

Negotiation- Porto Case

Buyer's Information - Porto

Gerald Stecklen, a buyer for Porto, is responsible for developing a negotiating plan and strategy for the purchase of a component (called New Prod) for a newly designed product. After evaluating the quotations submitted by potential suppliers, he has decided to pursue purchase negotiations with Technutronics.

New Prod was designed and developed by Porto engineers for a product currently under development. Prototypes of the component were produced by a small specialized firm without production volume capacity. Gerald knew the high tech industry had between five and eight potentially qualified suppliers who were familiar with the complex manufacturing process required to produce New Prod. Supplier capacity was available since the industry was just recovering from a period of underutilization.

Seven suppliers received a request for quotation. The RFQ included a 12 month delivery schedule for 200,000 units plus a possible follow-on order for up to 200,000 units. The quotes also included payment terms and shipping (F.O.B. point) information (Exhibit 1B)

Five of the seven suppliers receiving RFQ's responded. (Exhibit 2B). Technutronics had the lowest quoted price at \$5.90 per unit. Tyler Manufacturing was very close except for a high unit cost of transportation. Both companies were acceptable suppliers and Gerald decided to pursue negotiations with Technutronics. He is well aware that the lowest quoted price does not always mean the lowest total cost. For that reason, Gerald knows that issues besides price will have to be discussed with Technutronics. The requests for quotation were intended to reduce the list of suppliers before commencing negotiations.

Gerald requested a cost estimate for New Prod from his staff analyst to help him formulate his negotiating plan. The analysis (Exhibit 3B) provides a "should" cost of \$4.10 per unit excluding tooling and transportation. This cost included learning curve effects. He believed that production times for this component should decrease as volumes increased due to learning. Based on discussions with internal engineers, Gerald estimated that production of this component should demonstrate a 85%-90% learning rate.* He was not sure, however, that this rate applied specifically to Porto since he has not visited the Technutronics facility.

Quality control measures were a vital concern for Gerald. All products were subject to strict quality guidelines and New Prod was no exception. Technutronics, Tyler Manufacturing, and Space Metals each have a record of solid performance ratings for quality and delivery. With this information, Gerald now sat down and planned his negotiating strategy.

* This means that as production volumes double from a previous level, direct labor requirements should decrease 10-15% on average.

**Exhibit 1B
Expected New Prod Delivery Schedule**

Month	Quantity
December	20,000
January	20,000
February	25,000
March	15,000
April	15,000
May	15,000
June	10,000
July	10,000
August	15,000
September	20,000
October	20,000
November	15,000
Total	200,000

Payment terms: Net 25
 Transportation Terms: Sellers Plant, Freight Collect
 Using Location: Detroit, Michigan

**Exhibit 2B
Quotation Summary**

Supplier	Unit Price	Tooling Costs	Estimated Transportation Cost Per Unit
Bauer Manufacturing	No quote	-----	-----
Metal Modes	\$6.10	\$30,000	\$0.08
Tyler Manufacturing	\$5.95	\$40,000	\$.016
Avircraft, Inc.	No quote	-----	-----
Technutronics	\$5.90	\$40,000	\$0.06
Aerobotics, Inc.	\$6.25	\$45,000	\$0.08
Space Metals	\$6.40	\$50,000	\$0.09

Exhibit 3B
Buyer's "Should" Cost Estimate
(For 200,000 units)

	Total Cost	Unit Cost
Material:		
0.3525 lbs./unit x \$5.648/lb.	\$398,215	\$1.991
Direct Engineering Labor:		
1500 hours x \$11.50/hr.	\$17,250	\$0.0863
Engineering Overhead:		
\$17,250 x 120%	\$20,700	\$0.01035
Direct Manufacturing Labor:		
3900 hours x \$8.50/hr.	\$33,150	\$0.1658
Manufacturing Overhead:		
\$33,150 x 250%	<u>\$82,875</u>	\$0.4144
SUB TOTAL	\$552,190	
General and Administrative Costs:		
\$552,190 x 35%	<u>\$193,265</u>	\$0.9663
SUB TOTAL	\$745,455	
Profit: \$745,455 x 10%	<u>\$74,545</u>	\$0.3727
TOTAL	\$820,000	\$4.10
Estimated Tooling Charges:	\$25,000	

In addition to specific requests by the instructor:

1. Given the unit price, tooling costs, and estimated transportation charges presented in Exhibit 2B, calculate the cost per unit for each supplier (using 200,000 units). What are some possible reasons why two suppliers did not provide quotations to Porto?
2. Prepare to negotiate a contract with Technutronics. Identify the key issues and the range of your position on those issues. Remember that price is not the only variable subject to negotiation.
3. What do you think will be the most important issue(s) to the seller?
4. What do you believe is the lowest price that Technutronics is willing to accept? What is the highest price for New Prod you are willing to pay? (This defines your negotiating range on the price issue).