LAPPEENRANTA UNIVERSITY OF TECHNOLOGY
School of Business
Supply Management

Master's Thesis

OUTSOURCING CHALLENGES IN RUSSIA

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Examiners: Professor Veli-Matti Virolainen
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ABSTRACT

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The study focuses on the key factors in outsourcing from the viewpoint of manufacturing companies operating in Russia. The goal has been to give an overview of the different kinds of challenges companies might face in the case of outsourcing. Of particular interest are the possible risks which might originate from the subcontract relationship, as well as managing these risks.

The empirical material for this qualitative interview study was collected from three large-scale manufacturing companies operating in food industry in Russia. Two of the interviewed companies were local Russian actors, and one was an international firm.

According to the respondents, a big challenge is to find a suitable supplier in the Russian markets. If there are suppliers available, they may often not be capable of operating as outsourcing partners. The most common problems faced with suppliers are unstable quality and arbitrary pricing.

Whether the suppliers are capable to offer activities which satisfy the company's own and the end customers' requirements, seems to be the biggest concern in the interviewed companies. This quality risk is managed by the strategy of multiple sourcing. Single sourcing is seen as an impossible option. The interviewed companies have no organised risk management with their external suppliers.

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Tässä pro gradu –työssä tutkitaan ulkoistamisen avaintekijöitä Venäjällä toimivien tuotantoyritysten näkökulmasta. Tavoitteena on ollut muodostaa käsitys erilaisista haasteista, joita yritykset voivat kohdata Venäjällä ulkoistaessaan toimintoja. Erityisesti tarkastellaan mahdollisia alihankkija-suhteesta aiheutuvia riskejä sekä näiden riskien hallintaa.

Empiirinen aineisto tähän laadulliseen haastattelututkimukseen on kerätty kolmelta Venäjällä toimivalta elintarvikealan suuryritykseltä. Kaksi haastatelluista yrityksistä on venäläisiä ja yksi kansainvälinen yritys.

Vastaajien mukaan sopivan alihankkijan löytäminen Venäjän markkinoilta on suuri haaste. Mikäli ulkoinen toimittaja löytyisikin, useimmiten tämä ei ole kykenevä toimimaan alihankkijana. Laadun vaihtelu sekä mielivaltainen hinnoittelu ovat yleisimmät alihankkijoiden kanssa koetut ongelmat.

Haastatelluissa yrityksissä suurin huolenaihe on alihankkijoiden kyky toimia ulkoistavaa yritystä sekä loppuasiakkaita tyydyttävällä laatutasolla. Tätä laaturiskiä hallitaan usean alihankkijan strategialla. Vain yhden alihankkijan käyttäminen koetaan mahdottomaksi. Haastatelluilla yrityksillä ei ole suunnitelmallista riskienhallintaa alihankkijoidensa kanssa.

FOREWORD

Years ago, when I started my studies at Lappeenranta University of Technology, it was self-evident to start studying the Russian language. Several trips to Russia, and latest the period as an exchange student in St. Petersburg have raised the interest in Russia. I felt especially lucky when I got an opportunity in the Norhern Dimension Research Centre, NORDI, to combine Russia with my major in the Master's thesis.

There have been several people involved in this thesis. I wish to thank all my interviewees for their time and ideas for the research. Thanks are due to the supervisor of my thesis, Professor Veli-Matti Virolainen, whose contribution helped me during the research process. All my colleagues in NORDI, especially coordinator Maija Märkälä for her valuable comments, deserve my sincere thanks. I would also like to thank Konstantin Krotov from St. Petersburg State University Graduate School of Management for helping me to conduct the interviews in St. Petersburg.

I am very grateful to all my nearest and dearest for their support. My parents, Maija and Heikki, deserve a special mention here. They have all the time believed in me and never questioned my choices, even though Iraq, Kuwait, Kosovo, Pakistan and India have for their part postponed the day of graduation...

