

Negotiating effective procurement contracts in MNEs

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Abstract

The broad question surrounding this research field is ‘how can the procurement practices of MNEs be effectively managed in the age of globalisation’? The inherent difficulties of the (often) dynamic situational constraints between buyers and suppliers are commonly found in the negotiation stages of contracts. Therefore, this research seeks to demonstrate why culture, interpersonal attributes, tactics and the avoidance of conflict within the contractual procedure are central to establishing more effective procurement performance. An approach is taken that avoids traditional cross-country comparisons. By introducing the notion that procurement departments are nowadays compiled of an international cohort of individuals, this research is focusing not only on countries but also on industry sectors. By thoroughly reviewing the literature in this field, focusing on all the key aspects of negotiating procurement-based contracts in an international context, we explain the development of our hypotheses and the conceptual model that will be empirically tested during the next stage of this project.

Keywords: culture, cross-cultural issues, business negotiations, procurement

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1. Introduction

1.1 Rationale

In today's globally competitive business environment, developing sustainable competitive advantage is perceived as being of vital importance for firm survival and prosperity. As the procurement function is now recognised as being a key ingredient to achieving this, research has to date, has sought to identify its major success factors. Hence, the broad question surrounding this research field is 'how can the procurement practices of MNEs be effectively managed in the age of globalisation'? The inherent difficulties of the (often) dynamic situational constraints between buyers and suppliers are commonly found in the negotiation stages of contracts. Therefore, there is a need for a new research approach that investigates these 'complexities of reality'. To date, there has been very little work on the influence of negotiation antecedents on the outcomes of procurement performance that, at the same time, takes into account a pre-determined situational setting. This research seeks to demonstrate why culture, interpersonal attributes, tactics and the avoidance of conflict within the contractual procedure are central to establishing more effective procurement performance within a cooperative outlook. Also, a new approach is taken that avoids traditional cross-country comparisons. By introducing the notion that procurement departments nowadays often comprise of an international cohort of individuals, we focus not only on countries but on industry sectors, too. This way, new insights across nations and within industries are anticipated. Hence this project seeks to develop a framework to encapsulate the key negotiation requirements for increased procurement performance (strategic in scope) in MNEs within a confined, yet applicable manner. The research outcomes should both contribute to theory and have wider practical application.

1.2 Research problem

An influential body of literature has made it apparent that there are variations in terms of *what* the most influential antecedents surrounding the contracting procedure are and *how* this impacts on procurement performance. As a result, the research problem is divided into a theoretical, as well as an analytical part. Firstly, in an attempt to find the most appropriate antecedents and their impact on the procurement function, this paper shows why some of the

later discussed categories are to be included and which are to be excluded in order to arrive at a coherent and hence systematic enquiry. This task provides clarity by allowing us to filter out the extraneous areas of the wide body of business negotiation literature. Secondly, a rigorous analysis of both the qualitative and quantitative axis will derive in-depth knowledge and explanation, as well as disclose data and resulting information on tendencies and best practices in the form of a valid, reliable and above all utilisable framework.

1.3 Research questions and objectives

From the brief description above, it is possible to deduce the main research question, which reads as; ‘how can contractual procedures be negotiated to ensure effective procurement performance in MNEs?’ Upon closer examination, further questions also need to be addressed in order to achieve our goal of improving procurement performance. Therefore, seen from a procurement perspective, these questions are:

1. How should contract-related procedures within the procurement process be negotiated, compiled and later used to promote long-term relationship quality?
2. Are aggressive negotiation tactics used in cooperative surroundings? And in what way do negotiation tactics matter, when applied within the contracting stage?
3. What, if any, are the perceived differences between the buyer and supplier requirements within the contracting procedure?
4. How can the contract stage of the negotiation be managed to minimise conflict in order to avoid mediation and arbitration?

