In Aquanima USA, we have created a White Paper with the objective of explaining in detail the entire Strategic Sourcing project. Here you will find a complete analysis of each stage of the process from the 7 Steps of the Strategic Negotiations perspective.
Before starting to talk in detail about the 7 Steps of Strategic Negotiations, it’s important to describe what they are.

The official definition says:

‘Strategic Negotiations is an approach to procurement whereby the business needs and strategy of the organization are matched with the supplier market. It is much more than simply centralizing procurement. The approach is founded on a detailed understanding of both the spend profile of the organization as well as of the supplier market. This understanding is continually updated in order to deliver ongoing improvements to the organizations sourcing and procurement performance.’

What we can notice from this definition is that Strategic Negotiations is a ‘New Approach’, aligned with the Strategy for our company and the supplier market.

That should make us think…what is the difference between ‘Strategic Negotiations’ and ‘Traditional Negotiations’?

<table>
<thead>
<tr>
<th>STRATEGIC NEGOTIATIONS</th>
<th>TRADITIONAL NEGOTIATIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>FOCUS</strong></td>
<td>Focused on the Total Cost of Ownership (TCO) incorporating customer needs, organizational goals, and market conditions</td>
</tr>
<tr>
<td><strong>OBJECTIVE</strong></td>
<td>Getting the best product/service at the best value</td>
</tr>
<tr>
<td><strong>METHODOLOGY</strong></td>
<td>Driven by a rigorous and collaborative approach</td>
</tr>
<tr>
<td><strong>LINES OF ACTION</strong></td>
<td>Addresses all levers for savings</td>
</tr>
<tr>
<td><strong>DECISION MAKING</strong></td>
<td>Decisions based on fact based analysis and market intelligence</td>
</tr>
<tr>
<td><strong>DURATION</strong></td>
<td>A continuous process</td>
</tr>
<tr>
<td><strong>COST</strong></td>
<td>Lowest possible cost per unit</td>
</tr>
<tr>
<td><strong>QUALITY / QUANTITY</strong></td>
<td>High volumes for generating mass discount</td>
</tr>
<tr>
<td><strong>SKILLS SET</strong></td>
<td>Negotiation, analytical, proficiency skills</td>
</tr>
<tr>
<td><strong>LOCATION</strong></td>
<td>Locally known supplier base</td>
</tr>
<tr>
<td><strong>PROCEDURE</strong></td>
<td>‘what to buy and from whom’</td>
</tr>
</tbody>
</table>
As we can see, Strategic Sourcing is much more than ‘Only purchase’. However, what is Strategic Sourcing in detail for us?

Returning to the difference between Strategic Sourcing and Traditional Procurement, we can clearly see the difference in the following chart. Of course, doing Sourcing will also involve the Negotiation of the Pricing and the part of Award and Contract, but also includes additional steps at the beginning to match our projects with the strategy of the organization as illustrated below:

According to a definition established by authors Joe Payne and William Dorn in the book ‘Managing Indirect Spend: Enhancing Profitability Through Strategic Sourcing’ which, incidentally, became the fundamental basis for global consulting firm AT Kearney to delve into said concepts and is the foundations for what we know today as the ‘Strategic Supply Process’. In it, we find seven different steps in the process:

1. Understand business objectives
2. Data collection and spend analysis
3. Market research
4. Develop strategies
5. Select future supply base (RFQ / Negotiation)
6. Contracting
7. Manage relationship; implementation and continuous improvement

We will now proceed to look at each one in detail.

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1. Understand Business Objectives

It’s not a coincidence that this will be the first step in the process. Nothing can be done if we don’t know what the business needs or objectives are and if we don’t adapt ourselves and our process to accomplish that. As a general rule, three things are always important to keep in mind:

- Business Objectives will be always different than ‘Sourcing / Procurement’ objectives; they are two different things
- First Mandatory Goal: Understand Business Objectives to be able to adapt my process to the real needs of the business
- We can complete the Perfect Negotiation, but if we won’t accomplish Business Objectives (Timeline / Price etc.) our negotiation will be a failure

How we can know what the business objectives are? Simply by asking! As a part of our process, the first step is, after analyzing the information that we receive at the beginning of the project (from the Expense Request, e-mails from BUs, previous ARIBA negotiations etc), is to establish the Kick Off Meeting.

This meeting is probably the most important step in our process because not only will help us introduce ourselves and confirm to our client that we will be in charge of their project and will be the Single Point of Contact (SPOC) for helping them through the entire process, but will also help us ask as many questions we will need to ask to understand what those objectives are.