Lappeenranta, September 2008

Iivari Ahola

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1 INTRODUCTION

An important aspect in making strategic decisions is the question of what companies make in-house and what they procure from outside. Vertical thinking (i.e. owning or controlling every link in the supply chain) has given way to virtual thinking (i.e. creating a flexible web of supply relationships and focusing exclusively on what one does best), and companies are increasingly implementing new networked business models.

According to common understanding, economic players in Russia are still trying to ensure sustainable development and achieve competitive advantages using diversification and vertical integration. This approach differs notably from the current economic trends, which emphasize outsourcing and concentration on core competencies. In order to decrease their dependence on the changing conditions of their business partners, many companies in Russia try to embrace the whole vertical dimension of their business. Already now, this kind of policy has made a negative impact on financial results, and the rapidly growing competition and the need to invest in production have forced many manufacturers also in Russia to specialize.

1.1 Background of the study

Lappeenranta University of Technology has tight cooperation relations with Russian partners. In several academic occasions, Russian business managers have brought out their concern about outsourcing. However, outsourcing and networking as ways of action are still seen difficult to execute in Russia.

This thesis is a preliminary study for a larger international research project. The objective of the project is to increase understanding on the problems, risks, limitations and success factors of joint development work in international supply networks, and to develop methods and tools for joint development work and risk management in supply networks. The project is planned to be conducted in co-operation with St. Petersburg State University Graduate School of Management (Russia), European Business School (Germany), and Lappeenranta University of Technology (Finland).

Supply networks have been studied actively in recent years. For example the International Supply Chain Risk Management (ISCRIM) Network has been an active actor in doing research on supply networks. ISCRIM is a network of researchers interested in how to handle different types of risks in the supply chain. However, ISCRIM has not focused on supply networks operating in Russia.

This study deals with the key factors in outsourcing from the viewpoint of an original equipment manufacturer (OEM). The OEM is an actor which uses components of other companies in its products, and sells these products to resellers or end users under its own brand name. The focus of the study is on the different kinds of challenges the OEM might face in the case of outsourcing. A particular interest is directed to the possible risks which might arise when doing the outsourcing decision and also during the subcontract relationship in a network environment. The risk management process is also studied. The empirical part concerns the Russian business environment, and the outsourcing challenges are discussed from the viewpoint of the OEM operating in the Russian food industry.

1.2 The research problem and objectives of the study

The research problem of this study is the following:

What kinds of challenges do original equipment manufacturers (OEM) operating in Russia meet in the case of outsourcing?

There are three sub-problems as follows:

1. **How is the make or buy decision organized in Russia? Why to outsource or not?**
2. **What are the main risks originating from outsourcing the OEMs operating in Russia are aware of?**
3. **How is risk management realized in the network environment in Russia?**

The objective of the research is to clarify the decision making when a company operating in Russia is making significant decisions concerning its structure and position in a supply network.

1.3 Methodology

Due to the introductory nature of this thesis as a part of larger research project, the qualitative perspective has been chosen. When doing further research during the planned larger research project, also quantitative research will be done. According to Hirsjärvi et al. (2002: 155), the qualitative research is by nature comprehensive acquisition of information, and the research material is collected in real circumstances. People are favored as the instrument for data collection, and the researcher's aim is to reveal unexpected facts. The subject of the research is chosen expediently, not as a random sample.

The interviews conducted for this research were mainly semi-structured, but also a structured part was included. According to Eskola and Suoranta (2003: 86), both in semi-structured and structured interviews the forms and orders of questions are the same for all the interviewees. The idea is that the questions have the same meaning for every respondent. In semi-structured interviews the respondents answer the questions in their own words, and in structured interviews alternatives for answering are given.

The empirical material for this qualitative interview study was collected in April 2008 from interviews conducted in three manufacturing companies operating in food industry in Russia. Two of the companies were local companies in Russia, and one was an international actor. All the companies are so called large-scale enterprises; two of them operate in the bakery business and one in the confectionery business. The interviewed companies were chosen in cooperation with St. Petersburg State University Graduate School of Management and the School of Business and the Northern Dimension Research Centre (NORDI) of Lappeenranta University of Technology. The representatives of the Russian companies were interviewed in St. Petersburg in Russia, and the representative of the international company was interviewed in Helsinki, Finland.

