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PROCUREMENT MANAGEMENT

Purchasing is one of the key managerial activities in every organisation, its significance having been identified during the 19th century. According to **Kasilingham (2012, p.57)**, the period shortly before the Second World War marked the discovery of the fact that a firm's success was not so much dependent upon what it was capable of selling but rather on how able organisations were to acquire necessary services together with materials from vendors. This discovery was triggered by a global shortage of virtually all fundamental materials for supporting operations, coupled with an abnormal rise in prices following the First World War. Since that time, purchasing has gained significance for the critical role it plays towards ensuring continuity of production (**Hacioglu, 2019 p.265**). Worth noting is that purchasing acts as "an interface between suppliers and functional areas within the buying organisation" (**Crandall, Crandall & Chen, 2009 p.265**). Among some of the functional areas that are influenced by purchasing are finance, marketing, production, and quality assurance (**Magad & Amos, 2013 p.225**). A vital deduction that can be made from this latter statement is that for the purchasing function to proceed smoothly and make the other functions- and the entire organisation- active, organisations must cultivate and maintain good relationships with suppliers and all other players in the supply chain. In addition, organisations operate in environments that are highly unpredictable; the techniques needed to perform the purchasing function become more refined almost every day due to constant changes in the market (**Kasilingam, 2012 p.57**). Subsequently, there is a need for managers in organisations to understand and embrace the idea of sustainable procurement.

DEFINITION OF TERMS

Before delving into a detailed discussion of the relevance of sustainable procurement in the contemporary business environment, it is essential to understand the meaning of key terms that are commonly used. Purchasing and procurement are somewhat related terms, but the latter has a more futuristic outlook. By definition, purchasing refers to the process through which an organisation obtains the right services or materials at the right time and price and in the right quality and quantity while making sure that these are delivered to the correct place (**Magad & Amos, 2013 p.225; Gopalakrishnan & Banerji, 2002 p.254**). This is the classic definition of the term purchasing, but the modern view is that purchasing is "the process undertaken by an organisational unit that, either as a function or as part of an integrated supply chain, is responsible for procuring or assisting users to procure, in the most efficient manner...thereby contributing to the competitive advantage

of the enterprise and the achievement of its corporate strategy...” (Munch, 2015 p.42). The implication of this is that purchasing is part of the broader procurement function.

Johnsen, Howard and Miemczyk (2014, p.8) describe procurement as “the totality of acquisition starting from the identification of a requirement to the disposal of that requirement at the end of its life”. Alternatively, procurement may be viewed as a function of business management that ensures that the external resources needed for the accomplishment of an organisation’s strategic objectives are identified, sourced, accessed and managed. In other words, procurement assumes responsibility for an organisation’s strategic as well as operational activities and processes. In contrast, purchasing is tactical and transaction-based, assuming responsibility for the provision of required materials and services in the right quality, price and time. This is to say that whereas the focus of purchasing is on single transactions, procurement’s pure focus is on building relationships.

THE GROWING SIGNIFICANCE OF PROCUREMENT OVER PURCHASING

The tactical, transaction-based nature of purchasing compared to the strategic approach of procurement makes the latter more significant in today’s business world. Apart from this, the supply chain concept that has become an integral part of every organisation makes procurement more attractive than purchasing. Stated, supply chain management is the process of managing relationships between organisations and their customers as well as suppliers with the aim of ensuring that customers get superior value (Johnsen et al., 2014 p.11). Since purchasing encompasses activities such as contracting, buying, negotiating and expediting, its role in supply chain management is limited.

In contrast, procurement comprises activities such as sourcing and supplier relationship management (Johnsen et al., 2014 p.8). The element of supplier relationship management highlights why procurement is deemed a central ingredient for effective relationships with suppliers. As Hartmann (2002, p.7) observes, modern approaches to procurement increasingly seek innovativeness together with quality when selecting suppliers, rather than relying on price negotiations alone.

Additionally, substantial changes have taken place-and to continue taking place in the business environment, thus necessitating a robust relationship between organisations and their suppliers. Unlike in the classical period when the purchasing activities of buying and negotiating were regarded to be essential, the phenomenon of globalisation has resulted in intense, growing competition for scarce resources. Issues such as emerging

economies, specialization of labour, a paperless environment and the concepts of outsourcing have necessitated a shift from purchasing to strategic, sustainable procurement. Because of these and other changes, many firms have abandoned their market-driven strategies in favour of supply-driven business models (**Cordon, Hald& Seifert, 2013 p.14**).

