"THE RELEVANCE OF BEING A ‘PREFERRED CUSTOMER’ IN ORDER TO ACCESS INNOVATIONS FROM SUPPLIERS"

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UNIVERSITY OF TWENTE.
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LECTURE PRONOUNCED AT THE EVENT OF INAUGURATION AS PROFESSOR OF TECHNOLOGY MANAGEMENT – INNOVATION OF OPERATIONS

AT THE FACULTY OF MANAGEMENT AND GOVERNANCE AT THE UNIVERSITY OF TWENTE IN ENSCHEDE, THE NETHERLANDS, ON NOVEMBER 25TH, 2010

BY

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Mijnheer de Rector Magnificus, beste collega’s en studenten, dames en heren. Het is een bijzonder plezier voor mij om hier te staan ter gelegenheid van het aanvaarden van het ambt als hoogleraar “Technology Management - Innovation of Operations”. In het bijzonder wil ik graag het College van Bestuur van deze universiteit en de benoemingsadvies-commissie danken voor het vertrouwen dat ze in mij stellen.

Since many of the present audience does not speak Dutch as their first language, I think we should continue in English! I would now like to present my inaugural lecture as chair of “Technology Management – Innovation of Operations”.

This space has seen different types of inauguration lectures before me. For example, colleague Petra de Weerd-Nederhof had a presentation closely linked to this place – Twente – where she has spent most of her professional life. Rez Kabir presented a different “oratie” showing the breadth of his field, finance. Today, I shall try to do something different again, going into depth into one particular problem in the area my chair covers, which is the idea of being a preferred customer.

But before elaborating on the topic of preferred customer, I will first briefly define the chair of technology management and – since I do not come from Twente – explain a bit about my academic origin.
I have been working in industry and as a consultant for 10 years: Dresdner Bank, Preussag / TUI, PricewaterhouseCoopers Consulting / IBM and h&z business consulting and their respective clients were the firms I joined. What concerns the universities I have studied at the University of Maastricht and at Leibniz Universität Hannover, where I also earned my dissertation and my habilitation. Later I have been at Jacobs University in Bremen. For me it is very important to combine practical application with a very high level of academic research. For that reason I pursued getting the "habilitation", i.e. the "venia legendi", the right to teach. Getting the second degree after the promotion is the traditional German requirement to become a full professor. The wish to combine relevant with academically high quality research is also why I opted to go to a research university, the University of Twente.

Throughout many years, combining work as a consultant with academic work meant that during many weekends and evenings I was writing papers and planning surveys. This is the moment for addressing my wife and family: Without their support and acceptance of these activities I would never have had the chance to be standing here. My heartfelt thanks to them!

On my arrival in Twente about one year ago, I was entrusted with the coordination of the new study program: “International Business Administration – IBA”. Again, we tried to implement this same idea of practical application in combination with a strong scientific foundation.

For example, we implemented the “business club” and spoke with these firms about their requirements for university education, visiting many Dutch and German firms. One such requirement was that the students must have the time to run a long internship of more than two months. This is a requirement which a normal “Bologna-curriculum” is no longer able to match. Therefore, we have developed a study plan in such a way that students can take such a long internship. It is also worth mentioning
that our students will have chosen a specialization in a particular function before doing their obligatory internship. In this way they are likely to be well equipped to integrate into a firm. This is a message for the firm representatives among us: please welcome our students! I do genuinely believe that we have created a world-class program here.

Now, let’s move to the chair of Technology Management.

What is the meaning of “Technology Management - Innovation of Operations”?

The word “technology” has two meanings. According to the dictionary it can either mean “method” or it can denote an “industrial transformation process”.\(^1\) We chose the latter as relevant here.

What is management? The origins of the word are Latin, one interpretation being that it comes from “mansionem agere”, which means to care for the house in the absence of the owner.\(^2\) This is a very good description of management and clearly separates “management” from, for instance, “entrepreneurship”, where the owner is identical with the person executing the task.

In a more modern interpretation I would like to highlight that “Management is the art of replacing chance by probability.” Everybody can – with luck – have one good idea and even become rich through it. Still, such a person is not necessarily a good manager. A manager is able to repeat success by applying a set of skills and tools. These are taught at a good university. However, we have to acknowledge that we cannot program success; but we can increase the probability for it to happen.

