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Investigating the antecedents and outcomes of customer firm transaction cost savings in a supply chain relationship

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Abstract

Cost reduction has become a preeminent goal for businesses. Since firms spend a significant portion of their annual revenues on the acquisition of an array of goods and services from suppliers, organizational procurement has been identified as an area holding tremendous potential for the removal of nonvalue-adding costs. This effort examines how a vendor's order management cycle performance and trust can affect a customer firm's transaction costs, which in turn, affect such customer-related outcomes as customer satisfaction and future purchase intentions. The results are theoretically meaningful as they address gaps identified in previous writings and pragmatically useful as they offer managers practical insight into important bases for securing a competitive advantage.

Keywords: Order management cycle performance; Transaction costs; Trust; Customer satisfaction; Future intentions; Buyer–supplier relationships

1. Introduction

Cost reduction has become a preeminent goal for businesses (Denison, 2003). As a result, firms are "seeking ways to minimize overhead costs, to eliminate intermediate production steps, to reduce transaction and other "friction" costs, and to optimize business processes across functional and organizational boundaries" (Treacy and Wiersma, 1993, p. 85). Since 30–70% of a firm's annual revenues are expended on acquiring an array of goods and services (Killen and Kamauff, 1995), firms are pursuing such initiatives as enterprise resource planning (Trent and Monczka, 1998), just-in-time sourcing (Frazier et al., 1988), electronic catalogs (Pierson, 2002), reverse auctions (Jap, 2002), and global sourcing (Venkatraman, 2004) in an attempt to remove nonvalue-adding costs from the in-bound supply chain.

While research in marketing has been preoccupied with investigating factors that can affect top-line revenues, relatively little attention has been devoted to understanding how managing the middle line (i.e., cost of goods sold) can also contribute to driving the bottom line. Since reducing costs in the inbound supply chain is yet another means to enhance cash flows (Srivastava et al., 1999), this research examines issues pertaining to customer firm transaction costs within an industrial purchasing context. More specifically, the main research questions investigated include: (1) what factors can influence customer firm transaction cost savings in a buyer–supplier relationship? and (2) what is the effect of customer firm transaction cost advantage on customer satisfaction and future purchase intentions?

The answers to these questions are important for both theory and practice. Regarding the former, academics have called for examination into the factors affecting firm transaction costs (Rindfleisch and Heide, 1997; Dahlstrom and Nygaard, 1999) as well as into the relationship between customer firm transaction costs and future intentions (Cannon and Homburg, 2001). This article extends current marketing knowledge by taking a novel approach to explore

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how a seller's performance along the order management cycle as well as trust can influence customer firm transaction costs, which in turn, affect such customer-related outcomes as customer satisfaction and future purchase intentions. Given that firms devote significant resources to procurement and that transaction costs often exceed actual invoice costs (Noordewier et al., 1990), this research also provides managers with insight into the factors that can introduce nonvalue-added costs into their firm's procurement activity.

2. Conceptual framework and hypotheses

The theoretical model that guides this research appears in Fig. 1. Since the organizational buying literature stresses the importance of identifying the *key buying criteria* that a customer firm uses to select and evaluate vendors (Lehmann and O'Shaughnessy, 1974, 1982; Wilson, 1994), the ensuing discussion commences with a description of order management cycle performance and then elaborates upon the hypothesized theoretical relationships depicted below.

2.1. Order Management Cycle (OMC)

As products offered by industrial suppliers become increasingly commoditized, some authors prescribe that selling firms ought to take a more holistic view of their need-satisfying offering, and look to the "augmented" product as a means of differentiation (Corey, 1975; Levitt, 1980; Rangan and Bowman, 1992). Shapiro et al. (1992) advance that one means by which to move beyond the product is to explore the "order management cycle" (OMC), which refers to the critical activity sequence that a customer order follows from the time that the customer firm has placed an order through post-sales assistance.

Drawing upon the OMC, we view the supplier's order fulfillment, billing, and post-sales service as constituting the critical operational factors. These include: order cycle time, accuracy in filling orders, accuracy in billing processes, on-time delivery performance, ability to fill emergency orders, condition of products on arrival, and post-sales assistance (e.g., installation, training, and complaint resolution). These operational factors are tangible and measurable criteria for which metrics can be established for improving performance (Day, 1994). Given the ability of the OMC to impact critical operational metrics, Shapiro et al. (1992) advance that "focusing on the OMC offers managers the greatest opportunity to improve overall operations and create new competitive advantages" (p. 113).

2.2. Trust

Social Exchange Theory (SET) suggests that a firm will remain in an exchange as long as the benefits provided by a vendor outweigh those provided by alternative sources (Thibaut and Kelley, 1959; Frazier, 1983). SET predicts that if a vendor can outperform the others in a buying firm's consideration set, the buying firm is more likely to develop a favorable attitude towards the vendor. In the context of a supply chain relationship, a vendor's superior OMC performance over other vendors may lead to trust, which is a favorable attitude that exists "when one party has confidence in an exchange partner's reliability and integrity" (Morgan and Hunt, 1994, p. 23).

In fact, how trust emanates from a supplier's OMC performance can be explained well by how recurrent transactions allow the firm to gain confidence in the vendor. For one, a vendor that has been able to repeatedly meet the buyer's requirements along the OMC will be perceived as one that has delivered on its promises, both implicit and explicit. Since past research has demonstrated that a vendor will be deemed a reliable exchange partner if it is capable of demonstrating technical competence (Moorman et al., 1993; Narayandas and Rangan, 2004), it can be argued that a vendor that delivers products on time and in good condition, provides invoices that are accurate, and is able to reconcile issues through its post-sales assistance activity will be able to convey its reliability along the OMC. Second, the customer firm will be able to develop a better sense of its exchange partner's motives over recurrent transactions. Through these repeated interactions, the buyer will be able to secure the additional data points needed to more accurately discern the exchange partner's goals and objectives, and assess the vendor's likelihood of behaving opportunistically (Williamson, 1985; Doney and Cannon, 1997). Since it is difficult to know a priori which suppliers are trustworthy and which are not without direct, first-hand experience (Barney, 1990), the buying organization is likely to rely on its evaluation of the historical performance of its vendor along the OMC. This performance-based evaluation will enable the customer firm to gauge the vendor's

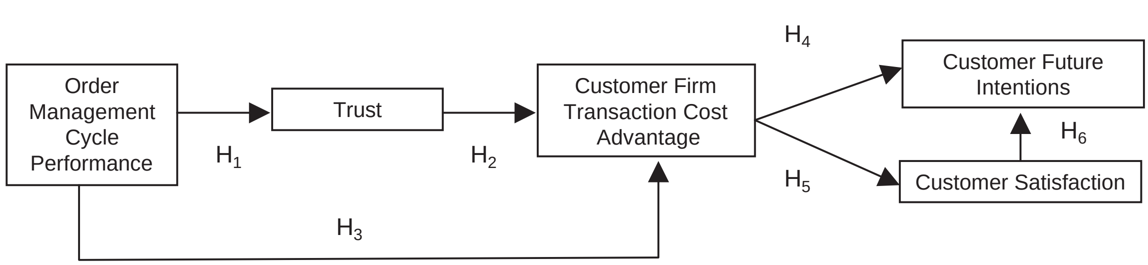

Fig. 1. Theoretical model.