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Social Factors to Manage Relationships**

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# **Buyer-Supplier Relationships in Small Firms: The Use of Social Factors to Manage Relationships**

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## **ABSTRACT**

*In this paper the authors explore customer and supplier relationships from the perspective of small firms (SMEs). They introduce the general supply chain literature and highlight some key problems when such theory is applied to understanding the practices of SMEs. In particular they introduce and critique current study focusing on the purchasing behaviour of small firms. This critique illustrates some key issues including the dominance of ideas that depend on the practices of large firms and the assumed homogeneity of the SME population. Following this critique the paper sets out a rationale for exploring what SMEs 'do' in terms of purchasing behaviour. The empirical studies outlined explore two groups of firms, a general control group across the SME population and a specific purposeful sample set in steel based manufacturing companies. The results illustrate the important role of social factors in the management of relationships.*

## **KEY WORDS**

*Purchasing, supply chain, customer, supplier, manufacturing, relationships*

The ability to provide high levels of customer satisfaction has been considered an essential ingredient of business success (Quayle, 1999). In many industries these increasing demands have led to a need for lower prices and improvements in quality and service (Quayle 1999; Quayle 2001). Such pressures have forced many firms to review their approach to operations management and, in order to remain competitive, they have examined the potential contribution suppliers can make (Flood and Isaac 1992; Scully and Fawcett 1994). This focus on supply chain management has also occurred due to increased specialisation and outsourcing, which has led many organisations to limit their own operations and increase the use of external specialists (Gadde and Hakansson

1993; Calabresse 2000; Axelsson and Larsson 2002). The role of external suppliers has increased significantly over the last decade and it is not unusual to find 50% of turnover spent on acquiring materials and services (Scully and Fawcett 1994; Perkins and Gunasekaran 1998; Quayle 2001; Axelsson and Larsson 2002; Boodie 2002). Purchasing has developed into a crucial management discipline and the functional purchasing practices that were prevalent in the 1970's have been superseded by more strategic approaches, drawing on an array of 'best practice' techniques, to secure competitive advantage and continued contribution to financial performance (Quayle 2001; Boodie 2002).

Throughout this period developments have been supported by, or developed in response to, academic and practitioner literature. Concepts such as: Total Quality Management (TQM); Just-in-Time (JIT); Partnership and Strategic Alliances; Supplier Development; International Purchasing and Supply Chain Management; have all drawn heavily from the US and UK research (Ramsay 1994). The adoption of these techniques, the majority of which have been derived from studies of larger firms, has been varied (Perkins and Gunasekaran, 1998) and their relevance and usefulness to smaller firms (SMEs) remains questionable (Ramsay, 1994). The purpose of this paper, therefore, is to explore the literature on purchasing practices in SMEs, which has typically drawn from work on larger firms, and to assess its contribution to understanding the 'actual' purchasing practices of smaller firms. Following the analysis of the literature the paper explains three empirical studies that have been undertaken to better understand these practices and to show how such practices might differ from those of large established businesses.

## **RELATIONSHIPS IN THE SUPPLY CHAIN**

The nature of the relationships between a firm, its customers and suppliers, has important business implications for all firms irrespective of size. Adversarial relationships between buyers and suppliers were prevalent in Western economies during the 1970's and 1980's. These relationships were short-term and price was the primary concern. The interaction between organisations was predominantly restricted to the level of buyer and supplier, typified by formal transactional type paperwork systems, which were used as the most frequent medium of communication (Saunders 1997; Langfield-Smith and Greenfield 1998). Negotiations were often confrontational and underpinned by a win-lose philosophy, the outcome of which often led to a change of suppliers (or at least the threat of change). Power was leveraged (or abused) for maximum organisational gain and there was a distinct lack of trust between trading parties (Saunders, 1997).

One of the major changes in the literature has been an apparent, or certainly an emphasis toward, a shift in the nature of the buyer-supplier relationship from the traditional adversarial type towards one of collaboration (Hines 1994; Schmitz 1995; Holmlund and Kock 1996; Saunders 1997). In support of these ideas a number of relational models have been developed within the purchasing literature. One of the earliest models is provided by Kraljic (1983) who presented the purchasing portfolio model which has since been the subject of further developments (Olsen and Ellram 1997). Hines (1994) also suggested an alternative approach for managing relationships called network sourcing<sup>1</sup>. Sako (1992) introduced more social concepts to the study of relationships in her discussion of trust and its role in long-term relationships and at the same time the concept of partnership sourcing and lean supply were being publicised by

Lamming (1993) as was the concept of Supply Chain Management by Macbeth and Ferguson (1994). The overall emphasis in these developments was to encourage purchasing practice to move away from the adversarial approach to one of collaboration. This change in emphasis also led to a reported change in the practices of firms, the extent of this change remains unclear (Morrissey and Pittaway, 2004). Cousins (2002), for example, noted that research on the subject can be divided into two main themes. First, those grounded in the economics of power within exchanges and secondly, those using humanistic assumptions where the emphasis is on social values and trust. While these exist as separate conceptual views in theory, in practice the two approaches exist simultaneously, although it is often recognised that one form tends to dominate particular relationships (Bachmann, 2001).

As with the general discussion of the purchasing literature, the discussions on relationship management have been developed from the perspective of large organisations (Schrunder and Mudambi, 1995). Rarely do such studies analysing co-operative relationships between buyers and suppliers come from the perspective of the SME (Schrunder and Mudambi, 1995; Mudambi, Schrunder et al. 2004). In the next section the paper explores studies that have examined these relationships in SMEs (presented in Table 1). Table 1 illustrates that only a small number of studies have been undertaken and as will be explained there are some major limitations of this work.

