

Empirical Research of Outsourcing In food Industries of Tehran, Iran

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ABSTRACT

The aim of this article was to investigate the extent of outsourcing practices, motivations, risks and firms criteria for selecting providers in Iranian food industries mainly based on descriptive analysis. It was found that the majority of survived companies (about 70 percent) outsource at least one activity. The most common activities that outsourced, were food Production, logistic and distribution of commodities, information technology and maintenance of equipments. This research also showed that there is a relation between size of company and doing outsourcing. The most criteria for selecting candidates were high quality of services provided by firms, good reputation, mutual trust and technical advantages. The main reasons for outsourcing were cost reduction, focus on core business activities, access to advanced technologies and capabilities, increase flexibility along with improving quality of services. The two main problems perceived by companies were losing control of the business and increasing dependence on suppliers.

KEYWORDS: Outsourcing, Iran, Food industry, motivations and problems.

1. INTRODUCTION

In these days, in order to firms gain competitive advantages, they must overcome to some issues such as limited sources, business difficulties, increase of prices, legal considerations and globalization.

In addition, in comparison with others, food industries have its own specific characteristics like consumers changing consumption patterns and life styles and their awareness about the need to eat safe, high quality and healthy foods – known as organic and functional foods.

In this competitive and complex environment, firms must be able to response customers' needs and market demands by means of reconsidering their management strategies to gain competitive advantages. One of the best strategies to prevail in domestic and global competition is outsourcing. Previous researches show that firms used it to gain competitive advantages by the aim of various factors like reducing cost, increasing flexibility, concentrate on core business and etc (Power et al., 2004; Lau and Zhang, 2006). There are numerous definitions for outsourcing; generally outsourcing can be defined as the activity that was previously done inside the organization to an external organization (Beaumont and Sohal, 2004). Also Lankford and Parsa (1999) defined outsourcing as the procurement of products or services from sources that are external to the organization. Outsourcing is quite a new business administration form that appeared and began to be used actively since 1990. Outsourcing is not very investigated phenomenon especially in food industry in Iran and most of published researches are focused on industries like automotive, bank, IT and insurance. Although outsourcing in agriculture and food industries has not been much studied in Iran (and even in the world) but some of Iranian firms used it to achieve some advantages. The objective of this study is to present a set of outsourcing reasons, problems and motivations in Iranian food industries in Tehran. Tehran is known as an important zone in economy development and represents Iran's growth market.

1.1. Motivations and problems of outsourcing

A large number of studies have analyzed the motivations of outsourcing from both theoretical perspectives (Quinn and Hilmer, 1994; Kakabadse and Kakabadze, 2000; Lankford and Parsa, 1999) and a practical point of view using case studies and surveys in different countries such as USA, UK, Australia, China, Spain, Iran and etc (Corbett, 1998; Fan, 2000; Bolumole, 2001; Gonzalez, 2005; Khaki, 2012). According to the literature, there are several motives that actuate institutions and organizations toward outsourcing. These motives can be categorized in economic, strategic and environmental classes (Lau and Zhang, 2006). Between this reasons, cost saving is one of the main economic objectives of outsourcing (Tijun, et al., 2012). Firms by outsourcing their non-core business activities try to focus to their basic competencies (Hayes et al, 2000). Hilmer (1996) suggest that outsourcing activities can allow the organization to maximize their returns on internal activities. He also states that outsourcing can facilitate the access to the service provider's capability and innovation efforts. Reducing risks, shorten lead times, improving quality of services, reducing costs, accessing advanced technology and management experiment are some of the other reasons for outsourcing (Bailey et al., 2002).

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Along with the multiple reasons for outsourcing there is also a potential risks which can lead to failure in outsourcing, Alexander and young (1996) highlighted that outsourcing can fail to create any new value for the company if it is implemented in the wrong circumstances. Gonzalez et al (2009) categorized outsourcing risks in three groups including generic risks, risks derived from the provider and risks derived from the clients. This survey also showed that the risks derived from the provider were more important than those derived from the clients. Some of the problems associated with outsourcing are identified by previous researches. Losing control of activity, poor supplier management and problems with confidentiality, legal dispute, disclosure, of commercial secrets and conflicts with vendor were the main listed problems (Bailey et al. .2002; Tijun, et al., 2012).

