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# The influence of reputation on supplier selection: An empirical study of the European automotive industry

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## ABSTRACT

Using an original database, integrated with information by the web, we propose an ex-post analysis on the main factors influencing the selection process of tier 1 suppliers in the automotive industry. There is plenty of literature on how buyers should select their suppliers, but the literature on how they really do so is scarce. We contribute analysing an original database collecting purchasing contracts information within the automotive components market in Europe. We investigate, through different econometric approaches the influence of traditional supplier selection criteria in combination with different reputation factors. Our findings suggest that reputation plays a crucial role more than classical criteria; in particular, suppliers, which serve a diversified customer portfolio or with strong exposure to premium brand customers have better chances to gain additional orders and broaden their customer base even more. The latter means that OEMs have to increase their reputation in order to be more attractive for suppliers.

## 1. Introduction

Supplier selection and supply chain restructuring are two related phenomenon (Schniederjans et al., 2015) that strongly influence the automotive industry (Choi and Hong, 2002). In the automotive sector, with its traditionally flat hierarchy, price was the main selection criterion (Fujimoto, 2001) but, gradually, other supplier selection criteria such as quality and technical capabilities (Birchall et al., 2001; Calabrese, 2001) have been considered more consistently (Choi and Hartley, 1996). Consequently, a real hierarchy among direct and indirect suppliers has been defined (Balcet and Consoni, 2007; Castelli et al., 2011) with a growing involvement of specialised suppliers to satisfy new requirements (Caputo and Zirpoli, 2001; Sturgeon and Van Biesebroeck, 2011) and with many minor firms relegated to the role of sub-suppliers (Rachid, 2001; Volpato and Stocchetti, 2007).

Two main consequences arise in the car components market: the reduction in the number of suppliers to the point of scarcity (Schiele et al., 2012), and the increasing power the so-called mega-suppliers (Chanaron, 2013; Frigant, 2013), as compared to carmakers. These firms are able to combine technical skills and logistical capabilities, as well as financial strength, good reputation and managerial competences, which are essential aspects for maintaining reliable and long-term relationship with carmakers (Cheraghi et al., 2004; Karlsson and Weimarck, 2001).

There is plenty of normative literature on how buyers should select their suppliers, with a general consensus on a number of factors influencing the individual choice, ranging from price, perceived quality, delivery to other more industry specific criteria, as documented by Lin and Purchase (2006). Reputational issues receive little attention in this body of work, as already highlighted by de Boer et al. (2001). Even in the presence of relevant phenomenon like competition, globalisation and the Internet boom, most recent - and not so recent - supplier rankings (Cheraghi et al., 2004; Karsak and Dursun, 2016) continue to be mainly based on general performance evaluation.

In fact, there is little literature on how buyers actually select their suppliers in practice. This paper is exactly focused on this point and analyses a database of real sourcing decisions in the automotive sector. We contribute to the literature by providing an extensive quantitative analysis of the supplier selection criteria based on contracts for components for all car models assembled in European plants during the period 2002–2014. Moreover, we investigate the effect of reputation in the purchasing decision by including different indicators of corporate reputation, defined as the “perceptual representation of firm's overall appeal to all of its key stakeholders when compared with other leading rivals” (Fombrun, 1996), within our econometric estimates.

We find two intriguing and promising results. First, suppliers that serve a diversified customer portfolio have a better chance to gain additional orders and further broaden their customer base, compared to

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suppliers that serve particular customers. Second, suppliers with strong exposure to premium brand customers gain more orders also from non-premium customers in the subsequent period. For the automotive supply chain, these results connect to the customer attractiveness literature, and to social exchange theory. The former argues that buying firms may want to become a preferred customer of their suppliers; hence also buyers have to build their attractiveness and their reputation in the supply market. The latter states that an actor starts a “business” relationship if the partner is sufficiently attractive, then checks if the relationship matches initial expectations, and then decides to continue or stop a relationship depending on the availability of alternative partners (Hüttinger et al., 2012).

The remainder of the paper is organised as follows. Section 2 reviews the relevant literature on reputation regarding supplier selection and develops our main research hypothesis. In Section 3 we present our empirical strategy and we describe the database through some preliminary descriptive statistics. In Section 4, we present and discuss all results. Conclusions, purchasing implications and limitations are reported in the last section.

## 2. Literature review, automotive peculiarities and hypotheses

As reported by Lienland et al. (2013), the recent literature on supplier selection remains essentially focused on descriptive/prescriptive research, which includes traditional performance aspects (quality, price, technical capability and delivery) among the most relevant factors in supplier selection (Cheraghi et al., 2004; Kannan and Tan, 2002). On the contrary, other factors like supplier reputation have received less attention (de Boer et al., 2001). Starting from the seminal paper by Dickson (1966), which lists more than 23 factors influencing supplier selection decisions, Weber et al. (1991) propose an overview of said factors, whereas Ho et al. (2010) consider 78 papers and find that they have only 14 purchasing factors in common. Traditional performance-based factors are used in more than 80% of the cases, whereas reputation is included in only 15 of the proposed scales. Cheraghi et al. (2004) point out relevant changes in the ranking of different supplier selection criteria due to stronger competition, globalisation and Internet use. Yet, price, quality and delivery consistently remain the most popular criteria in supplier rankings (Karsak and Dursun, 2016).

