The Effects of Outsourcing in Logistics Services to Competitive Advantage

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Abstract

As the competitive business landscape has dramatically changed in the past ten to fifteen years, firms have to face the fact that they should take the necessary steps to decrease the fixed costs and increase the quality for the long-term success and survival. Accordingly, the logistics in general, for the manufacturing companies in particular, becomes more and more important. Numerous companies, providing outsource services such as logistics, have emerged to answer this growing demand. Accordingly, in this study, we aim to reveal the effects of Outsourcing In Logistics Services (OILS) on firm competitiveness and success through Semi-structured interviews conducted on the logistics managers of 7 companies. The findings mainly demonstrate that; i) Companies attach a great deal of importance on OILS and ii) OILS contribute obtaining and sustaining competitive advantage which ultimately results in superior performance.

Keywords: Logistics, Outsourcing, Logistics Outsourcing, Competitive Advantage

1. Introduction

Recent years have witnessed a growing interest in outsourcing of logistics functions. As the competitive business landscape has dramatically changed, firms have to face the fact that they should take the necessary steps to decrease the fixed costs and increase the quality for the long-term success and survival (Koçel, 2001; Fearon and Johnson, 2002; Doğruer, 2005). Accordingly, the logistics in general, for the manufacturing companies in particular, becomes more and more important (Baki, 2004a, 2004b). Many enterprises, which engaged in production, have to face the burden of logistics cost, which comprises most of the fixed costs (Barney, 2001). Thus new approaches and techniques in logistics, such as outsourcing, have the potential to result in obtaining competitive advantage for the firms since they can significantly contribute to reduce fixed costs and increase the service quality such as the delivery timeliness (Ballou, 1992; Kasilingam, 1999; Craig, 2003).

Outsourcing is becoming increasingly widespread approach for many firms all around the world, independent from the firm size and industry type (Frazelle, 2002). To answer this growing demand; a variety of companies providing outsourcing services have emerged, such as logistics service providers (Ataş and Uluengin, 2001; Keskin, 2006; Kağnicioğlu, 2007). Thus, logistics outsourcing has received a great deal of attention from both scholars and practitioners (Razzaque and Sheng 1998). Researchers have studied OILS from a number of point of views, including industrial differences, keys to successful logistics outsourcing relationships, selection of service providers, and international perspectives on logistics

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outsourcing (e.g., Boyson et al. 1999; Lieb, Millen, and Wassenhove 1993; Lieb and Randall 1996; Murphy and Poist 1998).

In this study, we aim to reveal the effects of OILS on firm competitiveness and success through qualitative techniques. The remaining of this paper is organized as follows. In Section II the concept of outsourcing in general and the logistics outsourcing in particular are discussed based on a deep literature review. Next the methodology is presented and the results are interpreted. Finally the conclusion part reveals the theoretical and managerial implications of the paper.

2. Theoretical Background

2.1. Logistics: Definition and the Mechanism

Today there is only a slight doubt that services have grown to lead world economic activity. (McLachlan et al., 2002). This significant growth in services is not at the expense of manufacturing industry; instead services have become an additional vital factor that supports primary industries to achieve global competitiveness. In fact, a considerable amount of the growth in services industry is attributable to traditional manufacturing industries “spinning-off” or outsourcing a range of previously incorporated service-based functions – such as logistics, communications, human resources (HR) and others – (Soosay, Kandampally & Jay 2002, p. 358-371).

Logistics is basically described as the detailed organization and implementation of a complex operation. From business point of view, logistics is the management of the flow of resources between the point of origin and the point of consumption in order to meet requirements of the final customers. The resource managed in this process involves physical items, such as food, materials, animals, equipment and liquids, as well as abstract ones, such as time and information.

According to the wide-held definition of The Council of Logistics Management (CLM); logistics management is “the process of planning, implementing and controlling the efficient, effective flow and storage of goods, services, and related information from point of origin to point of consumption for the purpose of conforming to customer requirements” (Lambert, Stock & Ellram 1998, p. 3).

