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The supplier's side of outsourcing: Taking over activities and blurring organizational boundaries

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A B S T R A C T

Since most of the literature on outsourcing focuses only to the buying (outsourcing) company, this paper aims to highlight the supplier's side from a relational perspective. The paper stresses the importance of business relationships between suppliers of outsourced activities and their customers. The paper's purpose is specified in two research questions: (1) how is value created within outsourcing and (2) how does the supplier interact with the outsourcing company? Our method relies on an in-depth qualitative case study of Logoplaste, a Portuguese packaging company which supplies large consumer goods manufacturers through complex outsourcing activities. Our analysis identifies three key dimensions of outsourcing relationships: (1) value co-creation via inter-firm coordination (as opposed to unilateral externalization of activities); (2) mutual dependence between supplier and customer due to the supplier's taking over activities; and (3) the blurring of organizational boundaries because of mutual dependence. These dimensions manifest themselves, even though in different degrees, after the initiation of any outsourcing relationship: these variables are new to the literature on outsourcing, which focuses on the ex ante dimensions that influence the customer's pre-relational choices such as "make or buy" and relationship type.

1. Introduction

Since the 1990s outsourcing has become a widespread phenomenon (Quinn & Hilmer, 1995; Rodríguez & Robaina, 2006). This practice can be defined as "…the external contracting of determined non-strategic activities or business processes necessary for the manufacture of goods or the provision of services, by means of agreements or contracts with higher capability firms to undertake those activities or business processes…" (Rodríguez & Robaina, 2006: 52). The activities being outsourced range from IT services (Mahnke, Overby, & Vang, 2005) to healthcare provision (Roberts, 2001) and from manufacturing to logistics (Ram, Sriram, & Ravi, 2010). The growing body of research on outsourcing (for a review see Araujo & Spring, 2006; Contractor, Kumar, Kundu, & Pedersen, 2010; Holcomb & Hitt, 2007; Rodríguez & Robaina, 2006) focuses on the outsourcing company and analyses such issues as its "make or buy" decisions and selection of suppliers (see De Fontenay & Gans, 2008; Tate & Ellram, 2009; Tate & Ven der Valk, 2008; Verwaal, Commandeur, & Verbeke, 2009) or of offshoring countries (Demirbag & Glaister, 2010). As Contractor et al. (2010: 1430) point out there is a dearth of studies that focus on the "other side" of outsourcing, namely the supplier (see for an exception Yuan, Zelong, & Yi, 2010). There are even fewer studies that explicitly focus on the buyer–seller relationship (Anderson, Håkansson, & Johanson, 1994; Håkansson & Snehota, 1995) between outsourcing companies and their suppliers (for two exceptions see Tate, Ellram, & Brown, 2009; Zineldin & Bredenlöw, 2003). The purpose of this paper is to (1) highlight the supplier's perspective on outsourcing, and thereby to approach this phenomenon from the supplier's side; and (2) stress its relational and inter-organizational nature.

In order to accomplish this purpose we conducted an in-depth case study centred on Logoplaste, a firm supplying packaging operations via factories located wall-to-wall with customers, via close and long-term buyer–supplier relationships. The Logoplaste case provides a good empirical setting to investigate how suppliers provide complex outsourced services and how the boundaries of the supplier's organization become diffuse as a result of the ongoing relationship. Large investments and adaptations, in the form of mini-factories fully tailored to each customer, reduce Logoplaste's flexibility. However, this type of outsourcing relationship and its physical proximity provide a drastic reduction in distribution and inventory costs for both parties, and enable continuous interactive processes for solving operational problems on both sides of the relationship.

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Therefore, this case study suggests two specific questions that further specify the paper's purpose and help penetrate the supplier's perspective on outsourcing: (1) How is value created within the frame of outsourcing; and (2) How does the supplier interact with the outsourcing company? The first question focuses on the re-distribution of activities between the two involved parties, stressing that suppliers “take over activities” from the outsourcing company (Dubois, 1994). The second question focuses on the business relationship between the supplier and the outsourcing company (Ford, 2002; Håkansson & Snehota, 1995), and namely the mutual high dependency and the “blurring of organizational boundaries” that it implies.

Our analysis contributes to the outsourcing literature in two major ways: (1) expanding the focus from the unilateral setting of organizational boundaries by and within the outsourcing company (cf. Contractor et al., 2010) to what actually happens between the boundaries of the outsourcing company and of its supplier; (2) identifying three key dimensions of outsourcing relationships (value co-creation via inter-firm coordination, mutual dependence due to interlinked activities, and blurred organizational boundaries), which become salient after the initiation of such relationships, while the outsourcing literature focuses on the choices (including the selection of relationship types, Mudambi & Tallman, 2010) made by the outsourcing company before their initiation. The remainder of this paper is arranged as follows: the next section reviews the literature on outsourcing and business relationships. Then we discuss our method and present the Logoplaste case. The case is then analysed and discussed in order to extract three propositions related to our research questions. The paper concludes with suggestions for further research and managerial implications.

2. Theoretical review

Our literature review starts from established theories on outsourcing and stresses how they focus on the outsourcing company while neglecting the supplier's perspective. Therefore, we introduce a theoretical frame that accommodates this perspective by stressing the importance of buyer–seller relationships, namely the IMP (Industrial Marketing and Purchasing) view. We then discuss how outsourcing blurs the boundaries of the firms involved and entails simultaneously externalizing and taking over activities, while linking them in new ways.

