

The Role Of Purchasing In The Hungarian Small And Medium Enterprises

Work-in Progress Paper

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Abstract

Purpose of the paper and literature addressed: Small and medium enterprises (SME) play an important role in the economy. Studies on SMEs recently have focused on the role of a particular company function in the target group by linking the development of SMEs to new advanced options, such as supply chain management and e-business. From a brief overview of the relevant publications it is obvious that these studies do not provide a homogeneous picture of the purchasing practices of SMEs but the different authors in several cases cannot even agree in the conclusions regarding certain issues of secondary importance. This paper provides an overview of our questionnaire research focusing on the specific characteristics of both purchasing and SMEs.

Research method: The questionnaire survey providing the basis for our study enables us to make international comparisons as well as to present the current state of the Hungarian SMEs focusing on a particular business activity. As our survey indicates, there is still great potential for further development in the purchasing practices of Hungarian companies.

Research findings: Focusing on the purchasing aspects enables us to gain a deeper knowledge on the main causes of the instability of SMEs as well as on their expectations regarding suppliers and a better understanding on the preferences of the customer. As a result we can highlight the main options of developing supplier relationships, the supply chain as well as the IT support of purchasing in B2B relations.

Main contribution: Based on the answers, there is an unambiguous close interlink between expert training, purchasing activity development, IT support and suppliers' relationship development. among open, innovation ready SMEs.

Keywords: purchasing, e-activity, small and medium enterprises (SME)

INTRODUCTION

Small and medium enterprises (SME) play an important role in the economy, this is why researchers increasingly investigate their practice. Studies on SMEs recently have focused on the role of a particular company function in the target group by linking the development of SMEs to new advanced options, such as supply chain management and e-business. From a brief overview of the relevant publications it is obvious that these studies do not provide a homogeneous picture of the purchasing practices of SMEs but the different authors in several cases cannot even agree in the conclusions regarding certain issues of secondary importance.

PURCHASING AND SMES

A number of international and domestic studies analyse the role of purchasing in a company operation and conclude, that this function has significantly developed in recent years. This change resulted in an increased role of purchasing and in the development of means and methods applied. These studies mainly focus on the management of a complex supplier

relationship networks and purchasing system, i.e. they seek effective solutions for managing complex problems. This quest for new solutions requires deep and comprehensive knowledge of the market and cutting edge technologies, and the investigations of alternative analysis and solutions are based on this information. But this investigating method is based on the practices and needs of large companies, since these conditions (complex supply structure, large and multilevel organization, need for managing a multi-partner purchasing process, purchasing value representing market strength, etc.) are not typical features of SMEs. However, in the background of the role of purchasing some elements can be found, which might make this function an important factor in the life of SMEs as well. Business relationships (such as supplier relationships) represent significant resources for the company.

In international publications the topic of purchasing characteristics of SMEs has only recently emerged. However literature review of relevant articles provides us a number of valuable findings in context of the relationship framework of SMEs, the knowledge background of relationship management and the development and contextual factors of relationship management.

RELATIONSHIP NETWORK OF SMEs

There is a growing interest of investigating business relationships within the context of the ARA framework of IMP. Piricz et al (2009) investigated personal matching as one of the basic factors of fruitful cooperation. They concluded that among SMEs personal contacts are really essential, however clear business goals and interest are crucial as well. O'Tolle and McGrath (2008) based on ARA model classified 6 dimensions of relational capability. Their research findings highlight the importance of relational capabilities as the foundation for all SME network capabilities and that co-adaption and co-innovation capabilities are greatly facilitated through generation and integration of knowledge and opportunities emanating through networks. But the relationship of innovation and network in case of SMEs attracted a lot of attention. Ngugi et al (2008) developed a framework which links innovation and capabilities to market changes in the context of business relationships and networks. The framework suggests that by improving capabilities and innovativeness in relationship with their customers, SME suppliers can enhance their ability to keep pace with market changes and consequently gain from co-created value. This model may be expanded to other business relationship like supplier-buyer relationships as well.

Morrisey and Pittaway (2004) in their study describing the supply relations of SMEs do not see the co-operative strategy as the most important factor, but present the types of relations as much less complex than that of the large companies. Analysing the purchasing practices of SMEs the authors emphasize the fact, that among the purchasing tasks – as opposed to large companies – beside the financial and performance criteria the individual tasks of the manager-owner play also a very important role.

