Module 2. Supply Environment.

Ch.1 Negotiation.

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Negotiation.

Definitions.

- Conferring, discussing, or bargaining to reach agreement or
- The process of working out a mutually satisfactory agreement.

Objectives of Negotiation.

- A fair and reasonable price.
- Needed quantities and quality.
- Timely performance.
- Control over how the contract is performed.
- Supplier cooperation.
- Sound and continuing relationships with the supplier.
Negotiation Conditions.

Conditions Favoring the Use of Negotiations.

- Lack of competitions.
- Price, Quality and Service Needs.
- Buying production/Service Capabilities.
- High Purchaser/Seller Uncertainty.
- Urgency.
- Long Supplier Leadtimes.
- Necessity for Flexible Contract Type(s).
- Lack of Firm Specifications.
- Single Source Strategies.
Negotiation Conditions.

Negotiation Condition: Lack of Competition.

- **Competition is limited when any of the following criteria for competitive bidding is missing:**
  - Two or more qualified suppliers.
  - Suppliers who want the business.
  - Clear specifications (in the case of materials) or SOW.
  - An absence of collusion among suppliers.
  - A purchase dollar amount large enough to justify the expense of competitive bidding.
Negotiation Condition: Price, Quality, and Service Needs.

- Competitive price can be gained by offering
  - A supplier 100% of the volume, previously split between several suppliers.
  - Multi-year contractual agreements.
  - The promise of increased volume because of new market developments.
  - A willingness to share supplier identified cost savings.
  - A willingness to mutually grow and develop as a partner.

- Emphasis should be on working with suppliers to obtain the lowest total cost of ownership, rather than the lowest purchase price.
Negotiation Condition: Price, Quality, and Service Needs.

- Suppliers should have no doubt about incoming inspection criteria, so they can inspect and perform at that level. A good understanding of these conditions can save the time and money spent in resolving rejects.

- Good service is also a point of negotiation. The followings may be discussed at the process of negotiation.
  - A 24-hour emergency phone number.
  - Deliveries on holidays and weekends.
  - Emergency shipments.
  - Engineering assistance.
  - Responses to requests for early shipments.
  - A personal representative to handle the account.
Negotiation Condition: Buying Production/Service Capabilities.

- The purchase of service capabilities is often preceded by some form of negotiation in order to establish the requirements of the purchasing organization.

- The purchaser may need to present specific requirements in advance to allow the supplier to evaluate and establish a price.
  - Delivery time and frequency.
  - Quality.
  - Insurance coverage, and liability.
  - Material costs, and so on.

- Value analysis and cost-benefit techniques are often useful in identifying tradeoffs than may reduce price without compromising service and quality.
Negotiation Conditions.

Negotiation Condition: High Purchaser/Seller Uncertainty.

■ If the purchaser has a high degree of uncertainty about the supplier and the market within which the supplier operates, the purchaser may want to seek a negotiated commitment.

■ Or, a purchaser is not certain that the supplier has made the commitment necessary to service the purchaser's needs. Proposing a binding contract with a negotiated price can draw the required commitment from the supplier.
Negotiation Condition: Necessity for Flexible Contract Type(s)

- A purchaser may require a unique delivery schedule, have irregular volumes, require services the supplier does not provide, or be unwilling to make the type of commitment to which the supplier is accustomed.

- In such cases, a purchaser may need a flexible contract or agreement because the purchaser's needs will probably not fit within the "boilerplate" of the supplier's existing contract form.
Negotiation Condition: Lack of Firm Specifications.

- The lack of firm product specifications can cause the purchaser a number of problems during negotiations.

- In areas where the specifications are not clear, the purchaser may have to accept the supplier's specifications or negotiate a middle ground. Some of the greatest problems will often be encountered as the supplier's product moves through incoming quality control.
Negotiation Condition :Single Source Strategies.

- Single sourcing is the practice of deliberately concentrating purchases of a particular product or service with one source in preference over others in a competitive marketplace.

- The purchaser may want the single source because of good pricing, transportation advantages, or the supplier's technical expertise.

- There are several tactics for a single source.
  - Sell the supplier on the mutual benefit of a win-win approach to negotiations.
  - Drop the product line if pricing or other issues cannot be resolved with the supplier during negotiations.
  - Consider producing the product or service in-house.
  - Appeal to the supplier's sense of partnership.
Negotiation Planning

Negotiation Planning Process.

