

# **Principles of Purchasing**

## **Lecture 10**

### Global sourcing

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#### **Lecture Learning outcomes**

At the end of the lecture, you will be able to:

1. Explain how international sourcing strategies are applied
2. Understand the risks and cost associated with global procurement
3. Understand how to evaluate and execute import procedure and documentation requirements

#### **Introduction**

In a global economy, international purchasing is a term used to describe the process of sourcing goods and services around the world to satisfy diversified needs of organization's objectives.

International purchasing emerged initially as a reactive approach designed to reduce production costs in an effort to neutralize the threat of foreign competition. Today, world class firms have shifted the focus of their international sourcing efforts to that of a proactive strategy that pursues a sustainable competitive advantage.

#### **Reasons for sourcing internationally**

- ✓ Competitiveness of overseas sources e.g. lower prices, improved deliveries, better quality etc.
- ✓ Need for manufacturing flexibility.
- ✓ Stringent quality standards.
- ✓ Ever changing technology.
- ✓ The buyer may prefer to buy from foreign source which offers products which have features which are not available domestically.
- ✓ Insufficient domestic capacity to meet demand to ensure continuity of suppliers owing to shortages or strikes.
- ✓ Reciprocal trading and counter trade owing to policy reasons.
- ✓ Innovation or variety of style.

#### **Successful elements in sourcing abroad**

- ✓ Top management support.
- ✓ Development of efficient communication skills and system.
- ✓ Establishment of long term relationships with overseas suppliers.
- ✓ Vast knowledge of diverse culture and opportunities across the globe.
- ✓ Good understanding of international rules under INCOTERMS.
- ✓ Knowledge of foreign business practices.
- ✓ Obtaining expert assistance.
- ✓ Use of third part logistics services.

#### **Benefits of international/global sourcing**

- ✓ Access to lower-priced goods.

- ✓ Enhanced competitive position.
- ✓ Access to higher-quality goods.
- ✓ Access to worldwide technology.
- ✓ Better delivery performance.
- ✓ Better customer service.
- ✓ Increased number of suppliers.
- ✓ Helps meet countertrade obligations.

### **Difficulties in buying abroad**

- ✓ Fluctuations in currency exchange rates.
- ✓ Knowledge of foreign business practice.
- ✓ JIT sourcing requirements.
- ✓ Finding qualified foreign sources.
- ✓ Legal difficulties in case of a dispute.
- ✓ Duty and customs regulations.
- ✓ Nationalistic attitudes and behaviour.
- ✓ Logistics support for longer supply links.
- ✓ Understanding the political environment.

### **Factors to consider when planning international purchasing**

#### **1) International risks**

These risks relate to:

- ✓ Financial factors such as currency uncertainty, financial policy uncertainty and financial effect of economic performance
- ✓ Economic factors such as performers of economic indicators etc
- ✓ Political factors such as radical changes in government composition or policies
- ✓ Operational environmental factors such as the legal structure of the country of export, the rules and procedures governing international trade.

#### **2) Logistical barriers**

Long distances mean increased transport costs and long delivery times, hampering the supplier in rendering a service.

#### **3) Customs regulations and duties**

Import duties can disrupt prepared cost estimates at very short notice; political motives in the importing country can hamper purchases on specific foreign markets etc

#### **4) Nationalism**

Local source preference is a factor that influences the development of an international purchasing policy and strategy.

### **Sources of information about overseas suppliers**

- ✓ Professional contacts: Professional contact of the purchasing staff can facilitate an evaluation of specific suppliers capability
- ✓ Trade journals: Trade journals are published regularly by different industries in various countries and provide vital information on suppliers
- ✓ Directories: Directories are good sources of information and are often printed by an organised industry in a particular country
- ✓ Trading companies: Japan frequently uses this marketing channel which provides advantages of convenience, efficiency and assurance of supply to international buyers.
- ✓ Import brokers: They offer a buying and forwarding service in exporting country and often become very knowledgeable about the products
- ✓ Internet: This is global system of inter connected computer networks that use the standard internet protocol suite (TCP/IP) to serve billions of users worldwide. It enables business people to search relevant suppliers across the globe.

In contrast to domestic purchasing, the international purchasing mode has the following characteristics (Fan, 2007):

- **Increased purchasing scope:**

Because the scope of purchasing activities extends to the global arena and they no longer just focus on the resources available in one country, they can acquire their resources from all over the world. Therefore, it is more possible for the companies to obtain their ideal resources and products with a rational cost because of the greater abundance of potential vendors.

