Purchasing and Supply a Neglected Function in Nigeria: Implication on Profitability

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***Abstract* - The growth of every business enterprise depends on the level of profit it makes. One of the ways profit can be maximized is through application of the purchasing and supply strategic function. This paper attempt to examine purchasing and supply a neglected function in Nigeria and its implication on profitability with special focus on manufacturing industries. The findings proved that purchasing function is relegated to the background and regarded as a mere clerical function in most organisations compared with other business functions. However, where few purchasing departments exist, the function is handled by non-professionals. This paper concludes that the negative effect of this neglect is on the profitability of the manufacturing industries. The author therefore recommend that to avoid low profit perhaps business failure, purchasing and supply function should be practiced as a business function with the involvement of professionals. The purchasing function should be seen as integral part of a top corporate business strategy.**

***Keywords:* Purchasing and Supply, Function, Implication, Profitability, Manufacturing industries**

I. INTRODUCTION

Purchasing and supply is a business concept, function and a major contributor to profit maximization. The overriding concern is that purchased raw materials, goods and services are one of the major elements of cost for manufacturing industries. According to Zima, Klumpp, Regattieri and Herbage (2019), industrial firms spend more than half of their turnover on supplies that is why the purchasing function has become a central success factor for modern firms. Jain and Patidar (2011) described purchasing as a business activity directed to securing the materials, suppliers and equipment required in the operations of an organisation. Over the past four decades, according to Temidayo, Olawale and Oluseyi (2012), purchasing has evolved from a clerical function in the 1960s, through being an operational activity in the 1980s to a strategic nature in the 1990s.However, till date, the purchasing function is constantly changing and expanding in scope.

Regrettably, in spite of the evolution of purchasing and supply over the years and its strategic nature, some industries have failed to accord its function the recognition it truly deserves, compared to other business functions such as marketing and sales, finance and accounts, production and engineering, public relations, human resources e.t.c. To Msimangira (2003), purchasing has gained recognition amongst companies in the developed countries; the reverse is the case however in the developing countries. Oakland (1992) pinpointed that although purchasing is clearly an important area of managerial activity it is neglected by organizations. Temidayo et al (2012) explained that several organisations have transformed their purchasing capabilities into competitive advantage, others are still lagging behind. In Nigeria, the function of purchasing and supply is regarded more as a mere clerical function handling paperwork of buying instead of a strategic function that entails and utilizes the entire supply chain management process.

In most cases, the purchasing and supply function is merged with other departments such as production, accounts or marketing. People who are not competent are being saddled with such tasking and strategic responsibilities. While only a few instances of exclusive purchasing departments exist with specialists in the field of purchasing and supply. In spite of this, according to Carr, Leong and Sheu (2000) they still fail to include the purchasing professionals and practitioners as part of the organizational strategic decision-making team. The deliberate or sheer ignorance of neglect, has been a main cause of financial deplete to manufacturing industries and most surprisingly, the implication on profitability is unknown.

In the manufacturing industries, expenditure on procurement requires a huge portion of the working capital amounting to 50% or thereabout. This invariably makes the purchasing department the largest spending department of an organization. Yet some manufacturing outfits in Nigeria do not operate a proper and exclusive functional department handling the affairs of purchasing and supply. On the other hand, the duty of the purchasing professionals to see that the funds committed to purchases are fully utilized in line with purchasing ethics, principles and practice are assigned to inept. Lack of implementation of appropriate purchasing systems has led to low productivity. It has been one of the main causes of financial depletion in our industries. The purchasing and supply function is entangled with a whole lot of misplaced priorities. Thereby making our organizations incompetent in optimizing their performance. In spite of its strategic function, purchasing and supply has not been given its rightful place in Nigeria. It is on this premise that this research is aimed to examine the impact of purchasing and supply function on profitability.

1.1. Objective of the Study

The objective of the study was to ascertain the impact of purchasing and supply function on profitability as a specialized discipline that is meant to satisfy the material needs of an organization.

II. CONCEPTUAL REVIEW

2.1. An Overview of Purchasing and Supply Function as a Profit Center

Purchasing is a profit making function and a business success factor. For manufacturing industries, purchasing is a window to the outside world and a source of input. The prime function of purchasing is that of being sensitive to the external supply market situation and also of feeding back this information to the other function of the organization (Enock, 2015). The primary objective of a business firm is to make profit (Dwivedi, 2014). Profit is one of the indices for measuring the success and growth of a business. According to Dwivedi (2014) profit means the excess of revenue over all paid-out costs including both manufacturing and overhead expenses. The first place to start achieving profit in business is through the purchasing and supply function that most industries had ignored over the years.

