

# Outsourcing as a Decision Having a Strategic Dimension that Influences the Creation of Competitive Advantage of Companies

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Outsourcing is the conception of enterprise management, which involves using external resources and thus in the transfer to outside business partner implementation of specific processes in the enterprise. It is a concept that is gaining more and more followers among company managers. Currently, shall indicate the outsourcing as an element in shaping the business strategy of the company, whose aim is to achieve a competitive advantage. Outsourcing of logistics services is becoming a visible trend in modern business management because the company that order can reduce costs, reduce the number of investment and commitment of capital and allocate it to other purposes, to increase the level and quality of services and to concentrate on their core competencies, offering greater flexibility in adjusting offer to their customers. Outsourcing is based on the principles of a close partnership, and therefore confidence plays a very important role. The service provider takes over responsibility for the proper functioning of the outsourced areas of the company, in the case of full outsourcing - for the overall functioning. The paper attempt to present the stages of outsourcing evolution and forms of outsourcing. In addition, areas of implementation of logistics outsourcing, outsourcing implementation process and the benefits of its use are identified.

**Keywords:** outsourcing; logistics services; cooperation.

## 1. INTRODUCTION

Outsourcing is defined as contracting out a business process to a third-party in order to support own business processes<sup>1</sup>. Therefore outsourcing consists in using external resources that is handing over a completion of particular processes taking place in a company to an external business partner. The outsourcing of logistic services may be related to such fields as supplies, manufacturing, distribution, storage or transportation. The most important factors influencing the decision about implementing outsourcing in companies are: reducing the operating expenses of the company, using the knowledge of experts in a particular field without the necessity of employing them full time as well as access to licenses and most recent technologies not available in the company. At present it is considered as an element shaping the operations strategy of the company that aims to

achieve competitive advantage. In order to remain competitive companies try to focus on their fundamental activity, strategic competences that distinguish them on the market and, as a result, allow them to achieve competitive advantage. Thus, the conception of the activity called outsourcing is related to looking for external partners who are able to take over and manage effectively the rest of processes that are essential for the company to function successfully<sup>2</sup>.

The desire to distinguish departments that do not constitute the area of key activity is the main rationale for commissioning particular activities outside the company. Examples include storage, handling transport and activities related to distribution, book keeping, IT or cleaning and property protection services. As a result it is possible to contract activities out of the company and expect not only their higher quality from the external professional company, but also cost

<sup>1</sup> Corbett M. F., *The Outsourcing Revolution, Why It Makes Sense and How to Do It Right*. Addison Web, New York 2004, p.21.

<sup>2</sup> *Logistics*, Kisperska-Moroń D., Krzyżaniak S. (eds.), ILiM, Poznań 2009, p.223.

reduction. In case of manufacturing companies contracting out of the company not one or two logistic processes, but distinguishing logistic processes completely – ranging from collecting finished goods from production lines, storage to returns management, are becoming more and more popular.

## 2. THE ESSENCE OF OUTSOURCING

Outsourcing is very often defined as an undertaking consisting in distinguishing from the organizational structure of the parent company functions that it fulfills and contracting them to other business entities<sup>3</sup>. The term ‘outsourcing’ comes from the English ‘outside-resource-using’, which means isolating parts of the company or streamlining it. In contrast to a contract for specific work, outsourcing creates a completely new kind of relation between companies. This is not a supplier-consumer relationship, but a kind of a close cooperation that both parties are to benefit from. Outsourcing has been developing dynamically since the 1970’s. Ross Perot’s EDS (Electronic Data System) Company is believed to

be the pioneer in outsourcing<sup>4</sup>. In 1963 this company for the first time offered paid services consisting in handling IT functions of a company<sup>5</sup>. Ross Perot had an idea to purchase unused computational power of computers. At first the major argument for contracting some functions out of the company was cost reduction. Outsourcing was a natural consequence of globalization and increase in market competitiveness. International concerns that develop their activity on all continents have created structures made up of thousands of small partners, but themselves concentrated on the main strategic functions of their business. It was impossible to be good enough in everything in a more and more competitive and demanding environment<sup>6</sup>. The essence of outsourcing is seen in Henry Ford’s words: “If there’s something we cannot do more efficiently, cheaper or better than out competition there is no point of doing it and instead we should hire someone who would do a better job than us”. Outsourcing has become a solution supporting the completion of the strategy of the highest quality. Table 1 presents the stages of outsourcing development.