These questions will facilitate the main objectives (outcomes) of this study, which are:

1. Exploring the factors and underlying variables that have an effect on negotiating contracting procedures and the resulting performance effectiveness of the procurement function.
2. Development of a holistic research model within a pre-determined situational construct that includes empirically justified measurements.
3. Contributing to the clarification of strategic versus operational contracting procedures.

4. Development of a valid and reliable framework to encapsulate the key negotiation requirements for increased procurement performance.
5. Contributing to the international business negotiation (IBN) knowledge base, which lacks both empirical evidence and insights from a European, as opposed to an American standpoint.
6. A full examination of buyers and suppliers' view to gain a holistic understanding of the issues within the contracting stage of negotiations.

2. Literature review

2.1 Contextual study

To clarify the contextual borders of the research, we provide a brief theoretical explanation. Whilst procurement embraces the entire process of starting at the internal customer all the way to the follow-up and evaluation of the supplier, here we clearly focus on analysing the contracting stage between the buyer and supplier (see Figure 1). This is because negotiation expertise is particularly influential at the face-to-face negotiation stage (Dobler and Burt 1996; Ghauri 2003b; Van Weele 2005). Moreover, the broad scope of the procurement function suggests that full coverage of all aspects would result in a loss of detail and reliability.

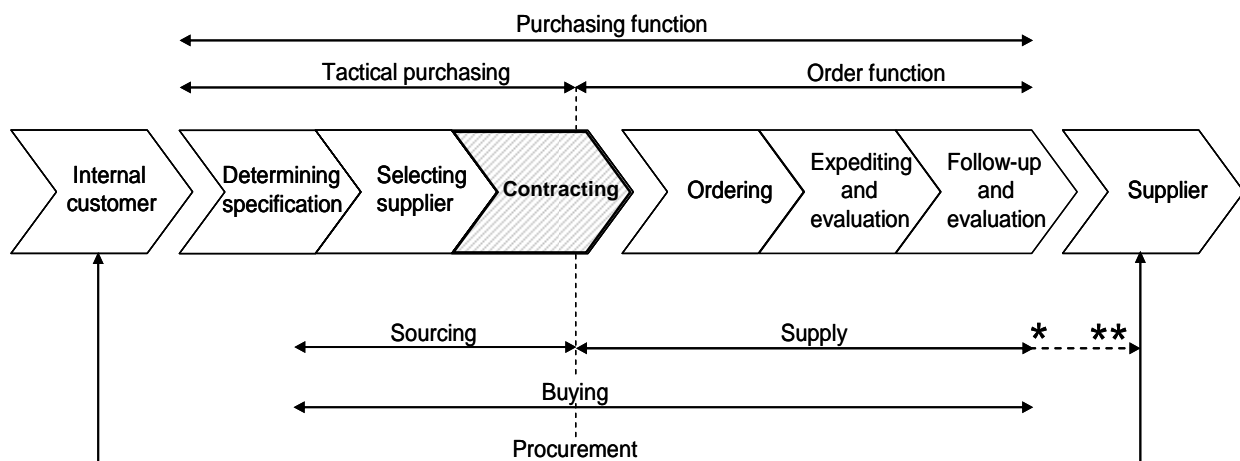
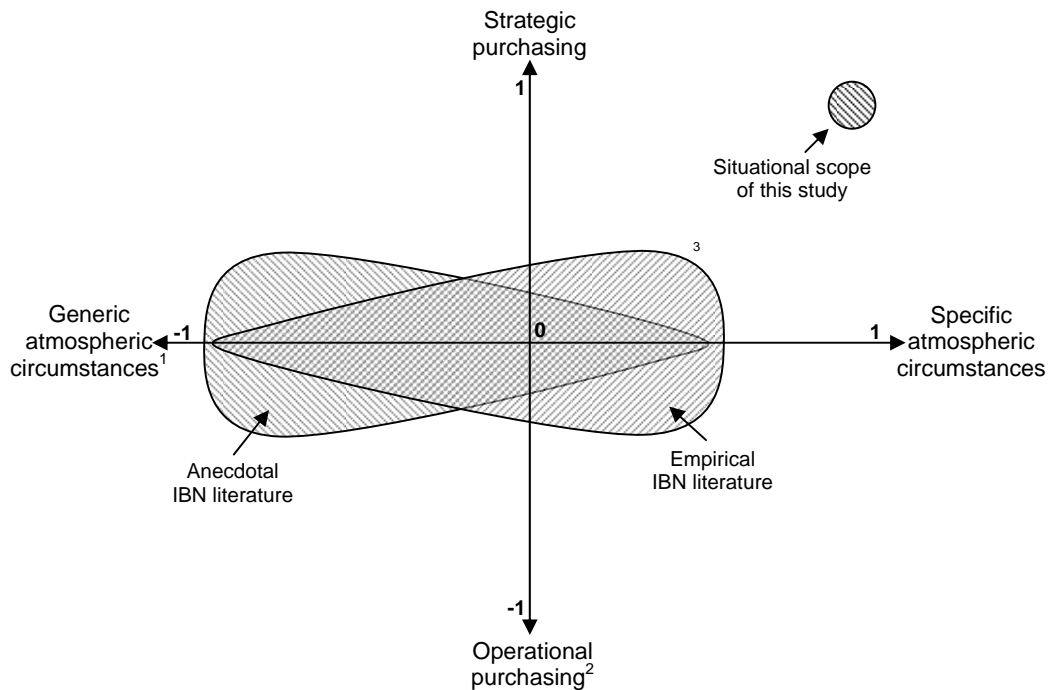