1.2. Selection of vendors

To maximize the potential benefits and minimize the dangers of outsourcing there is a need for an outsourcing strategy to select suitable vendor (Bailey et al., 2002; Choi et al.,1996;Tijun, et al., 2009). Every company who wants to outsource an activity needs to establish selection criteria and then to monitor the performance of outsources against these criteria. Bailey (1997) found that there is a significant link between how vendors were selected and eventual success of the collaborative venture. He stated that the most associated factors with the success were technical management, management ability, development speed and compatible aims of the contending company, bailey shows that the criteria used for selecting outsourcing contractors were mainly reputation, cost, previous contacts and technical capability. Tijun (2009) found that the main criteria for selecting outsourcing were high service quality and mutual burst.

2. METHODOLOGY

The aim of the research was to investigate the outsourcing activity in Iranian food industries in Tehran, their motivation for outsourcing, how outsourcing partners are selected and investigation the problems of outsourcing. A questionnaire developed from a framework established in the literature. This questionnaire consists of two sections. The first section investigated the background of the respondents and the companies; the second section consist of several questions in following aspects: having an outsourcing activity, trend of outsourcing, which activity are outsource , how vendors are selected, motivations of outsourcing and problems of outsourcing. All questions related to motivations, selection criteria and outsourcing problems were measured on a five point likert scalefrom “strongly agree” to “strongly disagree”. The developed questionnaire was sent by mail, to a sample of 125 active firms obtained through searching the Iranian ministry of Industry, Mine and Trade CD-ROM database. In total, information was obtained from 60 firms, almost a 48% response rate. The collected data were analyzed by Statistics Package for Social Science (SPSS).

3. RESULTS

3.1. General characteristics of firms

Table1 shows the general characteristics of the interviewed firms. A total of 60 food industries participated and comprised of food packers (8), dairy (8), cereal (7), fruit juice and beverage (10) and other industries (21). As it can be seen, the major sectors of food industries were present in this study. About 48% of surveyed companies employed 51-250 employees. Also the results show that working history of most of firms are more than 25 years (53%).

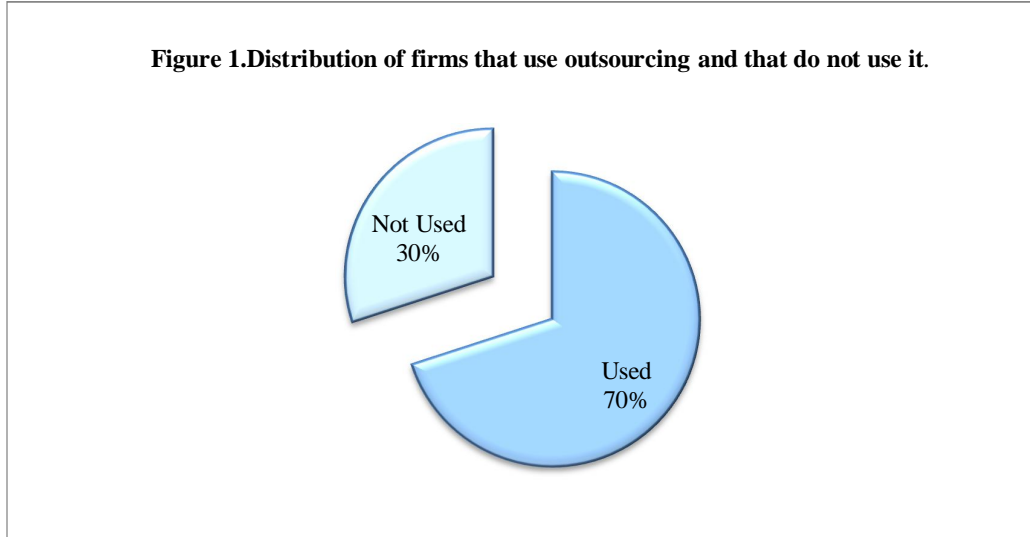
Table1. Demographic characteristics of the surveyed food industries(n=60)

