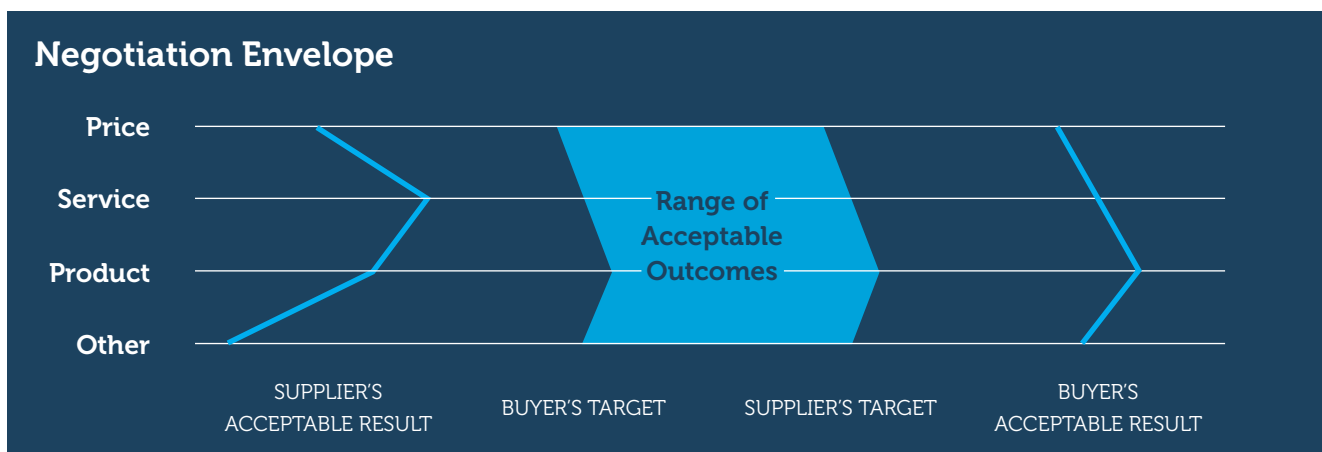
## Information

Information powers the negotiation process. When you begin the face-to-face negotiation you should have a wealth of data to use. This includes some or all the following:

- The analysis of the RFP responses
- The results of feedback given to suppliers relative to their competitive position and their revised responses based on that information
- You may have conducted a reverse auction rather than providing feedback. In some situations where there are many suppliers and numerous items to price, that's a good way to level out the bids and weed out uncompetitive suppliers to a short list, but should not be viewed as a substitute for negotiations. It generally drives the suppliers to a more competitive position but not to what they are really prepared to offer. Some suppliers make it a policy to not participate in reverse auctions so the use of this tactic should be well thought through.
- Cost models that predict the supplier's cost

Even with all this information you still don't know what the supplier is willing to do in terms of price or other non-price items. Your job in the negotiations is to get as close to that unknown position as possible. Understand that no matter how much research and analysis you have conducted that you do not know as much about the supplier's business and economics as the supplier.

The negotiation process is basically an exercise to find a mutually beneficial outcome, an outcome that brings you as close to the supplier's acceptable result and your target, i.e., the best they are willing to do that meets your objectives, which may be price or other considerations. The following exhibit shows the negotiation envelope, the "range of acceptable outcomes" for both parties that the negotiation process is designed to optimize.



## Preparation

The next step is to use this information to prepare for negotiations. Here are the key preparation steps:

1. Define all the quantitative and qualitative items to be covered in the negotiations including such things as:
  - Item price
  - Shipping cost
  - Delivery timing
  - Inventory management
  - Product performance
  - Technical assistance
  - Training
2. For certain negotiating items, develop an understanding of the value to you versus the cost of providing for the supplier. For instance, 2-day delivery may be very important to you, but not very costly for the supplier to accommodate. Or reducing your inventory by 10% could save you a half a million dollars, but the supplier could do that with an effort costing them only \$50,000. These are issues that can most easily be negotiated.
3. For each quantitative and qualitative item, establish your **Target** outcome (price or other result) and your **Acceptable Result** outcome (again price or other result). This should be based on the information you have developed.
4. Document the **Targets** and **Acceptable Results** so everyone on the team is on the same page. The following is an example:

