

Drivers and obstacles of outsourcing practices in China¹

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Abstract

Purpose – To explore the key factors that motivate organizations in China to outsource and the obstacles these companies are facing in comparison with the situation in Western developed countries.

Design/methodology/approach – A case study approach was adopted with primary data collected through in-depth interviews with six companies in China and secondary data aggregated from company reports and documents. Research findings were analyzed within and across all case studies to identify key drivers and obstacles of outsourcing.

Findings – Economic factor is a strong motivation for outsourcing in China, of which cost reduction, cost saving, and capital investment reduction are the main concerns. Strategic considerations, such as the use of outsourcing to accelerate re-engineering benefits, to focus on core competence, to increase flexibility, and to facilitate market penetration, are identified. Environmental factors like information technology (IT) development and capability of supplier can influence organizations' decisions to outsource. Meanwhile, companies in China have encountered obstacles and problems in the outsourcing process. They include the lack of capable service providers, loss of control, poor transportation and IT infrastructure, presence of local protection regulations, and lack of overall post-outsourcing measurement.

Originality/value – This paper presents a systematic exploration of the drivers and the obstacles of outsourcing in China and provides a framework that may guide business organizations to make better outsourcing decisions. It may assist organizations to clearly define their expectations, develop strategic outsourcing plans, and make appropriate decisions to achieve outsourcing objectives.

Keywords Outsourcing; Supply chain management; China

Paper type Research paper

Introduction

Outsourcing is a fast-growing aspect of the world economy with a worldwide spending of about US\$3.7 trillion in 2001 (Clott, 2004). According to the latest survey jointly conducted by Cap Gemini, Georgia Institute of Technology, SAP, and DHL, the use of third-party logistics (3PL) services continues to increase in Latin America, North America, South Africa, Western Europe, and Asia-Pacific. For the years 2002 to 2005, the average percentages of

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usage in the five regions studied range from 67 to 84 percent (Cap Gemini *et al.*, 2006). Another survey conducted by Lieb and Bentz (2004) reveals that 83 percent of the Fortune 500 manufacturers use 3PL services. Driven by globalization and rapid advance in information technology (IT), organizations strive to improve competitiveness and responsiveness to customer and market demands (Razzaque and Sheng, 1998). Outsourcing has increasingly become an important strategy that can significantly assist organizations to leverage their skills and resources to achieve greater competitiveness (Quinn and Hilmer, 1994; Welson, 1996).

As a fast-developing country, China has long been recognized as a popular place to outsource (Matteo, 2003). Low-cost labor and high-technology manufacturing have made China the leading destination for outsourcing (Brown, 2005). With its accession to the World Trade Organization (WTO), China is in more favorable conditions to implement its economic reform and industrial restructuring. This has stimulated the development of logistics industry and fostered a growing demand for outsourcing (Agarwal and Wu, 2004). Nevertheless, the 3PL industry in China is still regarded to be in its infancy (Trunick, 2003). Although much has been written about outsourcing to China (Matteo, 2003; Brown, 2005; Forrest, 2005; Hannon, 2005), limited studies have been conducted to thoroughly investigate the key outsourcing drivers and problems that organizations in China have considered and encountered.

Objectives of the Study

Owing to the differences in economic and infrastructure development between developed and developing countries, it is likely that there will be different reasons for outsourcing in China that have yet to be determined. This study attempts to fill the gap in the literature by exploring the key factors that motivate organizations in China to outsource and the obstacles they are facing. Six case studies involving companies of different types of ownership are discussed to examine the strategic reasons of organizations in China for outsourcing and the problems they have encountered. A comparison between China and Western developed countries on the drivers and challenges of outsourcing is also presented.

Literature Survey

A large number of studies have analyzed the drivers of outsourcing from both a theoretical perspective (Trunick, 1989; Quinn and Hilmer, 1994; Razzaque and Sheng, 1998; Lankford and Parsa, 1999; Kakabadse and Kakabadse, 2000; Jennings, 2002; Lynch, 2004) and a practical point of view using case studies and surveys in developed countries such as US, UK, Australia, and New Zealand (Corbett, 1998; Fan, 2000; Bolumole, 2001; Al-Qirim, 2003; McIvor, 2003; Beaumont and Sohal, 2004; Kakabadse and Kakabadse, 2005). While many drivers are unique to specific organizations and industries, there are some common key factors that motivate organizations of all industries to make outsourcing decisions. These factors can broadly be categorized as economic, strategic, and environmental ones as summarized in Table I. By means of outsourcing, organizations can gain competitive advantage through cost reduction and improved responsiveness to changing business environment and market demand.