For instance, if the cost of raw materials, equipment, services and supplies are unnecessarily high, absolutely, the cost of the finished product will also be pretty high. If inputs are defective, output will also be defective. To Nweke (2000), we can incur cost from excessive stock, storage cost, poor quality of raw material or poor output, poor inventory, cost of ordering, research e.t.c. In most cases, non-professionals who carry out purchasing activities, sustain waste through hasty spending and carelessness in handling the affairs. All of these, the adverse effect is on the profitability of the organisation. Benmoffat(2015) pinpointed that maintaining a reliable purchasing system to any organization is very important to the performance of that organization.

For every dollar of revenue collected on goods and services sales, more than half goes back to suppliers. Hence, according to Baily and Jacobs (2005) the objectives of purchasing function are to acquire the right quality of materials at the right time in the right quantity from the right source at the right price. Regrettably, Bowers or, Closs and Cooper (2002) stated that the process of acquiring these needed inputs has been considered somewhat of a nuisance. It is not difficult to see why purchasing is clearly a major area for cost savings (Monczka, Handfield, Giunipero and Patterson, 2009).Savings, for instance, resulting from efficient purchasing activities directly or indirectly enhance profit margin instead of simply increasing sales price. It is not how much money the company makes, but how much it could or should have made (Jain and Patidar, 2011). It is imperative for private organisations in Africa to adopt more strategic approaches to purchasing in order to facilitate commercial gains (Temidayo et al, 2012).

2.2. The Five Concept of Purchasing Mix

To understand more of the importance of purchasing and supply function as a profit center, we must take a cursory look at five dimensional and explanatory concepts of the purchasing mix that are often debated.

2.2.1. The Right Quality

In every transaction of procurement of goods and services the first thing that comes to the mind of a buyer is simply quality. It forms the main subject that attracts the buyers to the product. Okorie, Iyadi, Okoh and Ajire (2015) a buyer can only think of buying a product only when he is convinced that the product is of the right quality. People perceive product quality differently because quality conveys different meanings to different people. According to Bowers or et al (2002), quality rests in the eyes of customers and how they perceive an organization, its products, and its services. Quality is the totality of features and characteristics of a product or service that bear its ability to satisfy a given need (Nweke, 2000).

Quality is of prime importance to the manufacturing industry. An overriding concern of all organizations today is quality. The quality of raw materials purchased, fed into the production process determines the quality of output to be achieved. According to Bowers or et al (2002), in the competitive market-place, no company dares to fall behind in providing quality to its customers, consumers, or end users. Quality determinants according to Okorie et al (2015) are performance, reliability, conformance, durability and serviceability. Good quality saves money and poor quality cost money, therefore, spending on quality can improve company’s profitability.

2.2.2. The Right Quantity

The right quantity is the actual amount of materials needed for a specific production or purpose. The right quantity is also known as Economic Order Quantity (EOQ). Adeniji (2001) EOQ is the level of activity at which the cost of inventory control is minimized. It is the quantity of stock, which is normally ordered each time the stock is replenished. According to Jain and Patidar (2011) one of the basic problems of inventory management is to *find out the quantity to be ordered* for each of the supplies so that it is most economical to the company from the overall operational aspects.

The essence of determining the right quantity is to avoid wasteful spending of funds through over stocking or under stocking of inventories. Economic order quantity is the size of order that minimizes the total cost of acquiring and holding stock (Okorie, et al., 2015). Determining the right quantity using the EOQ method, the ordering cost is equated with holding cost as shown in the figure below.

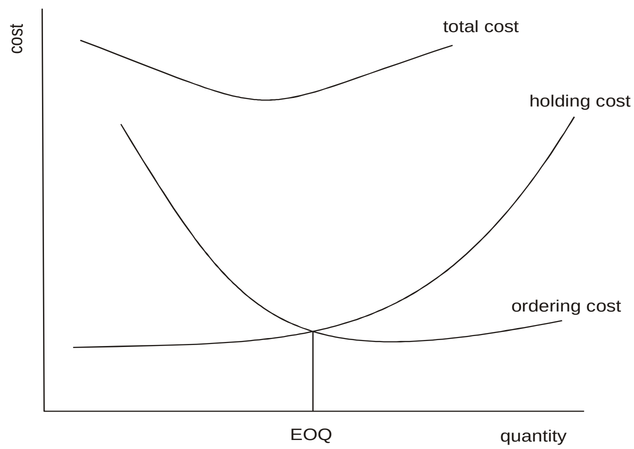

Fig.1: Economic order quantity Graph

Source:Okorie, et al., (2015). *Principles of Purchasing.*

Ordering cost:- these are costs incurred in the process of making purchase(s) of materials such as cost of negotiation, placing orders, progressing, transportation, and cost of getting payments to the supplier e.t.c.

