Eduvest – Journal of Universal Studies
Volume 4 Number 10, October, 2024
p- ISSN 2775-3735- e-ISSN 2775-3727

CASE STUDY OF A STATE-OWNED COMPANY: HOW DOES CENTRALIZED PROCUREMENT AFFECT OPERATIONAL RISK?

Mahardika Dwi Jayanti
Universitas Indonesia
Email: mahardika.dwi@ui.ac.id

ABSTRACT

This study aims to understand that the restructuring of the BUMN has a significant impact on the operational activities of the NUMN, along with its risks. The researchers used data saving from the procurement centralization process as an indication of the company's operational activities before and after restructuring. While variabel current risk exposure to indicate the conditions of the company's operational risk. Procurement centralization mechanisms tend to change before and after restructuring. So it gives the contractor his own sentiment about the operational risks and obstacles in the process. The data used refers to the company's monitoring report. Modeling between saving and current risk exposure uses double regression analysis. The results also indicate that changes in procurement centralization mechanisms have a significant impact on the company's operational risk. So in order to meet risk mitigation, the company should specifically regulate the mechanism of centralization of procurement between business groups.

KEYWORDS *Current Risk Exposure, Centralization of Procurement, Bussiness Group, Operational Risk.*

INTRODUCTION

The literature shows that business groups support affiliates in overcoming market failure, which is common in developing countries, thus serving as a source of competitive advantage. Min et al. (2022) compiled a study that concluded that affiliated firms perform worse in terms of organizational innovation than unaffiliated firms. In addition to organizational innovation, business groups also often have challenges in centralized procurement business processes, such as determining the right strategic commodities in Supply Chain Management (SCM). Wang et al. (2022). The two studies above explain that business groups do not

How to cite: Mahardika Dwi Jayanti (2024). Case Study of a State-Owned Company: How does Centralized Procurement affect Operational Risk?. Journal Eduvest. *4*(10): 8812-8819
E-ISSN: 2775-3727
Published by: https://greenpublisher.id/

always bring competitive advantages to companies and affiliates. Group business is also often a burden for those who lack experience.

The mechanism of restructuring SOEs into group businesses is not new. However, the approach, scale and focus of the Ministry of SOEs' restructuring this time has several aspects that distinguish it from previous efforts. Suwignjo (2022) even mentioned that the restructuring of SOEs was able to shape encourage organizational innovation and process innovation involving the introduction of goods, processes, marketing, and organization. Bing (1999) also concluded from his research that one of the most effective ways to reduce risks, especially those related to financial crises, is through joint ventures (JVs).

Globally, there are more than 2,000 state-owned enterprises (SOEs), most of which are located in countries that are members of the Organization for Economic Co-operation and Development. In addition, SOEs account for 10% of the world's largest companies in terms of market capitalization (Sánchez, 2016). In most countries, SOEs are entities that aim to provide goods and services to the market (Lienert, 2009). In the Ministry of SOEs' strategic plan for 2020 to 2024, SOEs are targeted to complete several work indicators including the establishment of SOE holding companies. Therefore, strategic steps continue to be taken by SOE companies in order to achieve the targets given by the Ministry of SOEs (Sasongko, 2024).

Gaughan (2013) states that a company may engage in horizontal integration or acquire a competitor if the integration generates synergies with the acquired company. Synergies refer to the combination of two companies that create a higher total value added than each separate company. Two common types of synergies are operational synergies and financial synergies.

Sumarna and Solikin (2018) mentioned that the concept of SOE transformation scenarios can be carried out in the form of restructuring or rearrangement; profitization or a significant increase in profits as a follow-up step to restructuring; and privatization or (releasing ownership from the state to the public. Changes in the structure of the Company as a holding company within the SOE group, as stated by Yu, Jia and Qi (2023), are expected to improve the parent company's professional ability to supervise and manage the management behavior of the subsidiaries, and show that the addition of external directors helps improve the independence of decision-making, and has a stronger effect on the supervision and management ability of the company. Directors gain decision-making power that was originally held by the government. Cai et al. (2019) even concluded that the power held by the board of directors can give the subsidiaries more opportunities to make budget management arrangements in accordance with their own development status and reduce abnormal cash storage problems due to government intervention. Restructuring helps promote management decentralization, thereby optimizing the subsidiaries. Lin (2003) mentions that an important objective of restructuring is to ensure that subsidiaries can also enjoy the rights of independent management.

