

THE ROLE OF ENVIRONMENTAL DYNAMISM ON OUTSOURCING PERFORMANCE IN MALAYSIA

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ABSTRACT

This research aims on the environmental dynamism and outsourcing success. This study was to examine the impact of environmental dynamism as a moderator on the outsourcing success. In this research, outsourcing performance will affect by three dimensions in environmental dynamism: (a) customer demand, (b) level of competition, and (c) technology changes. Postal survey from electrical and electronic manufacturing industries in Malaysia was used to collect data. The findings from the data collected by the hand delivery survey showed support for the hypotheses of the research. Hierarchical regression analysis was carried out to determine the moderating effect of environmental dynamism on outsourcing success. The result of the research indicated full support of these moderating effects. This paper presents a useful source of information for practitioners that seeks to improve the outsourcing performance.

Keywords

Outsourcing success, market competition, E&E manufacturing, customer demand.

1.0 INTRODUCTION

Vision of Malaysia is to become a more competitive developed country and achieve high-income economy by the year of 2020. Therefore, the nation has been carrying out an economic plan which is Economic Transformation Program (ETP) since October 2010 to achieve the vision. The objective of ETP is to increase the Gross Domestic Product (GDP) of Malaysia in which there will be a significant increase of employment opportunities, employee could enjoy higher paid jobs and learn and strengthen their skills base.

Productivity Report 2010/2011 claimed that one of the main contributors to the nation's GDP is manufacturing industry (MPC, 2010). In the meantime, as a largest contributor to the manufacturing sector, electrical & electronics (E&E) industry is an important engine of the economy growth. The significantly contribution of E&E is the

manufacturing output (31%), exports (48.7%) as well as employment (33.7%) in the country (MIDA, 2012). However, supply chain could be one of the potential factors affecting the performance in the manufacturing process because this is where the factory obtains the raw materials.

According to the International Trade and Industry Ministry of Malaysia, Datuk Seri Mustapa Mohamed, we must engaging and communicating actively within local and international levels to improve and enhance national competitiveness (Bernama, 2011). Companies could stand out from the competition with the appropriate and successful local or international outsourcing because outsourcing generated greater value for the companies. In the meantime, competitive edge has been enhanced while companies focus solely on their core competencies. When they rely heavily on the outsourcing partner for operations and process something that out of their area of expertise, this in turn saves them resources (Khong, 2005). The primary initial reason that companies start outsourcing is cost saving (Murray & Kotabe, 1999; Walker & Weber, 1987). This synergy is helpful to both parties in terms of monetary and non-monetary in the short and long run (Khong, 2005). As a result, competitiveness and financial performance, cut costs, increase capacity, productivity, efficiency, and profitability of an organization can improve through the successful outsourcing implementation strategy (Elmuti, 2003).

Greater efficiencies and cost reductions are two drives that motivating organizations to specialize in limited key areas and practice outsourcing (McIvor, 2010). Nowadays, small medium companies outsource almost everything from administrative services, knowledge-intensive services, cleaning and catering services to information technology (Perunovic, Christoffersen, & Mefford, 2012). Outsourcing has enabled company to improve their overall business performance when they do not have to take care of the non-core business operation. Moreover, some companies are also able to access to the new markets, get more resources and more advanced technology and skills which further enhance their competitive advantage in the

competitive and rapidly expanded market through outsourcing. However, some resources are very unique and help organization stand out from the competition and the scarce resources should be held only in the organization. Therefore, resources are a valuable asset to an organization to counter threats and exploit opportunities, the organization should be in the implementation of the outsourcing strategy of resource allocation. As said by the resource-based theory, every single company is a unique bundle of assets, resources that if employed in distinctive ways can create competitive advantage (Barney, 1991).

2.0 LITERATURE REVIEW

2.1 Outsourcing Success

Outsourcing enables the company investigated which areas of production are needed to maintain the value-added chain and on which products and activities the company should focus to achieve optimal performance (Dekkers, 2000). According to Gilley and Rasheed (2000), outsourcing is defined as “the substitution of activities performed in house by acquiring them externally, although the firm has the necessary management and financial capabilities to develop them internally. It is also an abstention from performing activities in house.” Meaning to say, outsourcing is a strategy that involves of long-term contract between two parties to attain win-win situation.