<table>
<thead>
<tr>
<th>RULE 1</th>
<th>RULE 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Don’t be afraid to ask and don’t assume things that you might not know! Not taking advantage of the opportunity of asking to know more, &amp;/or assume things that might be wrong can put the entire quality of your project in danger!!</td>
<td>Take advantage of the Kick Off Meeting to manage your stakeholders! You will need them during the entire project!</td>
</tr>
</tbody>
</table>

Also, during the initial meeting we can define what our internal strategy should be to manage those responsible for the business, based on their ‘Power’ and ‘Interest’ in the project in order to manage them properly. Not all interlocutors will need the same information and attention from us so we must know them to adapt and manage them efficiently.
- **MARGINALS:** ‘Least Important’
  - Keep informed via general communications (e-mail)
  - Aim to move them to box on the right of the grid

- **DEFENDERS:** ‘Show consideration’
  - Interested in low risk areas
  - They must be kept informed and consulted regarding their area of interest
  - They are a potential support / goodwill ambassador

- **LATENTS:** ‘Meet their Needs’
  - They must be involved and consulted about their area of interest
  - They try to increase the level of interest
  - They intended to move towards the box on the right of the grid

- **KEY PLAYERS:** ‘Principal Focus’
  - Efforts focused on this group
  - They are involved in management and decision making bodies
  - They must be involved and consulted regularly

Identifying each of the business partners within each quadrant from the initial meeting is essential to achieve business objectives... a Key Player can be crucial to get the important information and achieve results!
2. Analyze Category and Spend Analysis

The second step, when we know our business objectives, is to analyze the Category and the Spend. We cannot perform a good negotiation if we don’t know the dynamics of the category and how our own current or future spend will be.

There are 5 steps that we can use to profile the category:

1. Expenditure Analysis
   - Understand the internal expense of your organization for the information of the product / service that is being purchased
   - Is there more than one department buying the same product?

2. Volume
   - What is the volume of use of the products you are buying?

3. Suppliers
   - What is the price agreement and the T&Cs that you currently have with each of your suppliers?

4. Needs' Analysis
   - How many users does your products have?
   - Are you aware of their current and future needs?
   - What about potential users?

5. Supply Market Analysis
   - What does the supplier market currently look like?
   - What are the alternative solutions?

The output of the analysis must be our baseline, which is the guide that we will have to perform the negotiation and measure the savings.

What is the Baseline?

- It is the representation of what the future expense would be if Aquanima did not exist
- It is a convention since the real baseline is not observable
- It is the product of a negotiation with the client
- It is an offer comparison tool

Remember: The key for a Good baseline is to have a strong technical and mathematical strength.

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What is TCO?

The definition says:

‘Total Cost of Ownership (TCO) is an analysis that places a single value on the complete lifecycle of a capital purchase. This value includes every phase of ownership: acquisition, operation, and the softer costs of change management that flows down from acquisition such as documentation and training.’

As a part of a good baseline, we must identify the structure of the TCO and understand how the offers price was created, so we can negotiate a better deal.

What is the Baseline criteria?

- HISTORICAL PRICE: We must try to use this first

- BEST OFFER (RFQ)

- MIX: Historical + RFQ

Awarded Offer

Baseline

Savings
3. Analyze the market

We cannot perform our work if we don’t know the market. Therefore, we must analyze it and know in great detail its composition, quantity of vendor, new vendors, rivalry etc. All this information will be helpful during the entire process and, more importantly, for the negotiation and to maximize our results.

What are the components that I can use to analyze the market?

- **Our own experience or RFQ event**
  - Ariba y Aquanima History

- **Market reports & Internet Resources**
  - For Instance, Procurement IQ reports or Google search for news

- **Porter’s Five Forces Analysis**

If needed, at this point we can run a Request for Information or RFI:

- **Request For Information (RFI)** is used when you need more information from the vendors about a specific market

  - It will typically be followed by an RFQ or RFP. Sometimes it is also known as Registration of Interest (ROI)

- **Key aspects:**
  - In addition to knowing the market, it might also work to know the market or identify/classify vendors for next steps on the process
  - Prior to launching the event, it is important to define the matrix on how to evaluate results with the BUs or stakeholders in order to ensure that they qualify/disqualify the desired vendors.

**Remember:** Within the whirlpool of today’s society, where technologies and processes change rapidly in an increasingly globalized world, we must always ask ourselves when we do a market analysis, how digital transformation will change the profile of expenditure and, more broadly, how the evolution of technology is reshaping the profile of the category. Knowing and anticipating these changes will allow us to incorporate our discoveries as an integral part of our analysis, hence generating a competitive advantage when developing our processes.
4. Develop strategies

We are constantly developing strategies to achieve what we want (even without knowing that we are performing them). We can’t just wait to obtain what we want by chance, we must establish a plan to achieve it.

