

A STUDY ON THE BENEFITS AND THE RISKS OF OUTSOURCING LOGISTICS IN THE ROMANIAN INDUSTRY

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Logistics outsourcing is considered to be an excellent source of competitive advantage for companies. Its benefits are long praised about in the specialty literature, but its risks are often briefly described. We believe that both the benefits and the risks of outsourcing logistics extremely important and must be regarded as a source of success or failure as it will be described in this paper.

Our research objectives refer to investigating the main outsourcing risks and benefits in the contemporary Romanian industry sector, in order to be able to identify which are the most threatening risks and also the most wanted benefits in the opinion of the production companies.

We regard logistics outsourcing as an exceedingly captivating and up-to-date topic, because it provides a satisfactory solution to various company issues that pertain to increased specialization, collaboration and integration in efficient and effective supply chains. The management of this activity with its main functions including the benefits and the risks will be approached in our research. The outsourcing of logistic services is a complex concept that our paper undertakes to discuss in some costs, access to new and costly technologies, scale economies, of its aspects.

Our study is developed on 108 Romanian companies that have more than 50 employees. Based on our previous studies in Romanian industry, we decided that our research is best based mainly on quantitative methods. The instrument of our research is the structured questionnaire. The general goal of our research is to investigate the way in which companies manage the risks and the benefits both expected and attained in the process of outsourcing logistics.

The implications of our research for the field of logistics refer to the fact that we were able to identify which are the most important and attainable outsourcing logistics benefits out of the large number stated in the international literature. Furthermore, we structured the risks encountered by Romanian companies which took a chance on outsourcing logistics. All in all, we consider that this is an excellent starting point for our future research in this field as we plan to investigate further on this topic by analyzing the outsourcing logistics benefits and risks also from the perspective of logistics service providers from Romania.

Key words - logistics outsourcing, strategic decision, benefits, risks.

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I. Introduction

At a first glance, the process of outsourcing logistics appears to be quite smooth, but reality shows that it is rather complex, sophisticated and strenuous. It is this complexity that made the vast issue of outsourcing logistics a worthwhile object for our research. Our curiosity is understandable, if we consider the large number of failed outsourcing agreements, i.e. more than 55% within the first five years (Donath, Mazel, Dubin, Patterson 2002).

We regard logistics outsourcing as an exceedingly captivating and up-to-date topic, because it provides a satisfactory solution to various company issues that pertain to increased costs, access to new and costly technologies, scale economies, specialization, collaboration and integration in efficient and effective supply chains. The management of this activity with its main benefits and risks will be approached in our research.

It should be however noted that in spite of all arguments in favour of outsourcing, managers haven't always achieved the expected outcome and some even declared themselves utterly disappointed. Bengtsson claims that the effects of outsourcing have generated a rather small amount of inconclusive, contradictory results, explaining that only a few studies consider the relationship between the reasons of outsourcing and its effects, while other explanation does justice to the fact that outsourcing is a trade-off and a dilemma (Berggren and Bengtsson 2004).

To exemplify: the outsourcing that aims at reducing costs may also impair the capacity to design and assimilate new products and therefore, the capacity for innovation (Berggren and Bengtsson 2004; Dankbaar 2007). There are also situations where the results of outsourcing depend on the balance of internal and external integration (McIvor 2008; Espino-Rodriguez, Padron-Robaina 2006). The high level of complexity and interdependence of activities, processes and systems is often regarded as hindrance in the way of efficient and effective outsourcing.

II. Literature analysis

Logistics: concept demarcations

The concept of “logistics” appeared under several “guises”, i.e. alternative designation, throughout recent history: distribution, physical distribution, technical & material procurement, marketing logistics, logistic distribution, material management, logistic material management, procurement chain management, supply Chain Management, industrial logistics, business logistics (Lambert, Stock 1993: 4).

The list remains open for any further designation used in history, but we believe that the quoted ones are quite relevant and it should be noted that all these designations referred in fact to the same phenomenon: the management of the goods' advancement from the production to the consumption site. At present, the most popular term among experts is *logistics management* and we therefore chose to adopt it for the purposes of this paper also, along “logistics”.

