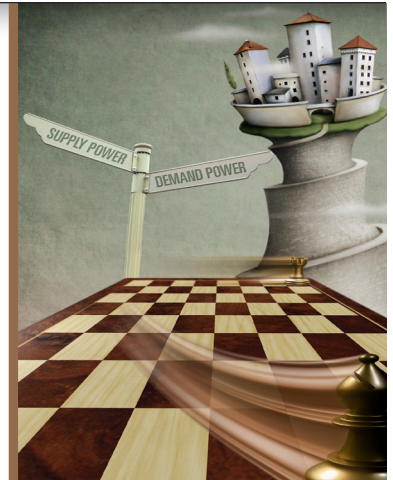


# Three “Chess” Moves to Restructure Supply Markets

## The A.T. Kearney Purchasing Chessboard®

*Suppliers often own the power position as they dictate prices while enjoying unusually large margins—leaving buyers with limited negotiations leverage. Buyers are not completely powerless, however. It is possible to restructure the supply market to their advantage using the A.T. Kearney Purchasing Chessboard.® The Chessboard examines factors that determine the supply-demand balance of power for each procurement category and identifies strategies applicable to every market situation. Using strategic chess moves, companies gain the flexibility to deal with challenges in this new age of purchasing.*



Supply-chain integration is blurring the lines between companies and their suppliers, and the assimilation has moved into more areas, including research and development (R&D), as well as sales and marketing. This close collaboration is healthy when the relationship is mutually beneficial and a balance of power exists between both parties. But when markets change and options for renegotiations dwindle, buying companies can lose the upper hand in negotiations with their suppliers.

In some cases, the balance of power has shifted so far in suppliers' favor that some firms are acquiring their suppliers for fear a competitor could purchase the supplier first and cripple the supply base. The Purchasing Chessboard offers a way to combat this imbalance of power.

### The Purchasing Chessboard

A.T. Kearney developed the Purchasing Chessboard in 2008 to help pro-

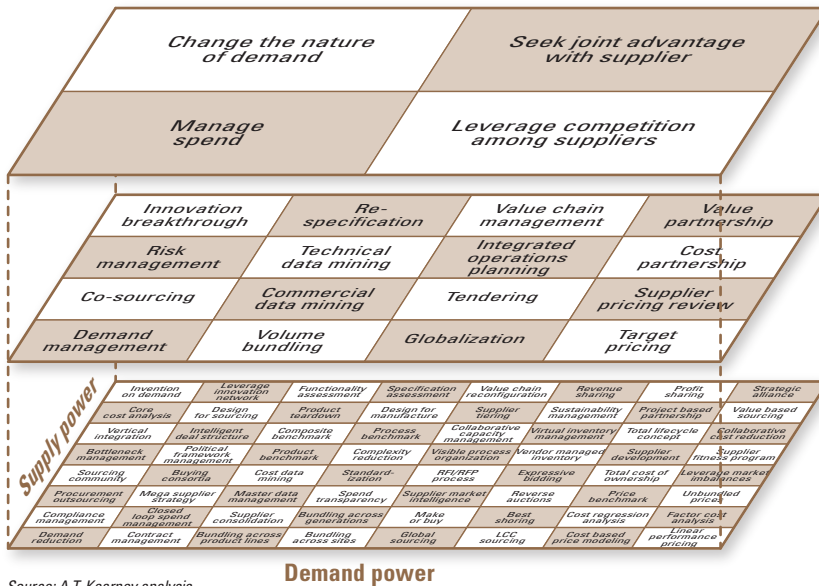
urement professionals in all industries master the tools of their trade.<sup>1</sup> The Chessboard identifies market situations that occur between purchasing organizations and their suppliers—examining factors that determine the supply and demand balance of power and the position of each procurement category within the market. The Chessboard is used to identify procurement strategies applicable to each market situation, and is flexible enough to adapt to changing conditions and challenges in this new age of purchasing.