KNOWLEDGE AND PROFESSIONALISM OF SUPPLY RELATIONSHIP MANAGEMENT

There a number of publications, which highlight the role of professionalism and the importance of knowledge of applying purchasing methods and techniques by SMEs. Ellegaards (2009) study is very enlightening, who investigated the purchasing practices of the owners of SMEs involved in product manufacturing. Ellegaard showed, that this company group represented a particular segment regarding purchasing. According to him the main characteristics are the following: the main priority is establishing sound supply; there is a frequent need for solving problems stemming from the lack of relevant rules and standards; lack of professional purchasing experience; too strong binding with the suppliers; loyalty. According to Dallago (2003) these companies cannot function efficiently mainly because

there is a lack of professionalism and well-established company procedures. Knudsen and Sarvais (2007) in their study analysing international purchases of SMEs emphasize the problems stemming from the difficulties managing different cultures, which is regarded by this company group as a significant risk. Consequently, their study also stresses the fact, that without sufficient purchasing expertise these companies cannot widen their limited purchasing options. The study also notes the practice of sticking to the same suppliers.

Quayle's (2002) investigation analyses the importance of purchasing, the knowledge of modern techniques and purchasing priorities in the practice of SMEs. His study shows, that although the sample used indicates relatively low importance of purchasing, but according to the traditional supplying criteria (price, quality, delivery) the performance of the suppliers is important, and in order to secure supplying stability the respondents would happily employ outside purchasing service providers.

Pressey and co. (2009) studying the characteristics of supply evaluation methods state – contradicting similar studies published earlier (Pearson, Ellram, 1995) – that applying evaluation methods is a common practice, however compared to the practices of large companies it is not as complex and formalised. Johnston and Wright (2004) in their study identify four factors affecting the e-business potentials of SMEs. These are: the outside environment (e.g. infrastructure, pressure), the inside environment (e.g. size, resources), attitudes (e.g. trust, relations, task-orientation), and expectations (e.g. expected benefits or risks). They explain the variations of the SMEs of different regions (USA, China, Japan, Mexico) by the differences embedded in these factors.

DEVELOPMENT AND CONTEXTUAL FACTORS OF RELATIONSHIP MANAGEMENT

Literature also deals with the effect of contextual and development factors. Beekman and Robinson (2004) explored the pace of the company growth and the companies' cooperation with the suppliers in the view of the concept of supply chain management. They concluded that the companies tend to use the existing purchasing network in the stage of their rapid growth even if the efficiency of those networks is not sufficient.

Tesar et al (2003) examined how a group of SMEs can work together to form a network designed to meet the demands and challenges from large domestic and international customers. They prepared a longitudinal case study, which followed a complete development and structuring of a network that provided a base for commercial activities. They resulted that the process to develop networks among small firms seemed to rely to different role models at different development stages.

Brush and Chaganti (1997) argued for the importance to take into account the lifecycle of companies analysing purchasing practices. Related study made by Daewoo and Hema (2001) investigates the factors influencing executives in choosing suppliers. They stated although rational considerations are dominant in the executives' decision-making some other factors such as age and education are also taken into account.

Noke and Hughs (2010) emphasize the importance of strategic considerations. In their analyses they show how purchasing can renew the manufacturing companies using strategic relations. Bordonaba-Juste és Cambra-Fierro (2009) promote an idea of supply chain management for SMEs. This article was heavily criticized by Ramsay in his 2007 article. In his opinion this idea uses a concept of supply chain and strategic relations for SMEs which is mainly relevant for large corporations. According to his position the purchasing practices of SMEs should focus on simpler purchasing functions.

From this brief overview of the relevant publications it is obvious that these studies do not provide a unified picture of the purchasing practices of SMEs, rather the different authors in several cases cannot even agree in the conclusions regarding some secondary issues either.

This can be explained by four major reasons. The research material used by these studies was taken from different geographical regions, the companies operate in different sectors – the fact emphasized by Brush and Chaganti (1997) -, significant differences stem from the given stage in the life-cycle of the companies, and finally, even the definition of SMEs differs according to regions.¹

THE RESEARCH METHOD

Our questionnaire with its enquires regarding the purchasing practices and characteristics of SMEs aims to clarify the role and place of purchasing in the practices of SMEs, and with its international publication background and its database it provides an excellent basis for international comparisons.

