VERTICAL INTEGRATION STRATEGY AND ORGANISATIONAL SURVIVAL IN MANUFACTURING FIRMS IN PORT HARCOURT, RIVERS STATE, NIGERIA.

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Abstract
This study investigated the effect of vertical integration strategy on organisational survival in selected Manufacturing firms in Rivers state of Nigeria. The sample for this study consisted of 205 managers from the 6 selected firms. The data for this research was collected using the questionnaire methods. The Spearman Rank-order correlation coefficient was used to test the relationships between the variables under review. Findings from the study revealed that there is a positive and significant relationship between the two dimensions of vertical integration strategy used for the purpose of this study (forward and backward integration strategy) and organisational survival. Our findings reveal a positive and significant relationship between the dimensions of vertical integration and organisational survival. In view of this we conclude that vertical integration enhances organisational survival. These findings give rise to several recommendations.

Keywords: Vertical integration, Forward integration, backward integration, Organisational survival.

1 INTRODUCTION

Given the dynamic nature of the business environment coupled with the pace at which technology is advancing leading to a more sophisticated business world, organizations are now facing the reality of this paradigm shift which portend a serious threat to the less innovative organisations, this is a wakeup call to most drivers of the organisation to brace up to this challenge and take advantage of the emerging technologies in fostering efficiency and effectiveness at workplace which will in turn result in the production of goods and services at lower costs, this will in many ways position the organisation strategically for global competition. In this period of harsh economic condition only organization with the best strategic option can compete for survival. In Nigeria today it is no longer news that most organization are winding up, a situation where most foreign companies are relocating back to their home countries due to the harsh economic condition the country is experiencing today, most indigenous firms are gasping for breath as they can no longer bear the brunt of the economic hardship being experienced across the length and breadth of this nation. In view of the retinue of challenges it becomes imperative that organization should among various strategic options for organizational survival choose a choice of strategy that will be beneficial to the overall organization and bring about her survival.

In trying to select a strategic option that will be best suited for these challenges, organisations may choose to either vertically or horizontally integrate. Manufacturing firms increasingly choose to vertically integrate; that is, rather than relying on independent suppliers, factors and agents, they choose to be the main producer of the input materials themselves (backward integration) and even distribute finished goods (forward integration). Moreover, new production technologies have given firms the opportunity to exert scope economies by producing a wider range of products at a lower cost, compared to those produced separately, leading them to horizontally integrate. **(Besanko et. al, 2007)**

In the past, series of scholarly work have dwelt on the question of the diversification-performance relationship. For instance **Santalo & Becerra (2008)** argued that, while several scholarly works indicated strong evidence of trading at a discount for diversified firms, others agree that diversified firms proved to be more productive when compared to the non-diversified businesses. Moreover, the early contributions of **Rumelt (1982)** indicated that, as firms diversify into more unrelated areas, a lower performance outcome is more likely.

Through diversification within their areas of business, the organizations desire to reduce costs and improve market effectiveness by utilizing economies of scale and scope.

There appears to be a dart of literature concerning vertical integration strategy in a single country especially in the Nigerian business environment.

It is on this premise that this study will evaluate the impact of vertical integration strategy on organisational survival in the Nigerian work environment focusing on selected manufacturing organisations in the Port Harcourt metropolis, Rivers State of Nigeria.

STATEMENT OF THE PROBLEM

In a harsh economic condition, where all the elements of the external environments are not under the control of the organisation, the importance of strategic option cannot be over emphasized. This is because the choice of a strategy has a direct impact on the organisations survival and its ability to have a competitive edge, as the trend in the labor market is highly challenging and dynamic in nature. It is obvious to note that for any organisation to be sustained in the competitive market and also retain its corporate image, it must always scan the environment in which it operates.

Thus as the organisation is a product of the environment, and cannot function without resources from its environment. The organisation has to scan the environmental input and design components to transform into outputs. This environmental scanning or diagnosis will help the organisation know what is on ground in its operating sector and in addition forecast what would come up within some space of time in the competitive market. Besides, when companies encounter changes, innovative knowledge brings about unexpected benefits. In support of this, Vertinsky (2003) opine that in order to sustain the intense competition, organisation have to effectively leverage their capabilities for survival. Manufacturing companies in Nigeria have been facing tremendous challenges occasioned by the Nation's economic downturn. These hardship are manifest in the area of epileptic power supply, the country's deficient infrastructure including bad nature of the roads, credit squeeze, low purchasing power, high cost of custom duties for importation of raw materials used in local production, continuous fall of the naira against the dollar, corruption, poor management, production of fake products, youth restiveness as witnessed in kidnapping and recent bombings of our oil pipelines and many more are some of the eminent problems bedeviling manufacturing companies in Nigeria. The external environmental factors are the most threatening because some of them are far beyond the control of managers.

