Beware of Bid Shopping

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Spend Matters is pleased to welcome a guest post from Paladin Associates, Inc.

You've just completed a competitive bidding event with large potential savings for at least equal quality and service. Congratulations! However, to capture the savings you must move significant business from an incumbent supplier. Do the following scenarios sound familiar?

Scenario 1: You approach the incumbent supplier to break the bad news. They offer to meet competing pricing if you leave the business with them.

Scenario 2: You go to internal stakeholders to sell the award recommendation. They ask you to have the incumbent supplier match competing bids in order to save the time and trouble of switching.

How do you respond? It's very tempting to take the path of least resistance, stick with the incumbent and quickly pocket the savings. However, there are significant downsides to this approach.

Bid shopping is the practice whereby a buyer discloses the bid price of a one bidder (often a non-incumbent supplier) to another bidder (often the incumbent supplier) in an attempt to obtain a lower bid price. The practice is used to achieve short-term savings while avoiding the effort to qualify and/or on-board a new supplier. However, this practice brings substantial risks and long term issues that should be considered.

First, bid shopping undermines long-term competition. How many times will non-incumbent suppliers offer aggressive bids if they are only used to drive down incumbent supplier pricing? One client was shocked when we delivered a 20%+ savings on a spend that had been "competitively bid" every year. As outsiders, we were able to convince the supplier community to participate aggressively. We assured them of our client's serious commitment to consider new suppliers.

Potential new bidders frequently express concern, especially where there is an entrenched incumbent supplier. In our pre-bid meetings, potential suppliers are candid in challenging the situation: "Why invest the time and effort to prepare a proposal when there is little chance of winning new business, and a high risk of divulging our confidential pricing?" This concern requires frequent reassurance throughout the sourcing process, particularly for a large or complex bid.

Although not publicized, it is well known that a buyer's reputation for bid shopping spreads quickly throughout the industry. Once this reputation is established, suppliers either quit bidding altogether or they provide non-aggressive pricing. The RFQ becomes a mere exercise, so the incumbent gets lazy and their prices and margins grow. Worse yet, competing suppliers now take their aggressive pricing and innovations to the buyer's competition!

Price matching rewards a supplier for not being aggressive and removes their incentive to improve. We've seen this time and again at clients where bid shopping is rampant. The incumbent supplier has enjoyed fat margins at the buyer's expense. They don't need to worry about being competitive because they know they will always get a second chance. They feel no compulsion to provide better value in service, quality, product R&D and innovation.

What if the incumbent supplier isn't enjoying large margins but quoted higher prices because of their unfavorable cost structure? Perhaps their equipment is outdated. Or maybe they have inefficient processes, unfavorable labor rates, poor sourcing practices, etc. Price matching may force the incumbent into a non-sustainable price structure. The more they sell, the more they lose! Eventually they go out of business and potentially interrupt your supply chain.

Many consider bid shopping to be unethical. Also, there are potential legal concerns such as violation of bilateral confidentiality agreements or inducing an illegally low price (Robinson-Patman). At minimum, bid shopping damages the credibility of the individual buyer. However, it also impacts the entire purchasing organization and corporate reputation as well. The company's reputation in one marketplace quickly spreads to other industries. The resulting damage to credibility, trust and competition from one isolated act can spill into every spend pool with the resulting negative implications. A single breach can take years to repair.

Although tempting for expediency, bid shopping risks serious long-term consequences. Is the short-term gain worth the long-term impact? It appears not!

- Robert J. Patton and Barbara M. Ardell, Paladin Associates, Inc.