Logistics, which is gaining more and more importance due to the today’s hyper-dynamic and competitive business landscape, has radically highlighted how the value is created through the supply chain, which ultimately results with a competitive advantage (Güner and Işık, 2003; 44). But how? Seeking an answer to this question, Ricardo Ernst claims that the global conditions have increased the importance of the process of logistics, which directly effects firm profitability. Indeed many firms were trying to develop processes focused on production, finance and marketing in past. This approach was stemmed from lack of knowledge about the value chain process, which takes up place between production and purchasing. Today, instead of decreasing the costs based on the production stage, firms aim to increase cash flow and profitability as carrying out the true processes of logistics to gain and maintain long term competitive advantage (www.btinsan.com). Dehler (2001, pp. 220-226) shows empirically that the higher the flow orientation of a firm, the higher is its logistics performance due to reduced logistics costs and increased levels of logistics service. This finding is of particular relevance, because Dehler (2001, pp. 233-244) also finds that logistics performance directly influences the overall firm performance.

Basic logistics functions can be sorted as demand forecast, inventory management, customer services, order processing, warehousing, handling and transporting. New trends and changes in the logistics field can be sorted as supply chain management, partnership agreements and logistics tools, globalization of supply chain, supplier controlled inventory management, just-in-time supply and production, negative stock and partial collection (milk run), consolidation, cross-docking, combined transportation, reverse logistics and integrated logistics and agile logistics.

All those given activities and functions should be implemented to meet customer requirements. Gaining and sustaining competitive advantage makes it necessary to meet or exceed the customer requirements through delivering the final customer the product or services with lower costs in a timely manner. Improvements can be achieved by concentrating on the coordination of the different functions. The coordination of lot sizes or just-in-time supply and production, where the required resources are provided exactly when needed. Resulting from the integrated understanding and planning of the procurement and production functions, cost and performance benefits emerge (Weber, 2002: 11). Such a management
approach involves inbound, outbound, internal and external movements. Here a main distinction in the nature of logistics arises in terms of inbound and outbound logistics (Porter, 1985)

Inbound logistics represents one of the primary processes of logistics, focused on purchasing and arranging the inbound movement of materials, parts, and/or finished inventory from suppliers to manufacturing or assembly plants, warehouses, or retail stores. On the other hand outbound logistics refers to the processes of storing and flowing of the final product and the related information from the end of the production line to the final user. Both types of logistics activities contribute to creating different kinds of value while at the same time they represent a source of logistics cost either. On the basis of basic logistics activities, the elements of logistics cost can be sorted as transportation cost, storage cost, handling cost, order tracking and information management cost, stock management cost and the other logistics costs.

Indeed the hyper dynamic business environments marked with dramatically changes on the market, technological and economical conditions result with tense the balance of cost and competition. So that, decreasing logistics cost is a mandatory for gaining and sustaining competitive advantage while simultaneously meeting the customer demands in a superior manner. How to keep the balance between reducing costs and keeping the customer satisfaction at the same time? Outsourcing emerges as a plausible way to achieve this end.

2. 2 Outsourcing

Outsourcing is a trend that seems to keep continuing over time. It has long been considered as a means to reduce costs, but cost reductions can only be achieved in specific conditions, e.g. the external provider must have access to economies of scale that the outsourcer does not. To sum up, if outsourcing was reduced basically to performing the same tasks at a lower cost, internal reorganization may well be a more efficient way to achieve this type of objective (Lacity and Hirschheim, 1993a), particularly since the managers often realize that cost savings are in fact not attained through outsourcing ventures. The switching costs are high and occurred as a result of outsourcing, such as those associated with supplier selection, negotiations, reorganization and control.

“When outsourcing first emerges, it was perceived as a tool for reducing the total amount of staff and creating cost advantage. But today it is not only used as a tool which decrease the costs, but also a business conduct that used for increasing operational effectiveness” (Özdil, 2002:17). In fact, outsourcing equates with more than just improved operational effectiveness. It is not just limited to peripheral tasks, such as catering or gardening, but also involves a growing number of the firm’s activities and functions, notably those that substantially contribute to its added value. This view of strategic outsourcing was introduced by Quinn and Hilmer (1994). However, if most firms in the same industry are to choose the same type of solution, such as outsourcing, the strategic advantage would no longer to be sustainable, as companies would all follow to the same business model (Porter, 1996). To be considered as a strategic choice, outsourcing must be a distinguishing characteristics of specific firms in an industry.

Alexander and Young (1996) question the conventional wisdom that core activities should be kept in-house and suggest several distinctions between the different types of core activities and core competencies. Activities critical to performance should be differentiated from the rest that create a competitive advantage. The second type refers to activities that create a current or potential competitive advantage for the firm. The first type refers to the activities, such as IT, logistics or facilities management, that support the core businesses, exclusive of a distinctive feature of a specific firm in its market. The overall scope of outsourcing is continuing to grow, as companies focus on their core competencies and shed tasks perceived as noncore (Lindner 2004).

