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Winning, Running, and Renewing the Outsourcing Contracts

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Abstract
The paper explores how vendors deploy competences and capabilities across the outsourcing process in order to win, run, and renew outsourcing contracts. The results of a multiple-case study of three contract electronics manufacturers (CEMs) show that different combinations of capabilities are required for a vendor to win, run, and renew outsourcing contracts. Permanent capabilities are constantly present across the process, while temporary capabilities, depending on customer requirements, can be added or removed from the portfolio of capabilities.
Key words: outsourcing, capabilities and competences, vendor's perspective

Introduction
The term *outsourcing* was first adopted in the 1960s and 1970s, predominantly with regard to manufacturing (Corbett, 2005), when Original Equipment Manufacturers (OEMs) rethought their manufacturing strategies. As components became commodities, they started to outsource their production to contract manufacturers (Greaver, 1999; Hadaya et al., 2000). Today, companies outsource everything that can be performed by others—from cleaning and catering services to business processes and IT management—and further to sensitive activities such as research and development (Engardio et al., 2006). Success in outsourcing has become an imperative and one of the most important factors for its achievement is a vendor's capabilities (Hunt and Jones, 1998; Levina and Ross, 2003; Feeney at al., 2005).

Publications in outsourcing tend to favor the outsourcer's perspective and even though the vendor's capabilities are important for the success of outsourcing, they are understudied, especially from the vendor's point-of-view. In this paper, we explore how vendors develop and deploy capabilities in order to achieve their objectives in outsourcing.

To understand the essence of capability, we drew upon the resource-based view (RBV) as a theoretical inspiration. By relying on the hierarchy among an organization's resources, we constructed the competences-capabilities-objectives triad, which served as a framework for data collection and analysis. We distinguish between competences and capabilities by taking the Hatten and Rosenthal's (1999) definitions of the two. Competences are perceived as a potential for conducting a business, while capabilities are measures of the actual performance as perceived by customers. By drawing on studies of the vendor's process in outsourcing, we contend that the vendor's objectives are to win, run, and renew outsourcing contracts. Having examined the current status of the vendor's perspective in outsourcing and the premises of the RBV, we have explored *how vendors deploy their competences and capabilities across the outsourcing process in order to win, run, and renew their outsourcing contracts*.

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This study has focused on the Electronic Manufacturing Service (EMS) provision industry, which is shaped and dominated by contract manufacturers. An exploratory multiple-case study of three contract electronic manufacturers (CEMs) has been used to capture their competences and capabilities, and analyze their influence on winning, running and renewing outsourcing contracts

Background and research framework

Levina and Ross (2003) showed that a vendors' capabilities are the most important factors for success in the outsourcing process. In their study of vendors in information technology (IT) outsourcing, *relationship management*, *technical competence* and *understanding the customer's business* were identified as capabilities contributing to that success. Another study of vendors in IT outsourcing (Feeny et al., 2005) proposed that vendors should be selected based on their *delivery, relationship management* and *transformation* capabilities. With respect to outsourcing of manufacturing, it is reasonable to believe that vendors are selected based upon traditional manufacturing capabilities such as *cost, quality, delivery*, and *flexibility* (Boyer and Lewis, 2002). Indeed, in the case of the EMS industry, Hunt and Jones (1998) identified *quality, cost and delivery* as core CEM capabilities for winning the contract.

Capability as a concept has been developed under the premises of RBV (Rumelt, 1984; Wernerfelt, 1984; Barney, 1991) and advanced within the concept of dynamic capabilities (Teece et al., 1997). RBV argues that the source of an organization's competitive advantage is based in the company's resources: their assets, competences, and capabilities. Accordingly, there is a hierarchy among the organization's resources. Assets are precondition for an organization to have competences, while organizational and managerial processes utilize competences to create capabilities, which are further deployed to achieve an organization's objectives. There is often confusion in distinguishing between competences and capabilities. In this study we use the definitions from Hatten and Rosenthal (1999): *Competences* are measures of an organization's potential to conduct business at the state-of-the-art level in both the firm's input market (labor, capital, information and technology) and the output markets with its customers. *Capabilities* are measures of the performance of business processes along dimensions defined by customers' needs and expectations, like for example, time, cost, and quality."