Four basic purchasing strategies comprise the Chessboard: change the nature of demand, manage spend, seek joint advantage with suppliers, and leverage competition among suppliers (see figure 1 on the following page). From these, we drill down to 16 approaches and 64 methods, each providing a standalone way for buyers to reduce costs and increase value in supplier relationships.

*The Purchasing Chessboard helps alter the imbalance of power that occurs between buyers and their suppliers. The Bishop, Castle and Queen moves can create a valuable competitive advantage.*

<sup>1</sup> The Purchasing Chessboard is a compilation of insights and experience from more than 500 purchasing projects performed worldwide over the past three years, and thousands more performed over more than three decades.

**FIGURE 1: The A.T. Kearney Purchasing Chessboard®**



Source: A.T. Kearney analysis

## Why Restructure the Supply Market?

Buying companies are at an obvious disadvantage when there is more demand than supply; prices rise and there are fewer purchasing options. These conditions often occur when suppliers merge or are acquired, reduce their capacity, integrate operations with another company, or develop breakthrough technologies.

When suppliers own the power position, how do buyers keep costs down? One way is to change the nature of demand. This is one of the four strategies on the Chessboard shown in the upper left quadrant in figure 1. For example, for companies installing upstream oil and gas offshore platforms, only a certain number of giant floating cranes could lift the modules into position over the base. The owners of these cranes owned the power position and could charge high rates. The industry then developed the “float-over” concept—floating the modules

over the base and then raising it up without needing such a giant crane. Platform owners had effectively changed the nature of demand.

Other approaches include altering product specifications, globalization, tendering and performing risk management, among others. Each approach not only has an impact on the end-to-end value chain, but also on a company’s short- and long-term competitive advantage.

The question for many buyers is not whether to restructure the supply market—for that is often a given in many situations—but how to do it. The Chessboard provides answers, offering methods to help buyers improve their purchasing positions. Returning to our earlier example of changing the nature of demand, buyers use the Chessboard to determine their next move, whether to adjust product specifications (develop the float-over concept) or perform more diligent risk management, for instance, struc-

turing longer-term contracts to minimize price increases. Choosing which approach to use will depend on a buyer’s unique motivations and desired outcomes. Is the motivation purely to capture savings, or to ensure supply security? What is the case for change? What is the impact of doing nothing?

Importantly, the key is not only in identifying the approach to use but also in predicting how the various value chain players might react to it. Will suppliers lower their prices to meet the competition, or pull out altogether as they consider your approach too aggressive? Will competitors follow suit, taking advantage of your efforts, or will they forge closer relationships with your suppliers and isolate you? Will your customers bypass you and purchase directly from suppliers? The potential risks of each move must be planned in advance to mitigate all possible adverse reactions.

## Bishop or Castle?

In restructuring a supply market, buyers must be prepared to employ strategies that increase demand power, decrease supply power, or both. When suppliers have all the power, we often suggest using a *Bishop* move to change the balance of power. This is a diagonal move on the chessboard, from the upper-left quadrant to the lower-right quadrant. For example, one successful Bishop move is to develop low-cost-country sourcing alternatives. Here, redesigned sourcing strategies include new supply choices in emerging markets—engaging smaller suppliers eager for partners—while increasing a buyer’s influence over demand.

Before making the Bishop move, however, it is wise to consider all of the potential consequences. The low-

supply, high-demand scenario might seem ideal, as it improves bargaining position, but it can give competitors the same benefits without any of the investments in time or resources. Therefore, it is best to deploy the Bishop move only in categories that are not vital for competitive advantage.

Another Chessboard move is called the *Castle*. This is a lateral move in which the buyer maintains control over its supply while increasing its influence over demand. For example, by using collaborative strategies, buyers can gain preferential access to a smaller supply base and create an “inner circle” that provides short-term monetary advantages and longer-term benefits.

Common Castle strategies include: **Supplier relationship management.** Buyers use supplier relationship management techniques to engage select suppliers in specific strategic, operational and tactical areas.