Figure 1: Purchasing process model and some related concepts (Source: Van Weele 2005, p.13)

2.2 Situational scope

Previous studies have largely followed a generic approach to research within the fields of procurement. Strategic purchasing and its importance in supporting company and business units has long been promoted by academics (Browning *et al.* 1983; Reck and Long 1988) and is clearly distinguished from operational purchasing processes (Carr and Smeltzer 1997; Ghauri 2003b). Van Weele (2005) explains that the economy of high transaction costs and high vertical integration, due to the high financial and strategic stakes involved evidently differentiate the two forms of purchasing. The research scope is shown in Figure 2.



Note¹: The atmospheric scope of the conflict/cooperation, power/dependence and expectations situation reaches from -1) unspecified (generic), 0) partially specified to 1) specified

Note²: Both areas are flattened on the y axis as most papers do not specify the purchasing modus

Note³: The anecdotal IBN literature identified tends to look for explanations on a more all-embracing level, whilst empirically based IBN literature tends to focus on specific circumstances as shown on the continuum. The situational scope it outlined within a B-to-B market

Figure 2: The study's situational scope

We propose that strategically-focused purchasing (y axis) and the inherently embedded contracting procedures may indeed engage in a specific and somewhat different *modus operandi*

of business negotiations. Although anecdotal evidence (Tung 1988; Tung 1991; Luo 1999) provides some insights, there appears to be no empirical evidence to support our problem definition. In connection with the focus on strategic purchasing, it is then possible to clearly define the atmospheric circumstances (x axis) of this investigation through a set of predetermined assumptions.

