

# Supplier Relationship Strategies in the Automotive Industry: An International Comparative Analysis

Alexandra Ioana IONESCU FLOREA<sup>1</sup>  
Răzvan-Andrei CORBOȘ<sup>2</sup>

## **Abstract**

*The automotive industry is a very important one as it has a large impact on the economies of every country and on our own lives. Analysing the supplier relations in this field is an interesting action as this industry is very mature in terms of development and application of purchasing practices. The first three world manufacturers cover 42% of the market and come from three different continents: Toyota, the leader, from Japan, Volkswagen, the second, from Germany, Europe and General Motors from America.*

*Their philosophy in terms of supplier relationship is not very different, but the implementation can really depend on the cultural specificities. This article aims to discover the differences in company culture and strategy in terms of supplier relations but also analyse the impact of these relations on annual sales. The international comparative analysis will point out whether the company culture can be easily implemented in locations all over the world or the local particularities are more important.*

**Keywords:** *supplier relationship, supply chain, procurement, international comparative management, automotive industry*

**JEL classification:** C44, M11, N80

## **Introduction**

In 2014 alone, the automotive industry sold over 71 million automobiles in the world, according to statista.com. Apart from being one of the most important industries of the world, the automotive business relies on a wide network of suppliers that have a direct and major impact on the success of each manufacturer.

Although there are five major manufacturers in the world (Toyota, Volkswagen, GM, Renault-Nissan, Hyundai-Kia), the first three of them cover approximately 42% of the market. In 2014, Toyota was the leader with no less than 10.23 million cars sold, followed by Volkswagen with 10.14 million and General Motors 9.92 million (The New York Times, 2015).

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<sup>1</sup> **Alexandra Ioana IONESCU FLOREA**, University of Economic Studies, Bucharest,  
Email: sandraionescu@hotmail.com

<sup>2</sup> **Răzvan-Andrei CORBOȘ**, University of Economic Studies, Bucharest,  
Email: razvan.corbos@man.ase.ro

As automotive manufacturers need thousands of different components in order to achieve a product that is nowadays very developed in terms of performances, security, comfort and user friendly devices, they understood from the very beginning that they had neither the capital, nor the know-how to manufacture all the spare parts in their own factories. So, they resorted to specialized suppliers, thus developing a large network of companies that not only must provide the components but in many cases answer the special needs of the OEMs in terms of philosophy of work or preserving the environment.

The first three manufacturers covering a large part of the market, and originating from three continents, this article means to analyse and compare the cultural differences in managing the supplier relationships in the following companies: Toyota, Volkswagen and General Motors. The study of management as an autonomous area of inquiry means a constant development of concepts, methods and techniques. (Zamfir, 2013)

Furthermore, the automotive industry is an ideal laboratory for studying supplier working relations (Henke, 2007) as this business has a large impact on the economies of every country and on our own lives, is a very mature industry in terms of development and application of purchasing practices and supplier working relations across the automotive OEMs are very diverse.

Supplier relations are very important in the automotive industry because its profits can be directly impacted by poor relations. Losses would have run up to \$2 billion in sales in 2014 for Ford, General Motors, FCA and Nissan, according to an economic survey that measures automakers' supplier relations and how they impact profits. (Putre, 2015)

### **1. The Japanese way: Toyota**

In 2014, Toyota was rewarded by Gartner with a third place among the best supply chains in Asia Pacific and a 22<sup>nd</sup> place in the global ranking. Toyota worked to improve inter-function communication, introducing new and better systems to collect and analyse supply chain data, and building flexibility in its production methods. They also put together information on vehicle reliability and performance from customers, suppliers and dealers in order to enhance customer care, as customer knowledge means accurate information about elements that determine the value perceived by the customer, preference for the product or company and ultimately, the willingness to pay. (Deac & Stănescu, 2014) The knowledge-based economy, impacted by the information technologies, brings to companies vast new opportunities in terms of communication and value co-creation. (Plumb & Zamfir, 2009)

According to the official Toyota website, the procurement policy stands on three pillars: fair competition based on an open-door policy, mutual trust leading to mutual benefits and local sourcing. Toyota operates a milk-run service picking up parts from multiple supplier locations delivering just-in-time to support the production. Only Toyota Manufacturing UK has no less than 800 suppliers, most of them being located in areas around the plants.

Toyota puts a great emphasis on developing mutually beneficial, long-term relationships based on mutual trust with all suppliers. This is not just a motto, as they successfully succeed, as showed by different surveys. According to an American survey, the suppliers rated Toyota among the best companies in terms of working relationships. Not less than 48% of them said they had good or very good relations with this automaker. Only 19% of them could say the same about GM. Volkswagen also got low scores (Sedgwick, 2015).