Table 1. Stages of outsourcing development

Outsourcing	The way it was viewed by a company	Functions delegated out of the structure	Characteristic feature	Character of cooperation
<b>First generation</b>	A way to reduce costs.	- tasks, activities that are parts of processes, - subprocesses,	- suppliers of outsourcing services using the scale effects, - having the possibility to acquire the necessary resources outside the company cheaper than in case of using own resources,	long-lasting contracts signed between the company and one supplier operating in the same area
<b>Second generation</b>	A way to focus on key activity of the company in order to achieve competitive advantage.	- processes that are not key ones for a company, - whole processes, - processes going beyond a single sector in a company and supported by using a high class technology.	- the business model undergoes transformation: a company defines its key competences, focuses own resources on their perfection; processes that are not key ones are outsourced. - competences acquired from outside the company support the accomplishment of strategic aims and outsourcing becomes an element of the strategy.	shorter contracts than in case of first generation outsourcing, for many companies the target model of activity is moving business processes to another country
<b>Third generation</b>	A way to ensuring company’s development and innovativeness.	- research and development departments, - marketing department and law sections.	- the supplier of services becomes a drive of change – it can provide new ideas, concepts and innovations, be the initiator of entering into a new market.	making contracts with several suppliers at the same time

Source: Own work based on: [www.brandnewday.pl/outsourcing](http://www.brandnewday.pl/outsourcing)

<sup>3</sup> Trocki M. *Outsourcing, the method of business activity reorganization*, PWE, Warsaw 2001, in: Jonkisz A., Jaroszyński, J., *Logistic outsourcing*. “Logistics” 2008, No. 6.

<sup>4</sup> Griffin R.W., *Elements of company management*, PWN, Warsaw 2002, p. 328.

<sup>5</sup> Trocki M. *Outsourcing, the method of business activity reorganization*, PWE, Warsaw 2001, in: Jonkisz A., Jaroszyński, J., *Logistic outsourcing*. “Logistics” 2008, No. 6.

<sup>6</sup> [www.brandnewday.pl/outsourcing](http://www.brandnewday.pl/outsourcing)

### 3. FORMS OF OUTSOURCING

Among various forms of outsourcing, it is especially important to differentiate between two forms, namely: contract outsourcing (external) and capital outsourcing (internal). We deal with external outsourcing when some of the company's functions are handed over for completion to an economically and legally independent business entity. In this case the company contracting the service has little influence on its quality<sup>7</sup>. The business entity that undertakes to complete the service operates under the contract (agreement). Very often external outsourcing means that a sector whose functions are to be outsourced outside the company is liquidated. We deal with internal outsourcing, on the other hand, in a situation when we isolate functions from the company in the form of a related daughter company. This means that sectors with isolated functions do not go into liquidation, but are transferred to a new business entity, that is the daughter company. The essence of internal outsourcing is transferring functions from the area of the organizational structure into the structure of a capital business activity. It is important for the isolated entity to have the ability to achieve advantageous and lasting hold on the market in its area of activity, which means that it should be able to achieve its economic goals, such as profitability and financial liquidity<sup>8</sup>. The daughter company is almost an independent entity, however, all of its own resources come from the parent company and the activity of such a company needs to be submitted to the decisions of the superior company. When it comes to cooperating companies we talk about economically and capital independent entities that together make up a service company whose aim is to provide outsourcing services<sup>9</sup>.

### 4. AREAS IN WHICH LOGISTIC OUTSOURCING IS COMPLETED

A company considering the possibility of using outsourcing services should conduct a detailed analysis of particular organizational units and answer the question concerning which areas of its activity it is competent enough and in which

areas its knowledge, experience and resources are insufficient to compete with other companies on the market. Outsourcing should be used when the external resources of higher quality are cheaper than the internal ones. Outsourcing can include such fundamental functions as: manufacturing of semi-finished products, distribution of finished goods, assembly of units, service (after-sale services) or functions support that have the task of supporting the strategy of the company including: external transport, storage, maintenance and equipment renovation or property protection and cleaning services. Examples of effective outsourcing of management functions are: accounting, human resources management, personnel recruitment and promotion. Therefore, all functions of business activity performed in the company's structure are the subject of outsourcing if there are conditions for their more effective and efficient completion under capital or contract structures.

