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BUILDING LONG-TERM BUYER-SELLER RELATIONSHIPS IN FOOD CHAINS

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Abstract

Building on the extent literature of buyer-seller relationships, we develop a model that describes the relationship building process. Starting from the suppliers offer quality, we demonstrate how relational satisfaction leads to trust and the customers desire to maintain the relationship. These variables are examined in relation to the situational factors (dependence and the exchange partners willingness to make idiosyncratic investments).

Introduction

Concentration and aggregation in both the food processing and the retail sector is having a profound effect on agribusiness. With consumers becoming more concerned about the integrity of the food they consume and the impact of

quality product, industrial buyers are moving away from the vagaries of the wholesale market to establish long-term relationships with preferred suppliers.

Relationship marketing is an integral part of the developing network paradigm that recognises that global competition occurs increasingly between networks of firms (Thorelli 1986). Firms are establishing relationships with their suppliers because it enables them to be more efficient and more effective (Kalwani and Narayandas 1995). By developing relationships with their suppliers, buyers and sellers can both achieve cost savings through reduced search and evaluation costs (Hakansson 1982), reduced transaction costs and the learning effects and relationship specific scale economies (Gundlach *et al* 1995). However, the primary reason for establishing relationships with suppliers is that customers realise that suppliers create value. Developing long-term relationships can improve access to markets and more reliable market information (Low 1996). Customers can anticipate improved access to a more reliable supply of inputs, improved product quality and performance (Han *et al* 1993), and a higher level of technical interaction in the form of information exchange, potential product adaptations and technical assistance (Cunningham and Homse 1982).

Relationship marketing provides a stronger, longer-term customer benefit that is more difficult for competitors to match and it becomes more difficult for competitors to enter the market (Hakansson 1982). Buyers may become less sensitive to price competition and suppliers may benefit from higher prices (Kalwani and Narayandas 1995). Suppliers benefit from being able to better plan and forecast production schedules, coordinate deliveries and undertake joint promotions (Easton and Araujo 1994).

Offer quality

A firm pursuing a relationship marketing strategy will attempt to create more value for its customers than that which is provided by the core product itself (Gronroos 1995). Anderson and Narus (1999) describe the market offer as the set of economic, technical, service and social benefits that a customer receives. Fundamentally, the market offer is comprised of the core product, the minimally augmented product, the augmented product and conceptually, the potential product.

The minimally augmented product adds to the core product, the least amount or number of services, programs or systems that a customer considers absolutely necessary for doing business with the supplier. This will include such aspects as payments terms, delivery and the provision of those customer services that deal directly with problems arising from the use or application of the core product itself.

While price is always an important consideration in the decision to purchase, perceived value is of much greater significance. Anderson and Narus (1999) use value to express, in monetary terms, the functionality or performance of the market offer in a given customer application. Fornell *et al* (1996) describe perceived value is the perceived level of product quality relative to the price paid. Value is achieved when the proper function is secured for the proper cost. Because functions can be accomplished in a number of different ways, the most cost efficient way of fully accomplishing a function will establish its value. Here, the concept of value-in-use constitutes the price that will equalise the overall costs and benefits of using one product over another (Hutt and Speh 1995).

From the more traditional quality perspective, Fiegenbaum (1991) describes quality as a customer determination based upon the customer's actual experience with the product measured against their stated requirements. Here it is important to understand that quality does not necessarily mean best: quality means "fitness for the intended purpose". From a supplier's perspective, quality means providing customers with products that consistently meet their specifications.

In describing a supplier's offer quality, Gronroos (1990) differentiates between technical quality and functional quality. Technical quality describes the customer's specifications. This is a physical description of the product in terms of its size; shape; colour; freedom from pests and diseases; purity (in terms of its freedom from chemical contaminants, pathogenic organisms and genetically modified plants); maturity or freshness; and the manner in which the product is packed.

Functional quality describes the way a supplier goes about delivering the product to the customer. While this fundamentally means being able to deliver the product when the customer wants it, by implication, it involves many inter-related activities such as production scheduling, storage and warehousing, logistics, ordering and invoicing. Since most market intermediaries purchase products in the expectation that they will be able to resell them, the timely arrival and efficient receipt of goods is critical to the success of most downstream manufacturing and retail operations.