In 1986, one of the group experts in this field, known as The Council of Logistics Management, formerly known as The Council of Physical Distribution Management SUA, provided a comprehensive definition of the management concept under analysis. According to this definition, *logistics management denotes “the process of planning, implementation, efficiency and effectiveness control related to the transfer and storage of raw materials, inventories, finished goods and information from the source to the final consumer in order to satisfy the customers' requirements”* (Stock, Lambert 2001: 3).

This is considered to be a relevant definition of logistics and is therefore still in use, after all these years. Emphasis is placed on meeting the customers' needs in this case. The only shortcoming of this definition would be the fact that it ignores service companies.

Outsourcing of logistic activities and services: concept demarcations

Outsourcing is a quite encompassing term in Romanian, it may assume various form, that are easily and often mistaken for each other. In contrast, there is marked difference between *outsourcing* and *offshoring* in English. The latter may itself assume various forms, i.e. it may be performed within one and the same major transnational company (“*captive offshoring*”) or in cooperation with a foreign third party (“*offshore outsourcing*”) (Gorp 2008: 14).

The two forms of outsourcing denote various strategies applied by some companies to penetrate foreign markets, as the term itself always conveys the notion of a company performing various activities in a foreign location. It is important to bear this detail in mind, because the phenomenon under our scrutiny, i.e. outsourcing, may take place either domestically or abroad, but always through a third party.

In Romanian, there is no marked distinction between these notions and English original terms are often used to avoid confusion. This paper will focus on the term *outsourcing*, construed as the strategic employment of external specialized suppliers to execute or manage activities or services that do not count as core competences for the company that resorts to outsourcing (Rushton, Walker 2007).

III. Research methodology

The main objective of our scientific endeavour concerns the analysis of outsourcing of logistic activities and processes among Romanian industrial companies in terms of identifying the main benefits and risks. We chose to base our research on non-probabilistic sampling, namely on rational theoretical guided sampling. For our empirical study we have selected industrial companies with more than 50 employees located in the North-West region of Romania.

As the application of the questionnaire regarding the outsourcing of logistic benefits and risks is concerned we chose to put together a sample of 300 companies to which questionnaires were sent either by e-mail or fax. This approach yielded a very high response rate: 125 questionnaires have been returned, 17 thereof being invalid. The questionnaires were collected and checked for validity. The 108 valid questionnaires were numbered and loaded in data processing software. The graphs and frequency tables were generated by this software.

IV. The results of the research

The participating companies have identified the fundamental benefits reaped from the outsourcing process. In addition to those suggested by us, some respondents have mentioned benefits related to the conservation of their own capitals in the blank space at the end of the question. Fig. no. 1 summarizes the benefits of outsourcing according to the participants.

As shown in fig. no. 1, the respondents consider cost reduction to be the most important benefit of outsourcing. This choice is justified, because logistic costs make up approximately 29% of a product's total cost (Fredricksson, Johansson 2009: 281). This is an effective motivation for resorting to outsourcing, given the fact that outsourcing contains a promise of cost reduction.