## **SUPPLY CHAIN RELATIONSHIPS IN SMALL FIRMS**

[Insert Table 1]

### **The Relevance of 'Power'**

The mainstream purchasing literature offers a wide and varied discussion exploring the concept and influence of power in supply chain relationships (Ramsay

1994; Cox, Sanderson et al. 2000; Cox 2001; Cox 2001). It is argued that those organisations able to recognise and use power during purchasing will benefit accordingly (Boodie 2002). Unfortunately, as highlighted in Table 1, there is limited research exploring the subject specifically from the perspective of the SME. This is perhaps surprising considering the disadvantages that SMEs can face as a consequence of power asymmetry within the supply chain. In the absence of uniqueness, the basic problem facing SMEs can be their size and lack of power. Mudambi et al. (2004) for example, confirmed that size asymmetry was a determining factor affecting the levels of cooperation a purchasing SME could expect from a larger supplier. Ultimately they found, that larger suppliers were able to dictate the degree of closeness they wanted in the relationship with their smaller customer.

Whilst it is broadly acknowledged that size based power cannot be ignored, this alone should not be considered the key factor influencing dependency. It is also evident that the level of importance that a customer places on a particular supplier in terms of volume or strategic value are also key variables in determining the nature of the relationship and this can be important regardless of firm size. For example, a small company operating in a niche market or offering specific expertise to its customers may hold a more important position in the view of its larger supplier than may be expected prima facie, given its size (Lamming and Harrison, 2001). Irrespective of the source, however, power can result in compliance and, in particular, it does drive the adoption of new purchasing practices (Axelsson and Larsson, 2002). Axelsson and Larsson (2002), for example, observed how 4<sup>th</sup> and 5<sup>th</sup> tier suppliers responded and adopted new practices because of the strong signals from their customers, which led them to apply new purchasing concepts on the request of their customers. Evidence supporting this small firm adoption principle in manufacturing can be found from the number of small

firms that have to achieve ISO accreditation in response to demands from buyers (Axelsson and Larsson, 2002).

Bates and Slack (1998) make similar observations and bring into question the relevance of many texts that assume an equal balance of power across supply chains.

*“The advice focuses on customer expectations which must be met in order for suppliers to ‘stay in the game’ which normally infers achievement of some degree of operational integration, a well developed policy on just in time, exchanging technical staff to optimise product development and facilitate early problem resolution, as a minimum. In situations where companies are confronted with larger and / or more powerful suppliers it would be questionable if they could ever enforce such a modus operandi”* (Bates and Slack 1998, pp74)

Zheng et al. (2003) further this view by explaining how a lack of purchasing power may affect the purchasing behaviour of SMEs. In their study, SMEs that lack purchasing power are reluctant to engage in the market, resulting in a fragmented approach and lack of strategic direction in their purchasing activities.

Competitor power is also of concern to SMEs, especially when buyers can at short notice switch suppliers. In this position dominant buyers are able to make demands not only on the deliveries and quality of the product but may in addition force weaker suppliers to manufacture unprofitable products (Holmlund and Kock 1996; Saunders 1997). For example, Saunders (1997) makes a relevant observation for SMEs when arguing:

*“In taking note of power dependency relationships, it is possible to distinguish the three types of partnership situation, although some people might like to dispute whether the relationship can be a genuine partnership, if it is dominated by one of the parties. It depends, perhaps, on how the dominant partner chooses to use that power and how far trust and mutual interests are pursued”* (Saunders, 1997, p260).

This observation suggests that instead of focusing on the relative power position between the two firms, SMEs may be better advised to seek out organisations and/or individuals with whom they feel they can develop relationships. Similarly it may be

prudent, where possible, to distance themselves from organisations that repeatedly demonstrate a high propensity toward profit maximisation.

What has been excluded from these discussions in the mainstream literature, however, are the motives and behavioural characteristics of the owner-manager which also have an impact on the forms of relationship they prefer (Morrissey and Pittaway 2004). Certain motivations, such as lifestyle goals, can lead to a preference for different forms of relationship despite the fact that these may seem illogical when prior theory is applied (Morrissey and Pittaway, 2004). For example, an owner-manager's desire for autonomy and possible disposition towards social aspects of relationships should not be ignored when trying to better understand the dynamics of power within SME buyer-supplier relationships.

### **The Role of 'Trust'**

In the absence of power, trust offers the SME an alternative for managing inter-firm relationships, especially in their relationships with suppliers (Zheng, Caldwell et al. 2003). Trust, like power, is a complex concept having a diverse range of definitions from a variety of disciplines. Some of the more prominent work includes that on system based trust (Luhmann 1975), institutional trust (Zucker 1986), calculative trust (Williamson 1985), trust as social capital (Coleman 1990), competence, contract and goodwill trust (Sako 1992) and personnel trust (Lane 1998).

In a purchasing context it is possible to identify dependency as the key source of power. The object and focus of trust, however, is highly variable and too complex to be reduced to a single dimension. This 'trust' is something that is rarely based on a single episode but instead developed over a period of time (Gadde and Hakansson 1993). Cousins (2002) for example, argues that: "*organisations do not trust each other; they manage risk based on business case decisions*" (Cousins, 2002, p71). He makes a

further assertion that trust and risk are the same thing, just at separate ends of the same spectrum. Consequently, trust is seen as positive whereas risk has negative connotations.

According to one previous study, SMEs can add value to their external relationships by acting in a trustworthy manner (Sako and Helper, 1998) but such behaviour can also be abused if it does not have an attitudinal fit with the partner. Sako and Helper (1998) highlight this point:

*“Customers can be made to behave in a predictably trustworthy or non opportunistic manner if they cannot replace their existing suppliers easily, regardless of other factors. It is when easily accessible alternative suppliers exist that suppliers give careful consideration to safeguards in deciding how much opportunistic or trustworthy behaviour to expect from customers” (Sako and Helper 1998, p407).*

This quotation also serves to reinforce the interplay between economic and social variables and shows how power and trust may be intrinsically linked in buyer-supplier relationships.