A part of the questionnaire was sent by e-mail to the targeted companies as preliminary data about three weeks before the semi-structured interviews (see Appendix 1). The aim was to give the respondents time for getting prepared. The questions were the same for all the interviewees, and it was possible to pose more detailed questions, depending on the answers of the interviewees. One part of the interviews was structured. The respondents were asked to evaluate the significance of the named risks in the scale from 1 (not significant at all) to 5 (very significant) during the interviews (see Appendix 2). A list of six outsourcing risks was not sent in advance. This was because one aim of the interviews was to find out what outsourcing risks the companies were aware of, and therefore this list of the risks was discussed in the end of the interviews after the questions related to outsourcing risks.

The interview with the first Russian company was conducted in English, and with the second Russian company there was an English-Russian interpreter. The international company was interviewed in Finnish. All the interviews were tape recorded and transcribed.

1.4 Structure of the thesis

The structure of the thesis consisting of six chapters is illustrated in figure 1.

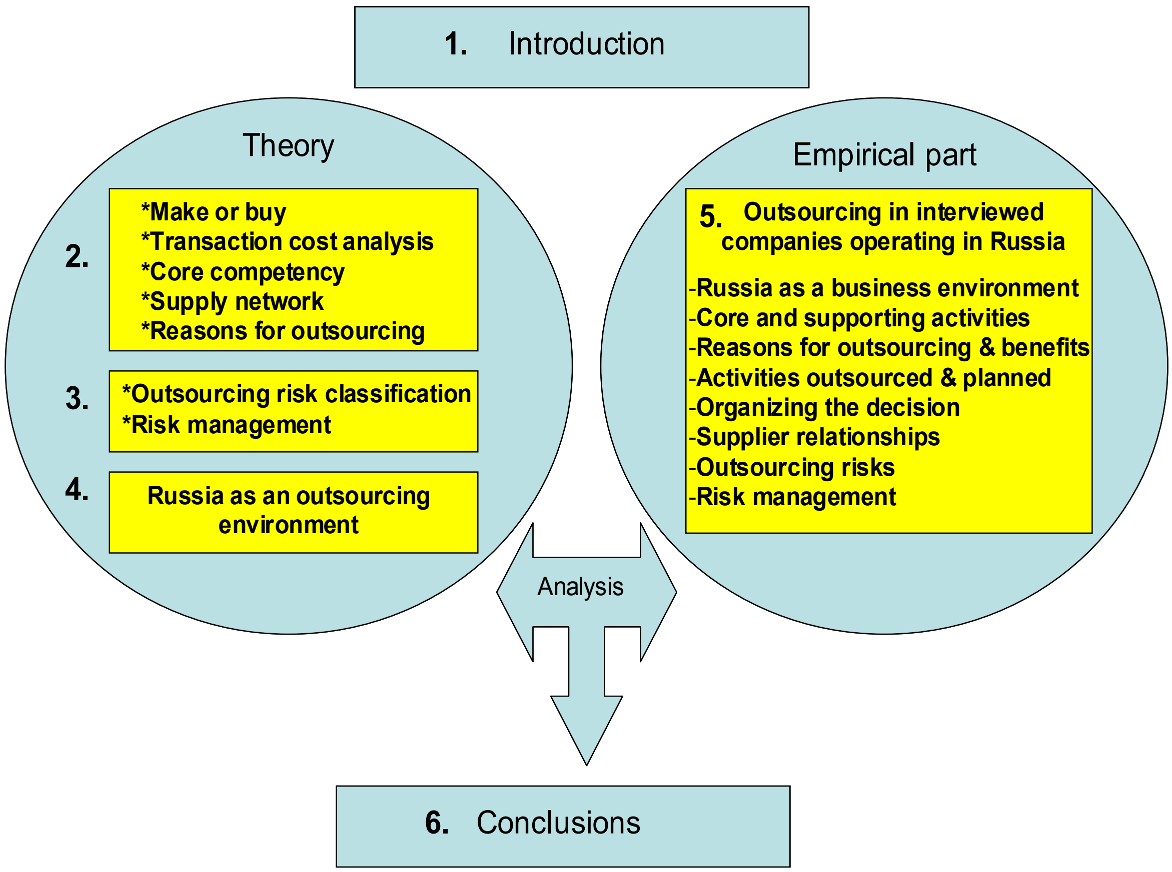

Figure 1: Structure of the thesis

Chapter 1 is an introduction to the study, consisting of the background of the study, the research problem with sub-problems, as well as the objective, methodology, and structure of the thesis.

In chapter 2, outsourcing is defined and the basic outsourcing factors are discussed. Firstly, the make-or-buy situation is described. A three-phase process, the different roles of actors involved in make-or-buy decision making, and the so called outsourcing “gray zone” are discussed. The second topic is transaction cost analysis and the factors that affect transaction costs. Core competency is the third topic. The supply network is discussed from two different viewpoints: the number of suppliers needed, and the way the suppliers are organized. Finally, reasons for outsourcing are explained in the end of chapter 2.

In chapter 3 the outsourcing risks are discussed. The chapter is divided into two subchapters: risk classification with seven different outsourcing risks presented in the literature, and risk management with different phases of risk management process. One risk management model for outsourcing is also demonstrated.