Characteristics	n (%)
<i>Type of food industry</i>	
Fruit juice	10(16.7)
Food packaging	8(13.3)
Cereal and bakery	7(11.7)
Dairy	8(13.3)
Meat processing	6(10)
Other sectors(Conservation , Canning, Pickling and Sauce making)	21(35)
<i>Size of company(number of employee)</i>	
50 or fewer	12(20)
51-250	29(48.3)
251 or more	19(31.7)
<i>Age of company</i>	
25 years or more	32(53.3)
15-25 years	17(28.3)
15 years or fewer	11(18.3)

3.2. Distributions of firms that use outsourcing and or don't use it.

According the data given in figure1, we can see that 70 percent of enterprises use outsourcing and 30 percent do not use it. In general one can state that outsourcing in food industries in Tehran is used and widely spread.

Figure 1. Distribution of firms that use outsourcing and that do not use it.



A Chi-square test was applied to determine if a relationship exists between firm size and the outsourcing practices (Table 2). Chi-square test shows that there is a significant difference between firms with different sizes and doing outsourcing practices (Chi-square: 16.929; sig: 0.00).

Table 2. Relationship between the size of the company and usage of outsourcing

Size		Use outsourcing	Do not use
Less than 50	Count	3	9
	%	25.0%	75.0%
50-250	Count	26	3
	%	89.7%	10.3%
More than 250	Count	13	6
	%	68.4%	31.6%
Chi-square Value		16.92	
df		2	
Asymp. Sig. (2-sided)		0.000	

Firms that their personnel were between 51-250 employees, used outsourcing more frequently than others. About 90% of companies that were in this group used outsourcing; while only 25% of small sized companies with less than 50 employees and 70% of large companies used outsourcing.

Relationship between the age of company and outsourcing was also investigated.

The obtained results (table 3) show that there were no significant differences in the company age and doing outsourcing at the level of 0.01. This result is consistent with Parlow (2000) findings. The table also shows that the rate of outsourcing is higher, in firms that have more experiences.

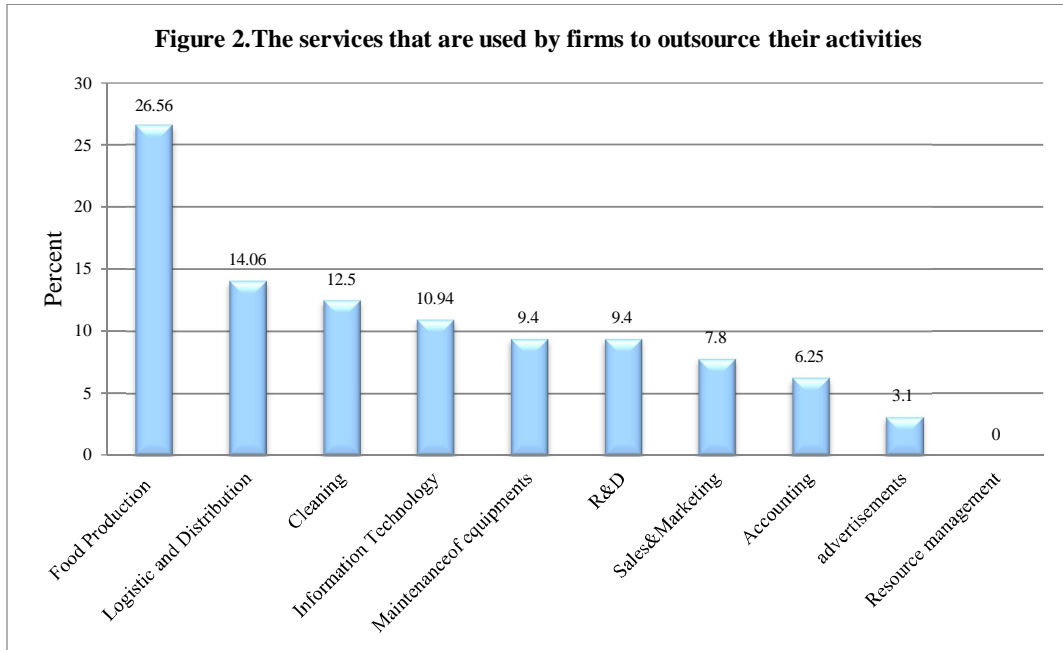
Table 3. Relationship between the age of the company and the usage of outsourcing

