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Outsourcing congruence with competitive priorities: Impact on supply chain and firm performance

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ABSTRACT

The growth of outsourcing has led outsourcing strategies to become an increasingly important component of firm success (Gottfredson et al., 2005). While the purported goal of outsourcing in supply chains is to derive a competitive advantage, it is not clear whether the outsourcing decisions of firms are always strategically aligned with their overall competitive strategy. In this paper we evaluate the degree of congruence (fit or alignment) between a firm's outsourcing drivers and its competitive priorities and assess the impact of congruence on both supply chain performance and business performance, using empirical data collected from manufacturing business units operating in the United States. We find outsourcing congruence across all five competitive priorities to be positively and significantly related to supply chain performance. We also find the level of supply chain performance in a firm to be positively and significantly associated with the firm's business performance.

1. Introduction

It is abundantly evident that outsourcing is a key business trend that has become increasingly important in recent years. While in the past, outsourcing was primarily relegated to the procurement of non-core components and services, today the outsourcing trend has expanded to include virtually every activity of a firm, including core and non-core components, business processes, information technology processes, manufacturing and distribution activities, and customer support activities (Chamberland, 2003; Gottfredson et al., 2005; Venkatraman, 2004). Today's hyper-competitive environment, characterized by constant change, market unpredictability, and the pressure to reduce costs and cycle times, coupled with the globalization trend, has provided further impetus to the growth of outsourcing (D'Aveni et al., 1995).

Outsourcing, which refers to the allocation of business activities from a source internal to an organization to a source outside of the organization, has become a key component of supply chain management strategies (Chase et al., 2004; Lankford and Parsa, 1999). Increasingly, manufacturing firms are now outsourcing functions and processes related to the supply chain, including research and design, product development activities, product component manufacturing, product final assembly and distribution and logistics functions (Heikkila and Cordon, 2002; Kirk, 2001). The growth of outsourcing has led outsourcing strategies to become an increasingly important component of firm success (Kakabadse and Kakabadse, 2000; Talluri and Narasimhan, 2004). While the purported goal of outsourcing supply chain functions is to derive a competitive advantage, it is not clear whether the outsourcing decisions of these firms are always strategically aligned with its overall competitive strategy (Garaventa and Tellefsen, 2001).

The numerous benefits of outsourcing are generally well established. The popular business press is replete with examples and cases of manufacturing firms that have been very successful in harvesting the benefits of outsourcing by reducing costs, improving speed and responsiveness, reducing cycle times, improving innovativeness, increasing flexibility and agility, and improving overall competitiveness (Chamberland, 2003; Jiang et al., 2006, 2007; Venkatraman, 2004). Clearly, there are important economic and competitive benefits from this ever-increasing outsourcing trend, however important debate continues to occur in the practitioner and the academic communities on whether organizations are often outsourcing functions without adequately conducting a strategic analysis of the long-term competitive impact of their outsourcing decisions (Hamm, 2004).

Recent research strongly advocates that to realize the potential for improved competitiveness, outsourcing decisions should be strategic in nature, and made in alignment with the competitive priorities of the firm (Chamberland, 2003). This requires that the

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outsourcing drivers are aligned or in congruence with the strategic goals and priorities of the firm. The competitive priorities of a firm are the direct manifestation of the firm's competitive capabilities and competencies, and are thus generally regarded as the firm's manifesto for operations (Ward et al., 1998). It is now well established in the recent operations management literature that a firm's competitive priorities can be defined along the dimensions of cost, flexibility, innovativeness, quality, and time (Skinner, 1966; Ward et al., 1998; Watts et al., 1992).

The relationship between strategic alignment and performance has been widely addressed in the literature. The strategy literature has generally shown that a fit between strategy and structure does have a positive impact on firm performance (da Silveira, 2005; Devaraj et al., 2004; Tarigan, 2005), but this does not automatically imply that a fit between "operations strategy" and "outsourcing drivers" will always produce favorable business results. In addition, to the best of our knowledge, the strategy as well as the operations literature seems to be devoid of any research study, empirical or analytical, that addresses the vital research questions related to what constitutes congruence between a firm's outsourcing decision drivers and its competitive priorities, and the impact of this congruence on supply chain and firm performance. While a large body of existing anecdotal and case based literature is available to help guide decision makers on outsourcing decisions, no comprehensive empirically based research studies exist in the literature that relate or link the alignment or congruence between a firm's outsourcing drivers and its competitive priorities to key indicators of firm performance. In light of the increasingly important strategic nature of the outsourcing of supply chain activities, this research effort is designed to examine if higher congruence between the drivers of supply chain outsourcing decisions and the operations strategy of a firm is significantly linked to improved supply chain and business performance.

