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Chapter 20
Relationship Establishment in SCM in a Market with Enforcement and Regulation Challenges:
Case of Tanzania

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ABSTRACT

In absence of effective state institutions, informal and private sector operations tend to govern the market. This problem is evident in the petroleum industry in Tanzania. However, little is known about how players in petroleum industry operate in those business environments. The purpose of this chapter is to explore establishment of a relationship between supplier-logistic firms in a post planned economy. The study employed case study interview with two petroleum products distributors in Tanzania to achieve its objective. Data were analyzed by thematic analytical techniques. Three major findings regarding buyer-suppliers relationships in developing economies are presented: actors do not prefer to enforce contract that they sign, discretional relationships exist in petroleum business among actors and 'undugunization' is the strongest criteria in selection of actors. Study implies that for a supplier-logistic relationship to exist government has a great role to play in enforcement of laws.

INTRODUCTION

Since 2000 when the petroleum business was liberalized in Tanzania, competition has increased upstream and downstream (Ernst & Young, 2013). It is estimated that there are 60 petroleum distributing companies and 1,074 retailing filling stations in the country. Most retailing filling stations are independently owned. This fact reduces the ability of distributors to dictate petroleum business in the country. Demand

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for total fuel consumption increased in Tanzania for 10 per cent from 2.6 billion litres in 2013 to 2.9 in 2014 (The Guardian, 2014). On the other hand, downstream petroleum and related product business became more competitive by more filling stations to be free to buy from any distributors. Which mean distributors have to improve their services to maintain and attract new customers (Ernst & Young, 2013).

Previous studies of supplier-retailer relationship in Africa focused on satisfaction of channel members (Bonsu & Sigue, 2012), the effects of conflicts on supplier-retailer relationship in brewery industry in Cameroon (Biboum & Sigue, 2014), the lack of trust and its effects on supplier-retailer relationship in Uganda (Ahimbisibwe, 2014). Furthermore, these studies employed quantitative analytical techniques. With the emergence of the private sector in Africa, it is very important to understand how distributors operate in the fragile yet growing business environment on the continent. Kuada (2008) studied the effects of power on establishment of the relationship in Ghana between local and foreign companies. He found that local companies, due to lack of power, have no chance to influence on the clauses of contracts which results in greater potential losses to them. Another study by Boampong (2009) examined how Ghana's exporters operate in market imperfections. The current study is on local actors and how they establish relationship.

Deshpande (1983) argues that for new phenomena qualitative measures are encouraged in order to understand various dimensions that prevail in business. Because this is a new phenomenon in most of African countries, and in particular Tanzania, the use of qualitative method is very appropriate to understand how actors select other players. In Tanzania studies on the fuel value chain focused on competition and price margin (Ernst & Young, 2013). Another study identified that native entrepreneurs in Tanzania were not trustworthy and committed to contracts (Stein, 2004). However, this study focused on the role of networks and business success.

Given the lucrative nature of the industry and the opportunities for cheating, it is very important to investigate how actors in value chain operate in this kind of environment in fuel sector. Furthermore, most of these studies were commissioned jobs by government agencies for instance Ernst and Young (2013) which reduce credibility of the influence of the third party on the reports. Despite the importance of the petroleum sector in the Tanzania's economy, most of previous value chain studies conducted in the country focused on agriculture commodities supply chain, neglecting the petroleum industry. Additionally, existing studies heavily relied on Gereffi et al's (2005) governance perspective supply chain. This chapter intends to fill that gap by examining the petroleum sector by using relational perspective of Supply Chain Management (SCM) as proposed by Dyer and Singh (1998). The marketing relationship with perspectives of distributors is explored. In particular, this chapter intends to answer the following questions:

- How actors establish relationships in petroleum retailing industry in Tanzania?
- What criteria do they use to choose a logistic firm?
- How long do these relationships last?

Since the emergence of the private sector in mid-1985 in Tanzania, private firms have been prominent for importing and retailing of petroleum products. Some companies acted as suppliers with retailing filling stations and others concentrated on importations as suppliers alone. The distribution of petroleum products involves partnerships between retailing firms and logistic companies.