Age		Use outsourcing	Do not use
25 years or more	Count	24	8
	%	75.0%	25.0%
15-25 years	Count	12	5
	%	70.6%	29.4%
15 years or fewer	Count	6	5
	%	54.5%	45.5%
Chi-square Value		1.635	
df		2	
Asymp. Sig. (2-sided)		0.442	

3.3. The kind of services that outsourced by companies

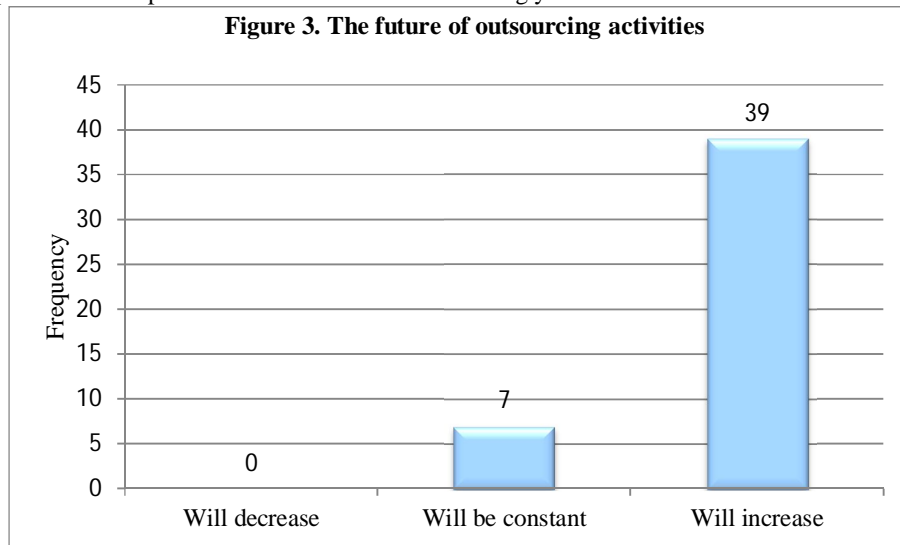
The range of activities that outsourced by firms is shown in figure 2. As can be seen the highest outsourced activity is food Production, followed by logistic and distribution of commodities, information technology and maintenance of equipments.

The least commonly outsourced activities were accounting and advertising services. The interesting issue was that none of the survived firms had not attempted to outsource their human resources management and all of firms want to do it by themselves. Results shows that Iranian food industries widely use from this phenomenon with different objectives.



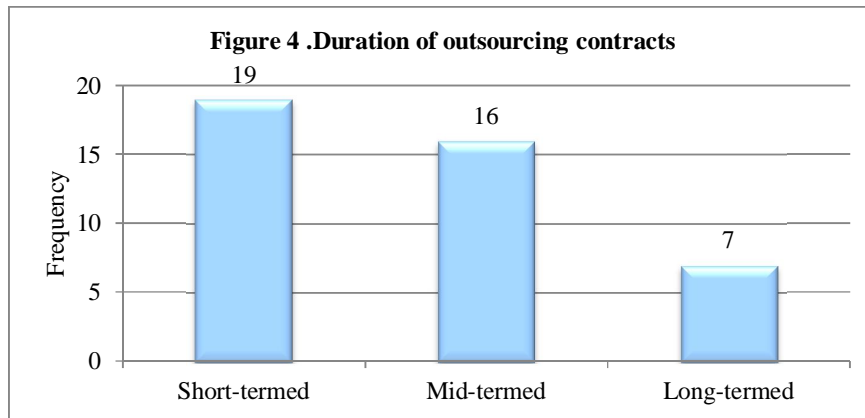
3.4. The future of outsourcing activities

