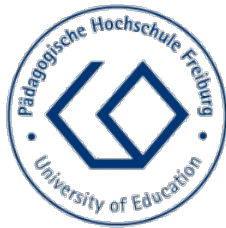


Supplier Relationships



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Learning Objectives

After this lecture students should be able to:

- Apply the network theory to the business environment
- Describe the role of relationships in business
- Explain how business relationships are developed over time
- Differentiate factors that impact supplier relationships
- Explain the role of trustworthiness in supplier relationships
- Outline the structure of fashion supply chains

Network Theory

No company is an island!

- Markets are constituted of networks: economic activities are embedded in social networks
- Companies are not isolated but embedded and connected through relationships with other units or actors, which they exchange knowledge, goods or information with
- Mutual dependency: the company is not able to implement a certain strategy completely independent but needs to consider other opinions

Network Theory

- A network consists of a set of actors or nodes along with a set of ties of a specified type (such as friendship) that link them
- The ties interconnect through shared end points to form paths that indirectly link nodes that are not directly tied
- The pattern of ties in a network yields a particular structure, and nodes occupy positions within this structure
- Networks present essential conduits of information and know-how and provide firms access to useful information and resources

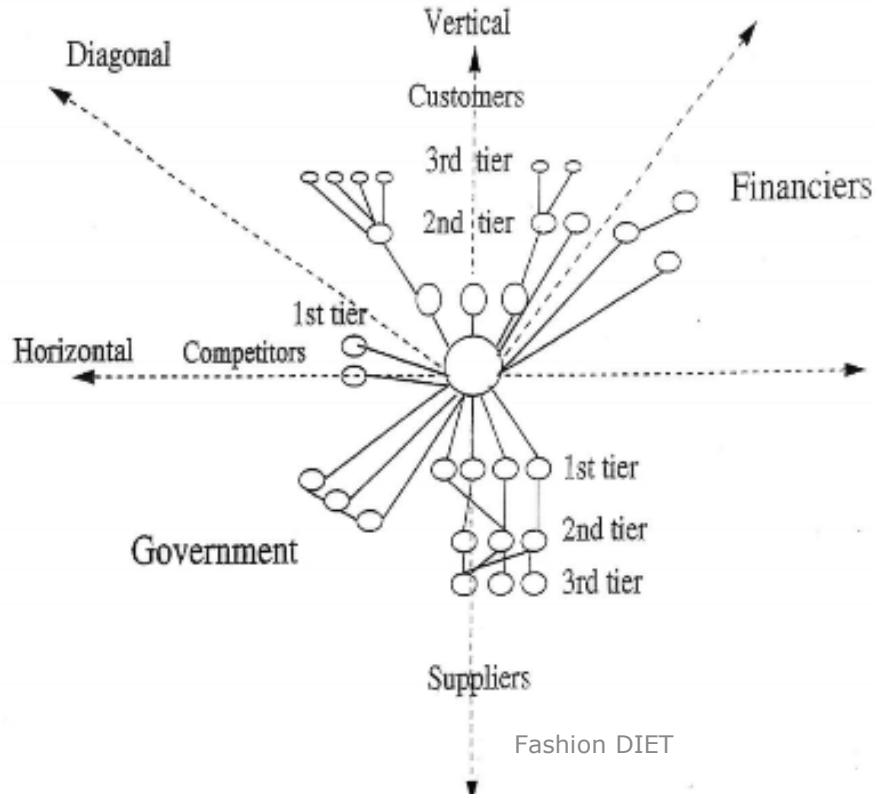
Network Mapping

- Network mapping helps companies to cope with relation complexity
- It illustrates the relationships of the different parties within the environment of the respective firm
- Helps to identify the different and the most important linkages and nodes



- Contributes to building awareness of the company 's position, embedded in a complex environment of dependencies and relationships
- Looking at an illustration of its network will make it easier for a company to set the scope of its strategy and enable them to focus marketing efforts

Network Mapping



Network Mapping

Three dimensions branch off either side:

- The *vertical dimension* includes customers, suppliers and consultants
- The *horizontal dimension* takes up major competitors
- The *diagonal dimension* covers financiers and government

All dimensions can be divided into different *tiers*:

- Direct relationships between the company and external parties are clustered in the *first tier*; includes linkages with customers, suppliers, competitors, governments, financiers, internal units