Nevertheless, some contributions highlight the growing role played by corporate reputation, especially in B2B markets (Murray and White, 2005; Wiedmann and Buxel, 2005), as a factor which strongly influences the purchasing decision process (Fombrun and Pan, 2006) and the duration of each relationship (Bennett and Gabriel, 2001). Corporate reputation is often described by the management and marketing literature. It is sometimes confused with corporate identity or corporate image. The so-called “Evaluative school” defines reputation similarly to what has been done by the financial community (Chun, 2005), while the “Impressional school” analyses how a company is viewed by the different stakeholders separately (Deephouse, 2000; Weiss et al., 1999). Finally, the “Relational school” links corporate reputation to how customers actually view suppliers (Spears et al., 2006), firstly in terms of internal viewpoint, image and brand, and secondly in relation to the other stakeholders’ view. In this sense, evaluating corporate reputation requires several years (Balmer, 2001) and damaged reputation may severely affect financial performance (Gatzert, 2015). Within the relational stream, Fombrun defines corporate reputation as “a perceptual representation of a company’s past actions and future prospects that describes the firm’s overall appeal to all of its key stakeholders when compared with other leading rivals” (Fombrun, 1996). The growing importance of reputation, as seen in this definition, is the basis for our first research hypothesis:

**H1:** *Corporate reputational factors are relevant in supplier selection compared to the traditional criteria based on performance.*

This hypothesis is also supported by the social exchange theory

(SET), and it is frequently used as theoretical background for attractiveness studies (Hüttinger et al., 2012; Mortensen and Arlbjørn, 2012), which analyse the motivations behind social exchanges among individuals (Homans, 1958; Blau, 1964) in terms of resources and benefits (Das and Teng, 2002). The buyer-supplier relationship is seen as referring to long-term cooperation based on trust and information sharing, so that reputation regards not only suppliers but also customers and their attractiveness. In particular, in the automotive industry, suppliers represent on average 80% of the added value of a vehicle (Clepa, 2017), and the strategic role of many components/modules can invert the burden of attractiveness (Schiele et al., 2012). In fact, car-makers are increasingly focused on core activities like brand management, style, engineering, assembling and manufacturing of some key components (Calabrese, 2002; Calabrese and Erbetta, 2005). Following the SET, many scholars stress the attractiveness theory in the buyer-supplier relationship (Cropanzano, and Mitchell, 2005; Dwyer et al., 1987; Halinen, 1997; Harris et al., 2003; Hald et al., 2009; Wilkinson et al., 2005; Ellegaard et al., 2003) and mention many factors modifying the traditional selection perspective focused more on supplier attractiveness than on customer attractiveness. Among these:

- Outsourcing increases the value added coming from suppliers, and customers are less able to influence them; reductions in technological spillovers induce customers to sign exclusivity agreements, so they can profit from suppliers’ innovations (Chesbrough, 2006);
- The scarcity of innovative suppliers makes it difficult to find substitute suppliers and relationships become stabilised (Schiele, 2010);
- The adoption of key account management in suppliers obliges customers to be more attractive (Ivens and Pardo, 2007);
- The diffusion of global sourcing reduces customer attractiveness, as suppliers believe that distant relationships entail greater risks and complexity than those established with local customers (Steinle and Schiele, 2008).

These trends are summarised in the cycle of the so-called preferred customership, which is based on three core elements (Schiele et al., 2012; Pulles et al., 2016): customer attractiveness, supplier satisfaction and preferred customership.

Customer attractiveness motivates suppliers and increases collaborative relationships along the supply chain. Moreover, a customer that boosts its attractiveness will have an additional motivational approach to influence supplier actions (Mortensen, 2012; La Rocca et al., 2012) and an additional tool to increase supplier satisfaction. Similarly to customer satisfaction, supplier satisfaction relies on the confirmation/disconfirmation paradigm, i.e. satisfaction is reached (confirmation) if ex-post experience coincides with or exceeds ex-ante expectations (Essig and Amann, 2009). For example, if a customer acts wrongly, an unsatisfied supplier might deliver low-quality outputs and even discontinue the relationship (Essig and Amann, 2009). However, a minimum level of satisfaction may be sufficient to maintain the relationship, and satisfaction can gradually grow during the relationship (Vos et al., 2016). Consequently, suppliers can change the status of a customer from attractive to preferred and devote a greater part of their development efforts to it (Cordón and Vollman, 2002). On the contrary, they assign the status of regular customer to any firm that fails to provide adequate levels of satisfaction (Schiele et al., 2012). The ‘preferred customer’ status requires great efforts and costs on the part of both the supplier, in assessing and comparing the performance of each relationship, and the customer, in beating the competition (Schiele et al., 2010). Hence, it is usually granted if a significant increase in competitive advantage and business performance is reached. This strategy is worthwhile in very critical supply markets, as in the case of the strategic items described by the Kraljic matrix (1983), whereas customer attractiveness is more suitable for leverage and bottleneck items.

Automotive is the reference industry in this paper, similarly to other

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