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Effects of Contractual Agreement on Performance of Procurement Function in Selected University

Campuses in Nakuru, Kenya

John Langat Ndugi*

Jomo Kenyatta University of Agriculture and Technology,

School of entrepreneurship and management, Kenya

Email: johnndugi@gmail.com Cell: 0728 861 878

Josephat Kwasira

Jomo Kenyatta University of Agriculture and Technology

School of entrepreneurship and management, Kenya

jkwasira@gmail.com

ABSTRACT

The purpose of this study was to assess the contribution of contractual agreement on performance of the procurement in selected university campuses in Nakuru County. The target population of the study comprised of 400 employees and sample size comprised of 80 employees. These employees were drawn from departments related to procurement functions. Data was analyzed using descriptive statistics such as frequency, percentages and inferential statistics; Pearson Chi-square test. The results shows contractual agreement was evident in almost all campuses surveyed (96%) but a significant section of the respondents could not tell exactly the kind of procurement contractual relationships (38%). Most respondents agree that contractual agreements contribute to positive trust among partners (53.3%). The null hypothesis postulated was rejected and concluded that contractual agreement contribute positively towards supplier loyalty and commitment ($P=0.001$). These contractual agreements however dot not always comes with affirmative benefits but sometimes with shortcomings such as the amount of time and effort involved in building this trust. It also results in that higher switching costs if problems were to arise with the supplier and there is a sharing of proprietary information, strategy, planning, and goals. Contractual relationships between the university and source partners must be supported from the entire organization. More importantly, for a procurement organization to operate both efficiently and effectively in such a complex environment communication strategy need to be created and suitable contractual agreement determined prior and fostered throughout the organization.

Key words: procurement, contractual agreement, performance

BACKGROUND INFORMATION

Procurement functions includes purchasing inputs such as materials, supplies and equipment Porter (1996). The factors influencing the success of procurement include the ability of the organization in obtaining alternate resources, the timely efficiency of procuring resources, the current adequacy of existing procurement channels and the contractual agreement. Procurement function encompasses the whole process of acquiring property and/or services. It begins when a procurement entity has identified a need and decided on its procurement requirement. Procurement functions continues through the processes of risk assessment, seeking and evaluating alternative solutions, contract award, delivery of and payment for the property and/or services and, where relevant, the ongoing management of a contract and consideration of options related to the contract (Waters 2004).

The sense of mutual interdependence between the buyer and the supplier brings about a long term relationship between the two parties concerned. However in order to achieve higher buyer commitment and supplier loyalty, both parties have to perceive that there is a sourcing level of strategic fit between them and this could be achieved by having contractual agreement among the parties. Therefore for the buying party the initial phase of undertaking a partnering relationship should be the analysis of the value of the supplier considering its long term purchasing needs. (Manion, Baurkett & Wiffen, 2010).

According to Cry (1999) any kind of alliance between two organizations building trust is necessity for success. When there is a level of trust between the purchaser and supplier, both parties believes that the other is committed to mutual success. Ulaga & Eggert, (2006) asserts that the level of complexity of negotiations for agreement, between the supplier and the buyer decreases when both parties trust each other. This allows organizations to get rid of the concerns regarding each other's behavior and to communicate more important matters rather than losing time on discussing small details. Thus, negotiations consume less time and resources with mutual trust.

Trust is seen to be more difficult to build if the buyer and supplier have a record of adversarial negotiations. The suppliers and the purchasers have to work closely to reduce cost and improve quality. Outsourcing contracts target a minimum of 15 % cost reductions, sometimes even going up to 20 or 25% (Lankford & Parsa, 1999) to achieve these targets, requires multi-year agreements so that economics of scale and cost cutting measures can take effect. The pressure to keep bids low and to turn a profit over the lifetime of a contract leads contractors in outsourced services to cut the pay, pensions and terms and conditions of staff, leading in turn of deterioration in services. This represents a significant threat to the reputation of the university. Evaluation of partners and suppliers before selecting them can significantly improve the performance of the procurement function in carrying out its mandate. This implies the need for contractual agreement to improve compliance and efficiency in procurement in public universities. This research sought to assess the effects of contractual agreement on performance of the procurement function at selected university campuses.