The importance of trust in buyer-supplier relationships is not a view shared by all theorists. Cox (1997), for example, questions the utility of trust within business relationships claiming that trust cannot be enforced and should not be volunteered. He goes on to suggest: *“...the only means of fostering collaboration is either through unequal power-relationships, or by incentivising the suppliers”* (Cox, 1997, p134). He also raises a further relevant point for SMEs, which is: *“...the purpose of a relationship is merely to serve the business objectives of purchase-supply”* (Cox, 1997, p130), suggesting that the rationale of privately owned firms is, first and foremost, the creation of profit. While this may be valid for the Original Equipment Manufacturer (OEM) and 1<sup>st</sup> tier organisations, the owner-manager may have a range of motives which are less transparent, where other factors may be placed before profit (Morrissey and Pittaway 2004).

## Creating Cooperation through Consortia

Much of the literature on SMEs highlighted in Table 1 explores relationships from the perspective that collaboration exists and that SMEs are willing participants. Axelrod (1984), however, concluded that one of the insights of game theory was the conclusion that cooperation is difficult to establish, even though the benefits are clear. Powell (1990) identifies perhaps one of the most important issues in his suggestion that to be effective, in network forms, members are expected to: *“...forgo the right to pursue self-interest at the expense of others ... and recognise their co-dependence with upstream and downstream partners”* (Powell, 1990, p103). A review of the small firm purchasing literature confirms that cooperation between small firms remains problematic even though it is one method for increasing power and reducing dependency on larger firms (Morrissey and Pittaway, 2004). Reporting on earlier work by Hines, for example, Quayle (2000) argues that there is a lack of evidence that firms make a sustained effort in establishing a foundation for lasting relationships. Instead the ‘partners’ had a tendency to choose the best parts from a cooperative relationship with little regard for their partners. In his view buyers would benefit if they showed more long-term commitment to initiatives, such as supplier development, rather than using it as a means to gain immediate results (Quayle 2000). Calabresse (2000) also supports this view and highlights that through acting opportunistically dominant buyers are able to maintain their power base:

*“The different position of strength between buyers and suppliers must be considered, analysing the relative asymmetrical situations that one of the parts (often the car maker), by offering part of its own knowledge manages to obtain information about the supplier, while safeguarding and increasing its own position of power”* (Calabresse, 2000, p62).

The difficulty for cooperation arises because relationships are not static. *“Even if relationships between supplier and customer calls for the customer’s response not to be*

*traditional and short term in a crisis, but to take the specific relational investment made into consideration, the temptation to transfer its difficulties to the weaker firms is great” (Esposito and Raffa, 2001, p358).*

A critical element of partnership arrangements is an open book policy; however, instead of engendering good relationships it has the opposite effect. Many view the process as nothing more than a ‘confidence trick’ resulting in a lack of trust (Tulip 2000). An appropriate example of the combination of power, trust and opportunism and the interplay between the three can be seen in the concept of purchasing consortia. Essig (2000) analyses and systemises previous work on consortia, providing an overview of the literature, and Quayle (2000) suggests consortia seem to be the ideal form for small business through which they can increase their purchasing power. Despite the apparent logic in this proposition there remains a continued resistance to the effective establishment of consortia amongst small firms (Morrissey and Pittaway, 2004). This occurs despite evidence of short-term collaboration that is designed to satisfy immediate goals. Lack of trust, the disproportionate benefits to the smaller organisations, and an underlying fear of opportunistic behaviour continue to restrict development of purchasing consortia. Similarly the power of the supply base and their reported unwillingness to supply via consortia is also a prohibiting factor (Morrissey and Pittaway 2004).

The literature outlined also alludes to, although implicitly, the lack of homogeneity across SMEs and between different types of owner-manager (Morrissey and Pittaway, 2004). Each actor in a consortium will have a discrete set of motives, values and needs influencing not only their actions, but their perceptions of other members. Such diversity gives rise to a complex and potentially conflicting value set within the group that can restrict the formulation of trust. Without too much deliberation it can be seen that, even for the simplest of products, different dimensions of trust may be of importance; trust in quality; trust in price; trust in timeliness and availability of deliveries; trust in the other

actors. Perhaps then the lack of homogeneity in the cognitive attributes of actors combined with the varied objects of trust in any one transaction will continue to restrict the formulation of trust and ultimately the consortium itself.

### **KEY CONSIDERATIONS**

Before embarking on the empirical studies that will be outlined in this paper it is important to identify the key conceptual considerations that arise as a consequence of prior study. First, considering that many manufacturing small firms are now dominated by major customers, their lack of influence in relationships means that the concept of collaboration may be questionable when one takes the perspective of the smaller firm. Some small firms find the situation unhelpful especially if they are seeking 'collaborative comfort' in a niche relationship with a larger company. Dominant customers can ensure that existing attitudes remain and can continue to operate in an adversarial way pushing down prices and demanding greater quality and more productivity despite rhetoric supporting collaboration. Secondly, mainstream purchasing models and techniques, grounded from the perspective of dominant and highly resourced companies are being used to measure the efficiency and effectiveness of small firms. It is questionable how appropriate these techniques are when applied to much smaller firms with fewer resources. Purchasing as an activity is important to many organisations and SMEs are no different but the nature of the practices and how they should be measured may differ substantially. Thirdly, the UK economy has many successful small businesses; if purchasing is important for the continued success of these businesses their ability to prosper must suggest that they are doing something 'right', albeit different from large firms, in managing their buyer-supplier relationships. Prior research has not sufficiently explored what small firms 'do' and consequently previous research has sought to critique SME practices without fully appreciating what these practices 'are'. Fourthly, all of the

studies reviewed assume homogeneity, that the motives underpinning practices are the same and that all SMEs can be grouped together. This is not solely limited to the assumed commonality between the motives of large organisations and owner-managers but also the assumption of homogeneity across the SME population. There is, however, likely to be significant difference in purchasing practices between sectors and between size categories within the SME population. For example, a manufacturing company with 80 employees, including a full time purchasing professional, will have different practices when compared to a manufacturing company employing 10 people, especially if the owner-manager is responsible for the purchasing.

In order to have a better understanding of purchasing practices in SMEs and increase the utility of research it is important that empirical studies are more focused. This should include both a more focused approach to industrial sectors and also organisational size. Such research needs to explain what small firms 'do' when they engage purchasing relationships rather than apply the conventional wisdom of purchasing behaviour which has been derived from the practices of much larger companies. It is with this objective in mind that the empirical studies to be explained in the next part of the paper were constructed.

