

Procurement and Supply Chain

Prepared by Dr. Tarek Mohamed

MGM 431

Lecture 7



Negotiation skills, practice and business

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Course Agenda

Chapter

1. Understand the meaning of negotiation.
2. Negotiation” as an executive tool-buyer perspective.
3. Understanding the different issues of negotiation.
4. Explaining the key negotiation vocabulary.
5. Describe the good and bad time for negotiation.
6. The different steps in negotiation a contract.
7. Discussing the strategic approach to negotiation.

“Negotiation” Defined

- Negotiation is a process by which two or more parties, linked by mutual dependence but with some apparent conflict, seek to achieve a better outcome through a jointly agreed-upon.
- Back-and-forth communication to reach an agreement, when some interests are shared and some are opposed.

“NEGOTIATION” AS AN EXECUTIVE TOOL



“NEGOTIATION” AS AN EXECUTIVE TOOL-BUYER PERSPECTIVE



**Price and Cost
Analysis**

**Negotiation
Position(s)**

Negotiate

Reach Agreement

Award Contract

★ **External Negotiation:**

- ★ Supplier agreements
- ★ Customer contracts
- ★ Purchase of property or equipment

★ **Internal Negotiation:**

- ★ Budgets, resource allocation
- ★ Work schedules
- ★ Work sharing on projects or reports
- ★ Decisions with conflicting priorities
- ★ Interpersonal problems and conflicts

Why are Negotiations Increasingly Important in Business?

1-Structural changes in organizations

- ✳ New authority relationship $\Rightarrow$ broader range of relationships
- ✳ Skills in negotiation, decision making, problem-solving important

2-Increasing use of teams in organizations

3-New relationships between organizations

- ✳ Partnerships, alliances, old-new economy partners

4-Globalization

- ✳ Cross-cultural relationships
- ✳ Relationships conducted through technology

5-Technological advances

- ✳ People more accessible; more people accessible

Key Negotiation Vocabulary

- **Non-negotiable points:** These issues are necessary and cannot be subjected to negotiations (for example, providing more favorable financing than permitted by organization policy).
- **Concession items:** These issues are relatively low in importance but may be considered by the Other party to be extremely valuable. Typically, providing these concessions to the other party may result in concessions from the other party.
- **Avoidance issues:** These are issues that the negotiator does not want to discuss during negotiations because they may represent weak points in the negotiator's position.
- **Bargaining issues:** These are issues where the negotiator may be willing to engage in meaningful give-and-take to achieve a fair and reasonable price.

Key Negotiation Vocabulary

- **Objective position:** This position represents the best estimate of a fair and reasonable price, which is the pre-negotiation objective.
- **Minimum position:** This position represents the lowest buyer value for a fair and reasonable price and highest seller value for a fair and reasonable price and should be usually be used by the buyer as the first counteroffer to an offer. Any lower price would represent an unreasonable price.
- **Maximum position:** This position represents the highest buyer price considered (by the buyer) to be fair and reasonable and lowest seller price considered (by the seller) to be fair and reasonable. The buyer should base this on market research or cost analysis, subject to the availability of funds.

Key Negotiation Vocabulary

- **BATNA:** The “Best Alternative to a Negotiated Agreement”. This may be an alternative Buyer (for the seller) or an alternative Seller (for the buyer). It may also be NO AGREEMENT AT ALL.
- **Walk-Out Price (WOP):** This is sometimes called Reservation Price or Required Price (RP). This is normally the Buyer’s maximum and the Seller’s minimum. When a party cannot negotiate a more favorable price than its “WOP”, the negotiation is normally considered ineffective and the party which has reached its “WOP” should normally terminate the negotiation.
- **Zone of Potential Agreement (ZOPA):** When there is an overlap between the Buyer’s maximum and the Seller’s minimum, there is a good chance the parties will be able to reach an agreement somewhere within this overlap or “ZOPA”. When there is no overlap between the two, the negotiation cannot succeed unless one or both of the parties moves its “WOP”. Empirical evidence shows that most negotiations end up somewhere in the original “ZOPA” and somewhere near the midpoint of the Seller’s Maximum and the Buyer’s Minimum (typically opening) price.

