

Investigating Outsourcing Implementation in Iranian Organizations

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Abstract: The aim of this study is threefold, first to explore the extent of outsourcing implementation in Iranian organizations, second, given contextual factors of the country to identify drivers and barriers of outsourcing implementation among the investigated organizations and thirdly, to survey if there is any relationship between outsourcing functions and organizational performance of Iranian organizations, mainly based on a descriptive analysis. Based on the review of literature 16 main functions and activities which are widely outsourced and drivers and barriers of outsourcing implementation were identified. A questionnaire was designed and distributed among Iranian organizations. Based on 197 returned questionnaires the extent of outsourcing for various functions in the surveyed organizations was determined. Results indicate that most of the sample organizations realize the importance and the role of outsourcing strategy in gaining and increasing competitiveness and competitive advantage over their competition which could hopefully lead to the increase of their profitability. However, the result of the chi-square test cannot confirm that the implementation of outsourcing is significantly related to greater company success in Iranian industries context.

Key words: Drivers and barriers, exploratory analysis, Iran, organizational success, outsourcing

INTRODUCTION

Now outsourcing is one of the most recent management strategies to emerge in response to demands for more efficient ways to address organizational competitiveness. In an age where management carefully weighs the costs and benefits of every discretionary investment dollar, finding evidence of the results of outsourcing is critical. In particular, research considering the context surrounding an outsourcing decision's results is likely to be essential and useful to corporate outsourcing management (Jiang and Qureshi, 2006). From the strategic management perspective, there are a number of studies which discuss the increasing significance of outsourcing issues (Simchi-Levi *et al.*, 2003; McIvor, 2005; Shy and Stenbacka, 2005). Outsourcing is a fashionable way of solving some business problems and there are numerous reports of its increasing use. Initially used primarily for Information Technology (IT), a wide variety of business process is now outsourced. The use of outsourcing is becoming more sophisticated; more organizations are outsourcing responsibility for business processes (Beaumont and Sohal, 2004). Outsourcing has been touted as the ideal way for organizations to reduce costs, focus on core business processes, improve services, enhance skills, reduce time to market and increase overall competitive advantage (Power *et al.*, 2004). Lau and Zhang (2006) state by means of outsourcing, organizations can gain competitive advantage through cost reduction and improved responsiveness to changing

business environment and market demand. In a recent study conducted by ASQ and the Metrus Group, a research and consulting firm, nearly 94% of the 1,920 participants reported their organization outsourced at least one of 15 important functions (Seibert and Schiemann, 2011).

Overview of outsourcing and research questions: The outsourcing of functions once performed by organizations internal departments has been increasing in quantity and scope. What began as an effort to shift low-value activities to outside suppliers has steadily grown to the point at which virtually any function may be subject to outsourcing: from corporate administrative functions (such as IT, finance and HR) to basic production and R&D. Even activities once thought of as an organization core strengths, requiring unique expertise and producing competitive advantage, are candidates for external procurement for some (Seibert and Schiemann, 2011). Embleton and Wright (1998) argue that the decision-making process that management must undergo when considering outsourcing, hinges on a "make or buy" philosophy. More variables are brought into play when management considers outsourcing a product or service that is currently being produced internally. Many more options exist currently than there were even a decade ago. In today's business environment it is now possible to outsource virtually any aspect of the business. Beaumont and Sohal (2004) define outsourcing as having work that was formerly done inside the organization performed by

an external organization. The vendor (hereafter the outsourcer and outsourcee are, respectively, referred to as vendor and client) may be an independent entity or a wholly owned subsidiary. Insourcing means applying outsourcing's discipline to internal suppliers, often having them compete with external suppliers. Also Lankford and Parsa (1999) define outsourcing as the procurement of products or services from sources that are external to the organization. For services, this usually involves the transfer of operational control to the suppliers. Embleton and Wright (1998) point out that "Note that outsourcing is not a synonym for contracting out. Contracting out refers to work assigned to an outside supplier on a job-by-job basis, usually involving a cost-plus arrangement. Outsourcing on the other hand, entails a long-term relationship between supplier and beneficiary, with a high degree of risk-sharing". Driven by globalization and rapid advance in Information Technology (IT), organizations strive to improve competitiveness and responsiveness to customer and market demands. Outsourcing has increasingly become an important strategy that can significantly assist organizations to leverage their skills and resources to achieve greater competitiveness (Lau and Zhang, 2006). In Iran during the past couple of years and with the start of deregulation policies of the government towards privatization of industries and expanding free market most of organizations in the country in order to increase their competitiveness and reduce the cost production and operations have shown a great desire for downsizing and outsourcing various functions and activities of their own.