## **METHODOLOGY**

There were a number of stages to the research reported in this paper. The first pilot stage involved interviews with six firms on which a questionnaire was based. The next two stages involved surveys targeting different populations of SMEs and different sampling methodologies. The data used in this analysis are principally drawn from the two surveys but some aspects of the qualitative research have been used to assist the discussion.

The first stage of the research began with a series of detailed unstructured interviews in which the participants were asked about their supplier and customer relationships. These firms were all SMEs, as defined by the number of employees (less than 250). The sample was drawn from the plastics moulding industry as it was considered to provide a fair representation of manufacturing firms. Plastics moulding firms provide a useful focus for this study because they operate in markets that tend to be dominated by relatively monopolistic suppliers and they supply products to relatively powerful profit maximising customers. The firms in the sample were selected from Kompass, and located in the North West of England. Initial introductions were made over the telephone where the researcher explained the purpose of the research and the experience of the researcher. Access was also negotiated with the respective owner-manager at the time of initial contact. Firm size varied from 17 to 80 employees with turnover ranging between £700 thousand to £4 million. The firms involved with the qualitative aspects of the study are summarised in Table 2 below.

[Insert Table 2]

The interviews were carried out at the business site of the owner-manager and typically lasted between 1½ to 2 hours. The interviews were recorded and transcribed allowing further detailed analysis. In each case the interviewee also received a copy of the transcript and was asked to confirm that their interpretation of the data was represented in the transcript. During data analysis the full transcripts were analysed using coding, individual transcripts were subsequently summarised and common themes were identified from all of the interviews.

The data from the interviews informed the development of a questionnaire that focused on different dimensions of customer and supplier relationships. The questionnaire was sent to a number of owner-managers for review and comment and was trialled before the full survey was undertaken. Modifications were made in

accordance with their comments and sent to a further set of owner-managers for comment. The comments from the second review confirmed the suitability of the questionnaire used in both surveys. The target audience for the initial survey (1) was random in so much as the questionnaire was enclosed within Insight, a North West business news magazine circulated to organisations working with the North and Western Business Link. Data protection prevented a more focused sample being selected; similarly we were unable to encourage responses via common methods, such as, follow-up calls. As a consequence the response rate for survey one was low, from approximately 4000 questionnaires sent out 53 were returned. Despite its low response rate the sample provides an adequate control group representing responses for SMEs in general across industries and sectors.

Survey 2 had a much greater focus and used a purposeful sampling technique. In this instance three UK based SMEs were identified who were involved with the process and supply of stainless steel products. Contact with the owner-manager was made and meetings arranged to discuss the survey method. It was requested that each of the focus firms provide a sample listing of their suppliers and customers to whom the questionnaire could be sent. Each focus firm advised the relevant suppliers and customers and emphasised the value of their contribution in completing the questionnaire. This was integrated into the focus firm's normal business activities. Questionnaires were then sent to a purposeful sample of 122 companies and 80 responses were achieved (response rate of 66%). Many of these firms confirmed their willingness to discuss the research in more detail and a future phase of the research includes interviewing some of these firms. Table 3 provides a summary of the respondents involved in the two surveys.

[Table 3]

The replies from the two surveys were entered into SPSS for data analysis and were analysed in relation to descriptive and analytical statistics. This paper will review the findings from the research with a particular focus on answering the question – what do SMEs ‘do’ when engaging in customer and supplier relationships? The results from this analysis are explained in the next part of the paper.

## **DISCUSSION OF RESULTS**

In this part of the paper the results are explained according to the key considerations outlined earlier. The data explained here explore the key factors driving relationships in the supply chain from the SMEs’ point of view; they analyse the role of trust and power and explain the key factors that were considered important.

### **Purchasing Function within SMEs**

In the two surveys manufacturing SMEs show the greatest tendency towards establishing a separate purchasing function to manage supplier relationships (35% in the second survey versus 19% in the first survey). In all SMEs, however, it is evident that the owner-manager remains sufficiently active in purchasing relationships. For example, in the control survey 57% of SMEs reported that the owner-manager was involved in purchasing decisions and this figure was similar to the industry specific survey (55%). More detailed analysis of survey 2 showed that more mature manufacturing firms, 10 years plus, demonstrated a tendency towards having a separate purchasing function (these were typically larger SMEs). Similarly 26 to 50 employees and a turnover in excess of £1 million seemed to be the threshold for the establishment of a discrete purchasing role. The results from survey 1 were almost identical other than for the number of employees. In this instance firms having 25 employees or less accounted for the majority of purchasing departments. This can perhaps be explained by the lower

relative size of firms in other non-manufacturing sectors (e.g. tourism). No correlation existed between the percentage of turnover spent on acquiring goods and services from third parties and the existence of a separate purchasing function. The data, therefore, support the view in the literature (Mudambi et al. 2004) which argues that sector is more likely to dictate the existence of a purchasing function than SME size. In this study manufacturing firms were more likely to have discrete purchasing activities, although where a firm spends less than £1 million and / or has less than 25 employees it is more likely that the owner-manager or another department will undertake the purchasing function.

Respondents of the two surveys were asked whether they felt they had better relationships with their customers or suppliers, 32% of survey 1 and 21% of survey 2 felt that they had better relationships with their customers, however, many firms (60% plus) have as good as, or even better relationships with their suppliers. These data consequently illustrate the important role of these relationships to SMEs, which somewhat contradicts the findings of Quayle's (1999; 2001) research. In the next part of the analysis the key drivers influencing the relationship are explored further and these provide more evidence of the value of supplier and customer relationships from the perspective of owner-managers.