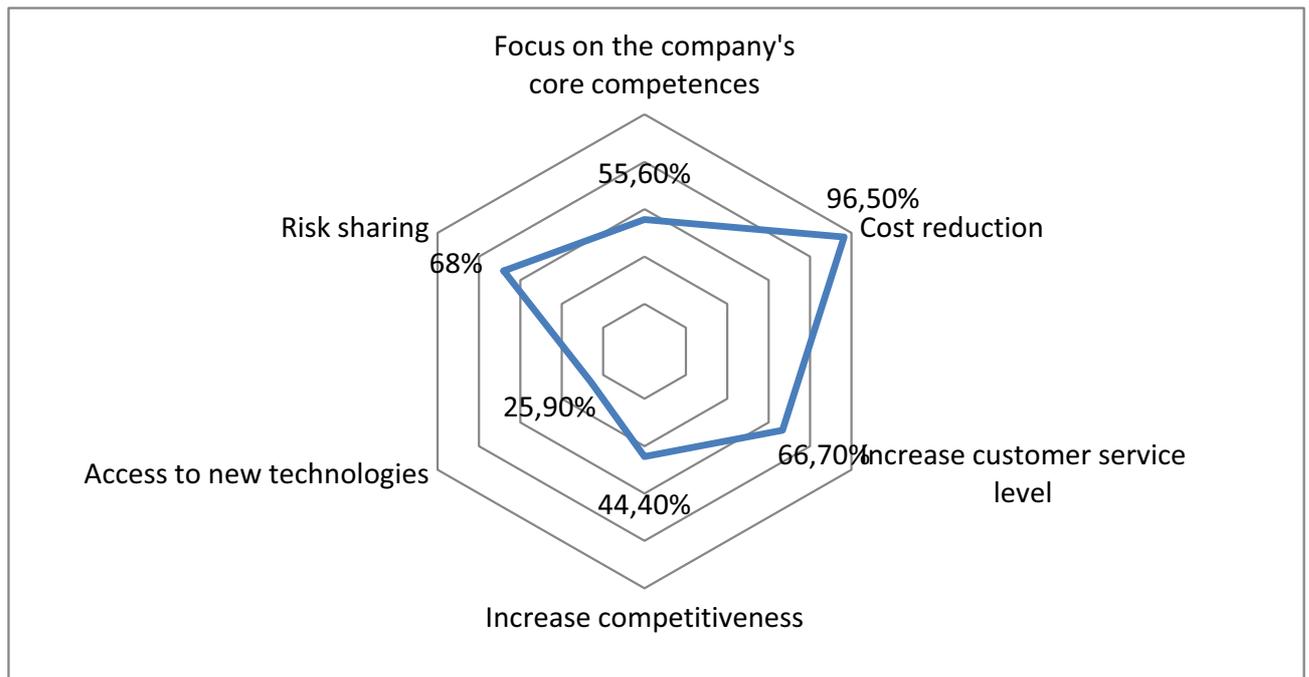


Figure 1. The benefits pursued by companies that resort to logistics outsourcing

Source: made by the author.

Although cost reduction seems to be the most wanted outsourcing logistics benefit, our studied population claims that risk reduction is the second most valuable benefit that they obtain in the process of outsourcing logistics. 68,5% of our respondents believe so.

Furthermore, Romanian companies also target to optimize the customer service level. 66,7% of our respondents stated that increasing the level of customer service is a popular benefit that they get by outsourcing some or all of their logistics activities.

Encountered risks

During our research we had the opportunity to notice that the most frequently cited outsourcing – related risks were: the supplier's failure to meet the required quality standards (43,5%), events of default (39,8%), poor communication with the supplier (33,3%). All problems encountered in the outsourcing process are listed in fig. no. 2. It should be noted that the respondent companies had several response alternatives to choose from.