2.3 Defining the atmospheric circumstance

In the explanation of similar studies by Ghauri (2003b) and Saner (2003) about cooperative conditions, the dyad between buyer and seller is shown as most likely to be cooperative if the desire for relational quality and interdependence is positive/complementary and the power/dependence distribution (relative power to each other) is equal. Furthermore, elevated trust perceptions (Cousins 2002) carry equal weight. In this context, Campbell (1985) refers to the typological circumference of a domesticated market. Assuming that such a cooperative stipulation forms the basis of this study's specific atmospheric circumstance, Campbell's (1985) list of conditions favouring a cooperative buying strategy is of value. By using the characteristics for cooperative buying inside the product, industry, company and individual compounds, a lucid and overall sensible method emerges, which forms the foundation for a thorough investigation. Tapping in to the literature about competitive advantage (Porter 1980), it becomes apparent that the relational view *per se* as proposed by Dyer and Singh (1998), as well as the relationship approach in the context of procurement (Cousins 2002) emerge as suitable theoretical lenses to complement the atmospheric boundaries of this research - an assertion, that finds its justification in the literature on strategic purchasing. To provide reasoning for this theoretical lens, Van Weele (2005) agrees and further asserts that in an ever-increasing globally competitive business environment, it is becoming of key importance within the realms of purchasing and supply chain management to develop long-term, mutually beneficial business relationships. By examining the performance effects of partnerships among manufacturers and suppliers for new product development for instance, results indicated "...that a higher level of supplier's involvement positively influences innovation and financial performance" (Chung and Kim 2003). Seen from the supplier point of view, relational behaviour in terms of initiating, signalling and the disclosure of information does seem to have a profound effect on the "share of business" (Leuthesser 1997). If share of business is defined as a performance indicator,

Leuthesser (1997) has lent anecdotal, as well as empirical support to recent calls for “relationship marketing”. Matthyssens and Van den Bulte (1994) agree with the former findings in that a shift away from an antagonistic model towards a cooperative model is taking place. That buyer-supplier interdependences within a B2B environment is to be seen as central to enhancing a firm’s bottom line is further supported by Carlisle and Parkers (1989).

With a collaborative long-term oriented relational approach in mind, Janda and Seshadri (2001), Lamming (1993), Lewicki *et al.* (1994) and others have demonstrated that purchasing efforts via cooperative negotiation boost both effectiveness and efficiency. Additionally, commitment and ensuing long-term, strategic relations and can further promote win-win solutions (Lewicki *et al.* 1994). Using the notion of game theory, it is believed that cooperative negotiation tactics in which the goals of both parties carry weight is more likely to derive a satisfying and productive relational outcome. Whilst Gugler *et al.* (2003) found the effects of mergers to be largely financially positive, increased numbers of failures of M&As have made alliances the preferable vehicle of choice for robust and integrative purchasing and supply chain management (Bernhut (2004); Browning *et al.* (1983); Reck and Long (1988) and Van Weele (2005)). Defining market relations as ‘domesticated’ then, we asserts that at the heart of generating sustainable competitive advantage, rests the nature of a long-term relationship outcome between the buyers and suppliers, which is established during the negotiation process.

2.4 Cultural digest

International business negotiation processes can only be fully appreciated if one takes into account the underlying concept of cultural consciousness. As hundreds of contributions have been made, only the major trains of thought on cultural awareness within business negotiations are mentioned here. Given the knowledge as to what culture is and how it has been ‘dimensionalised’ in previous studies of concern (e.g. Myers and Tan (2002)), Usuniers’s (2003) comprehensive census of identified cultural influences on the marketing negotiation process helps to understand how deeply embedded and all-embracing cultural individuality is.

Depriving culture of its importance, Teegen and Doh (2002) talk about an increased convergence in the *modus operandi* of negotiations. Hawrysh and Zaichkowsky (1990)

concluded that cultural differences do not affect persuasive tactics, concessions and outcomes, while Drake (2001) is convinced that the contextual effects of role, preconceptions about negotiating and mutual adaptation influence negotiators to a greater extent than culture does. Although cross-cultural awareness should be perceived as important, variations in geography, age, gender, class and other demographic attributes (interpersonal attributes) can be even more dominant (Tung 1982, 1991). Further support that negotiation strategies are similar across cultures is provided by Brehmer *et al.* (1970), Graham (1985) and Swee Hoon and Teo (1997).

Whilst the literature depicts an ambiguous picture, it comes as a surprise that none of these reviewed papers has embraced the notion that procurement or sales departments inside MNEs are nowadays often comprised of individuals from different cultural backgrounds (Charles and Charles 1999, Ghoshal and Bartlett 2002; Tung 2008). This in turn makes the tendencies revealed even more unclear. Therefore and as a result of pilot interviews with both academics and practitioners as part of this study, culture *per se* may not have the often ‘feared’ impact on negotiating contracts.