- **Step 1. In-depth analysis of the supplier's proposal.**
  - Evaluate price, delivery, specifications, terms, and any deviation from your requirements. A thorough knowledge of the supplier's proposal can be an advantage at the bargaining table.
  - Keep in mind that the supplier's proposal is usually the beginning point for negotiation.

- **Step 2. Setting Objectives.**
  - Is the goal a lower price, higher quality, an accelerated delivery, or a combination of these? In any case, a specific plan should be drawn up, and the negotiator should work toward the plan.
  - If a negotiating team is involved, the team leader should be selected, and all team members should be briefed on what not to say.
Elements for Negotiation Planning.

1. Negotiation Objectives.
   - Fair and Reasonable Price.
   - Timely Performance.
   - Meeting the Minimum Essential Needs of the Organization.
   - Control over Contract Performance.
   - Maximum Contractor Cooperation.
   - Sound Relations with Contractors.
Elements for Negotiation Planning.

2. The Negotiation Site.

- It is sometimes best to conduct negotiations at the purchaser's location, since the purchaser will be most comfortable there; will have all needed data, backup, and support; and can essentially control the negotiations. On the other hand, negotiations at the supplier's site give the purchaser the power to walk away.

- Regardless of the site selected, wise negotiators pay close attention to negotiation security.

- Knowledgable negotiations know that they must be careful about what they discuss in public places, must pay close attention to the security of work notes, and must make sure that confidential material is secured.
3. Team Selection.

- A negotiation team is normally used when a product/service is complex and one person does not have sufficient knowledge of all issues.

- The team should consist of purchasing and the other departments involved, such as engineering, quality assurance, operations, accounting, and marketing.

- A team leader - usually the purchasing manager - should be selected to guide the team in the right direction and to chair the pre-negotiation meetings. The leader should be the main point of contact between the purchaser and supplier, and should set up times and locations for the negotiation sessions.
3. Team Selection.

- An important aspect of team negotiations is the caucus. The caucus should immediately be used when disagreement, confusion, or misunderstanding occurs within a negotiation team.

- The caucus may also be used to slow down momentum if negotiations are not going well, to create a pause that causes the supplier's team to caucus.

- The caucus should be a routine part of negotiation tactics, so that the calling of a caucus does not provide any signals to the other party.
4. Relevant Information.

- Some areas of importance include the following:
  - Negotiation Objectives.
  - Cost Data.
  - Financial Reports on Suppliers.
  - Market Informations.
  - Financial Strength of the Supplier.
  - Strengths of Both Parties.
  - Weaknesses of Both Parties.
  - Price History.
  - Quality History.
  - Specification Issues.
  - Negotiation Styles and Personalities of those with whom the purchaser will be negotiating.
  - Negotiation Objectives.
  - Time Available.
Elements for Negotiation Planning.

5. Analysis of Supplier's and Purchaser's Position.

- A thorough study of the supplier should be made by the negotiator or negotiating team, to ensure that the supplier's position, strengths, and weaknesses are understood.

- The following elements may be considered in the process of negotiation:
  - Supplier's desire for a contract.
  - Supplier's certainty of getting a contract.
  - Amount of time for negotiation.
  - Adequacy of cost/price analysis.
  - Purchaser's availability of other options.
  - Supplier's competitive position.
  - Skill and authority level of the Negotiators/negotiation team.
  - Extent of planning for the negotiation.
  - Supplier financial condition.
  - Purchaser's financial condition.

- All things being equal, a seller's market gives the supplier a negotiating advantage, and a purchaser's market gives the negotiating advantage to the purchaser.

- However, many negotiations are conducted within the context of the overall, long-term relationship between the supplier and purchaser. Even though short-term market conditions may give one of them an advantage, both realize that taking excessive advantage of market conditions for short-term gain may lead to long-term problems.
Elements for Negotiation Planning.


- The planning of strategies and tactics for negotiations actually involves a three-dimensional function.

- **Strategic Planning.**
  - Strategic planning refers to the long-range goals of the organization. Strategic planning requires the negotiator to select sources that will optimize attainment of the overall philosophy and objectives of the purchaser's organization.
  - Knowledge of product-market mix, customer and environmental constraints, and the basic goals of the organization concerning technology, price, and policy are essential.

- **Administrative Planning.**
  - This planning refers to the logistics of getting people and information for negotiations.

- **Tactical Planning.**
  - This involves getting optimal results at the bargaining table.
  - It involves setting goals, and evaluating the strengths and weaknesses of the other party. A careful study should be made of issues, problems, agenda question, concessions, commitments, promise, pricing, quality, and delivery performance.
  - The team leader should be selected, and negotiating tactics should be reviewed and discussed.
8. Organization Cultural Factors.

