

Determinants of Logistics Outsourcing: A Review of Relevant Literature

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Abstract

Outsourcing is currently ongoing through stage of unstoppable growth. Logistics is the most famous function of outsourcing. Outsourcing has emerged as one of the popular and widely used business strategy of this globalized era. After exhausting the traditional modes of cost cutting, outsourcing has become the most favored avenue for cost cutting. In the light of increasing competition and potential economic benefits in the logistics sector, the objective of this paper is to examine the determinants of logistics outsourcing and identify the key factors that are required for a successful a logistics hub. For the logistics hub, the analysis on the determinants of competitiveness is made using literature which are presented information about logistics outsourcing.

Keywords: Logistics Outsourcing, Determinants

Paper type: Model Development.

Introduction

Many companies in 21st century following the trend of increased outsourcing or they are rationalizing their existing outsourced logistics or manufacturing operations because companies can minimize their cost and also maximize the value of the company. As an example, it is no secret that the world's 'most successful companies such as Apple, P&G and UPS have achieved their success to logistics and other business process outsourcing. As the information that mentioned above the logistics outsourcing means simply, a management tool that is used to make the company's operations that have done in-house are doing by outdoor parties.

Most of authors have written more information about logistics outsourcing. Followings are some valuable information saying about logistics outsourcing. Anderson and Norrman (2002) note that the same basic phases are identified in the logistics outsourcing literature as are outlined are typical processes available

in the purchasing literature. But, now it has represented requirements such as selecting suppliers, establishing contracts, ordering services and evaluating suppliers. Although logistics outsourcing represent the third party operations it is not limited to manufacturing operation and it has expanded from backroom function to strategic boardroom function, (Sheng, 1998).

Currently this growing concept is developing because of following reasons. As well as, there is a growing need to responsive to customer and market demand, logistics activities involve a large commitment of capital. The logistics function can be the key facilitator in cross functional effort towards supply chain integration. This paper is related to problems that Sri Lankan companies facing because of outsourcing their logistics and we are going to investigate about what are the problems facing by Sri Lankan companies because of logistics outsourcing and what are the solutions which we propose. This paper is referred to identify that the determinants affect for logistic outsourcing.

This paper is mostly based on literature of determinants or factors of logistic outsourcing. Therefore, more literature have collected for the base of the paper and there is a wide analyze of those literature and finally, the determinants or factors which are affected to the logistic outsourcing are identified as a conclusion.

Literature Review

Outsourcing means simply, a practice used by different companies to reduce costs by transferring portions of work to outside suppliers rather than completing it internally. Outsourcing is an effective cost-saving strategy when used properly. It is sometimes more affordable to purchase a good from companies with comparative advantages than it is to produce the good internally. An example of a manufacturing company outsourcing would be Dell buying some of its computer components from another manufacturer in order to save on production costs. Alternatively, businesses may decide to outsource book-keeping duties to independent accounting firms, as it may be cheaper than retaining an in-house accountant.

Outsourcing is spread for various factors such as manufacturing, marketing, information systems, communication, cleaning services, transportation, and other logistics and etc. This paper is about logistics outsourcing because these days organizations are mostly entering for outsource their organizational functions and logistics is most popular among those functions.

The logistics outsourcing means simply, a management tool that is used to make the company's operations that have done in-house are doing by outdoor parties. Although the simple meaning for logistics outsourcing is like that, most authors have defined the term Logistics Outsourcing in various ways. Kumar(2007) says that logistics outsourcing is generally a long-term activity requiring both parties to manage medium and long-term uncertainties, good relationship helps inbounding them together even for short term too, and thus good relationship encourages expanded outsourcing. Not only that, but also others have defined as outsourcing can be described as the process of purchasing goods or services on specification, from an external supplier, that were previously produced in-house (McIvor, 2011).

Leading companies have already recognized opportunities for efficiency through global sourcing and manufacturing and for increased market share and revenues via entry into overseas markets. Global distribution, while more complex, has become a necessary logistics function for many other companies. (Kant Rao Richard R. Young, 1994). The outsourcing of logistics services to partners, known as "third-party logistics providers" has increasingly become a powerful alternative to achieving competitive advantage. The outsourcing phenomenon has been increasingly receiving attention both from academic and practitioners (Gakure, 2014).