RELATIONSHIP, TRANSACTION COST ANALYSIS, AND NETWORK THEORY

The past two decades have witnessed a significant paradigm shift of modern business management from competition between individual businesses to competition between network of businesses and relationships, for the purpose of creating sustained competitive advantage (Dyer & Singh, 1998; Lambert & Cooper, 2000). This paradigms shift is an international one that is also evident in Tanzania and Africa. As firms seek to establish efficient business relationships and networks, Reutterer and Kotzab (2000) put forward that relationship establishment is an interplay of certain variables such as: 1) concentration of the core activities of the business; 2) consolidation of supply chain activities to realize economies of scale; 3) integration of all supply chain activities by using the same organizational and information technology (IT) standards at every echelon in the system; and 4) performance measurement to achieve better service levels and lower costs. According to Dyer and Singh (1998), business relationships and networks allow firms to procure assets, competences, or capabilities not readily available in competitive factor markets, particularly specialized expertise and intangible assets, such as reputation.

While Collins and Burt (2006) contend that any business relationship provides reduced excess costs, increased flexibility, reduced uncertainty and/or improved profitability by increasing sales and gross margins, and developing the right type of business relationships which is very challenging for supply chain partners which are associated with several challenges. These can include cheating, lack of mutual goals and expectations, and lack of proper basis for determining which members are critical to the success of the company and the supply chain (Arshinder, 2011; Lambert, 2008). We agree with the previous research that, the success or failure of any business relationship is based on: incentive design (i.e., how resources, risks and reward are shared between firms) (Wathne & Heide, 2004); trust (i.e., willingness to rely on an exchange partner in whom one has confidence) (Schulze, 2006); commitment (i.e., the desire by a party to a business relationship to maintain and strengthen that relationship) (Subramani, 2003); information and knowledge sharing (Sheu, 2006); institutional forces (i.e., certain external circumstances that influence formation and functioning of business relationship) (Kotelnikova, 2013) and the extent to which compatibility of organizational culture, value and beliefs between firms exist (Tepic, Omta, Trienekens, & Fortuin, 2011).

However, in this chapter, we use a broader definition of relational perspective as proposed by Dyer and Singh (1998) because it provides us with an increased understanding of critical factors contributing to relationship establishments. The authors propose two classes of relationship establishments: third-party enforced of agreements (e.g., legal contracts), and self-enforced agreements in which ‘no third party intervenes to determine whether a violation has taken place’. Relationships based on transaction cost analysis fall primarily within the first class as they suggest that relationship establishments and dispute resolution requires access to a third party enforcer, whether it be the state (e.g., through contracts) or legitimate organization authority. In contrast, self-enforcing agreements involve safeguards that allow for self-enforcement.

EMPIRICAL LITERATURE REVIEWS

Previous studies in value chain activities of actors have yielded three major perspectives of the concept which are governance, relational, and structural (Hoenen & Omta, 2012). This study focus on relational governance which emerges from values and agreed processes generated through interactions and exchanges in social relationships (Granoveter, 1985). The emergence of such relationship depends greatly on how actors in the value perceive each other. The focus and interest of each actor is to benefit each member in the future through their actions over time. Zenger et al., (2002) emphasized that relational governance involves rules based on implicit understanding which are usually socially derived and, therefore, not immediately accessible through written documents or sanctions through a formal positions.

A key concept in the relational view of governance is trust (Fortuin *et al*., 2011; Dwyer et al., 1987). Furthermore, Dwyer et al., (1987) argue that trust is a new concept that was introduced in the buyer-seller relationship. Trust involves confidence or positive expectation about another's behavior and willingness to expose oneself to vulnerability under conditions of risk and interdependence (Bhattacharya, et al., 1998; Das & Teng, 1998; Schurr, & Ozane, 1985). Lack of trust suggests that most traders do not invest much in social relationships with the expectation of long term benefit. Heide and John (1992) identified three dimensions inherent in inter-firm relations: flexibility or willingness to make adaptations, proactive information exchange, and solidarity or high value placed on the relationship. Information exchange is very important for buyer-seller relationships because through this exchange each part will be aware of the business environments as well as having information on the reputations of other's actors in the chain. This suggests that social capital is most influential in the decision to engage in business or not.