Among the most often outsourced logistic services is, apart from transport and storage, co-packing. Co-packing is related to a number of different activities. It is not only making promotional sets or multipacks, but also pasting testers, folding and gluing fliers, laminating, packing, re-packing, printing labels and bar codes and placing them on products. Thanks to outsourcing the process of packaging and customizing to an external company, one does not have to take part in the whole complex process, but only in its initial phase, that is in the detailed decisions concerning the creation of promotional sets. Food, cosmetic and chemical industries are the ones that use this solution most often. Outsourcing co-packing is also used successfully by the IT sector and the press in which supplements and product testers are pasted into magazines and newspapers. Outsourcing co-packing is used by companies that do not have experience in completing this process in the so-called peak sales period, as during Christmas when the demand for products is higher. Another argument for outsourcing co-packing to an external company are costs. In order to go through this process the company has to incur costs related to space rental, purchase or rental of equipment as well as employment of qualified personnel. Outsourcing co-packing reduces the costs of labour. It is the operator who is responsible for the

<sup>7</sup> *Logistics*, Kisperska-Moroń D., Krzyżaniak S. (eds.), ILiM, Poznań 2009, p.224.

<sup>8</sup> Trocki M., *The outsourcing process*, Gospodarka Materiałowa i Logistyka 1999, No. 10, p.208.

<sup>9</sup> *Ibidem*.

organization and completion of a number of activities constituting the co-packing process<sup>10</sup>.

## 5. THE IMPLEMENTATION PROCESS AND CHANCES OF OUTSOURCING

The company which decides to outsource logistic activities to an external company should take into account that it will have to give up some or all control over some processes that are related to logistics. Cooperation based on partnership and trust plays here a key role<sup>11</sup>. Before making a decision about isolating some activities out of the company's structure, one has to make a detailed analysis not only of the circumstances of such isolation, but also of advantages and risks that result from it. Knowledge of law, organization and management as well as the ability to use model solution is essential here. Figure 1 presents an example of stages of outsourcing implementation used as an organizational solution in a company.

The model of outsourcing implementation presented by M. F. Cook has found application in case of small and medium-sized enterprise sector. This model was used as an inspiration in empirical research, but during the implementation process changes in the order of some stages have been made that were aimed at adapting it to the specificity of small and medium-sized enterprise sector.

Before a company decides to implement outsourcing, special attention should be paid to all costs and other aspects related to own processes and it should be considered to what extent the solutions to be implemented will facilitate and improve their effectiveness. In the cost analysis of the supply chain one should into account not only transportation costs, but also costs related to storage, management and frozen capital. When analyzing the benefits that the company may get as a result of outsourcing implementation, one should take into account not only financial, but also