Chapter 4 deals with Russia as an outsourcing environment. The special characteristics related to outsourcing and the business management culture are discussed.

Chapter 5 is the empirical part of the study, based on interviews with OEMs operating in the Russian food industry. The framework of the different basic outsourcing factors discussed in chapters 2, 3, and 4 is placed in the Russian business environment. The outsourcing challenges are discussed from the viewpoint of the OEMs. The analysis is done by comparing the answers of the interviewees with each other and with the relevant part of the theory.

Lastly, in chapter 6, conclusions based on the research results are provided and suggestions for further studies presented.

2 OUTSOURCING ON THE BASIS OF LITERATURE

Business relationships have changed notably during the last decades. Above all supplier relationships have become vital through increasing outsourcing and networking of companies. To be successful in the market, companies need to interact with other firms and organizations. Inter-organizational networks help enterprises to concentrate on their core competencies/capabilities and achieve competitive advantages. The change in business relationships is never completed, but it is a continuous process. Cox (1996) has discovered that companies must all the time make strategic sourcing decisions based on changes in external and internal business conditions and environments.

Among others, Arnold (2000) has described outsourcing as an abbreviation for “outside resource using”. Outsourcing signifies the activities that have previously been carried out by the company itself, but now the products and/or services in question are purchased from external suppliers. Activity that has traditionally been done internally is shifted to an external provider, and the employees of the original organization are often transferred to the service provider. According to Karjalainen et al. (1999:5), this is to say that the needed capability exists or at least existed when the outsourcing decision was made. The change evoked with outsourcing is rather permanent than temporary by nature. Quelin and Duhamel (2003) have defined outsourcing as the operation of shifting a transaction previously governed internally to an external supplier through a long-term contract. Outsourcing involves also the transfer of staff to the vendor.

There are four main elements in the outsourcing model of Arnold (2000), as illustrated in figure 2: the outsourcing design itself, outsourcing subject, outsourcing object, and outsourcing partner.