Analysing the Hungarian practice our study focuses on the common topics discussed in the international publications. Therefore our main topics are:

- the role of purchasing in the practice of SMEs,
- the business goals of SMEs and the presence of these aims and expectations in the purchasing practice
- the linkage between two main business relations: the recognised customers' priorities and supplier relationship management.

Our study is based on Quayle's article published in 2002 on the purchasing characteristics of SMEs. Our own questionnaire, which was properly completed by 104 enterprises for our evaluating purposes, was also based on Quayle's results and questionnaire. From these companies 76 can be classified as a small and medium enterprise and 28 as a large company. Including large companies in the survey was especially important in order to discover any significant differences between large companies and SMEs responding to the same questionnaire.

In our questionnaire some elements were incorporated taken from the "Competitiveness survey" questionnaire created by the Company Economics Institute of the Budapest Corvinus University.² Merging the two questionnaires enables us to make comparisons with the existing English results and the previous domestic results.

The average number of employees working at the companies featuring in our survey is 210. In our survey there are no sole proprietors and micro companies employing less than 4 workers, since they behave much like individuals, their motivations are significantly different, and in their case issues of distributing responsibilities can hardly be discussed. The companies were selected randomly. The questionnaire was sent by both electronic and hardcopy forms, with a view of possible distortions caused by IT deficiencies. By the number of employees 17.5% of the companies can be classified as a micro company (employing less than 10, but at least 5 employees), 57.3% as a small and medium enterprise (employing between 11 and 200 workers), and 25.2% as a medium and large enterprise.³

The companies featuring in our survey are involved in a wide variety of business activities, such as: constructing, printing, food processing, pharmacy, machine manufacturing, plastic manufacturing, safe waste disposal, car manufacturing, catering, bakery, IT service, trading

¹ According to the Hungarian regulations based on the Act XXXV. 2004.

3. § (1) those companies can be classified as SMEs, which

a) have less than 250 employees, and

b) have maximum 50 million Euros net price income or have a balance of maximum 43 million Euros.

² Based on Vörösmarty' analysis (2002).

³ In our rating Quayle' study (2002) was followed.

and adult education. By selecting our sample we aimed to include as many business varieties as we could, therefore our survey cannot be regarded as representative.⁴

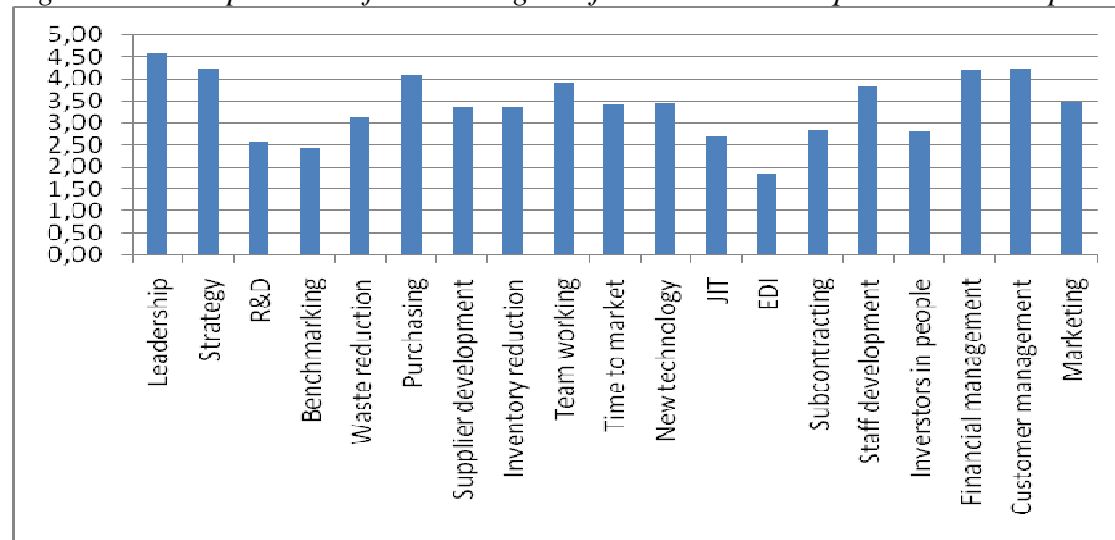
THE RESULTS OF OUR SURVEY

The following passage briefly summaries the results of our survey, highlighting the elements and features comparable with the international publications overviewed above.