Buyer and Seller Success Factors

Buyer

- Prepare adequately and completely
- Establish an upfront and respectful tone
- Establish and maintain effective communications
- Deal with issues honestly and forthrightly
- Encourage the cooperation of the entire team
- Exercise sound business judgment

Seller

When Is It a Good Time to Negotiate?? (Buyer's Perspective)

- When you are making a purchase for a new item.
- When the potential rewards in the long run are higher than accepting the original offer.
- When you have been giving or expect to give an ever-increasing amount of business to a supplier but are still getting the same high-volume price.
- When new untried suppliers are trying to obtain business and are giving you rather attractive bids and your existing supplier is performing very well.

When Is It a Good Time to Negotiate?? (Buyer's Perspective)

- When you are in no hurry to place an order but know you will need the material or service in the future.
- When it is a buyers' market and it has been over a year since you discussed your on-going purchases with an existing supplier.
- When the news media reports that prices for the products/services you purchase are doing down but you have received no reduction from your supplier.

When Is It a Good Time to Negotiate?? (Buyer's Perspective)

- When you are well informed about the product, the company you are going to deal with, and know the state of the marketplace.
- When the supplier is in a hurry to make an agreement with someone quickly.
- When the supplier announces a general increase or a supplier tells you he must increase prices.
- When you are trying out a new contract type or contracting procedure that may be unfamiliar to your suppliers.

When Is It a Bad Time to Negotiate?? (Buyer's Perspective)

- When you need the product or service immediately.
- When you are in a hurry or have a limited amount of time to spend.
- When it is a seller's market and it has been over a year since you discussed your on-going purchases with an existing supplier.
- When the news media reports that prices are going up, but you have received no hint of any increase from your supplier.
- When you don't have enough facts.

When Is It a Bad Time to Negotiate?? (Buyer's Perspective)

- When you don't know the product/service you are buying.
- When you don't know anything about the company you are going to deal with.
- When you don't know conditions in the marketplace.
- When you are tired, under stress, or emotionally upset.
- When you don't know the limitations of authority of the people you are dealing with.

When Is It a Bad Time to Negotiate?? (Buyer's Perspective)

1. When you don't know your own authority to make concessions.
2. When the supplier knows your business is failing, or that your company is near bankruptcy.
3. When you have not received adequate education and training on negotiation strategy, tactics, and procedures.

When is Negotiation Needed?(Buyer's Perspective)

- The lowest quotation appears to be unreasonable as to price.
- The buyer is contracting a large number of items at one time.
- The item/service has a high mark-up or profit factor.
- The buyer does a large volume of business with the supplier.
- There are alternative ways of furnishing the product or service.
- The low bidder has taken exception to the specifications or delivery conditions.
- There are agreement terms and conditions that buyer and supplier cannot agree to.
- The quotation can be made more advantageous to the buyer through negotiation.
- The delivery time needs to be improved.

When is Negotiation Needed? (Buyer's Perspective)

Whenever the Buyer (and Supplier) wish to arrive at a “QUALITY CONTRACT”.

When is “Negotiation” Or “Bargaining ”Used?

BARGAINING?

An “informal” process, often involving “Haggling” over price.

NEGOTIATION?

**More “formal” process that occurs when parties are trying to find
A mutually acceptable solution to a complex conflict.**

Characteristics of a “Negotiation ”Situation

- Intrapersonal, Interpersonal, Intragroup, or Intergroup process
- Conflict of Interest between two or more parties
- Parties negotiate because they think they can use some form of influence to get a better deal than by simply taking what the other side offers
- Parties prefer to search for agreement rather than “fight”
- When we negotiate, WE EXPECT GIVE AND TAKE!
- Tangibles (price) v. Intangibles (Need to look “good”, desire to “book” more business, save “face”, setting precedent for future, etc.)