**New product collaboration.** Collaborating on new products with an efficient product development and supply chain process reduces buyers’ costs and provides suppliers with defined margins.

**Bundling.** By bundling across sub-categories, buyers can match a weak sub-category with a stronger one, allowing the weak category to make a Castle-type move.

Because Castle moves require significant collaboration with suppliers, they are best reserved for products and categories whose competitive advantage is worth the extra effort. Selecting the right suppliers is crucial—since collaboration requires medium-to-long-term commitments from all parties—and like the Bishop, the Castle requires selective deployment. Also, because collaboration increases suppliers’ power without corresponding benefits for the

buyer, buyers should reserve the option to withdraw from the relationship on short notice to avoid significant negative impacts.

### Moving the Queen

In most cases, Chessboard users combine their Castle and Bishop moves to make a Queen move. The Queen balances the short- and long-term implications of all changes. We can use rising prices and company size to help illustrate this point, shown in figure 2.

Different size companies are affected in different ways by a change in the supply market. Smaller buyers are more vulnerable to supplier price increases as they lack negotiation leverage and could be forced to exit the market altogether; for these buyers, Bishop moves reduce supplier power. Larger buyers, in contrast, have negotiating power so do not feel the impact of significant price increases and will probably benefit if small players are forced from the market. In this “middle ground” scenario, a Castle move is advantageous. There is a third option: Doing nothing. By doing nothing, prices continue rising, massively shifting value from buyers to suppliers. In these circumstances, vertically integrated

buyers usually enjoy the most benefit.

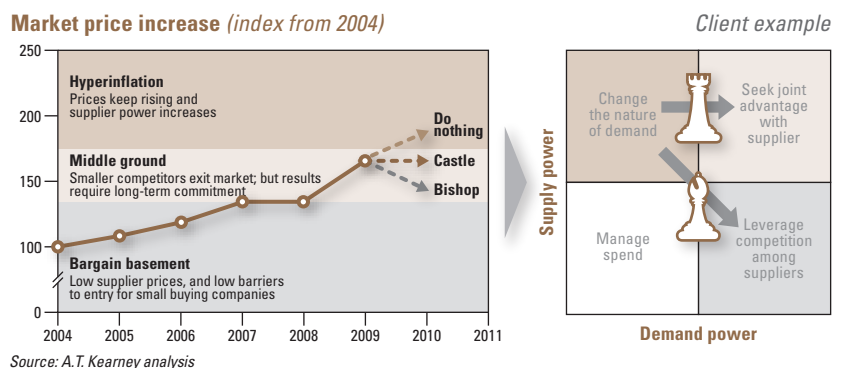
The Queen move is a combination of the Bishop and the Castle whereby strategies are developed to address individual situations and are flexible enough to change as needed to contend with suppliers’ reactions to the strategies. A classic Queen move is when a company identifies supply alternatives in low-cost countries (Bishop) while crafting an inner circle of smaller suppliers (Castle). The key is to monitor supplier, competitor and customer reactions and be prepared to launch strategies accordingly.

The following case study offers a brief overview of how we helped one company use all three moves—Bishop, Castle, Queen—to restructure its supply market.