Dwyer et al., (1987) noted the higher the information flow the more aware actors become. Hence, information flow can influence relationship development among actors. However, flow of information in many African countries is very low making it difficult for it to be a factor in decision making. Therefore, information asymmetry induced actors in the chain to decisions of their means to survive in this business environment. Furthermore, most value chain actors are not members of any business association and thereby do not have access to the greater range of information that business associations could provide. Whether this lack of membership in business associations is due to the absence of business association or negligence of actors themselves still handicaps the value chain actors.

In these business environments, contractual agreements between actors are important for protecting the rights of individuals in the value chain. Some of the challenges facing petroleum industry and particularly in Tanzania are petroleum adulteration and payment delay. Structural perspectives presume that the efficacy of inter-organizational cooperation is highly influenced by the initial design of the cooperative arrangement (Poppo & Zenger, 2002; Williamson, 1985). This assumption promotes the designing and formalization of buying procedures among actors and in most cases signing of contract is preferred. Contractual formalization involves externally (i.e., legally) enforceable contract, while extra-contractual agreements such as job descriptions, rules and procedures, are internally enforceable documents (Grandori & Furlotti, 2010).

However, previous study conducted in Ghana indicates that actors in the value chain do not prefer to sign contracts and enforcement of it (Amoako & Lyon, 2014). This influenced many factors such as uncertainty which caused a lack of supply and delayed justice in most of courts in African countries. Rational commitment is one of the very important factors which are based on the interest based reasoning of the structural perspective (Fortuin *et al*., 2011). The concept assumes that an individual would prefer to invest in a particular relationship with expectation to be rewarded in future. Furthermore, the relational commitment is not documented or formalized.

METHODOLOGY

Data were collected from two leading petroleum distributing companies: Tanzania Oil Company Limited (Oil Com) and Camel Oil Company (Camel). As indicated in Table 1, both companies control 17 per cent of the market share. The selection of the case is very important for the case study method (Gibbert, et al., 2008). The selection was based on the companies found in top ten lists of best performers, must be a distributor of petroleum products, and must be owned by indigenous entrepreneurs over 50%. These companies were found in the commercial city of Dar-Es-Salaam and they are owned by indigenous entrepreneurs. Originally, five companies were selected by researchers to participate in the study based on their performance as Table 1 shows, but three distributors declined the invitation to participate. Researchers visited the head offices of the two accepted companies by introducing themselves and explaining the purpose of the study.

Flyvberg (2006) argues that to use multiple cases or single case depends on the problem at hand and the circumstances. The petroleum business has been largely secret due to its importance, so there is strong control on price and measurements by government agencies. This situation limits most distributors to participate in open conversations such as research. For convenience, the contact person was asked for his or her easiest means of communication which was by mobile phone in most cases. After a telephone follow up for the selected contact person in each of the companies, three respondents declined our invitation with the reasons such as they are preoccupied; hence, they could not participate in the study. Interviews were conducted at the participants' offices and took an average of one hour. Respondents were comprised of general marketing manager, supplies manager and petroleum marketing consultant. All of the respondents from participated companies were male.

Respondents had working experience of an average of 15 years in the petroleum industry with different countries including Kenya, Uganda, South Africa, and India. Two researchers participated in the interview. One had guided the interview and the other was the scribe, taking notes during the interview. For data collection during interviews, participants were asked for their permission for researchers to use tape recorder and their willingness to accept the use of it during data collection. Both Kiswahili and English languages were used during the interviews.

Table 1. Petroleum and related product market share in 2013 (in %)

Name of the Company	2012	2013
Puma	12.2	12.7
ORXY	11.1	11.5
Oil Com	05.9	11.5
Gapco	12.1	08.6
Total	7.5	7.3
Mogas	5.1	6.6
Camel	6.3	5.5
Engen	5.3	5.5
Others	34.5	30.8
Total	100	100

Source: Ernst and Young, (2013)

Semi-structured questions were used to allow researchers to inquire about related issues for various important dimensions of the study. On-going questions and provocative questions were employed also implemented. Agee (2009) argues that ongoing qualitative research questions are very important to understanding unfold part and perspective of others. A thematic analysis technique was used for data analysis. Braun and Clarke (2006) argue that thematic analysis is flexible in that it can allow changes while the research is in process. The technique allows researcher to set dimensions and identify patterns emerge in the documents.