It can be seen, then, that outsourcing results from an economic climate where the emphasis is on cost savings and increased profit (Embleton and Wright, 1998). Researchers have identified numerous reasons why firms use outsourcing. Companies can expect to achieve many different benefits through successful outsourcing, although there are significant risks that are run if outsourcing is not successful (Kremic *et al.*, 2006; cited in Abdul-Halim and Che-Ha, 2010). On the other hand review of literature indicates that outsourcing has some advantages and disadvantages which have been referred to by authors like (Abdul-Halim and Che-Ha, 2010; Beaumont and Sohal, 2004; Lankford and Parsa, 1999; Embleton and Wright, 1998) therefore the aim of this study is threefold, First to investigate the extent to which Iranian organizations outsource their various functions. Second, given contextual factors of the country what are the main drivers and barriers of outsourcing for Iranian organizations? And finally it will be investigated whether the implementation of outsourcing is related to Iranian manufacturing organizations success or not. Therefore, for the purpose of this study the following research questions are posed:

RQ1: To what extent do Iranian organizations outsource various functions?

RQ2: What are the main drivers and barriers for outsourcing in Iranian organizations?

RQ3: What is the relationship between outsourcing and organizational success of Iranian organizations?

RESEARCH METHODOLOGY

To address the research questions, a survey-based empirical study was carried out in a representative sample of 237 organizations from various industry sectors in Iran, between March and June 2011. In order to make the findings representative, companies chosen for this study were selected across a wide range of industries and from those which are currently involved in outsourcing. However, the main part of the organizations (58%): came from one of the following industries: manufacturing and industrial products, transportation and automotive, governmental companies, and utilities and energy. Building on key informant approach (Silk and Kalwani, 1982), the pool of potential respondents was restricted to the top managers including managing directors of the respective organizations. Two data bases on organizations provided by ministry of industry and ministry of trade served as the basis for the survey. In total 197 statistically useful questionnaires were returned, resulting in a response rate of 83 %. Data analysis entailed the use of both descriptive methods to provide exploratory insights into the nature of outsourcing in Iranian organizations and the use of statistical analysis. Being exploratory, the survey was kept relatively short. Most items asked the respondents to rank issues surrounding their outsourcing endeavour. Issues included functions and the extent of outsourcing for various functions, drivers and obstacles of outsourcing, and the alternatives the respondents could choose from were predetermined by the researcher and generated using the existing literature (Lau and Zhang, 2006; Beaumont and Sohal, 2004; Kulkarni and Jenamani, 2008; Seibert and Schiemann, 2011) and the researcher's own experience of the topic. The choice of ranking scales was due to a desire to simplify for respondents. Ranking scales have the benefit of being easy to understand and therefore suitable for self administered questionnaires. One limitation of ranking scales is that a ranking of objects takes place regardless of the attitudinal position taken by the respondents (Kinnear and Taylor, 1991). To address this limitation, most questions included the opportunity for respondents to choose the category "other" and specify their choice (Ahlstrom and Westbrook, 1999). Regarding the functions and the extent of outsourcing for various functions organizations use, from a predetermined list, respondents were asked to mark the percent at which each possible function is partially or fully outsourced. The list and corresponding responses are shown in Table 1.