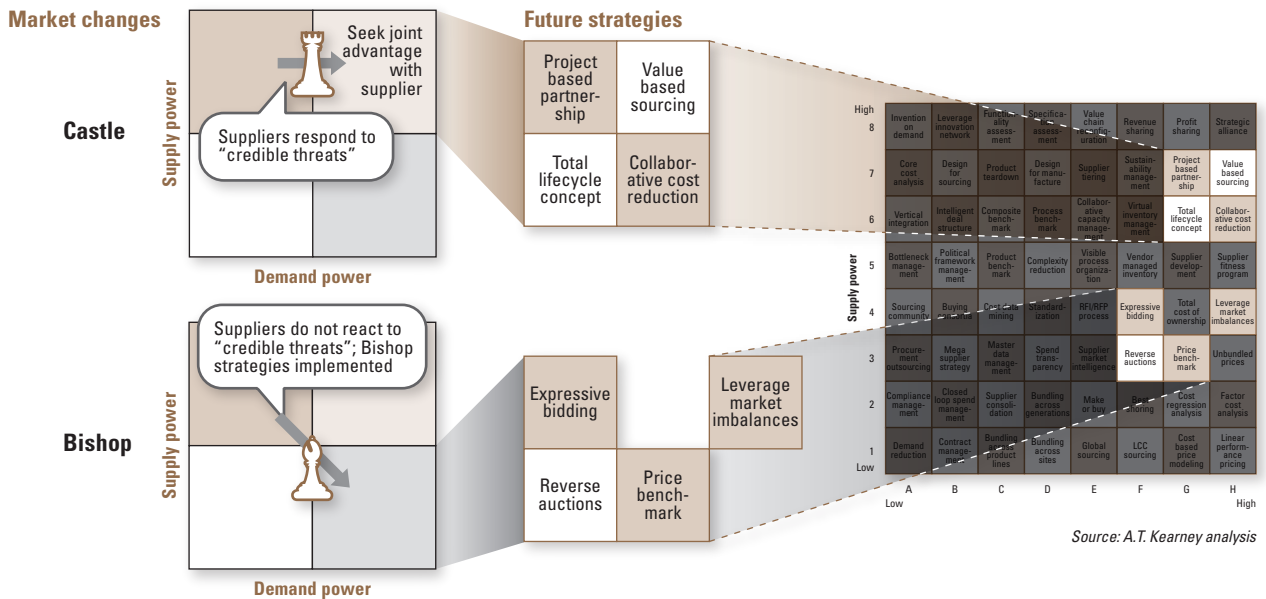
### A Case Study

A large international A.T. Kearney client faced an oligopoly of suppliers that had acquired power through aggressive acquisitions and capacity management, leading to increased prices (and profit margins)—at the buyer’s expense. We found that neither the Bishop nor the Castle strategy was ideal. The Bishop was expensive and could provide too much benefit to the company’s

**FIGURE 2:** Rising supplier prices posed a problem for our client



**FIGURE 3: Our client's next move depended on the supplier's response**



competitors, while the Castle required a long-term commitment that would delay the desired benefits. Doing nothing was also not viable, since the problem of supplier power would only get worse over time. We needed a Bishop-Castle combination—the Queen move.

The company developed several alternative options and analyzed whether to deploy them by identifying all credible threats to suppliers and monitoring their reactions. One strategy was to seek joint advantage with

a supplier, the upper right quadrant of the Chessboard. Figure 3 illustrates how reactions from the supply base dictated next moves. If suppliers responded positively, a Castle move was deployed and the alternatives put on hold; a negative response led to a Bishop move (provided that doing nothing was still not a good option).

The Purchasing Chessboard helped this company stay ahead of a dynamic supply market while maximizing benefits and competitive advantage.

## A Balanced Course

The Purchasing Chessboard provides a means to restructure supply markets and create win-win situations. Buyers gain favored access to newer and scarcer products, preferential pricing, and a stable position as a market leader. Suppliers get solid, predictable business volumes with definite margins, and become more competitive. A balanced course that combines several moves—Bishop, Castle and Queen—can be the best route to competitive advantage.

A.T. Kearney is a global management consulting firm that uses strategic insight, tailored solutions and a collaborative working style to help clients achieve sustainable results. Since 1926, we have been trusted advisors on CEO-agenda issues to the world's leading corporations across all major industries. A.T. Kearney's offices are located in major business centers in 37 countries.

A.T. Kearney, Inc.  
Marketing & Communications  
222 West Adams Street  
Chicago, Illinois 60606 U.S.A.

1 312 648 0111  
email: [insight@atkearney.com](mailto:insight@atkearney.com)  
[www.atkearney.com](http://www.atkearney.com)