Followings are some ideas about determinants of logistic outsourcing researched by several authors.

Cost, strategy and politics

As they have said like above, Rom(2006) said that there are three major categories of motivations for outsourcing: cost, strategy, and politics. The first two commonly drive outsourcing by private industry. Political agendas often drive outsourcing by public organizations. . Factors which may impact the decision of which function to outsource are represented by four variables: strategy, cost, function characteristics, and business Environment (Rom, 2006). It explores how outsourcing decisions (type of outsourcing, level of outsourcing, reasons for outsourcing, and factors in outsourcing success) in firms from diverse industries, and of varying size, affect eventual outsourcing processes (Akbari, 2013).

Omta(2010) has discussed that the cases indicate that cost reduction is one of the outsourcing considerations, and companies with food quality, speed or

flexibility priorities prefer to keep an activity in-house. This result partly fits with previous studies. Mentions that outsourcing of basic logistics functions is based on operational and cost-based reasons: study outsourcing of maintenance, repair and overhaul in airline industry and concluded that the low-cost airlines and new airline entrants preferred outsourcing of all maintenance, repair and overhaul activities. However, companies with food quality or flexibility priorities prefer to keep an activity in-house because they worry logistics companies have limited knowledge of food quality management or lack of flexibility.

Uncertainty

In the field of logistics, which features of transaction explain the decision outsourcing? The goal here is to analyze the specificities linked to the nature of transaction costs as well as transaction characteristics in our particular field. (Franzil, 2008). Both internal and external uncertainties appear to be closely linked in the field of logistics. Internal uncertainty has to do, for example, with the difficulty of companies to estimate precisely their future needs, particularly when it comes to volume the primary effects of uncertainty are twofold: industrial and commercial destabilization. Relocations and the specialization of production units and Just in Time particularly, upset the traditional models of logistic (Franzil, 2008).

Quality service and risk control

As per Gakure(2014) the conceptual framework adopted for this study presupposes those factors that influence logistics outsourcing to include cost reduction, quality service and risk control. Determinants of logistic outsourcing which include: compatibility, cost, quality, and reputation. Outsourcing can Improve the Quality delivered by IS services. There are several reasons for this. For example, the provider can access more advanced technologies and count on more motivated staff and better management systems in order to be able to achieve a better service coordination or control, or, simply, is more strongly committed than the internal staff to make the alliance with the client work properly (Reyes Gonzalez, 2009).

As well as,Llopis(2010) has mentioned that, it is precisely the fast pace of change in the field of technology that places firms in front of a dilemma: either making investments on new technologies very often or working with very mature technology. This problem can equally be minimized with technological outsourcing, since the technology accessed by the client is owned by the

provider, which means that this risk is assumed by the latter and not by the former. Firms can increase their level of flexibility through a process of continuous redesign of the contracts that will help them to cover their information requirements.

Long-term relationship

At the second level, the criteria which support the achievement of the upper-level determinants also known as dimensions are also identified. These dimensions are long-term relationship, operational performance, financial performance and risk management. (Agezzoul, 2007). Ankit Vijayvargiya A.K. Dey(2010) has said, at the second level, the criteria that support the achievement of the upper-level determinants – named as dimensions – are identified. These dimensions Are long-term relationship, operational performance, financial performance and risk management

Transaction cost

Drawing on transaction cost economics theory, the sourcing decision is often seen as a rational decision made by firms that have considered transaction related factors such as asset specificity, environmental uncertainty, and other types of transaction costs. Whenever an activity is conducted under conditions of high uncertainty, or whenever an activity requires specific assets, transaction costs, the costs of writing, monitoring and enforcing contracts, are likely to be high. When transaction costs are high, outsourcing is deemed to be relatively inefficient compared with internal, hierarchical administration (Solli-Sæther, 2005).