Table I Drivers of outsourcing

Economic factors	Objectives or anticipated outcomes	Authors
Cost reduction	<ul style="list-style-type: none"> - To improve profitability - To improve operating efficiency - To add value to product 	Trunick (1989), Richardson (1990), Gonzales <i>et al.</i> (2005)
Cost saving	<ul style="list-style-type: none"> - To improve cash flow - To increase efficiency 	Embleton and Wright (1998), Claver <i>et al.</i> (2002)
Capital investment reduction	<ul style="list-style-type: none"> - To make capital funds more available for core areas - To improve return on assets 	Corbett (1998), Razzaque and Sheng (1998), Trunick (1998), Lynch (2004)
Strategic factors	Objectives or anticipated outcomes	Authors
Acceleration of business process re-engineering	<ul style="list-style-type: none"> - To improve performance - To achieve competitive advantage 	Corbett (1998), Embleton and Wright (1998), Clott (2004)
Focus on core competence	<ul style="list-style-type: none"> - To improve business focus - To increase competitiveness - To leverage the firm's skills and resources - To enhance customer satisfaction 	Prahalad and Hamel (1990), Quinn and Hilmer (1994), Weerakkody <i>et al.</i> (2003)
Flexibility enhancement	<ul style="list-style-type: none"> - To reduce constraints of organization's own production capacity - To convert fixed costs to variable costs - To increase responsiveness to market change - To reduce risks 	Quinn and Hilmer (1994), Corbett (1998), Embleton and Wright (1998), Razzaque and Sheng (1998), Kakabadse and Kakabadse (2000), Jennings (2002), Lynch (2004)
Environmental factors	Objectives or anticipated outcomes	Authors
IT development	<ul style="list-style-type: none"> - To meet increasing demand for new information systems and resources more efficiently and economically 	Lynch (2004)
Globalization	<ul style="list-style-type: none"> - To help companies gain global competitive advantage 	Clott (2004)
Capability of supplier	<ul style="list-style-type: none"> - To enable partnering to improve service quality and customer service and increase competitive advantage 	Jennings (2002)

Although there are good reasons to outsource, a number of potential obstacles and problems associated with outsourcing are also recognized. There is evidence that outsourcing does not reduce costs as expected in some cases (Beaumont and Sohal, 2004; Gonzales *et al.*, 2005). As summarized in Table II, loss of control (Blumberg, 1998; Razzaque and Sheng, 1998; Lankford and Parsa, 1999; Kakabadse and Kakabadse, 2000; Claver *et al.*, 2002; Lynch, 2004), loss of critical skills (Quinn and Hilmer, 1994; Jennings, 2002; Beaumont and Sohal, 2004), inadequate capabilities of service providers (Razzaque and Sheng, 1998; Al-Qirim, 2003), loss of flexibility (Embleton and Wright, 1998; Beaumont and Sohal, 2004), failure to realize the hidden costs generated by the contract (Palvia, 1995; Kakabadse and Kakabadse, 2000; Gonzalez *et al.*, 2005), difficulty in obtaining organizational support (Razzaque and Sheng, 1998), indecisiveness on which activities to outsource (Lankford and Parsa, 1999), inadequacy of cost and benefit analysis systems (McIvor and Humphreys, 2000), fear of job loss (Razzaque and Sheng, 1998), and damage to morale of existing workers (Embleton and Wright, 1998), *etc.* are among the commonly cited inhibitors to outsourcing.

Table II Main obstacles and problems of outsourcing

Obstacles and problems	Impacts	Authors
Loss of control	- Loss of core competence - Risks of alienating customers	Blumberg (1998), Lonsdale and Cox (2000)
Loss of critical skills	- Loss of competitive advantage - Increased number of competitors	Quinn and Hilmer (1994), Jennings (2002), Beaumont and Sohal (2004)
Inadequate capabilities of service provider	- Loss of competitive advantage - Loss of market share	Jennings (2002)
Loss of flexibility	- Reduced responsiveness - Risks of alienating customers	Embleton and Wright (1998), Beaumont and Sohal (2004)
Failure to realize hidden costs of contract	- Increased operating cost	Palvia (1995), Kakabadse and Kakabadse (2000), Gonzalez <i>et al.</i> (2005)
Difficulty in obtaining organizational support	- Increased chances of failure	Razzaque and Sheng (1998)
Indecisiveness on which activities to outsource	- Increased chances of failure	Lankford and Parsa (1999)
Inadequate cost and benefit analysis systems	- Lower return on investment - Loss of competitive advantage	McIvor and Humphreys (2000)
Fear of job loss	- Increased resistance to change - Lower staff morale	Razzaque and Sheng (1998), Embleton and Wright (1998)