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\(^1\) See Müller / Köster / Trunk / Dudenredaktion (1982).

Coming to the second part of the name of my chair, “innovation of operations”, what does this mean? For innovation, the best description may be still one of the oldest, the one from Schumpeter: new combinations. And what is “operations”? In a modern interpretation, operations is comprised of three parts: purchasing, production and logistics. All of these represent the transformation process of raw materials or components into finished products.

Let’s have a look at the second part ‘innovation of operations’ a bit more in detail. Can we identify any trends? Let’s start with operations.

**Contrary to popular belief, production output in Europe is rising**

First of all, it may be worth noticing that industrial production is rising in Europe. These numbers may be evidence for the statement one hears from time to time that in our core industries there is hardly any product which cannot be produced at competitive prices in central Europe! US and UK authors may be overestimating the “service economy” a

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3 See Karlsson (2009).
little bit, reflecting the underaverage development in their countries, which, however, does not fully apply to us here “on the continent”. However, there is little dispute that one clear trend has emerged in the last two decades: Decreasing depth of production. Automotive firms illustrate the trend. They produce fewer and fewer components themselves and buy more and more components from their suppliers.

The trend towards outsourcing substantially changes the cost structure of a modern firm. Therefore, let’s have a look at the contemporary cost structure of a typical industrial firm. This exercise helps to define our future focus of work.

Imagine an automotive firm or an automotive supplier or a Siemens or Philips unit here. I took the data from that type of firm in the metal-electro industries. The profit margin is about 10% of the turnover. Margin varies per industry, but for instance with Siemens, it was
10.3% in the year 2009.\textsuperscript{5} Let’s assume a manager is exposed to a typical shareholder request to increase earnings by 5%, i.e. from 10 to 15%. How could this target be achieved? The manager can introduce more profitable products and hope that competitors will not erode profits away, again. Or that manager could reduce costs.

One of the things I have learned working as a consultant was first to visit the controller in the beginning of each project and ask for a cost break-down of the object at hand. Facing time scarcity, it is efficient to concentrate first on the largest influenceable cost block and develop ideas for its optimization.

Taking a cost block perspective in order to identify cost saving potential of an enterprise, it emerged that one big block of about 7% was comprised of overhead, costs of sales and financing costs. Just from an arithmetic perspective it becomes clear that this cost block can hardly deliver the 5% savings we are looking for. This does not mean that these cost blocks are not important – if the liquidity of a firm is not maintained, for instance, the whole activity has to be discontinued. But the target savings of 5% cannot be accomplished by innovations in that cost block.

Another large cost block is R&D. With the firms which I use to calculate this, the average R&D expenditure was 8.5%. There may be some room for increasing development efficiency and in theory that cost block could be cut in half and then we would have almost the required 5% savings. However, this is probably a very short term approach, considering that one third of the products in such firms are replaced every year. So that is also not a good option.

Now let’s come at the operations part. It is the largest cost block, responsible for about $\frac{3}{4}$ of the total costs. Which of its three elements - production, logistics and purchasing - is the largest part of operations?

\textsuperscript{5} See Siemens Annual Report 2009 (Profit in % of revenue, total sectors)
Remembering the trend towards low depth of production, it comes as no surprise that in such a streamlined firm production costs account for about 10 to 12% of the total turnover. Again, there is not so much savings potential left here. Logistics costs account for 1 to 2%. Sure, importing components from China, for example, may add up to 7% in logistics costs on these products, which is obviously a challenge requiring practical and academic attention. Also, if we were talking about retail, a different picture emerged. On the other hand, the supplier next door has hardly any transport costs. So again, we do not get our 5% profit increase out of reducing logistics expenses, either.

Fortunately for our manager desperately in search for 5% savings, there is one large cost block left. It is purchasing. In the example, 62% of the total turnover is directly handed over to suppliers. We have surveyed this extensively and it is rather reliable to posit that a modern industrial firm spends between 55% and 70% of turnover for purchased goods. Purchasing is by far the largest cost position within such a firm, and therefore it means that it also provides a good opportunity to realize 5% savings from this part.
All parts of operations are important and we will cover them. But based on the distribution of costs in a firm, it may be worth to explore more the supply side of the firm.