Talking about specialization of labour resources, it is worth noting that companies are increasingly outsourcing their activities to suppliers as this allows both the company and the person from which the activities are being outsourced to specialise, thereby enhancing effectiveness together with efficiency. Over and above this, the modern business environment is characterized by uncertainties as well as bounded rationality among decision-makers (**Hartmann, 2002 p.9**). As a result, suppliers, as well as buyers, are realising the importance of standardising their transactions through the establishment of strong relations with one another. Also worth noting is the observation that in organisations where products are developed jointly with suppliers, commitment from both partners tends to be stronger (**Hartmann, 2002 p.9**). For this reason, it is evident that effective procurement facilitated the development of robust, productive relationships between companies and suppliers. The uncertainties and complexities facing supply chain structures, and which are projected to increase significantly over the years, necessitating what is referred to as supply chain integration. In the future, it is expected that supply chain structures will become more complex and choosing the right supplier will be more critical. Increasingly stringent supplier requirements will become routine, and demanding purchasers will expect suppliers to demonstrate their essential competencies. Supply chain risk, scarcity of raw materials, environmental, sustainable and economic issues will lead to increased pressure on these buyer-supplier relationships. To address these issues, organisations are expected to embrace the idea of supply chain integration, which is fundamentally about eliminating redundancies and communication barriers through proper coordination, monitoring and control (**Power, 2005 p.253**).

Procurement helps in addressing the complexities that are typically encountered in supply chain structures by reducing the magnitude and impact of the so-called bullwhip effect. **Power (2005, p.253)** describes the bullwhip effect as a phenomenon resulting from dynamically complex circumstances and is a situation in which “the demand process seen by a given stage of a supply chain becomes more variable as move up the supply chain”. This is to say that the bullwhip effect is a scenario where there is more significant variability in a supply chain’s upstream orders (from suppliers) as compared to its downstream orders (from customers).

The above discussion can be summed up into the statement that when done well, strategic procurement is a valuable source of sustainable competitive advantage in organisations. This is supported by the resource-based

theory, which postulates that firms can utilise their strategic resources in the development of capabilities leading to superior performance (Nothnagel, 2008 p.20). The theory uses the word ‘resources’ to refer to all tangible as well as intangible assets such as the management skills, information, knowledge and organisational processes together with routines that a firm utilises in the choice and implementation of strategies (Barney, Ketchen & Wright, 2011 p.1300).

CASE STUDY

INTRODUCTION TO TESCO

The risks arising from an outsourcing arrangement, and the application of strategic procurement in managing effective supplier relationships, are best illustrated using the case study of Tesco. Tesco is a UK-based international grocery as well as general merchandising retail chain that was founded in the year 1919. The firm’s headquarters are in Chestnut (The Guardian Professional Network, 2010 para.1). Tesco has grown remarkably over the years to become one among the world’s largest and most admired retailers. Its founder is Jack Cohen who conceived the idea of starting the company after a visit to the U.S. where he was intrigued by the idea of customers being allowed to use self-service when purchasing foods and food-related items (“Risk Management”, 2012 p.45). As of the year 2010, Tesco had made revenue worth £62.54 billion, employing more than 470,000 people (The Guardian Professional Network, 2010 para.2,3). The company has ventured into other markets beyond the UK, and now has a geographical presence in North America and Asia.

IMPORTANCE OF GREECE TO TESCO BUSINESS

One of the critical things about Tesco is that most of its food products are sourced from Greece. To be more precise, the company is said to purchase 45 products that range from wine, fruits, olive oil, cheese, pasta and honey from a foreign supplier known as The Greek Deli (Thakur, 2017 p.54). At this point, it may be worth mentioning that Greece is a suitable source for Tesco’s food products owing to its strategic position: the country is located “at the intersection of Asian and European trade route, which helps companies to transfer their products in less time” (Thakur, 2017 p.54). Apart from this, this strategic location generates substantial cost savings to companies since the costs of transportation are relatively lower. Also, Greece is the ideal food

supplier for many countries due to its experienced labour force, low operating as well as logistic costs, and high quality of raw materials (Thakur, 2017 p.54).

OUTSOURCING ARRANGEMENT & STRATEGY

Tesco's outsourcing arrangement with Greece is based on the long-term agreement policy that the company enters into with its suppliers. Every 48 months, the company renews its contract of supply with The Greek Deli (Thakur, 2017 p.54). More importantly, the company has reportedly "launched an online supplier network which connects 50,000 suppliers to identify how suppliers are being treated" (Thakur, 2017 p.54). A vital feature of this network is that besides procurement, supplier relationship is one of the areas of emphasis in Tesco's outsourcing policy.