2.5 Interpersonal attributes

Personal relationships are core in face-to-face negotiations. Thus, reviewing literature on individual and successive interpersonal behaviour through a diverse set of attributes is key. For example, social capital theory postulates that high relationship quality can only be achieved by negotiators scoring high on relational, cognitive and structural dimensions (Kumar and Worm 2003). Within this construct, it is Money (1998) who adds the importance of social networks and the inherently based social congruence, which is of great importance in order to benefit from elevated levels of creativity and condensing latent ‘interactional’ difficulties. One must dig deeper to understand the building blocks of social interface and therefore a thorough examination of the major antecedents in this field should be provided. To start with, personality has a noticeable impact, as the thinking-feeling aspect is seen as the underlying cause for people’s decision making process and consequent preferences in content and style (Kale 2003). A wide body of literature suggests that individual demographics, as well as personality-related variables and gender (e.g Kimmel *et al.* 1980; Kray *et al.* 2002; Bowles *et al.* 2005) may have an effect on the negotiation process and outcomes. Due to incoherent and confusing results (Pruitt 1981),

such individualistic attributes ought to be incorporated in future conceptual modelling (Carnevale and Pruitt 1992). For example, Alexander *et al.* (1994) provided support for the fact that age, income, education as well as experience may alter behaviour within the negotiation process. Interestingly, most studies found that gender differences were insignificant (Min *et al.* 1995; Walters *et al.* 1998; Pradel *et al.* 2006). Therefore, gender as a factor will not be pursued further.

Emotional factors cannot be discounted within a multinational setting (Reynolds *et al.* 2003). Fiske and Taylor (1991) define affect as "...a generic term for a whole range of preferences, evaluation, moods, and emotions". Several scholars have turned their eye to negotiators' affective stance, mood and how experience and expression of emotion can influence the negotiation process (Hunt and Kernan 2005). Their findings show that affectively (opposed to cognitively) framed negotiation rounds indicate that although higher levels of involvement and positive emotions are apparent, lower levels of trust decrease the likelihood of the use of cooperative tactics. Other authors clearly suggest that affection profoundly influences negotiation processes as well as outcomes (Conlon and Hunt (2002); George *et al.* (1998)).

In contrast to the above arguments, conciliatory predisposition, trusting nature, and risk propensity under the mediating factor of cultural context between American and Filipino industrial exporters revealed that personality does not have a direct impact on the problem-solving approach (Calantone *et al.* 1998; Mintu-Wimsatt 2002). A possible explanation was found in what Limaye and Victor (1991) call the "third culture" theory. As Drake (2001) explains, within international circles, national negotiation patterns are overruled by international diplomacy. Hence, and due to the fact that we focus on international suppliers, we hypothesise that interpersonal attributes and constructed social interface do not impact the contracting stage of a negotiation.

2.6 Negotiation tactics and contracts

Tactics as a process measure has received a lot of attention from scholars. For our purposes, negotiation tactics are perceived as a lever to achieve a "win-lose" situation, where one side's gain is the other's loss (Perdue 1992). Vividly described by Perdue (1992) as a pivotal tool

if someone is to get the best deal, Gitomer (2007) believes that studying the science of negotiation tactics is key in order not to give away unnecessary concessions to the other party. Negotiation tactics is a vague terminology, as it can mean deceiving and manipulative practice or skilled strategic behaviour, concerned with preparation and good time management (Demers 2002; Lax and Sebenius 2002). It is, however, the deceptive (and hence aggressive and competitive) tactics that are of more interest here. This is for two reasons. Firstly, aggressive tactics are not to be used within a cooperative setting (Fisher *et al.* 1991; Lewicki and Stark 1996). However, studies have shown that even though a long-term partnership is sought by both negotiating parties, the anomaly (Harwood 2002) of aggressive bargaining tactics is still exercised (Lax and Sebenius 1986) – to what degree is unknown. Furthermore, a study published by Hendon *et al.* (2003) is among the few contributions looking at tactics and how they are used in different countries. The idea here is to provide more insights into the application of aggressive tactics comparing different industries within a cross-national setting (Hokey and William 1993). Secondly, strategically skilled behaviour is expected to exist at any rate to a lesser or greater degree in strategically important procurement contracts (Lax and Sebenius 1986; Bernhut 2004) and is therefore not to be hypothesised. Combining the most (ethically) inappropriate tactics as suggested by Lewicki and Stark (1996), Robinson *et al.* (2000) and Perdue (1992), we seek to explain in what way aggressive tactics during the contracting procedure and within a cooperative environment are applied.