In Sourcing, the same applies. The strategy to achieve the goals for our stakeholders and our goals is necessary to be defined at this point, after having completed the previous steps.

A good strategy needs to be aligned with the **Golden Circle** to respond to three main questions:

1. **WHY**: Why am I purchasing what I’m purchasing and what are the stakeholder’s goals?
2. **HOW**: How am I planning to achieve the results?
3. **WHAT**: What I’m planning to do in detail to achieve those?

To implement our Strategy, we can perform **three main steps**:

1. Classify the Category in the **Kraljic Matrix** based on the complexity of the supplier market and the Business Impact:

<table>
<thead>
<tr>
<th>Supply Market Complexity</th>
<th>Low</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bottleneck</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Strategic</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-Critical</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Leverage</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Business Impact</th>
<th>Low</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bottleneck</td>
<td></td>
<td></td>
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<td></td>
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<tr>
<td>Leverage</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

After analyzing the market and defining the strategies, we can identify our trading based on the Karljic matrix, the ‘Supplier Market Complexity’ (Y) and the ‘Business Impact’ (X). Identifying the correct quadrant will allow us to properly manage the negotiation.
2. Based on Our Market Position, determine the basic strategy based on the **Procurement Gemstone**:

**Exercise Power**
- Consolidate number of suppliers
- Aggregate volume across units
- Redistribute volume among suppliers

**Create Advantage**
- Conduct product value analysis
- Rationalize / standardize specifications

- Compare ‘total’ costs
- Model ‘Should-Costs’
- Renegotiate prices
- Hold an online auction

- Establish / develop key suppliers
- Employ strategic alliances / partnering

- Expand geographic supply base
- Develop new suppliers

- Reengineer joint processes
- Support supplier operations improvement
Once the right quadrant has been identified, we can define the right strategy or strategies, leveraging ourselves in the ‘Sourcing Diamond’.

<table>
<thead>
<tr>
<th>Basic approaches</th>
<th>Exploit the purchase power</th>
<th>Create an advantage</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Non-critical</td>
<td>Leverage</td>
</tr>
<tr>
<td>Concentration of volume</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Evaluation of best price</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Global purchase</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Improvement in product</td>
<td></td>
<td></td>
</tr>
<tr>
<td>specification</td>
<td></td>
<td></td>
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<tr>
<td>Joint improvement in processes</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Restructure of relationship</td>
<td></td>
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</tbody>
</table>

**Legend**
- High Value
- Low Value

3. With the results of both the aforementioned steps, determine the correct **strategic response**:

<table>
<thead>
<tr>
<th>Quadrant</th>
<th>Strategy / Relationship</th>
<th>Low</th>
<th>Medium</th>
<th>High</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategic</td>
<td>Strategy</td>
<td>Keep position</td>
<td>Keep position</td>
<td>Keep position</td>
</tr>
<tr>
<td></td>
<td>Relationship</td>
<td>Develop and maintain the best possible relationship, prevent the provider from trying to abuse your position</td>
<td>Collaborative relationship but maintaining the possibility of changing providers</td>
<td>Partner relationship but maintaining the possibility of changing providers</td>
</tr>
<tr>
<td>Leverage</td>
<td>Strategy</td>
<td>Exploit the position, if possible</td>
<td>Exploit the position</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Relationship</td>
<td>Try to develop the relationship to get better prices</td>
<td>Distant, demanding and somewhat aggressive relationship</td>
<td></td>
</tr>
<tr>
<td>Bottleneck</td>
<td>Strategy</td>
<td>Change Position</td>
<td>Change or Keep Position</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Relationship</td>
<td>Diplomatic and very careful relations trying to maintain or increase our attractiveness</td>
<td>Ensure that the position of power can be maintained, if it could not, change the position</td>
<td></td>
</tr>
<tr>
<td>Non-Critical</td>
<td>Strategy</td>
<td>Exploit the position, if possible</td>
<td>Exploit the position</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Relationship</td>
<td>Low relationship limited to the essential</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
5. Select future supply base (RFQ / Negotiation)

In this step, we must first create an RFQ to receive the vendor’s proposal. This RFQ must be created taking into account what we’ve learned in the previous steps of the process and know in detail what we need to ask the vendor, both from a technical and an economic perspective.

From a technical aspect, remember that the business unit is the interested party so we must validate with them in detail the technical detail that we are requesting. The same must be done regarding the needs of the client and in detail so as not to leave any ‘grey areas’ for the supplier to consider as an opportunity to offer additional products that are not necessary. The RFQ request is not an opportunity for them to sell more products but rather the opportunity to respond to what we technically need.