Tesco's outsourcing strategies are modelled along with the Toyota model, whose priorities are total quality management and just-in-time delivery. To ensure that the products obtained from The Greek Deli are of high quality, the company performs rigorous tests on the delivered products, paying keen attention to their colour, quality and compatibility with safety together with health regulations. In addition to this, Tesco subjects its suppliers to ethical and technical audits (Thakur, 2017, p.55). The supply chain network through which Tesco receives food products from The Greek Deli is as shown in the following figure:

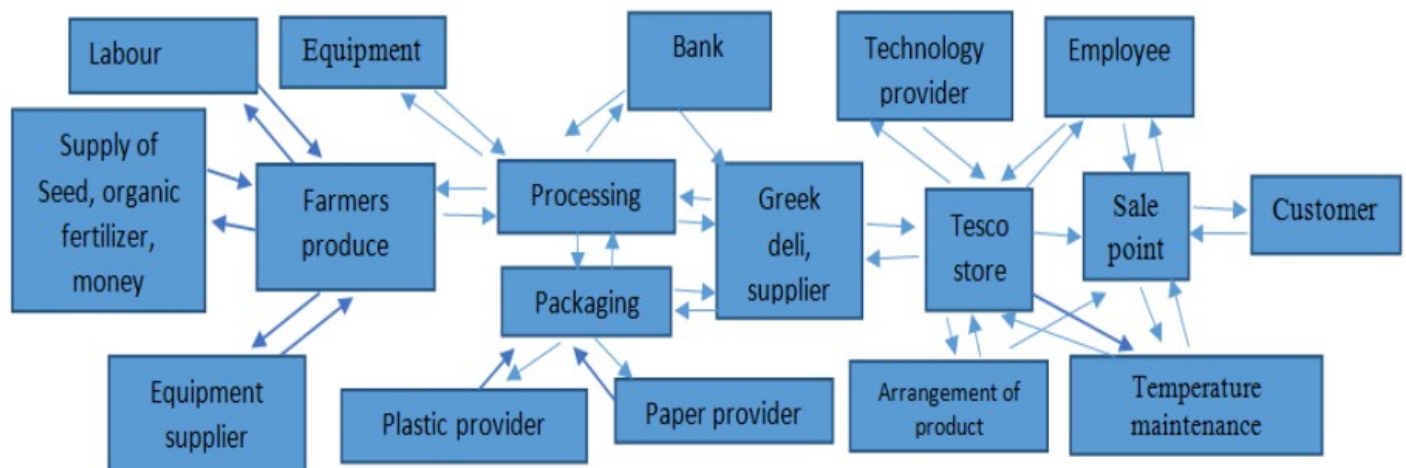


FIGURE 1 SUPPLY CHAIN NETWORK OF FOOD SUPPLIED FROM GREECE TO TESCO, UK (FOOD AND AGRICULTURE

Source: Thakur (2017)

As indicated in the figure, once farmers harvest their produce, they take it to processing centres which in turn hand over the fully processed foods to packaging centres. It is from these centres that The Greek Deli obtains foods ready for delivery to Tesco warehouses. The company then distributes the food products to its various sales points for ease of collection by customers. One of the observations made by **Thakur (2017, p.55)** about this network is that it lacks full agility. In the author's viewpoint, the flexibility of primary producers-the farmers- is significantly reduced while exporters, together with wholesalers enjoy greater flexibility.

The above observation is an indicator that even with all the benefits-both real and perceived- that outsourcing generates to companies, there are specific undesirable outcomes, dangers and risks that must be mitigated if firms are to enjoy a sustainable competitive advantage from their procurement policies. **Qi and Chau (2012, p.859)** acknowledge that the growing popularity of outsourcing notwithstanding, "a significant percentage of outsourcing deals are considered either a failure or suffered from serious problems". Some of these problems relate to the inability to create and maintain healthy relationships, in addition to negotiating decent contracts. Talking of decency, it is quite shocking to learn that "Tesco deducts money unfairly as fine from the bill of the supplier without following the contract and pays the bills 90 days later than the due date" (**Thakur, 2017 p.54**). If this allegation is anything to go by, the relationship between Tesco and its Greek suppliers is not as it should be, and this could have grave implications on the long-term outlook of the company's outsourcing practices. As it manages its outsourcing relationship with The Greek Deli, Tesco needs to bear in mind that there are a number of risks and dangers that could arise from this arrangement and negatively affect the company.