2. 3. Logistics Outsourcing

Outsourcing undeniably is a strategic decision about at least one or more activities to implement or buy/hire (Hong, Chin and Liu, 2004:18). Rabinovich et al. (1999, p. 353) define logistics outsourcing relationships even more broadly as “long and short-term contracts or alliances between manufacturing and service firms and Third Party Logistics (3PL) providers”. It is necessary to examine the issue of logistics in outsourcing relationships. Unlike other forms of inter-firm relationships, such as joint equity ventures, franchising, alliances and buyer–supplier relationships, outsourcing is considered as a powerful vehicle to reduce costs, avoid risks and improve the efficiency of core functions by allocating part of a product value-adding function to external sources (McIvor, 2009). As a result of outsourcing, firms can focus on their main
operations and reduce the stock levels, by the time it reduces the capital investments for logistics activities. When the ratio of customer satisfaction increases for the firms, logistics costs can be reduced (Hong, Chin and Liu, 2004:18).

In the last couple of years, especially some industries giving more importance to OILS with the understanding of customer satisfaction and minimum stock level in the flow of goods and services from manufacturer to the last user (Wilding, 2004:628). While OILS has been defined in a variety of ways, this study follows the conceptualization of Murphy and Poist (2000), whom define logistics outsourcing as a relationship between a shipper and third party which, compared with basic services, has more customized offerings, encompasses a broader number of service functions, and is characterized by a longer term, more mutually beneficial relationship. This view of logistics outsourcing relationships underlines as a long-term exchange that suggests possible long-term benefits and advantages (Abdur Razzaque and Chen, 1998).

Outsourcing seems to be a more complicated mechanism than it has been in previous century. In past, most of the transportation activities were primarily being executed for physical performance of the service and have only the logistics services of transportation or storage. However, outsourcing relationships now are much more loosely coupled, mostly rely on contractual agreements, and have less or even no risk -or resource- sharing activities. Such relationships are open to external uncertainties, as fewer complementary resources are pooled to harden collaborative competitive advantages (Khanna et al., 1998); fewer commitment and risk sharing structures are triggered (Osborn and Baughn, 1990); and fewer mechanisms are set up for joint problem-solving and crisis management. Therefore, integration is important for outsourcing relationships. In recent years, because of standardized delivery systems and the rapidly changing technologies used in logistics, professional logistics providers have been able to perform much more efficiently and at lower costs than firms can achieve in house (Logan, 2000). More and more firms now are contracting out their logistics activities to third parties. Logistics outsourcing provides a great market value and is increasingly viewed as a key antecedent of a nation's business activities (Chen et al., 2010). So today, OILS includes long term planning which contains the control of the integrated logistics processes (Waters and Page, 2003:420).

With the benefit of OILS, outsourcing market will grow day by day and the suppliers of this service continue professionalization and give numerous services (Fernie, 1999:83). The primary advantages of outsourcing are (Bhatnagar et al., 1999:572, Kasilingam, www.utikad.org.tr, Baki, 2004:102); Focusing on the core competencies, reducing the costs, transformation of fixed costs to variable costs, knowing the costs before, determining the level of service, correct using of IT, processes and procedures, wide and flexible pool of resource, supply continuity and reducing the risks of costs and technology. In addition to those given advantages Fearon and Johnson (2002:300) put forwards the possible risks and disadvantages that stem from outsourcing are: Loss of control, exposing the risk of supplier: financial power, loss of outsourcing decision, slow application, lack of sensitivity etc. Good outsourcing decisions can result in lowered costs and competitive advantage, whereas poorly made outsourcing decisions can lead to a variety of problems, such as increased costs, disrupted service and even business failure (Cross 1995).

In logistics, the philosophy of “all or nothing” is not the right way of thinking. It should be taken into account that different combinations can be made in logistics services. Especially in warehousing and operations, which require improved technology, both insourcing and outsourcing activities can be witnessed. Particularly, a balanced combination can make the firm have the best results (Wilding, 2004:629). While outsourcing of logistics continues to grow, the level and type of outsourcing vary significantly across time, sectors, and companies. Some of the firms use service suppliers simply as a source of lower cost labor while others entrust suppliers with vast responsibility over their logistics network. Such differences reflect a range of motivations for outsourcing logistics that can be best described as “waves” of outsourcing (Kajita and Ohra, 2001).