Fortunately, we are quite good at this in Twente! We have recently been named as one of only four “Academic Centres of Excellence” by the IPSERA (the International Purchasing and Supply Education and Research Association). I think this is quite good! We have to be fair, here international means: outside the United States. There are also some good American universities. Important: Twente finds itself already in a leading position, with members of the faculty of management and governance and other faculties being active in the field.

This includes Professor Jan Telgen, who leads a group working in the purchasing field with particular emphasis on public procurement and operations research applications in procurement, and Hans Voordijk from the building technology faculty, who works on supply management.
in the construction industry and with whom we are also collaborating. Purchasing, as a particular part of operations, is one of Twente’s strong points, making this university unique in Europe. And I believe we do have an excellent chance to strengthen this area even more.

That we have been named a “Center of Excellence” is no fluke. Our leading position has been confirmed recently at the latest annual meeting of the Academy of Management. With 8,000 participants it is arguably the most important conference in business administration in the world. The University of Twente has been nominated for both prizes the operations management division had to award!

One of these papers with a “best paper” nomination was on supply risk management, written together with Petra Hoffmann. She is a PhD researcher I supervise jointly with Koos Krabbendam. In collaboration with h&z consulting, where I have worked before, we had hosted a workshop attended by 15 firms. Subsequently we tested these findings with a large-scale survey. In essence, a process emerged, which can help firms to identify potential supplier failures three month earlier, i.e. twice as early as the common average before: a blueprint for practical relevance and academic excellence combined!

Coming back to the question of achieving a 5% profit increase, the purchasing volume of the firm emerged as a good candidate. So how can we reduce the purchasing costs? We conducted a secondary data analysis, evaluating 134 material cost-reduction workshops run by h&z consulting in industrial firms. During such workshops, cross-functional teams discuss and indentify costs savings.

I will not go into details of the analysis of the 7,000 hours of workshops – you can get more information from our forthcoming paper written

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6 See Schiele/Hoffmann (2010).
together with Philipp Horn and Bart Vos. The key finding was the following: The bulk of the costs savings came from innovation-oriented sourcing strategies!

Take as an example “product improvement”: Eliminating 100 g of metal from a component by redesigning it makes it cheaper because it is no longer necessary to pay for that 100 g of raw material. Such redesign is a typical exercise that is done in collaboration with the supplier who produces the component. This is not science fiction. But research has indicated that about no more than 10% of innovations are “new to the world” innovations, the rest mainly of such improving type.

Another aspect which our study made clear is that more traditional sourcing strategies like price oriented strategies or global sourcing are less promising. Global sourcing is a research project of my PhD student Philipp Horn. For instance, he analyzed almost 200 China-

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8 See Tidd / Bessant (2009).
sourcing projects, finding that year after year more than 80% of them fail. Even worse, our data reveal a trade-off between global sourcing and innovation with suppliers. So global sourcing is not very likely to be the strategy which delivers the 5% savings we are searching! Instead, research indicates that the bulk of cost savings with suppliers are derived from collaborative innovation.

The importance of innovation-oriented cost saving strategies connects well to the second part of the subtitle of my chair, i.e. the “innovation” in “Innovation of Operations”. Therefore, let’s have a closer look at innovation. How do innovations come about nowadays?

The strongest trend in the 1990s was the move from a closed to an open innovation model, which the panel study depicted here indicates and which can also be detected for the Netherlands. It is clear that innovations “happen” nowadays in close cooperation between

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9 See Poot/Faems/Vanhaverbeke (2009); Roberts (2001).
different firms, for instance manufacturers and their suppliers. The UK innovation survey assessed that suppliers’ contribution to innovation was about as important as customers’ contribution.\textsuperscript{10} We want to explore the supply side of innovation more in research and in teaching.

For instance, in the new double master in innovation management which the University of Twente is offering in collaboration with TU Berlin, I will be offering a new class on innovation with suppliers.

Allow me, at this point, to draw a short intermediate conclusion. We found that the largest cost block in a firm is purchasing. We further found that the largest savings potential in the purchasing volume of a typical modern industrial firm stems from innovation-oriented sourcing strategies. We then saw that innovation tends to appear in an open-innovation process which is often characterized by collaboration between buyer and supplier. In other words: in order to continue to reduce costs and stay competitive at the same time, firms may benefit from strengthening their power of innovation in a collaborative process with their key innovative suppliers.