THE IMPORTANCE OF PURCHASING

Survey results indicate that on a 5-mark scale the importance of purchasing among 20 factors was put on the 5th place with a 4.012 average in the sample containing only SMEs. These results in themselves indicate a significant development compared to similar surveys (Vörösmarty, 2002, Quayle, 2002), but the increasing importance of purchasing has been a characteristic feature of all companies in this period.

Figure 1: The importance of the investigated features based on questionnaire responses



Among the 19 features investigated, leadership, strategy, financial management and customer management are in the first four places, followed by purchasing. This supported the initial hypothesis that in case of SMEs there is increased inherence between customer expectations and supply goals. However companies indicating the importance of purchasing also consider the following factors as important: reducing waste, reducing stocks, improving supply chains. and sufficient financial control (invoicing, handling suppliers' outstandings). Since according to our factor analyses neither of the strategic considerations are related to purchasing.

To highlight the enherence between customer expectation and purchasing goals it was also studied what kind of costumer considerations are related to the purchasing importance indicator and what kind of the external and the internal conditions make purchasing a priority. As a conclusion of the factor analyses it can be stated that purchasing becomes a priority when their operation is largely effected by their purchasing option. The costumer

⁴ In Hungary 99.8 % of the companies can be classified as a SME. 94.7 % is a micro company, 4.4% is a small company and 0.7% is a medium company. The report by the European Union Enterprise and Industry Department published in 2009⁴ highlights the fact that the number of SMEs per 1000 persons is significantly higher than the Union average of 40: in Hungary it is 55. However, interpreting this fact it has to be also taken into account that about half of these are part-time enterprises, and in the Hungarian economy the number of employees working in SMEs is higher, while the added value produced by them is lower.

consideration which is most closely related to the importance of purchasing is the product reliability.

Since improving supply chains is considered as important mainly by larger companies, it can be assumed, that with the increasing company size the importance of purchasing also increase. There is a weak correlation between the two factors ($H=0.025128$).

However, there is an interesting connection between the importance of purchasing and the size of the purchasing organisation. As opposed to logical expectations, namely, that there should be a strong correlation between these two factors, the correlation is only 0.273 (as an indicator for company size the price-income was investigated). Further studies indicated that instead of the factors traditionally influencing the number of employees involved in purchasing (the value of purchasing compared to the price-income, innovation requirements) the main determining factor is the dependence on suppliers.

Generally it can be stated that with the increasing number of employees there is a need to increase the purchasing organisation as well. At small companies in average there are two purchasing employees per 100 employees. However, this ratio decreases with the increase of the number of employees, which means that there is no linear relation between the number of purchasing employees and the total number of staff. At large companies the ratio is one purchasing employee per 65.36 employees. Our regression calculations show that creation of purchasing department tends to depend on the number of company employees (McFadden R^2). However it can also be stated that apart from the size there are many more factors influencing purchasing.

To sum up, purchasing is regarded by SMEs as mainly an operative task, determined by outside forces, chiefly by the supply chain or the introduction of quality insurance requirements. However, in this process the potentials of purchasing organisations are not taken advantage of.

The main task of purchasing is to ensure the sound supply of basic materials needed for production and to support quality expectations of the customers. Nevertheless, the view of company process and supply chain process can only weakly influence the practices of Hungarian SMEs, since –purchasing cooperates mainly with the financial department. This Hungarian result supports Ellegard's studies (2009) about the behaviour of SMEs. Although at time of formulating our questionnaire Ellegard study was not available yet, so supporting his findings could not be our aim, the results are nevertheless very similar.