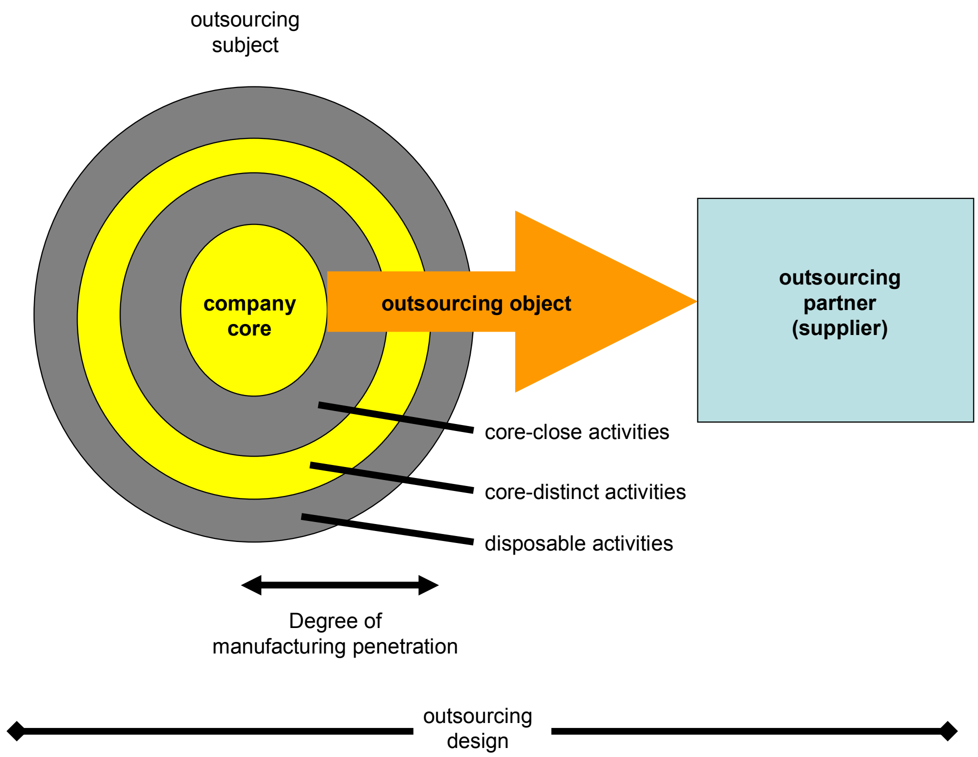

Figure 2: Outsourcing design (Arnold 2000)

The outsourcing subject is the company which does the outsourcing decision, or decides not to outsource. The outsourcing object is the activity which it is possible to outsource. The outsourcing partner is a possible supplier to take care of the outsourced activity. In addition there are four kinds of activities inside the company (i.e. outsourcing subject): the company core, which is essential for the company's existence, core-close activities which are directly linked with the core activities, core-distinct (supporting) activities, and activities with general availability, i.e. disposable activities. Core competencies are discussed more closely in chapter 2.3.

2.1 Make or buy

Outsourcing decision making is always based on a make-or-buy question. The make-or-buy decision is the act of making a strategic choice between producing the necessary components or services internally (in-house) or buying them externally (from an external supplier). In the “make” option, the company has to organize the whole production process, for example new factories must be launched and the supply chain must be organized. The company faces all the costs arising during the production process. In the “buy” option, the company purchases the product or service from another company. It delegates all the rights to produce the components and services to the other organization. The other organization takes care of the production process and bears all the production costs.

According to Leenders et al. (2006: 482), almost no function is immune to outsourcing. They mention functions like janitorial, food and security services, which have been outsourced during recent years. The role of information systems has recently become notable as a candidate to be outsourced. Also mail rooms, copy centers, and travel departments have been popular outsourcing targets.

Platts et al. (2002) divide the make-or-buy process into three phases:

(1) preparation,
(2) data collection, and
(3) analysis and results.

In the first phase, the preparatory work for the project occurs. The project team is selected and the process to be considered is identified and specified. The second phase is the most demanding one. The outsourcing decision that will be made in the third phase is based on the results of the data gathering in the second phase. The factors influencing the performance of in-house and external supply are analyzed to give a figure which provides an indication of the relative merits of making or buying.