Our previous research has revealed that no more than 5% to 10% of the (large) A and B suppliers of a firm fall into the “innovation” category.\textsuperscript{11} Then, what are the characteristics of such innovative suppliers? How do they look and how can a firm recognize them and distill them out of the multitude of suppliers they may have? We have done intensive research on the question of how to identify innovative suppliers which can subsequently be integrated as partners in the joint innovation process.

Five years ago we started an explorative research using a method of academic-practitioner research collaboration called “consortial

\textsuperscript{10} See Stones (2001).
\textsuperscript{11} See Schiele (2010b).
benchmarking”. We formed a research consortium with several firms interested in answering the question on innovative suppliers. Here are their names on the left. We then organized visits to “best practices” firms in order to learn from them how they recognized innovative suppliers. We visited each of these firms for two days. The single most relevant finding was the discovery of the importance of being a “preferred customer”.

Imagine the typical setting of a consortial benchmarking visit to a best practices firm, in this case to Leica Geosystems in Switzerland. There were 15 participants in the visit, including the heads of R&D and purchasing of the member firms of the research consortium as well as the academic delegates. We were at Leica, all in a single room, and asked their R&D and purchasing managers a series of questions about how they recognized innovative suppliers. The managers listed some criteria but in the end had to conclude that

12 See Schiele (2010); Schiele/Haas (2007); Schiele/Krummaker (2011).
good suppliers had sufficient R&D capacities, laboratories and all possible certificates, but that the same was true for the disappointing suppliers. There needed to be something more to explain why Leica was able to co-develop innovative solutions with one type of supplier and not with the other – at the first glance – similar type of firms.

In this situation, one of the Leica managers said “Apparently some of our suppliers simply seem to like us. That is why they collaborate with us!” His colleague seconded, adding: “And these good suppliers like us more than they like our competitors. This is the reason why we get their best engineers to work with us.” Someone from the consortium then said “You seem to be their ‘preferred customer’.” That is how the idea of being a preferred customer was born.

How could we preliminarily define the “preferred customer”? In general terms, a buying firm has preferred customer status with a supplier if the supplier offers the buyer preferential resource allocation. This can mean, for example, dedicating the best personnel to new joint product development projects, customizing its products, pro-actively offering innovations or even agreeing on an exclusive contract.13

In the old way of thinking, which did not emphasize co-developed innovation, suppliers were supposed to sell a finished product at a cheap price. From an innovation-oriented perspective it becomes clear that it is not that simple. For instance, we want to have the best people from the supplier working for us. Not the average employees – they can work for our competitors. The availability of talent in a firm follows a normal distribution pattern, though in a good firm it may present itself as right skewed. Still, suppliers need to make a choice and cannot assign employees to two projects at the same time. As a consequence, most

of the “right” part of the talent may work for the preferred customers, whereas the “left” part is occupied with serving the standard customers.

After the idea materialized and was corroborated during the remaining benchmarking visits, the next logical step in research was to test the new concept on a larger quantitative sample.

With a survey we wanted to substantiate the assumption that being a preferred customer explains a substantial part of supplier innovativeness. Supplier innovativeness, in this context, is defined as the supplier’s capability and willingness to collaborate in joint innovation projects and to offer innovations to the buyer.

We sent a survey to firms, asking them to select good and disappointing suppliers and to characterize them. The questionnaire covered the technical capabilities of the supplier and further contained questions on whether the firms had the perception of being treated as a preferred customer of the supplier or not.
These two variables together can explain an astounding 63% of the observed differences between innovative suppliers and those which are not. As necessary condition for supplier innovativeness it seems to emerge that the supplier has good technical capability. What is more important – and this seems to be a sufficient condition for a particular supplier to collaborate with us as a particular buyer – is that the supplier awards us as buyer with preferred customer status.

It may be fair to conclude that the concept of the preferred customer describes a real phenomenon with ample explanatory power and is thus worth investigating further.

For details, limitations and the other parts of the model I would like to draw your attention to our forthcoming paper.\textsuperscript{14} It was created together with our assistant professor Jasper Veldman and with Lisa Hütttinger, another PhD researcher I supervise. Lisa is financed by industry and is

\textsuperscript{14} See Schiele/Veldman/Hüttinger (2011).
investigating the question of how large firms can become a preferred customer of their key suppliers, i.e. how they can become more attractive than their competitors.