### **The Drivers of Supply Chain Relationships**

Owner-managers in the two surveys were asked to rank price, quality, delivery speed/reliability and technical support in terms of what they perceived to be the most important to their customers. The most important attribute was ranked 1 whilst the least important was ranked 4. The results from survey 1 show that when the owner-manager was responsible for sales the selling price was deemed to be the most important attribute. In contrast when a sales manager (or employee) had the most contact with

customers quality was considered the most important factor and rated higher than price. The results from survey 2 show a different picture and are less conclusive. When the study focused on the relationships of manufacturing SMEs the owner-manager placed equal importance on price, quality and reliability, whereas sales managers tended to place greater emphasis on reliability and price, as important drivers of the relationship. This result contrasted with the general population of SMEs in survey 1 where sales managers considered quality as the most important factor driving relationships (for results see Table 4).

[Insert Table 4]

In the next part of the questionnaire respondents were asked to consider the importance of these factors as they related to their relationships with suppliers. Table 5 presents these results. Survey 1 shows that quality is considered the most important factor irrespective of whether the owner-manager or purchasing manager is responsible for supplier relationships. It is worth noting, however, that owner-managers rate price second in importance when compared to their purchasing counterparts who choose reliability. The manufacturing relationships in survey 2 present a different set of responses. Here the owner-managers emphasise the importance of price, a topic of less concern for the buyers, who once again choose quality as the most important factor.

The two surveys show some interesting differences about the drivers of supply chain relationships that confirm the problems of previous theory as outlined in the key conceptual considerations part of this paper.

[Insert Table 5]

As survey 2 was a study focusing on a competitive and aggressive market sector price competition was an important contextual factor influencing the perspectives of owner-managers, whose personal livelihood could be affected by the nature of their relationships with customers and suppliers. In contrast survey 1 analysed a range of

sectors, looking at SMEs views in general, and found different drivers within different sectors. These results, therefore, indicate that empirical study on purchasing behaviour in SMEs needs to become more heterogeneous recognising that contextual factors based on sectors have major implications for the nature of SME supply chain relationships.

The results of both surveys also present some interesting discussion points. For example, in survey 1 owner-managers when dealing with customers feel they place more emphasis on price, when compared to sales managers. This is surprising because one would expect sales managers to rate price more highly as they are usually more central to customer negotiations than owner-managers. On the same theme it is surprising in survey 2 that owner-managers rate price in their dealings with suppliers more highly than purchasing managers because these managers are more typically involved with negotiation on price. One possible explanation for these results could be that owner-managers have greater financial and emotional exposure than employees of the business and, therefore, take on more responsibility for supplier-customer relationships and because of their personal financial exposure have an intrinsic desire for profitability. The findings would, therefore suggest two conclusions. First, owner-managers personally take on responsibility for key aspects of supply chain management (this does depend on SME size). Secondly, they do so because the management of these relationships is essential for the profitability of the business. Consequently, from the point-of-view of SMEs, price emerges from this study as the key driving force behind supplier-customer relationships, which rather undermines the current concepts, based on larger businesses, which promote collaboration in supply chains (Hines, 1994). The question remains, however, why should purchasing professionals put more emphasis on other factors (than price) when one would expect the opposite, especially as they are more likely to be dealing with the detailed tactical day-to-day negotiations. An initial

observation is that the 'trained' purchaser, who is schooled in concepts that are designed to reduce the total cost of acquisition, has a more sophisticated view of these relationships seeking to influence the business in terms of quality, therefore, trying to avoid the costs associated with non-conformance rather than focusing narrowly on price.

An alternate explanation, particularly in the second survey, may lie in the criteria for ISO accreditation. It is a basic requirement for many large companies to only source from ISO accredited organisations. With this demand comes the continual requirement to measure supplier performance including quality and delivery reliability. If one combines this with the 'stigma' attached to the more traditional adversarial models of purchasing whose primary focus is price, one can see a different 'model' of supply chain practice for purchasing professionals as that pursued by owner-managers.

One final observation from this part of the study was that irrespective of the particular supply chain it was found that whatever pressures were applied from the customer base tended to flow through to the suppliers. For example, an owner-manager who perceived price as most important to their customer would place similar emphasis on price when managing their suppliers. This finding illustrates the pressure that can be created for SMEs in supply chains when there is lack of competition between OEMs or where the industry is relatively concentrated having only a few major competitors (e.g. supermarket chains). One positive point from this observation is that whilst their relational management skills may not be as refined or as extensive as the larger corporate, owner-managers in general tend to adapt their approach depending on the requirements of particular supply chains.

### **The role of trust**

Both surveys sought to analyse the importance of trust in commercial relationships (see Table 6 for results). Respondents in both surveys highlight the role of

trust and its value when seeking to create effective customer and supplier relationships. The respondents to both surveys also considered it worthwhile investing resources in the development of customer and supplier relationships as a means to create trust. Although the quantitative elements of the study restrict our ability to explain what is meant by 'trust' by these respondents and how they act to create it the qualitative aspects of the study do provide some initial thoughts. For example, as reported by Morrissey and Pittaway (2004) individuals place much significance on the quality of relationships, both commercially and socially, but this alone does not explain why the respondents are prepared to commit scarce resources in the development of such relationships. The interviews confirm that owner-managers are not only fully aware of their relative power position (between themselves and their customers and suppliers) but are extremely aware of the relationships that have most importance to the business. Owner-managers in SMEs will typically seek to develop and maintain strong business relationships based on 'trust' while remaining realistic about the utility of this 'trust'. In this sense, it seems fair to suggest that the management of 'trust' in direct commercial relationships is an important competence for the successful management of an SME. Whilst it was agreed by the survey respondents and interviewees that a strong relationship would not necessarily guarantee continuous business, many felt that such relationships provided them with an opportunity to respond if circumstances in the relationship changed. For example, if a small firm's customer threatened to move to a competitor it was generally considered that 'trust' in the relationship would at least ensure that they are notified of the threat and given a reasonable time to respond. In the absence of 'trust', it was considered that the SME would lose the work without any prior notification. Unfortunately the empirical work undertaken, which is reported here, only provides half of the picture. In order to more fully understand how trust can be generated and the benefits it can bring to SMEs one also needs to focus on the

viewpoint of the trading partners. Such work needs to explore their general disposition towards social norms such as trust and take into account the context of particular relationships. Consequently, only more detailed qualitative research will be able to delve more deeply into this aspect of the subject.