Network Mapping

- All direct essential relationships are allocated in the first tier
- The *second tier* comprises indirect relationships of the company (e.g. the suppliers' suppliers)
- The *third tier* might be found or not: This is a decisive point when drawing a network map → the network is too huge to be entirely covered
- A reasonable limitation needs to be set to remain clear and handy

Network Density

- Each network is characterized by a potentially varying *network density*
 - *Network density* describes the degree of interconnection among the various parties within the network
 - A high degree of interconnection sets a higher density
- it represents the strength of relationship between the different nodes

Relationships in Business Networks



Overall Relationships and Individual Episodes

- Complexity of buyer-seller relations and importance of mutual adaptations → the analysis of relationships must be separated between the overall relationship itself and its individual episodes
- Every product delivery, price negotiation or social meeting takes place within the context of the overall relationship
- Every episode is affected by the norms, atmosphere, conflicts and procedures of the relationship

Ford (1980), p.341

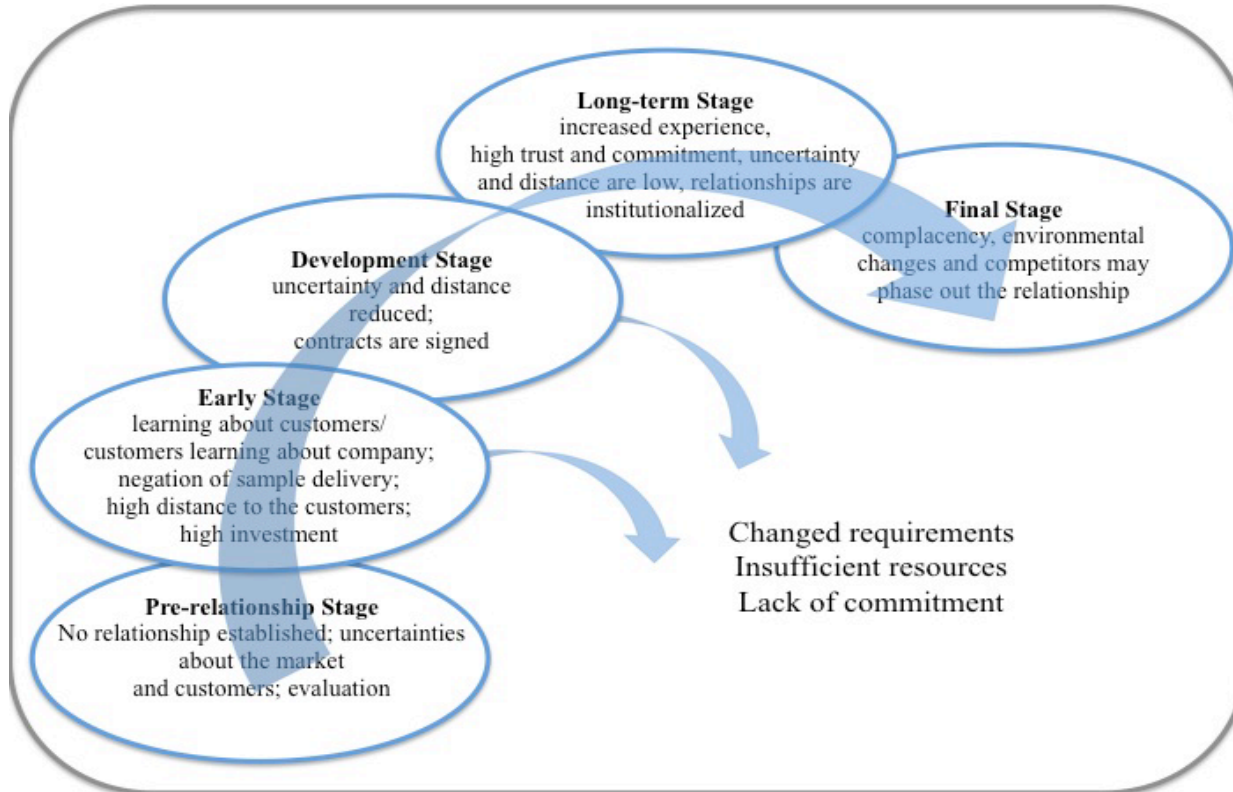
Overall Relationships and Individual Episodes

