

**Transforming an Adversarial Relationship**  
by Frank Smeekes and Reid Wilk

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# Transforming an Adversarial Relationship

A survey of automakers and their suppliers unearths the management prerequisites for working together profitably.

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**T**he U.S. and European automobile industry is in the midst of a critical period in its history. Margins continue to decrease; for many, legacy costs such as debt service, pensions, and health care remain an ongoing burden. Volatility in the commodities markets is making cost management difficult at best. Competition has increased, not just from such established Asian manufacturers as Toyota and Honda but from new market entrants such as Tata and Chery. At the same time, however, there is extraordinary opportunity: Research and development efforts in alternative fuels and high-performance materials are reaching a critical mass as the globalization of markets and of the supply chain offers a wider range of possibility for purchasing and sales.

Taking advantage of these opportunities and overcoming these challenges requires a healthy relationship between manufacturers and suppliers. This relationship is the root of innovation implementation, quality targets, and cost control. Furthermore, many of the industry's opportunities can be exploited only if manufacturers and suppliers work in concert, making "big bet" investments in research, infrastructure, and markets and sharing advanced technology. However, the manufacturer-supplier relationship is beset by a great deal of friction, the result of decades of mistrust between

historically unequal partners. That friction has increased in recent years because of lower margins and greater market pressure; indeed, some manufacturers that were once praised by suppliers for evenhandedness have recently adopted a more aggressive approach.

To determine the elements of a successful manufacturer-supplier relationship and the skills needed by leaders working toward or sustaining such a relationship, Booz & Company joined with executive search firm Russell Reynolds Associates to conduct 43 in-person interviews of senior executives at nine major manufacturers and 19 leading suppliers in the United States and Europe. Included in this survey were companies such as Ford, BMW, Volvo, and Mercedes on the original equipment manufacturer side, and BorgWarner, Visteon, Lear, and Johnson Controls among the suppliers. These interviews covered the nature of the arrangements between automakers and suppliers, how their relationships have changed over time, and areas in which their partnerships have worked and where there was room for improvement. An analysis of those interviews produced a clear view of the characteristics of a high-performing relationship, the environment necessary to sustain it, and the qualities needed in executives charged with implementing it.

Much of the discussion regarding the manufactur-

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er–supplier relationship in recent years has been framed in terms of two contrasting models. The first is the price-based sourcing relationship, which has traditionally dominated in the United States. Here, the manufacturer calls for competitive bids on the desired goods in an effort to get the lowest price for components and materials that meet the specifications it set. Suppliers, in turn, look to meet exactly those requirements at the highest price they can command — and recover what they give up in price concessions by charging aggressively for design changes. There is little motivation for either side to collaborate or share knowledge.

In contrast, the second model — relationship-based sourcing — is centered on collaboration. This model is the favored approach in Asia, where it integrates naturally with lean manufacturing and just-in-time supply chain management. Suppliers and manufacturers work together to develop ways to provide components and materials more cheaply and share knowledge to foster innovation. The supplier receives a price that reflects a profit margin both sides agree to, as well as incentives for product improvement and further cost reduction. Although the supplier has less autonomy over its bottom line, it enjoys a steadier and more secure business partnership.

The survey found that, in general, most automakers and suppliers prefer the relationship-based model over the price-based approach. Apparently, they are drawn to the potential value of close, interwoven — and sometimes interlocked — relationships with their partners. But at the same time, they acknowledge that the relationship-based model is difficult to implement. Hence, it often ends up a wish list item that recedes from possibility even as these companies may transform

themselves in other ways, such as by improving corporate governance and manufacturing efficiency.

The tendency to regard relationship-based sourcing as the superior model primarily comes from the success of Toyota and Honda, as well as a number of European manufacturers, in developing and perfecting it. But it must be remembered that Asian manufacturers often have a significant ownership stake in their suppliers, making direct comparisons difficult. Further, the relationship-based sourcing model has yet to be tested in an extended global downturn. In fact, in the current competitive environment, some automakers traditionally identified with the relationship-based sourcing model have begun to implement the profit improvement targets usually seen in price-based sourcing.