- **Increased purchasing risk:**

Because international purchasing always involves a series purchases, companies usually buy the materials or goods on a larger scale, which requires greater monetary transactions. Larger scale transactions are exposed to greater risks due to currency fluctuations. Moreover, the cross-border transaction results in complicated procedures and processes, which exposes the company to lots of additional existing potential risks.

- **Decreased purchasing price:**

Because all possible resources from the whole world can be considered, the business can “shop around” to obtain the high-quality goods with a rational price through the mode of comparative cost.

- **The need for a systematic criterion in supplier selection:**

Because the suppliers under the international purchasing come from different parts of the world, they hold various models, standards, and cultures. Hence, it is very significant for businesses to develop systematic and standardized criteria and conditions in order to select a dependable supplier.

- **Stable purchasing channels:**

A business using global purchasing cooperates with suppliers worldwide because of the concept of supply-chain management. Therefore, the buyer and seller are developing a

relationship of strategic cooperation. Hence, this business with an international purchasing strategy forms a relatively stable purchasing channel.

## **DRIVERS OF INTERNATIONAL PURCHASING**

According to Porter's generic strategies, the competitive strategies can be divided into **low-cost strategy** and **product-differentiation strategy**. Both of these are highly related to global sourcing strategy. There is no doubt that the search for lower costs has been the greatest driver of global sourcing.

Several main driving reasons for global sourcing are concluded as follows:

- **Materials are not available domestically**

Due to reasons of geography and technology, some domestic manufacturers may be unavailable to supply specific materials. Moreover, probably they are incapable of meeting the required delivery time or supplying some materials due to their limited technical capabilities.

- **Unsatisfactory quality of domestic products**

The quality of products obtained from the domestic market may not meet the requirements of buyers. The quality of domestic goods may not be sufficient for the manufacturers to sell their products to international markets where higher standards may apply. In addition to the quality of the goods themselves, maybe the supplier cannot provide satisfactory warranties or after-sales services to the manufacturers.

- **Price**

Especially in developed countries, the materials or products supplied by domestic suppliers may be too expensive, and they can obtain the same goods with a cheaper price elsewhere around the world.

- **Technology**

Especially in developing countries, some enterprises may have no choice but to source internationally; otherwise they cannot get access to world-class levels of technology.

## **Basic Benefits of international purchasing**

According to previous research, it has shown that the initial motive of **international purchasing** is cost savings.

With the progress of globalization, product differentiation in contemporary markets is not that remarkable anymore, to some extent, which leads to a greater emphasis being placed on price competition.

However, many enterprises procure goods from **international purchasing** for other reasons

- Access to fresh research, design or specialized intellectual capital.
- Availability of new technology and capacity. Many companies source overseas because domestic suppliers lack the capacity and are not making the necessary investments to stay competitive.
- Plans to sell or service locally. Some companies source locally to help break the barrier to local market entry. Or their customers have now moved manufacturing processes to that country and want to be serviced locally.
- Proximity to raw materials.
- Superior quality. Many companies praise the quality of international sourced products compared to domestic products. This is typically due to supplier investment in technology and capacity to attract global business as mentioned above.

### **Risks from international purchasing**

Finally, we can conclude that global sourcing involves the following risks:

- **Security Risks:** Many developing countries identified for low cost global sourcing are subject to political uncertainty or even internal political turmoil. That risk needs to be assessed in terms of whether your offshore supplier will be able to provide the products successfully.
- **Cost Risk:** Because of the different cultures and different time zones, there can be other hidden costs when a company adopts global sourcing. In addition, monitoring global manufacturers also means greater costs.
- **Quality Risks:** Global sourcing can lead to quality problems that, if not managed well, can damage the company's brand and result in a huge financial penalty.
- **Intellectual Property Risk:** The proprietary knowledge regarding design, engineering, materials and other elements can be exposed to the light of day easily. So the enterprises have to take the risk of losing intellectual property.

### **IMPORT PROCEDURES**

The import procedure can be summarized into four parts as follows:

#### **Before placing the order for the goods**

- i. Ensure you have a trade license
- ii. Ensure you have an import license, if required
- iii. If it is food, drugs or chemical substance obtain permit, where necessary
- iv. For agricultural products

- obtain plant import permit
  - establish the phytosanitary requirements
- v. Establish the Kenyan standard for the product you are importing
- vi. Determine the goods you need to import in respect of
- Description
  - Quality
  - Specifications
  - Quantity
- vii. Send out information to the identified supplier clearly stating the following:
- Description of the goods
  - Technical specifications
  - Quantity
  - Price
  - Delivery period
  - Regulatory requirements e.g quality standards, health and safety standards
- viii. Check to ensure that the goods are not prohibited or restricted from importation
- ix. Check to determine whether the goods are exempted from duty
- x. Check to determine whether the goods attract countervailing and/or anti-dumping duties
- xi. Determine the cost of the goods to be imported
- xii. Organize for funding either internally or externally
- xiii. Consult your bank and obtain advice on how to deal with the supplier