From the previous empirical research, it showed evidence of a positive relationship between outsourcing and the financial performance of firms (Friedrich & Gellrich, 2004). Friedrich and Gellrich (2004) indicated that the organizational performance is as well mainly evaluated by financial element. Through outsourcing, firms allow to increase focus on its core activities (Quinn, 1999), decrease production costs as particular suppliers are used (Kotabe, 1998), and increase the firm’s strategic technological capabilities. This helps to lower fixed costs and break-even point of a firm reducing investment in manufacturing capability. Hence, outsourcing management may become a supportive model of enhancing a firm’s financial performance.

Outsourcing not only brings the improvement in terms of profitability but it also enhances the productivity of firms. There is some empirical research shows the positive relationship between the rate of outsourcing and productivity growth (Elmuti, 2003; Jiang & Qureshi, 2006). Quinn (1992) defined outsourcing as “virtually all staff and value chain activities are activities that an outside entity, by concentrating specialists and technologies in the area, can perform better than all but a few companies for whom that activity is only one of

many”. According to Abraham and Taylor (1996), firms “contract out” services in order to enhance production cycles and promote to specialization.

Outsourcing tends to ensure accessibility of higher quality goods and services in the future by creating competition among outside suppliers Kotabe (1990). Despite the fact that, outsourcing has its own risk also (Quinn, 1992). An outsourcer has the chances to take advantage of emerging technology capabilities without investing any capital in that technology. Therefore, the outsourcer has the choice of suppliers when market conditions demand.

2.2 Environmental Dynamism

Business operating in environmental dynamisms characterized by the high level of competition within industries, variable customer demand, and rapid technology changes. Environmental dynamism may enhance and increase the effect of outsourcing (Gilley & Rasheed, 2000).

Resource-based theory (RBT) is important to a company, as this theory is influential in business strategy decision particularly in outsourcing aspect (McIvor, 2010). He claimed that the unique capability of a firm is essential to create, maintain, and improve its competitive advantage. According to Joongsan and Rhee (2008), technology uncertainties act as a moderator in Korean automotive industry from Asia perspectives. Thus, this supports that the benefits of outsourcing increases as the increasing of environmental dynamism.

Customers demand. D’Aveni and Ravenscraft (1994) claimed that when the industry demand varies, without implementing an outsourcing strategy, the particular firm has to bear a huge amount of expenses in terms of administrative, coordination and information processing cost. Therefore, in this event, outsourcing is recommended, as the risk of declining demand would be shifted to the supplier firms.

The inability to forecast accurately the volume requirements or customer demand is defined as volume unpredictability (Walker & Weber, 1984) which contributed by the instability of the downstream market and the manufacturer’s share of this market. Therefore, an essential characteristic of collaboration in the face unanticipated change is the required to decline taking short-term advantage of the situation to one party’s unilateral benefit. It is easier to implement when the firm is more assured that both expectations of continuity offer it the capacity to reciprocate forbearance and to react against opportunism.

Technology changes. The emerged of technology changes may lead firms to decrease the usage of firm-specific resources (Harrigan, 1985, 1986) and cut down the firm's internalization process in the long-run. Since firms are allowed to partly transferring the risk of task variability to the intermediate markets with strategic outsourcing, specialized firms in these markets may be better able to achieve cost efficiencies that are difficult for focal firms to achieve by balancing task requirements across multiple customers. Teece (1980) state that as technological uncertainty increases, internal economies of specialization deteriorate in relation to the external economies of specialized firms. Managers may have the flexibility to change suppliers as technological advances warrant by increasing their reliance on manufacturing outsourcing during periods of high environmental dynamism.

Strategic outsourcing provides more conventional and organized patterns of exchange within and between firms. It may also act as a coping strategy helping to deal with risk by providing scale economies during periods of technological changes.

Level of competition. Kohli and Jaworski (1990) state that the level of competition arises from rapid changes in the composition of market share as the results of fast evolving customer demands and preferences. In high level of competitive markets, relationship orientation is more likely to be associated with positive outsourcing performance (Eisenhardt & Martin, 2000)

3.0 OUTSOURCING ACHIEVEMENT

According to Elmuti (2003), outsourcing success will help manufacturing firms to enhance their organizational competitiveness and financial performance, cost reduction, and improve profitability, capacity, efficiency, and productivity. This research study describes the outsourcing success from the aspect of strategic performance or internal process.