- Each episode affects the overall relationship → a single episode can change it radically, e.g., a relationship can be broken off because of a single failure in delivery
- It is important to analyze both individual episodes and the overall relationship to understand the interaction between the two

The Development of Buyer-Seller Relationships

- The process of establishment and development of relationship over time can occur in different stages in their evolution
- The stages are dependent on factors related to experience and learning: reduction or increase of uncertainty and commitment between both parties
- All steps are followed subsequently over time
- BUT: establishing relationships is not an inevitably developing process:
 - There is no certainty to evolve and proceed to the next stage
 - Failure or regress of development might occur

Relationships in Business Networks



Modified from Ford (1980)

Stage 1: Pre-relationship stage

- The evaluation of a potential new supplier will take place without any commitment to that supplier at this stage
- It is conditioned by three factors: *experience, uncertainty, distance*
- Experience in existing and previous relationships provides the criteria by which the potential and performance of a new partner is judged



With a partner of which the company has no experience, it will face uncertainty about the potential costs and benefits

Stage 1: Pre-relationship stage

- Costs for making a change to a particular partner
- Opportunity costs involved in the continuing relationship, when compared with alternative partners, e.g., in a buyer having to accept less frequent deliveries
- The distance which is perceived to exist between buyer and seller has several aspects (see next slide)

Stage 1: Pre-relationship stage - Distance

- *Social distance*: the extent to which both the individuals and organizations in a relationship are unfamiliar with each others' ways of working
- *Cultural distance*: the degree to which the norms, values or working methods between two companies differ because of culture
- *Technological distance*: the differences between the two companies' product and process technologies
- *Time distance*: the time which must elapse between establishing contact or placing an order, and the actual transfer of the product or service involved
- *Geographical distance*: physical distance between the companies' locations

Stage 2: The Early Stage

Time to negotiate or develop a specification for a purchase

Experience

- At this early stage in their relationship, both buyer and seller are likely to have little experience of each other
- They will only have a restricted view of what the other party requires of them, or even of what they hope to gain from the relationship

Stage 2: The Early Stage

Uncertainty

- Human resource investment will be made at a time of considerable uncertainty, when the potential rewards from the relationship will be difficult to assess and the pattern of future costs is undetermined

Distance

- There will have been little opportunities to reduce the distance between the parties at this early stage in their dealings

Stage 2: The Early Stage

Social distance

- Absence of personal relationships between the individuals involved
- Judgements made of each company will be on their reputation

Geographical distance

- Beyond the control of the seller
- Can be reduced by the establishment of a local sales office or by sending staff out to the customer on a residential basis

Stage 2: The Early Stage

Cultural distance

- Can be reduced by employment of local nationals
- Potential lack of trust between the companies, e.g. a supplier may believe that he is simply used as a source of information
- The distrust of an individual supplier can cause a purchaser to place emphasis on cultural stereotypes — e.g., a customer may attach importance to the alleged "discipline" of German suppliers / "undisciplined" British suppliers

Stage 2: The Early Stage

Time distance

- At the beginning: agreements/transactions which may only come to fruition at some considerable time in the future



- Maximizes the buyer's concern whether he will receive the product in the specified form/at the promised price/time
- Similarly, the seller will be concerned as to whether orders being discussed will ever materialize in the way it expects

Stage 2: The Early Stage

Commitment

- Both companies will be aware of the risks and will have little/no evidence on the partner's commitment
- Commitment of both parties might be low at this time



Commitment is strongly influenced by factors outside the relationship (e.g. number/importance of its other customers or suppliers)

Stage 3: The Development Stage

The development stage of a relationship occurs as deliveries of continuously purchased products increase

Experience

- Increasing experience between the companies of the operations of each other's organizations
- The individuals involved acquired knowledge of each other's norms & values

Stage 3: The Development Stage

Uncertainty

- Uncertainties in the relationship are reduced by experience
- The adaptations required to meet the wishes of the partner company will have become more apparent and the costs involved in these adaptations will also become clearer
- Each company will be better able to judge the adaptations to meet its own requirements: includes those made by itself and those which it should require from its partner

Stage 3: The Development Stage

Social distance

- Reduced by the constant social exchange
- Increasing of each other through personal relations → trust

Geographical and cultural distance

- The seller company may reduce geographical/cultural distance through the establishment of a local office employment of locals