RESEARCH METHODOLOGY

Research design

A descriptive case study research design was used in this study specifically using a descriptive case study technique. The case studies will comprise four university campuses namely; Egerton University Town campus, Kenyatta University Nakuru Town, Nairobi University Nakuru Town campus and Jomo Kenyatta University Campus. The study employed mainly qualitative approach using structured questionnaire with open and close ended questions. The metric for qualitative analysis was measured using Likert Scale with five degree scales; strongly agree (SA), Agree (A), and Neutral (N) Disagree (D) and strongly disagree (SD).

Target population, sample size and sampling procedure

According to Cooper and Schindler (2003), target population comprises all the elements from which the sample is actually drawn. The target population of this study comprised of employees in four selected university campuses. According to selected University campuses Staff registry, as of 2016, the total number of employees in its payroll from the selected university campuses was 400. This university campuses are divided into various departments. This is the population from which the sample was drawn.

Determination of Sample Size

According to Cooper and Schindler (2003), sample size is the number of items to be selected from the universe to constitute a sample. The minimum sample size was calculated to increase precision, confidence and variability. In order to determine a representative sample from the general population, Yamane's (1967) sampling formula was used as follows;

$$n = \frac{N}{1 + Ne^2}$$

Where;

n is the sample size

N is the population size

e is the level of precision (0.1)

$$n = \frac{400}{1 + 400 (0.1)^2} \quad n=80$$

The distribution of sampling units within university campuses were as follows;

Table 1: Sample Frame

| Sampling Unit | Frequency | Percent |
|---------------|-----------|---------------|
| Egerton | 40 | 50.00 |
| Kenya | 15 | 18.75 |
| Nairobi | 11 | 13.75 |
| Jomo Kenyatta | 14 | 17.50 |
| Total | 80 | 100.00 |

Sampling Technique

Stratified random sampling method was used to identify a representative sample where basic all respondents in the sample were eligible to answer questionnaire. Stratified sampling was selected because in this method, each member of the target population has an equal and independent chance of being included in the sample. Stratified random sampling technique is a technique that identifies sub-groups in the population and their proportions and selects from each sub-group to form a sample. It groups a population into separate homogeneous sub-sets that share similar characteristics so as to ensure equitable representation of the population in the

sample, (Sakaran, 2003). The strata were identified on the basis of procurement function, levels of management and departments. Simple random sampling was used to select individual respondents to answer questionnaire from this strata.

Research Instruments and data collection procedure

The questionnaire formed the basis for data collection. The questionnaire was semi-structured comprising both open and closed ended questions covering the three objectives. Questionnaire was administered to the staff in departments related to procurement using hand delivery and interviews method. In some circumstances, questionnaires were left with respondents to fill and later collected. The hand delivered questionnaires was collected at the end of each survey period. Respondents were selected from departments related to the procurement function on simple random basis.

Pilot Testing

The research instrument was pre-tested before final administration to the respondents. According to Mugenda & Mugenda, (2003) pre-testing allows errors to be discovered before the actual collection of data begins and 1% of the population is considered adequate for pilot study. The questionnaire was piloted to evaluate its practicability and was done on 10 respondents from Egerton university Town Campus who did not form part of the actual sample, this was done one week before collection of data commence. An alpha score of 0.70 or more indicated the instrument is reliable. This feasibility study was useful in checking the questionnaire validity, acceptability and accuracy.

Results of pilot testing

A pilot study was conducted to test the reliability and validity of the questionnaire. A sample of 10 respondents was selected in Egerton University town campus and the response was 100%. The Cronbach's Alpha Test was conducted on all measures for the independent and dependent variables which gave a threshold of >0.7 . A correlation coefficient greater or equal to 0.7 is acceptable (George & Mallery, 2003). Therefore, all the variables were retained for the study. These results from the pilot study were not included in the final data analysis.