It is at the contracting stage where the above background and atmospheric antecedents (Ghauri and Usunier 2003) determine the behavioural aspect of the face-to-face negotiation process. Broadly speaking, the contracting stages are split into the phases of the initial offer, discussion, adjustment, preparation and negotiation phase (Ghauri and Fang 2001). Here we treat them as one procedural entity. We are further interested in the contextual design of long term relational or potentially transactional contracts, as well as their future usage (Roxenhall and Ghauri 2004). In this context, Fortgang *et al.* (2003) refers to social versus economic contracts which indeed can be complementary. Contextual design here is defined as “the actual detailing of Service Level Agreements (SLAs) as well as their corresponding Key Performance Indicators (KPIs)” (Van Weele 2005). Whilst the entire contract normally consists of legal, security and

other terms and conditions, SLAs embrace the general idea of what is expected and to which quality level (KPIs) and thus reflects the core of the deal.

Although power/dependence sources, as well as expectations may share common ground between the parties, there is almost always room for improving one's own margin (Ghauri 2003a). Kale (2003) is convinced that organisations with the characteristics of high conformity standards, centralised and collective decision-making policies, complex organisational structures and formalised procedures may enforce rules upon employees for negotiating contracts. Therefore, it is logical to suggest that such dimensions are more likely to be found in MNEs and their strategic procurement dealings. Nonetheless, cultural discrepancies, individual differences and the usage of inappropriate negotiation tactics might yield distorted behaviour at this stage and derive conflicting situations (Martin and Herbig 1997). This of course also holds true for the level of future usage of the contract, which hereafter is referred to as the "frequency of technical and administrative control based on the signed contract" exercised by the parties as seen in Roxenhall and Ghauri (2004). As a result, it is our interest to understand whether the identified antecedents have any impact on the contextual design and future usage within an MNE setting.

2.7 Negotiation outcome and conflict

A satisfactory, as opposed to a dissatisfactory agreement between the parties, is the most obvious outcome variable as a measure of successful negotiations. In this light, Shanley and Correa (1992) point to the high match between perceived and actual agreement in the interest of the firm. Thompson (1990) adds in that such a *positive bargaining zone*, negotiators profit from this mutual or joint agreement. The dual concerns model (Pruitt and Rubin 1986) teaches us that concern for oneself, plus concern for the other party leads to increased joint outcome (Ben-Yoav and Pruitt 1984), and hence puts an interesting spin to the causal link between aggressive negotiation tactics and contracting procedures. Additional clues are given by Janda and Seshadri (2001), who link effective purchasing strategies and their outcomes to lasting supplier-buyer relations, as well as the compliance to anticipated quality levels in terms of the product/service. Reynolds *et al.* (2003) also point to individual profits (Graham 1986) and joint gains. As described by Sharland (2001), technical activities such as preparation, levels of support from

other departments, negotiation speed and senior management involvement may be explanatory variables as to how relationship building within buyer-supplier arrangements is achieved.

Most interestingly hence, is the formation of the question as to whether increased contractual input and usage may raise performance levels. This is in terms of a satisfactory agreement and a continuously rising degree of relationship quality (Kale and Barnes 1992; Luo 1999) for both the buyer and supplier. It is also of interest to see if there is a decreased likelihood of opportunism (Heide *et al.* 2007) at the same time.