In recent years, the Chinese government has designated logistics as a strategic industry and invested heavily in improving infrastructure such as nationwide multi-modal transportation networks and large-scale modernized logistics and distribution centers (Trunick, 2003). The accession of China to the WTO has opened up several of her transportation and logistics sectors to direct foreign participation (Hertzell, 2001). Consequently, more intensive competition between Chinese and foreign companies, both inside and outside China, is expected (Agarwal and Wu, 2004). Meanwhile, the pattern of ownership of Chinese enterprises has gradually shifted from absolute dominancy of the state-owned enterprises to co-existence of ownership in hybrid forms (Chen and Huang, 2005). The increase in competition and growing awareness of the role of logistics lead more companies to exploit the potential of outsourcing. Manufacturers are increasingly looking for logistics solutions to move their goods to the fast-expanding consumer markets. Further, the trend towards consolidation in many of the industries and the emergence of national chains are also creating demand for outsourcing (Hertzell, 2001). Table III summarizes the key factors that are expected to stimulate the growth of outsourcing in China.

Table III Key factors stimulating the growth of outsourcing in China

Key factors	Descriptions	Results
Government initiatives	- Investment in logistics infrastructure	- Has encouraged domestic companies to outsource a greater percentage of their logistics needs
Entry to WTO	- High-quality foreign 3PL providers entering Chinese logistics market - Relaxation of regulations - Increased competition	- Has enabled companies to outsource more functions - Has encouraged more companies to exploit outsourcing potential
Economic reform and development	- Enlargement of consumer market	- Has increased demand for logistics solution
Consolidation in industries and emergence of national chains	- Creation of large and more complex players	- Has increased need for transportation and logistics solutions

Despite the favorable factors, China's 3PL industry is still in its early stage of development. Compared to an overall transportation and logistics expenditures of US\$230 billion in 2001, outsourced logistics was estimated to be just under US\$4.8 billion or about 2 percent (Kadar and Huang, 2002). Poor infrastructure and entrenched regulatory environment are among the obstacles that hinder the development of 3PL. Although the Chinese government has made significant investments in the logistics sector in recent years, there is little integration of transportation networks, information technology, warehousing, and distribution facilities. Meanwhile, regulations exert tight controls on business activities at provincial level, which hinders the creation of national networks (Kerr, 2005). Therefore, it is difficult for 3PLs in China to fully meet the requirements of their clients. Table IV summarizes the key challenges for the Chinese logistics industry.

Table IV Key challenges for the Chinese logistics industry

Challenges	Problems	Impacts
Poor Infrastructure	<ul style="list-style-type: none"> - Lack of effective transportation networks - Lack of IT infrastructure - Little integration of transportation networks, IT, warehousing, and distribution facilities 	<ul style="list-style-type: none"> - Higher transportation costs - Lack of reliability in pick-up and delivery time
Regulation issues	<ul style="list-style-type: none"> - Local protection 	<ul style="list-style-type: none"> - Has restrained the development of national service networks - Has made it difficult for 3PLs in China to fully meet the requirements of their clients
Finding qualified staff	<ul style="list-style-type: none"> - Lack of logistics training programs - Lack of high-quality providers with the scope and scale to fully meet customers' requirements 	<ul style="list-style-type: none"> - Shippers have little confidence in the service levels of 3PLs - Difficult to find good providers that can deliver high quality and consistent services across geographical regions

Methodology

This research uses a case study approach which means in-depth investigation of a contemporary phenomenon within its real-life context (Yin, 2003). The case study approach lends itself to a concentrated focus on the topic and allows a combination of multiple sources of evidence which enables the researcher to capture and place the complex reality under scrutiny (Saunders *et al.*, 2003; Yin, 2003). Despite its ability to explore the complexity of an issue, however, case study approach does have its limitation in the generalization of results. This is mainly because case studies are usually based on small samples for in-depth study. Inherent to most interview surveys, variations in position, knowledge level, experience, *etc.* of the participants in structured interviews also render generalization of survey result difficult.