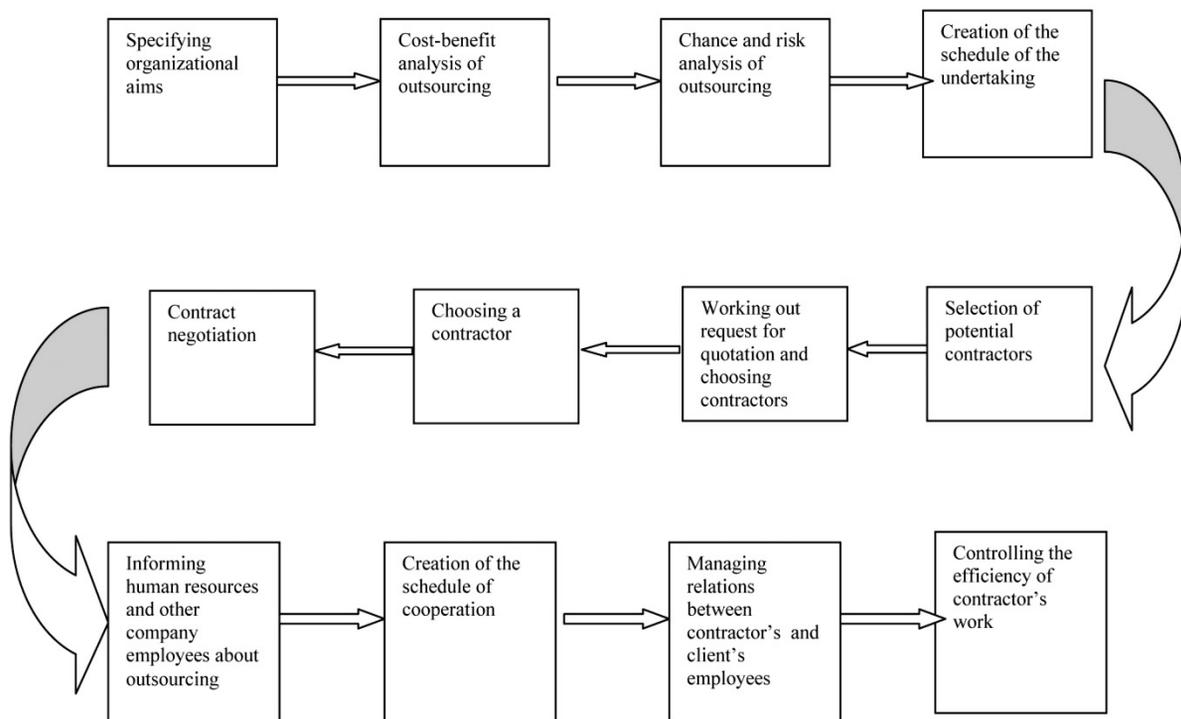


Fig. 1. The process of outsourcing implementation

Source: Own work based on: Majetun, M. The outsourcing process in the business practice of small and medium enterprises, in: Matwiejczuk W. ed. The dilemmas of business entities. Theory and practice at the beginning of the XXI century, Difin, Warsaw 2011, p. 121-139, quoted after: Cook M.F., *Outsourcing of human resources function*, Oficyna Ekonomiczna, Cracow 2003, p. 39.

<sup>10</sup> Why is it worth using outsourcing co-packing? TSL business 2010, no. 6, p. 18.

<sup>11</sup> Kawa A., *The Polish market of logistic services*. Outsourcing as a strategic orientation, Eurologistics 2002, No. 4, p. 25-26.

strategic aspects, such as accessibility of goods on the market or customer satisfaction. An important argument for the implementation of outsourcing in the company is also the predictability of cost base. When costs related to payments made to the

external company are known, it is possible to precisely evaluate budgets and plan costs more accurately – both in logistics and in the whole company<sup>12</sup>.

Contracting logistics services to a specialized external company by assumption aims to reduce costs of manufacturers and distributors' activity, but how much the company will save depends on, above all, operational possibilities and experience of the logistics operator and its mode of operation.

The decision to outsource logistics takes on an especially important meaning in case of sectors of the economy that have a seasonal character. As a result of this feature, there are months in which the company's activity increases and when there is an increased need for goods, but there are also months in which amount of labour is considerably lower<sup>13</sup>. The company that manages its logistic itself has to invest in storage space, workers and equipment to the same degree all year round. When the decision to contract the logistic operator is made, the company does not have to incur costs in periods when it is not necessary, and therefore can reduce them. Due to their seasonal character, some sectors of the economy require large capital expenditures

even during smaller demand for their products on the market. Using an external logistic operator the company can order its human and financial resources more effectively.

When taking the decision about using outsourcing one needs to conduct not only benefit analysis, but also analysis of risks related to its implementation. One of the major risks is defining needs and requirements towards the contractor erroneously. If we do not determine correctly what we want and what our expectations towards the service are, then the service offered by the external company may never satisfy us. Forming a strategic partnership requires good communication, creating a detailed plan of action and joint vision of both partners. Of course financial aspects favour outsourcing, but another important aspect that needs to be taken into consideration is the social aspect. Transferring a group of employees to the contractor's company, fear of being made redundant or fear of lay-offs of some employees are very important social aspects that must not be ignored. Table 2 presents examples of opportunities and threats related the implementation of outsourcing.