3. Methodology

In this study, we aimed to reveal the consequences of outsourcing in logistics services on firm competitiveness and success through qualitative techniques. Briefly we try to identify if outsourcing in logistics services is an effective options for the firms, which try to minimize the costs and maximize the performance in a competitive environment, or not? We seek to find the answers of the following questions:

What are the positive or negative effects of OILS
Do OILS have any effect on the firms to obtain competitive advantage?

In addition, we also aim to enrich the Strategic Management literature by demonstrating the perceptions of managers towards OILS as a long-term strategic choice.

Our sample consists of seven big sized firms, located in Marmara Region operating manufacturing industry. Semi-structured interviews are conducted on the logistics managers of those companies. We assume that all of the questions, which were asked to the logistics managers, are understood correctly and all of the answers represent the exact opinions, thoughts and view of those managers.

We use qualitative research methodology (e. g. semi-structured interviews) in this paper to reveal the perceptions of logistics managers towards the effects of OILS on firm competitiveness and success. When focusing on a specific point, just like in our study, qualitative research techniques seem to be more proper as they adopt an interpretative approach on the methodical research problems. Thus, qualitative researchers can handle phenomena in their own environment. In this study, the main reasons of choosing the qualitative research techniques in this paper are given as follows:

Consideration of the possibility of not receiving the correct data through surveys, and

The intention of conducting a deeper research.

By means of semi-constructed interview forms, we intend to reach deeper and comprehensive information that represents the perceptions, views, ideas and experiences of the respondents.

**Table 1. The Questions Asked to The Logistics Managers.**

| Q-1 | What is the importance of logistics for your firm? |
| Q-2 | Do you outsource in logistics services? If you do, what are the reasons? |
| Q-3 | In which logistics services do you outsource? What is the most satisfactory and troubled outsourcing activity? |
| Q-4 | Which departments of your firm is most effective on your decision of logistics outsourcing? |
| Q-5 | Do you outsource from variety of service suppliers or a 3PL supplier? |
| Q-6 | Are the contracts which you signed with the logistics service suppliers long-term? If they aren't, what is the reason? |
| Q-7 | What is the most critical selection criteria for you about logistics service suppliers? |
| Q-8 | What are the results of logistics outsourcing for your firm in your opinion? |
| Q-9 | Is logistics outsourcing activity make you obtain competitive advantage against your rivals? |
| Q-10 | Do you think that you are successful in logistics outsourcing? If you don't, what are the reasons? How could you be more successful? |

After completing the interviews, recorded speeches are transformed into transcripts. Then the coded transcripts are submitted to content analysis. Content analysis, as a qualitative technique is generally being understood by the analysis of the materials, which is oral or written, systematically (Balci, 2000). There are four steps in content analysis:

Coding the data

Finding the themes

Arranging the codes and themes

Identifying and reviewing the findings

The themes and the focal points are determined by content analysis. Through the content analysis, resembling data are gathered around in the frame of specific concepts, themes were being edited and interpreted for the readers to understand (Yıldırım and Şimşek, 2005). The data are codified and carefully transcribed in order to keep the expressions of logistics managers without any change.
4. Results

The findings indicate that even logistics are considered to have a vital importance for firm competitiveness and ultimately firm success; the managers don’t perceive it as a main business line. Rather they are more likely to see logistics as a support function, which they need to carry out in order to implement the main activities. But one can easily come to the conclusion that any problem occurred on logistics services, can affect the main functions negatively. In this context, logistics functions do not only affect the firms’ goods or services’ unit costs, but also the quality.

The participants also indicate that they outsource most of the logistics services. Due to the structure of the firms, the content of these outsourced activities can range from stocking, distribution (transportation) to the all logistics services. Most of the participants claim that the main reasons underlying the outsourcing decision are decreasing the unit cost, sharing the responsibility and gaining time for the main business functions. The firms mostly outsource transporting, warehousing, typography and catering services. The most satisfactory results are reported for catering and warehousing while the most troubled one is transportation. The main reasons for those troubles arise from the lack of professionalism and the low education level of the transportation service’s personnel. In fact, there are some firms, which set up their own transportation firm as a forward integration strategy, based on a foresight of indecipherable distress about transportation sector. The precautions of making more comprehensive contract management and signing short-term contracts (one-year) are considered as a plausible solution for being more successful for transportation services.