Nevertheless, case study research is a commonly adopted strategy in the study of outsourcing decision (Benson and Leronimo, 1996; Fill and Visser, 2000; Bolumole, 2001; McIvor, 2003). The use of case study approach in this study ensures an in-depth exploration of the research question and enables the researchers to gain an insight into the real motivations behind the companies engaged in outsourcing, the obstacles and problems in the outsourcing process, and their impacts on the organization performance. In order to make the findings representative, companies chosen for this study were selected across a wide range of industries and from those which are currently involved in outsourcing.

Six in-depth, semi-structured face-to-face interviews, each lasting for about two hours, were carried out to collect primary data for this research. Judgment sampling was employed to

select sampling units of this study (Boyce, 2003; Zikmund, 2003). Survey respondents were selected from companies of three major ownership types in China, namely, state-, private-, and foreign-owned (The Institute of World Economics and Politics, 2005). Six persons, one from each of the six companies including departmental and senior managers directly participated in or responsible for making outsourcing decision, were interviewed. Secondary data such as company documents, reports, and web sites were also gathered to better understand the background of the responding organizations and their outsourcing performance. Tables V and VI summarize the profiles of the six companies studied and their outsourced activities, respectively. The name of each responding company has been coded to preserve anonymity.

Table V Profiles of the six companies studied

Company	Ownership type	Industry type	Establishment	Location	Annual company revenue	No. of employees	Position of interviewee
A	State-owned	Textile import and export company	1951	Beijing	US\$1.45 billion in 2004	700	General manager of a strategic business unit
B	State-owned	Agricultural product and food import and export company	1952	Beijing	US\$2.7 billion in 2004	1,000	IT department manager
C	Private-owned	Electronics and home appliance retailer	1982	Beijing	Eight billion Yuan in 2004	15,000	General manager of a chain store
D	Private-owned	Cultural business company	2000	Beijing	Ten million Yuan in 2004	10	General manager of the company
E	Foreign-owned	Measurement product manufacturer	1985 (entered China)	Beijing	US\$1 billion in 2004	2,000	Logistics department manager
F	Foreign-owned	Soft drink manufacturer	1979 (entered China)	Shanghai	US\$343 million in 2004	600	Human resource (HR) department manager

Table VI Outsourced activities of the six companies studied

Company	Main activities outsourced	Starting time
A	<ul style="list-style-type: none"> - 100 percent transportation - 100 percent warehousing - 100 percent freight and charge settlement, customs declaration, inspection, and insurance - IT outsourcing under planning in 2005 	1983
B	<ul style="list-style-type: none"> - 100 percent transportation - 100 percent warehousing - 10 percent IT support - There is plan to outsource more IT functions 	1982
C	<ul style="list-style-type: none"> - 90 percent transportation and warehousing - 100 percent deployment of seasonal workforce - 90 percent customer services including returns handling, installation, and maintenance work - 100 percent cleaning and catering - IT outsourcing under planning in 2005 	1999
D	<ul style="list-style-type: none"> - 100 percent printing - 100 percent cleaning and catering - There is plan to outsource other functions 	2000
E	<ul style="list-style-type: none"> - 100 percent transportation and warehousing management - 40 percent training - 100 percent renting of personal computers - 30 percent maintenance work - 100 percent cleaning and catering - There is plan to outsource more activities such as HR, accounting, administration, and manufacturing 	1999
F	<ul style="list-style-type: none"> - 100 percent transportation and 90 percent warehousing - 6 percent IT services - 30 percent training - 100 percent renting of vehicles for company use - 100 percent cleaning and catering - There is plan to outsource more activities such as IT, HR, accounting, and administration 	1990

Content analysis, which categorizes responses from individual respondents into categories of themes or patterns, was used to facilitate within- and cross-case comparisons (Carson *et al.*, 2001; Lukas *et al.*, 2004). The within-case analysis identified issues, some are unique to the individual case and some are common to all six companies. Focusing on the more significant issues, the cross-case analysis compared and contrasted the findings across the six cases studied. Also, a comparison with the observations in Western developed countries was made to identify similarities and differences in the key drivers and obstacles of outsourcing between developed countries and China.