Picking up on the argument that micro-behavioural determinants may derive divergences, conflict is an important variable. Conflicting views or even deadlock are common in international negotiations and yet understudied (Persson 1994). Even though parties desire a mutually sound and timely solution to a given problem, differences in cross-cultural cognitive conflict, as well as policy cause conflict and may stop the parties from doing so (Brehmer *et al.* 1970; Black and Mendenhall 1993; Gulbro and Herbig 1999; Friedman and Antal 2005). Saner (2003) pays tribute to conflict arising from different personality- or in this case, interpersonal attributes. Last but not least, the application of tactics on conflict (aggressive or otherwise) is by no means clear cut. The direct cause of antecedents of contracting procedures to conflict situations is an auxiliary thought that finds its roots in the aforementioned arguments about organisational cultures found in MNEs. Therefore, we will seek to find an answer to a proposition that is based on the assumption that with more detailed contracts, as well as frequent future use of it, conflicting situations should tend to decline.

3. Hypotheses, model and next steps

3.1 Comparative study and unit of analysis

One major contribution that we aim to achieve is the comparative analysis of dissimilar industries. To date, little attention has been paid to cross-industrial studies. Cho and Chu (1994) are among the few, who have looked at contracting procedures within an unbalanced dyadic relationship in terms of bargaining power, contained by the specific circumstances of the manufacturing industry. Whilst their paper neglects the measures we have identified, vital clues

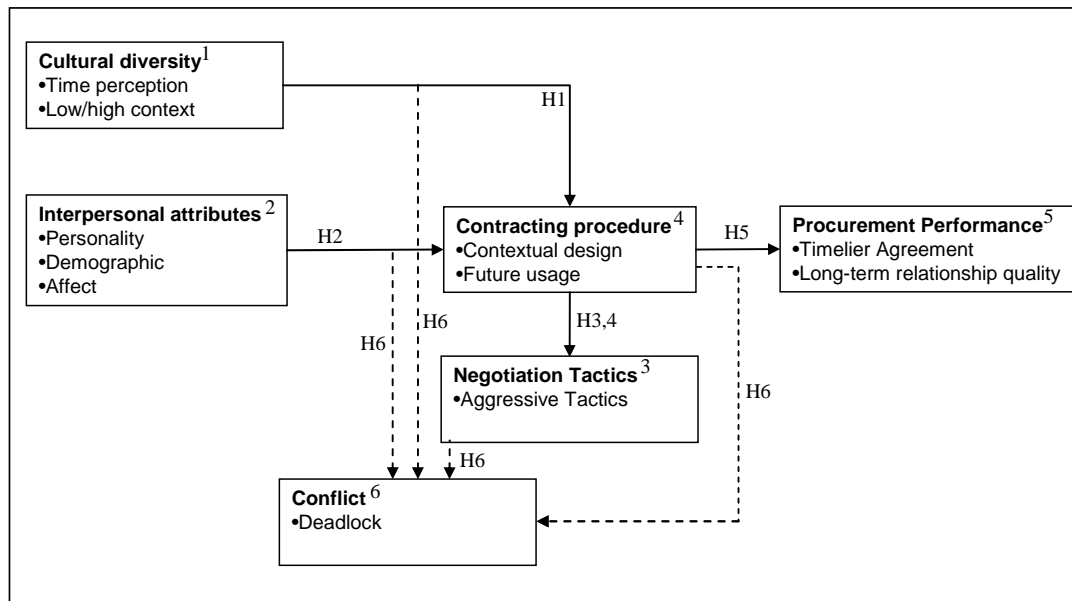
are given with regards to specific industry sectors entailing a unique set of characteristics. A more detailed picture is provided by Gulbro and Herbig (1995b), who conclude that whilst service-oriented companies put more emphasis on behavioural orientation, manufacturers tend to avoid extensive humanistic rapport building. The authors also point to the likeliness of industrial product firms to be more tactical and more compromising during the contracting procedures. Consumer product firms, on the other hand, focus on solidifying agreements and believe in their strong understanding of cultural aspects (Gulbro and Herbig 1995a). As a result, one can predict that the answers to the propositions may differ according to unique industrial settings. Henceforth, the unit of analysis that we will follow primarily focuses on the company that the individual represents, as well as the industry sector. The other key factors of cultural diversity, interpersonal attributes, contracting procedures and negotiation tactics are extrapolated and measured on an individual level.