Negotiation Worksheet		
Deep Down Mining Company	Sourcing Group: Ventilation	Supplier: Ace Ventilation
Negotiation Item	Target	Acceptable Result
<b>Quantitative</b>		
Price Reduction	6%	4%
Contract Length	2 years	2 years with option for 3rd year
Volume Discount	5%	3%
VMI / Consignment Charge	No Charge	2%
<b>Qualitative</b>		
Price Review Period	12 months with potential trigger anytime within period	6 months with potential trigger anytime within period
Price Review Trigger	10% change in material cost	5% change in material cost
Price Review Formula	Based on actual material cost of each item in RFP	Based on industry material cost index
Warranty	Clearly defined policy on warranty period and claims process	Clearly defined policy on warranty period
Training	Clearly defined commitment incl. frequency and staffing	Clearly defined commitment incl. frequency
KPIs And Reporting	Meet 95% delivery performance within 6 months and report monthly	Meet 95% delivery performance within 12 months and report monthly

5. Define the roles of each team member in the negotiation such as who will take the lead in negotiating, who will have any analytical data that may be shared with the supplier and who will take notes. There should not be anyone on the team that is not fully briefed and committed to the plan. And the team should be small, just those who really need to be there.

## 6. Establish an agenda for the meeting including:

- Feedback on their current bid
- Objectives of current session
- Key messages that can set the tone for the negotiation
- Sequential list of negotiation points to cover

Share the agenda with the supplier and add any items that they want to include.

## Execution

There are several strategies that make sense, but none are cast in stone. Here are some of the key ones:

- For each negotiation point start at or above your Target. If you don't, you have no chance of achieving it. Don't rush to your "bottom line" (Acceptable Result).
- Start with some of the easy items to establish a cooperative environment
- Make logical concessions based on the supplier's responses, keeping in mind your Acceptable Result
- Understand that the supplier may not be able to respond at the moment and may need to consult superiors or do some analysis
- Look for opportunities to trade for concessions, no free gifts. Use "If you could ... then we would be able to ...", a quid pro quo approach
- If the supplier initially offers better than your Target, consider if there is an opportunity to further exceed the Target, rather than immediately agreeing
- Don't let time be your enemy. Don't cave to a result just to meet an artificial deadline.
- Keep your options open; don't irrevocably agree to a single point until the entire agreement has been finalized
- "Nibble" towards the end for small, but valuable things that the supplier is likely to give to get the deal done

There are also several dynamics of the negotiation to keep in mind to help make it successful. Here are some of the key ones:

- Keep it at a professional, friendly, business like level. With the attitude that each party is going to end up with a win.
- Highlight the broad benefits to the supplier – key messages like "we think our partnership will create huge sales growth for both of us"
- Listen actively to understand the supplier's thinking
- Be sympathetic to the supplier's problems; help look for solutions that work for both parties
- Mirror back tentative understandings
- Don't answer your colleagues' questions – wait for the supplier to answer
- Don't answer questions "off the cuff", say "need to think about it, do some analysis"
- Use silence, don't fill the void, wait for the supplier to respond
- Understand what your alternatives are if you can't come to an agreement that is acceptable to you

Finally, document what has been tentatively agreed to at each negotiation session and at the conclusion of negotiations. Also, keeping in mind that any single negotiation point is not finalized until the entire agreement is finalized and agreed to.





## Summary

Negotiations is not an art or special gift that only certain individuals possess. Successful negotiations are the result of executing a solid, thorough process – “doing the homework”. It’s basically a fine tuning of the position that resulted from the RFP process, including iterations of the RFP process such as feedback and reverse auctions. Understanding that its objective is to get as close to what the supplier is willing to agree to as possible. Carefully documenting the issues or points of negotiation and establishing targets and minimum acceptable results prepares you for the negotiations. Executing the face-to-face negotiations is a professional discussion and process to seek out a win-win result for each party.

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