OUTSOURCING WITHIN A SUPPLY CHAIN MANAGEMENT FRAMEWORK

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ABSTRACT
The study focuses on the analysis of the outsourcing process, by identifying the advantages and disadvantages of outsourcing, analysing the collaborative buyer-seller relationship, the outsourcing lifecycle process but also determining the influence factors on the outsourcing success or failure. The purpose of this paper is to present the outsourcing concept within a Supply Chain Management framework. The undertaken research used the methodology of bibliographic study and qualitative research using various secondary sources. It is shown that more big companies appeal to outsourcing as an efficient technique to gain competitive advantage. They entrust part of their activities to other companies in order to focus on their core activities. Positive aspects but also negative aspects of outsourcing are highlighted in order to expose the success of this process but also the dangers that can appear.

KEYWORDS: *outsourcing, supplier, Supply Chain Management, competitive advantage*

JEL CLASSIFICATION: *L14*

1. INTRODUCTION

The increasing competition along companies as both in local as also in international market determined managers to focus on gaining competitive advantage in order to stay in business. Nowadays achieving customers' fulfilment and gaining their trust became more and more difficult. This can be purchased through improvement of products and services. As both Supply Chain Management and outsourcing have been acknowledged as ways to gain competitive advantage. (Raja & Kherun, 2006)

Increasing organizational performance can be realized among traditional methods to improve competitiveness, also by outsourcing the activities from the global chain of the carried out activities. The goal of outsourcing is to make the company more flexible and adaptable to new environmental conditions, by focusing on its core activity, entrusting part of the tasks, activities or functions to other companies. (Florea)

The general purpose of this research is to analyse the outsourcing process in a Supply Chain Management framework. As specific objects we can identify determining advantages and disadvantages of outsourcing, influence factors on outsourcing success or failure and analysing the outsourcing life cycle.

The paper analyses the outsourcing process in a Supply Chain Management environment. The first part of the paper consists of describing the Supply Chain Management and procurement concepts. After that the outsourcing process is analysed, taking into consideration the collaborative buyer-seller relationship, the advantages and disadvantages of outsourcing, factors that influence the

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success of outsourcing, but also outsourcing dangers and outsourcing life cycle. The research ends with conclusions and authors' opinions.

The outsourcing process is analysed by using the methodology of bibliographic study and qualitative research by diverse secondary sources.

Analysing various bibliographical studies, some gaps have been discovered concerning the research in the field of outsourcing, especially in the Romanian specialty literature. This fact formed the decision basis in order to analyse the outsourcing process, its advantages, disadvantages and the factors that influence its success or failure.

3. SUPPLY CHAIN MANAGEMENT

Supply Chain Management (SCM) is the management of a network of businesses and organizations to provide products and services based on customer requirements with regard to value, cost and time. A Supply Chain encompasses all activities in fulfilling customers' demands and requests. These activities are associated with the flow and transformation of goods from the raw materials stage, through to the end user, as well as the associated information and funds flows. (Ling 2007) The products move through a series of organisations as they travel from original source of raw materials through the final customer.

Supply Chain Management represents the planning and management of all activities involved in establishing sources and purchase of products, their conversion and logistics activities' management. Supply Chain Management includes coordination and collaboration between business partners, as suppliers of products, intermediate channels, service providers and customers in order to integrate and achieve an efficient management of supply and demand.

Companies focus nowadays on their core activities, on their strengths, so that many supply chain activities are outsourced to different organisations that are more specialized in the required activities. (Sweeney & O`Riordan, 2007)

4. PROCUREMENT

Procurement by definition represents the process of obtaining goods and services from preparation and processing of a requisition through to receipt and approval of the invoice for payment and is highly bond to Supply Chain Management. Purchasing is responsible for acquiring all the materials needed by an organization. Purchasing is the function responsible for issuing purchase orders and initiating the flow of materials. (Monczka 2010)

It is argued that purchasing describes the actual buying, while procurement has a broader meaning which includes different types of acquisition (leasing, rental, contracting, etc.) as well as the associated work of identifying and selecting suppliers, negotiating, agreeing terms, expediting, monitoring supplier performance, analysing orders, material administration and others. But these differences are largely semantic and thus the focus is on the principle rather than drawing artificial boundaries around functions.

