Buying Alliances

CIPS is expressing beliefs on buying alliances, which are forms of collaborative purchasing, as these are becoming increasingly prevalent and a key resource for purchasing and supply management professionals.

CIPS Positions on Practice

CIPS views, opinions and beliefs are stated throughout the document; however the broad practice statements which underpin the text are as follows:

- There are many different forms of buying alliance and CIPS encourages purchasing and supply management professionals to continue to develop collaborative purchasing to suit their specific needs.
- Buying alliances are increasingly common which may reasonably be expected to continue.
- If appropriate, organisations can collaborate on any type of purchase.
- Purchasing and supply management professionals should be cognisant of legal implications when considering entering into a buying alliance.
- The buying alliance should not be so big that its power distorts the marketplace - a reasonable rule of thumb is 15% of the relevant market.
- Buying alliances (collaborative purchasing) is an important element within the purchasing and supply management toolkit.
- There are many benefits to collaborative purchasing over and above the obvious advantage of leverage.
- Purchasing and supply management professionals should, ideally, obtain approval from their Board, or equivalent, before entering into longer term collaborative arrangements such as buying consortia.
- Purchasing and supply management professionals should be cognisant of legal issues related to collaborative purchasing.
- It is good practice to have a 'charter' or 'memorandum of understanding' between members of a buying alliance which sets out goals, objectives, plans and decision making authority, whether or not it is a formal longer term contractual arrangement.

Definition

Buying alliances are becoming increasingly common and are manifested in several different forms. The CIPS definition of a buying alliance is:

"Two or more organisations, or groups within organisations, collaborating on certain aspects of their spend in order to generate leverage and better value for money for all."

Opinions vary as to what the main forms of buying alliance are. Buying alliances generally fall into two broad types: 'consolidated buying' which is where separate organisations purchase together, and joint ventures which include partial equity ownership. Within these two broad categories there are, at least, a further four forms: 'vertical', 'horizontal', 'intra' and 'inter' organisational buying alliances.

There are several definitions of what is meant by vertical and horizontal buying alliances. CIPS' preferred definition is that 'vertical' means the same industry sector buying things specific to that sector whereas 'horizontal' cuts across industry sectors and would include activities such as the purchase of office equipment to be found in all sectors of industry. This does not prevent organisations within the same industry sector purchasing things that are not specific to them - indeed this practice is very common in the public sector with the use of consortia which purchase, amongst many other products and services, PCs, stationery and furniture.

'Intra' organisational buying alliances are groupings within the same organisation, or group of companies, buying together.

'Inter' organisational buying alliances apply across different (and indeed often competing) companies, industries and organisations.

Clearly, there are various combinations of the above e.g. inter-organisational vertical buying alliances would include for instance, universities purchasing scientific equipment together. In all cases however the driver is the requirement for similar products and services.

Purchasing and supply management professionals should not be constrained by the above definitions and instead be creative, as far as is practicable, in developing buying alliances to suit their needs. Indeed, one new method of collaborative purchasing is where organisations come together and set up a separate company to buy on their behalf; this not only aggregates requirements but minimises duplication and shares resources.

This approach is not strictly a buying alliance, but can provide a service based on the buying alliance principle.

Benefits of Buying Alliances

CIPS considers that the benefits of buying together, in addition to the obvious purchasing power through leverage, are:

- reduced acquisition costs
- shared market intelligence and product knowledge
- shared resources - people/time, management information
- investing together in supplier development and R&D so enabling improvements can be shared
- increasing the suppliers' interest as a greater value is placed on the group e.g. suppliers provide excellent service; their commitment reduces risk of interruptions to supply
- presenting a united front to suppliers e.g. to ease communication
- releasing time to concentrate on more strategic procurement
- inter-member trading can be set up to cover for shortages; inventory can be managed more effectively
- supplier benefits from greater market penetration.

CIPS would however advise buyers in the public sector contemplating entering into an alliance, to be aware of the
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regulatory factors that prevent some public bodies working with the private sector and indeed with certain other bodies in the public sector as well.

Key Issues

There are a few issues that need to be managed carefully when entering into buying alliances including the risk of the relationship with other members breaking down. This can be minimised by selecting partners whom one knows well or gradually building up a relationship through an activity such as benchmarking.