From an economic aspect, when making the RFQ specification, we must pay special attention to how we request the price. Having the previous analysis of the TCO, we should ask for the price considering the greatest possible margin so that we can have room for maneuver in the negotiation.

For example, receiving a future proposal with a fixed price of X is not the same as receiving a proposal that explains how that price X was shaped. In the opening phases, we can see the components of the price and, aligned with the negotiation strategy, are able to negotiate a better agreement.

Remember that the supplier will never give us the detail of what we did not request so the RFQ must be done taking into account what we need to receive in order to subsequently negotiate.

As soon we receive the proposals (which will never be aligned 100% with our goals), we must negotiate.

Negotiation it’s an art! Before starting, we must define three important concepts:

**LAA:** The minimal conditions that make it still worthwhile to move forward with the solution or agreement, but anything less than LAA results in no agreement.

**MDO:** The ‘ideal situation’ you want to achieve in a negotiation

**ZOPA:** The possible agreement zone describes the range in which an agreement can be reached. Within this zone, an agreement is possible. Outside it, the negotiations will not reach an agreement.

**BATNA:** Your back-up plan that you are comfortable implementing if an agreement cannot be reached at or above your LAA

Remember: A negotiation is a method by which people establish and resolve differences. It is also a mechanism for generating long term relationships and credibility.
Knowing our LAA and MDO, identifying them based on active listening to what the supplier’s LAA and MDO would be, but knowing that a Negotiation consists mainly of concessions, we have to know our ZOPA (based on the needs of our clients previously defined) in order to be able to close an effective agreement, making use of our BATNA as a last resort if necessary.

How can we identify what is the supplier’s LAA and MDO and, more importantly, what is my supplier’s real intention of negotiating? Obviously, just like in a poker game, nobody is going to reveal their cards at the beginning of the negotiation, so a good exercise before starting a 1:1 negotiation is to identify the importance that my company and the project itself is to my supplier, based on two quadrants ‘Account Attractiveness’ and ‘Relative Business Value’.

- **The Nuisance quadrant**: Suppliers may treat the business as marginal if the procurement values are low and if there is little else that the buying organization can offer to attract them. Suppliers in this quadrant will rank the organization as lowest on their list of priorities. The buyer can also expect no interest from them in developing any form of co-operation.

- **The Exploitation quadrant**: Here, the level of procurements is likely to be important to the suppliers, but the business for other reasons is not very attractive to them. Suppliers in this quadrant are likely to maintain the business as long as it does not involve any particular effort for them. If they consider that the business is secure, they may attempt to exploit the buying organization, for example by raising prices.

- **The Development quadrant**: Suppliers in this quadrant will consider the buying organization’s business to be attractive, although its value is currently relatively low. Suppliers are attracted here by perceptions of future business potential. Consequently, they are ready to invest time and effort in developing a long-term relationship with the buying organization with the goal of increasing their sales over time.
The Core business quadrant: Suppliers located in this quadrant will most likely consider the buying organization to be a part of its core business.

I imagine that at this point you are wondering...OK, I have already identified my initial negotiation situation (LAA, MDO, BATNA & ZOPA) and analyzed the supplier to understand in which quadrant they are going to position me for the negotiation. Also, I have carried out several previous steps and, as part of the 7 stages of Strategic Negotiations, I have analyzed the industry and defined an initial strategy aligned with the business objectives... so, what can I do with all this information?

The answer is simple: Combine all that knowledge in order to achieve the expected results! Based on the qualification of the negotiation within the Kraljic matrix, the strategies defined in the Sourcing Diamond and what is the attractiveness of my business / project for the supplier, we can identify the dependencies that my company has with the supplier (and vice versa, their dependencies with us) in order to identify what is the base negotiation strategy that I should use.

From here, negotiation is an art and adapting to it is key. Remember two important concepts should always prevail:

- **Actively Listen**: During the negotiation, to ‘identify the suppliers’ cards’ and his strategies, to be able to understand them, manage them and adapt them to our objectives, listening is always more important than talking.
The supplier is not an enemy to defeat. If we understand from the outset that we can never develop our business without having the correct suppliers, just as they could not develop their business without having clients such as us, we can understand that there is always (although sometimes it costs more to find it), a ZOPA where a viable agreement can be found and with positive results for both parties.

Finally, it is important to highlight that, in Aquanima, whenever possible and there is sufficient competition to do so (with at least two or more suppliers in the final instance), what we know as Online Negotiations will prevail.