3.1 Strategic Performance/Internal Process

Kotabe, Mol, Murray, and Parente (2012) claimed that outsourcing success of a firm is related to its market share. They argued that market share would increase through outsourcing strategy. Outsourcing may be a good alternative to improve performance of a particular firm particularly in financial aspect in the short run (Gilley & Rasheed, 2000). However, up to a certain extent when the firm further outsources, the market share generally decreases. Kotabe et al. (2012) have furthered examined, analyzed and empirically confirmed this argument

by observing over 19,000 manufacturing firms. Meaning to say, they lost competitive advantages in the long run through excessive outsourcing (Gilley & Rasheed, 2000). For instance, Sony struggled from the competition within the electronic industries. They face crises, as they heavily depend on the electronic manufacturing services instead to produce lithium-ion battery and blue laser diodes. As the consequences, Sony postponed the release of Play Station 3 in the Europe and lost confidence from their consumers (Nikkei, 2006).

Khong (2005) investigated the effects of outsourcing on customer service quality. He claimed that customer service is an important element driving the success to a company as customers have the right to choose the best product in the competitive market. Therefore, quality customer service management contributed to high customer retention (Khong & Richardson, 2003). A survey questionnaire copy was sent to 1000 companies in Malaysia and 124 firms eventually responded. The foundation of the questionnaire was the framework being used in the past research. The findings significant indicated there was a positive relationship between outsourcing and customer service. Meaning to say, companies could improve customer service management through outsourcing.

4.0 RESEARCH METHODOLOGY

Postal survey is chosen to conduct the research study due to some reasons. This method is less costly compared to the other methods. Based on previous research study in Malaysia, postal survey is known as one of the most common methods used. Therefore, the target respondents are expected to express their perspectives in the survey successfully without the guidance of researcher. Besides that, from the theoretical aspect, it is possible to gather information data from a greater number of target respondents from different locations in Malaysia as it is more assimilated and practicable to manage compared to other methods which are labor intensive and costly. Regarding to previous researchers (Boon-itt & Himangshu, 2006; Rajagopal, 2006; Thi, 2006), there are high non-response rate with the postal survey. This brings effect to the quality and quantity of the data obtained from the sample. Since this effect cannot be eliminated exclusively, therefore a risk mitigation plan is needed. The purpose is to develop a well designed survey question layout, keep it attractive, stress on confidentiality, explain the intention of survey in the cover letter and give attention for non-response by estimating non-response bias through sampling non-response from the completed sample. The late respondents were followed up by resending reminders through postal survey again or by email contacts.

4.1 Sampling Design and Data Collection

According to MIDA (2012), E&E significantly contributes to the manufacturing output (31%), exports (48.7%) as well as employment (33.7%) in the country. The study covers the Malaysian electrical and electronic manufacturers listed on the FMM (2011) directory where the respondents targeted are from purchasing, planning, logistics, materials, corporate executive, and operation or production management level of the selected companies to provide information. They are expected to have adequate knowledge on the operation and management of outsourcing in their organization. The target companies which manufacture a range of electrical and electronic devices, equipment or apparatus were selected based from 12th International Standard Industrial Classifications.

The Directory of Federation of Malaysia Manufacturers has been commonly used by various researchers as a database to select population and sampling frame (Abdul-Halim & Che-Ha, 2010; Abdul-Halim, Che-Ha, & Geare, 2009; Abdullah, Che-Ros, & Kumar, 2007; Khong, 2005). In this study, there are a total of 865 electrical and electronic companies that are selected as the target respondents as they meet the selection criteria which are suggested by Ying (2006). The criteria stated that one should only consider companies that have more than 100 employees in outsourcing management studies since they are large enough organizations to participate actively in outsourcing management practices.

Postal survey was used to collect data from target respondents. Postal survey had been implemented from February 2013 to April 2013. There is a cover letter to describe the importance and objective of the research in the context of Malaysian outsourcing management for electrical and electronic manufacturing industry which includes the names of the academic institution and the signature of the project supervisor in order to improve the response rate.