- Cross-cultural negotiations are normally thought as being between parties of different nations.

- When conducting cross-cultural negotiations, the ability to understand the culture of the other party can reduce the number of misunderstandings that inhibit negotiations.

- For example, a purchaser for a country government who is purchasing computers from an organization that usually markets to businesses may have to educate the supplier on the process of public-sector purchasing.
9. Fall-Back Alternatives.

- When preparing for negotiations, consider that give-and-take is a normal part of the process. Therefore, when preparing for negotiations for purchaser should identify optimistic, target, and pessimistic positions for each issue.

- As negotiations proceed, the purchaser can then assess progress on each issue, and progress on the total package. In some instances a purchaser may agree to less than the pessimistic position on one issue, if the supplier makes concessions that exceed the optimistic position on another issue.
1. Win-Win/Cooperational.

- This philosophy is likely to be used when both parties have a high degree of concern for their own and the other's outcomes.

- Examples of this include most negotiations between partners, and negotiations where the purchaser and supplier want to do business with each other.
2. Win-Lose/Adversarial/Competitive.

- This philosophy is likely to be used when the negotiator has a high degree of concern for this or her outcomes and a low degree of concern for the other's outcomes.

- When both parties have moderate concern for their own and the other's outcomes, the philosophy is likely to be compromising, where both parties split any differences.
3. Lose-Lose/Confrontational.

- This philosophy is likely to be used when both negotiators have a low degree of concern for their own and the other's outcomes.

- Lose-lose/confrontational negotiations are likely to occur when both parties prefer not to do business with each other but are force to because of circumstances beyond their control.
Negotiation Planning Process.

- The choice of negotiation strategies and tactics results from the negotiation planning process. This process includes analyzing the supplier's proposal. This process includes:
  - Analyzing the supplier's proposal.
  - Establishing objectives.
  - Formulating optimistic, target, and pessimistic positions on each issue.
  - Analyzing and estimating the supplier's optimistic, target, and pessimistic position on each issue.
  - Defining and organizing the issues to identify points of similarity and difference between the purchasing organization and the supplier.
  - Developing strategies and tactics.
  - Selecting the negotiation team.
  - Developing an agenda.
Negotiation Strategy.

- Three practical strategies.
  - **Reveal no position.** Revealing no position is used when the purchaser does not want to discuss position. This strategy attempts to maneuver the supplier toward the purchaser's position by probing the supplier's proposal point by point.

  - **Reveal the optimistic position.** This strategy is the most common approach when the purchaser has the supplier's proposal. This approach establishes the range for negotiation on each issue. The purchaser and the supplier can then discuss and resolve each issue.

  - **Reveal the optimistic position and the immediately offer the target position.** This strategy can work if the purchaser can sell the supplier on the merits of the approach. This strategy can backfire if the supplier refuses the offer. The purchaser may then have to settle for something closer to the pessimistic position.
Negotiation Strategy and Tactics.

Negotiation Tactics.

- Effective negotiators are able to adapt their tactics to the situation and can recognize tactics used by the other party. The following summarizes some basic negotiation tactics.

  - Sequence/prioritize the issues for discussion.
  - Use questions wisely.
  - Listen effectively.
  - Maintain the initiative.
  - Use solid data.
  - Use silence.
  - Avoid emotional reactions.
  - Make use of caucuses.
  - Don't be afraid to say no.
  - Be aware of deadlines.
  - Be aware of body language.
  - Keep an open mind.
  - Get it in writing.
  - Use "the bogey" tactics.
  - Make appropriate concessions.
  - Use the "missing person" tactics.
  - Use the "take it or leave it" tactics.
  - Never negotiate beyond your physical and mental endurance.
Some Negotiation Tactics.

- Make use of caucuses.
  - Caucuses, or recesses, are an excellent way to rethink your position, interrupt the supplier's momentum, or evaluate a counterproposal.

- Make appropriate concessions.
  - It can produce significant gains. Concession need not be made "one for one" or be of equal value. Your willingness, or unwillingness, to make concessions will set the tone for additional negotiations.

- Use the "missing person" tactic.
  - The "missing person" is the deliberate absence from the negotiations of the person with final authority. This tactic gives the negotiator more time and provides a way out of a tight situation.
Some Negotiation Tactics.