What is an Online Negotiation? It is the execution of a negotiation using technological tools available in the organization to maximize the concepts of Transparency and Credibility and results.

3 Principal drivers to have a SUCCESSFUL ON-LINE NEGOTIATION

1. Transparency
   - State clearly in the Rules of the Negotiation the awarding conditions prior to the on-line negotiation.
   - Define clearly the percentages that will be awarded to each supplier in when we will award to more than one supplier for risk strategic negotiations.
   - Any cost of change or technical weight factors used must be clearly identified in the Rules and communicated to the supplier prior the on-line negotiation.

2. Credibility
   - Based on the trust of the suppliers that they will be awarded if they win the on-line negotiation as client is committed with the e-Bid Outcome.
   - To ensure this commitment Aquanima must agree with the client before the e-Bid all the factors (qualitative or economic) that need to be taken into account in the award decision.
   - Avoid the usage of Ghost suppliers.
   - Invite similar quality suppliers.

3. Strategy
   - Definition of the Bidding parameters to determine the total cost and the ranks in the e-bid.
   - Analysis of the historic behaviour of the suppliers in on-line negotiations (if available).
   - The e-bid format (OLN Menu)

Did you know that Aquanima has carried out more than 13,000 online negotiations worldwide where the final savings results are, on average, 3.9% higher than offline negotiations? The potential of online trading tools not only allows greater transparency and credibility but also maximizes the results obtained.

As previously mentioned, selecting the correct type of event is a shared function and is defined in a particular way for each project, always leveraging on the experience of our NOL (Online Negotiations) Committee.

Last but not least, the results of the negotiations (whether they are ‘Offline’ or directly with a single supplier or ‘Online’ using the different technological tools that Aquanima has at its disposal), are the calculation and presentation of Savings or Negotiation Savings.
But what are Savings and how are they defined?

Savings can be described as the difference between the final value awarded and the baseline value (the definition of the Baseline was explained in Step 2).

Now, not all savings are the same. We can identify two types of savings:

1. **Soft Savings or ‘Procurement Acquisition Savings’**: These are savings that will not have a direct economic impact on our client’s budgets and are mainly related to the so-called ‘Cost Avoidance’ savings.

2. **Hard Savings or ‘Budget Savings’**: These are the savings that will have a direct impact on our client’s budgets. They are those obtained when the Baseline has been carried out following the criteria of updated Historical Price and validated with the budgets defined by the client.

**Remember**: Whenever possible, historical expense should be considered when preparing the baseline and validated against the client company’s budgets, since, if positive results and savings are achieved in the negotiation, these will have a doubly positive impact that should be properly quantified and presented in the final negotiation report of the or ‘Final Report’.
6. Contracting

Procurement contracts are the agreements to use certain products and services on a project. The types of procurement contracts and are typically either fixed-price, cost-reimbursable, or time and materials. Some agreements can include more than one of these payment structures on a single procurement contract.

Remember:

- No savings are valid until the contract is signed and the payments negotiated are effective
- It is the place to mitigate risks and define SLAs and KPIs
- Contract records are important because they serve as an audit trail of how the process was carried out

Additionally, an important point prior to the closing of any commercial contract is the correct compliance of the awarded supplier.

We must know and validate that with whom we are doing business as this is essential from a risk perspective. If not, we can believe that we are closing the best agreement, having followed all the steps and with excellent commercial and savings results for our company, but an undetected or managed risk in time can not only jeopardize or throw overboard the whole agreement but also generate associated costs (both in costs and reputation), which can seriously affect our company.

In Aquanima, we have a team specialized in this area - Vendor Risk Assessment Centre (VRAC) - who is in charge of carrying out this two pronged analysis: financial approval, in which the supplier will be analyzed from an expense perspective and service approval, in which the supplier is analyzed based on the five specialized areas relevant to the service provided: GDPR, Cybersecurity, Security, Facilities and Business Continuity.
7. Manage Relationship. Implementation and continuous improvement

To finalize, we must understand that we are not alone in this game. The vendor is not my enemy or someone that I need to defeat. It is an integral part of our business and I can’t exist without them (and vice versa). So, it’s not only trying to accomplish the best possible deal in order to achieve my goals and obtain a Win / Win situation where possible but it is also a matter to manage the relationship with the vendor, establishing different types of relationship based on the importance of the vendor, my strength in the market and the future relationship that we would like to have with them, hence creating the Closeness of the Relationship.

![Diagram showing the relationship between vendors, preferred suppliers, and business alliances]

Identifying and investing in the right relationship is an integral and critical part of the strategic negotiation process.

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