RBV puts the business process in focus because of its role in mobilizing an organization's competences and capabilities (Teece et al., 1997; Hatten and Rosenthal 1999). One of the first efforts to map a vendor's generic process in outsourcing was made in Jenster et al. (2005). They defined the process to consist of three phases: identifying a need for additional competences; managing the entry phase (this challenge stems from activities around the assessment of the business opportunity such as assessing the potential outsourcer and the preparation of the bid); and running the contract. Similarly, in a study of software developers, Perunovic and Christoffersen (2007) suggest that the vendor's process in outsourcing should be considered to be cyclical, as vendors strive to win new customers, to satisfy their expectations by running the process satisfactorily, and to therefore keep existing customers in the loop with new projects or extended outsourcing contracts. Vendors may have various strategic goals, but in the context of the win-run-renew process, it can be argued that the vendor's objectives are to *win, run,* and *renew* their outsourcing contracts.

The RBV hierarchy suggests that the impact of capabilities on an organization's objectives is influenced by competences, but there is still little evidence to illustrate whether and how vendors act along the elements of the hierarchy. Therefore, we were

interested to ask *how do vendors deploy their competences and capabilities across the outsourcing process in order to win, run, and renew their outsourcing contracts?* The research question has been explored by focusing on the competences-capabilities-objectives triad as shown on Figure 1.
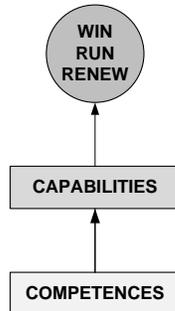

Figure 1 – The competences-capabilities-objectives triad

Method

In order to pursue answers to this question, we have utilized a case study to design an appropriate research strategy. It is suitable for uncovering areas for research and theory development and identifying key variables and linkages between them (Voss et al., 2002). Procedures for its conduct are well established in the literature (Eisenhardt 1989; Miles and Huberman, 1994; Voss et al., 2002; Yin, 2003), and we have followed them both in designing the research and in collecting and analyzing the data.

The EMS industry is globalized and the CEM process consists of more or less standardized steps (Hunt and Jones, 1998). However, contextual factors that stem from operations management (Sousa and Voss, 2007) and different cultural roots and national characteristics (Franke et al., 1991) can play a significant role in the varied operational performance of CEMs. In order to increase external validity i.e. to establish the domain in which a study's findings can be generalized (Yin, 2003) and to mitigate potentially biased interpretation from a single case study (Voss et al., 2002), a multiple-case study of three CEMs has been used.

The data collection lasted from 2006 to 2008. In multiple site visits, more than 40 people were interviewed. The interviews were all recorded and then transcribed. Additional data has been gathered by examining internal company material, reports from the EMS industry, customer satisfaction surveys and via questionnaires to the customers. In order to capture capabilities and their influence on the objectives, we asked both vendors and their customers to identify capabilities that make vendors win, successfully run and renew their outsourcing contracts. A modified version of a questionnaire from Andriessen and Tissen (2000) was used as an interview guide for capturing competences. We looked for competences in organizational units, as suggested by Hatten and Rosenthal (1999), and at the corporate level.

We have performed three consecutive single-case studies, and finalized the study with a cross-case analysis. Coding techniques, displays, and tactics suggested by Miles and Huberman (1994) have been utilized as primary tools for the data analysis. The initial drafts have been sent to the key informants to verify the accuracy of the interpretations of the summarized data.