These problems have led to some employees leaving their organisations for better opportunities. When employees move away from their companies, the knowledge gap created by their absence generates significant costs to the employers, but even more trouble is the potential loss of institutional knowledge. Another problem is ageing workforce which presents potential knowledge vulnerability. When an organisation is faced with these myriad of challenges there is need for an appropriate strategic choice that will ensure organisational survival.

RESEARCH HYPOTHESES

In order to have a clear test and validity of the study, the following hypotheses were tested.

Ho_1: There is no significance relationship between forward integration and organisational survival.

Ho_2: There is no significance relationship between backward integration and organisational survival.

2. LITERATURE REVIEW

THEORIES OF VERTICAL INTEGRATION

Coase (1937) opined that the idea to float a firm is at first a function of the existence of the marketing costs. The nature of transactions as well as the overall activities of the firm within its boundaries helps in the assessment of the firm's size, instead of its output. These boundaries are defined as the vertical boundaries since these activities are related at the various levels of the supply chain; **Sudarsanam (2010)** defines vertical integration as "the integration of successive activities in a vertical chain under a common coordination and control." Vertical integration defines the activities that the firm performs within its boundaries, compared to the purchases from independent firms in the market **(Besanko et.al, 2007)**. In other words, vertical merger replaces two or more independent firms with a single firm, and rather than relying on arm's length market-based transactions or contractual dealings, it internalizes the coordination of the successive activities of the firm. **Fan & Goyal (2006)** indicate that vertical mergers procure acquiring companies with ownership and control over contiguous stages of production. These mergers allow firms to substitute internal exchanges within the boundaries of the firm for contractual or market exchanges.

Make-or-Buy Decision

Make-or-Buy decisions provide answers to such questions as: Why do some organisations go for a vertically integrated structure, where others are specialists in one stage of production and outsource other stages to outside firms? The concern here is, should a firm produce its own inputs, buy them in the spot market or preserve the relationship with a specific vendor.

This decision will go a long way in determining the firm's level of vertical integration, since each decision is a pointer to the nature of the operation a firm will engage in and which it will outsource from the suppliers **(Walker & Weber, 1984).** This thinking is concerned with the decision whether the firm should integrate backwards, which is "to internalize production of the raw materials instead of sourcing it from the external supplier." **(Sudarsanam, 2010)** Therefore the 'make' part of the decision shows that ownership is joint and control rights are integrated, whereas under the latter, they are separate. Moreover, organisations need to factor in the costs and benefits of either alternative. For instance, this choice may be a function of a range of factors such as; "the current and future availability of spot markets for arm's length transactions, the cost of sourcing from the direct and indirect costs of contracts and informal arrangements, uncertainty and information asymmetry between buyer and seller and indirect costs of internalizing production.

In view of these factors, the organisation may choose to carry out the activities in-house or prefers buying them from the specialists in the market firms (**Besanko et. al, 2007).**

The Transaction-Cost Theory

This theory can be traced back to **Coase (1937)** who assert that production will take place within the firm when the cost of putting in place production through the market exchange is higher than within the firm. This cost of doing business with independent market firms is defined by **Coase (1937)** as the cost of using the price mechanism. The firm's size will be a function of the cost of using the price mechanism, in which "a firm will tend to expand until the costs of putting in place an extra transaction within the firm become equal to the costs of carrying out the same transaction by means of exchange on the open market or the costs of transacting in another firm.

Leiblein and Miller (2003) argue that, although the applicants of the theory generally assume that markets ensure a more efficient mechanism for exchange when compared to hierarchy, in certain situations the costs of the market exchange may just be be too high and surpass these efficiencies procured by the market. Therefore, the theory focuses on determining the features of exchanges that are best suited to the firms and the market.

The Property-Rights Theory

This theory as developed by **Grossman and Hart (1986)** laid emphasis how ownership of asset can change investment incentives. Two types of contractual rights were proposed by them which are the specific rights and residual rights of control. "When it becomes too costly for one party to specify a retinue list of the particular rights it desires over another's party's assets, it may be optimal for such party to purchase all the rights except for those specified in the contract. All the residual control rights of the physical assets in question are held by the entity under integration, whereas under non-integration, the assets are owned individually **(Hubbard, 2008).** Moreover, **Grossman & Hart (1986)** argue that the allocation of residual control rights to one party will strengthens the investment incentives of that party, while making the counter party's investment incentives weak. "Integration shifts the incentives for opportunistic and distortionary behaviour, but it does not remove these incentives.

Therefore, both costs and benefits from integration will exist. One of the concluding remarks of **Grossman & Hart (1986)** is that, integration is instrumental when one party's investment incentives are relatively more important to the other firm's incentives. On the other hand, when both investment decisions are equally and somewhat crucial, non-integration is becomes imperative.