Service quality is the final dimension. Service quality best describes the extra things a supplier is prepared to do to retain the customer's business. However, the exact meaning of the term service varies with the nature of the product and the requirements of the buying organisation (Hutt and Speh 1995). Service may include such variables as technical assistance, innovative suggestions, credit arrangements, support for special needs or advance notice of impending price changes or shortages in supply. As such elements are different types of services, the more the firm adopts a relationship marketing strategy, the more it has to understand how to manage the service elements of its market offer.

Satisfaction

Woodruff (1997) implies that there is a strong relationship between the concept of customer value and customer satisfaction. Satisfaction (or dissatisfaction) arises from the customer's feelings in response to an evaluation of one or more use experiences with the product. According to the disconfirmation of expectations model, customer satisfaction is the result of a comparison between performance and the focal firm's expectations (Oliver 1980). Whenever performance exceeds expectations, satisfaction will increase. However, whenever performance falls below expectations, customers will become dissatisfied.

Between channel members, satisfaction is described as a positive affective state resulting from an appraisal of all aspects of a firm's working relationship with another (Frazier *et al* 1989). As such, Geyskens *et al* (1999) propose that satisfaction should capture both the economic and non-economic (psychosocial) aspects of the exchange.

Economic satisfaction is defined as the channel member's positive affective response to the economic rewards that flow from the relationship. An economically satisfied channel member considers the relationship a success when it is satisfied with the effectiveness and productivity of the relationship with its partner and the resulting positive financial outcomes.

However, satisfaction with the exchange also affects channel members moral and their incentive to participate in collaborative activities (Geyskens *et al* 1999). Both Frazier (1983) and Anderson and Narus (1990) suggest that satisfaction with past outcomes indicates equity in the exchange. Equity generally refers to the fairness or rightness of something in comparison to others (Halstead 1999). Equitable outcomes provide confidence that neither party has been taken advantage of in the relationship and that both parties are concerned about their mutual welfare (Ganesan 1994).

Firms that are able to lower the overall level of conflict in their relationship experience greater satisfaction (Anderson and Narus 1990). Conflict in channel relationships most often occurs over economic issues (Geyskens *et al* 1999). Channel members that are satisfied with the economic rewards that flow from their relationship generally perceive their partner as advancing their goal attainment as opposed to impeding or preventing it. Satisfactory conflict resolution will increase mutual trust and reinforce each members commitment and confidence that mutually satisfying outcomes will continue to be obtained (Thorelli 1986). Mackenzie and Hardy (1996) propose that as satisfaction increases so also will trust.

Trust

Anderson and Narus (1990) view trust as the belief that the partner will perform actions that will result in positive outcomes for the firm and not to take unexpected actions that may result in negative outcomes. Moorman *et al* (1993) define trust as the willingness to rely on an exchange partner in whom one has confidence. While both of these definitions view trust as a behavioural intention that reflects reliance on the other partner, both definitions, in part, capture quite different aspects of the construct.

Moorman *et al* (1993) define trust as a belief, a sentiment or an expectation about an exchange partner that results from the partner's expertise, reliability and intentionality. This component of trust, which Ganesan (1994) describes as credibility, is based on the extent to which the buyer believes that the supplier has the expertise to perform the activity effectively and reliably.

Trust also relates to the focal firm's intention to rely on their exchange partner. Ganesan (1994) describes this component as benevolence, because it is based on the extent to which the focal firm believes that its partner has intentions and motives beneficial to it. A benevolent partner will subordinate immediate self-interest for the long-term benefit of both parties and will not take actions that may have a negative impact on the firm (Geyskens *et al* 1998).

Heide (1994) considers inter-organisational trust to be a governance mechanism that mitigates opportunism in exchange transactions characterised by uncertainty and dependence. Trust reduces the need for structural mechanisms of control (Achrol 1997) and both firms learn to become more interdependent (Kumar 1996). When trust exists, buyers and suppliers believe that long-term idiosyncratic investments can be made with limited risk because both parties will refrain from using their power to renege on contracts or to use a change in circumstances to obtain profits in their own favour (Ganesan 1994; Doney and Cannon 1997). Trust increases the partners tolerance for each others behaviour, facilitating the informal resolution of conflict, which allows the partners to better adapt to the needs and capabilities of the counterpart firm (Hakansson and Sharma 1996). Trust reduces the perception of risk associated with opportunistic behaviour, it increases the buyer's confidence that short-term inequities will be resolved and it reduces the transaction costs in an exchange relationship (Ganesan 1994).