The procurement department's mission is to provide the organisation with the right amount of the right product, at the wright time at world class costs.

5. COLLABORATIVE BUYER-SELLER RELATIONSHIP

External integration can be achieved through various types of cooperation, with suppliers this is generally referred to as buyer-seller relationship. (Fred & John 2007) Most buyers and sellers recognize the need for collaboration as the best way of improving costs, quality, delivery, time and other measures of performance. (Johnson & Fearon, 2006)

The following characteristics can define a collaborative buyer-seller relationship:

- For each purchased material there are a limited number of suppliers;
- Long-term contracts with agreed performance targets;
- Mutual benefits and sharing of rewards;
- Joint efforts to improve supplier performance across critical performance areas;
- Join efforts to resolve disputes;
- A credible commitment to work together during difficult times – which means that neither party returns to old practices at the first sign of trouble;
- A commitment to high quality, defect-free products with design specifications that the supplier’s process is capable of meeting.

No matter how high or well-structured the collaboration with a supplier is, there will always be conflicts which are an inevitable part of trade, especially in a big company. The company does highlight finding the root cause of each conflict but a higher emphasis is put on how to resolve the issue and ensure it never happens again.

Supplier performance has a great impact on the productivity, quality and competitiveness of the company and the Procurement department is aware of this. Big companies’ inclinations to buy, to outsource, to improve quality, to lower stock levels, to integrate supplier and purchaser systems and to create cooperative relations such as partnerships have underlined the need for outstanding supplier performance.

In general, flexibility and customer service in the supply chain became very important. Flexibility refers to the ability of making available the products or services to meet the particular customer demands. Flexibility is a key measure of supply chain performance and is often regarded as a reaction to environmental uncertainty. (Gunasekaran et al., 2001)

Although advances in practice and theory have contributed to enhanced knowledge of buyer-seller relationships, the discipline is far from mature. More effective buyer-seller relationships help both parties manage uncertainty and dependence, increase efficiency by lowering total costs, and enhance product development and market orientation through better knowledge of customers and their needs. To realize these benefits, more big companies manage to interrelate and conduct relationships with customers and suppliers to achieve effectively the diverse objectives and outcomes possible from each relationship. (Cannon and Perreault, 1999)

6. OUTSOURCING IN THEORY

Outsourcing can be defined as “the strategic use of outside resources to perform activities traditionally handled by internal staff and resources”. (Baily et al., 2008) Outsourcing is a strategy by which an organisation contracts out major functions to specialised and efficient service providers, who become valued business partners. (Griffiths)

6.1. Insourcing and Outsourcing

Insourcing means that a company internally makes a particular material that is needs for its operations. Outsourcing means that it buys the material from an external supplier. (Monczka et al., 2010)

Insourcing and outsourcing occur when the decisions are made to reverse past buy-or-make decisions. (Johnson & Fearon, 2006) Procurement managers have to use a variety of knowledge for the insourcing-outsourcing decision. Their essential approach is to analyse and compare the benefits of insourcing and outsourcing.

The sourcing decision is important because it affects costs, but it also defines the boundaries that a company draws around its operations. Companies are likely to keep operations internal that are considered part of their core activities, while they are more likely to outsource activities considered more marginal. (Monczka et al., 2010)

The following table presents the disadvantages and advantages of outsourcing in comparison with insourcing.

Table 1. Advantages of insourcing and outsourcing

Insourcing	
Advantages: - Higher degree of control over inputs - Visibility over the process increased - Economies of scale/scope	**Disadvantages:** - High volumes required - High investment needed - Dedicated equipment has limited uses - Problems with supply chain integration
Outsourcing	
Advantages: - Greater flexibility - Lower investment risk - Improved cash flow - Lower potential labour costs	**Disadvantages:** - Possibility of choosing wrong supplier - Loss of control over process - Long lead times/capacity shortages - Intellectual property leakage

Source: adapted from Monczka et al. (2010)

Nevertheless, for this important decision, managers should also consider a variety of other factors that go beyond costs, such as supplier's competency, quality, delivery time, risk mitigation, technology, reliability and continuous improvement.