[Insert Table 6]

In the next part of the analysis the questionnaire explored the factors that were considered important within customer relationships in more detail and this illustrated in depth the role and value of trust in relationships. Respondents were asked to rank on a scale of 1 to 5 the relative importance of particular attributes to their customer relationships (20 attributes in total). The following attributes were assessed: being kept informed; attitude of customer staff; long-term contracts; on time payments; credit terms; input into new products; demand for cost transparency; price determining factor; honesty; openness; early involvement in projects; mutual advantage; words backed by action; receptive to ideas; attitude; loyalty; price pressure; fairness in negotiations; confidence in personnel; and, honouring agreements. The results are shown in Table 7.

[Insert Table 7]

From the list of 20 attributes respondents in both surveys were asked to confirm what they felt were the most important to their customer relationships. In this instance 1 was of no importance whilst 5 indicated high importance. In survey 1 the top five factors were: honesty; honouring agreements; openness; loyalty; and, words backed by action. In survey 2 the top five factors were: honouring agreements; honesty; attitude; words backed action; and, openness. What is striking about these results, if one explores Table 7 in detail, are the clusters of factors rated as important in both surveys. The first cluster, which includes the first six attributes, are all linked to social aspects of the relationship and are based on different dimensions of trust (e.g. honesty, openness, honouring agreements, loyalty, attitude and words backed by action). The next cluster

tends to focus on the more formal dynamics and processes involved in the relationship (on time payments; being kept informed; attitude of customer staff; fairness in negotiations; confidence in personnel). The final two clusters which overlap concentrate on formal contractual issues (long-term contracts; credit terms; price the determining factor; price pressure; demand for cost transparency) and aspects of innovation (mutual advantage; early involvement in projects; input into new products). From the data one can conclude that the social dimensions of relationships are seen by SMEs as the key mechanism through which they can manage their customer relationships. Obviously more detailed research on the dynamics of social dimensions would add a further contribution to knowledge on purchasing relationships in SMEs.

Other important observations can be made from this data. First, the means in the second survey concentrating on a specific manufacturing sector are consistently higher than those in the first survey, and secondly, there is a much lower standard deviation in the second survey. The first difference illustrates the important contextual factors that can influence perceptions of supply chain relationships. Clearly, a more intense supply chain will lead to more intense opinions and this is represented in the data. It is also important to point out, however, that the relative order of the attributes is the same in both surveys. This result indicates that the control group of SMEs have similar views to the industry specific group, which shows that the social aspects of customer relationships are viewed to be the most important cluster of attributes across all sectors and, are therefore, relevant to SMEs in general. The difference in standard deviations between the surveys is also interesting. It illustrates a consensus of opinion in the industry specific group but not necessarily in the control group. The lack of consensus may illustrate some differences between sectors or types of SMEs and the next phase of the research will explore these differences using more detailed analytical statistics.

## **CONCLUSIONS**

This paper has examined current theory and research exploring supply chain relationships in SMEs. The review illustrated that purchasing had become recognised as an important management consideration and that current theory based on the practices of larger firms had been based on conceptions of collaboration. When concluding current thinking on purchasing and SMEs a number of problems were identified:

- i) The dominance of large firms in supply chains and their consequent power in relationships brings into question the concept of collaboration when viewed from the perspective of SMEs.
- ii) Consequently, it was expected that adversarial practices continue in relationships despite the rhetoric of collaboration expressed through the purchasing policies of larger businesses.
- iii) One of the weaknesses of prior research has been to use theory and empirical study, which is based on larger businesses, assuming that it can be applied to smaller enterprises. Many of the techniques and models used to judge the efficiency and effectiveness of SMEs in the purchasing domain may be questionable as a result.
- iv) SME practices in purchasing are still successful and may be quite different from the usual conceptions of 'best' practice.
- v) Studies have tended to erroneously assume homogeneity of the SME population.

The empirical research conducted was designed to explore some of these problems and issues by exploring what SMEs do when managing supplier and customer relationships.

As outlined in the methodology three empirical studies were carried out, one small qualitative study, one broad survey of SMEs in general and one sector specific survey. In total the views of 130 businesses were explored in the empirical data presented in this paper. The key results help answer some of the questions set by the limitations of current theory. It was found that a majority of SMEs actively manage their purchasing relationships. In smaller firms and those outside manufacturing this is typically carried out by the owner-manager. In larger manufacturing SMEs there is often a specific purchasing role, however, owner-managers tend to take the lead role. The results show, in contradiction to prior research (Quayle 1999; 2001), that SMEs do actively manage and value their purchasing activity. What is evident, however, is that the role is often incorporated into the general role of the owner-manager or other non-professional due to resource constraints placed on the business.

The analysis of the data proceeded to examine the key drivers of relationships questioning the idea of collaboration. In this part of the study it was identified that owner-managers tend to be more price driven in their management of supplier and customer relationships. It was also evident that this was different for employed professionals (sales and purchasing managers) in SMEs. Although there are a number of reasons for this finding it was highlighted that the financial exposure of the owner-manager could be a reason for a price focused approach. The data collected focusing specifically on owner-managers, therefore, is in direct contradiction to current theories of collaboration (Hines, 1994). It is concluded that the concept of collaboration is a concept which is a luxury of large organisations and is not accepted as a reality by smaller firms. As there is also a difference between the perspective of owner-managers and professional employees this subject requires further more in-depth qualitative study.

