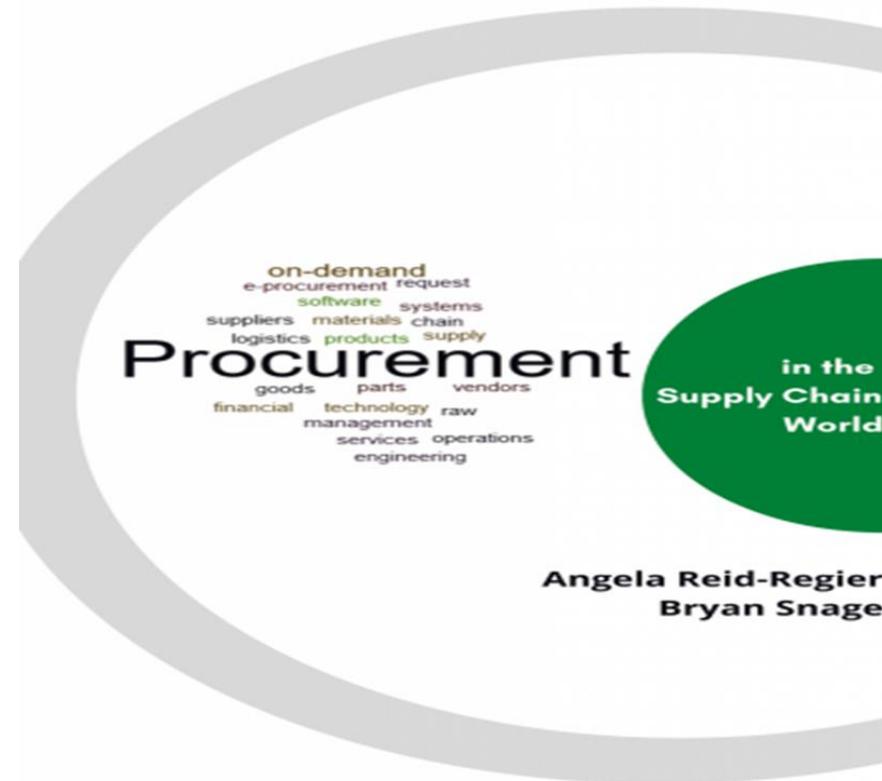


Procurement in a Supply Chain World

Chapter 6: Insourcing, Outsourcing, Making or Buying



Accessibility Statement

- This PowerPoint is compatible with assistive technology
- Images have alternative-tags applied
- Complex images have long descriptions and are available in the notes section of each slide
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Learning Objectives

Learning Objectives:

- Explain why companies outsource.
- Describe the reasons why the use of outsourcing and offshoring has grown.
- Explain some drawbacks companies face when they outsource their activities.
- Understand that choosing whether to make or to buy a product or choosing to have services performed by an outside company, are outsourcing decisions.
- Compare costs to keep the product or service in-house to the cost of buying the product or service from an outside party.

Introduction

Firms review their supply chains for efficiencies and look for suppliers to outsource functions that can:

- Add value to a function that the firm can not
- **Reduce overall costs**

Firms commonly outsource transportation:

- Freight Forwarders
 - Travel agents for freight
- Third-party logistics (3PLs) Firms
 - Outsource entire order processing and shipping departments

The Growth of Outsourcing and Offshoring

Beginning in the 1990s, companies began to outsource activities beside transportation with the goals to

- Lower costs
- Focus on activities the company does best

Many “producers” of products no longer produce them at all but outsource their production instead

- Outsourcing work to companies abroad is called offshoring

(McGrath, 2017)
Principles of Marketing (2015)

Some Ins and Outs of Outsourcing

Trade-offs:

- Loss of control
 - Product testing
 - Patented technologies
- Increased time to receive products
 - Overseas shipping times
 - Source alternative suppliers
 - Cost to move back to in-house production (insourcing)

Evaluate and Determine Whether To Make or Buy a Component

- Most common outsourcing scenario is buying a component rather than making it.
- Make or buy analysis is also applicable to the service industry.
- Sometimes more cost-effective to outsource service activities rather than hire staff.
- Expertise and costs and benefits need to be considered.

~~Companies outsource for the same reasons. Many companies have found that it is more cost-effective to outsource certain activities, such as payroll, data storage, and web design and hosting. It is more efficient to pay an outside expert than to hire the appropriate staff to keep a particular task inside the company.~~

Fundamentals to Make or Buy

The make versus buy decision involves both quantitative and qualitative analysis.

Quantitative **component** requires a cost analysis:

- Look at the cost to buy the component versus the cost to produce the component
- Analyze unavoidable costs.
- When buying, the avoidable costs will go away but unavoidable costs will remain.

Advantages and Disadvantages of Outsourcing

Advantages of Outsourcing

- Utilizes external expertise, removes the need for in-house expertise
- Frees up capacity for other uses
- Frees up capital for other uses
- Allows management to focus on competitive strengths
- Transfers some production and technological risks to the supplier

Disadvantages of Outsourcing

- Takes away control over quality and timing of production
- May limit ability to upsize or downsize production
- May have hidden costs and/or a lack of stability of price
- May diminish innovation
- Often makes it difficult to bring the production back in-house once it has been removed

Key Takeaways

- Companies outsource to add value to their products or reduce costs
- Deciding to outsource is a choice between alternatives
- Outsourcing reduces costs while allowing companies to focus on what they do best
- Offshoring by outsourcing to companies offshore has grown in supply chain functions.
- Outsourcing decision include whether to make or buy a product or choosing to have services performed by an outside company

References

McGrath, S. (2007, December 14). China Shipping Advice. *Smart Sourcing*. <http://www.smartchinasourcing.com/shipping/china-shipping-advice-cif-shipping-terms-explained.html>

Principles of marketing. (2015, October 15). Universities of Minnesota Libraries. <https://open.lib.umn.edu/principlesmarketing/>