Attride-Stirling (2001) argues that for the thematic analysis to be of meaningful, it is of important to define and elaborate the means of connections between dimensions. Dimensions which were established based on the previous discussions of the theories and empirical findings included: trust and commitment (reputations, payment period, fulfillment of promises, signing of contract, period of relationship), social and network (family members, where do they meet, frequency of meeting or telephone call). Data were transcribed and manually codded for identifications of emerged patterns. Basit (2003) defines codes or categories as labels assigned to the units of words to allocate a particular meaning from gathered data. Furthermore, data were corroborated with newspapers reports and research reports.

FINDINGS

Criteria for Selection of a Partner

One of the crucial issues in the supply chain is the selection of a partner either downstream or upstream. Empirical evidence shows that each partner has a great role to play in the success of other members. However, in practice most actors are opportunistic resulting in a decline in profit for the affected members; hence, deterioration of the trust in most cases. A major challenge in developing economies is the enforcement of laws. As a result, actors do not prefer to go to court to settle disputes; instead, they use some activities or techniques to reduce anticipated problems. Therefore, selection of the partner in the value chain is very important.

Respondents were asked how they choose a partner. In general, this study indicates that partners are selected based on presentation of legal certificates such as business license, physical address of the company and long term relationship. Furthermore, this study identified that ‘undugunization’ is very important elements for a company to be selected. *Undugunization* is a blending of Swahili and English word whereby ‘Undugu’ can be translated as relative or next of kin. ‘Undugunization’ is similar with ‘guanxi’ in the Chinese business environment, but the difference is in the parameters that form each other. While ‘Guanxi’ is formed by the characters that depict pride, respect and trust, ‘undugunization’ characterized with ‘respect, family relationship, and trust’. Pride is not part of that. One of the participants said:

To minimize risk some time we choose people whom we know to work with such as next of kin.

Previous study by Alan *et al*., (2009) on entrepreneurship and gender found a network is likely to be established among next of kin entrepreneurs in Tanzania. In some cases there were specific skills that were considered important. For example, the ability of a carrier to transport huge quantities of a products is a criteria used for the selection of a logistic firm. Reputation of the firm also emerged to be a strong factor as well. In these cases, the interest is in legality of the company such as certifications, and the bank's recently financial position.

We ask for certifications such as trucks registrations and insurance certificates. We also cross if the company has a good record in paying its employees especially drivers.

Governance Formalization

Interview data show there there is mix of conduct among actors in the petroleum value chain in Tanzania. First, distributors are used both as system contracts and no contract to operate in the oil business. However, contract signing has been the most preferred for a long time.

Petroleum business is business that involves huge sum of money just on one truck. Therefore when we rare engaging in a deal that assumes more than four Lories for one company we would like to have contract with a buyer.

The agreements between actors are on delivery, quality, and price and payment mode. When further asked if they enforce contract once there is a breach, both indicated they are not in favor of court divisions for their business operations.

We don't prefer to settle our problems in court. Because once you are attending court hearings that is the end of your future business and for us we like to have long time relationship with our buyers.

Because resolution of conflicts in a court of law is limited by delays in court decisions which, in turn, affects business operations, most trade partners prefer to settle their problems out of court. Similar findings by Amoako and Lyon (2014) for the Ghana's entrepreneurs deal with foreign business. Mkandawire (2009) referred to this as the focus of institutions to 'stabilize' business environments with less interest on 'development'.

Contract Signing

Most firms tend to reduce risks associated with working with untrustworthy logistic firms by signing a contract. However, it has been observed that for less complex business decisions, distributors do not sign contracts with the logistic firms, preferring instead to work with a company with which it has had an extended relationship. Similar to the findings by Stein (2004), the current study finds lack of trust and commitment among actors in the petroleum value chain in Tanzania. Trust, one of the important dimensions in business, is evident when parts fulfill their promises and continue doing business for a long time and solve their problem outside the court room. Participants said:

Retailers don't pay us on time. This causes problems with our partners such as logistic firms. Therefore, if we have a long term relationship with retailers and we know it for sure with the previous history he will pay. The company can pay a logistic firm in advance to secure the relationship.