The respondents were asked to indicate whether they believed their level of outsourcing was likely increase, decrease or remain the same. Figure3 shows that the majority of respondents (92.2percent) believed that their level of outsourcing will be increased in future and only 7.8percent of respondents answered that their level of outstanding will be constant. No one thinks that outsourcing will be decrease in next future. The obtained results show, in the opinion of the all respondents, outsourcing is important for companies and will increase in the coming years.



3.5. Duration of outsourcing contracts

As we can see in figure 4, 45.2% of survived firms have used short termed contracts, which take half year to one year. 38.1% of firms used mid-termed contract which take 2-3 years and long termed contracts which take 3-5 years. The results show that many of firms prefer short and to some extend medium termed contracting; this could be due to country's economic conditions and rapid change in business environments.

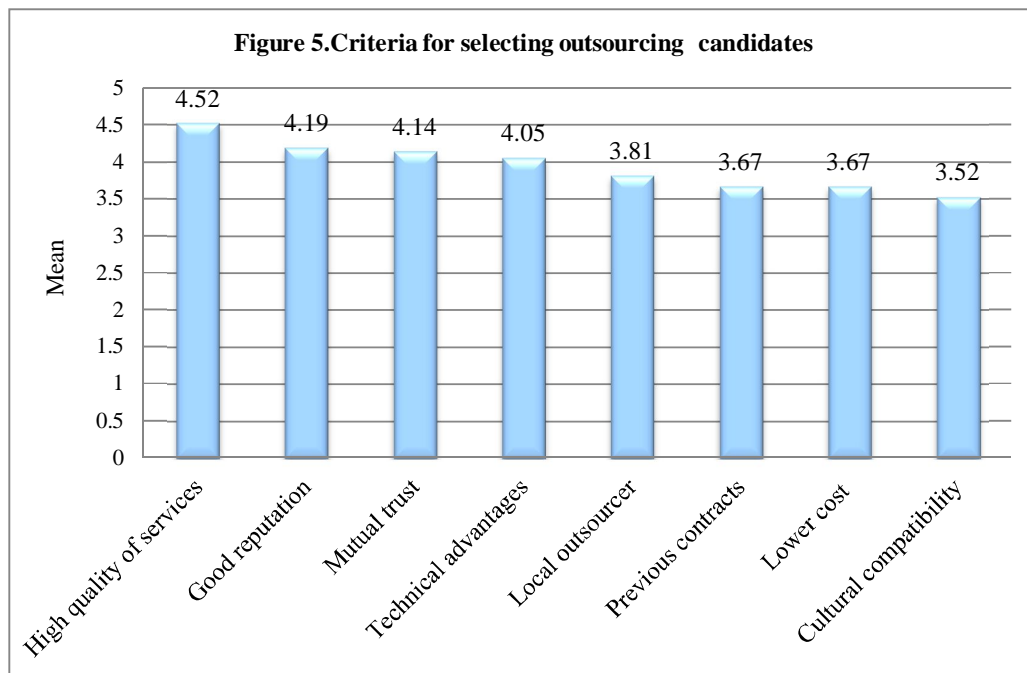


3.6. Criteria for selecting outsourcing candidates

From figure5 it is clear that, the most criteria for selecting candidates were high quality of services provided by firms, good reputation, mutual trust and technical advantages which all of them had a mean value more than 4. These results reveal that in the opinion of respondents the most important item for selecting outsourcing partners is the quality of services that provided by firms. The interviewees said that quality and safety standards are very important for them because, consumers demanding tasty, healthy and safety foods. For this purpose many of them have established quality control teams that visit supplier's production line periodically and even, in some cases they provide training programs for them.