The Theory of Relational Contracts

Looking at issues relating to contracts, the third insight is formed by **Baker et al. (2002)** pointing out that "relational contracts are informal agreements and unwritten codes of conduct that powerfully shapes the behaviours of individuals within firms, these relational contracts affect the behaviours of firms in their business relations with other firms, whether vertical or horizontal. **Baker et al. (2002)** underline in their study the ease of relational contracts between and within the firms, compared to the difficulties encountered in formal contracting. Therefore, a relational contract empowers the parties to exploit their detailed knowledge to their particular situation and to adapt this situation to new information as it becomes available.

3. METHODOLOGY

RESEARCH DESIGN

The quasi-experimental design involving cross-sectional survey was used for this study, as the researchers do not have control over the elements.

POPULATION OF THE STUDY

The target population of this study was drawn from managers of manufacturing firms in Port Harcourt purposively selected for the study. Top and middle level managers of the organisations under study were selected.

DATA COLLECTION METHOD

This study made use of both primary and secondary data. A set of questionnaire was administered to the managers in the manufacturing firms under study. This method will allow the respondent to answer questions thoughtfully and at their own pace; the researcher also made use of vital documents from the organisations under study.

4. TESTING OF RESEARCH HYPOTHESES

The research hypotheses were tested using the Spearman Rank Order Correlation coefficient and was analyzed using the SPSS statistical package version 20.0 as shown below:

HO_1: There is no significant relationship between forward integration and organisational survival

Correlations

Type	Variables1	Statistics	F. I	O. S
Spearman's rho	F.I	Correlation Coefficient	1.000	.543**
		Sig. (2-tailed)	.	.000
		N	205	205
	O.S	Correlation Coefficient	543 **	1.000
		Sig. (2-tailed)	.000	.
		N	205	205

**. Correlation is significant at the 0.01 level (2-tailed).

The SPSS table above as shown in the appendix, revealed that: Spearman's rho is 0.543** and Probability is 0.000 this showed that: There is a significant relationship between forward integration and organisational survival. $P < 0.05$ level of significance. Decision Rule: when $p < 0.05$ accept the alternate hypothesis and reject the null hypothesis.

HO_2: There is no significant relationship backward integration and organisational survival.

Correlations

Type	Variables1	Statistics	B.I	O.S
Spearman's rho	B.I	Correlation Coefficient	1.000	.424**
		Sig. (2-tailed)	.	.000
		N	205	205
	O.S	Correlation Coefficient	.424**	1.000
		Sig. (2-tailed)	.000	.
		N	205	205

**. Correlation is significant at the 0.01 level (2-tailed).

The SPSS table above as shown in the appendix, revealed that: Spearman's rho is 0.424 and probability is 0.000 this showed that: There is a significant relationship between backward integration and organisational survival. $P < 0.05$ level of significance. Decision Rule: when $p < 0.05$ accept the alternate hypothesis and reject the null hypothesis.

5. DISCUSSION OF FINDINGS

The Spearman's rank order correlation coefficient analyzed using statistical package for social sciences version 21.0 (SPSS) revealed that: for the two hypotheses; There is a significant relationship between vertical integration (forward and backward integration) and organisational survival. . This result is consistent with the findings of Bettis (1981), Rumelt (1982) who indicate that the vertically integrated companies are outperforming the non-vertically integrated ones in terms of corporate performance. Previous research points to the fact that vertical integration occurred when the investment involved high specificity in knowledge, assets and know-how (Monteverde &Teece, 1982). A rise of complexity and specialization of the inputs would increase the probability to vertically integrate (Masten, 1984). Based on this finding we say that vertical integration strategy enhances organisational survival.

5.2 CONCLUSION

The purpose of this study was to investigate the impact of vertical integration strategy on organisational survival in selected Manufacturing firms in Port Harcourt rivers state. The results of this study however reveal that the two vertical integration strategy dimensions (forward and backward integration) as used in this study were positively related to the organisational survival. In view of this we conclude as follows: that both forward and backward integration strategy enhances organisational survival.

RECOMMENDATION

Given the result so far revealed by this study, we therefore recommend that:

1. Since vertical integration strategy is positively related to organisational survival, management should adopt a vertical integration strategy (forward and backward integration)

in order to strategically position the organization for survival especially at this period when many organisations are gasping for breath.

2. Managers should take the initiative as regard vertical integration strategy, this initiative should include making vertical integration issues a part of their performance review.

3. Management should have the understanding that the extent to which employees appreciate their strategic option is a function of the ability of management to provide the necessary management support for its subordinates. This is very necessary especially when assigning persons to managerial positions.

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