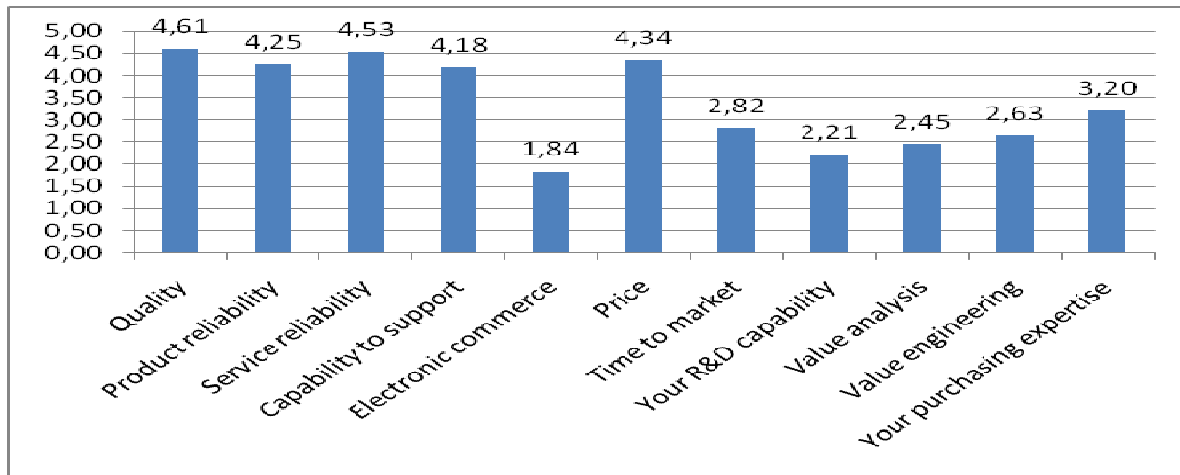
THE AIMS OF SMEs AND THE REQUIREMENTS OF THEIR CUSTOMERS

As it was highlighted in Morrissey's and Pittaway's study (2004), there can be significant differences between the basic aims of SMEs and those of large companies. While the basic aim of large companies is the long-term profit maximalization, the aims of SMEs can relate to a particular way of life, which can influence their relations with outside partners and hence their purchasing strategies as well. This is supported by Andrási Z. et al (2009) and Szirmai P. et al (2009), two studies about the increase of Hungarian SMEs.

According to the survey the aim of the companies is to provide the best possible service for the customers, and maintaining good relations with them is also an important issue. The importance of these factors was indicated as 4 or 5 by all but two companies (on the 5-mark scale)⁵.

Figure 2: Customer priorities

⁵ One of these is an agricultural small company, the other one is a large service provider. The first is definitely a way of life company, while the second is largely dependent on the state.



The major preferences of the customers of SMEs are: quality, reliability of the service, price, product-reliability and readiness for cooperation. In this respect there is no significant difference between SMEs and large companies in the sample. The differences regarding the requirements considering company size are innovation-related. The customers of small and medium companies are much less concerned about these factors. However as it will be shown later the SMEs approach to innovation and innovative solutions is very different.

However, there is a strong correlation between the price and the importance of successfully involving sub-contractors in the business philosophy of a company. Our study assumed that price as a factor can have different importance in different sectors. It was later supported by the fact, that investigating separately constructing companies and companies involved in building maintenance it was found, that for the clients of these companies (which make up 20.19% of our sample) price is an important priority. Disregarding the constructing companies the importance of price is lower, in average it is 4.22. In these cases the reliability of the product is more important than the price.

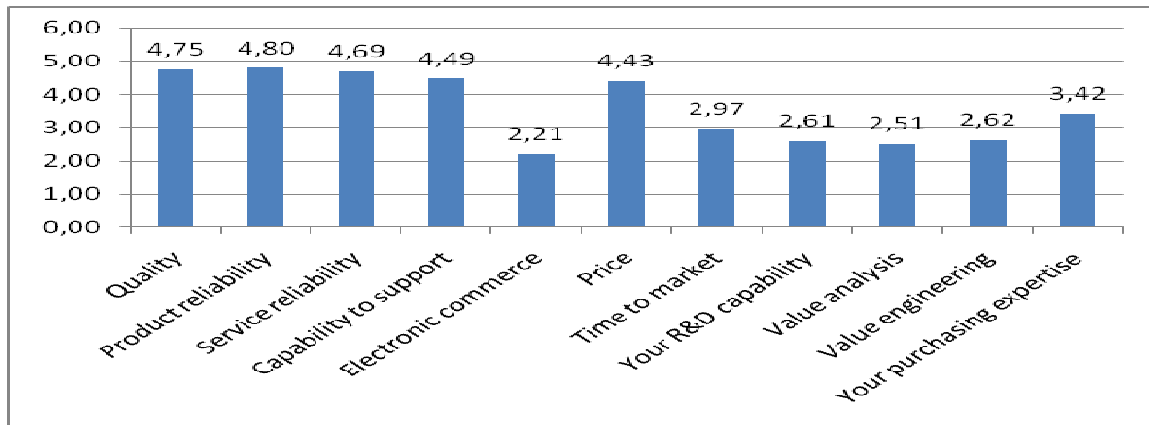
Those SMEs whose operation is mainly determined by the outside competitive environment consider the potentials of electronic commerce as a more important factor, and good supplier relations as a highly important one. According to these companies their ability of value analyses and value engineering is considered as a significant value by their clients. However, no particular company group could be identified. The main reason for this is that these factors are typically undervalued by the companies.

