



Improving logistics outsourcing through increasing buyer–provider interaction

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ABSTRACT

Logistics outsourcing has been at the top of the management agenda during recent decades. Through this approach companies have been able to improve logistics performance. However, several studies point out severe problems with outcome and it is even claimed that in some cases “logistics outsourcing has become a source of corporate failure and disappointment” [Boyson, S., Corsi, T., Dresner, M. and Rabinovich, E. (1999). Managing effective third-party logistics relationships: What does it take? *Journal of Business Logistics*, 20 (1), 73–100.]. Previous research shows that many companies have taken outsourced functions back in-house. The aim of this paper is to explore the reasons behind the problems in logistics outsourcing. Our analysis is based on an extensive literature survey. This examination indicates that outsourcing decisions require a holistic perspective. We apply the industrial network model [Håkansson, H. and Snehota, I. (1995). *Developing relationships in business networks*. Routledge, London.] for the analysis of potential consequences of logistics outsourcing. The main conclusion of the paper is that increasing interaction between buyer and provider would be beneficial to the outcome of outsourcing.

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1. Introduction

Logistics outsourcing and third-party logistics originated in the 1980s as important means of improving supply chain effectiveness (Maloni & Carter, 2006). Third-party logistics (TPL) was initially defined as “the use of external companies to perform logistics functions that have traditionally been performed within an organization. The functions performed by the third party can encompass the entire logistics process or selected activities within this process” (Lieb, 1992:29). Like other outsourcing arrangements third-party logistics expanded rapidly. Estimates indicate that the proportion of companies in the US implementing this approach has increased by 5–8% annually between 1996 and 2004 (Ashenbaum, Maltz, & Rabinovich, 2005). Moreover, in 2005 no less than 80% of the Fortune 500 Companies stated that they relied on TPL (Lieb & Bentz, 2005a). Current predictions indicate growth rates in the range of 15–20% between 2009 and 2011 in both Western Europe and the US (Deepen, Goldsby, Knemeyer, & Wallenburg, 2008).

Despite the attention paid to outsourcing, the actual realization of expected benefits is far less well documented, since “there are actually very few empirical studies of logistics outsourcing performance” (Deepen et al., 2008:76). This situation applies to outsourcing in general, where it is claimed that cost savings and other benefits “tend to be taken for granted, but detailed analyses of actual outcomes and potential side effects are hard to find” (Berggren & Bengtsson, 2004:211). Within logistics there are numerous claims concerning the potential benefits of out-

sourcing arrangements (see, for example, Bowersox, 1990; Tate, 1996; Bhatnagar & Viswanathan, 2000; Halldorsson & Skjoett-Larsen, 2004; Marasco, 2008). In reality, however, there is no doubt that the outcome of third-party logistics shows mixed results. Lambert, Emmelhainz, and Gardner, (1999) conclude that while some realized benefits of TPL are well documented, the pitfalls and problems have received less attention. Furthermore, it is argued that there is clear evidence that in some cases “logistics outsourcing has become a source of corporate failure and disappointment” (Boyson, Corsi, Dresner, & Rabinovich, 1999:73). In their survey a significant proportion of the respondents indicated that they had to modify their logistics arrangements and take previously outsourced functions back in-house. Other studies, too, point out severe problems with outcome: for example, it is reported that 55% of logistics alliances were terminated after three to five years (Gulisano, 1997). Similar results were obtained in a study by the Outsourcing Institute where it was found that more than half of third-party partnerships had failed (Foster, 1999). Among the problems having these consequences are poor service performance, such as “disruption to inbound flows, inadequate provider expertise, inadequate employee quality, sustained time and effort spent on logistics, loss of customer feedback and inability of 3PL-providers to deal with special product needs and emergency circumstances” (Selviaridis & Spring, 2007:130).

The aim of this paper is to explore the reasons behind the problems mentioned above. Our analysis is based on an extensive survey of the literature on logistics outsourcing. The examination of previous studies indicates that outsourcing decisions require a holistic perspective. We apply the industrial network model (Håkansson & Snehota, 1995) for the analysis of potential consequences of logistics outsourcing. The main conclusion of the paper is that increasing interaction between buyer and provider would be beneficial to the outcome of outsourcing.

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2. Challenges in logistics outsourcing

The literature review shows that there are two major difficulties with logistics outsourcing:

- insufficient analysis of the potential effects of outsourcing and
- problems in the implementation of TPL-arrangements.

The main reason for the disappointing outcome of logistics outsourcing seems to be inadequate strategic analysis. Outsourcing decisions are often taken with too narrow scope concerning potential consequences. For example, *Ackerman (1996)* claims that pitfalls in logistics outsourcing tend to occur because neither buyer nor provider has achieved a realistic understanding of what a change in this respect actually implies. One particular drawback emanating from these conditions is the severe difficulty of estimating the real costs of logistics outsourcing (*Lieb & Randall, 1996*). In most cases costs are underestimated, which is an obvious reason for dissatisfaction with outcome.

The inherent complexity of logistics outsourcing has been accentuated over time owing to some significant changes in its characteristics. On the provider side of TPL-arrangements substantial re-organization has occurred in terms of mergers, acquisitions and the entrance of new enterprises (*Lieb & Bentz, 2005a*). These changes affect both the geographical coverage of TPL-firms and their features (*Bolumole, 2003; Kim, Yang, & Kim, 2008*). Originally third-party logistics providers emerged out of companies previously involved in warehousing and transportation. In the early 1990s firms formerly specializing in express parcel deliveries entered the arena (e.g. DHL, UPS, TNT and FedEx), followed by firms originally focusing on financial services, IT-services, and management consulting, which brought in their competences related to information system and supply chain planning (*Selviaridis & Spring, 2007*). The capabilities of these entering firms extended the scope of the outsourcing arrangements towards the entire logistics process, involving a broader number of service functions (*Murphy & Poist, 2000; Persson & Virum, 2001*).