The survey packet contained a cover letter as explained earlier on, the survey instrument brochure and a self addressed envelope. Self addressed envelope was used for the respondents' ease of returning the questionnaire. The respondents were given approximately four weeks to respond. Then a follow up mail with a replacement questionnaire was sent to increase the rate of response for those who have not responded. These follow-up letters served as a "thank you" to participants and as a reminder to those who had not yet returned their completed surveys (Dillman, 1978). The reconciliation of the survey ends by the eighth week.

The study focuses only on the Malaysian electrical and electronic manufacturing companies. The unit of analysis is at the organizational level as the objective of the study is to identify the effect of environmental dynamisms on outsourcing success. A total of 865 survey packets were sent to the entire population to increase the data collection rate. The returned questionnaires are sorted into early and late responses over two to three month period. A non-bias response analysis was conducted.

5.0 FINDINGS

Table 1 presented the analysis and finding of the study. Besides providing the data regarding the general characteristics of the sample and descriptive statistics of the major variables involved in the study. The findings from the data collected by the hand delivery survey showed support for the hypotheses of the study. Hierarchical regression analysis was carried out to determine the moderating effect of environmental dynamism on outsourcing success. The result of the study indicated full support of these moderating effects. The summary of the hypotheses on the relationship between environmental dynamism and outsourcing success is shown in Table 1.

Table 1: Summary of hypothesis testing for the interaction between environmental dynamism and outsourcing success

Hypotheses	Statement of Hypotheses	Remarks
H _A : a	Customer demand has a significant positive impact on the outsourcing success	Supported H _A : Hypotheses
H _A : b	Level of competition has a significant positive impact on the outsourcing success	Supported H _A : Hypotheses

6.0 IMPLICATIONS OF THE STUDY

6.1 The Managerial Implications

This study also provides practical contributions which can help supply chain managers especially in Malaysia in improving the outsourcing performance. Firstly, electrical and electronic manufacturing industries are facing various challenges in their business environment. These challenges may stem from internal factors such as their employees or external factors such as their competitor and customers.

6.2 Theoretical Implications

Particularly, this study found the empirical evidence for the theoretical relationship in the research

framework. This study has one hypothesis. The hypothesis is fully supported. This study discussed the role of environmental dynamism as a moderator on outsourcing performance of the manufacturing industries. This study found evidence that the manufacturing industries outsourcing performance can be related to the environmental dynamism. In general, outsourcing success is moderated by environmental dynamism which is customer demand and market competition.

Based on the prior study, there is a lack of study about the moderating effect of environmental dynamism in the strategic relationship, specifically outsourcing success in electrical and electronic manufacturing industry. Therefore, this study has established a research framework to access the moderating effect of environmental dynamism. Although this study is a new term of identifying the role of environmental dynamism as moderator, it is still governed by the relational view (Palmatier, Dant, & Grewal, 2007) and other related literature. These findings are an extensive contribution to the frontier of knowledge.

In brief, this study provides evidence that environmental dynamism plays a critical role in moderating the outsourcing performance. These findings provide support for the relational view of the organization, which focuses on the importance of uncertainty (environmental dynamism) in explaining outsourcing performance.

7.0 LIMITATIONS OF THE STUDY

In order to achieve superior outsourcing performance and sustain competitive advantages, companies are required to develop and implement practices that contribute to superior environmental dynamisms. There are several limitations in this study which give credit to the desirability of future research on effect of environmental dynamisms on outsourcing success. First, time series studies might discover how dynamic changes in the configuration of strategic relationship orientation might affect company specific outsourcing performance as a firm evolves in nature and in response to environmental changes. Second, learning constructs are only focused on the effect of environmental dynamisms on outsourcing success. The two main variables of environmental dynamism to be focused are customer demand and market competition.

8.0 CONCLUSION

This study has added to knowledge of the outsourcing performance by adopting process theory and resource-based view at the same time. The resulting framework is useful in providing a better understanding of how to develop effective strategies

or practices and decide the appropriate level of investment in outsourcing management from a managerial perspective. Future research should attempt to further specify the degree to which additional organizational and/or inter-firm variables might strengthen the validity of relationship orientation as a construct worthy of study in outsourcing management in different manufacturing industry.

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