In every make-or-buy situation, two main roles are recognized: an advisory role and a decision-making role. Advisors are the persons who by recognizing the need start the make-or-buy process. They are also responsible for gathering all the data required for the evaluation of each alternative. The decision-making role goes with the authority to make the final decision. It is important that all departments that contribute to the decision, or will be affected by it, should be involved in making the decision. The decision-making committee should include representatives from different departments, such as the financial, engineering, production, personnel, sales, marketing, and purchasing departments. This kind of committee is in a strong position to determine which aspects of their products give them a competitive edge and whether critical competence lies in-house or with an external supplier. (Moschuris 2007)

It is also possible to use a so-called “gray zone” between 100 percent make and 100 percent buy. This kind of solution could be useful for testing and learning, because there is no need to do the final make-or-buy decision. Especially when buying services without any need to make equipment investments it may be economical for the company to use low-cost internal labor instead of expensive external staff or low-cost outside staff instead of expensive inside staff. (Leenders et al. 2006: 479)

2.2 Transaction cost analysis

There are always transaction costs when making an economic exchange. For example when a construction firm buys spare parts from a hardware store for a cement mixer, the costs will not only be the price of the spare parts themselves, but also the energy and effort it requires to find out which of the various spare part producers is preferred, where to get the spare parts suitable for that specific cement mixer and at what price, the cost of travelling from the construction site to the store and back, the time used, and the effort of the paying itself; the costs above and behind the price of the spare parts are the transaction costs. When rationally evaluating a potential transaction, it is important to consider the transaction costs, which may be significant, like search costs, contracting costs, monitoring costs, and enforcement costs.

Transaction cost analysis (TCA) is used when the company is making the decision of whether to perform an activity internally (vertically integrate or insource), or in the market (horizontally integrate or outsource). The decision between outsourcing and vertical integration depends on the transaction costs associated with them. When the marginal costs of using the markets (i.e. transaction costs) are higher than the costs of using own recourses (i.e. management costs), a transaction should be organized within the company and vice versa. Transaction costs are seen as organizational failures due to environmental (uncertainty, asset specificity, small number of potential trading partners) and human (bounded rationality, opportunism, information asymmetry) determinants. The level of transaction costs depends on the frequency of the transaction, the level of transaction-specific investments, and external and internal uncertainty. These factors are discussed in the following chapters. (Ellram & Billington 2001, Hallikas et al. 2004)

2.2.1 Frequency of transactions

Williamson (1985) has described different transactions, as depicted in table 1. Three different investment characteristics are divided in two frequency categories: occasional and recurrent.

		Investment Characteristics		
		Nonspecific	Mixed	Idiosyncratic
Frequency	Occasional	Purchasing standard equipment	Purchasing customized equipment	Constructing a plant
	Recurrent	Purchasing standard material	Purchasing customized material	Site-specific transfer of intermediate product across successive stages

Table 1: Illustrative transactions (Williamson 1985:73)

Occasional transactions may create contractual problems and make opportunistic behavior possible, and hence a recurrent business contact normally decreases opportunistic behavior. An example of frequent transactions is standard material purchases for manufacturing processes, whereas infrequent transactions include for example the procurement of productive machinery. (Komonen 2001: 43)

2.2.2 Specificity

The most significant aspect of a transaction is specificity. Specificity can be divided into two main types: asset specificity and human capital specificity. If the asset in question cannot be redeployed to alternative uses, it is said that the asset specificity is high. A lot of information must be exchanged before, during and after the exchange of goods and services with high specificity. If particular skills or services have high specificity, these activities must be undertaken internally. This stems from the fact that the more dependent a company is on its supplier, the higher are the transaction costs. It is also not possible to realize large scale effects when only a few suppliers exist. Low specificity means that little information has to be exchanged with the transaction partner. Objects with low specificity can be outsourced and the economies of scale can be exploited by using external outsourcing partners. The significance of asset specificity for outsourcing is that if activities that require transaction-specific investments are outsourced, the company will find itself locked in to its supplier. (Arnold 2000, Cox 1996, Hallikas et al. 2004)

2.2.3 Uncertainty

There are two types of uncertainty affecting transaction costs: environmental and behavioral. Environmental uncertainty stands for the development of external factors that cannot be influenced by companies. It depends on the market in which the companies operate. If the level of environmental uncertainty is high (e.g. demand fluctuates remarkably and unpredictably), the likelihood of vertical integration increases. The idea behind behavioral uncertainty is that the situation involving the transaction is such that the contracting parties cannot be sure if the other party has fulfilled its obligation or not. The two forms of uncertainties are interrelated. This is to say that behavioral uncertainty does not facilitate opportunistic behavior or contract difficulties, if there is no environmental uncertainty or only little of it exists. (Ellram & Billington 2001, Komonen 2001: 43)

