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Reconsidering outsourcing solutions

Per V. Freytag *, Ann H. Clarke, Majbritt R. Evald

Department of Entrepreneurship and Relationship Management, University of Southern Denmark, Engstien 1, 6000 Kolding, Denmark

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Summary Outsourcing continues to be an important strategic tool for firms. While outsourcing can take place without major problems, some firms experience problems. Unfulfilled expectations or new opportunities can make alterations to existing sourcing solutions necessary. Such reconsiderations may be due to internal or external changes. This article focuses on the reasons for reconsidering outsourcing activities, in addition to suggesting possible solutions that could be adopted by firms. Based on four case studies of Danish companies, four generic solutions for reconsidering outsourced activities are identified and discussed, which are based on three rival theoretical perspectives. The four generic solutions comprise: (1) maintain the original outsourcing partner; (2) obtain a new outsourcing partner; (3) backsource to own business; or (4) establish a new organisation. Finally, this paper discusses the rationales that underscore the four generic solutions, and outlines central considerations in the outsourcing process.

During recent years, many firms have changed their sourcing strategies after re-evaluation of their position, in order to improve activities and obtain the best conditions for developing, manufacturing, commercialising and delivering products or services to customers. This assessment has placed particular focus on outsourcing. Outsourcing refers to the practice of ''the operation of shifting a transaction previously governed internally to an external supplier through a long-term contract, and involving the transfer to the vendor'' (Quélin & Duhamel, 2003, p. 648). Outsourcing differs from a simple financial or purchasing decision (McIvor, Humphreys, McKittrick, & Wall, 2009). The strategy of outsourcing appears to have become today's solution to saving costs (Sharma & Loh, 2009) and strengthening core competences (Arnold, 2000).

* Corresponding author. Tel.: +45 65501380; fax: +45 65501357.
E-mail address: pvf@sam.sdu.dk (P.V. Freytag).

While outsourcing can provide benefits, it is often related to difficulties and unfulfilled expectations (Fill & Visser, 2000) or objectives (Barthélemy & Geyer, 2001), and there are increasing numbers of reports of firms that must re-evaluate their outsourcing solutions. An international survey by Dun and Bradstreet found that 20% of outsourcing agreements are terminated after two years, and 50% of agreements are terminated after four years (Business Wire, 2000). Moreover, a survey by Deloitte Consulting (2005) showed that 70% of respondents had negative experiences of outsourcing because their outsourcing objectives were not fulfilled, and 25% of outsourcing clients brought originally outsourced services back in-house (Mucisko and Lum, 2005). According to Veltri, Carol, Saunders, and Kavan (2008), two major reasons for terminating an outsourcing arrangement are either problems that cannot be resolved or new opportunities that appear. Brandes, Lilliecreutz,

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and Brege (1997) illustrate various problems with outsourcing that manifest through the outsourcing process (pace and commitment), the outsourcing decision (core competence, financial problems and cost efficiency reasons) and/or the outsourced unit (relation with parent, resource base and customer base). However, the difficulties that are experienced are not the only reason why companies reconsider their outsourcing activities. Internal and external business changes can create opportunities through which a new sourcing solution becomes attractive (Gadde & Håkansson, 2001). This corresponds with Narasimhan, Narayanan, and Srinivasan (2010), who found that outsourcing engagements evolve over time, leading to different outcomes. By studying successful outsourcing engagements it was found that operational (i.e. cost reduction and better quality), strategic (i.e. greater revenue and better resource allocation) and learning outcomes (increased process know-how) may be achieved depending on motives and contingencies (Narasimhan et al., 2010).

Recently, some authors primarily within IT have looked at different strategic choices to outsourcing problems. For example, continue outsourcing, switch vendor or backsourcing are given as solutions to outsourcing problems (Barney, Low, & Aurum, 2009; Veltri et al., 2008; Whitten & Leidner, 2006; Whitten, Chakrabarty, & Wakefield, 2010). Backsourcing is the act of bringing a once outsourced activity back into the organisation, with the goal to rebuilding internal capabilities (Veltri et al., 2008; Whitten & Leidner, 2006). The reasons for backsourcing IT were found to be senior management changes, costs, desire to regain control, poor relationships with vendor, performance and contract problems and/or a change in the perception of the outsourced activity (Veltri et al., 2008; Whitten & Leidner, 2006).

