

## STRATEGIC OUTSOURCING AND PURCHASING MANAGEMENT

### STRATEŠKO POVJERAVANJE DIJELA PROIZVODNJE VANJSKIM IZVRŠITELJIMA I UPRAVLJANJE NABAVOM

ZAVRSNIK, Bruno & VUKOVIC, Goran

**Abstract:** *Outsourcing is becoming more and more important in today's world. In the paper we will introduce a few models of strategic outsourcing which have been developed by various authors in the past few years. Our research activities are focused on the outsourcing in the Slovene firms, especially what the effectiveness of outsourcing depends on in these firms, activities of purchase given in outsourcing with the supplier in these firms and on the importance of different phases and elements in the process of outsourcing.*

**Key words:** *strategic outsourcing, global outsourcing, the model of strategic outsourcing, purchasing management, outsourcing suppliers*

**Sažetak:** *Povjeravanje dijela proizvodnje vanjskim izvršiteljima postaje sve važnije u današnjem svijetu. Strateško povjeravanje dijela proizvodnje vanjskim izvršiteljima je način stvaranja novih dugoročnih konkurentskih prednosti. U radu ćemo predstaviti nekoliko modela strateškog povjeravanja dijela proizvodnje vanjskim izvršiteljima koje su razvili različiti autori u nekoliko proteklih godina. U našem istraživanju fokusirali smo se na slovenska poduzeća. Posebno nas je zanimalo o čemu ovisi učinkovitost povjeravanja dijela proizvodnje vanjskim izvršiteljima u ovim poduzećima, te važnost različitih faza i elemenata u postupku povjere dijela proizvodnje vanjskim izvršiteljima.*

**Ključne riječi:** *strateško povjeravanje dijela proizvodnje vanjskim izvršiteljima, globalno povjeravanje dijela proizvodnje vanjskim izvršiteljima, model strateškog povjeravanja dijela proizvodnje vanjskim izvršiteljima, dobavljači vanjskim izvršiteljima*



**Authors' data:** Bruno Završnik, Ph.D., Faculty of Economics and Business, University of Maribor, Maribor, bruno.završnik@uni-mb.si; Goran Vuković, Ph.D., Associate professor Faculty of Organizational Sciences, University of Maribor, Kranj, goran.vukovic@fov.uni-mb.si

## **1. Introduction**

Outsourcing is not a new phenomenon; however its use over the last decade has expanded considerably because of its impact on the restructuring of companies. Companies have been actively using outsourcing more and more in order to increase their efficiency and become more competitive in the market.

Research in the area of strategic outsourcing and purchasing management done in North America and Western Europe has established that strategic outsourcing in connection with contemporary leading purchasing processes is a strong competitive tool, which has an impact on market conditions.

Global research on strategic outsourcing from 2004 and 2005 by the researchers Monczka, Markham, Carter, Blascovich and Slaughter from universities and institutes for researching purchasing management in North America, Europe and Asia (CAPS, 2006) had established a similar outcome.

Purchasing management has changed incredibly over the last three decades. This has happened especially because of the computer revolution, electronic commercialization, the increase in international competition, new types of management and because of strategic cost management.

Today, we should expose the following development trends in purchasing (Giunipero, 2004):

- strategic relations management with suppliers,
- strategically reducing costs,
- integrated management systems and cooperation,
- stronger focus on costs and selection of suppliers,
- stronger strategic purchasing orientation versus tactical orientation,
- outsourcing,
- e-purchasing systems,
- efficiency in making purchases,
- the need for greater management capacities of employees and managers,
- the focus of purchasing on the supply chain process,
- the construction of internal and external relations with buyers,
- crosswise-functional project teams,
- global purchasing strategies.

## **2. The role of purchasing when deciding about outsourcing**

The role of purchasing in a company has changed and increased over the last years. Managers have recognized the decisiveness of purchasing when forming the costs and as a consequence the profits of the company.

Information technology had a significant impact on this as it increased the transparency, control and management over purchasing, where they started to look at it as a function, which contributes its share to the added value of the company.

Historically speaking, the purchasing function includes providing goods and services from suppliers. The importance of purchasing increase with the growth in the value of goods and services purchased. With the increase in the use of outsourcing the

quantity of raw materials and services needed for production is reduced, whereby the needs for some purchasing activities typical for the purchasing function are consequentially reduced. As a result of this efficiency of the purchasing function becomes more crucial for company business operations.

Ever since the role of purchasing has been included in the strategic role of supporting the competitive position of a company, the role of purchasing also includes: co-ordinating suppliers, the research of upstream markets, cost analysis, creating an upstream strategy, benchmarking, make-or-buy decisions and an analysis of supplier capabilities.