However, trust between firms does not occur automatically. Experience with the channel partner breeds trust (Dwyer *et al* 1987; Anderson and Weitz 1989). Achieving a trusting relationship and a reputation for trustworthiness requires a deliberate strategy of forbearance with a view towards future pay-offs and accumulated evidence of non-reneging behaviour (Parke 1993). Luhmann (1979) argues that trust involves learning and that such learning processes are only complete when the person to be trusted has had the opportunity to betray trust but not taken it.

Commitment

Firms that trust their partner are more committed to their relationship (Anderson and Narus 1990; Morgan and Hunt 1994; Gundlach *et al* 1995). Trust and commitment encourage firms to work at preserving relationship investments by cooperating with exchange partners and to resist short-term alternatives in favour of expected long-term benefits (Morgan and Hunt 1994).

Moorman *et al* (1993) define commitment as an enduring desire to maintain a valued relationship. Morgan and Hunt (1994) propose that a firm will commit to an exchange partner when the relationship is considered so important as to warrant maximum efforts to maintain it. Such implies that the relationship is important and that there is a desire to continue the relationship into the future (Wilson 1995).

Hakansson and Snehota (1995) see commitment as the tendency to persist with a course of action, often without an apparent causal motive, on the basis of some vague expectation. Thus, to some extent, a commitment is an act of faith. Commitment implies the adoption of a long-term orientation towards the relationship and a willingness to make short-term sacrifices to realise long-term benefits (Dwyer *et al* 1987).

However, commitment is comprised of two components; an attitudinal component and an instrumental component (Gundlach *et al* 1995). Commitment is most often seen as an attitudinal construct described in terms of an affective commitment, psychological attachment, identification or affiliation (Achrol 1997). People develop an affective commitment towards organisations they feel they belong to; which provide them with assistance and support during difficult times; offer long term security or returns; and whose future and fortunes they feel they can actively participate in determining.

However, attitudinal commitments alone are a precarious quantity. Commitments that are not supported by investments lack staying power (Achrol 1997). Such investments have been described variously to include pledges, credible commitments, idiosyncratic investments and the dedicated allocation of resources (Anderson and Weitz 1992). Such credible commitments act as powerful self-interest stakes in exchange relationships.

Idiosyncratic investments

Williamson (1985) suggests that such investments stabilise relationships by altering the firm's incentive structure. By making idiosyncratic investments, the firm creates an incentive to maintain the relationship. Engaging in opportunistic behaviour and thereby risking the dissolution of the relationship is contrary to the self-interest of a channel member, for, if the opportunism is detected and the relationship terminated, the investment may not have generated adequate returns. Furthermore, the making of such idiosyncratic investments may also provide a powerful signal to the other party. Observing the other party's pledges causes the channel member to be more confident of the other party's commitment to the relationship, because the other party will sustain considerable economic loss if the relationship is terminated (Heide and John 1988).

When organisations interact with one another for more than short periods, they often adapt to each other's needs (Hallen *et al* 1991). Adaptations can be seen most clearly by such things as a supplier's modification of a product to suit a customer, a buyer's modification of a production process to accommodate a supplier, delivering to meet a buyer's production schedules rather than the supplier's, or the joint establishment of a stock-holding facility (Ford 1984).

Adaptations are important because most relationships are based on some kind of match between the operations of the two firms (Hallen *et al* 1991). Inter-firm adaptations imply considerable investments by one or both firms. Since these investments cannot always be transferred to other business relationships, adaptations tend to bond the exchange partners together in a closer relationship and to create barriers to entry for potential competitors.