Core Competency

An another author who is Kant Rao Richard R. Young(1994) says about the determinants of logistics outsourcing that is The degree to which such offerings may be employed by major importing and exporting firms depends on several factors influencing the economics and utility of those services and five key factors emerge as interacting drivers in the decision of shippers to either utilize third parties or retain in-house capabilities to execute logistics international functions: (1) Centrality of the logistics functions to core Competency; (2) risk liability and control ;(3) operating cost/service tradeoffs ;(4) information and communications systems ;(5) market relationships.

Activities, which are not core competencies, should be considered for outsourcing with best-in-the-world suppliers. Some non-core activities may have to be retained in house if they are part of a defensive posture to protect competitive advantage. Although some authors indicate characteristics of core competencies, most of the literature on this subject seems tautological – core equals key or critical or fundamental (Solli-Sæther, 2005).

Logistics outsourcing is also able to reduce cost and allow firms to pay more focus on their core business activities which directly impact their market positioning. Other than these factors, there are also firms which outsource logistics activities to avoid investment in specific areas thus allowing them to focus on core competence areas which will determine their business success. (ZAYZAN, 2011).

Flexibility

The great change experienced by technology in recent years gives many firms a chance to obtain a considerable advantage from outsourcing, as they will prevent becoming technologically obsolete without having to make large investments in technology. Business organizations can increase their flexibility through a continuous redesign of their contracts that will allow them to meet their information needs at any given time. Outsourcing additionally provides a large degree of flexibility in the utilization of IT resources and makes it easier to face business level volatility, as the provider is left to deal with fluctuations in IT workloads (Llopis, 2010).

Reputation

As well as, in the field of logistics, in the case of product distribution, for example, the degree of frequency can provide information if the volume of merchandise hauled is high enough to justify the cost of specific in-house equipment (Franzil, 2008). Ankit Vijayvargiya A.K. Dey(2010) have wrote that the analytic network process (ANP) for the final selection of the 3PLs providers can also be applied. This tool classifies the criteria in three levels. The first one contains strategic criteria – determinants – which are: compatibility, cost, quality, and reputation.

The foregoing discussion indicates that the decision to outsource depends largely on the characteristics of the user firm. Eight such characteristics, namely, size, financial strength, degree of centralization, degree of corporate control, degree of formalization within the logistics function, extent of IT use, industry type, and

managerial level at which outsourcing decision are made, seem to play important role in the outsourcing decision. In addition to that, service providers understand the importance of these attributes in a competitive business environment and give due attention to them in developing their marketing strategies, they are likely to lose out to their more proactive competitors. (Sheng, 2008).

Technology

Outsourcing brings client firms advantages related to technology, as these business organizations can have access to specialized, state-of-the-art technology which is supposedly supplied to them by the provider. On the other hand, the efficient use of outsourcing will most probably reduce the need to make investments in mature technology, simultaneously increasing the availability of resources related to new technologies for the client. Additionally, the most “timid” organizations – which prefer to wait and see what happens with state-of-the-art technology – may resort to outsourcing as a way to minimize the risks incurred if the technology used is not the most appropriate. In this respect, outsourcing is likely to emerge as a way to experiment with new technologies (Llopis, 2010).

Llopis(2010) says, when a service is outsourced, clients gradually lose their understanding of the service over time. Even if the provider delivers innovative services to the client, a large proportion of the new knowledge required remains in the hands of the provider and cannot be transferred to the client. What is more serious, the firm may lose its capacity to stay up to date with the technological breakthroughs. Furthermore, the innovation capability of the firm itself can be reduced, since every innovation requires a sufficient availability of technical and economic resources, something that is not precisely favored by outsourcing