Table 2: Pilot results

| Variable | No. of Test Items | Cronbach's Alpha |
|-----------------------|-------------------|------------------|
| Contractual agreement | 4 | 0.721 |

Data Analysis

Data was analyzed using descriptive statistics which includes frequencies, percentages, measures of central tendencies and bivariate correlation test using Statistical Package for Social Sciences computer software (SPSS V23). In addition, the researcher used Pearson correlation so as to determine the relationship between performance of the procurement function (dependent variable) and the independent variable; contractual agreement.

RESULTS**Descriptive results****Table 3: Effects of contractual agreement on procurement performance**

| Effect of contractual agreement | N | SA | A | N | D | SD | Mean | Std. Dev. |
|----------------------------------|----|------|------|------|------|-----|------|-----------|
| Higher commitment | 75 | 50.7 | 33.3 | 5.3 | 8.0 | 2.7 | 15.4 | 13.91 |
| Enhances loyalty among suppliers | 75 | 32.0 | 37.3 | 10.7 | 16.0 | 4.0 | 14.2 | 10.32 |
| Creates Trust among partners | 75 | 18.7 | 53.3 | 10.7 | 9.3 | 8.0 | 16 | 13.75 |
| Efficiency and effectiveness | 75 | 20.0 | 18.7 | 18.7 | 30.7 | 12 | 15.2 | 4.49 |

In this study, contractual relationships have been hypothesized to have a positive significant effect on the performance of the procurement in the selected organizations. The respondents surveyed showed that most respondents agree that contractual agreements contribute to positive trust among partners (53.3%). Only smaller proportion was not sure if there is any contribution to commitment owing to contractual agreement in procurement (5.3%). While almost all respondents were aware of the existence of contractual agreements, the largest proportion agreed that procurement contributes to supplier loyalty and commitment (37.3% and 32%).

Inferential analysis**Table 4: Relationship between contractual agreement and performance in procurement**

| | | Greater flexibility |
|-----------------------|---------------------|---------------------|
| Contractual agreement | Pearson Correlation | 0.390* |
| | Sig. (2-tailed) | 0.001 |
| | N | 75 |

*. Correlation is significant at the 0.05 level (2-tailed).

H_0 : There is no significant relationship between contractual agreement and the performance of the procurement function in selected universities.

H_A : There is significant relationship between contractual agreement and the performance of the procurement function in selected universities.

Contractual agreement was evident in almost all university campuses surveyed but a significant section of the respondents could not tell exactly the kind of procurement contractual relationships. A bivariate correlation in Table 4 was used to highlight the relationship between contractual agreement and performance of procurement function. The null hypothesis anticipated in this study prior to survey that there is no significant relationship between contractual agreement and the performance of the procurement function in selected universities was rejected and concluded that contractual agreement contribute positively towards supplier loyalty and commitment ($P=0.390$). This value shows that there was a strong correlations between contractual agreement and commitment and loyalty (Sig. =0.001)

Table 4.5: Results of t-test on effects of contractual agreement on performance on procurement function

| N | 95% Level of Significance | R | t (Statistic) | df |
|----|---------------------------|---------|---------------|----|
| 75 | 3.731 | 0.390** | 5.849* | 75 |

*P< 0.05.

DISCUSSION

There was positive correlation between contractual agreement and procurement function performance. This can be interpreted to mean the staff perceived the contractual relationship with source partners as a positive relationship (Table 4). In other studies conducted elsewhere, organizations are increasingly emphasizing co-operative relationships with critical suppliers and the strategic alliance between buyers and suppliers therefore has become perhaps the most important aspect in the procurement performance (Kemunto & Ngugi, 2014). As a result, maintaining credible suppliers has become a priority for the buyer. This relationship ensures efficient and timely delivery of the supplies while building loyalty and commitment among the partners.