However, firms will adjust products and processes to their partner's requirements, subject to the constraints imposed by technology (Easton 1992). Because technological innovations are often complex and may alter existing products and production processes, buyers are often unable to use the innovation to its full potential (Athaide *et al* 1996). Failure to derive a significant benefit from the innovation will have negative consequences for the supplier, as the associated negative word-of-mouth will tend to slow down the rate of acceptance. Consequently, suppliers need to both stimulate adoption and facilitate its successful implementation. Where technological innovations are involved, suppliers should consider how they can help buyers rationalise their purchase decisions and to achieve the full benefits from the innovation. Realisation of the desired benefits makes future marketing activities easier, assists with product improvements and leads to positive word-of-mouth, all of which increase the likelihood that the innovation will succeed

Power dependence

When the outcomes obtained from the relationship are important or highly valued, the focal firm is said to be more dependent upon its exchange partner (Heide and John 1988). The higher the percentage of sales and profits derived from the business and the greater the expectations of sales and profits in the future, the more dependent the focal firm becomes (Frazier *et al* 1989).

Dependence is also increased when the outcomes from the relationship are comparatively higher than or better than the outcomes available from alternative relationships. Firms dealing with the best exchange partner are more dependent because the outcomes associated from dealing with that partner are better than those available from alternative partners (Heide and John 1988). Anderson and Narus (1990) view dependence as the outcomes given comparison level for alternatives. Dependence is a measure that represents the overall quality of the outcomes available to the focal firm from the best alternative exchange relationship.

When fewer alternative sources of exchange are available to the focal firm, or when replacing or substituting a current exchange partner is difficult because there are fewer potential alternatives, dependence will increase (Heide and John 1988; Frazier *et al* 1989).

However, it is the firm's perception of its dependence relative to its partner that is of most interest in channel relationships. Relative dependence determines the extent to which a firm will have influence over or be influenced by its partner (Anderson and Narus 1990). With increasing dependence comes greater vulnerability (Krapfel *et al* 1991). Dependence in an exchange relationship may make one firm more susceptible to the power and influence of another. The more powerful partner may be in a position to create more favourable terms of trade for itself (Heide and John 1988; Frazier *et al* 1989; Lohtia and Krapfel 1994).

In general, firms will seek to reduce their dependence on other firms and to increase the dependence of other firms upon itself. Firms seek to reduce and manage dependence by purposely structuring their exchange relationships with other firms (Heide 1994), or to deal with multiple entities (Ganesan 1994). Where there are few alternatives, Heide and John (1988) suggest that a supplier can reduce its dependence on the buyer by engaging in various bonding behaviours with the customer. This may include such actions as developing close personal relationships and creating an identity with the customer separate from the product lines. Other actions may include adding value to the product and creating specialised procedures to use in ordering, shipping and invoicing. Such actions create exit barriers whereby the buyer will incur significant switching costs if they were to change to an alternative supplier.

Channel conflict is the only construct considered to have a direct negative effect on satisfaction. However, what is more significant is the manner in which conflict is resolved. Geyskens *et al* (1999) suggest that the most pervasive channel construct known to influence satisfaction is the use of power. Satisfaction increases when non-coercive sources of power are employed (Frazier 1983). Non-coercive influence strategies include information exchange, discussion of business strategies and requests (Frazier and Summers 1986). Conversely, conflict will increase when coercive influence strategies are employed by an exchange partner. Coercive influence strategies typically include threats and promises. When a channel partner frequently pressures or coerces the focal firm into either taking some action that it would not otherwise have taken or it is forced to forego some positive outcome, the focal firm is expected to feel tension and frustration because its decision autonomy is constrained. Consequently, the use of threats will decrease the focal firm's satisfaction.

Not only will the fear of exploitation reduce the focal firm's satisfaction with the relationship, but it will also impact upon its desire to continue the relationship (Anderson and Weitz 1989). The more dependent firm can be expected to re-evaluate the benefits it derives from the relationship and to estimate the switching costs it will incur in pursuing an alternative relationship.

Exchange partners who have been subjected to unfair trading practices are also more likely to demonstrate hostility towards their partner (Kumar *et al* 1995). When trust is low, while the relationship may still continue, it will become increasingly intolerable because of uncertainty and dysfunctional behaviours.

Thus, the manner in which power is distributed and employed in the relationship will dictate the way the relationship both operates and develops. If the more powerful firm is perceived to be using its power to achieve collective goals and does not impede the other in attaining its desired rewards, a high level of goal compatibility will exist. Conversely, if the more powerful firm frequently pressures the other into taking actions that are against its own interests, conflict will inevitably result and trust will decline (Frazier and Summers 1986). Partners will resist further influence attempts and try to enhance their power at the expense of the other.

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