Few other authors (but see Narasimhan et al., 2010) outside of the field of IT have discussed solutions to outsourcing problems, and none have looked at broader generic solutions; thus, solutions such as spin-offs have not been discussed. This deficiency has not gone unnoticed, as Barney et al. (2009) note that few studies concentrate on what firms do after they terminate or fail to extend an outsourcing contract, and they argued that there is a need to study this important and increasingly frequent decision.

Therefore, there is a need for a better overall understanding of which options are available to firms when they must re-evaluate their sourced activity due to problems or new opportunities. Such information would gain further insights into what considerations ought to be made. Therefore, the aim of this article is to understand the options available to companies when faced with the challenges of outsourced activities that call for action and solutions. The article discusses this issue with respect to three questions:

1. What are the reasons for reconsidering outsourced activities?
2. What are the likely solutions when reconsidering an outsourced activity?
3. What are the rationales underlying various solutions?

First, we look at why firms may turn to alternative solutions of outsourced activities. This is discussed through a general literature review. From this review, three different theoretical perspectives on outsourcing are considered, to highlight different proposed solutions to outsourcing. Second, the methodology is presented; and third, the findings from four case studies are described. Fourth, in the analysis section, four generic solutions are proposed and discussed based on the three theoretical perspectives, to increase the understanding of the rationales underlying the four solutions. Finally, managerial and theoretical implications and recommendations for further research are given.

Reasons for reconsidering outsourcing

Outsourcing has developed from comprising mainly manufacturing activities to including all possible activities within a firm, such as product development, market intelligence, logistics, administration, sales, IT and business process services (Freytag, 1999; Rapp, 2009; Sharma & Loh, 2009). The elements of outsourcing have further transitioned from traditional manufacturing and peripheral functions to critical activities. Thus, outsourcing has become strategic in nature, and more risky (DiRomualdo & Gurbaxani, 1998; Hoecht & Trott, 2006; Quélin & Duhamel, 2003).

There are many arguments, and much evidence, stating why it is advantageous to outsource. Some of these advantages are listed by Lonsdale and Cox (2000), who emphasise the opportunity for firms to focus their resources on core activities, reduce their costs, convert their fixed costs to variables, attain benefits from the investments and innovations of their suppliers and the possibility of improving time to market. Moreover, various explanations concerning how to outsource an activity also exist. For example, some of these emphasise that it is important to control vendor opportunism and to incorporate incentives and penalties in contracts, in addition to pricing and monitoring clauses (Barthélemy & Quélin, 2006) and leadership capabilities needed for outsourcing (Useem, 2000). Other reports underline the importance of management maintaining a focus on the long-term consequences of outsourcing, which depends on ''the organization culture, the management philosophy, and the long-term and enduring choice of resources (capital, work, knowledge)'' (Kavcic & Tavcar, 2008, p. 247). Thus, little scepticism seems to exist about the benefits of correctly conducted outsourcing, and the task seems to be to identify the reasons for experiencing problematic outsourcing, which has been covered by several authors. For example, the ''Seven Deadly Sins'' of Barthélemy (2003) identify problems experienced by firms when outsourcing. These seven core problems were caused by (1) poor judgement of whether the activity should have been outsourced in the first place; (2) selecting the wrong supplier; (3) poor preparation of the agreement between the involved parties; (4) a lack of discussion regarding personal matters; (5) the firm losing control of the overview of the outsourcing process; (6) hidden costs of outsourcing which were overlooked; and (7) the absence of consideration for how to terminate the agreement with the supplier (an exit strategy). One of the problems often referred to is project cost overrun, or worse, the outsourcing project results in an increase in overall operations costs for the client (Shi, 2007). Also Lonsdale and Cox (2000, p. 450) highlight a list of problems concerning firms that appear to not have ''a robust