Holding cost:- these are costs incurred with stock of materials (inventory) kept in the store such as cost of capital tie down, insurance and audit, store labour and administrative cost, damages and pilferages, interest on money borrowed to buy stock, warehouse upkeep e.t.c.

Every company must ensure that inventory is maintained at desired levels. Too much and too low inventories bring down the level of profitability of an organization. Peavler (2019) stated that a company's profitability will start to suffer if it has too much or too little inventory on hand. If the business has too much inventory, it could be slow-moving or obsolete inventory which keeps cash flow hostage and drags down the company's inventory turnover ratio. If the company has too little inventory, then it is subject to stock outs, stoppage in production, lost sales, and declining customer goodwill. To maximize company’s profit, a business has to minimize the costs of ordering and storing its inventory. That means, it has to have some sort of financial metric to calculate the optimal quantity of inventory to order and store. That metric is economic order quantity (EOQ). Inventory represent capital, therefore, according to James (2016) an efficient management of inventory is required because a substantial share of a firm’s funds is invested in them.

2.2.3. The Right Price

The “right price” is one of the most significant components of the purchasing mix. Price is a monetary expression of worth of an item and is the central stage of the exchange process. Price serves as a determinant of a buyer’s preference. Price is defined as the amount of money paid by a buyer to a seller for a particular product or service (Iyadi et al., 2017). According to Nweke (2000) price is defined as the value of a product or service measured in monetary terms.

In some situations, price is considered the major criteria in procuring materials from potential suppliers. Though price is paramount, it does not take priority over other factors. The right price is not necessarily the lowest price but in all situations, therefore the right price will be that particular price that is not only reasonable enough but also fair enough to the major parties of the exchange process that is the seller and the buyer. A whole lot is saved when purchases are made at the right price.

2.2.4. The Right Place

Purchasing function ensures that equipment, materials, supplies and services are obtained from the right sources (Okorie et al., 2015). The right place is that source where the buyer’s needs can be met in terms of acquiring the materials, equipment, supplies, service at the right quality, quantity, price and time. We can’t be mentioning the right quality and other rights of the purchasing mix without a source of supply. Developing supply alliance is an asset to an organization. Therefore, selecting a source of supply is a critical issue that needs to be handled with utmost care and without sentiments. Nweke (2000) defined sourcing as a means of finding suppliers who are willing and able to provide consistently, quality service (delivery) at a competitive price within a specified period. Adopting a wrong or incapable source of supply can frustrate the procurement effort as well as production plan of an organization.

Imagine, having spent weeks or months – sourcing and evaluating – finalizing and transacting with a supplier, only to discover thereafter that you had made erroneous choice. How will you feel? It has a whole lot of cost implication. Of what importance is a source of supply if you can’t obtain the right materials at the right quality, in the right quantity, at the right price and time? You may have succeeded in contracting with a supplier that offers you a reasonable and fair price, but only to discover lately that some of the deliveries are faulty. Regrettably, a wrong source can cause delay, alter production plans, even cause untold damage to a business. Burt, Dobler and Starling (2003) stated the objective of sourcing as the identification and selection of the supplier whose costs, qualities, technologies, timeliness, dependability, and service best meet the firm’s needs.

In today’s business world, information is key. In getting suppliers’ information, the questions that run in your mind are: Who are the suppliers? Where are they located? How do we get information concerning them? Simple! According to Okorie et al (2015) information on suppliers can be obtained from the following areas such as the internet, trade shows, specialized trade journals and media. Others are suppliers’ catalogue, sales force, professional organizations, specialized trade directory and other buyers.

