OUTSOURCING – A WAY TO MAXIMIZE PROFIT

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Abstract:
In order to achieve the expected results in any kind of economic activities, this requires costs. Production activity generates high costs, because this activity involve side relationship, so that can not be discontinuity in process, a lot of personnel (salary costs), competitive fixed assets (expensive new technologies), etc..
This paper examines the economic implications of outsourcing within the context of the minimizing the costs, and implicitly maximizing the profit.
Outsourcing represents a huge economic opportunity for a developing any economy. Outsourcing means to delegate tasks or objectives to an external entities, which has expertise in some areas or offers a better price-quality report. Also, outsourcing includes a wide spectrum of activities, from operationally process to the firms functions.

Key words: *outsourcing, costs, profit*

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1. The concept of outsouscing

Outsourcing is subcontracting a process, such as product design or manufacturing, to a third-party company.[1] Outsourcing has been described as the assignation of services from one company to another (an activity as old as the first firms). It is essentially a division of labour.

The term has come to encompass the specific trend of importing services from low-cost providers located offshore – “**offshoring**.” The decision to outsource is often made in the interest of lowering cost or making better use of time and energy costs, redirecting or conserving energy directed at the competencies of a particular business, or to make more efficient use of land, labor, capital, (information) technology and resources.

Outsourcing involves the transfer of the management and/or day-to-day execution of an entire business function to an external service provider. The client organization and the supplier enter into a contractual agreement that defines the transferred services. Under the agreement the supplier acquires the means of production in the form of a transfer of people, assets and other resources from the client. The client agrees to procure the services from the supplier for the term of the contract. Business segments typically outsourced include information technology, human resources, facilities, real estate management, and accounting. Many companies also outsource customer support and call center functions like telemarketing, CAD drafting, customer service, market research, manufacturing, designing, web development, content writing, ghostwriting and engineering.

Outsourcing involves contracting with a supplier, which may or may not involve some degree of offshoring. Offshoring is the transfer of an organizational function to another country, regardless of whether the work is outsourced or stays within the same corporation/company.

[1] http://www.ventureoutsource.com/node/18/print

Multisourcing refers to large outsourcing agreements (predominantly IT).[2] Multisourcing is a framework to enable different parts of the client business to be sourced from different suppliers. This requires a governance model that communicates strategy, clearly defines responsibility and has end-to-end integration.

For any supply chain function, the most significant decision is whether to outsource the function or perform it in-house.[3] Outsourcing results in the supply chain function being performed by a third party. The process begins with the firm identifying the activity to be outsourced and generally using a make-buy analysis to justify the decision.

Due to the complexity of work definition, codifying requirements, pricing, and legal terms and conditions, clients often utilize the advisory services of outsourcing consultants (see sourcing advisory) or outsourcing intermediaries to assist in scoping, decision making, and vendor evaluation.

In the following figures it is displayed an activity evolution totally in-house and an activity evolution with outsourcing process.