Lewis (2004) wrote that in running a company, it is important to implement operational risk controls that can cause direct or indirect financial losses and lead to potential loss of opportunities for profit. In addition, operational risk control can make it easier for regulators to make assessments related to losses that can affect the capital of related entities.

Operational risk is defined as the risk of loss from inadequate internal processes, people and systems or from external events. Therefore, operational risk is related to losses stemming from various operational errors that affect the company's revenue. Operational risk can be categorized based on the stages of operational activities, which can occur during the production stage, supply chain, or even after the product is received by the consumer (Hanggraeni, 2010). The definition of operational risk can also refer to the Basel Committee on Banking Supervision (BCBS). BCBS states that operational risk is the risk of loss due to inadequate internal processes or failure of internal controls. Operational risk also comes from external events that are not always under the control of the organization. (Chorafas, 2004).

Hecht (2020) through his research said that managerial characteristics affect various company practices, including risk management. The strong position of a CEO affects risk management practices, companies are more likely to use strategies that pay attention to risk when the CEO is more mature with a certain educational degree. In addition, the relationship between CEOs who are affiliated with corporate owners also has an influence on higher derivative volumes.

Rapidly shifting economic conditions hinder the expansion of multinational enterprises (MNEs), thus forcing MNEs to create sustainable and resilient business strategies to effectively overcome external business constraints. To enhance the resilience of MNEs with global value chains (GVCs), it is important to build innovative business models (Hillmann & Guenther, 2021). MNEs can utilize global value chain (GVC) capabilities to take advantage of better financial opportunities, larger product markets, and arbitrage different opportunities (Manuj & Mentzer, 2008). Multinational corporations must have the ability to continue procedures to identify, analyze, evaluate, and appropriately handle loss exposures and monitor financial resources and expertise to prevent unforeseen and adverse consequences of such losses. Multinational companies must develop new and better business models to manage risks in such situations (Deloitte, 2021).

Risk mitigation is currently the most frequently used approach, with management decisions usually based on qualitative or even intuitive measures. Risk mitigation does not fully protect the impact of operational risks, rather management decisions must be supplemented with financial instruments such as insurance (Cruz, 2002). Consumer value is generated through three aspects: marketing, operations, and finance, which are often not generated independently by the company. Instead, companies rely on suppliers (vendors) who are able to offer a variety of needs from basic operational activities to more complex matters such as financial management services. Collectively, vendors form a supply chain, which is a global network of organizations and activities that provide goods and services to companies (Heizer, Render, & Munson 2017).

Nicoletti (2013) defines procurement as encompassing a wide range of activities designed to facilitate the transfer of a good/service product from its origin to its point of final use. Brandmeier and Rupp (2010) describe procurement as a significant financial expenditure for any entity making it imperative to consistently improve performance throughout its phases, especially in highly competitive sectors. de Araújo, Alencar and de Miranda (2017) agree that the success of the entire procurement process depends on the vendor selection phase as well as its thorough performance evaluation including during the delivery phase. However, procurement is not only about managing resources and vendors but also involves aligning internal organizational targets with external availability. This alignment is strengthened through collaborative efforts between procurement and other internal departments, which promotes efficient organizational decision-making (Pereira, 2014).

RESEARCH METHOD

Virolainen (1998) outlines that throughout the procurement phase, companies must design and maintain a strong and effective procurement strategy. There should be a distinction between administrative procurement and strategic procurement that targets broader goals within the corporation. Through technological or other innovative methods, according to Edquist and Iturriagagoitia (2012) procurement can become more efficient, transparent and faster. Unplanned procurement and unstable interactions between buyers and vendors can potentially derail procurement goals and, by extension, the organization's ongoing operations.

While Marinez and Levi (2019) revealed that the strategy that vendors can implement is modeling the cost of providing goods or services. Procurement commodity grouping plays an important role in the success of global companies. Fluctuations in commodity prices caused by global issues, such as wars, pandemics, and trade wars, pose major challenges in managing operational costs. Companies must also have risk-taking ability, resilience, and a proactive attitude that enhances the global value chain's ability to cope with challenging, unpredictable, external situations (Chatterjee, 2024). Understanding supply chain resilience is increasingly important in supply chain management. This is due to the increasing complexity of today's supply chains and the greater likelihood of disruptions (Brandon-Jones, 2014).