Cases

The data was collected according to the competences-capabilities-objectives triad, charting capabilities and their impact on objectives and competences and their impact

on capabilities. The data is presented for each case and company in tables 1, 2, and 3. Capabilities are delineated in columns. The dots above indicate whether capabilities have impact on the win, run, or renew objectives. Competences, grouped within organizational units, are given in rows. The squares indicate the impact of competences on capabilities.

Prometheus
PROMETHEUS is a tier-two CEM (revenue larger than 100 million USD) headquartered in Asia run by a diverse team of international executives, and operating in four countries. Profits have grown steadily, providing the resources for organic growth as well as making acquisitions possible. Today, PROMETHEUS is a vertically integrated CEM which can design, develop and manufacture electronics, plastics, tools for plastic moulding, and provide complete product solutions (box-build).

The sales group consists of business developers and key account executives. Business developers are in charge of finding new customers and managing the quotation process. They use their competences to obtain new customers by focusing on PROMETHEUS' price, quality, the benefit of vertical integration, and their various locations. Key accounts are those which fuel growth, as PROMETHEUS grows with the growth of their existing customers. Each customer has specific requirements and PROMETHEUS' key account executives are the principal bridge in satisfying those requirements. The sales competences are deployed in way that influences capabilities like cost management (through quotation activities), delivery, initiative, quality, relationship management, responsiveness, and vertical integration. A design and development manager states: "Some customers arrive with a preliminary prototype or even just a concept of a product, and we can offer them design for manufacturing. We can do electronic and mechanical design, as well as PCB layout according to their functional specification". PROMETHEUS' competences in their design and development (D&D) have enabled their design and development capability, as well as strongly influenced their relationship management and vertical integration.

The operationalization processes are conducted by people organized into NPI and engineering (technical operationalization), and procurement and supply chain (commercial operationalization) functions. Technically competent, business process oriented and initiative-driven employees influence D&D, on-time delivery, flexibility, high-mix manufacturing, responsiveness, and technical competence capabilities. Procurement and supply chain management, which are part of the operationalization unit's competences, enable capabilities such as cost management, delivery, and relationship management (with suppliers).

Over the years, PROMETHEUS has been building competences in the manufacturing of electronics and mechatronics. They are able to apply various technologies in order to manufacture simply a PCB or the entire product. Manufacturing of both electronics and mechatronics require strict quality levels. Failing to achieve this capability would discourage customers from renewing their outsourcing contracts with PROMETHEUS. Competences in manufacturing are also characterised by competent technical mastering of various technologies that PROMETHEUS possesses, and flexibility in handling the high mix to low volume production. Adding the manufacturing of plastic parts to PROMETHEUS' portfolio of services has significantly influenced their vertical integration capability.

The quality and testing departments are organizationally positioned in the support function. They are competent in designing and fabricating testing hardware and software, and in the application of various technologies for PCB testing. Competences

within the quality department, which is responsible for the testing phase of the process, have a strong influence on their vertical integration capability. Competences in testing, and in securing the general quality of PROMETHEUS's products influence the quality capability which is recognized as one of the capabilities enabling the inflow of new projects from existing customers.

Many of the competences residing at the corporate level have a strong impact on capabilities. Alternative locations for manufacturing enable PROMETHEUS to perform cost management and to engage some sites for high-mix manufacturing. This vertical integration competence is recognized as a capability. The modular process enables initiative and vertical integration, while the box build is also an enabler of the vertical integration. The ability to introduce new technologies is reflected in PROMETHEUS' capabilities of flexibility, initiative, responsiveness, and technical competence. Multilayered relationship management enables the capabilities of relationship management and responsiveness, while PROMETHEUS' preferred list of vendors has good cost management as a consequence.