When the analysis began to focus on the role of trust in relationships further interesting results were highlighted. Across both surveys 'trust' was shown to be a

fundamental element of the way in which owner-managers manage relationships. When asked to highlight the key factors that mattered both the control group and the industry specific group highlighted socially-based factors (e.g. openness; honesty). Although the approach undertaken in this study sought heterogeneous samples, recognising differences in the SME population, this result was found to be correct for the sample as a whole. It can be concluded for this work and in direct confirmation of humanistic assumptions (Cousins, 2002), that owner-managers use social factors in commercial relationships to build trust and manage the relationship. This is also in direct contrast to the practices of larger firms that tend to be governed more by formal arrangements (such as, contracts; credit terms). In conclusion this research provides evidence supporting the view that SMEs use different methods when engaging in purchasing relationships and should, therefore, be viewed differently. It is evident that more detailed empirical research is required that can delve into these practices more deeply, possibly via the use of qualitative methods.

Based on this study a number of recommendations can be made for policy and research. First, policy interventions (e.g. ISO accreditation) need to be careful not to apply theories of purchasing behaviour based on large firms in an attempt to change the behaviour of owner-managers. As purchasing relationships may be guided more by social practices these interventions may be an anathema to the effective operation of relationships in the SME sector. Likewise interventions will be restricted by the contextual situation of particular industries and supply chain pressures; consequently formulaic approaches may not work. It is recommended that work is carried out to assess such interventions in light of this paper's conclusions. Secondly, more detailed research is required to delve into the complex nature of trust and power in these relationships to better understand how owner-managers leverage social aspects of commercial relationships for the purposes of profit. Without undertaking such study

researchers will struggle to understand the true dynamics and motivations underpinning supply chain relationships, as they are perceived and managed by smaller enterprises.

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**TABLE 1**  
**Overview of the Literature on Purchasing in SMEs**

<b>Year</b>	<b>Author</b>	<b>Method</b>	<b>Purpose and Findings</b>
1994	Scully & Fawcett	Survey – 500 USA firms, 72 responses (44% SMEs)	To compare and contrast international sourcing activities between small and large firms. Found that SMEs successfully engage in IS although there is a difference in how they do it compared with large firms. In particular SMEs were more limited and there was an emphasis of resolutions to immediate and specific / opportunities or concern
1996	Holmlund & Kock	Semi – structured Interviews	Examines the relationship between a dominant buyer and four small sized suppliers. The purchasing manager at the buyer firm ranked quality first then reliability and finally price. Due to the weak negotiation position of the suppliers some were forced to manufacture what were considered as unprofitable parts. Suppliers considered themselves as independent rather than in co-operation with the customer, and did not feel it necessary invest in, or try and build any social bonds although they appreciated the personal contact. Concluded that the apparent dependency was due to insufficient active searches for new buyers and a lack of uniqueness in their offering.
1996	Corless, Jordan et al	Single case – manufacturer, 65 employees	Introduced a more reactive approach to material procurement in a SME. Recommend adoption of a hybrid approach combining the planning features of MRP with principles of JIT. Benefits included a reduction in inventory and obsolescence that would in turn contribute to an increase in cash flow.
1997	Kasouf & Celuch	Survey – 154 USA / Canadian firms, 62 responses	Provided a study of the relationship orientation in a fragmented supplier industry of firms operating within a competitive context. The results confirmed that those suppliers with limited resources and under pressure to provide more service / develop closer relationships faced intense price pressure. Those firms that remained optimistic about industry growth perceived alliances as important. Recommended that OEMs should develop a greater understanding of the support necessary for small firms.
1998	Perkins and Gunasekaran	Single case	An investigation into the effectiveness of purchasing in a small company. The main recommendation was the centralisation of what was a fragmented purchasing function supported through IT.
2000	Calabresse	Interview – 25 SMEs	Provides an empirical study into the purchasing activities of 25 SMEs to the Italian Automotive Industry. Results focused on three consequential trends namely market vertical disintegration of sector, rationalisation of supply base and an evolution of buyer supplier relationships
2000	Quayle	Survey – 400 Suffolk SMEs, 232 responses	Research is to establish awareness of effective purchasing and the priority accorded to purchasing in SMEs. Results confirmed that purchasing, subcontracting and supplier development were given low priority. Customers were perceived as having high focus on quality, price and reliability. Similarly high focus was placed on price and quality from suppliers. A key recommendation was the establishment of purchasing consortia.
2000	Quayle	Literature review & 10 cases	Gives an overview of the supplier development and supplier association literature. Develops a step / stage process for SMEs to achieve a network development model. Concludes that small firms ignore strategic procurement and supplier development.
2001	Quayle	Survey – 480 Welsh SMEs, 288 responses	Seeks to identify the adaptation of supply Chain Management techniques and the relationships between customers and small suppliers. The results confirmed a lack of effective adaptation from traditional adversarial relationships to the modern collaborative 'e' – supply chain model. Customers were advised as pressing product-based issues such as quality price and reliability that were also evident with the suppliers. Supply chain management strategies were missing from SMEs business plans not surprisingly issues such as supplier development and e commerce was both considered of low importance. Concluded that the rationalisation of the supply base as part of strategic supply chain management may not be as important as it is currently perceived to be. Recommendation was SMEs to use e commerce as a business tool and perhaps to facilitate small firms consortia.
2004	Mudambi, Schrunder et al. 2004 et al.	Survey – 621 with a 25% response & 24 in depth interviews	Identifies evidence of advanced purchasing practice. In doing so they take attributes of co-operative relationships from mainstream literature. Of the 25% response rate only 24 were deemed to have 'advanced purchasing strategies'. The authors identified three distinct groups namely those with a deliberate strategy, those with an emergent strategy and finally those with close yet still adversarial
2004	Morrissey and Pittaway	In depth interview with 6 SMEs	Analyses the buyer-supplier relationships from the perspective of the SME emphasising the lack of homogeneity of size, resources, motives etc of actors in the supply chain bringing into question the validity of current literature. Key findings included a rejection of purchasing consortia, partnership concept treated with scepticism, and the influence of non-financial issues in the decision making process. Conclude that current purchasing models do not make sense when applied to SMEs in particular they lack complexity, suggesting that they need to be revised and grounded in actual procurement behaviour taking into account the heterogeneity, underlying motives and objectives pursued by SMEs.