Monitoring costs and coordinating costs are closely related to uncertainties. For example it can be difficult to monitor a partner’s capability to produce the suitable quality (monitoring cost), and often it is necessary to coordinate the activities with external suppliers strictly when starting to execute a business idea of one’s own (coordinating cost). (Komonen 2001: 43)

2.3 Core competency

According to Arnold (2000), only the goods and services which are considered to be core competencies (i.e. with highest specificity) should be produced internally. Core competencies should not be outsourced. That is because core competencies are the activities that provide long-term competitive advantage. If the supplier markets were efficient, companies would outsource all activities except core competencies. Core competencies consist of three elements. Firstly, they differentiate the company from its competitors. In the eyes of the customers the characteristics of the core competency must be essential. Secondly, competitive advantage must be sustainable, and the resources and know-how for the product must remain unique. It must be possible to protect the core competency against imitation by competitors. Thirdly, to be core competencies, these resources must be usable for multiple purposes.

Ellram and Billington (2001), on the other hand, have listed characteristics of core competencies as follows. Core competencies are a company’s unique sources of leverage in the value chain. They are areas where the company can dominate and perform activities important to the customers better than others. These elements are important to the customers in the long run. It is not a question of products or functions, but skills or knowledge sets embedded in the organization's systems which are capable for long-term adaption or evolution. The number of core competencies is limited, and generally one company may have two or three of them.

2.4 Supply network

Outsourcing not only impacts the organization and its immediate relationships, but also changes the structure and processes of the supply network. Increased outsourcing allows access to global markets, and may cause organizations to seek international sources for perceived “best in class” performance. This has contributed to supply networks becoming globalised. (Harland et al. 2002)

The supply network is illustrated in figure 3. The network includes suppliers and suppliers’ suppliers and so on upstream to the original source, and customers and customers’ customers and so on downstream to the end customers. In the other words, a business network is comprised of several tiers of suppliers.

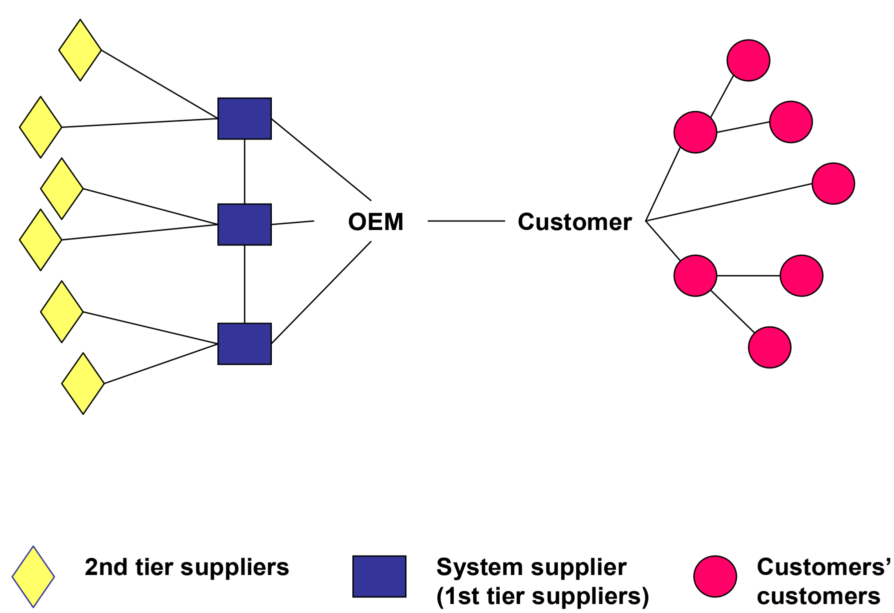

Figure 3: Structure of the industrial network (Hallikas et al. 2002a)

The first tier suppliers working for the OEM have again their suppliers. Thus, like the buying companies, they need to take the responsibility of the work of their suppliers against the OEM. Hallikas and Virolainen (2004) have defined a supply network as a set of supply chains, describing the flow of goods and services from original sources to the end customer. In the network environment there is a strong interdependency between actors, resources and activities.