OUTSOURCING RISKS

Common outsourcing risks that are faced by companies are operational, compliance, reputational and concentration. To mention, operational risks are those arising from failures or inadequacies in a supplier's internal systems or processes. In contrast, concentration risks occur when a company obtains all its products and services from a few suppliers that are concentrated within a limited geographical area (**Vallabhaneni, 2019 p.164**). This second type of risk may be said to apply to Tesco, the reason being that most of its food products are sourced from Greece. Compliance risk is said to arise when a company delivers products or services that do not comply with relevant regulations and laws, while reputational risk refers to the risk arising from poor performance on the supplier's part, thereby creating a negative impression in public (**Vallabhaneni, 2019 p.164**).

Outsourcing risks have been proven to be a reality in many organisations. The popular airline Boeing, business solution provider IBM and product designer Nike are just a few practical illustrations of the risks likely to arise from outsourcing arrangements. According to **Sodhi and Tang (2012, p.148)**, Boeing outsourced a massive 70% of its development tasks to external suppliers. Apple also outsourced the development of the IC chip to an Indian company known as Pinexe Systems.

Focusing on Boeing, the leading aerospace firm in the world (**Ireland, Hoskisson & Hitt, 2008 p.78**), it emerges that the decision by the company to outsource design activities to Mitsubishi, Kawasaki and Fuji Heavy Industries posed substantial risks. Correctly, the company realised that the outsourcing process called for cooperation between itself and the three Japanese firms. The problem was that the collaboration implied that Boeing had to allow the three firms “acquire some of [its] core competencies starting with wing technology and the new lightweight materials” (**Ireland et al., 2008 p.78**). Eventually, Boeing found that its suppliers were now controlling the critical processes and knowledge body, which implies that the company will gradually lose its critical technical expertise.

IMPACT OF OUTSOURCING DECISIONS

Boeing has also had to deal with substandard work and shortage of supplies as a result of its outsourcing decisions. It is reported that when the company introduced the 787 programs, there were many novelties and complexities that drove the company to outsource up to 70% of the work. This decision had unintended undesirable consequences as a majority of the subcontractors that the company engaged found the work overwhelming. Consequently, the quality of products delivered was very low (**Ireland et al., 2008, p.78**). The outcome of these delays and unintended consequences was a 14-month delay in launching the 787 programs. Much as the risks and dangers discussed above are worth considering by Tesco; there is relief in the various success stories of numerous firms that have adopted outsourcing successfully. Companies such as Nike, Apple, Google, IBM and Microsoft are just but a few illustrations that when done right, outsourcing is an effective procurement strategy through which organisations can manage a network of vendors and suppliers that can quickly become inoperative due to rapid shifts in the business environment.

PROCUREMENT ROLL IN SUPPLYCHAIN

Having described procurement as mainly oriented towards creating and maintaining healthy, fruitful relationships between companies and actors in the supply chain, it goes without saying that outsourcing arrangements-and supplier relationships in general-call for collaboration and cooperation between firms and suppliers. For Tesco, the approach used by automobile company Chrysler may help. According to **Sodhi and Tang (2012, p.149)**, Chrysler highly values its suppliers and has identified a network of suppliers it considers strategic. With these strategic suppliers, Chrysler has formed long-term partnerships and reviewed its procurement function such that procurement is no longer viewed as the management of standard transactions but rather the process of developing as well as managing relationships with its key suppliers.

In addition, Tesco needs to train and develop a team of procurement professionals who will act as the link between the company and its supplier. The procurement professional will also be in a better position to ensure that the company makes the most feasible choice by objectively assessing various sourcing options.

CONCLUSION

It is impossible for firms to fulfil their objectives unless there is a functional unit responsible for procuring materials, services and products. Traditionally, this was the responsibility of the purchasing department. Over time, it has been discovered that the scope of the purchasing function is limited to single transactions. Due to globalisation and constant changes and uncertainties in the market, it has become necessary to adopt a broader, more comprehensive outlook, hence the development of the procurement function. Procurement is primarily about managing relationships in the supply chain. A critical finding made in this paper is that strategic procurement is not risk-free, and this means that firms must evaluate their outsourcing maturity and their ability to relate productively with suppliers.

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