**TABLE 2**  
**Description of the Companies Interviewed**

<u>Company</u>	<u>Established</u>	<u>No of Employees</u>	<u>Turnover</u>	<u>CEO</u>	<u>Purchasing Manager</u>
A	1978	74	£4 million	Owner	No
B	1968	40	£1 million	Owner	No
C	1974	80	£3.5 million	Manager	Yes
D (x2int)	1978	40	£1.7 million	Owner	Part dedicated
E	1981	20	£700K	Owner	No
F	1942	17	£800K	Owner	No

**TABLE 3**  
**Description of the Survey Respondents**

		<u>Survey 1</u>	<u>Survey 2</u>
<u>Survey Details</u>	Sample	4000	122
	Response	53	80
<u>Industry Sector</u>	Manufacturing	34%	61%
	Distribution	13%	32%
	Service	40%	3%
	Other	13%	4%
<u>Size of Firm</u>	Micro (0-10)	36%	28%
	Small (11-50)	47%	38%
	Medium (51-250)	13%	28%

**TABLE 4**  
**The Drivers of Customer Relationships**

<b>Survey 1</b>					
Most Customer Contact2		Customer Relationships - Price	Customer Relationships - Quality	Customer Relationships - Reliability	Customer Relationships - Technical Support
MD (23)	Mean	1.70	1.74	2.21	3.48
	Std. Deviation	1.11	.81	1.00	1.08
Sales (19)	Mean	2.16	1.42	2.21	3.37
	Std. Deviation	1.17	.84	1.03	1.12
<b>Survey 2</b>					
Most Customer Contact2		Customer Relationships - Price	Customer Relationships - Quality	Customer Relationships - Reliability	Customer Relationships - Technical Support
MD (25)	Mean	1.89	1.86	1.79	3.14
	Std. Deviation	1.07	1.11	.92	1.38
Sales (40)	Mean	1.89	2.13	1.87	3.44
	Std. Deviation	1.03	.92	.82	1.03

**TABLE 5**  
**The Drivers of Supplier Relationships**

<b>Survey 1</b>					
Major Contact (Purchasing)		Supplier Relationships - Price	Supplier Relationships - Quality	Supplier Relationships - Reliability	Supplier Relationships - Technical support
MD/Owner (30)	Mean	1.97	1.47	2.33	3.16
	Std. Deviation	1.16	.73	.88	1.23
Purchasing (10)	Mean	2.50	1.70	2.30	3.50
	Std. Deviation	1.18	.95	.82	.85
<b>Survey 2</b>					
Major Contact (Purchasing)		Supplier Relationships - Price	Supplier Relationships - Quality	Supplier Relationships - Reliability	Supplier Relationships - Technical support
MD/Owner (35)	Mean	1.56	1.83	2.25	3.28
	Std. Deviation	.77	.94	.84	1.21
Purchasing (24)	Mean	2.08	1.79	1.96	3.54
	Std. Deviation	1.02	.88	.69	.88

**TABLE 6**  
**The Importance of Trust in Customer-Supplier Relationships**

<b>Survey 1</b>					
	<u>N</u>	<u>Minimum</u>	<u>Maximum</u>	<u>Mean</u>	<u>Std. Deviation</u>
Best Customer Relationships built on Trust	53	1.00	5.00	4.00	1.32
Worth Investing Time and Effort in Customer Relationships	53	1.00	5.00	3.94	1.38
Best Supplier Relationships built on Trust	53	1.00	5.00	3.87	1.30
Worth Investing Time and Effort in Supplier Relationships	53	1.00	5.00	3.83	1.25
<b>Survey 2</b>					
	<u>N</u>	<u>Minimum</u>	<u>Maximum</u>	<u>Mean</u>	<u>Std. Deviation</u>
Best Customer Relationships built on Trust	79	1.00	5.00	3.98	1.33
Worth Investing Time and Effort in Customer Relationships	79	1.00	5.00	3.87	1.44
Best Supplier Relationships built on Trust	79	1.00	5.00	3.89	1.23
Worth Investing Time and Effort in Supplier Relationships	79	1.00	5.00	3.86	1.25

**TABLE 7**  
**Key Attributes in Customer Relationships**

	Survey 1			Survey 2			Overall	
	N	Mean	Std. Deviation	N	Mean	Std. Deviation	Mean Both Surveys	Rank
Honoring Agreements	53	4.23	1.34	71	4.62	.66	4.43	1
Honesty	53	4.25	1.27	71	4.56	.69	4.41	2
Openness	53	4.17	1.28	71	4.32	.84	4.25	3
Words Backed by Action	53	3.92	1.38	71	4.38	.78	4.15	4
Attitude	53	3.93	1.44	71	4.35	.83	4.14	5
Loyalty	53	3.94	1.41	71	4.31	.82	4.13	6
On Time Payments	53	3.85	1.32	71	4.23	.94	4.04	7
Being Kept Informed	53	3.83	1.24	71	4.18	.96	4.01	8
Attitude of Customer Staff	53	3.81	1.32	71	4.06	1.00	3.94	9
Fairness in Negotiations	53	3.72	1.35	71	4.13	.86	3.93	10
Confidence in Personnel	53	3.77	1.34	71	3.97	.88	3.87	11
Receptive to ideas	53	3.62	1.40	71	3.89	1.02	3.76	12
Mutual Advantage	53	3.47	1.38	71	3.87	1.02	3.67	13
Early Involvement in Projects	53	3.42	1.38	71	3.59	1.30	3.51	14
Long Term Contracts	53	3.21	1.35	71	3.54	1.09	3.38	15
Credit Terms	53	3.06	1.41	71	3.68	1.07	3.37	16
Price Determining Factor	53	3.11	1.31	71	3.49	1.09	3.30	17=
Price Pressure	53	3.19	1.16	71	3.41	1.04	3.30	17=
Input in New Products	53	3.15	1.46	71	2.92	1.25	3.04	19
Demand for Cost Transparency	53	2.45	1.22	71	2.68	1.14	2.57	20

<sup>1</sup> Both these models have been compared and contrasted in detail by Dubois and Pedersen (2002)