Table 1: Functions and activities of outsourcing

• Manufacturing/ production
• IT services
• Logistics/distribution
• Marketing/market research
• R & DHR, accounting, and administration
• Customer services including returns handling, installation, and maintenance work
• Procurement/purchasing
• Legal
• Sales
• Quality
• Security
• Communications/public affairs
• Cleaning and catering
• Training
• Transportation and warehousing

Table 2: Ranking of functions based on the extent of outsourcing according to respondents

1	Cleaning and catering
2	Logistics/distribution
3	Manufacturing/ production
4	HR, distribution and administration
5	R &D
6	Marketing/market research
7	Customer services including returns handling, installation, and maintenance work
8	IT services
9	Procurement/purchasing
10	Customer service
11	Sales
12	Communications/public affairs
13	Finance/accounting services
14	Legal
15	Security
16	Quality

RESULTS

Although 80% of the organizations under study indicated that most of functions and activities mentioned above are “important” or “very important” but about half of them just outsource a few of functions and activities. About 50% of them mentioned that they partially outsource these functions. It is not surprising, since as Seibert and Schiemann (2011) note most organizations partially outsource some functions and it is unusual for a function to be completely outsourced. However 25 % of organizations surveyed indicated that they fully outsourced activities such cleaning and catering, transportation and warehousing, and IT services. The ranking of the functions based on the extent of outsourcing by the respondents of surveyed organizations are found in Table 2.

Drivers and barriers for implementation of outsourcing: A large number of studies have analyzed the drivers of outsourcing from both a theoretical perspective. While many drivers are unique to specific organizations and industries, there are some common key factors that motivate organizations of all industries to

Table 3: Drivers for implementation of outsourcing in Iranian organizations

1	Cost saving
2	Cost reduction
3	Capital investment reduction
4	Productivity enhancement
5	Flexibility enhancement
6	Focus on core competence
7	Share of risk
8	Capability of supplier
9	IT development
10	Acceleration of Business process reengineering
11	Small-volume requirements
12	Quality problems
13	New product development
14	Workload fluctuations
15	Geographical

make outsourcing decisions. These factors can broadly be categorized as economic, strategic, and environmental ones (Lau and Zhang, 2006). Also based on the literature review they point out to obstacles of outsourcing implementation and argue that there is evidence that outsourcing does not reduce costs as expected in some cases. loss of control, loss of critical skills, inadequate capabilities of service providers, loss of flexibility, failure to realize the hidden costs generated by the contract, difficulty in obtaining organizational support, indecisiveness on which activities to outsource, inadequacy of cost and benefit analysis systems, fear of job loss, and damage to morale of existing workers, etc. are among the commonly cited inhibitors to outsourcing.

Asked for their own, subjective evaluation of outsourcing, 80 % of the respondents considered that their main driver and reason for outsourcing implementation is cost reduction, cost saving, and capital investment reduction. This finding is consistent with a wealth of literature which suggests that most outsourcing deals are driven by a desire to reduce cost (Lau and Zhang, 2006). The other reasons which Iranian companies have marked as the reasons for implementing outsourcing are shown in Table 3. It is worth noting these drivers have been ranked based on the frequency of responses.

Table 4: Barriers for implementation of outsourcing in Iranian organizations

1	Poor transportation, non standard roads and IT infrastructure
2	Instability of economic conditions
3	Loss of internal control
4	Inadequate cost and benefit analysis systems
5	Inadequate capabilities of service provider
6	Failure to realize hidden costs of contracts
7	Reduction of employee morale
8	Indecisiveness on which activities to outsource
9	Trustworthiness of the supplier
10	Quality of service
11	Defficulty in obtaining organizational support
12	Fear of job loss
13	Loss of critical skills
14	Loss of flexibility
15	Lack of overall post-outsourcing measurement
16	Design secrecy is required to protect proprietary technology

Table 5: Chi²-square for group differences

Success indicator	Method	Value	df	Asympt. Sig
Return on assets	χ^2 (Pearson)	1.114	2	0.372
	Likelihood ratio	1.218	2	0.361
Net profit margin	χ^2 (Pearson)	1.111	2	0.352
	Likelihood ratio	1.232	2	0.397

Also to assess the barriers and difficulties encountered by the surveyed companies, respondents were asked to rank a number of outcomes on a predetermined list. In Table 4 the barriers and difficulties associated with implementing outsourcing have been ranked, which is based on the frequency cited by respondents on each of them.