Sometimes potential buying alliance members cannot join because they are tied into an existing contract for the supplies in question. The supplier will often agree to release the buying organisation provided they can then compete for the buying alliance’s business.

Other issues include customer ‘buy-in’ - this is a perennial problem in those organisations where purchasing is decentralised as end users who are empowered to contract with suppliers must be willing (or mandated) to purchase from the contracts that have been let via the buying alliance.

Another issue is whether the organisations which collaborate on purchasing have to have a similar level of spend for the category in question i.e. would a larger organisation always allow a smaller organisation to obtain the same prices as them? It is easier if all organisations have the same spend but major volumes are required from at least one. There are ways around this issue by using differentiated pricing for the different members of the alliance provided that the alliance enables better value for money than if the members had purchased alone.

In addition to price, other factors such as service levels come into consideration - thus some participants might be offered more frequent deliveries than others, based on factors such as geography or size of order.

There is also the risk of finding oneself trapped in an existing arrangement when one wants to take advantage of new technological opportunities but others do not.

A further aspect to consider is geography. Buying alliances are often formed between organisations in one geographical region for obvious benefits such as supplier distribution, use of local suppliers and travelling to meetings. However, it might be better for two organisations in distant regions to collaborate if they are to purchase from a global supplier - specialist equipment for instance i.e. one delivery each of an

record keeping and co-ordination are also important issues in buying alliances. For example, someone needs to be responsible for co-ordinating details of the total volume of business from each of the participants, or the achievement of order levels which secure higher levels of discount.

For bodies within the public sector, the EU Directives also generally required by all businesses. However, buying alliances are increasingly common in ‘security/bottleneck’ categories (low value-high risk) as, by aggregating requirements, the members of the buying alliance become a more attractive customer to the supplier who may not otherwise be particularly interested in supply security and continuity considerations.

The CIPS view is that in practice there is no reason why organisations cannot collaborate on any type of purchase. An example of innovative collaborative purchasing is where three
banks (competitors in the same industry) all had to renew some expensive machinery that they had in common so they formed an alliance and bought the manufacturer of the machinery. Occasionally, suppliers suggest to customers that they purchase collaboratively in order that the supplier receives more business and their contract/customer management costs are reduced.

Buying alliances between competitors may be appropriate for commodities and non-strategic items where margins are very low and/or where there is another dominant buyer in the marketplace. However, some competitors may choose to create a buying alliance for specific items where the objective is to exclude some of their competitors.

Buying alliances encourage standardisation of specification. The process of selecting suppliers and a range of standard specifications helps to challenge organisational perceptions of acceptability. However, standardisation is not necessarily a pre-requisite of buying alliances (there is no necessity for all members to specify the same products) - as long as the required products are available from one or more suppliers, all members' preferences can be satisfied.

CIPS considers it is advisable to obtain permission from the Board before embarking on a buying alliance, whether or not it has a formal legal standing. Buying alliances have a higher chance of success if they have senior executive support and commitment from the start. The Board will need to be satisfied that there is no risk to reputation from such alliances and that they do not, for instance, conflict with or compromise any other strategy the organisation is trying to pursue e.g. partnering on R&D with the competition of the proposed buying partner.

Conclusion

Buying alliances take time, commitment and effort to put in place but can deliver value for the members. CIPS believes that buying alliances will become increasingly common in the future due to the need to keep gaining leverage but also because of developing technology. eCommerce and eProcurement technology are drivers and enablers of buying alliances as they allow electronic orders to flow through defined portals to suppliers, facilitating internal compliance and demonstrating volume movements to suppliers. Similarly, buying alliances are increasingly making use of eAuctions to drive down costs.

The increase in buying alliances may result in price range differentials between larger and smaller companies and suppliers may respond with defence strategies, such as creating supplier alliances with their competitors.

CIPS believes that all purchasing and supply management professionals should explore buying alliances as a means of leveraging spend and obtaining the other benefits outlined in above. It is a valuable component of the purchasing and supply management professional's toolkit. In particular, this should be a preferred route for low-value, high-volume goods and services which has the significant consequence of allowing the purchasing and supply management function to concentrate on more complex value-add procurement activity. As with other aspects of purchasing and supply management, relationship management skills are a key feature of working in collaboration with others.