E-procurement vs. Negotiation

"Most B2B activity to date has centered on on-line exchanges and auctions, and most observers have assumed that these electronic marketplaces would come to dominate the B2B landscape. Once you look beyond the hype, however, you quickly see that most Internet exchanges are floundering. (…) The current B2B model has […] fatal flaws.

First, the value proposition offered by most exchanges – competitive bidding among suppliers allows buyers to get the lowest possible prices – runs counter to the best recent thinking on buyer-supplier relations. Most companies have come to realize that getting supplies at the lowest price may not be in their best economic interest. Other factors such as quality, timing of deliveries, and customisation, are often more important than price in determining the overall value provided by a supplier. (That's particularly true for the many manufacturers that have adopted lean, low-inventory production systems that depend on reliable, precisely scheduled shipments of supplies and components.) Many companies have spent the last two decades methodically forging tighter, more strategic relationships with suppliers – many such affiliations have involved joint product-design efforts, integration of complex processes, and long-term service contracts. The online exchanges' focus on price-driven transactions flies in the face of all this hard work.

Second, the exchanges deliver little benefits to sellers. Yes, suppliers have access to more buyers with only a modest increase in marketing cost, but that benefit is overwhelmed by pricing pressures. Few suppliers want to be anonymous contestants in ruthless bidding wars, and for the highest-quality, most innovative suppliers, price battles are anathema. As a result, the buyer-biased exchanges that characterize B2B today will not be able to achieve a critical mass of participants and transactions – they will be forever starved of liquidity.

To be successful in the long run, B2B markets need to offer strong incentives to both buyers and sellers."

Source: Richard Wise and David Morrison, *Beyond the Exchange – The Future of B2B*, Harvard Business Review, November-December 2000

Comments

It seems to me that the opinion expressed in the article quoted above is too negative.

Capturing procurement relevant data in electronic form has made the development of Supplier Relationship Management (SRM) systems and E-commerce platforms possible. This technical development met legitimate needs in the procurement field:

- Transparency and consistency: previously, companies often did not know what their different divisions, affiliates, etc. were buying from the same supplier and at which conditions. Suppliers were therefore able to hide deliberate or unintentional discrepancies in their price policy and to benefit from this lack of knowledge
- Reduction of transaction costs
- Geographical broadening of sourcing
- Optimization of price setting and full utilization of the competition dynamics
- etc.

The impact of SRM systems and e-commerce platforms on negotiations between buyers and sellers is at least threefold:

Transparency

Transparency has become fashionable. Who would dare nowadays to be against it? Strikingly enough however, the conditions which need to be met so that the actors involved make themselves transparent voluntarily are rarely being addressed. It seems to me that one key condition is related to trust. I do not think that I would ever freely disclose the cost structure and profit margin of my products, unless I would be extremely confident that the other side will not use my transparency against me.

Fairness

For the purposes of principled negotiation, the parties should address their conflicting interests with explainability and fairness in mind.

When negotiating prices for instance, openly disclosing all relevant information (cost structure, etc.) would be the best way to determine the figure which both sides could consider as well-founded and fair. Along this pathway (transparency → well-foundedness → fairness), the buyer may however be tempted to take advantage of the situation. And even with the best of intentions on both sides: defining what a fair margin is, will never be an easy task!

The issue of fairness is also often raised in connection with reverse auctions. Those, in my view, are not unfair as such. On the contrary: an auction is an impartial selection process offering competitors equal opportunities. Problems arise however if:

- the modalities are not clear enough or contain discriminatory elements;
- the rules of the game are not respected or modified during the course of the auction;
- auctions are used to buy products or services which do not differentiate themselves on price only (though using them in such cases is more unwise than unfair).

Procurement process

E-commerce platforms lead to a strong standardization of the procurement decision making process, which is mostly driven by the buyers and can hardly be influenced by the suppliers. (This evolution actually started before e-commerce; it was initially the result of an increasing professionalization of procurement and e-commerce platforms just pushed it to a higher level.)

Standardization creates in my view a real dilemma.

On the one hand, companies have a real problem if anyone inside is free to buy anything without any method or control. Companies have an absolutely legitimate interest in eliminating useless costs and taking advantage of efficiency increases. This interest justifies the standardization of the procurement decision making process and needs to be respected by suppliers.

On the other hand, the essence of procurement is in many cases (a) to find creative solutions which exactly match the needs of the customer while making optimal use of the resources of the supplier; (b) to ensure conditions which are acceptable for both sides. Such innovative and cost-saving solutions can only be designed through negotiation. Now: my understanding of negotiating is that the parties should not only talk about issues and solutions, but also about the decision making process in the framework of their negotiation. When the buyer dictates every aspect of the process – the questions to be answered, at the exclusion of all others; the individuals with whom the suppliers are allowed to talk to; etc. – the process cannot be called a negotiation anymore. As always: outcomes matter, but no more than the fairness of the process that produce them.

How to resolve this dilemma is however another question...

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