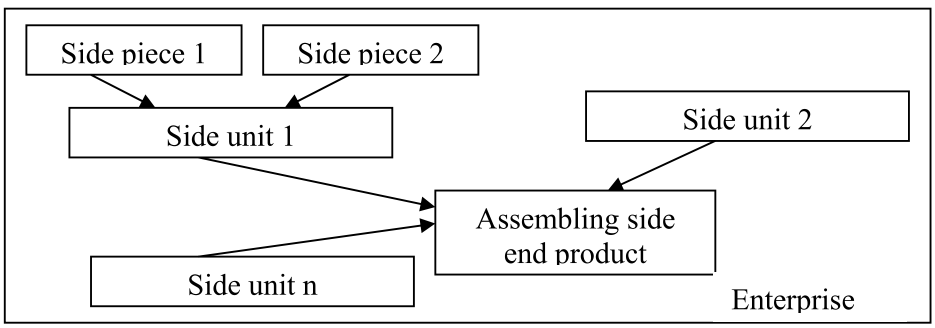

Fig. 1. Activity evolution totally in-house

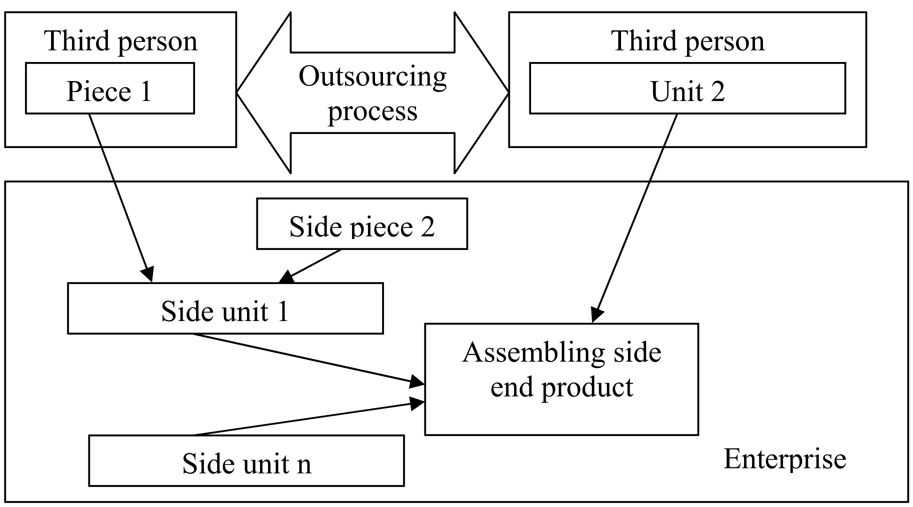

Fig. 2. Activity evolution with outsourcing process

When choosing a supplier or vendor, sourcing managers must compare options based on the supplier's impact on the total cost of ownership. Several other factors besides purchase price are included in total cost of ownership analysis. They may

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[2] http://www.btquarterly.com/?mc=mandatory-multisourcing-discipline&page=ss-viewresearch

[3] Chopra Sunil, Meindl Peter, Supply Chain Management: Strategy, Planning, and Operation. New Jersey. Pearson Education, Inc., 2007

include replenishment lead time; on-time performance; supply flexibility; delivery frequency(minimum lot size); supply quality; inbound transportation cost; pricing terms; information coordination capability; design collaboration capability; exchange rates, taxes, duties etc.; supplier viability.

2. Forms of outsoucing

a. Business process outsourcing is a form of outsourcing that involves the contracting of the operations and responsibilities of a specific business functions (or processes) to a third-party service provider. Originally, this was associated with manufacturing firms, that outsourced large segments of its supply chain.[4] In the contemporary context, it is primarily used to refer to the outsourcing of services.

This type of process is typically categorized into back office outsourcing - which includes internal business functions such as human resources or finance and accounting, and front office outsourcing - which includes customer-related services such as contact center services. When is contracted outside a company's country is called offshore outsourcing.

It is also categorized as an **information technology enabled service**, given the proximity of outsourcing to the information technology industry. Knowledge process outsourcing and legal process outsourcing are some of the sub-segments of business process outsourcing industry.

a_1. Knowledge process outsourcing is a form of outsourcing, in which knowledge-related and information-related work is carried out by workers in a different company or by a subsidiary of the same organization, which may be in the same country or in an offshore location to save cost. Unlike the outsourcing of manufacturing, this typically involves high-value work carried out by highly skilled staff. A fully developed service economy enables knowledge process outsourcing by treating all functions as services. It is easier to outsource a job if it is already being performed outside the head office.

a_2. Legal process outsourcing refers to the practice of a law firm or corporation obtaining legal support services from an outside law firm or legal support services company. When the outsourced entity is based in another country the practice is sometimes called **offshoring**. However, in recent years the so called "near shore", "back-door" "specialized legal firms" have sprung up to satisfy law firms and corporations that demand quality and confidentiality.

a_3. Recruitment Process Outsourcing is a form of business process outsourcing where an employer out sources or transfers all or part of its recruitment activities to an external service provider.

"Recruitment Process Outsourcing is when a provider acts as a company's internal recruitment function for a portion or all of its jobs. Recruitment process outsourcing providers manage the entire recruiting/hiring process from job profiling through the on-boarding of the new hire, including staff, technology, method and reporting. A properly managed recruitment process outsourcing will improve a company's time to hire, increase the quality of the candidate pool, provide verifiable metrics, reduce cost and improve governmental compliance."[5]

The Recruitment Process Outsourcing Alliance, a group of the Human Resources Outsourcing Association, approved this definition in February 2009: "Recruitment Process Outsourcing is a form of business process outsourcing where an employer transfers all or part of its recruitment processes to an external service provider. An recruitment process outsourcing provider can provide its own or may

[4] http://www.ventureoutsource.com/node/18/print

[5] Recruitment Process Outsourcing Association

assume the company's staff, technology, methodologies and reporting. In all cases, recruitment process outsourcing differs greatly from providers such as staffing companies and contingent/retained search providers in that it assumes ownership of the design and management of the recruitment process and the responsibility of results."

It could be said that the biggest distinction between recruitment process outsourcing and other types of staffing is process. In recruitment process outsourcing the service provider assumes ownership of the process, while in other types of staffing the service provider is part of a process controlled by the organization buying their services.

b. Co-sourcing is a business practice where a service is performed by both staff from inside an organization and also by an external service provider.

The aim of work may focus on one or more aspect of the internal audit function. Examples of co-sourcing services are supplementing the in-house internal audit staff with specialized skill such as information risk management or integrity services, providing routine assistance to in-house auditing for operations and control evaluations in peak period activity and conduct special projects such as fraud investigation or plant investment appraisals.