Results

The findings elicited from the six case studies indicate that the common drivers of outsourcing can be broadly grouped into three categories: economic, strategic, and environmental. Successful outsourcing helps the six companies achieve various objectives resulting in cost saving or efficiency improvement which ultimately leads to a competitive advantage. The case studies also reveal that there are various obstacles and problems of outsourcing in China, such as the lack of capable service providers, which pose challenges to companies planning to outsource. To a certain extent, these challenges limit the scope of outsourcing and its pace of development in China. The key findings drawn from the six case studies are summarized as follows:

Drivers of outsourcing

- (1) Table VII lists the prominent reasons for outsourcing of the six responding companies. Among the identified drivers, some are considered more important than the others with one company (Company B) ranked the most important two. All the companies consider economic factors pivotal in the outsourcing decision process. “Cost reduction” or “cost saving” is the primary reason for outsourcing of all the six companies except Company B which ranks it as the second most important reason. This finding concurs with a wealth of literature which suggests that most outsourcing deals are driven by a desire to reduce cost (Corbett, 1996; Fan, 2000; Kakabadse and Kakabadse, 2000; Zhu *et al.*, 2001; Lynch, 2004).
- (2) For all the six companies studied, outsourcing enables them to focus on their core competence, to increase their flexibility, and to enable them to access to expertise and technology.
- (3) “Capital investment reduction” is also the most prominent reason for outsourcing of Companies C, D, E, and F which expect to reduce capital investment in transportation, warehousing, manufacturing, IT, and employees in order to release capital for core business and to improve return on assets. This supports Razzaque and Sheng’s (1998) view that outsourcing reduces the need to invest capital in facilities, equipment, IT and manpower. The findings also suggest that for private- and foreign-owned companies which were established or entered China as a result of the Chinese economic reform, reducing capital investment and cost is an important part of their survival strategies in order to enhance competitiveness and flexibility.
- (4) All six companies choose to outsource their business activities in order to focus on their core competence and increase flexibility. This agrees with the literature which suggests that organizations should outsource activities for which they do not have a critical strategic need or special capability, and focus their attention on core competence to increase customer value (Lankford and Parsa, 1999; Jennings, 2002).
- (5) “To accelerate re-engineering benefits” is one of the strategic factors that influence the decisions of Companies A and B to outsource while “to facilitate market penetration” is a strategic concern of outsourcing for Companies C, E, and F. This finding supports Rothery and Robertson’s (1995) and Corbett’s (1998) view that re-engineering gives companies the opportunity to consider outsourcing as one of the tools that they can use in the new process to improve company performance and reduce operational costs.
- (6) All six companies consider outsourcing an effort to increase flexibility in the utilization of transportation and warehousing capacity and to reduce risks in IT investment. These are consistent with the findings from surveys in the US and Europe (Rabinovich *et al.*, 1999; Claver *et al.*, 2002). Outsourcing is also used to provide seasonal workforce and to overcome constraints in production capacity. These also agree with previous research findings by Embleton and Wright (1998) and Kakabadse and Kakabadse (2000). The study also reveals that outsourcing has been used to convert a largely fixed cost business to one with variable costs in which expenses can change according to the business climate. This finding is also in agreement with that of McFarlan and Nolan (1995).
- (7) “To facilitate market penetration” is regarded as a strategic reason for outsourcing by Companies C, E, and F. Although “to facilitate market penetration” is not principally described as a strategic factor in the literature, this finding is in line with Lynch’s (2004) view on global outsourcing that it can help organizations enter new markets quickly without heavy initial investments and get geographically closer to customers to enhance responsiveness to changing customer needs.

Table VII Drivers of outsourcing considered by the six companies studied

Drivers of outsourcing	Company A (Case 1)	Company B (Case 2)	Company C (Case 3)	Company D (Case 4)	Company E (Case 5)	Company F (Case 6)
Cost reduction	√(most important)		√(most important)		√(most important)	√(most important)
Cost saving		√(2 nd most important)		√(most important)		
Capital investment reduction			√(most important)	√(most important)	√(most important)	√(most important)
To accelerate re-engineering benefits	√	√				
To focus on core competence	√	√	√	√	√	√
To increase flexibility	√	√	√	√	√	√
To facilitate market penetration			√		√	√
Capability of supplier	√	√	√	√	√	√
IT development (Access to expertise / technology)	√	√(1 st most important)	√	√	√	√