Why is it so challenging to become a preferred customer and why was this less of a problem in the past? This may have to do with the third – and last – trend I would like to discuss today, the trend towards supplier scarcity.

The number of suppliers is decreasing in many industries, such as we see here in the example of the automotive industry. At the same time – that is the black line in the next figure – notice that the suppliers’ role is expanding, for instance, as expressed by the share of patents registered.

The challenge: the gap is increasing. Fewer and fewer suppliers are available in the supply market and on average they are becoming more and more important. From a buyer’s perspective we are running into a problem: it is also more and more difficult – at the same time strategically more important – to become a preferred customer and to closely collaborate with any of them.

Please notice that we are not talking about a “new edition” of the often failed partnering approach popular in the early 1990s. The motives for close buyer-supplier collaboration this time are different. Twenty years ago collaborations often collapsed at the moment when the buyer identified an alternative supplier offering slightly lower prices. Today, there may not be such alternative supplier left. Collaboration becomes an imperative dictated by scarcity.

Can we look into the future? Sometimes, with a certain probability, we can, if there are places which have a good chance of anticipating

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15 See Verespej (2005).
trends. Is there such a place where we can study the reaction on supplier scarcity? The UK, which lost most of its industrial base, could be a case at hand. And in fact, there I was able to find the most cases of well-functioning partnering, still in place a decade after the fashion wave. In what is left over from the UK industrial base, tightly linked buyer-supplier pairs were left alone many times, sharing a common destiny, thus doomed to collaborate.

Is this trend true for all industries? Many of the examples presented here stem from the automotive industry, which often has trend anticipating character. What happens there first, usually spreads to other industries later. But: In business administration, as a social science, we cannot present universal truths. There may well be industries where the number of suppliers is actually increasing. In the absence of natural laws, each firm has to analyze for itself if they are facing supplier scarcity or not. One indication for that can be determined by calculating the share of the purchasing volume provided by suppliers that also serve the three largest competitors of a firm.
The Japanese character for “crisis” is composed of two elements: challenge and chance. The chance firms have at the moment is to establish themselves as a preferred customer with the few leading suppliers before their competitors do so and in this way achieve a competitive advantage. The example here is of a firm active in an industry with very short product life-cycles and which prefers to remain anonymous. In their key commodity group they are implementing a preferred customer strategy, once they analyzed that there were only three globally leading suppliers. They are working on securing the latest products of two of these suppliers at least two month earlier than their competitors.

Chance and challenge can be very close to each other, as the following example illustrates.\textsuperscript{16}

It’s about springs. Analyzing the springs market, there are three world market leaders producers of springs. One of them is located in the United States and two are located in Germany, about 30 km away from each other and both are part of the Sauerland metal manufacturing cluster. These firms, as well as the smaller ones, draw on two main suppliers which are the two technically leading steel companies in this field.

Steel is the most important component of a spring. It may not be difficult to imagine that with a better variety of steel, the properties of the spring would improve. Since the spring-producing companies “just” shape the raw material into the form they need, but buy the material from the steel mills, it is essential for them to have a good steel supplier, preferably the best of the world.

What happened in this case? A series of hectic activities started, when producer Alpha was able to hire a person from producer Beta.

\textsuperscript{16} See in the following Schumacher/Contzen/Schiele/Zachau (2008).
Arriving at Alpha, he brought news with him. He told them that his former employer was co-developing a new steel variety with supplier one, which was the common supplier to both Alpha and Beta. The only alternative technically leading supplier is located in Korea and in Alpha’s judgment that would not be a realistic alternative. Managers at Alpha then thought: “What happens if our competitor is indeed successful in co-developing this new steel variety? Then our common supplier will probably only supply this new variety to our competitor, at least for some time, such as already happened in the past. And then we do have a painful problem on the market!”

On a very short notice, and not without some slight nervousness, they got into two cars and drove down to their common supplier in order to convince him to co-develop with them a new type of steel variety, too. Fortunately (for the happy end of this case) they succeeded with this request and competitive parity was restored, again.
The R&D manager of manufacturer Alpha explained to me that their success had also to do with the fact that they already had some ideas about new steel varieties sitting on the shelf, but never got any OK from the board of directors to continue their development. Knowing that the competitor was doing exactly this, their board finally decided to engage in an open innovation process and co-develop a new steel variety with their key supplier.