What Issues Are Negotiated?

Intangibles may be as or more important than tangibles

✿ Division of tangibles

✿ The substance of the deal

- ✿ Rate / price / volume
- ✿ Terms: Delivery date, etc.
- ✿ Features / quality
- ✿ Wording of agreements
- ✿ Specific settlements

✿ Resolutions of intangibles

✿ Emotional / psychological factors

- ✿ “Winning”
- ✿ Beating the other person
- ✿ Standing by principles
- ✿ Maintaining precedent
- ✿ Saving face, looking good to my constituency
- ✿ Being fair

Steps in Negotiating Contract (Buyer's Perspective)

- ✿ Planning/Preparation
- ✿ Organization
- ✿ Fact-finding
- ✿ Objectives
- ✿ Pre-Negotiation Review
- ✿ Negotiation Conference(s)
- ✿ Documentation

Steps in Negotiating a Contract (Buyer's Perspective) Planning/Preparation

- The **first step** of planning or preparation is probably the most important.
- Includes the processes of price and cost analysis, the development of the buyer's preliminary negotiation position(s) based upon those analyses and planning the strategy and tactics for the impending negotiation conference(s).
- One important product of this step is the agenda for negotiation,

Steps in Negotiating a Contract (Buyer's Perspective) Organization

- The **second step** is organizing the buyer's team and establishing the ground rules to be followed by the various members of the team.
- The buyer will generally want his technical representative and his cost person to attend the more complex negotiation sessions.

Steps in Negotiating a Contract (Buyer's Perspective) Fact-Finding

✳ **Can be done in two major ways.**

1. The best way is go over the proposal with the supplier team in advance of the negotiation conference in order to understand their problems and approaches and to know where to look in greater depth. Such preliminary discussions are not meant to end in an agreement on anything, since such agreements should be reserved to the negotiation conference.
2. The other way is to use the first part of the negotiation conference for fact-finding, essentially making the negotiation a two-stage affair.

Steps in Negotiating a Contract (Buyer's Perspective) Objectives

- After the facts are known and the issues relating to those facts are resolved, the buyer team must identify those issues which still remain and formulate positions on those issues.
- The buyer is reevaluating his/her position prepared in the planning step.
- The buyer should think of a range of positions, all the way from the maximum price he/she is willing to pay to the rock bottom position he/she would like to pay assuming everything goes right in the negotiation. Somewhere in the middle would be what the buyer really expects to pay (target or objective position).

Steps in Negotiating a Contract (Buyer's Perspective) Pre-negotiation Review

- Most buyers have to seek higher level approval for their negotiation positions.
- This higher-level approval will require him/her to document the basis for his positions, including the documentation of the price and/or cost analysis performed.

Steps in Negotiating a Contract (Buyer's Perspective) Negotiation Conferences

- In the negotiation conference(s), the buyer team brings to the “table” its planned strategy and tactics as well as its plan for achieving its cost and profit positions.
- This lecture covers this process in some detail and from different perspectives.

Steps in Negotiating a Contract (Buyer's Perspective) Documentation

- The buyer prepares a negotiation memorandum.
- The negotiation memorandum tells the story of the negotiation and justifies the final price and other final agreements to management.

Recommended Format for Negotiation Memorandum

- Summary comparisons reflecting the cost and profit/fee elements according to the in-house estimate, according to the supplier's cost proposal, as a result of the buyer's pre-negotiation cost and price analysis, and as a result of negotiation.
- Discussion of reasons for differences between pre-negotiation and final negotiated positions on all issues negotiated.
- Identification of final cost data and the degree to which the data was relied upon.
- Identification of supplemental information and data obtained during negotiation and evaluation of the information/data which shows how the information/data supports the price and other terms negotiated.
- Attachments should include all documents submitted and used during the negotiation.

