

Investigating the Role of Open Costing in the Buyer-Supplier Relationship: Implications for Global Apparel Supply Chain Management

Huicheng (Jeff) Wu, Jin Su and Nancy Hodges
The University of North Carolina at Greensboro, NC, USA

Keywords: Apparel supply chain management, global sourcing, buyer-supplier relationship

Background and Purpose. Recent research in supply chain management (SCM) indicates that firms should not only focus on building competitiveness and performance as stand-alone entities, but as part of the broader supply chain in which they operate (Handfield, Cousins, Lawson, & Petersen, 2015). Moreover, a key to increasing a firm's competitiveness is building long-term, collaborative buyer-supplier relationships (BSR) (Elfenbein & Zenger, 2014). The costing and subsequent pricing of a product is an important factor for both buyer- and supplier-side decisions, particularly decisions regarding whether to engage in a contract and commit to a long-term relationship (Ulaga, 2003). Norek and Pohlen (2001) found that costing practices in particular can influence relationship dynamics, which ultimately impact the quality and performance of the BSR. An increasingly popular practice, open costing is a method by which a supplier uses the best knowledge available to compile an itemized list of factors deemed necessary in the production of the product sought by the buyer, rather than a fixed price. To date, few studies have examined how the supplier's costing methods and presentation of costing results enter into the BSR in the context of the global apparel industry. Thus, the purpose of this study was to explore the role of open costing within the BSR as part of the apparel supply chain. Findings of this study contribute to the SCM literature by highlighting the role of open costing in the BSR and specifically from the supplier's perspective.

This exploratory study applies the theoretical framework of social exchange theory (SET) (Homans, 1958; Thibaut & Kelley, 1959) to investigate the role of open costing practice in the BSR within the apparel supply chain. SET posits that people in dyadic relationships (e.g., the relationship between buyer and supplier) will act out of desire for reward maximization and cost minimization, and particularly within the context of business relationships (Ulaga, 2003; Whipple, Lynch, & Nyaga, 2010). SET provides a useful theoretical lens through which the complex dynamics of BSRs can be understood (Lambe, Wittman, & Spekman, 2001). Indeed, a key theme of the BSR, and an underlying premise of social exchange theory, is the importance of trust and commitment in ensuring relationship success (Morgan & Hunt, 1994). Thus, in this study, the role of open costing and its implications for BSRs were examined from the SET perspective.

Method. Because there is little empirical research on open costing in apparel SCM, a qualitative approach was deemed suitable for the current study. According to the World Trade Organization (2018), China and Bangladesh were the top two clothing exporting countries in 2017, accounting for close to 42% of the global total value. Thus, suppliers from these two countries were recruited to participate. With IRB approval, a total of 30 participants (19 from China and 11 from

Page 1 of 4

Bangladesh) occupying operational and managerial roles with job titles ranging from merchandiser to owner, were recruited using the snowball method (Mason, 1996), starting with the first author's industrial contacts. Guided by the specific objectives of this study, only professionals with in-depth experience in interacting with buyers and the practice of open costing were included.

The semi-structured interview was the primary method employed to collect data (Merriam, 1998). Interviews averaged between 20 to 70 minutes and were conducted in either face-to-face or video format. With participant's consent, interviews were digitally recorded and were conducted in Mandarin for the Chinese participants and English for the Bangladesh participants. Questions were adapted from the extant BSR literature related to product cost determination (Brito & Miguel, 2017) and were developed to explore how open costing, as a buyer-supplier interaction mechanism, affects the BSR relative to apparel SCM. Questions included, *What are the benefits of open costing compared to other methods used when negotiating with a buyer? What are the challenges?* Interview data provided the basis for developing an in-depth understanding of the role of open costing in the BSR as a social relational exchange.

All interviews were transcribed verbatim and when necessary, translated to English by two of the researchers who are native Chinese. Hermeneutic interpretation of the interview texts was employed to analyze commonalities and differences across the data (Kvale, 1996). Categories of meaning were identified and agreed upon by the authors, and key themes that emerged from the analysis process were used to structure the interpretation within the social exchange framework (Keegan, 2009), including *Mutual Trust, Fairness, Flexibility, Efficiency, and Sustainability*.