This evolution in development has an impact on the position of the purchasing function when forming the competitive strategies of a company.

Purchasing can contribute to the achievement of strategic planning (Giunipero, 2004)

- monitoring trends in upstream markets,
- interpretation of trends in upstream markets,
- looking for the materials and services needed.

We have concluded that from the basic responsibilities of the purchasing function the following adapted purchasing activities within the strategic outsourcing process can be developed (Svenšek, 2006):

- a) giving an incentive/suggestion for outsourcing (development of new products, selection of new technologies);
- b) researching the market for suppliers of outsourcing and gathering other relevant information;
- c) analyzing the data of potential suppliers for outsourcing;
- d) participating in the selection for the most suitable supplier for outsourcing;
- e) participating in the decision making for strategic outsourcing;
- f) negotiating with the suppliers of outsourcing;
- g) entering outsourcing contracts;
- h) participating in and organizing the transfer into outsourcing;
- i) control over the operative implementation of outsourcing in accordance with the goals and plans of outsourcing;
- j) aid in monitoring and measuring the economic-financial efficiency of outsourcing;
- k) cooperating in the building of business partner relations;
- l) aid in resolving disputes with outsourced suppliers;
- m) informing other company management functions company about the finding regarding outsourcing;
- n) cooperating in the termination of cooperation or prolonging the contract with the outsourcing supplier.

When outsourcing is used as a system the role of purchasing really differs from traditional outsourcing. The integration nature of new systems will require different employee abilities and a new generation of managers will be needed (Giunipero, 2004).

In their research in 2004 (164 companies from 24 different industries and 12 countries, mainly from North America, Western Europe and China), PS Research and

A.T. Kearney, Inc. established the level of involvement of purchasing in the process of strategic outsourcing according to different activities in a company.

The results of the research showed that the role of purchasing in strategic outsourcing is (Monczka, et al., 2005):

1. Of key importance for decisions linked with activities on the purchasing side (purchasing management, production operations and distribution);
2. Moderately important for decisions linked with the operative support activities of companies (call centres for sales, external sales units), in some developmental-technological activities of the company (development of products, engineering and design) and in some general activities of the company (human resources, information technology, finance and accounting);
3. Less important for decisions linked with some sales activities (sales and marketing), some developmental-technological activities (research) and some general activities of the company (law).

In 1999 the Greek research team of Laios and Socrates (1999) researched the level of involvement of six business functions (purchasing, production, technique, engineering, finance and sales) and five hierarchical levels of decision making (owners, the management board, executives, managers and company employees) with a sample of 85 companies when making a decision about strategic outsourcing. They established that a low level of complexity for products and services and a low level of risk are characteristic for products and services that stayed in the company after deciding on outsourcing.

The decision was adopted mainly by managers and executives in production. A high level of complexity in the products and services and a high level of risk are characteristic for products and services that were outsourced.

The decisions were most often adopted by top level managers and executives, especially based on the opinion of the technical departments.

They established that purchasing when deciding on strategic outsourcing is not of crucial importance. At this point, the role is significantly reduced regarding completely new products and services, which are more complex and represent a high level of risk.

Experience has shown that only purchasing in outsourcing can help reduce costs (Brown 2005):

- the price of delivery and services by 10 to 25% as a result of strategic outsourcing;
- administrative costs by 50 to 75%;
- consumption and expenditure by 10 to 20 %.

### **3. Strategic outsourcing research from the standpoint of purchasing management**

The research included 77 Slovene companies. The questionnaire was completed and returned by 47 of them or 61% of those participating.

The arrangement of the sample according to group activities showed that 53% of the companies that participated were manufacturing companies, 34% retail companies and 13% service related companies.

With the research we wanted to try to establish, which activities do the companies intend to outsource. We established that the majority of the companies intend to outsource security activities of a company (26%) and health and safety activities (21%). 19% of the companies intended to outsource informatics, transport, legal services and dealing with manufacturing services.

The purchasing function stands out as no companies intend to outsource these activity.

	Number of Companies	% of Companies
Security services	12	25,5
Health and Safety and Work	10	21,3
Informatics	9	19,1
Transport	9	19,1
Legal Services	9	19,1
Manufacturing Services	9	19,1
Cleaning	7	14,9
Production of semimanufactures	7	14,9
Logistics	6	12,8
Finance in Accounting	5	10,6
Distribution of Products	5	10,6
Research	5	10,6
Specialized Technological Know-How	5	10,6
Human Resources	4	8,5
Food and Cafeteria Services	4	8,5
Sales	4	8,5
After-Sales Services	4	8,5
Development of Products and Services	3	6,4
Other: Marketing	1	2,1
Purchasing	0	0,0

Table 1. Activities that the companies intend to outsource over the next few years

Foreign research shows that companies are going to increase their outsourcing activities for up to 15% over the next few years (Monczka, et al., 2005).