Accordingly, the key objectives of this research proposal are to evaluate the degree of congruence between a firm's outsourcing drivers and its competitive priorities, assess the impact of this congruence on both supply chain performance, and investigate the relationships between supply chain and business performance. By utilizing survey based empirical data to address these research objectives, this study uses a novel methodology to measure the performance impacts of the degree of alignment between the emphasis placed by firms on their competitive priorities and the drivers of their outsourcing decisions.

The remainder of this paper is organized as follows. The next section presents the theoretical development of the research hypotheses. In Section 3, the research design and scale validation is presented. In Section 4, the methodology and analysis used to test the hypotheses is discussed, and the results are presented in Section 5. The managerial contributions of the findings are discussed in Section 6 and the contributions, limitations, and possible research extensions are presented in Section 7.

2. Theoretical development

2.1. Background

Outsourcing decisions require a firm to determine which activities they should vertically integrate and perform using internal resources ("insource") and which activities they should procure from a third party supplier ("outsource") (Stuckey and White, 1993). The growth in the importance of outsourcing can be attributed to the ability of outsourcing programs to create or protect competitive advantages for a firm (Narasimhan and Das, 1999; Venkatesan, 1992). This growth in importance has transformed outsourcing from a tactical procurement exercise to a strategic component of a business strategy (Kakabadse and Kakabadse, 2003). The strategic benefits and competitive advantages generated by a well-executed outsourcing plan can provide numerous competitive benefits, including improved quality, lower costs, increased flexibility, and superior product designs (Ettlie and Sethuraman, 2002).

Existing research in the outsourcing literature primarily addresses issues related to supplier selection, supplier management, supplier relationships, procurement strategy, outsourcing risks and benefits, etc. (Bozarth et al., 1998; Holcomb and Hitt, 2007; Jiang et al., 2006, 2007; Metters and Verma, 2008). To the best of our knowledge, there are no studies in the literature that address the issue of strategic congruence between the outsourcing drivers and competitive priorities of a firm and the impact of such congruence on firm performance.

2.2. Competitive business strategy and competitive priorities

The role that firm's business or competitive strategy plays in determining the firm's functional manufacturing and supply chain management strategies has been the subject of a considerable body of previous research (Devaraj et al., 2004; Kathuria, 2000; Miller and Roth, 1994; Skinner, 1966, 1969, 1974; Vickery et al., 1997). Competitive strategies usually drive a firm to compete as cost leader, differentiator, or as a focused provider (Porter, 1980). In manufacturing firms, the competitive business strategy is translated into competitive priorities and executed or operationalized through operational action plans (Hayes and Schmenner, 1978). Competitive priorities are the strategic business objectives and goals of the manufacturing organization (Koufteros et al., 2002). In the manufacturing environment, there are five traditionally accepted competitive priorities: cost, time, innovativeness, quality, and flexibility (Leong et al., 1990; Ward et al., 1998). The determination of the competitive priorities of a firm can be related to a firm's core competencies in two ways. First, a firm's competitive priorities may lead to the development of a supporting set of competencies and capabilities (Koufteros et al., 2002). Similarly, a firm may possess core competencies and capabilities that play a role in determining which priorities a firm chooses to focus on (Krajewski and Ritzman, 1999).

When determining its competitive priorities, a firm decides on the amount of time and resources that it invests in the various areas of its operations across the five competitive priority dimensions (Boyer and Lewis, 2002). This decision results in a trade-off strategy where a firm ideally focuses more resources on the activities related to its competitive priorities and fewer resources on non-priority activities (Boyer and Lewis, 2002; Kathuria, 2000). The focus of this study is not to determine how a firm establishes their competitive/operations strategy, but to assess (via our survey instrument) what operations strategies were being currently emphasized by the firms in our sample. The main objective of our paper is to assess the alignment between the operations strategies being emphasized by the firms, and the outsourcing drivers being employed by them.

The competitive priority scales adapted for use in this study measure the emphasis that a business unit places on each of the five competitive priorities when positioning the its primary product. The importance given to each competitive priority is measured independently of the other priorities, which allows us to assess the overall strategy, including strategic trade-offs adopted by a firm.

2.3. Outsourcing drivers

Consistent with the existing literature, we refer to the motivation, objectives, and goals of a firm's outsourcing effort