### **Ordering the goods**

- i. Discuss with the selected supplier and agree on terms and enter into a contract
- ii. Advise your supplier on the bank you will use
- iii. Make payment arrangements according to the contract

### **Before Goods Arrive**

- i) Obtain the documents that your bank requires. Normally they will be:

- i. Commercial invoice
  - ii. Packing list
  - iii. Bill of lading/Airway bill
  - iv. Certificate of conformity
- ii) Appoint a clearing agent. The clearing agent assists the importer to clear all the customs duty on behalf of the importer.
  - iii) The clearing agent computes customs duty, port charges and transport charges required and advises you.
  - iv) The clearing agent makes arrangement for transport of the goods to your premises
  - v) The clearing agent prepares the customs declaration entry electronically, pays duty at the bank and lodges the supporting documents with Customs
  - vi) Ensure the relevant quality certificates for the goods are available.
  - vii) The Clearing agent clears with the Port Health Office,

### **Once Goods Arrive**

- i. Customs processes the documents
- ii. Release order is issued
- iii. Authentication of relevant compliance certificates and release of goods
- iv. Port charges are paid and goods are released to importer or clearing agent
- v. Goods are collected and transported
- vi. Goods are received at your premises

### **IMPORT DOCUMENTATION**

A typical import clearing transaction requires the following documents:

- i. Supplier's invoice

The supplier will provide the importer with the invoice for the goods sold to you. The invoice provides the details of the goods such as description of the goods, price and quantity.

- ii. Packing list

Packing list provides the details of the contents of a particular package. It is also provided by the supplier.

### iii. Bill of lading / airway bill

This is the document evidencing a contract of carriage of goods between a shipper and a carrier of goods (ship or airline). The supplier will send the document to you after s/he has passed the goods onto the carrier for shipping and they have acknowledged receipt.

### iv. Import Declaration Form (IDF Form C-61)

Issued by the KRA Customs Services offices and is required for all imports. You will need to pay a processing fee of Kshs 5,000 minimum or 2.75 percent of the CIF value. The IDF is completed by the clearing agent who enters information such as the importers and exporter's names and contacts, invoice details, description and quantity of the goods.

### v. Declaration of customs value (Form C- 52)

Issued by the Customs Services Department. As an importer, you are required to complete it and sign it to show that you have declared the true and accurate value of the imported goods.

### vi. Certificates of compliance

This is processed as required by the different authorities such as KEBS. Examples include certificate of conformity, certificate of analysis and phytosanitary certificate. These are issued by the competent authorities in the supplier's country after inspecting the goods. The supplier will then send you the relevant certificate to show that the goods comply with the local requirements.

### vii. Release Order

Release order is issued by the port authority. This document allows the goods to be released to you or to your agent's custody after verification and payment of the storage and other charges that may have accrued.

## **IMPORT COSTS**

There are several costs incurred while importing goods into the country. These may include;

#### i) Purchase price

This is the cost incurred on purchase of the goods. It is the cost indicated by the purchase invoice.

#### ii) Freight

This is the cost of transporting goods from the place of origin to the port or place of destination.

#### iii) Insurance

This is the cost of insuring the goods while on transit to the importer. Most of the time is paid by the supplier.

iv) Customs duty and taxes

This refers to the tariffs paid to the revenue authority while importing goods. ie custom duty

v) Port charges

viii) Local transport

ix) Clearing agent fee

## **Conclusion**

In conclusion, international purchasing has evolved from a reactive cost-cutting tool into a proactive strategy for gaining a competitive edge. Companies source globally due to benefits like cost savings, access to advanced technology, and product variety. Effective international purchasing relies on top management support, efficient communication, and solid supplier relationships, though challenges include exchange rate volatility, legal complexities, and logistical barriers. To mitigate risks such as political instability and quality issues, firms must follow systematic supplier selection and comply with import procedures and documentation requirements. With thoughtful planning, international purchasing can foster innovation, cost efficiency, and market expansion.

## **Revision questions**

1. Define international purchasing and explain how its strategic importance has evolved in a global economy.
2. Identify and discuss three primary reasons organizations choose to source internationally. Give examples for each reason.
3. What are the main risks associated with international purchasing, and how can companies mitigate these risks?
4. Outline the basic import procedures before ordering, during ordering, and after goods arrive, highlighting the importance of each step.
5. Explain the types of documentation required in a typical import clearing transaction and their significance in the import process.