2.1. From outsourcing decisions to building business relationships

According to Rodríguez and Robaina (2006: 52), outsourcing implies divesting resources and capabilities applicable to perform important value-creating activities as other firms can perform them better. Such improvements include economies of scale or operations in low-cost countries that can reduce product cost (Dabhilkar, Bengtsson, von Haartman, & Åhlström, 2009). Most studies agree that outsourcing impacts the boundaries of the firm because some activities are acquired externally (Rodríguez & Robaina, 2006). Therefore, the literature has focused on the discrete decisions on how to set the boundaries of the firm through “make or buy” choices. Several authors (e.g., Holcomb & Hitt, 2007) point out that transaction cost economics (TCE, cf. Williamson, 1986) dominates as an explanation for outsourcing and boundary-setting decisions: low uncertainty, low transaction costs and low risk of opportunism make it more cost-efficient for a firm to perform transactions on the market rather than in-house activities (Coase, 1937).

However, whereas TCE focuses on transaction-specific “make or buy” decisions, the issue of boundary setting should be viewed in a broader and dynamic context, embracing both the historical development of a firm's internal capabilities and their connections to those of external counterparts (Mota & de Castro, 2004). There are accordingly also other theoretical approaches to analysing outsourcing, including the resource-based view (RBV), knowledge-based perspectives and industrial networks (Mota & de Castro, 2004; Holcomb & Hitt, 2007; Marshall, McIvor, & Lamming, 2006; Mols, 2007; Mudambi & Tallman, 2010). For instance, Contractor et al. (2010) suggest that, after identifying “true core activities” in the value chain of a firm, non-core and “essential” activities can be outsourced, especially those with a high degree of knowledge codification and standard interfaces (Contractor et al., 2010: 1427). Mudambi and Tallman (2010) apply both RBV and TCE to identify ex ante factors that influence the choice not only between “make or buy”, but also between different types of outsourcing relationships, namely contract-based and institutional (JV) ones. These authors find that besides typical RBV factors (e.g., tacit knowledge) and TCE factors (e.g., transaction-specific investments), the co-specialization between supplier and customer favours institutional relationships (Mudambi & Tallman, 2010: 1452).

Marshall et al. (2006) apply also both TCE and the RBV and find that inter-organizational collaboration and political motivation have more impact on outsourcing than transaction costs. Similarly, Rodríguez and Robaina (2006) focus on the impact of outsourcing on the level of vertical specialization of a firm's activities, which may modify the firm's boundaries in relation to specific counterparts: outsourcing can entail a stable, long-term relationship in which the supplier becomes a partner in a complex exchange of activities, and not simply an arm's-length provider of standard solutions. The IMP (Industrial Marketing & Purchasing) perspective provides a conceptual framework to analyse specifically this type of long-lasting relationships: we therefore chose to apply it to the phenomenon of outsourcing. Since the 1980s, a large body of IMP research (e.g., Anderson et al., 1994; Araujo, Dubois, & Gadde, 1999; Brennan & Turnbull, 1999; Ford, 1980; Ford & Håkansson, 2006; Gadde & Mattsson, 1987; Gadde & Snehota, 2000; Håkansson & Snehota, 1995; Johnsen & Ford, 2006; Medlin, 2004) has shown that buying and selling is not a series of independent transactions but is rather part of a pattern of long-lasting and complex relationships (LaPlaca, 2004). Håkansson and Snehota (1995) and Ford (2002) emphasize that business relationships include complex exchange processes and especially mutual adaptations between firms, which increase mutual dependence, while they also enable handling risk via mutual trust. Buyers and sellers often have convergent interests: gain access to each other's resources, while accepting mutual dependence (Håkansson & Ford, 2002).

Håkansson and Snehota (1995) analyse business relationships by breaking them down into the three layers of activities, resources and actors forming the so called “ARA” model, where the substance of a business relationship can be described by the activity links, the resource ties and the actor bonds connecting the two companies together. In turn, these connections between the two counterparts are embedded in a broader structure defined as the network, whereby each single relationship is affected by (and affects) other relationships to direct and indirect counterparts (Håkansson & Snehota, 1995; Axelsson & Easton, 1992). Thus, the IMP perspective provides new theoretical insights applicable to outsourcing for three reasons: (1) it enables viewing outsourcing not only from the perspective of the outsourcing company, that is, the “buyer” of external activities, but also from that of the other party in an outsourcing relationship, namely, the “seller” of external activities; (2) it stresses the fact that any ex ante outsourcing decision implies building some form of ex post relationship with the supplier to whom a given activity is outsourced (cf. Gadde & Håkansson, 1993, 2001); and (3) the “activity layer” of the ARA model (Håkansson & Snehota, 1995) is particularly relevant for analysing the externalization of activities, typical of outsourcing, in an interactive perspective.

2.2. Blurred organizational boundaries in outsourcing relationships

While Chandler (1992) and Grossman and Hart (1986) stress the clear-cut nature of the firm's boundaries, defined by formal administrative control over employees (Rubery, Carroll, Cooke, Grugulis, & Earnshaw, 2004) or legal asset ownership, the IMP view stresses the fluid nature of these boundaries. For instance, according to Araujo,