Achieving efficiency and effectiveness in Purchasing and Supply Management: Organization design and outsourcing

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http://dx.doi.org/10.1016/j.pursup.2017.06.003
Received 5 January 2017; Received in revised form 9 June 2017; Accepted 14 June 2017
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1. Introduction

Purchasing and Supply Management (PSM) has a key strategic role in many contemporary business organizations (Barney, 2012; Hayes et al., 2005; Van Weele and van Raaij, 2014). As firms increasingly rely on suppliers’ inputs and contributions, the strategic importance of the PSM function as the interface managing these inputs has also increased (Van Weele and van Raaij, 2014). In the current global economy, PSM is under increased pressure to find additional value generation beyond efficiency seeking behavior and to search for effectiveness; for example by bringing in supplier product or process innovations, ensuring sustainability, and participating in product innovation activities (Barney, 2012; Caniato et al., 2012; Schiele, 2010, 2012; Turkulainen and Swink, 2016).

One of the fundamental managerial approaches to seek efficiency and effectiveness in different functional areas is outsourcing. Outsourcing has increased tremendously and has had transformational impact on how organizations manage their global operations and supply chains (Gray et al., 2009b). Despite its prominence, outsourcing continues to pose significant managerial challenges (Kroes and Ghosh, 2010; McIvor, 2009; Narasimhan et al., 2010) and many businesses fail to realize the benefits anticipated from their outsourcing initiatives (Gray et al., 2013; Handley, 2012; Handley and Benton, 2009; McIvor, 2000).

In this paper, we study outsourcing in the PSM context. Outsourcing in the PSM context refers to transferring tasks, such as order placement and source selection, outside the boundaries of the focal firm (Brewer et al., 2014; Maltz and Ellram, 1999). Understanding outsourcing in the PSM context is important as despite of its strategic nature (McIvor, 2000), and not outsourcing in the PSM context. Moreover, research on PSM outsourcing is considered “sparse, and also largely atheoretical” (Brewer et al., 2014: 187). In this paper, we aim to develop more detailed understanding of outsourcing in the PSM context. We address the following research question: How does the design of the

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purchasing and supply organization (PSO) support outsourcing parts of PSM? Understanding the organizational design aspects in the context of outsourcing is critical, as organizational design is one of the major reasons for outsourcing challenges (Ishizaka and Blakiston, 2012). We elaborate research on PSM organizational design and illustrate how a change of organizational design has supported outsourcing parts of PSM at a global chemical and pharmaceuticals company (Global Chemical Company GCC – a pseudonym).

This study contributes to research on PSM and outsourcing. First, the results give preliminary evidence on the relationship between an activity-based PSO design and outsourcing parts of PSM. Herein, an activity-based design refers to organizational design, which is based on bundling certain activities (rather than, say, business units) (Trent, 2004: 15). The organization design focus allows us to complement prior research on outsourcing of PSM (e.g., Amaral et al., 2006; Ellram and Billington, 2001; Norlet and Beaudieu, 2005). We also develop insight into one of the recent concerns of “outsourcing cascade” and the question of whether PSM follows manufacturing out the door (Brewer et al., 2013). And finally, the study complements prior research on organization design view to outsourcing in general (e.g., Handley and Benton, 2012; Narasimhan et al., 2010).

2. Conceptual background

2.1. Organizational design in the PSM context

Following Greenwood and Miller (2010), we use the term organizational design as a conventional designation for “organizational architecture”. In the PSM context, most research on organizational design has addressed the degree of centralization (locus of decision-making) at the firm level, describing PSOs as having a centralized or decentralized design (Arnold, 1999; Gunipero and Monczka, 1997; Glock and Hockrein, 2011; Johnson et al., 2014; Narasimhan and Carter, 1990; Schneider and Wallenburg, 2013). A hybrid organizational design also has been identified, combining aspects of both centralized and decentralized designs (Johnson and Leenders, 2001). In a hybrid design, for example, responsibility for negotiating some long-term contracts are maintained at the firm level, while subsidiaries place orders within the limits of these contracts (Trautmann et al., 2008a). Therefore, in contrast to centralized and decentralized designs, hybrid designs require both a global level and local level of analysis.

For developing understanding of the potential relationship between organizational design and outsourcing in the PSM function, the degree of centralization level fails to offer sufficient detail; there are potential variations in how companies might have organized themselves beyond the centralized-hybrid-decentralized framework. Classically, firms’ division of tasks and generic organization designs are assessed along functional, geographic, and product-based dimensions (Galbraith, 2002). Taking a closer look at organizational designs for PSO reveals that companies can design their PSOs by purchasing categories, geographic area or product lines (Gunipero and Monczka, 1997; Karjalainen, 2011; Narasimhan and Carter, 1990; Trautmann et al., 1990). Jia et al. (2014) highlight that firms can have four levels of purchasing: global commodity team (category), business unit (BU) purchasing, plant purchasing, and International Purchasing Offices (IPOs). Both plant level purchasing and IPOs could be considered as a geography-based design. Moreover, some practitioner research identifies activity as the fourth structural alternative beyond category, geographic area or product line (Procurement Strategy Council, 2009, 2013).¹

¹ A practice-oriented study suggests that companies structure their PSOs rather equally mainly by category (28%), activity (26%), and customer (24%), somewhat less by geography (17%) (Procurement Strategy Council, 2013). While the advent of such an activity-oriented organizational orientation in PSM was predicted by Trent in 2004 already, its realization was not reported in research until recently.
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