Supplier Selection a Strategic Tool of the Purchasing Function: Its Role in Profit Maximization

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***Abstract* - The profit potentials of a manufacturing firm through an efficient and effective supplier selection process of the purchasing function is high and guaranteed. Profit is the ultimate goal of shareholders in establishing business enterprises. This paper attempt to examine supplier selection a strategic tool of the purchasing function and its role in profit maximization. The authors discussed three dimensions of supplier selection such as negotiation, competitive bidding, and constrains in the contemporary supplier selection process. Since purchasing function is responsible for controlling a dominant share of the company's revenue. The authors, therefore, recommend that it should be the duty of the purchasing personnel to negotiate, select supplier(s) and execute all company commitments within the purchasing framework to get the optimal profit — right quality at the lowest cost, to develop the satisfactory supply chain and maintain good partnering relationships with suppliers. Thus, to maximize profit, manufacturing firms in Nigeria should adopt a well-organized and functional purchasing systems where the supplier selection process is handled by highly qualified professionals in line with the purchasing ethics, principles, and practice.**

***Keywords:* Supplier Selection, Strategic tool, Purchasing, Profit maximization**

I. INTRODUCTION

There is a growing awareness of the specialized nature of the purchasing function in current literature as a *profit-making hub* of a business. Profit is the ultimate motive of most established business enterprises in the world today. According to Dwivedi (2014), the primary objective of a business firm is to make a profit. Profit is the excess of income over expenditure accruing from an investment or a business transaction. Profit is a residual and essential tool for business growth and survival. According to Ohwovoriole (2019), Dangote Cement was the most profitable firm on the Nigerian Stock Exchange, with a profit after tax of N390 billion recorded in the 2018 financial year. Kolakowski (2019) Saudi Aramco is the most profitable company in the world with a profit of $110.9 billion in 2019 Fortune Global 500. For being profitable, a company must work in conditions of profit, which means that the revenue has to exceed costs involved in achieving the activity (Achim and Borlea, 2010). Over the years, Okpighe (2020) profit is one of the indices for measuring the success and growth of a business enterprise. However, considering the strategic importance of purchasing function in the developed countries of the world and with the notion that the function is capable of stimulating higher profit potentials, with this realization, the purchasing function is becoming an issue of high concern in Nigeria.

A company is performing globally if it can satisfy the interests of all partners: shareholders, employees, suppliers, customers, creditors. Today the most privileged of these partners are the shareholders (Achim et al, 2010). Thus, to create higher value for the shareholders, according to Dey (2009) executives are under constant pressure to deliver higher profit. In any given organization, there are several approaches to drive and maximize this profit to the optimum level. One of these method that is important, is the supplier selection process of the purchasing function. According to Akenroye, Ojo and Aju (2012), aside from the immediate contribution on price savings, a performing purchasing function can improve shareholders value as well. Okpighe (2020) stated that the first place to start achieving profit in business is through the purchasing and supply function that most industries had ignored over the years. The reason is that purchasing is a strategic business unit (SBU) of value creation, and in terms of money spent, is by far the largest spending unit of any manufacturing enterprise. According to Okorie et al (2015), modern production outfit spends over 55% of its funds on raw materials and other items needed for production. Straub and Attner (1988) pinpointed that production thrives on machinery, raw materials, parts, and supplies, all of these are bought.

Supplier selection is a strategic tool of the purchasing function, very important in a business undertaking, if not the most important. Selecting suppliers who are capable of facilitating, stimulating and generating higher profit potentials is key to any organisation involved in purchasing activities. According to Straub et al (1988), the importance of careful purchasing was emphasized by the manager corporate purchasing for Atlantic Richfield Company, who claimed that reducing purchase price by 1 per cent company-wide would save the firm $25 million per year. Also, Putra (2018) stated that a $1 reduction in the cost of purchased goods produces a profit of $1. Furthermore, Okorie et al (2015) averred that the level of profit in an organisation is highly influenced by the purchasing department and its activities. According to Gafamy (2005), improvement of profitability margin and earnings per share growth has been the number one organizational priority for purchasing. And so, the way supplier selection activities are organized, coordinated and implemented within the purchasing framework can either make or mar the company's profit potentials. Gafamy (2005), supplier selection has been the subject of extensive conceptual and empirical work in business management literature and is widely considered to be of the most fundamental responsibility of the purchasing function of management. This underscores the importance of the supplier selection tool as it represents one of the most strategic functions of the purchasing department.