On the buyer side two important changes have occurred. The first concerns the increasing importance of the logistics function. Logistics issues are at the top of the management agenda owing to the significance of just-in-time deliveries and customization in terms of build-to-order production. These approaches are based on logistics processes characterized by “speed, predictability and accuracy in the delivery of goods since available inventory has been cut back” (*Bonacich, 2003: 41*). These conditions in combination with the extended scope of outsourcing arrangements have led to the second change on the buyer side. Once logistics became increasingly important its role and features changed. The development of the logistics function has been expressed as an evolution “from a passive, cost-absorbing function to that of a strategic factor which provides a unique competitive advantage” (*Chapman & Soosay, 2003:639*). This makes outsourcing of logistics an issue of strategic significance.

The changes on the buyer and provider sides increase the complexity of outsourcing decisions. Providers have extended their capabilities to involve a broad range of service functions. For buyers, logistics have become an increasingly strategic function implying that outsourcing failures may have far-reaching consequences. The changing nature of third-party logistics has put the relationship between buyer and provider at the forefront, and it has been claimed that “many 3PL-relationships are increasingly complex and management of those relationships is quite challenging to both parties” (*Lieb & Bentz, 2005a:5*). In spite of this, it is argued that current literature “does not address adequately the potential impacts and antecedents of relational exchange” (*Panayides, 2007:134*). This shortcoming appears particularly severe since it has been shown that cooperation in close relationships significantly impacts on the performance of TPL-arrangements (*Deepen et al., 2008*).

Our literature review reveals that the second main reason for problems in logistics outsourcing concerns the implementation of the ar-

rangements. It seems obvious that inadequate analysis of the potential effects of outsourcing should result in challenges in the implementation phase. Furthermore, as mentioned above, the nature and management of the provider–buyer relationship impacts on the performance of outsourcing arrangements. In particular the involvement between the parties has been shown to be critical to the outcome concerning both ‘standardized’ outsourcing (*Smyrlis, 2006*) and more ‘advanced’ outsourcing (*Lei, 2007*). Moreover, the features of the business relationship have been used as explanations of both unsuccessful (*Whitten & Leidner, 2006*) and successful outsourcing (*Lewin & Peeters, 2006*). Relationship problems in the implementation phase primarily concern the failure of outsourcing firms to manage providers properly and the lack of understanding of the other party. These conditions, in turn, are contingent on insufficient sharing of information among the parties and subsequent problems with providing an appropriate context for cooperation (*Razzaque & Sheng, 1998; Bagchi & Virum, 1998; Knemeyer & Murphy, 2005; Panayides, 2007*). Other issues stem from the risks perceived by the outsourcing firm of losing control over logistics operations (e.g. *Bolumole, 2001; Selviaridis & Spring, 2007*). These perceptions have led to buyer approaches classified as “command and control patterns” (*Bolumole, 2001:104*). As shown below these conditions tend to constrain the opportunities of the provider and create tensions in the relationship.

Our conclusion from the literature review is that problems in TPL emanate from a narrow perspective of what outsourcing actually means. A holistic framework for analysis of outsourcing decisions would improve conditions in this respect and uncover potential implementation issues.

3. Framework for analysis

Early research on TPL focused on the buyer of the logistics services (*Berglund, van Laarhoven, Sharman, & Wandel, 1999*). Over time, increasing attention has been devoted to logistics service providers (e.g. *Lieb & Bentz, 2005b; Carbone & Stone, 2005; Yeung, Selen, Sum, & Huo, 2006*). What still seems to be quite an unexplored area is the relationship between buyer and provider. *Maloni and Carter (2006:30)* conclude that “very few studies have attempted to look at both buyers and providers simultaneously”. Our literature review revealed that the relationship between the two parties is highly significant to the outcome of outsourcing, and explorations with alternative units of analysis are therefore needed for a better understanding of TPL-decisions and implementation.

Several researchers have suggested supplementary perspectives on TPL in order to expand the unit of analysis. For example, *Halldorsson and Skjoett-Larsen (2004)* applied a ‘resource and competence based’ framework. *Knemeyer and Murphy (2004)* adopted a relationship marketing approach to the research of a buyer and a provider of logistics services. *Bask (2001)* used a supply chain management approach in the exploration of logistics service providers and their clients. These studies – and others not mentioned here – improve our understanding of what takes place in a relationship between buyer and provider.

In this paper we take the exploration one step further. However careful the analysis of a particular relationship is, this view will provide only partial understanding. A specific relationship is never isolated since both buyer and provider are involved in other relationships simultaneously. Because relationships are connected, changes in one will impact on others, thus calling for a wider context of analysis. The supply chain perspective also represents a simplification of reality. Since any firm is involved in several chains, modifications in one of these will impact on others, thus making the efficiency in a particular supply chain dependent on its relations to other chains (*Christopher, 1998; Gadde & Håkansson, 2001*).

Two recent reviews of the state-of-the art of TPL-research have suggested the industrial network model (e.g. *Håkansson & Snehota, 1995*) as an appropriate approach for further studies of logistics outsourcing.

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