Risk management in the supply chain is a systematic process of identifying, analyzing and responding to risks. Such management includes maximizing the likelihood and consequences of positive events and minimizing the likelihood and consequences of adverse events with desired objectives. Supply Chain is influenced by external factors that can exert both direct and indirect influence. Among these external factors are political, economic, technological or geographical as stated by Kleindorfer and Saad (2005). While on the internal side, according to Caniato (2003), supply chain risk is influenced by problems within the organization such as errors in machinery, equipment or problems related to information technology.

Hanggraeni (2010) states that in a management aspect operations are the most important part of an organization, because operational activities are the most costly. The existence of this risk is divided into two categories, the first is the risk from suppliers where suppliers cannot be trusted or suppliers are slow, suppliers experience bankruptcy and the risk of procurement policies owned by companies purchasing from places that are too far away and using sole source (Hanggraeni, 2010).

It is not easy to escape the risks in the procurement process. If the supplier goes bankrupt, the supply stops and causes the factory to stop production so that the relationship with the supplier becomes unfavorable or to management decisions that believe in one supplier, or the supplier is far from the company. The following is a discussion of the risks associated with suppliers (Sadgrove, 2005). This study uses two data collection methods and two types of data: primary data and secondary data. Primary data came from a survey questionnaire, which was conducted on 30 respondents selected through a stratified rando sampling mechanism. Secondary data were collected from relevant departmental performance reports from January 2019 to March 2024. The study also examined literature on SOEs, management theory, and other related studies.

This study uses two types of variables: qualitative and quantitative. Qualitative variables refer to individual values or attributes, while quantitative variables are ratios or percentages. This study explores the variables to determine hypotheses about problem-solving situations. The concept of problem solving can be understood as a combination of three elements: problem structure, problem rejection, and decision making about work methods.

RESULTS AND DISCUSSION

The variables used in this study are related to the risk of business failure. Addressable expenses are defined as the cost of work that is not met by the target, and risk records are used to monitor the risk of failure. The dependent variable is used to represent the outcome of a specific task.

This research produces a conclusion in accordance with the research objectives, namely that there is an effect of restructuring on the company's operational risk. The conclusion is the result of the analysis of respondents' sentiments, where from the analysis it is known that there is a significant difference between the procurement centralization situation before and after restructuring. Similar to procurement centralization, operational risk also experienced differences before and after restructuring.

The contract value has a negative influence on current risk exposure, where the higher the contract value, identical to the potential loss value is also high. So as a mitigation, the contract is accompanied by stricter project assessment requirements and the risk owner will highlight the implementation of risk mitigation which causes the current risk exposure value to decrease significantly. Similar to the contract value, saving has a negative impact on current risk exposure. Because the value of saving in value (IDR) will go hand in hand with the contract value, where the higher the contract value, the higher the chance of saving value.

Meanwhile, addressable spend has a significant positive impact on current risk exposure. This influence is related to the determination of the risk tolerance limit (BTR). The BTR is set based on the set of operational costs including addressable spend. Furthermore, current risk exposure is a combination of %BTR and addressable spend, so the higher the addressable spend, the higher the current risk exposure.

During the preparation of addressable spend for a project, the work owner will identify potential risks that can cause lost events. Based on the research results, the company can mitigate operational risks by improving the mechanism for determining addressable spend. This includes including the value of lost events and risk mitigation costs in the constituent elements of addressable spend. This will cause the value of addressable spend to be higher but reduce the potential for lost events.

The survey results which state that the significant difference before and after restructuring is the risk of fraud. With the roles of holding and subholding, there are obvious differences with the supervision and decision-making mechanisms by both management and regulators. Further research is needed to recognize whether the difference is in the direction and positive or otherwise.

CONCLUSION

The conclusion of this study is that centralization of procurement in state-owned companies has a significant impact on the company's operational risk. The research shows that there is a significant difference in operational risk before and after procurement restructuring. Contract value and savings contribute to a decrease in current risk exposure, while*addressable spend* has a positive effect on risk exposure. This study recommends that to mitigate operational risk, companies need to improve the mechanism for determining addressable spend by considering the value of potential losses and the cost of risk mitigation.

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