Stage 3: The Development Stage

Technological distance

- The adaptations reduce the technological distance between them
 - Their respective products, production and administrative processes become more closely matched with each other
 - Savings for one or both parties

Stage 3: The Development Stage

Time distance

- Time distance between negotiation and delivery is eliminated in the case of continually delivered products
- In the case of irregular purchases of each cycle of order and delivery can be marked by similar time distances

Commitment

- It is not possible to put a timetable on the process by which a relationship reaches the long-term stage → reached after continuously purchased products have occurred

Stage 4: The Long-Term Stage

Experience

- The considerable experience of the two companies in dealing with each other leads to the establishment of standard operating procedures, trust, and norms of conduct
- Prices are negotiated on an annual basis

Stage 4: The Long-Term Stage

Uncertainty

- Uncertainty reduction can create problems: “institutionalization”
- It is possible that routine ways of dealing with the partner will cease to be questioned by this stage
- Institutionalized practices may also allow a company to drift into overdependence on a partner or incur excessive costs in its dealings
- One company may exploit the other's institutionalized practices and lack of awareness → reduce its own costs at the expense of the partner

Stage 4: The Long-Term Stage

Social distance

- Minimized in the long-term stage: An extensive contact pattern will have developed between the companies
- Strong personal relationships developed between individuals in the two companies → it may be difficult to separate personal relationships from the business relation
- Interactions by the different functions may become separated: e.g., the technical problem solving between a supplier and its customers can be separate from the commercial transactions which take place
- Can lead to problems of coordination and control if different departments are not to work in conflict with each other

Stage 4: The Long-Term Stage

Technological distance

- Successive contracts and agreements between the companies lead to extensive formal adaptations → motivated by cost reduction for both companies

Commitment

- It is likely to be difficult for a company to balance the need to demonstrate commitment against the danger of becoming overly dependent on that client
- A customer's perception of a supplier's commitment to a relationship may differ from the actual level: because the required investment of resources has largely been incurred before the long-term stage is reached

Stage 5: The Final Stage

This stage is reached in stable markets over long periods of time

- Marked by an extension of the institutionalization process to a point where the conduct of business is based on industry codes of practice
- These may have relatively little to do with commercial considerations, but correspond more to a "right way to do business", e.g., the avoidance of price cutting and restrictions on changes

Companies should examine their existing relationships to see which of the stages described here they fall into:

1. What is the likely potential of this relationship?
2. What resources are required to fulfill this potential?
3. Where do the threats to this development come from?
4. Where does this relationship fit within the context of the company's overall operations and resource allocation in that market?
5. Are the current efforts devoted to the relationship appropriate to this overall strategy?
6. Are we overcommitted to this customer?
7. Are our ways of dealing with this customer appropriate both to its needs and our strategy or are they dealings based on habit or history?

Trustworthiness

- One way to develop and maintain mutual, long-term relationships through the social linkage within the company's relationship network is based on *trustworthiness*
- Of high importance throughout the entire process and considered crucial for a successful business relationships
- “Trust is the mutual confidence that no party to an exchange will exploit another's vulnerabilities” (Barney, 1994, p.176)
- Trustworthiness refers to the particular action one side expects from the other side

Trustworthiness

- Trustworthiness takes place within the relationship between an individual and an organization
- It is, e.g., reflected by a company's belief that the customer will meet his payment obligations or a buyer's confidence in the promised quality or delivery on time
- When trust exists, uncertainty is reduced and individuals are more willing to share resources and collaborate
- Creating trust between partners is therefore a distinctive governance mechanisms that undergirds the establishment of network ties
- Trust may evolve from an cognitive or emotional direction

Trustworthiness

Cognitive trust

- Arises from an accumulated knowledge that allows predictability and reliability that the partner will meet his obligations
- It is rather formal and instrumental than emotional

Trustworthiness

Affective trust

- Trust that is rooted in human emotions
- Based on friendship, sympathy or affiliation to a particular (social or cultural) group
- Occurs if individuals feel genuinely concerned for their partners' welfare; are personally and emotionally involved into the relationship
- Implies that network ties are “relationally embedded” which means that they are embedded within social relationships

Supplier Relationships in the Fashion Industry



Global Apparel Supply Chains

- Global sourcing gained increasing attention during the early seventies when the advantages of offshore production have been realized, particularly in terms of costs as the most dominant driving factor
- **Outsourcing** = Arrangement between a company and its independent supplier to manufacture components or to provide services according to defined specifications
- Single or multiple steps of the manufacturing process can be transferred to a foreign contractual partner: Pre-production, final production, refining or complete production

Global Apparel Supply Chains

Benefits: Cost savings – especially in labor-intensive production processes in low-wage countries; savings in taxation, lower energy costs; raw material; Concentrate on core competences (e.g. product design, marketing, etc.)