Toyota also has high expectations of the environmental and social responsibilities of the entire supply chain, and, in this way, they issued a set of guidelines to outline the responsibilities of the suppliers. This set will contribute to the sustainable development of the society, as indicated in the Toyota Earth Charter, as sustainable development is a desideratum of the humankind (Năstase & Demetrian, 2014). This philosophy is summarised in the 'Guiding Principles of Toyota', which expects its business partners to support these initiatives and practice management based on 'Respect for people'. As seen in Niculescu (2014), successful employee engagement leads to higher efficiency, and a more motivated workforce.

The supply chain set of responsibilities implies commitments not only for the suppliers, but also for Toyota. The company commits to principles like providing a safe environment in which the supply chain may operate or treating all suppliers fairly, without discrimination. The suppliers must comply with workforce rights (health and safety, working hours, rates of pay and others), environmental considerations, community involvement, sub-supplier management. Working hours and holiday planning are very important, as in Japan employees have short periods of vacation and they all go on holiday at the same time. (Popescu, 2011)

Planning Perspectives is a research company, leading authority on company-supplier working relations. It leads surveys that reveal a lot of insights about the automotive industry, gathered in the Annual Automotive Industry Study. The 2015 study shows that Toyota has been ranked amongst the first places for a long period of years, since the study's inception in 2002. For the fifth year in a row it's holding the first place at supplier relations. Henke, the CEO of Planning Perspectives, explained this position with one word: commitment. Toyota takes very seriously supplier relations and particularly the purchasing department works with suppliers on a daily basis. It's important for the OEM to achieve foundational activities in relation with their suppliers, activities which fall into two categories. One involves the business practices side of the purchasing function and the other category, the OEM's buyers themselves and their ability to do the job. The study shows that the suppliers with good relations with an OEM provide considerable benefits like investing in new technology and sharing it with the company, supporting beyond contractual terms, communicating more openly and honestly with the OEM and giving greater price concessions.

Toyota proves that its commitment goes beyond making cars by organising each year the Opportunity Exchange forum, where no less than 1700 attendees can meet Toyota officials. Everyone can register to this event and can eventually

become a Toyota supplier, if they meet the set of responsibilities established by the company. Small companies, with two or three employees, or companies run by women can become suppliers and grow together with Toyota, as showed by many examples. In the US, the company Forma Automotive LLC, managed by Rosa Santana has just become a direct supplier of Toyota, being the first of this kind managed by a woman. The Opportunity Exchange means also that suppliers can meet each other and begin business relationships between them.

Even if Toyota became the largest vehicle manufacturing company in the world in 2008, a series of events impacted its sales during the years throughout 2013. After the financial crisis triggered by the sub-prime mortgage debt, Toyota was affected by the unintended acceleration problems at its own cars, but also by the 2011 earthquake and tsunami disaster in Japan which led to shortages in inventories, exactly when the market began to move again. According to IHS Automotive, one of the factors that helped Toyota manage to regain its first place in world sales was the fact that its suppliers supported the OEM during those years. This meant that after a period when production lowered, the suppliers made efforts to increase the part volumes, even if this meant a lot of investment.

In a 2007 interview given by Mark Adams for Supply Business, senior general manager of purchasing at Toyota Motor Europe at the time, he emphasized the fact that the philosophy in working with suppliers relies on 'the Toyota way' values. Its key pillars are continuous improvement and respect for people. The negotiations between the OEM and the suppliers are near to an open-book negotiation. The purchasing organisation is composed by the buyers, which ask for quotations and discuss the price, and the purchasing engineers that go to the suppliers' factories and work with them on improvement activities. Mark Adams describes the behavioural purchasing as tough, but fair, professional and human, and logical. Toyota tries to act as a partner with all suppliers, and does not segment them into strategic and non-strategic. For Mark Adams, all suppliers should be strategic. Also, Toyota's approach is to have a manageable number of suppliers and the differentiation in treatment is related only to the time spent on the shopfloor by their engineers. The Japanese Toyota business practice is mirrored across the countries, as it means a formalised approach to problem-solving and one of the key elements of improving the activity with the suppliers. It's a standardised process worldwide, linked to a never-ending quest for kaizen, added Mark Adams. Even if regional variations in practice exist, the fundamental DNA of Toyota methodology can be identified everywhere.