6.2. Why outsource?

Companies have always hired contractors for specific types of work, or to reduce their workload, and have formed long-term relationships with companies whose capabilities complement or supplement their own. (Johnson & Fearon, 2006)

There are many whys and wherefores that might influence a company to outsource. Such as:

- External supplier has better capability
- Freeing resources for other purposes
- Reduction and control operating costs
- Infusion of cash by selling assets to provider
- Reducing risk
- Lack of internal resources
- Desire to focus more tightly on core business
- Economies of scale
- Benchmark

In the early days, the most common reasons to outsource were cost or headcount reduction. In today's world the drivers are often more strategic, and focus on carrying out core value-adding activities in-house where an organisation can best utilise its own core competencies. Unfortunately, rarely is there a clear organisational focus for determining which activities are core activities or for determining strategic impact. (Griffiths)

6.3. Most important factors influencing success in outsourcing

The critical areas for a successful outsourcing programme are (The Outsourcing Institute Membership, 1998):

- Understanding company goals and objectives
- A strategic vision and plan
- Selecting the right, high quality supplier
- A properly structured, effective contract and contract monitoring
- Good relationship with the supplier

An important part of managing outsourcing is the consideration of potential exit strategies. There are many instances where outsources services have been taken back in-house – clear evidence that even if companies outsource they can eventually retain long-term control. (Baily et al., 2008)
Strategic objectives, such as outsourcing initiatives, must come from the top levels of a company. It is essential that both the company and the supplier have a clear and shared understanding not only of the specification but also of the goals and objectives, and that this understanding is translated into a workable strategic plan. Following the careful and rigorous procedures necessary for appointing an external supplier the contract should be well-designed and mutually acceptable. Managers are looking ahead and are aware of the responsibility for guaranteeing the success of their company's outsourcing initiatives. (Griffiths)
On-going management of the relationship is important and top management must stay involved during the implementation of the contract. Not only should there be a clearly defined escalation procedure, but management should meet at appropriate intervals to discuss the outsourcing relationship. Meetings should also be held at the operational level to address the workings of the outsourcing contract in practice, to identify and resolve any issues along the way, and agree on changes to ensure continued satisfaction.

6.4. Outsourcing dangers

It is commonly seen in companies which outsource that both customer and provider fail to appreciate the complexity of the contract and the resources needed to manage a structured relationship effectively. Implicitly this demonstrates a lack of meaningful engagement between suppliers and clients.
Continuous contract management is often non-existent or far too simplistic. As seen in the process framework, success lies in a personalised deal that is flexible enough to meet changing business models over the life of the contract. Active management of performance, service and relationship are vital to ensure that the jointly acceptable objectives are met.
Lack of planning. Planning deficiencies are often characterized by spare of the moment decisions rather than evaluated, discussed and purposefully executed and measured events. (McWilliams, 2010)
Wrong market forecast. It is possible that the company may estimate a high future demand than the market actually can support. This leads to high investments that need to be diminished in a short period of time.
Cash flow. Since many outsourcing start-ups require some capitalization, companies will use operating cash flow to build this business. Unfortunately this becomes a starving principal for growth. It robs the company of the necessary nutrients to grow and flourish. In addition, it also robs the operation and places excess demands on sales quotas which put the operation at risk. (Goolsby 2010)
Overspending. Companies might spend money where they think it makes sense but without a plan for how much should be spent and what the results should be the risk of overspending increases considerably. While there are uncertainties about results one should focus on those areas where a known degree of delivery can be seen as being produced.
Inadequate Learning Development. An essential part of company growth is to accommodate learning development. This involves not only the individual but also the company. Company learning deals with the strategic interest of the business while the individual's learning is of a tactical nature.
Communication skills. English may very well be the second language of an employer that communicates with the supplier. On a positive note the accent is apt to captivate and even cause the supplier to listen intently. This doesn't have to be over played, advanced presentations have to be prepared and also relying on supporting collateral is very important. (McWilliams, 2010).