1.1 Objective of the Study

The objective of the study was to ascertain the role of supplier selection as a strategic tool of the purchasing function and its role in profit maximization. The specific objectives are as follows:

1. To examine the impact of supplier selection on a firm's profitability
2. To examine how negotiation contributes to profit maximization
3. To examine how competitive bidding enhancefirm's profitability

There is increasing attention being paid by all modern manufacturing firms to practice holistic purchasing function globally, firms in Nigeria are still lagging in the implementation of this strategic business practice (SBP). Management executives are under constant pressure to deliver higher profit for shareholders, groping for profit and at the same time despising the supplier selection strategic tool of the purchasing function, a major player in profit maximization. There is this constant failure of not taking cognizance of the strategic implementation of supplier selection as a significant part of a business in boosting the efficiency and profitability of a firm. However, with the continuous use of inept the supplier selection activities are often carried out unethical, not in line with purchasing principles and practices. This witlessness of not implementing appropriate supplier selection processes within the purchasing framework had truncated productivity and caused a huge diminution in profit in our manufacturing firms. It is on this premise that this research aimed to examine supplier selection, a strategic tool of the purchasing function and its role in profit maximization.

II. CONCEPTUAL REVIEW

2.1 An Overview of the Purchasing Function

No longer is purchasing like the buying of the olden days. Purchasing has developed into a science and has its own rules, conventions and practices and uses all the processes of management that make it contribute effectively to the company's profits the question of organizational importance (Anni-Kaisa and Katrina, 2012). One of the fundamentals of the purchasing function is that purchases of the best products are made at the best possible prices, delivery dates and legal terms to deliver the best profit for the company. In the industries, the term purchase means buying (procurement) of equipment, raw materials, tools, parts and services required for smooth industrial operations. If companies fail to get their purchases right they will never go into profit. There is more to purchasing than just buying because the entirety of function exceeds the buying (procurement) activities. Purchasing function overarches material planning & control, inventory, store & warehousing management. Other related functions are value analysis & value engineering, just-in-time, standardization, simplification and specification. However, one cannot lose the sight of the fact that purchasing research, negotiation, competitive bidding, supplier sourcing, selection and evaluation among others are also significant areas of the purchasing function. According to Anni-Kaisa and Katrina (2012), the higher the status of purchasing and supply management in the company, the better the abilities of the company to take into account the influence of supply actions and decisions on firm's value creation.

2.2 Supplier Selection

The essence of supplier selection is to ensure an effective and efficient procurement process of an organization. The purchasing department has the function of selecting the source of supply and ensures that the right materials or services needed are obtained from the right source. The supplier selection is a broad evaluation using some measures to identify a supplier with cost-saving potentials, who is capable of meeting the specification of the buyer without delay. Gafamy (2005) stated that the overall objective of the supplier selection is to identify suppliers with the highest potential for meeting a firm's need consistently and at an acceptable cost.

> *According to Nweke (2000), a good supplier is one who at all times honest and fair in his dealing with customers, his employees and himself; who has adequate plant facilities and know-how to be able to provide materials which will meet the purchaser's specification in the quantities required at the time promised; whose financial position is sound; whose prices are reasonable both to the buyer and to himself; whose management policies are progressive; who is alert to the need for contained improvement in both his product and manufacturing processes; and who realizes that in the last analysis, his interest is best served when he best serves his customers.*

A good supplier can also be seen is one who can satisfy the Carter's 10C's requirement. The Carter's 10C's model is a method of supplier selection that is internationally recognized, all-encompassing with the following wide range of factors to consider:

1. Competency
2. Capacity
3. Commitment
4. Control
5. Cash
6. Cost
7. Consistency
8. Culture

9. Clean
10. Communication

A supplier who satisfies these factors is the right source to maintain the right contract of providing the right materials needed at the right quality, in the right quantity, using the right transportation system, at the right price, to effect deliveries at the right time and the right place with the right attitude. According to Okorie et al (2015), the role of the purchasing officer does not end with ensuring materials are bought at the right quality, price and quantity. It is the role of the purchasing officer to ensure that equipment, materials, suppliers and services are obtained from the right source. It becomes a problem and cost-ineffective to source materials from the wrong source. The wrong source of supply can add unimaginable and unnecessary cost to production. It can cause delay and alter production plans, even cause untold damage to your business reputation. Nweke (2000) stated that the selection of the wrong supplier may lead to a delivery problem or failure to meet the lead time or total breach of the contract. According to Beil (2009), to avoid the dire outcomes of supplier non-performance, buyers typically take proactive steps to verify a supplier's qualifications before awarding them a contract. Gafamy (2005), the effective selecting of suppliers is very important to the success of a firm in achieving high-quality products and customers satisfaction. In today's competitive business environment, the companies attach importance to procurement since the acquisition of goods and services can influence the achievement of the company's main goals and objectives (Prasad, Kamath, Barkur and Nayak, 2016).