The relationship between Toyota and its suppliers is yet not always the same and not always improving, as showed in the 2014 global study on OEM-supplier relations made by IHS Automotive. The SuRe index, developed by IHS is based on an annual survey of the automotive supply industry, including the participation of more than 1000 senior to middle managers working at automotive suppliers. The study includes views of representatives of 51 of the world's top 100 automotive suppliers. In 2014, Toyota and BMW occupied the top positions, but their scores were are much lower compared to 2006 and 2007 highs. OEMs are

again pushing the limits of cost reduction and several suppliers are drawing attention to the return of unwelcome practices. But still, Toyota is seen as a trustworthy organization and had exceptional results in Europe, where suppliers indicate it as the customer most willing to excel in quality and technology.

Toyota's relationship with suppliers can also be described as lean supply chain. Initially, lean manufacturing was used to describe the Toyota Production System (TPS), but it was then deployed to each activity in a company. Lionel Grealou (2015) simplifies this idea using a five-step principle:

1. Identify value: specify what creates most value from the standpoint of the end customer;
2. Map the value stream: identify the key value-added steps in the value stream, reducing or eliminating the non value-added activities;
3. Create flow: define the tight sequence of value-creating steps so the product will flow smoothly toward the customer;
4. Establish pull: as flow is introduced, let customers pull value from the next upstream activity;
5. Seek perfection: optimize the flow by removing waste.

Liker (2006), after a thorough analysis of the Toyota way, turned up with 14 principles that characterize TPS. The eleventh principle is related to the relationship with the suppliers. Liker points out the fact that Toyota is seen by the suppliers as the best client but also the most demanding, this meaning very high excellence standards. This excellence is sought in innovation, engineering, manufacturing and global reliability of the suppliers. From the very beginning Toyota understood that it could not manufacture itself the thousands of components that make up a car, and that it was essential to find solid partners. As the employees, the suppliers became members of the extended family that built its competence and success. Even after internationalisation, Toyota conserved the partnership principle and the new suppliers were at first evaluated for a long period of time and they got only small orders. The suppliers had to prove their engagement towards the very demanding quality, cost and delivery standards. Toyota does not change a supplier just because they found cheaper elsewhere, but helps them improve and teaches them how to reach the ambitious goals.

## **2. The European way: Volkswagen**

Analysing the Volkswagen group is more difficult because of its own nature. The group comprises twelve brands from seven European countries, as shown on their website: Volkswagen passenger cars, Audi, Seat, Skoda, Bentley, Bugatti, Lamborghini, Porsche, Ducati, Volkswagen commercial vehicles, Scania and Man. Volkswagen acquired throughout the years these brands together with the manufacturing plants, keeping each brand's own character and operating as an independent entity on the market. Also, as McElroy (2012) points out, Volkswagen made a choice of building a lot of components in-house, being a very vertically integrated company. In 2006, its volume of procurement, of about € 60 billion per

year, corresponded with a purchase quota of around 60% to 70%, as shown in the Sustainability in Supplier Relations at Volkswagen report.

Although the procurement strategy is the same for all VW plants, the IHS 2014 study rates independently each brand of the group in terms of supplier relations. The best SuRe index is received by the high end brand Porsche, followed closely by Audi. The sport brands find themselves on the top of the ranking, among the first 12 brands in the world. Volkswagen and Skoda are at the middle of the ranking, but with rates above the average. Seat is at the bottom of the ranking, with very bad scores. This results show that differences in company culture can have a direct impact on the performances.

Although the manufacturing operations are decentralised, Volkswagen put in place a procurement strategy, based on sustainability in supplier relations. According to the group website, the four goals of the supply activity are:

1. to actively shape the technical and environmental innovation processes in order to provide market-centric premium quality and innovations at competitive conditions;
2. to meet cost targets and ensure the profitability of the products over their entire lifecycles;
3. to ensure stable and efficient flows of goods and safeguard global volume growth through the permanent availability and consistently high quality of procured components;
4. to create optimal conditions so that we can continue to raise employee satisfaction and the attractiveness of the procurement function.

Volkswagen launched in 2014 the FAST initiative – Future Automotive Supply Tracks – in order to strengthen the working relationship with the suppliers, including all brands and regions. This program is based on 7 basic principles: future, innovation, globalization, transparency, commitment, dialog, speed. At the beginning of 2015, the group nominated the first 44 suppliers that would take part in this initiative, after a selection process. These suppliers are to be involved in the relevant product innovation cycles within the group at an even earlier stage than previously and the production networks will be harmonized even more closely in order to generate further synergy effects and derive the optimal benefit, as shown on FAST website. The new procurement philosophy is explained by Dr. F.J. Garcia Sanz, member of board, pointing out that no longer the negotiating skills bring advantage to a corporation, but an optimal supplier network.

Also, Volkswagen is now implementing a mechanism, in which all procurement processes and systems are optimized and standardized, in order to achieve maximum transparency and a high degree of consultation and integration within the group.