Enforcement of Contracts

One of the challenges in suppliers-retailers relationship is problem of enforcement of law when the contract has been breached. However, our findings suggest that suppliers do not prefer to take their problems to court as mentioned earlier. This is very interesting because the theory of power indicates that they can exercise their power to punish or even threatening companies that breach the contract (Kuada, 2008). When asked why the other party does not abide by the contract as stipulated, managers who were interviewed explained three major reasons:

One possibility of any of your enemy to be your best allies is high. Therefore, in most cases actors don't prefer to solve their problem by presenting their matter to the court of law. The other reason is delay of judgment, that company has to use its scarce resources on follow-up of the court decisions and during the time possibly most of the fund can be frozen by the decision of the court. When funds are frozen a particular firm is one that is facing challenges if faced with budget constraints. The last reason seems to be human and on the fact that most of the employees expected at any time to join one of the companies, this results in not enforcing the contract.

However, we suspect that an important factor is that actors in the petroleum value chain choose their relatives as we have seen in the issue of 'undugunaization'. It is likely that when problems occur, neither of the parties would like to cause trouble because they will potentially be disruptive at the family level. Thus, there are strong family values that limit parties taking matters to court when a contract is breached. Furthermore, this suggests that Tanzania's business environment is changing faster than the country's policies. The finding is similar with previous findings by Nkya (2002), Ferrali, (2012) on the mismatch between policy reforms and entrepreneurial spirits in Africa.

CONCLUSION

Most African countries are witnessing the growth of transport sector which accelerates the growth of petroleum business on the continent. One of the major challenges faced by the petroleum sector is development of positive relationship between actors in the value chain. Currently, the petroleum business can be characterized as a discrete relational model. MacNeil (1980) defined discrete relationships as formed of the basis of money on one side and measured by commodity on the other. As has been articulated, parties prefer not to adhere to contracts. However, the current study demonstrates that despite the form of relationships that prevail in the Tanzanian business environment as one focused primarily on material benefit, firms in the petroleum industry are trying to establish a long time relationship through franchising one by one.

The growth of the economy indicates that there is stiff competition in many sectors including petroleum retailing. For firms to survive either at downstream or upstream, collaboration with other members is very important. However, the study indicates that collaboration is facilitated by the enforcement of a particular country's laws and regulations. Future research can be conducted on outcome of the relationship among the actors with focus on the performance of key indicators such as sales, profit and margin among actors in the value chain. There are many challenges of having access to financial matters in developing countries like Tanzania where most of the companies do not have audited financial reports and few who do are not ready to share with outsiders. Maintaining proper records is also a challenge to most firms in developing countries. However, we propose a qualitative survey with questions on estimated figures as part of the questions instead of relying on them to provide figures.

Understandably the weakness of this approach is that will be highly influenced by the researchers but could lead to reduce the problem of accurate data and biasness. Further study is proposed to include other actors in the value chain such as logistic companies, government officials and business associations. Undugunization studies in Africa have contradictory findings. For example, a study in Madagascar by Minten and Fafchamps (2000) found it reduces a firm's efficiency. Hart (1988) found that kinship is very strong in enabling marginalized people in community in raising capital in African community. But more studies are needed across varied industries including services and petroleum in order to understand impact of working with next of kin (Undugunization) on firms' performance in developing economies.

Competing by collaborating with the members in the supply chain is becoming increasing necessary but, at the same time, collaboration is prone to conflicts. Hence, supply chain managers need to diagnose and understand the impact of their decisions in supply chain collaborative. Our findings provide several guidelines as to how managers can manage their relationship. First, to minimize risk of loss, managers must seek information from other actors in the value chain or work with consumers with good social capital. One way to accomplish this is to work very closely with other members who can share information on partners when necessary. Second, attention must be given to the circumstance of collaborations to avoid much loss and delay of payment from petroleum retailers. In this manner, managers can avoid loss by working companies that have a long relationship with and next of kin with some of their member of staff.

The current study has a number of weaknesses: (1) recruitment of respondents based on convenience sampling which was caused by the availability and acceptance of the participants. This caused us to have only among of the best performer and lacked information from below the line; (2) the study concentrated only with distributors which limit the ability to compare with the views of other actors in the chain such as retailers.

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