For sure, the case of the spring producer is an extreme case, but generally firms may profit from
a) identifying their strategic suppliers,
b) assessing their competitiveness and
c) understanding if they are preferred customer with them or not.

We have developed an actionable method for conducting such an analysis. Those of you who have attended the keynote presentation by Frank Schöpke from Siemens Industrial Automation this evening have seen how it can be applied. Next to paving the way for successful early
supplier integration in new product development processes, a preferred customer analysis can also be used to prepare a supplier portfolio.\textsuperscript{17}

On the y-axis the “preferred customer” portfolio differentiates the status a firm has with its suppliers. A firm can either be a standard customer or a preferred customer. On the x-axis the competitiveness of the respective supplier is depicted. So, four quadrants can be distinguished. Ideally, a firm has a substantial number of suppliers in quadrant “II”, i.e. those which are highly competitive – the best of their kind – and which like to supply the buying firm and award it with preferred customer status. With them, a strategy for competitive advantage can be pursued.

The big problem arises with those suppliers placed in quadrant “III”: they are good, but do not consider us as buying firm their preferred customer. Either they are replaced or the firm manages to get preferred customer status. There are some pieces of evidence that several spectacular firm failures of the last years may need to be re-interpreted from a preferred customer perspective.

One case at hand is Fairchild Dornier, the small Bavarian-based manufacturer of airplanes. They were trying to develop a plane to directly compete with the Fokker 100, called 728. We were able to collect some evidences of a lack of preferential treatment by suppliers shortly before Fairchild Dornier’s collapse. They had asked to implement an electronic complaint registration system, in the hope to solve their supplier problems by making these suppliers’ poor cooperation transparent. However, with at least 10 out of 12 key suppliers for their new 728 Jet they had the impression of not being a preferred customer, rather these being typical quadrant III suppliers. With such “partners” it may simply not be possible to start such an innovative development project. In the end not only their largest project failed, but the entire firm went out of business.

\textsuperscript{17}See Schumacher/Contzen/Schiele/Zachau (2008).
There are more examples of similar failures, which I will not elaborate here. I do not want you to leave the room with a depressive feeling! Therefore, I will conclude with some positive reflections which show that it is possible for firms to become more attractive with their suppliers. However – attention – that story also starts with a problem statement. It is about the US automotive industry.

Consider this quote from 2005: “There are more and more signs that if the Big 3 [US automotive firms] don’t take a new approach to procurement, auto parts suppliers will shift more and more of their loyalties – and product innovations – to Japanese firms. In fact, it’s already occurring. A larger number of the new product innovations are now showing up on the vehicles of the non-Big 3 companies.”

So, if suppliers were co-developing innovations with other firms that was a serious problem for the US automotive manufacturers.

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**Assuming the trend for reliance on suppliers continues, the link between innovativeness and supplier relations gets stronger**

Feeding innovativeness former "Big 3" US automakers

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<td>• &quot;There are more and more signs that if the Big 3 doesn't take a new approach to procurement, auto parts suppliers will shift more and more of their loyalties – and product innovations – to Japanese firms&quot;</td>
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Here we see a recent cartoon. The press is already making a fool of the poor power of innovation of some American firms. The text says “General Motors presents the new electric car with an astounding range of 40 (!) miles.” It is an extension cord 40 miles long that provides the car with energy! It seems that the prediction of 2005 was not fully wrong...

The issue is: Why did this happen? Can we find support for the assumption that unsatisfactory supplier collaboration was one of the causes for poor innovativeness? And in case, can such a firm become more attractive for their suppliers, again?

Science up till now does not have a full range of answers to the question of how to increase customer attractiveness – without paying more money, of course. Fully understanding how to become a preferred customer is our next frontier in research. There are of course some ideas, such as testing the supplier’s new product versions, helping the supplier to get access to new markets, awarding it with a “last call” option in bids etc. Also supplier development – the buying firm investing resources in order to help the supplying firm to improve – seems to play an important role with firms wanting to become a preferred customer. This is what Agnes Blonska, who recently joined our university as assistant professor, found in her research on preferential customer treatment.

One neglected issue seems to play a pivotal role in achieving preferred customer status: supplier satisfaction. Achieving supplier satisfaction, as a pre-condition for getting preferred customer status, could well be the new arena of competition.