- **Use the "take it or leave it" tactic.**
  - This lets the supplier know that the purchaser is firm on an issue and will not move. Do not use this tactic unless you mean it. Think carefully before using this tactic as a bluff. If you have to back down, your credibility will suffer.

- **Use "the bogey" tactic.**
  - In this tactic the purchaser tells the supplier that he or she likes the product but $X is all that he or she will pay. This tactic often bring a favorable response from the supplier.
Considerations for Negotiations.

Fact-finding Sessions.

- A complete study of the supplier's business history, length of time in business, growth, and overall success should be conducted.

- Based on previous negotiations and meetings, develop profiles of the supplier's negotiators to assess individual personalities, evaluate strategies and tactics they are likely to use, identify strategies and tactics that are likely to work with them in the future.

- Financial data can be gained from Dun & Bradstreet reports (www.DNB.com), libraries, newspapers, government filings, and stock market analysis reports.

- Valuable information can also be gained by talking to people and organizations who have dealt with and/or know the supplier.
Best and Final Offer.

- Telling the other party that this is the best and final offer is a risky negotiating tactic that the purchaser should use with caution. Because the supplier may decline, the purchaser should have an alternative source before using this tactic. Another risk of the best and final offer is that the purchaser has no room for further negotiation.

- If the purchaser is presented with a best and final offer, the purchaser can accept the offer, reject the offer, make a counteroffer, be noncommittal, or remain silent.

- This avoids confrontation, provides the supplier with no feedback, and gives the purchaser time to decide how to respond.
Considerations for Negotiations.

Negotiating with Sole Offeror vs. Entire Competitive Range.

- Dealing with a supplier that does not have competition, or that has very limited competition, is a difficult position from which to negotiate.

- Several tactics for generating competition within this area.
  - The purchaser can advise the supplier that the purchaser’s organization is considering making the item in-house.
  - The purchaser can advise the supplier that if the price is not reasonable, the purchaser’s organization will no longer consider making the product that requires the component.
  - The purchaser can advise the supplier that he or she is considering substitute items.
Considerations for Negotiations.

Negotiating with Sole Offeror vs. Entire Competitive Range.

Several tactics for generating competition within this area.

- If the supplier is already supplying products to the purchaser, the purchaser can advise the supplier that his or her long-range interest should be in keeping the purchaser as a customer, rather than achieving a temporary price advantages.
- The purchaser can seek a win-win situation where cost, risks, and saving are shared.
- If the supplier has high inventory levels and needs to lower them, the purchaser can use this as leverage.
- If the supplier has financial problems and can use the additional business, the purchaser can use this to his or her advantage.
Considerations for Negotiations.

Negotiating with Small and Historically Underutilized Business.

- Special consideration may be given to these negotiations in order to help develop the supplier as a new, viable competitor in the marketplace.

- Some considerations that can help develop a small and historically underutilized supplier.
  - Providing technical and engineering assistance,
  - Sharing cost saving,
  - Furnishing raw materials and components,
  - Helping the supplier identify new sources and customers,
  - Training supplier personnel,
  - Setting up financial and operation systems,
  - Providing long-term orders, and
  - Providing assistance in developing business and marketing plans.
Considerations for Negotiations.

Documentation of Negotiation.

- **Documentation should include the following:**
  - **Subject** - An overview of the negotiations, including supplier's name and location, contract number, and a description of the item to be purchased.
  - **Introductory Summary** - A description of the type of contract and the types of negotiation action involved, plus comparative figures of the supplier's proposal, the purchaser's objectives, and the negotiated results.
  - **Particulars** - A description of the product/service to be purchased and who was involved in the procurement.
  - **Procurement Situation** - A description of the factors in the procurement situation that affected the final decisions.
  - **Negotiation Summary** - A description of the supplier's contract pricing proposal, the purchaser's negotiation objective, and the negotiation results, tabulated in parallel form.
Considerations for Negotiations.

Negotiations as a Consortium or Cooperative.

- **Consortium and Cooperatives.**
  - **Consortium.** A consortium is a formal organization, usually comprised of private-sector, for profit, non-competing organizations from varied industries. Members are usually active in the management of the consortium, whether commodity purchases are made by lead members or by a hired third party.

  - **Cooperatives.** A co-op is a profit or not-for-profit business that serves members in a single industry, such as hospitals, universities, or country governments. Co-op members play no role in the management of the co-op's suppliers and administrative activities. Members may recommend suppliers, but co-op management evaluates and selects suppliers.
Considerations for Negotiations.