In support of these findings, Veludo *et al.* (2006) concluded that supplier-buyer relationships have today become the backbones of economic activities in the modern world and a focal point of organizational competitiveness, performance and long-term business success. With specific benefits, Kemunto & Ngugi, (2014) identified as: lower overall costs, higher quality products, less time to market due to open communication and improved technology and innovation. These contractual agreements however do not always come with affirmative benefits. It comes with shortcomings such as the amount of time and effort involved in building this trust. Buyers' time must be spent nurturing the relationship opposed to other value adding activities.

There must also be time spent to begin the relationship and earn the trust of the supplier. According to Benton *et al.* (2005) there are also higher switching costs if problems were to arise with the supplier and there is a sharing of proprietary information, strategy, planning, and goals, [and] most firms do not feel comfortable exposing such elements to other firms, fearing a loss of control. Another drawback of the contractual relationship may be depicted in terms of product quality. Relationship value seems to be positively correlated with relationship quality and vice versa (Ulaga and Eggert, 2006).

However, it is also possible that a relationship is high value but low in quality. For example, partners may gain cost savings but collaboration is still difficult. A relationship may also be of high quality, collaboration working just fine, but the cost of the relationship is too high. Thus, a successful contractual relationship requires that both value and quality of the relationship are high. On the other hand this finding however contradicts with the conclusion of Narayanan *et al.* (2007). Contractual agreements might not be desirable when a company has a certain amount of leverage over its suppliers, or if the suppliers have all the power then the buyer might not be willing to enter into a relationship.

The relationship between contractual and relational governance has been studied mainly in the private sector where practices and environments are different compared to the public sector as discussed earlier. However, Narayanan *et al.* (2007) argued that even though formal controls are necessary and dominant in public procurement for accountability and transparency reasons, informal controls may play an important role especially during the contract implementation phase. Trust between partners is seen as particularly beneficial in enhancing the quality of service provision and relationships in general.

In the private sector relationships may be already moving towards more cooperative partnerships, enabling the delivery of more complex solutions through collaboration and co-development (Lee & Kim, 2005). If holistic solutions are objectives in the

public sector, too, traditional contract-based relationships may no longer be sufficient. Proactive contracting and relational contracting may offer new insights into public procurement, emphasizing the functionality of the contract and relational aspects alongside the formal contract.

In further support of this findings, Griffith & Myers (2005) in their study concluded that the management of supplier-buyer relationships as a primary driver of both customer and shareholder value have a positive impact on performance of procurement function. This is particularly true due to the increased adoption of globalization and outsourcing strategies (Warner, 2004) leveraged by company specialization and focus on their core competencies in order to withstand today's competitive market pressures (Blome & Schoenherr, 2011). Supply disruptions are also less likely as the relationship is similar to friendship and suppliers and buyers look out for one another rather than opportunities to take advantage of one another.

In other studies elsewhere, Vonderembse (1999), found out that the strategic roles played by suppliers in organizations play a vital role in creating a competitive advantage and their actions have a significant impact on the performance of the organization. In the study conducted by Kemunto & Ngugi, (2014) procurement policy and relationships coefficient of (0.811) were found to be positive at significant level of (0.001) and this indicates that policy and contractual agreements have a positive influence on procurement function performance.

CONCLUSION AND RECOMMENDATIONS

These contractual relationships ensure efficient and timely delivery of the supplies while building loyalty and commitment among the partners. Supplier-buyer relationships have today become the backbones of economic activities in the modern world and a focal point of organizational competitiveness, performance and long-term business success. The contractual agreement with source partners however, comes with shortcomings such as the amount of time and effort involved in building this trust. Buyers' time must be spent nurturing the relationship opposed to other value adding activities. There must also be time spent to begin the relationship and earn the trust of the supplier. Suppliers play a vital role in creating a competitive advantage and their actions have a significant impact on the performance of the organization. The study concluded that contractual agreement contribute positively towards supplier loyalty and commitment

The study recommends that contractual relationships between the university and source partners must be supported from the entire organization. A buyer must have the authority to negotiate with a supplier and come to an agreement that carries mutual trust and benefit.

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