Table 1 – Prometheus' Competences – Capabilities – Objectives Triad

OBJECTIVES	Cost management	Design and development	Delivery	Flexibility	Initiative	Quality	Relationship management	Responsiveness	Technical competence	Vertical integration
Win	•	•					•			•
Run			•	•	•	•	•	•	•	
Renew	•	•				•	•	•	•	•
COMPETENCES / **CAPABILITIES**	Cost management	Design and development	Delivery	Flexibility	Initiative	Quality	Relationship management	Responsiveness	Technical competence	Vertical integration
Sales	■		■		■	■	■	■		■
Design and development		■					■			■
Technical operationalization		■	■	■	■	■		■	■	
Commercial operationalization	■		■				■			
Electronics manufacturing				■		■			■	
Mechatronics manufacturing				■		■			■	■
Support					■					■
Corporate	■				■	■		■	■	■

Asterion
ASTERION is a tier-three CEM company established in 2004 after the merger of an electronics manufacturing and an electronics development company. This has provided a basis for vertical integration. ASTERION has a strong design and development unit which specializes in the development of electronic applications for the agriculture and ventilation industries.

ASTERION's sales department is strong in managing relationships with existing customers. In addition to good personal relationships and networks, their key account executives use their analytical skills to follow their customer's latest developments. Thus, the relationship management capability is influenced by sales competences.

The D&D unit is perceived companywide as the treasure of ASTERION's competences. Development consists of experienced engineers with extensive electronics knowledge, specifically in relation to specific industries such as agriculture and agriculture-related moving equipment. In addition to their technical competences, D&D collaborates with both the sales and purchasing units. They participate regularly in sales activities, and in the purchasing of components. Developers are also responsible for

NPI, i.e. the development of prototypes, which requires a certain level of knowledge of manufacturing processes. D&D's early involvement, even in the sales process, and their care for customers, also influences relationship management.

The supply chain function organizationally consists of the purchasing sub-unit and manufacturing. The purchasing sub-unit is a small unit with traditional professional competences. However, one of their distinguishing characteristics is that they are "fire fighters" who (due to uncertainties both at the customer's end and at ASTERION) must obtain components quickly. The purchasing unit contributes to the flexibility, speed, and sourcing through their ability to pool components when necessary. A production manager explains the key strengths of the production unit: "We are capable of organizing production of small and medium scale quantities, and we are capable of running through this process extremely fast, from placing the order to receiving the first product. We have the competence to understand the customer's needs".

Speed and flexibility come partly from good collaboration with customers where sales and development are also involved. Production is also responsible for quality management. "Each time we improve quality, we reduce the price of the product because we don't need to put more hours in finding the mistake", argues production manager.

Table 2 – Asterion's Competences – Capabilities – Objectives Triad

OBJECTIVES	Delivery	Flexibility	Low volume manufacturing	Relationship management	Speed	Technical competence	Vertical integration
Win	●	●	●	●	●	●	●
Run	●	●		●		●	
Renew		●		●	●	●	
CAPABILITIES / COMPETENCES	Delivery	Flexibility	Low volume manufacturing	Relationship management	Speed	Technical competence	Vertical integration
Sales				■			
Design and development		■		■	■	■	■
Purchasing		■			■		
Manufacturing	■	■	■	■	■	■	
Support							
Corporate		■			■	■	■

Since ASTERION grew from a merger of two different business cultures, one more manufacturing oriented and the other more development, their natural competence still being exploited is having development and manufacturing under one roof. Another corporate competence is ASTERION's quality management system. The manufacturing process is composed of several phases, where quality control is conducted after each stage and thus minimizes errors in the final product inspection stage. A D&D manager illustrates it this way: "Test as early as you can and make sure that your test is testing the process. Thereafter, you don't need to test functionality, because functionality is guaranteed by design. We are moving from testing the equipment towards testing the process".

The way in which NPI and manufacturing are systematized and organized is also one of ASTERION's competences. The same production manager argues that "we are not unique in manufacturing but the way we have organized NPI and manufacturing is good, which makes us fast and flexible".