We see here the supplier satisfaction index elaborated annually in the United States.\(^{19}\) The index tells us quite clearly that automotive suppliers in the US on average did not like to supply the American

\(^{19}\) See Planning Perspectives Inc. (2010).
manufacturers and most likely did not send them the best people and the best ideas! The lack of preferential treatment may in turn offer some explanation for the poor power of innovation of the former “Big 3”. There may be, of course, a couple of other pieces of explanation.

And now there is a very interesting development going on in the moment: the ranking in the supplier satisfaction is changing! Some firms have been able to use the crisis of 2008 to improve their position, while others have deteriorated. Please observe the ascension of Ford, who is becoming increasingly popular with the supplier, even overtaking Nissan (Renault). Ford’s growth in popularity shows that supplier satisfaction can change and can be influenced and as such is a management task. With all due skepticism concerning this firm, this is a sign for optimism!

In fact, this type supplier satisfaction chart – concerning their particular industry – may have to be placed and discussed in the boardrooms of the future.
We even take up the challenge to understanding the mechanisms behind such developments and to provide indications for action not “only” for the large and famous firms we see here on display, but also for the small and medium enterprises. Our new PhD researcher Niels Pulles is working on this issue.

Based on the idea that supplier satisfaction is an antecedent to preferred customer status we can conceptualize the following relation: If the supplier is fully unsatisfied with a customer, i.e. the customer does not provide any value to the supplier, the latter may in the worst case discontinue the relationship. Being generally satisfied, the supplier may continue serving the customer, but a priori only treating him as a “standard customer”. If the supplier, finally, is more satisfied with this particular customer than he is with his other customers then he may award “preferred customer” status to that buyer. In other words, there is a strategic element involved.

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An interesting question arises which is of growing interest among researchers: Why and when, that is, under which conditions, are suppliers satisfied and how can a buyer achieve and keep supplier satisfaction? It is self evident that the assumption is not to pay commercially unviable prices. Costs that are too high would not be the basis for a sustainable business.

One way of approaching the question on why suppliers are satisfied involves expectations. Meeting the expectations a supplier has towards the business relationship with an attractive buyer may be a sufficient condition to achieve supplier satisfaction. And what is the necessary condition? First of all, the supplier needs to know the buyer and his requirements!

This statement may sound trivial, but it addresses one of the major issues in supply chains. Of course every supplier knows, for instance, a firm like Siemens. But does he know what requirements its unit Siemens IA AS has at this exact moment regarding the casting for a newly designed component with particular high temperature requirements, at the same time having a shape which is mountable with the available robots? 10 years ago, during the e-business hype, it was thought that this question could be positively answered. After the failure of the electronic market places we meanwhile had to realize that this is not the case.

We therefore argue that customer attractiveness, in the sense of a supplier knowing exactly what a (potential) customer needs and at the same time having a positive expectation towards supplying this part, is an antecedent to supplier satisfaction, which in turn is the condition for achieving preferred customer status, the ultimate aim.

Customer attractiveness is the third puzzle piece in our model. Here again, some early research has been conducted. Currently we are hosting a workshop which brings together key researchers working on customer attractiveness, supplier satisfaction and preferred customer-
ship in an attempt to systematize the state of the art and develop research plans for the future.

To round up: the conceptual model works as follows. A supplier identifies a customer which appears to be sufficiently attractive to enter into a business relationship or to extend the already existing relationship. Expectations are built. In the next step the exchange takes place. As a result, expectations are either confirmed or not and as a consequence the supplier evaluates his satisfaction. Assuming the supplier is more satisfied with this customer than with another customer, he awards the preferred customer status, which may of course not be a formal procedure. As a consequence, buyer and seller grow closer, jointly reduce costs, get more similar and the interaction intensifies. The supplier learns more about the buyer and his issues. A good previous experience increases the expectations for future business exchange even more: the customer appears to be even more attractive. If these expectations are fulfilled again,
satisfaction increases and the status of the buyer increases even more, and so on. Ideally, a cycle of positive reinforcement develops.

This is a first, tentative model, which we are discussing right now. It allows integration of existing research streams and in this way creates a research agenda. We still do not fully understand how many of its mechanisms work and in which way they can be influenced most effectively. One thing however we already know for sure is the following: Exploring the preferred customer paradigm effectively means inverting our perspective.