Not enough drive/Too Much Drive. Everything in balance too little or too much enthusiasm can turn a supplier off. Too little drive might be interpreted as arrogance, laziness or a hidden agenda. Too much drive may indicate desperation.

As companies have gained more experience in making outsourcing decision and crafting outsourcing contracts, they have become better at applying sourcing and contracting expertise of these decisions. From writing the statement of work or request for proposal to defining the terms and condition, the success lies in the details.

6.5. Subcontracting

Subcontracting is a type of work contract that seeks to outsource certain types of work to other companies. Outsourcing is done with another company to provide services that might otherwise be performed by in-house employees.

The incentive to hire subcontractors is either to reduce costs or to mitigate project risks. Often the tasks that are outsourced could be performed by the company itself, but in many cases there are financial advantages that come from outsourcing.

Subcontracting offers a number of advantages but also disadvantages. Among the advantages, outsourcing allows work on more than one phase of the project to be done at once, often leading to a quicker completion. Also because subcontractors already have the expertise and equipment to provide the service, it is often much cheaper for them to do the work.

6.6. How to implement outsourcing – the outsourcing life cycle

Outsourcing should be implemented by using a process-driven approach when outsourcing provides a systematic look at the 'how-to' details of developing an outsourcing plan. The steps in the process need to be followed to ensure that the company is being thorough in the management of the outsourcing relationship. Because the components of the outsourcing process do not change over time or between projects, one thing that changes is the effectiveness and efficiency of the process.

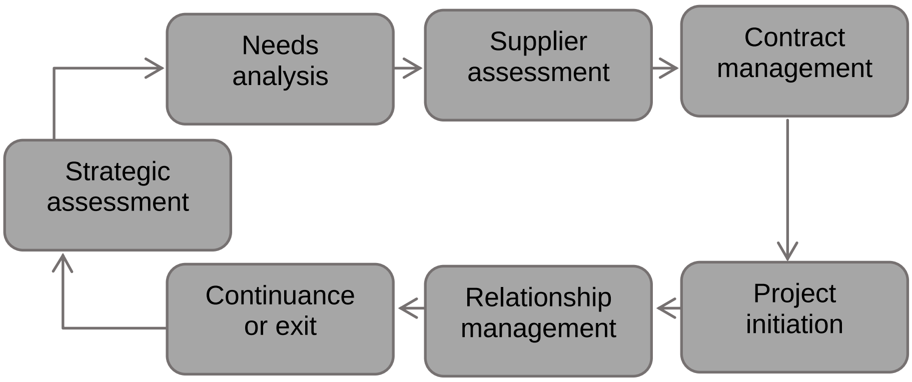

Figure 2. Outsourcing life-cycle

Source: adapted from Mark et al. (2008)

The framework should be used to move through outsourcing engagements and improved for better results. The outsourcing life cycle is made up of the following stages which are presented in the above figure:

- strategic assessment
- needs analysis
- vendor assessment
- negotiation and contract management
- project initiation and transition
- relationship management
- continuance modification or exit strategies

Each of the stages of outsourcing has subcomponents and sub processes that need attention. For effective outsourcing, the initiative must be evaluated in the context of the strategic posture of the company.

After completing the strategic assessment, the project solutions have to be identified as suitable for outsourcing. This involves prioritizing the company's needs by conducting a thorough needs analysis.

The third stage is one of soliciting, evaluating and choosing the vendor for the outsourcing needs. The vendor selection and contracting phase provides a structured framework to guide the company through critical supplier selection and contracting activities. Choosing the right supplier is very important as the chances are that if the company makes the right decision from the beginning the company will have a potentially lasting relationship, while choosing the wrong supplier could damage and ruin a well-intentioned outsourcing project.