3.2 Hypotheses and model

Resulting from the literature review, the following six main hypotheses were developed to shed light onto the exposed knowledge gaps. Owing to the nature of the subject area, we are seeking to expose tendencies on a continuum, as opposed to a black and white approach (Herbig and Gulbro 1997). Therefore and regardless of the industrial sector, we will test the following hypotheses:

- H1:** Cultural differences between the parties do not tend to influence the contracting procedure.
- H2:** Interpersonal attributes of the parties do not tend to influence the contracting procedure.
- H3:** The higher the level of the contracts' contextual design, the lower the intensity of applied negotiation tactics.
- H4:** The more often the contract is referred to in the future, the lower the likelihood that negotiation tactics are applied.
- H5:** Higher levels of the contracting procedures' engagement result in increased procurement performance.
- H6:** Conflict does not arise because of cultural diversity, different interpersonal attributes, contracting procedures or the use of negotiation tactics.

The resulting model, shown in Figure 3, has been designed in a way that allows for both a qualitative (interview based explanatory information) and quantitative (questionnaire based multivariate) analysis.



Sources: ¹) Ghauri (2003b); ²) Brooks and Rose (2004), Alexander *et al.* (1994); ³) Perdue (1992), Lewicki and Stark (1996); ⁴) Roxenhall and Ghauri (2004), Van Weele (2005); ⁵) Thompson (1990), Janda and Seshadri (2001); ⁶) Persson (1994), Saner (2003), Pruitt (1981)

Figure 3: Proposed interdisciplinary research model

As the main hypotheses can be broken down into more detailed elements, we have further developed a set of sub-hypotheses to be able to work through each of the causal links of the individual items (see Table 1). This will both allow us to comply with academic rigour and extract more meaningful and accurate answers from our study participants. The next steps will involve the accumulation and analysis of participant information, which will then be aggregated to form the tendencies this research has set out to discover.

H1a:	Different cultural time perceptions of the parties do not tend to influence how frequently a contract is referred to in the future.
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H1b:	Different cultural context perceptions of the parties do not tend to influence how the contextual design of the contract is specified.
H2a:	Differing personality traits of the parties do not tend to influence how the contextual design of the contract is specified.
H2b:	Differing personality traits of the parties do not tend to influence how often a contract is referred to in the future.
H2c:	Differing demographics of the parties do not tend to influence how often a contract is referred to in the future.
H2d:	Differing demographics of the parties do not tend to influence how the contextual design of the contract is specified.
H2e:	The affect of the parties does not tend to influence how the contextual design of the contract is specified.
H2f:	The affect of the parties does not tend to have an influence how often a contract is referred to in the future.
H3 & H4:	do not require further sub-hypotheses
H5a:	The more often the contract is referred to in the future, the higher the likelihood that agreements are signed more rapidly.
H5b:	The more often the contract is referred to in the future, the higher the likelihood that an elevated long-term relationship quality can be achieved.
H5c:	The higher the level of the contracts' contextual design, the higher the likelihood that agreements are signed more rapidly.
H5d:	The higher the level of the contracts' contextual design, the higher the likelihood that an elevated long-term relationship quality can be achieved.
H6a:	Cultural diversity does not tend to cause a conflict situation.
H6b:	Differing interpersonal attributes do not tend to cause a conflict situation.
H6c:	The application of negotiation tactics does not tend to cause a conflict situation.
H6d:	Higher levels of contracts' contextual design and future usage result in lower levels of conflict.

Table 1: Sub-hypotheses

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