

The Purchasing Cycle Explained



How much your company spends to do business, and how often, plays an important role in your overall success.

Transforming cash into goods and services, the *purchasing cycle* is at the core of procurement and can have a major impact on your productivity, competitiveness, and profitability.

Understanding your company's purchasing cycle is the first step toward optimizing it.

With the help of technology and process improvements, you can ensure your purchasing department is building value for your company while reducing costs due to wasted time, energy, and resources.

What is the Purchasing Cycle?

The purchasing cycle—also called the *procurement cycle* or *procure-to-pay* (P2P)—is the process by which you order, obtain, and pay for the goods and services your business needs.

It typically begins with identifying the need for a product or service, followed by requisitioning, supplier selection, negotiating terms, issuing purchase orders,

receiving goods or services, invoicing, and finally, payment.

This structured approach helps businesses streamline operations, control costs, and ensure efficient inventory management.

Integrating technology like procurement software can further optimize the purchasing cycle by automating tasks, enhancing visibility, and facilitating data-driven decision-making throughout the procurement process.

For companies of all sizes, from local small businesses to global megacorps, the purchasing cycle begins with needs analysis and ends with payment and record keeping. In between, they may generate a purchase order, pay for goods directly, or invite tenders (also known as bids) to encourage more aggressive and price-effective competition between suppliers wishing to fulfill a specific need.

The Purchasing Cycle, Step By Step

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Most companies have a quirk or two, but in general the process follows a fairly straightforward series of events:

1. Needs Analysis

This stage of the purchase cycle is dedicated to identifying the need to be met, whether it's a reorder, raw materials for a new product produced by the company, or office supplies.

2. Needs Clarification

Once the need's been identified, the variety (e.g., brand), amount

required, and delivery schedule need to be established.

3. **Purchase Requisition and/or Purchase Order**

With the details settled, the requesting party has a couple of options. Generally, those without the authority to approve direct purchase orders will first create and submit a *purchase requisition*, which is an internal document requesting that approved parties obtain goods and services. Upon approval, the purchase requisition is used to create a *purchase order*, which is the actual order sent to the supplier for the goods and services required.

4. **Authorization**

The purchase order (generated from a purchase requisition or not) must also be approved. The purchase order process benefits from automation and artificial intelligence (AI), usually through the use of purchase order software that's part of a comprehensive procurement software package.

Not only does automation permit role assignments and automatic routing and tracking of all purchase orders and approvals/rejections/revisions, but it allows for real-time adjustments and transparent communication between all parties involved. In addition, automatic reminders can be created to ensure no PR or PO is left to languish.

5. **Supplier Review**

If you've already integrated an automated procurement solution into your workflow, chances are the list of approved and available suppliers will obviate this step in the process—especially for repeat orders. But if you're adding new products, or new suppliers for existing products to the system, then each candidate must be reviewed for compliance, performance, and reliability.

6. **Supplier Selection**

At this stage, the purchaser chooses the supplier who'll be filling the

order, either from the pre-vetted list in their software catalog or through other means.

7. **Price and Term Negotiations**

This step is also made infinitely easier if your workflow is built around procurement software automation. Centralized contract and document management and information sharing means previously-negotiated contract terms and best price are already available for each vendor on the approved list. New vendors being added to the system will have this information added as your legal team completes and certifies your company's agreement(s) with the vendor.

If your company doesn't use automation, then your team will need to sit down with the vendor to negotiate payment terms and conditions.

8. **Order Placement**

At this point, the buyer officially places the order and creates a binding purchase agreement between your business and the vendor.

9. **Receiving and Inspection**

For material goods, arriving shipments are inspected for completeness and integrity, with any shortages and broken goods marked to be credited back to the buyer. The invoice is either included with the goods or sent separately by the vendor.

Inventory management is either manually updated or handled automatically by the procurement software, which links the shipping documentation to the original purchase order, invoice, related correspondence, and other documents for data analysis and auditing purposes.

10. **Payment**

The invoice is reviewed for accuracy against the purchase order, invoice,

and other documentation. Depending on the terms established for the supplier and the approval of the reviewing party, payment is issued (usually within 30, 60, or 90 days).

11. **Records Management**

Businesses still using manual systems follow up by updating their inventory totals and purchasing ledger. Purchasing software automates this step, as documents are cross-connected and update automatically across all departments.

What About Tenders?

The purchasing process when using tenders is very similar to the standard purchasing cycle, with a few important changes:

1. **Needs Analysis** is much more narrowly defined at inception, and often supported by a business case.
2. **The Approval Process** requires more review and may be granted by departmental or even C-level management.
3. **The Tender Process** is used instead of the PR/PO model, and involves:
 - A very specific Request for Proposal (RFP), written to formally outline the goods and services needed and request approval.
 - Tender invitations, which are posts made to the public (either online or in print) inviting vendors to bid for the right to fulfill the request.
 - Pre-Qualification Questionnaires (PQQs) are sent to each of the most promising candidates to provide greater detail about their capacity, history, and operations.
 - Tenders (i.e., bids) arrive from the pre-qualified candidates within the specified period.
 - Each bid is reviewed, and the candidates interviewed to further qualify them for consideration.
 - All valid tenders are carefully reviewed over the course of days or even weeks. The winning bidder is granted the contract, based on their credentials.

4. **Negotiation** brings the winning supplier and the buyer together to hammer out the terms and conditions (in general, price is already locked in during the tender process). The legal contract is formally awarded to the bidder when negotiations conclude.
5. **Contract Management** is handled by the company's procurement, financial, and legal staff. During the management period, goods are received and reviewed, and fulfillment of the required terms and conditions verified.
6. **Review, Approval, and Payment** all rely on complete, accurate, and on-time fulfillment of the contract. Any exceptions are noted and the buyer is compensated according to the terms negotiated. Once the contract terms are confirmed, payment is made and the relationship either ends, or the supplier is added to the company's vendor management system as a pre-approved candidate for future tenders.
7. **Records Management** is identical to the standard procurement cycle.

Take Control of Your Purchasing Cycle

Having mastered the purchase cycle, you're ready to squeeze maximum value from it.

Combined with machine-learning-enabled software and automation, formalizing your purchasing cycle lets you fine-tune *all* the stages of the procurement process to reduce your workload, eliminate delays and errors, and simplify everything from inventory to materials management to financial forecasting.

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