The locality of outsourcers also gains a moderate importance from point view of respondents. Iran has a unique geographical diversity and every region is suitable for the production of particular agriculture commodities, in such circumstances it is natural that companies in order to diversify their basket of commodities, they must find suppliers in certain areas of the country.

The less important criteria for selecting eligible firms were cultural compatibility, lower cost and previous contracts. Regarding cultural compatibility, despite the respondent point of views, many of previous researches have shown that one of biggest reasons for failing outsourcing practices is cultural differences (Kvedaraviciene and Boguslauskas 2010). Although some of firms said that whenever they want to form a long-term and strategic partnership they consider factors like cultural compatibility, good reputation and mutual trust.

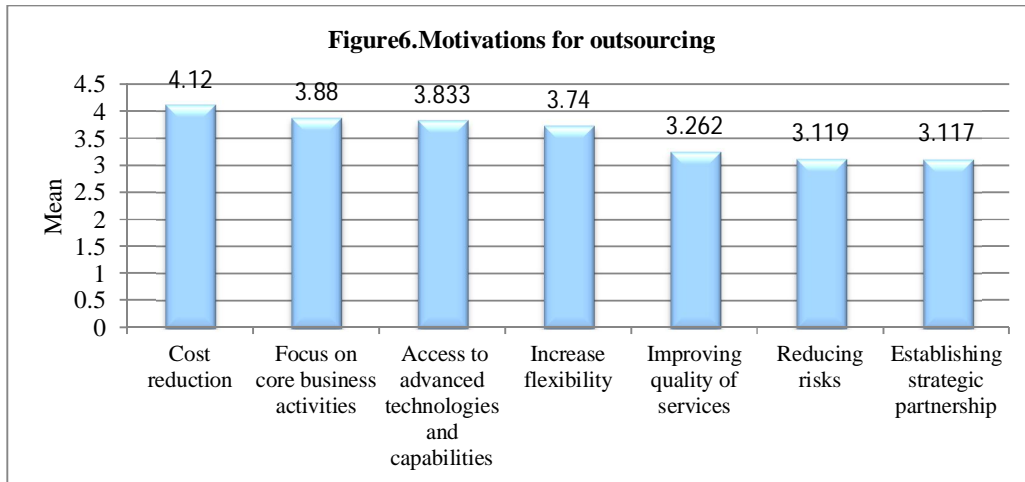


3.7. Motivations for outsourcing

The results are shown in Figure 6. As can be seen from this figure cost reduction was the primary reason for outsourcing. This finding supports Valohammadi (2012) and Lau and Zhang (2006) views. The second most important motivation for outsourcing was focus on core business activities. The respondent firms believed that outsourcing enables

them to focus on their core business activities and increase effectiveness of management and activities. Access to advanced technologies and capabilities, increase flexibility along with improving quality of services had high scores. The other

According to these results reducing risks, establishing strategic partnership forms were the least important motivations for outsourcing. Regarding to strategic partnership, many of respondent firms said that their aim of outsourcing wasn't forming long term strategic alliances with their providers. They also said that there have been cases that they have changed their service providers.



3.8. Problems of outsourcing

As can be seen from figure 7, the main two problems that firms indicated were losing control of the business and increasing dependence on suppliers. The mean score of these two items were the same. Loss of control is a problem that closely related to risk of business. Losses of control over outsourced functions posse a Substantial threat to ongoing operations inside a firm. This issue may affect firm's decisions moving for outsourcing their key activities in future. Excessive dependence created by outsourcing of important elements of work to the suppliers was another important concerns which ranked by firms.