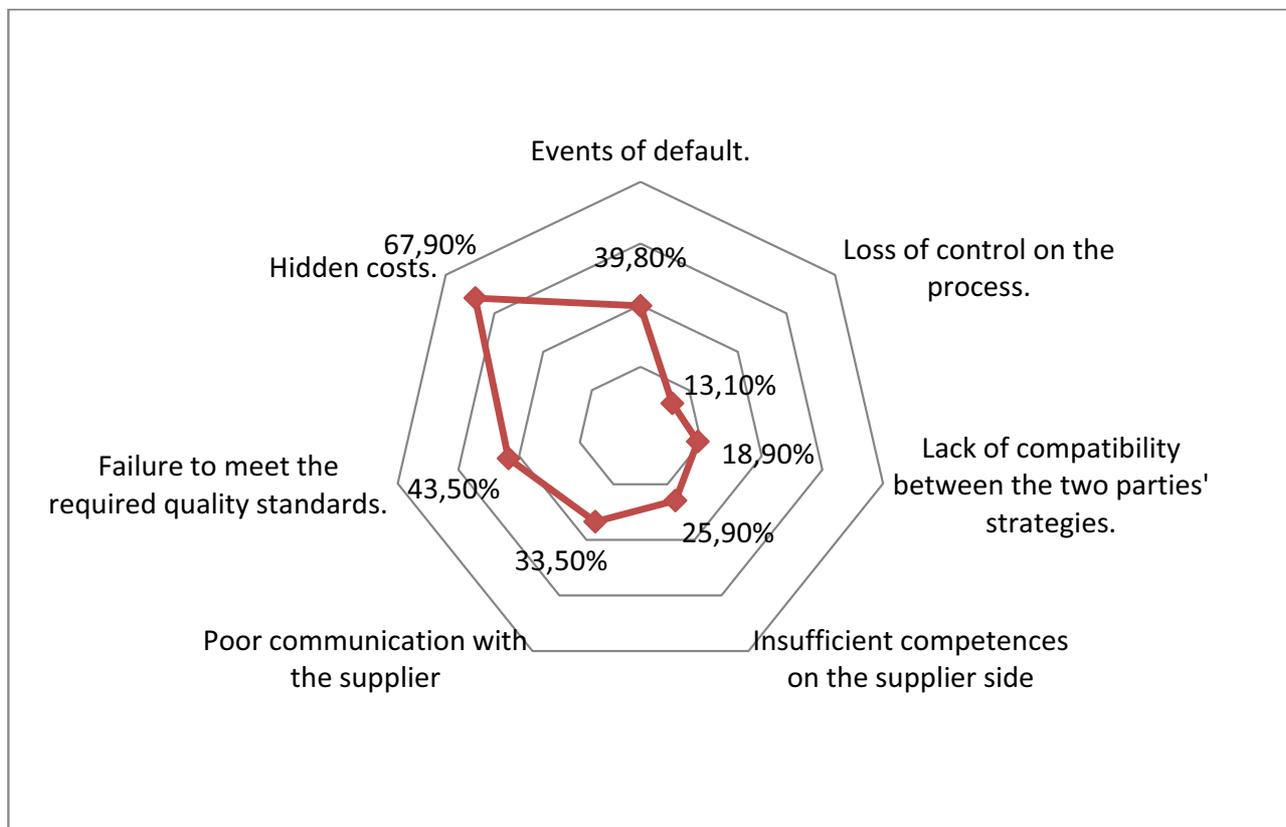


Figure 2. Problems encountered during the outsourcing of logistic activities

Source: made by the author.

Our respondents admitted that all of these risks are truly endangering the outsourcing process and that what they fear the most are all the hidden costs that they encountered only after they enrolled in the process. The risk related to the hidden costs can be minimized through a solid outsourcing contract, but for doing this the companies must benefit from a large experience in this field. This matter will be subject of our future research in which we will identify the most suitable ways to eliminate or reduce the outsourcing logistics related risks.

V. Conclusions

The decisions regarding the outsourcing of logistic services are designed to optimize the performances within the value chain if the compatibility with the competitive strategy of the company is secured. A company whose competitive drive is the performance of the logistic system will provide a competitive edge in terms of costs, quality and innovation in case of outsourcing. In order to benefit from the advantages of logistics outsourcing, managers must treat this area as a source of competitive edge.

As a company grows, one of the most challenging tasks is to choose the outsourcing strategy, in which the outsourcing of logistic services plays an important part, securing a medium- and long-term competitive edge.

Today many companies with a significant position on the domestic and international markets resort to suppliers of logistic services that – given the complexity of the global logistic chain - establish regional, national and international distribution centers. This fact compels managers to scrutinize the external environment, the market respectively, with utmost attention, to plan logistic activities and processes, to analyze their necessity and adequacy, to develop control procedures and to monitor their success or failure.

The aim of outsourcing logistic activities and processes is to develop optimal logistic systems for the targeted market and for each market area. The increasingly limited opportunities for growth in

terms of efficiency and effectiveness among manufacturing and services companies motivates intensified efforts for the discovery of new “critical area” in the companies' activities that might enable the companies reach their targets ducts, services and customer service level. These critical areas are also linked to the area of logistics, that offers considerable opportunities for increasing competitiveness and securing a competitive edge and still provides unexploited or insufficiently exploited resources, in which the drawing up and implementation of outsourcing strategies play an important part.

The limitations of our research refer to the fact that we only found respondents from the North-West region of the country. We intent to extend our future research to investigating companies from the entire country. Another limitation includes the fact that our research does not establish any ways in which the outsourcing logistics related risks can be minimized or even eliminated. For this reason our future work will focus on this matter.

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