Outsourcing part of software development activities to an external organizations, while keeping part of the development in-house is another example of co-sourcing.

c. Crowdsourcing means the act of taking a task traditionally performed by an employee or contractor, and outsourcing it to an undefined, generally large group of people or community in the form of an open call. The public may be invited to develop a new technology, carry out a design task, refine or carry out the steps of an algorithm, or help capture, systematize or analyze large amounts of data.

d. Engineering process outsourcing for the architecture, engineering and constructions industry is a vertical domain for the industries of the built environment.

It is playing crucial role in efficiently supporting dynamic architecture, engineering and construction industries worldwide. While at the other end it has opened up huge market for developing nations. Engineering process outsourcing for architecture, engineering and constructions industry is different from manufacturing and information technology for the simple reason that each project is unique. Architecture, engineering and constructions industry has huge variations and immense complexity and one of the biggest factor of economic indicators.

3. Profit - reasons for outsourcing

Outsourcing is one of the most important advantages of organizations because it is increasing a company’s flexibility. This process enhances the flexibility of an organization in different ways.

A company is becoming more flexible by transforming fixed into variable costs. This is possible because most services provided by outsourcing vendors are offered on a fee-for-service basis. A variable cost structure helps a company responding to changes in required capacity and does not requisite a company in investing in assets and hereby making the company more flexible. Outsourcing may provide a firm with increased flexibility in its resource management and reduce response times to major environmental changes.

Focusing on its core competencies, without being burdened by the demands of bureaucratic dictate a company is more flexible. Key employees are herewith released from performing non-core or administrative processes and can invest more time and energy in building the firm’s core businesses.

Another way in which outsourcing increases organizational flexibility is by increasing the speed of business processes. Using techniques such as linear programming is a way to reduce cycle time and inventory levels, which reduces a company's slack. Supply chain management with the effective use of supply chain partners and business process outsourcing increases the speed of several business processes, such as the throughput in the case of a manufacturing company.

A company can hereby help maintaining ambitious growth goals, which do not fit with regular incumbent strategies. Outsourcing therefore allows firms to retain their entrepreneurial speed and agility, which they would otherwise sacrifice in order to become efficient as they greatly expanded. It avoids a premature internal transition from its informal entrepreneurial phase to a more bureaucratic mode of operation.

Conclusions

It is obviously in the interests of profit maximizing firms to outsource activities. This will have the effect of reducing costs and hence increasing profitability. The benefits of outsourcing should therefore translate into higher productivity levels and output for the firms benefiting from outsourcing.

A lower cost maximize the profit because it is well-known that profit is induced as the subtract of the incomes and the costs.

Apart from the cost factor outsourcing also has some other benefits that help companies to earn profit. Researchers have also found that small firms and new startups gain more from outsourcing than large corporations. The latter have managerial structures that hinder their ability to take full advantage of outsourcing's benefits. Smaller and younger companies can easily organize themselves to utilize outsourcing, thereby gaining sales and competing better in today's global marketplace.

Organizations that outsource are seeking to realize benefits or address the following issues:

- The lowering of the overall cost of the service to the business. This will involve reducing the preoccupation, defining quality levels, re-pricing, re-negotiation, cost re-structuring.
- Resources are focused on developing the core business.
- Operating leverage is a measure that compares fixed costs to variable costs. Outsourcing changes the balance of this ratio by offering a move from fixed to variable cost and also by making variable costs more predictable.
- Achieve a step change in quality through contracting out the service with a new service level agreement.
- Services will be provided to a legally binding contract with financial penalties and legal redress. This is not the case with internal services.
- Access to operational best practice that would be too difficult or time consuming to develop in-house. Access to a larger talent pool and a sustainable source of skills, in particular in science and engineering.
- An improved method of capacity management of services and technology where the risk in providing the excess capacity is borne by the supplier.
- Companies increasingly use external knowledge service providers to supplement limited in-house capacity for product innovation.
- Through outsourcing the time is reduce to market. The acceleration of the development or production of a product through the additional capability brought by the supplier.
- An approach to risk management for some types of risks is to partner with an outsourcer who is better able to provide the mitigation.
- Countries offer tax incentives to move manufacturing operations to counter high corporate taxes within another country.

Although the above-mentioned arguments favor the view that outsourcing increases the profit of organizations, management needs to be careful with the implementation of it. Some tends to change their attitudes, personalities and character on how the way they talk to other clients. Among problems, which arise in practice are: a failure to meet service levels, unclear contractual issues, changing requirements and unforeseen charges. When outsourcing does not work out as planned the company might well experience the way in which outsourcing makes a company very dependent on a vendor and therefore very inflexible. Consequently, these challenges need to be considered before a company decides to engage in business process outsourcing.

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