Different integration levels of sourcing resulting in global sourcing strategies that involves worldwide geographically fragmented locations

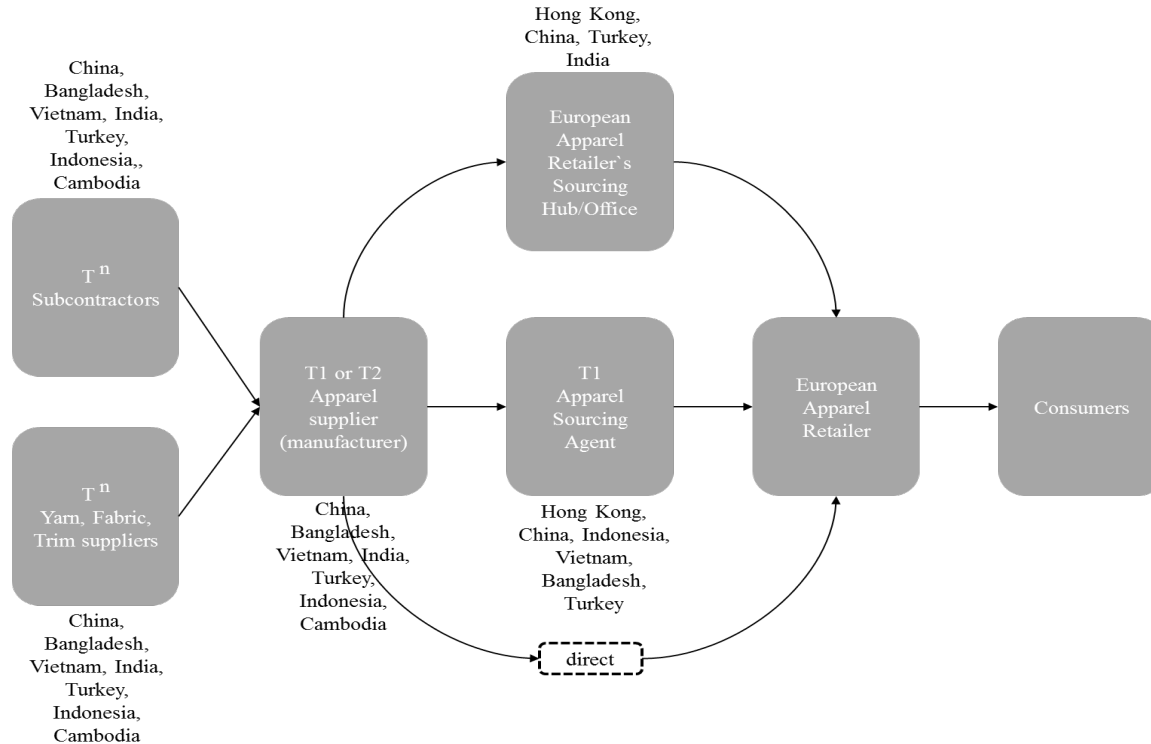
The operationalization of global supply chain networks comprising multi-tier suppliers (first- and lower tier suppliers) is a highly challenging task and needs strategic management actions

Global Apparel Supply Chains

In practice, apparel retailers approach their outsourcing and offshoring activities in three ways:

- direct sourcing,
- sourcing intermediaries,
- or sourcing hubs

Global Apparel Supply Chains



Global Apparel Supply Chains

- Lower-tier suppliers are considered being less responsive for social and environmental issues and have weak relationships with the downstream supply chain
- Due to the complex and long supply chains there is a substantial lack of visibility as they indicate that apparel retailers might even not know the suppliers who manufacture their garments what can induce considerable social risks such as the use of child labour

Social SSCM

- in order to achieve compliance with social standards, five main supplier practices are suggested that retailers should make use of:
 1. supplier evaluation and selection,
 2. supplier communication,
 3. supplier auditing,
 4. supplier development,
 5. supplier monitoring.

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