Key Supplier Collaboration: New Way to Drive Value

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The 2008 economic crisis had unpredictable yet lasting effects on the power dynamics of suppliers and buyers around the globe. Suppliers typically gain power when they have a low risk profile, a limited supply base, and a product that’s essential to their customers. The economic crisis, coupled with fluctuating raw-materials prices and natural disasters, culled lesser suppliers and increased the power of those that remained.

Yet the crisis also concentrated power on the demand side: Buyers typically gain power when they can offer their suppliers stable revenue amid turbulent times, growth opportunities, competence development (Six Sigma or Lean Manufacturing, for example), and brand enhancement (such as a public relationship that can build confidence among the supplier’s investors). In the turbulent times following the crisis, stable buyers offer suppliers rare opportunities to achieve these goals.

What happens when both suppliers and buyers grow in power? One result is that both parties need to look for new ways to drive value. This column will explore how one such approach, key supplier collaboration, can bring about sustained growth, improved risk management, efficiency through value chain optimization, and enhanced structural capabilities.

Opportunities and Methods

When either a supplier or a buyer has unmatched power, the powerful party can use a transaction to extract value from their weaker partner. But when both parties are powerful, they must shift to value creation through collaborative techniques, such as:

- Establishing a strategic alliance, in which buyer and supplier each contribute and share complementary strategic capabilities over the long term.

- Using tiered sourcing, in which the buyer identifies a set of first-tier suppliers to act as integrators, managing the second-tier suppliers. This model can effectively organize a complex supplier landscape; however, it requires the buyer to find the best structure for each situation.

- Committing to supplier development, in which the buyer seeks to enhance a selected supplier relationship through investment, volume guarantees, exchange of know-how, initial price premiums, or other measures.

- Working on a project-based partnership, in which the collaboration has a defined period of time or scope of activity, such as development of a new product.

Despite the value of these approaches, our research indicates that companies lack a structured process for implementing them. Only 20 percent of respondents to A.T. Kearney’s Key Supplier Collaboration Survey (2009) stated that they had a systematic process for collaborating with suppliers.

A Two-Phased Approach to Collaboration

What does such a systematic process look like? As demonstrated in Exhibit 1, it has two phases. It is also best approached as part of a holistic effort at Collaborative Value Creation across the entire value chain. (See accompanying sidebar on Collaborative Value Creation.)

In the first phase of key supplier collaboration, the buyer prepares by analyzing its suppliers and operations. Because companies should collaborate only with a select group of strategic suppliers, it’s important to first segment the supply base to determine the best potential partners. As the figure shows, that segmentation asks which
relationships are most valuable and which inputs most critical or complex. But an equally important part of getting ready is conducting an internal assessment of the current operating model.

Companies need to ask themselves if they are capable of engaging the supply base in a collaborative manner. Who will interface with the supplier? Are appropriate communication channels in place? Are there internal obstacles that would prevent the relationship from creating value?

Once these questions are answered, the second phase implements the collaborative relationship. Depending on objectives, the buyer may engage the supplier on a one-to-one basis (the supplier-centric approach) or use a community approach around a theme. The supplier-centric approach draws on a deep understanding of the mutual importance and value of the relationship. The buyer proceeds by first analyzing the relationship, then developing objectives and strategy, and finally engaging the supplier to develop objectives for mutual value generation. Conversely, the community approach targets several suppliers at the same time. For example, a buyer may work with transportation suppliers to reduce carbon footprint by addressing truck idle time and back haul opportunities.

Creating Mutual Strategic Value
Companies have found that successful key supplier collaboration programs yield benefits including:

- **Growth**: Innovation is often the key to growth, and the flow of innovation to both products and processes can improve when a company’s key suppliers are intimately involved. Growth also comes from improving the value proposition for existing customers.
- **Risk Management**: Supply constraint scenarios can pose risks, but mitigation powered by collaborative supplier relationships can secure continuity of critical supplies. In fact, it can even turn those risks into opportunities to gain advantage over competitors.
- **Value Chain Optimization**: All companies have different advantages and core competencies. When suppliers and buyers build trust through collaboration, they may find that they can line up their respective advantages to reduce redundancy.
- **Structural Capabilities**: Key supplier collaboration can improve other dimensions of competitive advantage, such as cost, agility, responsiveness, scalability, or corporate social responsibility.

By taking a holistic approach, the partners have created value that is both mutual—accruing to both buyers and suppliers—and strategic—making an impact in the areas most critical to long-term success.

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**Collaborative Value Creation**

All businesses work as both customers and suppliers; all businesses are simultaneously competitors and potential alliance partners. So as value chains undergo rapid changes—including spreading across numerous geographies and markets—effective relationship management becomes increasingly important. In other words, partners become more important in generating value.

Opportunities exist to reach out both tactically and strategically, with both suppliers and customers:

- **Most businesses are familiar with supplier relationship management (SRM), in which a company seeks to maximize the value contributed by its suppliers.**
- **A more strategic approach is key supplier collaboration.**
- **Think of customer relationship management (CRM) not as technology, but as the downstream equivalent of SRM, maximizing the value of the customer landscape.**
- **Key customer collaboration similarly applies a more strategic perspective to CRM.**
- **All of these efforts are linked to key partner management, the company’s core principles for managing relationships with the parties it is closest to.**

Implementing these linked approaches helps companies create more value by collaborating more effectively along the entire value chain.