2.2.1 Negotiation in Supplier Selection

The purchasing function of a company does not only guarantee the availability of all the materials required for production but also responsible for the proper supplier selection process and profitably negotiating on purchasing contracts. To survive competitively in the business world today, it's important to negotiate and select the right suppliers who are willing and competent in all ramification of supplies. Ramanathan (2007), the selection of the right suppliers has a significant role regarding the quality assurance of a corporate organizational output. Production delays due to parts shortages and recalls of faulty products produced by non-compliant suppliers have cost buyer firms millions of dollars through recalls, warranty costs, and associated inventory adjustments, and have inflicted untold damage on the reputations and future sales potential (Beil, 2009). Effective purchasing negotiation in supplier selection is one of the ways toward strategic partnership and to achieve optimum profit in business. Burt, Dobler, and Starling (2003), to be fully effective in purchasing, negotiation must be utilized in its broadest context – as a part of a decision-making process.

According to Weitz, Castleberry and Tanner (2013), negotiation is the bargaining process through which buyers and sellers resolve areas of conflict and/or arrive at agreements.

> *Lysons and Farrington (2006) see negotiation as a dialogue between two or more parties, intended to reach an understanding, resolve the point of difference, or gain an advantage in outcome of dialogue, to produce an agreement upon courses of action, to bargain for individual or collective advantage, to craft outcomes to satisfy various interests of two people/parties involved in the negotiation process.*

Supplier selection and negotiation are critical parts of the purchasing function and has a very important impact on the company's growth and sustainability.

In supplier selection, negotiation is described as an important aspect of building a strong foundation for profitable business relationships between partners. With the use of proper negotiation strategies and tactics, the purchasing function can easily enhance the profitability of a firm through bargaining lower prices with suppliers. If materials are purchased at a lower price, the money saved directly increases the profit margin of a business, not necessarily increasing selling price at all times. Be that as it may, in supplier selection and negotiation, an agreement is not only based on the lowest price, according to Beil (2009), the primary goal of "supplier qualification screening" is to reduce the likelihood of supplier non-performance, such as late delivery, non-delivery, or delivery of non-conforming (faulty) goods. Effective negotiation achieves optimum value for money by exploring all the possible ways in which both parties can benefit, win-win. The success of a purchasing deal depends on how effectively both parties are able and willing to negotiate. According to Barnes (2005), John F. Kennedy said: "let us never negotiate out of fear, but never fear to negotiate". Negotiation gives better informed-decisions and the opportunity for buyers and suppliers (partners) to interact and discuss the terms relating to a given purchase contract. Never lose out on negotiation by being too greedy (Barnes, 2005).

Burt et al (2003) stated six objectives of negotiation in the process of supplier selection as follows:

1. To obtain the quality specified
2. Obtain a fair and reasonable price
3. Get the supplier to perform the contract on time.
4. To persuade the supplier to give maximum cooperation
5. Develop a sound and continuing relationship with competent suppliers
6. Create a long-term relationship with a highly qualified supplier.

Negotiation takes place in every sphere of human life and people negotiate daily for one thing or the other. The negotiation process usually consists of three main stages: prenegotiation stage, actual negotiation stage and post-negotiation stage.

2.2.2 Competitive Bidding in Supplier Selection

The search for greater choice and value for money leads to more purchase being made by competitive methods (Prajapati, Pitrodaand Bhavsar, 2015). The purpose of the competitive methods is to select a supplier who will make an offer based on the best value for money. These methods are adopted in government procurement to achieve sustainable best value for government funds, sometimes applicable in the private sector. It is the most "secure" method in procurement. Competitive bid methods can bring an organisation a whole lot of benefits of profit maximization. According to Prajapati et al, (2015), the perceived benefits of these methods have resulted in a phenomenal rise in the number of bids and tenders. Competitive bid or tender is a transparent procurement method aimed at obtaining goods and services at the lowest price by encouraging competition, and by avoiding favouritism. This process creates competition among suppliers in the broader marketplace, value for money and a quality finished product. To maintain the integrity of the competitive process, the assessment of bids must be undertaken objectively, consistently and without bias towards particular suppliers.