As the logistics cover the functions from the purchasing to the marketing even the reverse logistics processes, the effectiveness of firms’ departments of production, warehousing, distribution, marketing and purchasing affect the logistics managers’ decision-making on OILS. According to the logistics managers, marketing and purchasing departments are on the forefront to make decisions regarding OILS.

The respondents approach 3PL services suppliers from the different point of views according to their firms’ structure and capacity. The managers of the firm, which make mass production and have higher capacity, express that their outsourcing activities are conducted with the 3PL service suppliers; while the rest indicate that they co-work service suppliers, which meets the contracts, enough for OILS.

The durations of contracts also differ according to the type of outsourced service. If the logistics service is critical for the core business and require the investments of the service supplier or the firm, the contracts are more likely to be set up for the long-term. On the contrary, if there are a variety of alternative logistics service providers, short-term contracts are preferred.

Sustainability, quality, reliability, availability, durability and adaptability of the service suppliers and the precautions about environment, health and safety; are found to be the key selection criteria by the logistics managers. But the most important issues emerge as the cost and the quality. The ranking of the criteria alters in line with the structure and capacity of the firm. The selection of the service suppliers’ is very important for most of the respondents. Indeed some of them admit that their firms have to cope with many complaints as a result of improper service suppliers, such as dirty trucks and environmental insensitiveness. On the contrary, some others address the good logistics services provided by the 3PL’s to be the main reason for their customer satisfaction. These are the indicators of OILS’ effect for gaining and sustaining

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Table 2. The Themes of The Research.

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<thead>
<tr>
<th>I.THEME</th>
<th>The Importance of Logistics for The Firm and Manager's Point of View of about Logistics</th>
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<tbody>
<tr>
<td>II.THEME</td>
<td>OILS Reasons and State</td>
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<td>III.THEME</td>
<td>OILS Fields and Satisfaction Rate</td>
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<td>IV.THEME</td>
<td>The Departments Effective on OILS</td>
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<td>V.THEME</td>
<td>Service Supplier Decision of The Firm and The Point of View About 3PL Service Suppliers</td>
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<td>VI.THEME</td>
<td>The Period of Contracts and The Reasons Effect</td>
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<td>VII.THEME</td>
<td>Choosing Criteria of Logistics Service Supplier</td>
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<td>VIII.THEME</td>
<td>The Results of OILS on The Firms</td>
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<td>IX.THEME</td>
<td>The Advantage of OILS on The Rivals of Firms</td>
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<tr>
<td>X.THEME</td>
<td>The Success, The Reason of Failure and The Ways of Success of Firms on OILS</td>
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</table>
competitive advantage as most of the logistics managers precisely declare that OILS has significant effects on having competitive advantage against their rivals.

As a sum, the interviews reveal that logistics is vital for their firm competitiveness and success even though it is not considered to be a main business function. The quality of logistics services has the potential to affect the quality of the product they produce as well as the unit costs. Because the time and effort that otherwise should be spend on possible problems instead of their core business activities. OILS seem to be a common way to gain and sustain competitive advantage. OILS enable the firms to get rid of high investment costs, renewal of the materials, extra personnel management and the costs of amortization. There are also the rivals who outsource in logistics service. But the road to competitive advantage and passes through establishing and maintaining synergic and harmonic relationships with the service suppliers based on a good contract management.

5. Conclusion

This study reveals the fact that, focusing on core business functions and transferring logistics functions to the professional and experienced service suppliers, contribute both customer satisfaction and unit-cost. Therefore, firms can take the benefit of saving their resources and they can become lean. Outsourcing in general OILS in particular emerges as an excellent way that enables firms to focus on their core functions and obtain competitive advantage.

Our study is followed by implications for practice. Based on the findings there are four main recommendations stand for the managers:

OILS should be recognized as an effective strategy for the firms to gain and sustain competitive advantage.

The service supplies selection process is vital (especially on the field of transportation). The contents and sanctions of contracts should be determined carefully.

The contents and period of the contracts should be shaped according to the importance of the service and the lack of the reasonable alternatives.

The firms should shape their structure according to the service suppliers in critical logistics processes on the environment of changing competitive atmosphere.

This study doesn’t only involve the logistics manager's understandings and views the positive/negative outcomes of logistics outsourcing, but also the contract management, employee potential, investments etc. In this way, the managerial and theoretical implications of OILS are discussed from a holistic manner.

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