Once a vendor was chosen, the next steps are to engage in negotiation and to reach an agreement about the details of the outsourced process. This is followed by the composition of the outsourcing contract.

The stage of project initiation and transition is the one where the Procurement department is most involved in. Here is where all the materials are delivered to the subcontracting company, issues are solved with the help of all involved departments, the outsourcing relationship is formed and the effectiveness and efficiency of the process is measured. The focus of this stage is to keep up to date with the outsourcing relationship. The relevant activities include evaluation of the relationship, problem resolution, communications management, knowledge management and process management.

Before implementing outsourcing some critical points need to be made. The outsourcing process is cyclical and it is important to follow through on each step in an organized manner. One of the reasons it is recommended to follow the steps in a structured way is that this greatly reduces difficult decision making while moving through the process.

6.7. When to implement outsourcing

The decision to outsource is very critical when doing business. The following scenarios come to aid when deciding to outsource (2011):

- When the company needs assistance with a particular function. Outsourcing a short-term job would not only be much cheaper but also easily sustainable.
- When the company needs to expand to meet the growing demand and deliver increasing number of orders in time, but there is a lack of infrastructure or resources to drastically upgrade, thus outsourcing is the perfect solution.
- When there is a need to start a new process in-house in a short period.
- When you need to transform an in-house process, it is advisable to outsource it on a short-term basis to allow the change to occur in a stable manner and once the operations are running smoothly and steadily, it can be transferred back home.
- When there is a skill shortage in a particular field, difficulty in finding right candidates coupled with high pay packages only underline the need for outsourcing. Moving the workload to skilled professionals who demand lower wages would result in huge savings for the company in terms of costs as well as quality.
- When a project or function is being inefficiently performed in-house for any reason, outsourcing would insure the company against the operational and financial risks.

7. CONCLUSIONS

Outsourcing is a powerful business strategy. By using it correctly, outsourcing indeed delivers benefits such as cost reduction, ability to focus on core business competencies, improved quality, superior skills and capabilities, reduced time and competitive advantages. Outsourcing is strongly bonded to Supply Chain Management and Procurement.

The need for collaboration between buyer and seller is recognised as the best way of improving costs, quality, delivery, time and performance, by joining efforts, sharing rewards and commitment to high quality. The supplier has a great impact on productivity, quality and competitiveness of the company. Outsourcing certain goods or services increases the flexibility, improves cash flow, decreases the investment risk and the potential labour costs.

The subcontracting project adds a value to the company as it allows the company to focus on core activities, reduce costs and increase efficiency, reduce the risk of in-house failure and by benchmarking offers the best practice sharing experience.

Disadvantages are the extra costs of managing the cooperation with external companies, the loss of control, the adverse impact on the flexibility of the company, the dependence and possible over-dependence on external partners, and the potential opportunistic behavior of partners. Negotiation and relationship-building skills are essential for building a good outsourcing relationship with the suppliers. Once the outsourcing project is under way, the user should put a lot of effort to ensure that what was agreed upon is actually occurring. To do this successfully, it is important to manage the relationship so as to achieve the company's objectives with minimal hostilities with the supplier.

Outsourcing has moves from initiatives that are financially motivated to a stage of being strategically motivated. In financially driven outsourcing efforts, it is common for a company to structure a long-term deal with a single supplier so as to get the best possible discounts and secure the most stable relationship. Strategic driven outsourcing efforts are capability and competency-intensive.[3]

Outsourcing can free resources for other purposes, can obtain an infusion of cash by selling assets to provider and can reduce costs and risk. Companies focus on carrying out core value-adding activities in-house where an organisation can best utilise its own core competencies. In order to decide if outsourcing is the best solution to implement, disadvantages and dangers of outsourcing need also to be taken into consideration.

In order to improve specialty literature in the field of outsourcing, it is recommended to continue the study of this issue, by focusing also on study cases in companies and comparative management studies between companies.

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