2.2.5. The Right Time

Time is money, purely irrecoverable and a major factor in the purchasing mix. Time is so significant that even when other factors in the purchasing mix such as right quality, quantity, price, and place are met but failed to obtain those factors at the right time, all the effort becomes futile. And this will pose a threat to the organization, which stands to lose a great deal. According to Mete (1996) the right time is the time, which the user requires the materials to be supplied for use in operations. Nweke (2000) maintained that inaccurate timing of deliveries may affect production plan and other operations adversely. Getting procurement at the right time will overcome scarcity and possibly, price fluctuations. Failure to keep the right time has an adverse effect on business operations and profitability. Okorie et al., (2015) identified the following effects of later delivery as loss of reputation and goodwill, loss of customers, stoppage in production and loss of profits.

To avoid the adverse effects of late delivery, there is the need to understand "procurement lead time". Mete (1996) stated that procurement lead time is the time required to place order and the time required receiving the goods into the appropriate receiving point. There is also the need to understand the term "expediting". Ogbonnaya (2001) stated that expediting is the continual act of monitoring orders placed with a given supplier to ensure that such materials are received at the time already agreed upon. Mete (1996) see expediting as a follow up of an order to make sure it is delivered on time.

2.3. Other Area Where Savings Are Derived

2.3.1. Value Analysis and Value Engineering

A functional purchasing department is known for its cost minimization and profit maximization programes and activities. One of the ways of achieving these objectives is through the practical application of a technique known as "value analysis" or "value engineering". The main objective of these concepts is to reduce and avoid unnecessary cost of a product or process without compromising its quality and performance. The concept of value analysis or value engineering was developed during or at the end of World War II, when many of the material resources were in short supply. Lawrence D. Miles, a production engineer working at General Electric Company (GEC) of USA led a committee assigned to identify substitute materials for production without hindering quality and performance.

From the outcome of the exercise, it was discovered that many of the alternative materials used were providing equal and better performance at a reduced cost. Scheuing (2000) defined value analysis as "a systematic and objective evaluation of the value of a good or service, focusing on an analysis of function relative to the cost of manufacturing or providing the items or service. Rick and Holweg (2000) defined value analysis as a process of systematic review that is applied to existing product designs in order to compare the function of the product required by a customer to meet their requirement at the lowest cost consistent with the specified performance and reliability needed. Ikechi et al (2008) defined value analysis as a systematic approach to investigating all aspects of cost and eliminating unnecessary cost in the manufactured product.

Any cost that does not add value to the customer satisfaction is regarded as unnecessary cost. If a company's objective is to reduce cost of a product and still maintain its quality or improve on it, it must find out those costs that provide no value to the customer at first. If such costs are eliminated, it must be without negative implication on the function, quality, reliability, maintainability or benefit required by the customer. If business organisations are able to identify every unnecessary cost by applying value analysis techniques, there is high probability that the organisation will improve tremendously in the area of cost reduction, organizational growth, profitability and general wellbeing of the organisation (Okorie and Omogbiya, 2017).Valve analysis and value engineering are closely related terms, intertwine, interwoven such that many people use them interchangeably. Though the orientation behind the two concepts is the same - identification and elimination of unnecessary costs yet they are different. The difference lies in the time and stage of application. While value analysis is applied at the post production stage, value engineering which is the same set of techniques is applied during the pre-production stage.

III. METHODOLOGY

The aim of this paper is to explore purchasing and supply a neglected function in Nigeria, and its implication on profitability in the manufacturing industries. This paper is strictly qualitative in nature. The researcher has mainly relied on secondary data. The secondary data were collected from published articles, researcher papers, academic books, census survey and sources through related websites e.t.c. Some of the integrated elements of the purchasing function that will certainly increase the chances of enlarging profitability and business growth were examined.

IV. CONCLUSION

In the course of this paper, it was observed that the function of purchasing and supply is truly relegated to the background in most manufacturing industries in Nigeria. This is as a result of low perception and awareness of the strategic role of purchasing and supply function in modern times. This has been one of the reasons for low profit perhaps business failures amongst our manufacturing industries. It is not overemphasized to ever describe purchasing function as a strategic tool for achieving profit potentials. The purchasing function is so strategic that there is a direct relationship between purchasing efficiency and organizational profitability.

The foregoing are the indications that purchasing and supply function is the most value-enhancing function in an organization. The function is capable of reducing economic waste, cost reduction, profit maximization and consequently an anchor for business sustainability and growth. However, it is in the view of this paper to recommend that purchasing and supply as a business function should be practiced professionally and be seen as an integral part of a corporate strategy of top management and as one of the most important tools for improving profitability of the organization. However, strategic application and implementation of an organized purchasing and supply function as a business function will be at its best in solving purchasing related problems facing our manufacturing industries in Nigeria.

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