### **3. The American way: General Motors**

Although GM was the third manufacturer in the world in 2014, the company doesn't seem to have a very good relationship with its suppliers. The 2014 IHS survey grants it a low SuRe index of only 500, being under the average

of 504. Many efforts were made during the last years to improve this relationship, but there is something in the genes of GM that prevents it from reaching the levels of contentment of suppliers achieved by the first two world car manufacturers.

After 6 years of study, between 2002 and 2007, the company Planning Perspectives observed that in the United States, domestic OEMs (Chrysler, General Motors and Ford) had worst supplier working relations than the foreign domestic ones (Toyota, Honda and Nissan) (Henke, 2007).

It's clearly that the Japanese companies put more emphasis on good relations with suppliers than the American ones. Furthermore, only 8 percent of the GMs suppliers rated that they had 'good to very good' relations.

In 2005, Bo Andersson, Chief Procurement Officer of General Motors, launched a programme to improve supplier relationships. In an interview given to SupplyBusiness.com in 2007, Andersson reveals its philosophy, as the company was doing well on the hard metrics: delivery, quality, programme launches and productivity, but lower on the soft metrics: communication, teamwork, availability, visits on supplier's plants. The objectives of the initiative were to improve the hard and soft metrics, analyse whether spending more time with the suppliers had an impact and getting to know better the plants of the suppliers. Every buyer needed to have a better understanding of the part, the production process and the cost structure of the ingoing components. The idea was to work with the suppliers in order to help them reduce their costs, not only demanding the price cuts. Andersson also explained the segmentation of their suppliers in three main groups: large global suppliers like Lear and Bosch, which needed less help as they had a lot of expertise in the field, smaller and mid-sized companies that needed more help and local suppliers in emerging markets. He also put in place a senior communications programme with the top 300 suppliers and strengthened the working relationship with engineering.

As a result of the way GM has treated its suppliers in the past, one of the biggest components company, Delphi had to go through a bankruptcy procedure in 2006. (Nussel & Barkholz, 2006) Formerly owned by GM, Delphi became an independent company in 1999. During this process, Delphi revealed shocking losses on thousands of GM contracts and sought permission to call off the contracts and renegotiate them as GM had forced prices down. In a 2006 interview for Automotive News, Julie Brown, CEO of Plastech Engineered Products Inc., a plastic parts maker supplying the automotive industry, characterized the model of the industry as really wrong. The suppliers are pressured by the raw materials distributors and also by the customers who are pushing down the prices. (Brown et al., 2006)

Like Bo Andersson in 2005, another purchasing chief from GM, Grace Lieblein put in place in 2014 an initiative to forge deeper strategic partnerships in its supply base. (Colias, 2014) The Strategic Supplier Engagement program offered advantages as better access to GM purchasing brass, joint strategic planning and training for those suppliers rating highly on several key measures – from cost containment and other basics to 'cultural' aspects such as open communication and

technology sharing. With this move, GM wanted to convince the suppliers to deliver technology in areas such as safety and fuel efficiency.

All these plans improved the scores of GM that defined the relationship with the suppliers, but it was clearly not enough, seeing the last scores from 2014. The report done by the consultancy company Planning Perspectives concluded that even if GM put in place a good leadership, it was the poor execution by buyers who interface with suppliers that led to the poor scores. (Colias, 2014) Lieblein pointed out the difficulty in driving her message through GM's 6,000-employee purchasing enterprise, as the cultural change is hard to get all the way through the organization, explains Colias (2014).

### **Conclusions**

The first three automobiles manufacturers in the world come from different countries, even continents. Even if their annual sales are not so different, around 10 million cars per year, and their philosophy, strategy and principles concerning the relationship with the suppliers are very similar, the implementation is not always the same and the ratings are very different.

Toyota received very high rates from the consultancy companies and in all the suppliers' surveys and this is not accidental. They not only put in place procurement policies and guiding principles, but also successfully implement them in the day-to-day work of the employees that come into contact with suppliers. Even if their plants are in Japan, Europe or America, the Toyota way is thoroughly respected and believed in, proving that TPS - Toyota Production System is a real and successful way of conducting a business.

Volkswagen group proves that decentralised management in diverse plants, especially in Europe, leads to large differences in rating. Although the group tries to implement the same procurement strategy, cultural particularities leave their mark on the way suppliers are treated.

General Motors exemplifies how big companies are resistant at change. Although for years GM managers have become aware of the importance of good supplier relationships and have tried to put into place programs in this way, the employees will not change very quickly their approach.

The conclusion of this analysis is intriguing, as very different approaches lead to similar results on the market. Their philosophies are the same but their implementation is very different. And yet, the annual sales of these three giants are all around 10 million cars, showing that management can be very diverse but still leading to outstanding results in business.

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