To sum up and to come to a conclusion: In the “traditional” perspective all effort was dedicated by the seller to convince the buyer. There were sufficient sellers. The oligopolisation of business-to-business markets, however, changes the rules of the game. Suppliers fade away, reducing the choice the buyer has. In this situation it starts to

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get important to understand what the other buyers are doing, because they are competing with us on the supply market for the few remaining world-class suppliers. In my experience, though, asking purchasers to describe the sourcing strategy of their competitors brings many of them into problems. This has to change!

And what happens now, if these competing buyers start an initiative to become more attractive with the suppliers? Please notice that the arrows in the picture have different directions.

Unless firms accept becoming second-class customers, waiting for deliveries, paying higher prices and giving up the aspiration of being leaders in innovation, firms need to react. The effort becomes to be an attractive customer. We may invert our perspective, figuring out how to coin supplier-buyer relations (not buyer-supplier relations).

Conceptualizing buyers competing for suppliers (rather than the other way round) is an exigent intellectual journey that we are starting now and
we welcome everybody to join. In order to systematically identify and explore knowledge and skill gaps, the “attractiveness cube” may be helpful.

One dimension of the attractiveness cube reflects the cycle-stage a business relationship can be in: either at the very beginning, i.e., building-up attractiveness, in the next step, where suppliers (and of course also buyers) evaluate their satisfaction with the relation, or at the “final” stage (in a circular model it may of course be difficult to speak of a beginning or an end), i.e., the buyer has been awarded preferred customer status and benefits can be seized.

The different categories of benefits (or value created) can be depicted as another dimension of the attractiveness cube. Depending on their strategies, firms may place more emphasis on some of the benefits, though, again, they may be interlinked. For instance, successful supplier development programs may, even if not primarily intended, generate innovations. Finally – from a research perspective – the level of analysis, representing the third dimension of the cube, can be distinguished. It has been argued that attractiveness and satisfaction depend on the mutual understanding and similarity of the individual actors on both sides of the supplier-buyer dyad (here depicted as micro-level). At the same time, the character of a commercial relationship between two firms is also influenced by the way how they see each other as a firm. For instance, the strategic (or commodity) character of the material sourced from a supplier influences the sourcing strategies, independent of the sympathy the respective employees may have for each other (meso-level). Finally, there are pieces of evidence that possibly also the country level plays a role (macro-level). It may be easier to become a preferred customer of a supplier located nearby than from a previously unknown supplier embedded in a different cluster on another continent.22 Off course, cross-cultural issues on a micro-level

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22 See Steinle / Schiele (2008)
may interfere here. Therefore, from a holistic perspective, it might be too narrow to only consider one single level. In order to ensure awareness for the multi-level character of a business relationship in the illustration circular arrows connecting the levels are depicted.

The overarching question which motivates the emerging field of research on customer attractiveness has been defined in the following way during our workshop on customer attractiveness: “Can we help the customer to be more preferred with the key suppliers in order to influence these suppliers to deliver extra value to us as buyers?”

It is sometimes challenging to invert the direction of our reasoning. Often, I have the impression, that the brain is returning to its old paths and we find ourselves tempted to again think in the old way. How often do we mix preferred supplier and preferred customer in a discussion, feeling like Eskimos in the desert!

But:

- Turning our perspective upside down could revitalize the stagnating research in early supplier integration in new product development processes. Avoiding collaborating with a partner who does not really want to do so, saves resources and avoids multiple frustrations.
- Furthermore, efficient supplier-buyer collaboration may be the next frontier in achieving additional cost savings.
- Focusing on those suppliers that award preferred customer status may also allow the business to climb the next step in efficient supplier development. It may not make sense to invest any effort in suppliers who prefer to serve another client.
- Many operational challenges and delivery problems could be substantially reduced by a diligent application of this new perspective.

Finally, a successful preferred customer campaign may change the strategic equilibrium between competing manufacturers. For firms this is a big chance at the moment, a window of opportunity.

We are confident that we will be able understand the mechanisms and to provide the tools for seizing these benefits. Therefore, we conclude:

Welcome to the exciting new world of low depth of production, open innovation and supplier scarcity— and the preferred customer imperative!

Ik heb gezegd.
REFERENCES