The Two Major Negotiation Strategies

Characteristic	Win/Win Style	Win/Lose Style
Negotiation goal	Obtain a result that is satisfactory to both sides, including a fair and reasonable price	Obtain the best possible deal for one side, regardless of the consequences to the other side
Focus	Solve mutual problems	Defeat the other party
Environment	Cooperation and trust	Mistrust and gamesmanship
Negotiation characteristics	■ Negotiators attack the problem, not each other ■ Focus on long-term satisfaction ■ Available alternatives considered ■ Results based on objective standards ■ Focus on positive tactics to resolve differences ■ Emphasis on a win/win result	■ Tactics designed to increase or emphasize relative power ■ Focus on negotiating positions rather than long-term satisfaction ■ Argumentative ■ Reluctance to make any meaningful concessions ■ Highly competitive

- ✱ **Simultaneous Development of Goals & Frames.**

- ✱ **Direct Effects of Goals on Choice of Strategy**

- ✱ Wishes are not goals
- ✱ Our goals are often linked to other's goals
- ✱ There are limits/boundaries to what goals can be
- ✱ Effective goals must be specific

✱ Strategic Options--Vehicles for Achieving Goals.

✱ Alternative Situational Strategies

- 1.Avoidance: The No engagement Strategy
- 2.Competition/Dominance/Forcing (Win-Lose)
- 3.Collaboration/Integrating (Win-Win)
- 4.Compromising
- 5.Accommodation/Obliging

Negotiation Goals & Strategy

★ Negotiation Goals

- ★ Short-term or long-term
- ★ Tangible or intangible issues
- ★ Compatible or incompatible

Negotiation Strategy

- ★ Be Collaborative
 - ★ Long-term goals
 - ★ Tangibles & intangibles
 - ★ Some compatibility of goals
- ★ Be Competitive
 - ★ Short-term deal
 - ★ Emphasis on tangibles
 - ★ Zero-sum game

✱ **The Need for Planning--Do your “homework”!**

- ✱ Defining the Issues
- ✱ Assembling Issues & Defining the Bargaining Mix
- ✱ Defining your Interests--Why do we “want” it?
- ✱ Consulting with Others
 - ✱ Constituencies
 - ✱ Other side

★ **The Need for Planning--Do your “homework”!**

- ★ Assessing the Other’s Priorities

- ★ Knowing your Limits

- ★ **Setting Targets**

 - ★ Where to start--Optimistic, Realistic, or Pessimistic

 - ★ Anticipation of “Packaging” among Issues/Objectives

 - ★ Understanding of Trade-Offs and “Throwaways”

Strategic Approach to Negotiation: PLANNING

★ **The Need for Planning--Do your “homework”!**

- ★ Developing Supporting Argument--Research

- ★ Analyzing the Other Party

 - Resources, Interests, Needs

 - Objectives

 - Reputation & Style

 - Other Party's Alternatives

 - Other Party's Authority

 - Other Party's Strategy & Tactics

Strategic Approach to Negotiation: PLANNING

1. Step 1: Brainstorm your alternatives
2. Step 2: Find your Best Alternative to Negotiated Agreement (**BATNA**)
3. Step 3: Try to improve your **BATNA**
4. Step 4: Determine your Walk-out-Price (**W-o-P**)
5. Sometimes referred to as Required or Reservation Price (**RP**)
6. Step 5: Simulate step 1 to 4 from the other's perspective
7. Step 6: Calculate Zone of Possible Agreement (**ZOPA**)

Develop your BATNA

BATNA: What you will do if the negotiation fails.

It's the alternative with which you compare any potential deal.

When developing your BATNA:

- Invent a wide range of alternatives.
- Improve on some of the most promising ones.
- Select, tentatively, the best alternative.
- Consider the other side's BATNA

Summary of Learning Objectives

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Thank You