To a certain extent, a company's choice of relationship model depends on its underlying company culture and how it perceives itself in the marketplace. Correctly or not, a company whose financial back is to the wall may not see itself as having the “luxury” of adopting a more collaborative approach. Taking a price-based approach may in fact be a rational choice, if one is in a position of strength or dealing in commodity goods. Such an arrangement, however, may not be optimal in the long run or even sustainable, especially if fortunes shift.

Manufacturer–supplier relationships are more fluid and less rigidly defined today than they once were. Some companies opt for a middle ground that acknowledges the possibility that collaborative relationships may become more adversarial (when focused, for example, on commodity goods); in companies that take a zero-sum approach, pockets of collaboration can emerge between manufacturers and suppliers. This evolving

middle path, known as “co-opetition,” involves companies moving deliberately among competition, collaboration, and its various hybrids as the situation demands, but always with transparency and an eye on protecting the long-term relationship.

Survey respondents identified the elements they prized the most and the areas needing improvement in their manufacturer–supplier relationships. From these responses, we identified eight relationship best practices that apply no matter which model is used.

#### **1. Securing commitment from the top.**

Establishing and maintaining a high-performing relationship between manufacturers and suppliers requires commitment from the CEO and senior management to trust and transparency, and assurance that the purchasing and supply leaders have the authority, people, and resources to perform as required. The CEO must communicate by word and action that behaviors that impede a high-performing relationship with business partners will not be tolerated.

**2. Creating alignment.** Partners share information more readily with manufacturers when they perceive their interests to be linked by growth opportunities.

#### **3. Recognizing the value of a good relationship.**

Good relationships have a real impact on the bottom line and are nurtured like the assets that they are; the cost and effort of maintaining them is seen as an investment rather than as an expense.

**4. Establishing clarity of purpose.** Understand what can and cannot be accomplished in the relationship. Manufacturers, for example, can't look to suppliers to erase their legacy costs.

**5. Understanding the other side's business.** The innovation that comes from true knowledge sharing can't take place unless each team has the technical expertise to roll up its sleeves and work alongside the other.

**6. Streamlined decision making.** Each side must have one accessible person who is in charge of the relationship both externally (to maximize responsiveness) and internally (to foster cross-functional communication between departments and teams).

#### **7. Getting beyond the transactional.**

Manufacturers should realize that suppliers are eager to work with them to tackle complex problems, from reducing supply chain costs to achieving sustained excellence in areas that reinforce the brand message. Each side should challenge the other to think beyond conventional solutions and methods and to break down siloed thinking.

**8. Codifying the relationship.** Establish a knowledge management system and bilateral action plan that ensures the relationship survives beyond the involvement of current participants. This should include instituting agreed-upon key performance indicators for assessing the state of the relationship, identifying areas for improvement, and establishing protocols to maintain open communication and transparency. Setting priorities will also encourage thinking with a long-term horizon and help keep parties from reverting to old behaviors when times get tough.

Our survey of automotive manufacturers and suppliers reveals both opportunities and challenges for an industry in significant need of new thinking. Both sides are dissatisfied with the status quo. The conditions and best practices that characterize high-performing relationships are clear and achievable, and it is possible to identify the qualities needed in executive leadership on both sides to achieve that change. +

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## Resources

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Ronald Haddock, Michael Pfitzmann, and Reid Wilk, “Knowledge-based Sourcing in China,” *s+b Leading Ideas Online*, 10/14/08: How structural shifts in China's economy are forcing companies to adopt more personal strategies for supplier relationships. [www.strategy-business.com/li/leadingideas/li00097](http://www.strategy-business.com/li/leadingideas/li00097)

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