Results and Discussion. According to participants, it is possible for the practice of open costing to help build mutual trust between the buyer and supplier. This is because suppliers must be convinced of the buyer's credibility before and during implementation of open costing as an interaction mechanism. Fairness is important in a BSR when open costing is practiced, in as much as participants think that suppliers' perceptions of fairness is a requirement for the open costing practice to be successful. According to participants, open costing increases flexibility throughout the entire process, starting with the buyer's initial product cost inquiry and ending with delivery of the finished product. Once trust and fairness have been established and operational procedures have been standardized, open costing can lead to increased efficiency in the exchange between the two parties, primarily because improved buyer-supplier interactions can reduce overall production lead time. Finally, from participants' perspectives, open costing encourages sustainable production practices by including the suppliers' costs associated with them. As a result, open costing can help avoid the typical conflict that arises when buyers expect social and environmental compliance but are reluctant to pay the costs suppliers must incur to be compliant. Overall, the themes indicate that open costing is important to building a strong BSR and to managing the overall global apparel supply chain.

Based on interpretation of the data, several key findings support the importance of open costing in the BSR, as well as the relevance of using SET in studies on the topic. First, it appears that open costing enhances a supplier firm's attractiveness within the exchange. That is, open costing is a result of not only competitive but collaborative efforts between buyers and suppliers

Page 2 of 4

to improve overall efficiency for both parties, and thereby can reduce internal and external costs for both. Second, participants overwhelmingly reported that trust is a foundation for the open costing mechanism due to the “no reservation” action of open costing. Third, through the honest exchange between parties, resolution of hidden BSR conflicts stemming from expectations of social and environmental compliance becomes possible through the implementation of open costing. Finally, the perceived equity of the BSR prompted by open costing within the exchange process appears to motivate suppliers to invest in long-term relationships and engage less in opportunistic behavior.

Limitations and Further Research. Findings of this study contribute to the existing apparel SCM literature in terms of understanding the mechanism and practice of open costing within the BSR and apparel SCM, and specifically from the perspective of suppliers operating in China and Bangladesh. However, because this study was exploratory in nature, and among the first to examine the practice of open costing in the apparel industry, any generalization of the results should be made with caution. Further empirical study of the causal effects of open costing on developing the BSR is needed, and particularly studies that examine its impact on BSR performance and satisfaction. Continued research on methods of costing and buyer-supplier interaction mechanisms is important to advancing knowledge in the apparel SCM field.

References

- Brito, R. P., & Miguel, P. L. (2017). Power, governance, and value in collaboration: Differences between buyer and supplier perspectives. *Journal of Supply Chain Management*, 53(2), 61-87.
- Elfenbein, D., & Zenger, T. (2014). What is a relationship worth? Repeated exchange and the development and deployment of relational capital. *Organization Science*, 25(1), 222–244.
- Hadfield, R. B., Cousins, P. D., Lawson, B., & Petersen, K. J. (2015). How can supply chain management really improve performance? A knowledge-based model of alignment capabilities. *Journal of Supply Chain Management*, 51(3), 3-17.
- Homans, G. (1958). Social behavior as exchange. *American Journal of Sociology*, 63(1), 597-606.
- Keegan, S. (2009). *Qualitative Research: Good Decision-making*. London: Kogan Page.
- Kvale, S. (1996). *Inter-Views*. Thousand Oaks, CA: Sage.
- Lambe, C. J., Wittmann, C. M., & Spekman, R. E. (2001). Social exchange theory and research on business-to-business relational exchange. *Journal of Business-to-Business Marketing*, 8(3), 1-36.

- Mason, J. (1996). *Qualitative Researching*. London: Sage.
- Merriam, S. (1998). *Qualitative Research and Case Study Applications in Education*. San Francisco, CA: Jossey-Bass.
- Morgan, R., & Hunt, S. (1994). The commitment-trust theory of relationship marketing. *Journal of Marketing*, 58(3), 10-20.
- Norek, C., & Pohlen, T. (2001). Cost knowledge: A foundation for improving supply chain relationships. *The International Journal of Logistics Management*, 12(1), 37-51.
- Thibaut, J. W. & Kelley, H. H. (1959) *The Social Psychology of Groups*. New York: Wiley.
- Ulaga, W. (2003). Capturing value creation in business relationships: A customer perspective. *Industrial Marketing Management*, 32(8), 677-693.
- Whipple, J. M., Lynch, D. F., & Nyaga, G. N. (2010). A buyer's perspective on collaborative versus transactional relationships. *Industrial Marketing Management*, 39(3), 507-518.
- World Trade Organization (2018). *World Trade Statistical Review 2018*. Retrieved from https://www.wto.org/english/res_e/statis_e/wts2018_e/wts2018_e.pdf