Negotiations as a Consortium or Cooperative.

- **Issues for negotiation regarding collaborative purchasing agreements relate to forming or joining a consortium or co-op.**
  - Protection from antitrust problems.
  - Limitation of liability concerns.
  - Ease of entry and exit.
  - Definition of rights and obligations of members.
  - Protection of confidential information.
  - Costs and membership fees.
  - Requirements to buy from participating suppliers.
  - Special needs, such as storage, delivery, or quality requirements.
  - Rules of behavior.
1. Which of the following is the BEST policy to following regarding the inclusion of the buying organization's attorney on a negotiation team?
   A. An attorney should be present at all times during negotiations.
   B. An attorney should be present only if the opposing side has its attorney present.
   C. An attorney should be present only if a legal matter is likely to be raised.
   D. An attorney should not be present during negotiations at any time.

2. Which condition clearly indicates that negotiation is preferred over competitive bidding?
   A. The dollar volume of the potential purchase is very large.
   B. The product isn't actually needed until five months into the future.
   C. Each firm that is competing is a technical giant in the field.
   D. There will be substantial preproduction engineering and tooling required.
3. Which of the following is more closely associated with negotiation tactics as opposed to negotiation planning?
   A. The process of determining goals and developing a strategy for implementing the goals.
   B. The art of influencing someone else's decisions.
   C. The determination of current prices and trends for the product to be purchased.
   D. An understanding of the needs and systems of one's adversary.

4. All of the following factors will strengthen the buyer's position in a negotiation session EXCEPT
   A. Unclear specifications.  B. A strongly competitive field.
   C. A lack of urgency for a contract.  D. A thorough cost/price analysis.
5. Which of the following is the LEAST likely source of relevant information about a supplier when planning for a negotiation session?
   A. External database.
   B. Persons who previously negotiated with the supplier.
   C. *Dun and Bradstreet* Report.
   D. *NAPM Report on Business*.

6. All of the following are steps involved in preparing for negotiations with a supplier EXCEPT:
   A. Analyzing the supplier's negotiating position.
   B. Analyzing the supplier's proposal.
   C. Deciding whether to negotiate alone or in a team.
   D. Preparing an initial contract draft.
Performance Check.

7. Of the following, which of the LEAST important reason for employing the team approach to negotiations?
   A. The contract is for a large amount.
   B. The contract is complex.
   C. The chief negotiator has little technical knowledge of the product.
   D. The chief negotiator desires safety in numbers.

8. It is important for a team to present a unified position during negotiations in order to maintain the appearance of
   A. Flexibility.  B. Superiority.  C. Strength.  D. Confidence.
9. All of the following are characteristics of an ideal negotiator EXCEPT a tendency to
   A. Set high goals.
   B. Take as long as is necessary to reach a goal.
   C. Make concessions in small increments.
   D. Discount information that challenges assumptions.

10. Which of the following situations is MOST likely to enhance the bargaining position
    of the buyer during negotiation?
    A. A "win-lose" philosophy on the part of the buyer's team.
    B. A single-source purchasing policy.
    C. A sound supplier evaluation system.
    D. A supplier that needs to keep its work force fully employed.
11. Of the following, the MOST important element in successful negotiation is
   A. The buyer's bargaining strength.        B. Advance planning.

12. A buyer tells a seller during negotiations that the most that the buyer can pay for a piece of equipment is $70,000, due to constrained resource. The negotiation tactic that the buyer is using is known as
   A. The bogey.
   B. Take it or leave it.
   C. Best and final offer.
   D. Concessions.
13. All of the following are tactics for negotiation in sole source situations EXCEPT
   A. Informing the supplier of one's intention to use another supplier.
   B. Presenting the possibility of altering the product's design.
   C. Pointing out the existence of high supplier inventories.
   D. Emphasizing the supplier's long term interests over short-term gains.

14. Business negotiations involve which of the following ?
   I. Preparation and planning.
   II. Assessing strengths and weaknesses.
   III. Adaptability.
   IV. Luck.

   A. I and II        B. I and III        C. I, II and III        D. I, II, III and IV
15. Reasons to use negotiations would include all, EXCEPT:

A. Quality, price, and service needs.  
B. High buyer uncertainty. 
C. Short product leadtime. 
D. Urgency.
Performance Check.

Solutions.

1  2  3  4  5  6  7  8  9  10  11  12  13  14  15
C  D  B  A  D  D  D  C  D  D  B  A  A  D  C