Table 2. Opportunities and threats of outsourcing

Opportunities	Threats
<ul style="list-style-type: none"> <li>▪ the possibility of reducing costs,</li> <li>▪ the possibility of concentrating on own business activity (on key activities),</li> <li>▪ increasing effectiveness, efficiency and flexibility of one's activity,</li> <li>▪ improvement of quality and productivity,</li> <li>▪ access to the knowledge of experts in a particular sector,</li> <li>▪ gaining access to skills and technologies not available in the organization,</li> <li>▪ the possibility of making use of permits and licenses owned by the company providing outsourcing services,</li> <li>▪ boosting the company's credibility thanks to the cooperation with prestigious partners,</li> <li>▪ exchanging fixed costs for variable ones,</li> <li>▪ reducing expenditures related to logistics,</li> <li>▪ increasing the possibility to react to changes in the environment,</li> <li>▪ improving the company's competitiveness,</li> <li>▪ simplifying organizational structures and procedures,</li> <li>▪ becoming aware of real logistics costs,</li> <li>▪ division of risk and responsibility.</li> </ul>	<ul style="list-style-type: none"> <li>▪ the possibility of losing control over some functions,</li> <li>▪ the possibility of losing valuable information,</li> <li>▪ errors in the stage of evaluation and selection of external entities,</li> <li>▪ readiness for partnership with all of its consequences (e.g. information limitation),</li> <li>▪ deregulation of relations between partners,</li> <li>▪ deterioration of quality of fulfillment of functions that so far have been fulfilled by the company itself,</li> <li>▪ prolongation of lead time,</li> <li>▪ becoming dependent on the external entity,</li> <li>▪ employment reduction,</li> <li>▪ having less regular contact with customer,</li> <li>▪ interferences in information flow.</li> </ul>

Source: Own work based on: Logistics, Kisperska-Moroń D., Krzyżaniak S. (eds.), ILiM, Poznań 2009; Companies specializing in the completion of logistics tasks, Żelewski Ł.K. (ed.), in Kozłowski R., Modern solutions in logistics, Sikorski A. (ed.), Oficyna Wolters Kluwer Business, Cracow 2009.

<sup>12</sup> Kowalczyk K., *Logistic outsourcing – for and against. Better or cheaper*. Logistic operators 2011, No. 1, p. 13-14.

<sup>13</sup> *Logistic outsourcing can help to reduce costs*, TSL business 2010, No. 5, p. 14.

The fundamental benefit resulting from contracting secondary and support functions to external companies that is the main argument for outsourcing mentioned so far is cost reduction. Other factors are important as well and these

include: aspiring for higher quality of services, focusing on the company's key activity and access to specialized knowledge. Outsourcing makes it possible to concentrate strengths, resources and managerial processes on the company's fundamental aims. The company achieves better results and its market value grows. What is more, the company increases the flexibility of its activity and, by saving time and human resources, its effectiveness as well. Outsourcing services provides the access to knowledge and experience of market leader and the worldwide data base.

A great change behind outsourcing is the possibility to constantly develop and improve the quality of a given product by using the know-how of the external contractor and its experience of many years. This advantage brings other benefits such as reduction of fixed costs resulting from the possibility to reduce the level of equity investment and using scale effects and the possibility of development of own key competences. As a result, the company has a chance to create a more flexible, less hierarchical organization that makes it possible to shorten the time of production cycle and a faster reaction to customer needs<sup>14</sup>. The abovementioned advantages result from a correctly carried out outsourcing implementation process. In order to achieve these advantages it needs to be remembered that the implementation of outsourcing in an organization is a complex process made of multiple stages, that requires detailed planning, analysis and risk management skills.

## CONCLUSION

In the past few years outsourcing has become an incredibly popular conception of company management that consists in isolating functions from the structure of a parent company and contracting them to other business entities. It is a conception that is gaining more and more advocates among company managers. Outsourcing is based on the rule of a close partnership and that is why trust plays a key role here. After all, a contractor takes over the responsibility for the proper functioning of commissioned areas of the company's activity and in case of complete outsourcing – for the general functioning of it. It needs to be added that such a cooperation requires

demands and the joint vision to be specified clearly by both parties. Outsourcing can take various forms – from the simplest ones to an advanced cooperation at a strategic level.

Outsourcing will bring benefits only if its implementations is preceded by a deep analysis of the inside situation in the company and its surroundings. A precise specification of key competences, the right choice of the contracting company and creating a structure enabling a peaceful and steady cooperation are factors deciding about the success or failure of this kind of cooperation. Entrepreneurs most often discern in outsourcing the possibility of boosting the effectiveness of ventures they undertake and improve quality, the possibility of focusing on key activity of the company and reducing costs that are allotted to non-productive sectors of the company's activity.

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<sup>14</sup> *Logistics beyond borders*, Abt S., Richter K. (eds.), Biblioteka Logistyka, Poznań 2000, p. 193.

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