Note: Drivers marked with “√” are considered prominent reasons for outsourcing by the responding companies

Problems and obstacles of outsourcing

- (1) In general, the organizations interviewed are satisfied with the service providers' performance. However, none of them have achieved the desired benefits from outsourcing. All of them have not realized the expected cost reduction in areas of transportation, warehousing, administration, and operation. These findings are similar to the results of a survey by PA Consulting Group (1996) that few organizations have achieved high levels of benefits from outsourcing objectives (cited in Fan, 2000). All the six companies have encountered some obstacles and problems in the outsourcing process, which are summarized in Table VIII. These findings support many researchers' view that there are daunting challenges hindering the development of 3PL industry and the demand for outsourcing in China (Hertzell, 2001; Trunick, 2003; Kerr, 2005).
- (2) “Lack of capable service providers” is the major problem of outsourcing identified, which includes inability to provide effective transportation networks, poor transportation tools, old-designed warehousing facilities, lack of qualified staff, and lack of IT capability. These findings support Mercer's (cited in Kadar and Huang, 2002) conclusion that not many logistics providers in China are considered reliable, high-quality providers with the scope and scale to fully meet customers' requirements.
- (3) Another problem cited by the six companies interviewed is “loss of control” over the outsourced activity, which is also considered one of the most commonly cited inhibitors to outsourcing in the literature (Blumberg, 1998; Razzaque and Sheng, 1998; Lankford and Parsa, 1999).
- (4) “Poor transportation and IT infrastructure” and “local protection regulations” are also regarded as major obstacles to outsourcing, which are not viewed as critical problems in

Western developed countries. In addition, “local protection regulations” lead to the increase in logistics cost and damage rate, thus reduce company profit margins. They also limit the choices of companies in selecting their desired suppliers. These findings support the results of several studies (Hertzell, 2001; Trunick, 2003; Kerr, 2005) that poor infrastructure and entrenched regulatory environment are two of the daunting challenges that will hinder the development of 3PL industry in China.

- (5) The six companies studied have no comparison of pre- and post-outsourcing costs in areas like administration, operation, and office expenses. This is similar to Fan’s (2000) finding from a survey of the British companies that the majority of respondents have no clear post-outsourcing measurement.
- (6) Though widely considered as a major obstacle of outsourcing in the literature, “loss of critical skills” is not evident in this study. One possible explanation is that the six companies interviewed are still having a relatively small extent of outsourcing at this stage and the majority of the outsourced activities are “peripheral”.

Table VIII Major obstacles and problems of outsourcing encountered by the six companies studied

Major obstacles and problems	Challenges
Lack of capable service providers	- Less than expected service quality - Failure in realizing expected cost reduction or capital investment reduction - Hindrance to further outsourcing of activities
Loss of control	- Inconsistent service quality - Inefficiency in communication
Poor transportation and IT infrastructure	- Higher logistics costs - Unreliability in pickup and delivery time - Higher rate of loss and damage of goods - Poor customer service
Local protection regulations	- Higher logistics cost and damage rate - Limitation in choices of suppliers
Lack of overall post-outsourcing review	- Failure in knowing if the outsourcing process is working as planned - Failure in identifying areas of improvements or changes

Comparison between Western developed countries and China

The findings also show that there are similarities and differences between the key outsourcing drivers and obstacles in Western developed countries and China. As shown in Table IX, cost reduction, cost saving, and capital investment reduction are the main economic reasons for outsourcing both in China and in developed countries. Organizations in China and developed countries alike use outsourcing to achieve certain strategic goals such as to accelerate re-engineering benefits, to focus on core competence, and to increase flexibility. However, to facilitate market penetration is also cited as a strategic reason for outsourcing in China but not significantly stressed in the developed countries. This difference is understandable as companies in developing countries are generally young and fast-developing striving to occupy the maximum market share. The findings also reveal that environment factors, such as IT development and capability of supplier, can influence organizations’ decisions to outsource in China, which is similar to the situation in developed countries. However, the study results indicate that globalization, which is often cited as an environment factor that facilitates the greater use of outsourcing in developed countries, is currently not a major concern of organizations in China in making their outsourcing decisions. This suggests that the focus of the companies in China is still placed on capitalizing the huge potential consumer market in the mainland. The findings further reveal that organizations in China are facing certain obstacles and problems in the outsourcing process, of which lack of capable service providers,

loss of control, poor transportation and IT infrastructure, local protection regulations, and lack of overall post-outsourcing measurement are the major ones. Although the literature indicates that Western developed countries also face many obstacles and problems in outsourcing, loss of control and loss of critical skills are the ones often stressed. This difference suggests that outsourcing in China is still in its infancy stage as observed by Trunick (2003).