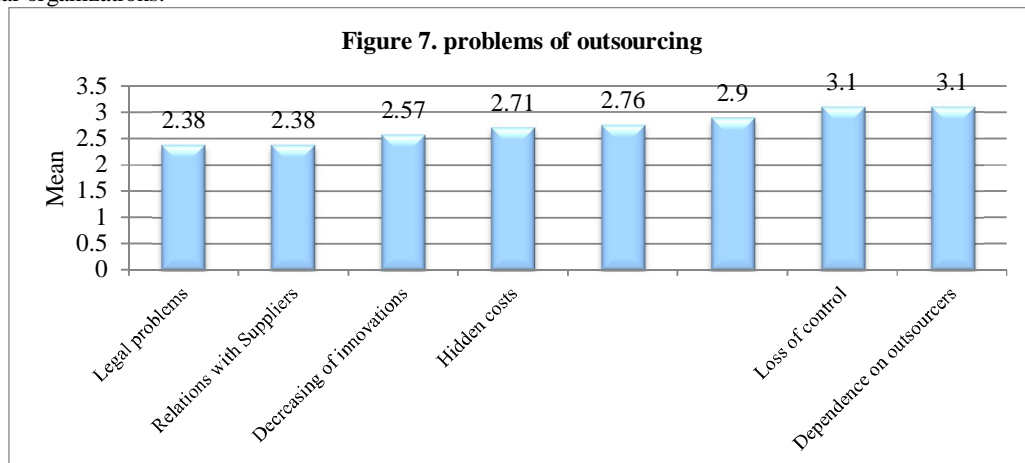
Disclosure of commercial secrets was another problem that respondents marked it. Some of the respondent companies were concerned about the exposure of their business tasks like experience, knowledge and professional skills.

Instability of economics conditions was the fourth most important risk encountered by respondents. This problem stems from inflation of raw material prices and services especially because of Iranian Targeted Subsidiary Plan implementation which hinders the process of negotiation and reaching an agreement with suppliers more difficult.

Another risk identified by respondents was hidden costs. On the base of respondent point of view these costs were related to provider selection, coordination and evaluation of vendors and creating good contracts.

Decreasing of innovations was the other item that respondents believed that was not important; this implies that firms did not believed outsourcing could affect the innovation process in a firm.

Legal problems and relation with suppliers were the less important risks related to outsourcing. Regarding legal problems, majority of respondents believed that Iranian legislations related to outsourcing and inter-firm cooperation were properly acted; although the few interviews said that they had problems in connection with the internal regulations of some governmental organizations.



4. Conclusion & discussion

The aim of this article was to investigate the extent of outsourcing practices, motivations, risks and firms criteria for selecting providers in Iranian food industries mainly based on descriptive analysis.

The obtained results showed that majority of surveyed firms (70 %) outsource at least one or more of their activities. The most commonly outsourced firm's activities were food Production, logistic and distribution of commodities, information technology and maintenance of equipment.

The most important motivation for outsourcing was cost saving. Reducing risks and establishing strategic partnership were the least important motivations for outsourcing. These results showed that firms when making outsourcing decisions, take consider both economic and strategic factors. Although some of these strategic factors were rated far lower in comparison of other motivations.

The most important criteria for outsourcing were high quality of services, good reputation and mutual trust. The less important criteria are related to lower costs and cultural compatibility. This view was not supported by the many of the literatures. For example Hendry (1995) and Kvedaraviciene & Boguslauskas (2010) have emphasized on the importance of cultural compatibility on success or failure of outsourcing practices while respondents were not considered cultural factor to be significant. Another important issue was that the outsourcers did not focus on cost as the main factor for selecting outsourcing partners. This can be a strong point for the surveyed companies because, on the basis of Bailey (1997) and Choi & Hartley (1996) findings giving only priority to cost rather than quality and technical ability could have deadly results for outsourcing. Regarding risks, the main identified risks were loss of control, dependence on suppliers, the instability of economic conditions and disclosure of commercial secrets. Although these problems were considered not important or of little importance by the great majority of the respondents, but underestimating the associated risks can threaten the future of outsourcing. Thus all managers should be aware of these difficulties and with considering cost, as well as qualitative and quantitative criteria difficulties correctly identified and right providers be selected.

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