To sum up, the data reflect that the Hungarian SMEs feel, that the clients expect *quality* from them, which can be achieved by providing *high standard service*, if they can completely meet all the quality requirements and in the mean time they can achieve the largest *profit* possible. However, analysing the relevant data it seems that the profit target is rather a kind of additional result and not a basic aim for the company, since the main basis for surviving is providing a complete service for the clients of the company.

EXPECTATIONS REGARDING SUPPLIERS

The main expectations regarding suppliers are in priority order: reliability of the product, quality, and reliability of the service. Price is only on the 5th place. Abilities for value analyses, value engineering and R+D are at the end of the priority list.

Figure 3: Expectations regarding suppliers



Only a slight difference can be detected between SMEs and large companies, namely that at the top of the list price has a somewhat more importance at large companies. One of the reasons for the lower importance of price can be, that SMEs have only limited options for reducing price, since they do not purchase in such quantities which could make it possible for them to reduce prices, compared to the major suppliers they are small and do not have the necessary purchasing knowledge (negotiation techniques, value analyses, etc.) which could help them further reduce prices. Under these conditions the price of a particular product becomes an external eventuality, so other factors become important in purchasing (e.g. technical and service elements).

Another typical behaviour pattern could be identified regarding prices: although price cannot generally be considered as a dominant criterion, but if a company has very limited financial resources and the client market reacts flexibly to price change, then the price of basic materials becomes a high priority. The same pattern can be identified if purchasing resources become limited.

The least valued factor in the expectations regarding suppliers is the ability of electronic commerce. This is a surprising fact, since according to our studies and other publications (e.g. Ellegaard 2009) the majority of the companies cannot use a lot of resources for maintaining good relations with the suppliers, nevertheless they expect the highest possible willingness for cooperation of them. These low expectations regarding good relations must be highlighted, since for most of the companies their own ability to engineer value and finance R&D is closely related to the ability of the suppliers to engineer value and finance R&D. One of the possible reasons for the low priority of electronic commerce might be the deficient IT infrastructure of these companies. Those IT solutions are preferred, which do not require more serious IT knowledge and can be used by private individuals. For example there is a general tendency to use Internet and E-mails for purchasing purposes.⁶

It can also be stated based our factor analyse quality means product reliability for the respondents of our survey. However capability to support is also one of the main priorities whereas e-commerce has the lowest priority. It can be concluded that the most important three priorities for SMEs are: product quality, maintaining personal (not electronic) contacts and price.

⁶ Our conclusion supports Csapó K. et al's opinion (2004) pp. 77. about the e-activities of SMEs. According to this: „E-business mainly effects inside working processes in the company. Most of the companies can improve the efficiency of inside working processes by applying ICT solutions. The basis of efficiency improvement is applying simple applications and solutions which do not require sophisticated and expensive business softwares. These applications are available and affordable for small companies as well, therefore they are also useful.”

Protecting the environment has an interesting role in our analysis. The Hungarian SMEs consider environmental issues as important factors when evaluating suppliers, but this consideration probably arises from the requirements of the customers, since the answers to this question are strongly related to the reliability of the service and to the cooperation readiness.