As can be seen in Table 4 the most important barrier and difficulty for the surveyed companies is poor transportation and IT infrastructure, it is consistent with the argument of Embleton and Wright (1998) where they note that IT and the ability to produce products have dramatically changed the structure of work. The type of work and who does it are now dependent on computers. Due to poor IT infrastructure in the country Iranian organizations face with various difficulties. Also Iran suffers from lack of effective transportation networks and suitable and standard roads with the highest road accidents and mortality rate in the world. Thus it is not surprising that respondents rank this obstacle as the most important barrier in their way to implement outsourcing.

The second obstacle, i.e., instability of economic conditions which was ranked as the second most important obstacle stems from the inflation and instability of raw materials prices which hinders the process of negotiations, and reaching an agreement with suppliers more difficult. Regarding the third most important obstacle ranked by respondents it should be noted for many organizations, the complexity of the supply chain has led to the loss of control of the full manufacturing process. This lack of control contributes to a high level of concern over outsourced products and processes. As outsourcing continues to become more widely used, these concerns will continue to grow. So it may be the main reason which surveyed organizations ranked third this obstacle. Another driver that respondents have emphasized is share of risk that needs to be taken into consideration. Through tight control of suppliers, organizations can greatly reduce the risk of poor product quality. Organizations will be able to define the mission critical criteria that suppliers must meet, and will have the visibility and access to the data to ensure that these criteria are met. Brand owners will then be able to find critical, high risk areas and work with the suppliers to put controls in place to minimize any potential risk.

Today's knowledge and service-based economy offers innumerable opportunities for well-run companies to increase profits through outsourcing. When used properly, outsourcing can boost profitability in many ways (Jiang and Qureshi, 2006). To address RQ 3, the

researcher examined whether there is a statistically significant relationship between the implementation of outsourcing and company success. Jiang and Qureshi (2006) argue that profitability is the most important criterion of evaluating the performance of a firm. Profitability metrics measure the return that the firm's owners receive from their investments. Therefore, Return on Assets (ROA) and net profit margin were chosen to represent profitability and as success indicators. For both success indicators, no statistically significant difference between those companies which implement most of the outsourcing functions and activities and those that just apply a few of functions could be identified, using a chi-square test (Table 5).

Accordingly, the present study cannot confirm that the implementation of outsourcing is significantly related to greater company success in the Iranian industries context. This could have various reasons such as non competitive market of the country which is largely exclusive, though some activities have been set out towards privatization of the Iranian industry. So the success of the surveyed companies which about 70% of them were governmental or most of their shares belong to the Iranian government and take advantage of various facilities is not surprising (Valmohammadi, 2011).

DISCUSSION AND CONCLUSION

As the dynamics of manufacturing and services in the modern day change, organizations are becoming more and more dependent on outsourced, global suppliers and contract manufacturers to reduce their costs. The results of the empirical investigation demonstrate that outsourcing is still infrequently used in Iranian organizations, despite an increased perception of the relevance of this topic and application of it in the developed counties. Although about 80% of the surveyed companies consider various functions and activities of outsourcing as "important" or "very important", only 25 % of these companies implement fully some kinds of outsourcing. In this regard, the main arguments of Iranian organizations against the implementation of various functions and activities of outsourcing were lack of poor IT infrastructure and transportation network and non standard roads of the country and instability of economic conditions which makes negotiations and reaching an agreement with suppliers more difficult. The aim of this article was to investigate the extent of outsourcing implementation, drivers and obstacles of

outsourcing given the contextual factor of the country, and the relationship of outsourcing with organizational success in Iranian organizations, mainly based on a descriptive analysis. It was found that outsourcing of various functions and activities is still underused in Iranian companies. Though the surveyed organization have found out the importance and the role of outsourcing strategy in gaining and increasing productivity and flexibility of their organizations which will lead to fulfilling of customer satisfaction and ultimately increase of their competitiveness and competitive advantage in the target markets.

Iranian organizations' top managers should be aware in order to make a successful decision regarding outsourcing they should consider costs, as well as quantitative and qualitative criteria. Most importantly, however, decisions regarding outsourcing should be made holistically: such decisions should be made with regard to the benefit of the whole organization, which necessitates a cross-functional approach. However, once this process has taken place, the final decision, as Brannemo clearly articulates, should be left to management (Strategic Direction, 2007).

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