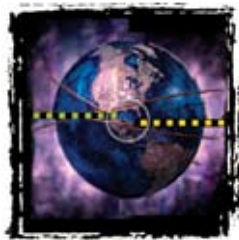


# Buying in a Sellers' Market

***Suppliers have become more powerful than ever, which means buyers must adjust quickly to a new playing field. To help supply management professionals make that adjustment, A.T. Kearney has developed The Purchasing Chessboard.***

By Christian Schuh and Ramon Romero Perez



Since the 1980s, most procurement professionals have operated in a buyer's market. Using relatively simple tools—RFIs and RFPs, bundled products and services, and

multi-year contracts—companies could negotiate from 1 to 3 percent annual price reductions from suppliers. But this “golden age” of purchasing appears to be over. The ongoing consolidation of the supplier market, rising energy prices, and the increasing demand for raw materials from emerging markets means more companies are in a seller's market. Accordingly, buyers must adopt new tools and strategies to compete effectively on a new playing field.

In a seller's market, old purchasing strategies such as pitting suppliers against one another, or simply requesting price reductions, do not work. In a recent A.T. Kearney survey, we discussed the impact of this new seller's market with more than 200 CEOs and managing directors of major companies. Among the most often heard remarks about the market is that their procurement departments are not up to the challenge.

## The Purchasing Chessboard

To help procurement professionals master the tools of their trade, we developed The Purchasing Chessboard, trademarked by A.T. Kearney Inc. The Purchasing Chessboard is a compilation of insights and experience from more than 500 purchasing projects performed worldwide over the

past three years, and thousands performed over the past three decades. The chessboard constitutes 64 methods, each representing a stand-alone, differentiating way to work with suppliers to reduce costs and increase value. These methods are derived from these four purchasing strategies encompassing 16 general approaches. (Exhibit 1 gives the 64 stand-alone methods.)

**1. Leverage competition among suppliers.** The most celebrated and perhaps most frequently employed procurement strategy is pitting suppliers against one another in a price competition. This is particularly popular in high-demand, low-supply markets. Purchasing basic forgings or welded steel structures fits nicely into this category. Companies typically use four procurement levers: tendering, leveraging global supplier markets, reviewing suppliers' prices, and enforcing target prices. Experience shows that most procurement organizations readily employ the first two levers, but only a few companies focus on the latter two: pricing and enforcing target prices.

With this in mind, a cost regression analysis is a key component of the Chessboard. The analysis is performed via a statistical methodology that determines target prices based on the technical characteristics of a module. Once identified, the target price becomes the fact base for renegotiating with existing suppliers. In the past three years, this analysis has proved successful for procurement professionals in various industries.

**2. Seek joint advantage with suppliers.** When buyers and suppliers in a transaction have equal market power, the first strategy is not sufficient. The automotive industry, for example, pro-

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cures numerous unique modules (such as engine controls) from its suppliers, so simply pitting suppliers against one another will not suffice.

Instead, companies must strive to find common advantages with their suppliers. The goal is to build joint cost-value partnerships, an integrated and transparent operations planning process, and to manage the entire value chain jointly. Such partnerships can reduce costs while also generating value. Suppliers and buyers work together to generate ideas for optimizing costs and then agree to share in the respective benefits. What begins as an ad-hoc program could eventually turn into a longer-term strategic alliance.

**3. Change the nature of demand.** In low-demand, high-supply markets—where suppliers are in monopolistic or quasi-monopolistic positions because of their technical expertise—companies must change the nature of demand. Low-demand markets stem from developing long-term partnerships with key suppliers; these suppliers soon become indispensable, particularly in terms of research and development (R&D) or technological expertise. Companies prolong the problem when they choose not to endure the time and costs associated with shifting to new suppliers.

In such markets, the objective is to change the nature of demand. This is done by re-specifications of components, data mining, development of new technical options, and risk management. In our Chessboard, we call this “invention on demand,” which is one of the 64 methods. The company systematically challenges the basic elements of a technical system and searches for alternatives throughout the field of science—essentially replacing technical options for modules delivered by suppliers. This approach is relevant for industries where patent-protected components or systems are already successfully employed, for instance, in aviation, engineering and automotive.

EXHIBIT 1

**The Purchasing Chessboard Constitutes 64 Stand-Alone Methods**

High	8	Invention on Demand	Leverage Information Network	Functionality Assessment	Specification Assessment	Value Chain Reconfiguration	Revenue Sharing	Profit Sharing	Strategic Alliance
	7	Core Cost Analysis	Design for Sourcing	Product Teardown	Design for Manufacture	Supplier Tiering	Sustainability Management	Project-Based Partnership	Value-Based Sourcing
	6	Vertical Integration	Intelligent Deal Structure	Composite Benchmark	Process Benchmark	Collaborative Capacity Management	Virtual Inventory Management	Total Lifecycle Concept	Collaborative Cost Reduction
	5	Bottleneck Management	Political Framework Management	Product Benchmark	Complexity Reduction	Visible Process Organization	Vendor Managed Inventory	Supplier Development	Supplier Fitness Program
	4	Sourcing Community	Buying Consortia	Cost Data Mining	Standardization	RFI/RFP Process	Excessive Bidding	Total Cost of Ownership	Leverage Market Imbalances
	3	Procurement Outsourcing	Mega-Supplier Strategy	Master Data Management	Spend Transparency	Supplier Market Intelligence	Reverse Auctions	Price Benchmark	Unbundled Prices
	2	Compliance Management	Closed Loop Spend Management	Supplier Consolidation	Building Across Generations	Make or Buy	Best Sourcing	Cost Regression Analysis	Factor Cost Analysis
Low	1	Demand Reduction	Contract Management	Bundling Across Product Lines	Bundling Across Sites	Global Sourcing	LCC Sourcing	Cost-Based Price Modeling	Linear Performance Pricing
		1	2	3	4	5	6	7	8
		Low							High

Source: A.T. Kearney

**The Purchasing Chessboard incorporates 64 methods, each of which represents a stand-alone, differentiating way to work with suppliers to reduce costs and increase value.**

**4. Manage spend.** The final strategy, managing spend, is particularly useful in low-demand, low-supply markets—for example, for most indirect material categories such as office supplies or MRO (maintenance, repair and operations). In these situations, the focus should be on volume bundling, commercial data mining, co-sourcing, and demand management. Apart from defining and monitoring guidelines, the creation of transparency regarding the spend behavior (for example, through IT-based spend-cube solutions) is a concrete approach to reduce costs and increase value.

**Flexible and Strategic**

The Purchasing Chessboard maps each market situation that takes place between a company’s purchasing organization and its suppliers. It is flexible enough to adapt to changing market conditions, such as rising raw material prices, and strategic enough to address the challenges in a new age of purchasing.