Table IX Comparison of drivers and obstacles of outsourcing between China and Western developed countries

Drivers of outsourcing	China	Western developed countries
Economic factors	- Cost reduction - Cost saving - Capital investment reduction	- Cost reduction - Cost saving - Capital investment reduction
Strategic factors	- To accelerate re-engineering - To focus on core competence - To increase flexibility - To facilitate market penetration	- To accelerate re-engineering - To focus on core competence - To increase flexibility
Environmental factors	- IT development - Capability of supplier	- IT development - Capability of supplier - <i>Globalization</i>
Obstacles and problems	- Loss of control - Lack of capable service providers - Poor transportation and IT infrastructure - Local protection regulations - Lack of overall post-outsourcing review	- Loss of control - <i>Loss of critical skills</i>

Note: Bolded items are those identified in China but not in Western developed countries. Italicized items are those found in Western developed countries but not in this study.

Conclusion

This paper has explored the key drivers of outsourcing and the main obstacles or problems faced by organizations in China. The findings indicate that economic, strategic, and environmental factors are the main drivers that motivate organizations in China to engage in outsourcing. They are similar to those identified in the Western developed countries. For economic factors, cost reduction, cost saving, and capital investment reduction are the main concerns. This is in agreement with the literature reporting the situation in developed countries (Razzaque and Sheng, 1998; Kakabadse and Kakabadse, 2000; Claver *et al.*, 2002; Lynch, 2004).

The findings also show that organizations in China have taken some strategic considerations when making outsourcing decisions. They include the use of outsourcing to accelerate re-engineering benefits, to focus on core competence, and to increase flexibility. This is also in agreement with the findings in the literature reporting the situation in developed countries (Quinn and Hilmer, 1994; Corbett, 1998; Mazziwi, 2002). Meanwhile, to facilitate market penetration is also cited as a strategic reason for outsourcing in China but not in developed countries.

The findings further demonstrate that environmental factors such as IT development and capability of supplier can influence organizations' decisions to outsource in China, which is in agreement with the literature (Razzaque and Sheng, 1998; Lynch, 2004; Kakabadse and Kakabadse, 2005). However, the results indicate that globalization, which is often cited as an environmental factor that facilitates the greater use of outsourcing in developed countries, is not a major concern of organizations in China when making their outsourcing decisions. On

the other hand, capability of service supplier in terms of service quality, availability of extensive domestic transportation network, financial strength, reputation, reliability, use of latest technology, price, and relationship with client, etc., are regarded as the most important considerations when it comes to the selection of a service provider.

The study also reveals that organizations in China have encountered some obstacles and problems in the outsourcing process, of which lack of capable service providers, loss of control, poor transportation and IT infrastructure, local protection regulations, and lack of overall post-outsourcing measurement are the major ones. Although the literature indicates that Western developed countries also face many obstacles and problems in outsourcing (Blumberg, 1998; Razzaque and Sheng, 1998; Lankford and Parsa, 1999; McIvor and Humphreys, 2000; Al-Qirim, 2003), loss of control and loss of critical skills are often cited as the major ones.

Based on the findings of this study, a framework for making outsourcing decisions in China is proposed in Figure 1. The framework suggests that organizations in China should consider both economic and strategic implications when making outsourcing decisions. From an economic perspective, companies may need to undertake a total cost analysis to identify and measure all the costs associated with the outsourcing of an activity so as to ensure cost-effectiveness. In addition, outsourcing decisions should also be made from a strategic perspective and be fully integrated into the business planning process to achieve long-term success. A detailed evaluation of IT development and a careful analysis of the supplier's capability may also be required. In order to minimize the risk of failure, companies should also be aware of other potential problems such as impact on customer service level when deciding to outsource.