The intention for a company to decide on outsourcing is linked with the reasons for and against outsourcing and this is why we asked the participants what their reasons for and against were.

The companies who were surveyed (3 companies did not reply) stated the following as the most frequent reasons against deciding on outsourcing. „the main company activities are not outsourced“ (57% of the companies surveyed), „loss of control over performing activities“ (48% of the companies surveyed), „policy/philosophy/culture of the company“ (39% of the companies surveyed), „possibility that the supplier

becomes a competitor“ (30% of the companies surveyed) and „the size of the company“ (30 % of the companies surveyed).

For a comparison, Australian research in 2004 showed that the most frequent reason against outsourcing is the loss of control, the uncertainty of cost savings and fear of losing business secrets (Beaumont, et al., 2000).

The companies stated the following as the most frequent reasons for outsourcing: »reducing operating costs“ (75% of the companies surveyed) „increasing the productivity of the company“ (62% of the companies surveyed), „increasing the flexibility of the company“ (57% of the companies surveyed), „increasing profits“ (55 % of the companies surveyed), „improving the quality of products and services“ (53% of the companies surveyed), „improving end-consumer satisfaction“ (53% of the companies surveyed) and „focusing on the key activity or company activity“ (51 % of the companies surveyed).

American research on global outsourcing included a sample of 270 countries from North America, Europe and The Middle East and it established that the primary reasons for outsourcing are the following: reducing costs, improving quality, access to worldwide technology, improving deliveries and reliability, access to goods abroad, access to foreign markets, achieve satisfactory flexibility for satisfying market demands, access to resources, which are not accessible at home for specialized know-how and capacities for particular activities, implementing a capital fund, available for more profitable activities and the battle for the implementation of domestic competitive supply (Elmuti, et al., 2000).

#### **4. Conclusion**

Most business people around the world are interested in ways of seizing opportunities and challenges which outsourcing creates. Strategic outsourcing is the way of creating new long-term competitive advantages.

Regardless of the strategic goal of outsourcing companies must completely understand the consequences of implementation of outsourcing which are essential for achieving success.

Outsourcing is researched from the point of view of purchase management and the role of purchase when deciding about strategic outsourcing and its management.

Foreign research in the area of strategic outsourcing and purchasing management are based on the knowledge and experience of big, international companies, which in most cases originate from the developed world and use outsourcing as a tool in less developed countries.

The smallness of Slovenia and as a result the smallness of the Slovene market has an impact on the size of Slovene companies, which usually do not represent a comparable quantity according to international standards until they become part of some bigger foreign companies.

Slovene economic conditions are specific because of Slovenia's own path within the conditions of economic transition, which are present today in globalization processes and Slovenia's entrance into the system of the European Union.

The role of purchasing is linked with the role of purchasing management in the outsourcing process.

## 5. References

- Beaumont, N. & Amrik S. (2004). Outsourcing in Australia. *International Journal of Operations & Product Management* Vol. 24 No. 7, 688-700 ISSN: 0144-3577
- Brown, D. & Scott W. (2005). *The Black Book of Outsourcing*. John Wiley & Sons, Inc. Chichester
- CAPS: Center for Strategic Supply Research. (2006). *Strategic Supply Management at Japanese Companies*. Supply Management Research Group, Japan., Available at: [www.capsresearch.org/publications/reports.cfm](http://www.capsresearch.org/publications/reports.cfm) Accessed: 2007-10-05
- Elmuti, D. & Yunus K. (2000). The effects of global outsourcing strategies on participants' attitudes and organizational effectiveness. *International Journal of Manpower*. Vol. 21, Issue 2. 112-128. ISSN: 0143-7720
- Giunipero, L. & Robert B. H. (2004). Purchasing Education and Training II. CAPS Research. Available from [<http://www.capsresearch.org/publications/reports.cfm?Section=1>] Accessed: 2007-07-06
- Laios, L. & Socrates M. (1999). An Empirical Investigation of Outsourcing Decisions. *The Journal of Supply Chain Management* Vol. 35 No. 1, pp.1-33. ISSN: 1523-2409
- Monczka, R. Trent, R. & Handfield, R. (2005). *Purchasing and Supply Chain Management*. Thomson South-Western. ISBN: 0-324-02315-4
- Svenšek, V. (2007). *Model strateškega outsourcinga z vidika managementa nabave*, Magistrsko delo, EPF. Maribor.