NEGOTIATING WITH SUPPLIERS FROM A POSITION OF STRENGTH

REPRINT OF 2010: RISING COMMODITY PRICES
NEGOTIATING WITH SUPPLIERS
FROM A POSITION OF STRENGTH

Suppliers have a natural informational advantage when it comes to understanding and exploiting rising raw material costs to push through increases in product prices. Most retailers feel themselves lacking in good arguments and consequently unable to counter supplier demands effectively. Some, however, have developed the skills needed to fight back.

Currently many commodities markets are following a steep upward trend. Retailers are being confronted with scores of cost increase demands from their suppliers – while the ability to pass these increases on to the consumer remains as limited as ever. In addressing this challenge, retailers need to ask themselves a few important questions:

Does your supplier’s argument really make sense or is he intentionally hiding something? Is your supplier saying different things to different people, for example reporting EBIT improvements to the investor community due to input cost savings while at the same time asking you for more money? Are the cost increase demands actually in line with the importance of the raw material as a proportion of total product cost?

The exhibits show just one example of how better information and some homework can help fend off or mitigate unjustified price increases. Given the increased volatility of many commodities markets, retailers must do everything they can to gain an edge in commodity-related negotiations. While this does mean extra homework and analysis, it does not require investment or increases in headcount. In our experience, four things suffice to get the job done:

- Access to up to date and comprehensive raw material information, centralized in a company data base.
- An analysis of the most important commodities per supplier and category and an estimate of product cost structures.
- Automated calculation of list-price development over time, normalized for mix and other relevant effects.
- A software tool with an easy to use-interface that allows buyers to view and integrate supplier and cost information.

Retailers must do everything they can to gain an edge in commodity-related negotiations.
Paper product supplier demands a price increase of 10% based on soaring pulp cost

Retailer reply: Supplier owes the retailer money. Pulp is only a portion of his total product cost and in the last quarter pulp has reverted to historic levels following an extended downturn

Index: Last commodity-driven list cost change as starting point (beginning of 2008)
ABOUT OLIVER WYMAN
With offices in 50+ cities across 25 countries, Oliver Wyman is a leading global management consulting firm that combines deep industry knowledge with specialised expertise in strategy, operations, risk management, organisational transformation, and leadership development. Oliver Wyman is part of Marsh & McLennan Companies [NYSE: MMC].

In the Retail practice, we draw on unrivalled customer and strategic insight and state-of-the-art analytical techniques to deliver better results for our clients. We understand what it takes to win in retail: an obsession with serving the customer, constant dedication to better execution, and a relentless drive to improve capabilities. We believe our hands-on approach to making change happen is truly unique – and over the last 20 years, we’ve built our business by helping retailers build theirs.

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