Califia

CALIFIA is a tier-three CEM headquartered in North America and operates from three facilities in two countries. They were formed early in the 1980s as an OEM company specializing in the design, manufacturing, and sales of intelligent graphics terminals for IBM mainframe computers. Since the OEM business was becoming obsolete, CALIFIA moved to CEM business in 1996. CALIFIA is a manufacturing-only CEM with the capacity for high mix/low to medium volume. One of its specialties is a group that does specialty business prototypes: small volumes very fast.

Prototypes and NPI are very strong capabilities of CALIFIA. Competences at program management, manufacturing and materials are the key to a successful NPI, which makes CALIFIA deliver on time with good quality and deepen relational elements (trust and commitment) with the customer.

Criticality to on-time delivery is equally shared by materials and manufacturing. If components were not in place on time, and if the workforce were not able to manufacture and inspect on time, it wouldn't be possible to achieve this capability. The Prototype group also has a very high contribution to the on-time delivery. Their competence to work on short-term notice without any rules is impressive and often leads towards winning contracts with larger volumes.

Quality, one of the most important capabilities delivered by CALIFIA, is predominantly influenced by competences within the manufacturing department, and to a large extent by materials through their acting in securing the right components with trusted and in-house based suppliers. Coordinating and project management skills of program management also contribute to the quality levels. It is certain the corporate policy towards certifications in general led CALIFA towards achieving high quality standards.

Table 3 – Califia's Competences – Capabilities – Objectives Triad

OBJECTIVES	Fast prototyping and NPI	On-time delivery	Quality	Relationship management	Responsiveness
Win	●	●	●	●	●
Run		●	●		●
Renew		●	●	●	●
CAPABILITIES / COMPETENCES					
Sales	■	■		■	■
Program Management	■	■	■	■	■
Materials	■	■		■	■
Manufacturing	■	■	■	■	■
Finances and Administration				■	■
Corporate	■	■	■	■	■

The relationship management has gained significant momentum. It is led by the sales with new customers, program management with the existing customers, and materials with suppliers.

Responsiveness seems to be a common characteristic distributed across the company. Everyone works towards being flexible and responsive. The manager of purchasing commented: "What I saw when I arrived here were many people that were in the OEM business trying to run a CEM business. These businesses are very different. You work at

a different pace in CEM than in OEM. It is a much faster pace in CEM and you got to react a lot faster. The pace in CALIFIA was slower and lot more methodical but we have had improvements in delivery and quality so things seem to work."

Discussion

Exploratory multiple-case research of three CEMs revealed several interesting findings which can be useful for both academic and industry communities.

We found that different portfolios of capabilities are characteristic for each of the companies. Some capabilities are present in two or three companies, but have different roles in achieving the organization's objectives. For instance, *delivery* impacts the run objective in PROMETHEUS, *win and run* in ASTERION, and *win, run, and renew* in CALIFIA. Further, different combinations of capabilities within a company are required for winning, running, and renewing outsourcing contracts. For example, we identified 10 capabilities in PROMETHEUS, but only 4 were needed to win the contracts, 7 to run it, and 7 to renew it. Each portfolio consists of two types of capabilities: *permanent capabilities*, which impacts all three objectives; and *temporary capabilities*, which, depending on the requirements from the customers, can be added or removed from the portfolio of capabilities. Traditional manufacturing capabilities (cost, quality, delivery, and flexibility) are not present in all companies. Instead, relationship management has emerged as an important capability in the EMS industry.

The cases also showed that the impact of competences on capabilities can take different paths. Most of PROMETHEUS's capabilities are influenced by their sales, technical operationalization (NPI), and corporate competences. The concentration of competences that influence capabilities in the stages of the process also differs from stage to stage. Because of the nature of PROMETHEUS's competences to change and fluctuate readily, this impact is perceived as *versatile*.