With heavy investment in logistics infrastructure and accelerated economic reform, business environment in China has become more and more dynamic. The entry of global logistics providers in the Chinese market will certainly encourage the use of 3PLs. Outsourcing will become one of the most effective business strategies for organizations in China to achieve cost-effective performance and long-term success. To fully investigate the impacts of outsourcing in this fast-changing economic climate, more studies are required to explore the best practices of outsourcing in China. To help determine the validity of the proposed framework proposed in this study, further research with a larger sample across a wider spectrum of industries and companies of different operating scales is, therefore, recommended.

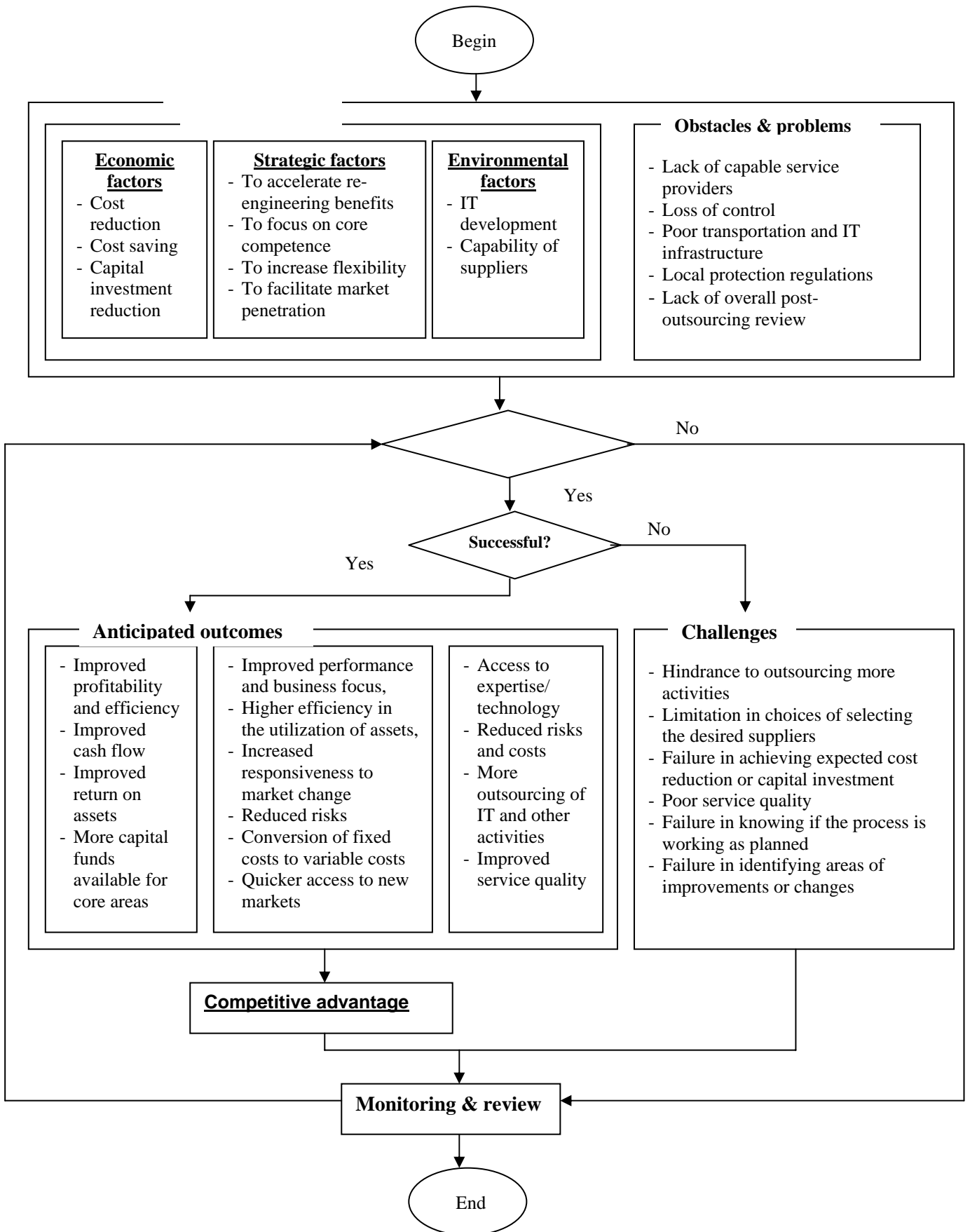


Figure 1 A proposed framework for making outsourcing decisions in China

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increases from \$3 to \$4? Why?