Experience, fashion

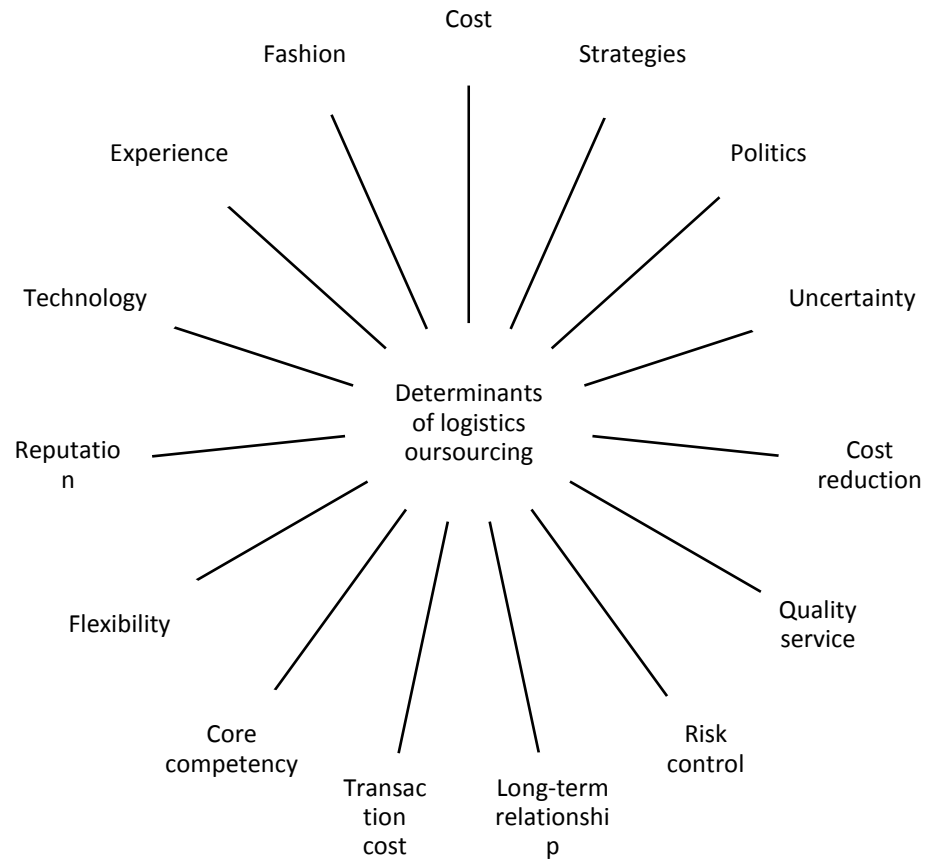
Followings are the determinants of value added outsourcing presented by Williams(2009). Those are, experience, high risk, potential to offshore, high need of proximity to customers, opportunity for cost saving.

Organizations are doing more outsourcing than ever before and managers are in desperate need of information in an organized form that will help them identify opportunities, challenges, and decision factors related to outsourcing. According to the literature of the determinants of logistics outsourcing there are so many determinants affecting to the success of logistic functions. There is a successful

investigation about determinants of logistics outsourcing and a collection of information.

This last argument is not a trivial one firms decide to adopt outsourcing in order to copy the success of other organizations that have already outsourced. In addition to this imitating behavior, consideration should be given to the pressure exerted by the providers of these services, the positive attitude of the Stock Exchange toward the phenomenon of outsourcing, and the great coverage in the popular press as well as in the economic press which have made outsourcing become a really 'fashionable' management form (Reyes Gonzalez, 2009)

According to the information which are several authors have discussed about the determinants of logistics outsourcing. Each of them have identified something new ideas in addition to past. The following figure shows that the determinants which are identified by us using the literature which is pointed out the determinants of logistics outsourcing.



Summary

This research contributes to identify the determinants that are affecting to the logistics outsourcing decisions. Here, there are many research papers have collected and discussed above. Authors have pointed out the determinants of logistics outsourcing by using their researches in literature. In common, most researchers have identified as determinants of logistics outsourcing such as cost, strategy, core competency, politics, uncertainty, technology and long term relationship. In addition to that, there are many new determinant factors have identified by other researchers. They are, quality service, risk control, flexibility, reputation, experience and fashion. So, there are new needs have pointed out in addition to traditional outsourcing needs to the help of organizations to achieve their new coming goals and future benefits by reducing operational risk, cost and other barriers in logistics.

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