Two organizational units in ASTERION are generators of the majority of competences that influence key capabilities. Design and development is a kernel of technical competence while manufacturing is a source of flexibility. They are both engaged in the sales process and have strong customer focus, therefore strongly influencing their relationship management capability. Managerial and organizational processes on the corporate level strive to merge the two sources of competences into an efficient process. Therefore the corporate competences also significantly influence one of the key capabilities – flexibility. These two competences, together with the corporate competences, influence the winning, running, and renewing capabilities, while a less dominant group of competences (sales and purchasing) interchange during the process. Since competences in design, development and manufacturing are powerful and prevailing over all others, we perceive their impacts as *unit dominant*.

In the case of CALIFIA there is an even distribution of the impact of competences on capabilities. All unit-based competences with support from corporate competences have an almost equal impact on all capabilities and on permanent capabilities. In addition, all competences evenly impact the capabilities grouped around winning, running, and renewing the contracts. For these reasons this impact of competences is perceived as *balanced*.

Implications for research

In contrast to the practice of studying capabilities as industry-specific, findings from this research suggests that capabilities are idiosyncratic for each company and that they should be considered organization-specific. Further, the results advocate more research of relationship management capability in the context of outsourcing manufacturing.

Clearly, there is a need to consider both perspectives for a mutually beneficial, long term relationship to arise. In reality both the vendor and the outsourcer influence and are influenced by each other's competences and capabilities. In a global business environment where technology change is rapid and the competitive environment can quickly change, an ability for the supply chain to react appropriately and rapidly is a competitive advantage (Hammer, 2001). This, however, requires a level of communication and trust that is not common in most contract manufacturing relationships. Movement to a longer time frame partnership relationship will foster the necessary commitment to make this practical (Liker and Choi, 2004). Vendors need to develop their competences into capabilities that matter to the outsourcer to win, run and renew their contracts. The outsourcers, in turn, can assist the vendors in developing the requisite capabilities and competences by coordination at all stages of the supply chain. In the end the partnership puts the focus in the win-run-renew triad on the run portion as the relationship becomes long term, and there is less concern by both parties on changing partners. This promises to be fertile area for further research. With respect to competences, the most influential competences are embedded within several functions, on the corporate level or in the CEM process. Therefore, when looking for competences, one has to go beyond functions, as proposed by Hatten and Rosenthal (1999), and also look into processes and on the corporate level.

Implication for practice
Vendors should be aware that there is no need to copy competitor's capabilities. Instead, they should concentrate only on those capabilities that satisfy their own objectives, and on competences that trigger those capabilities. Instead of constantly exploiting the whole portfolio of the capabilities, with the advance of the phases in the staged-process in outsourcing only those competences that impact winning, running, or renewing capabilities should be activated. In this way vendors can optimize the resources that are necessary to achieve the objectives. Many man-hours could be freed which could lead towards decreasing the costs, increasing the speed, and improvements in flexibility and technical competence. One might argue that an organization should cut unnecessary competences loose, but they are still necessary for running the business. Further, in a dynamic technology and competitive environment competences that are currently not critical may become so in the future and it would be a mistake to let them deteriorate. Finally, relationship management should be perceived as one of the most important capabilities that need to be permanently present across the outsourcing process.

Conclusions
The paper explores how vendors deploy competences and capabilities across the outsourcing process in order to win, run, and renew the outsourcing contracts. By utilizing the premises of RBV we developed the competences-capabilities-objectives triad which served as framework for the data collection and analysis in a multiple-case study of three CEMs. The results show that different combinations of capabilities is required for the vendor to win, run, and renew the outsourcing contracts. Permanent capabilities are constantly present across the process, while temporary capabilities, depending on the requirements from the customers, can be added or removed from the portfolio of capabilities. Vendors can benefit from this by activating only those competences that impact capability, which has an active role in either winning, running, or renewing outsourcing contracts. Still, if the technology, competition, or needs of the customers change, a vendor may be left short by not having a broad base of

competences. Outsourcers can also benefit from understanding how to assist vendors in developing the requisite capabilities and competences for success.

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