It is important to know that low bids can often be rejected if they are judged to be lacking merits of minimum job requirements. High-quality service cannot always be achieved if only the lowest tender is accepted. According to Prajapati et al (2015), the evaluation of contractor competence should consider a wide range of factors such as financial soundness, technical ability, management capability, reputation and safety performance.

By law, request for tender is made open and public, and the contract is awarded to the lowest bidder provided the lowest bidder is considered qualified to perform the contract. Ikechi et al (2008) defined tendering as the procedure by which potential suppliers are invited to make a firm and unequivocal offer of the price and terms, which acceptance, shall be the basis of a subsequent contract. Ikechi (2019) "Request for Bids" or "Invitation for Bids" is an official request from the buying firm asking suppliers to quote the price at which they will perform under the terms and conditions of a contract, should they be the successful bidder. The tender process requires submitting a sealed envelope detailing price and terms for the offer. In the end, the recipient of the offer then chooses the bidder with the lowest price or best terms,

2.3 Supplier Selection Constraints

The supplier selection decision is a very complex and difficult task due to some uncontainable and unpredictable underlining factors capable of hindering the decision-making process. According to Akenroye et al (2012), the process involved in supplier selection is lengthy, and it utilizes different standards and criteria ranging from delivery time, pricing structure, service level and product quality. These criteria are neither fixed nor standardized to evaluate suppliers. Their applications in the entire selection process vary amongst organisations. According to Gafamy (2005), suppliers should be selected based on how their actions will impact all the performance and competitive elements of the supply chain. They further averred that one of the competencies essential to the supply chain success is an effective supplier selection decision.

Ikechi (2019) stated some problems which buyers are likely to encounter in selecting the right supplier(s) out of the lot. Such as:

Nepotism: This is the practice among people with power or influence of favouring their relatives. Some Chief Executives Officers use their vetoes to award contracts to relatives who may not be the right suppliers.

Reciprocity: This is the principle or practice of mutual exchange. In this context, it is an organisation policy, which makes it incumbent on buyers to buy from those suppliers who are also customers of the buying.

Buying syndrome: This is an erroneous idea some people have about the buying function. The belief has often led to the use of incompetent and unqualified buyers in the execution of the buying function.

Inertia: This means lack of vigor. Most professional buyers today are lazy. They find it difficult to explore supply market and evaluate suppliers accordingly.

Quota system: Under the quota system, some “men in high places” are expected to come up with a number of suppliers whom they must select as successful bidders.

Ensuring fair dealing is important for minimizing the potential risk from undue influence under the circumstance of supplier selection. Avoiding the dire outcomes of supplier non-performance, buyers must be fair in their dealings before awarding any contract of purchase.

III. METHODOLOGY

This paper aimed to explore supplier selection a strategic tool of the purchasing function and its role in profit maximization. This paper is strictly conceptual. The researchers has mainly relied on secondary data. The secondary data were collected from published articles, research papers, academic books and sources through related websites e.t.c.

IV. CONCLUSION AND RECOMMENDATION

This study examines the supplier selection as a strategic tool of the purchasing function and its role in profit maximization. The profit potentials of efficient and effective supplier selection processes of a manufacturing firm are enormous and cannot be overemphasized. If the purchasing function can make money, it can also lose money from the poor supplier selection process that can reduce the company's profit potentials. This scenario is common to most manufacturing firms in Nigeria and their profit has been so drained unknowingly. It's not the profit a company makes that is important, but the optimal profit it could or should have achieved. In furtherance, the supplier selection is so strategic that there is a direct relationship between purchasing efficiency and organizational profit.

It is therefore recommended that since purchasing function is responsible for controlling a dominant share of the company's revenue, it should be the responsibility of purchasing personnel to negotiate, select supplier(s) and execute all company commitments within the purchasing framework to get the optimal profit—right quality at the lowest cost, to develop satisfactory supply chain and maintain good partnering relationships with suppliers. To maximized profit, manufacturing firms in Nigeria should therefore adopt a well-organized and functional purchasing systems where the supplier selection process is coordinated by well-qualified professionals, adhering to purchasing ethics, principles and practice.

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