To sum up, SMEs expect sound high quality products from the suppliers. For this quality provides the basis for the quality of their own products. However, they do not insist on maintaining relations with their suppliers and do not wish to be involved in the R&D activities of the suppliers. Although price is a factor to be taken into account in their decisions, it is not necessarily the main priority. Its importance becomes higher if the position of the company is endangered due to a price competition created by a new player on the market. It is also typical, that the expectations of the clients are reflected in the expectations of the company regarding their suppliers.

SUPPLIER RELATIONSHIPS OF SMES

SMEs can measure the efficiency of their purchasing organisation by the following tasks: quality improvement (4.481), finding the right supplier (4.587), maintaining long-term partnership with the supplier (4.462). Cost reducing, price (4.43) are closely related to the professionalism of purchasing in SMEs. The multi-factor analysis of the data indicates that the first three criteria seem to be qualifying factors (helping stay in the competition), while price seems to be a competition criterion.

An earlier study (Vörösmarty, 2002) where similar criteria were studied on a sample of mainly large companies provides an interesting option for comparison. According to this cost reducing turned out to be the most important indicator for the efficiency of purchasing. In the sample of large companies maintaining long-term partnerships seemed to be less important (using the same scale the figure is 3.78 for large companies compared to 4.46 for small companies).

SMEs tend to use only a few suppliers, which is reflected in the fact, that reducing the numbers of suppliers is considered to be the least important factor. In the publications on management reducing the number of suppliers is considered as a first step towards strengthening relations, which can be an important consideration for large companies.

However, some results regarding other activities of large companies are applicable for SMEs as well. Improving the performance of the suppliers is closely related to the evaluation of suppliers in SMEs as well. Meanwhile maintaining good relations with suppliers is not considered as an important priority, and only 15 companies have supplier improvement programmes. On closer look three important information relations can be identified. The first is the communication of the expected volume of purchasing, the second is the occasional communication about the evaluation of the supplier, and the third is the occasional meetings and company visits. It is worth noting, that the least typical information relation, i.e. the communication about the planned product development is also present in the 50% of the sample. This contradiction has already been analysed in earlier domestic studies. One possible solution for this might be the fact, that the companies considering product development are not cooperating with their suppliers and provide information only concerning their needs for the existing plans' specifications, in order to help them chose the right future partners. According to our study development of operation, IT development, improving supplier relations are closely related factors. Companies giving higher marks to these questions have already achieved a more developed purchasing practice (typically these companies have higher price income). It is regrettable however, that exact knowledge of the suppliers market was also put among these questions.

As a consequence of all this Hungarian SMEs have only one or two key suppliers, whose performance are mainly evaluated according to the reliability of delivery and quality due to the deficient knowledge of the market. Larger companies have a developed purchasing practice, but the main priority of smaller ones is maintaining a long-term relation with suppliers. Smaller companies, as it has already been shown by other studies (e.g. Knudsen and Sarvais, 2007), are willing to change their supplier only as a last resort, since they do not have the knowledge necessary for finding and involving new suppliers, and also because their transaction costs are very high due to the low IT support. Cost reducing and environment protection might acquire higher priority among their considerations if it is required by the client market or official regulations. Other considerations however, are more typical in companies having a more developed purchasing organisation.

SUMMARY

For the surveyed SMEs purchasing has medium priority, which means that the importance of purchasing is increasing for both large and small companies, and compared to previous result it represents an improvement reflecting the general economic trends. However it is also typical that purchasing mainly accomplishes operative tasks: maintaining production, services, guarantying quality whereas new techniques such as e-commerce tools have the lowest priority. Strategic purchasing decisions and supplier relation management actions are taken by the managing director, who does not necessarily have proper capabilities and knowledge of relationship management methods.

The lack of proper relationship management capabilities is reflected in the fact that small companies prefer long-term relations, partly because they consider it as a quality guarantee, partly because they do not have sufficient information about the supplier market or they do not have sufficient resources for a regular and comprehensive market analysis. However real partnership quite seldom emerge. With increasing company size – and with increasing purchasing organization – competitive supplier management approach is becoming an important factor, and price is becoming a determining consideration. Hungarian companies do not really take advantage of the potentials of purchasing and supplier relationship management.

The results highlighted that the innovative culture of an SME might contribute to innovative approach to supplier relations. The driving force of development is often one single factor, for instance an important customer. As easily applicable solutions available or definite expectations (such as environmental standards) are identified than these companies are open to consider them.

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