According to Kulmala et al. (2002), when compared to traditional competition, networking includes four main characteristics: (1) strong commitment to partners and communication on all levels of the organization, (2) transfer of competencies to decentralized, flexible and independent units, (3) end product and customer approach for component and system suppliers, (4) increased speed of change and operations. These trends lead towards intense networking. Close relations to suppliers make easier supply chain management possible. Competency transferred to suppliers cannot be utilized without trustworthy relationships. The customers must have influence over the supplier's process and product development to make cost reduction possible.

2.4.1 Single sourcing versus multiple sourcing

There are two main issues in the design of a supplier structure. The first is the number of suppliers needed, and the second is the way the suppliers are organized. In this chapter, the basic problem in procurement strategy is discussed: the choice between single and multiple sourcing. The way the suppliers can be organized is discussed in chapter 2.6.

Today the use of a limited number of suppliers or even one supplier is favored in order to develop a long-term partnership with the suppliers to achieve the same benefits as provided by multiple sourcing. The benefits of single sourcing include higher quality at lower total cost to the buyer and the fact that the suppliers are linked to higher levels of cooperation. Purchasing managers who prefer single sourcing are less interested in low initial price and much more interested in the total life cost of the product. In addition, single sourcers are more concerned about the technical support available and the reliability of the product than multiple sourcers, primarily because they plan to concentrate purchases with these firms over the long run. Selecting an appropriate partner is becoming a more important responsibility for purchasing professionals. (Berger et al. 2004, Swift 1995)

A critical difference between single sourcing and sole sourcing must be remembered. In the single sourcing approach there are multiple suppliers available, but the buyer uses only one of them. In the sole sourcing approach there is only one supplier available, and the buyer must use it. (Larson & Kulchitsky 1998)

In the multiple sourcing approach there are several suppliers competing intensively against each other. When there are many suppliers, and since a supplier responds to the demands and specifications of a particular quotation, the buyer has the opportunity to get lower prices. However, dealing with several suppliers requires longer time in negotiation, and this may delay or disturb production schedules. In the case of multiple sourcing, the traditional attributes of price, quality, and delivery are emphasized. (Berger et al. 2004, Swift 1995)

2.4.2 Economic institutions as design alternatives

The basic idea of TCA is to find a governance structure with the lowest costs for each transaction. The most effective way to handle standard transactions is typically the use of markets. Vertical integration becomes the best choice when the investments are specific by nature. Between the market option and vertical integration there is space where co-operative alliances should be favored. Choosing the right relationship with suppliers is at least as important as the consideration of the make-or-buy question itself. This is because it is of major importance that the competitive position of the company is not compromised once the organization no longer has total control over the production of the outsourced products.

Markets

In the markets the price mechanism is the decisive factor steering transactions. There are immediate incentives for all transaction partners. If customers' requirements cannot be met by a certain supplier, this kind of supplier will not be able to participate in economic exchanges any longer. The market option can be chosen when the degrees of uncertainty and complexity are minor and the danger of opportunistic behavior is small. If there are several possible suppliers available and the transactions do not need any specific investments, the market option should be preferred. (Arnold 2000, Blomqvist et al. 2002)

Vertical integration

Vertical integration, i.e. combining activities from different stages of the value system, is an opposite to markets. The more activities a company performs from producing the raw materials to delivering the final products to the end user, the higher is the level of vertical integration. Vertical integration is based on the centralization of property rights by management. Thus it is seen as the best alternative when the level of uncertainty and the danger of opportunism and complexity are high. Also when asset specificity is high and there are only few providers of complementary capabilities, and trust between partners is lacking, the vertical integration should be preferred. (Blomqvist et al. 2002, Arnold 2000)

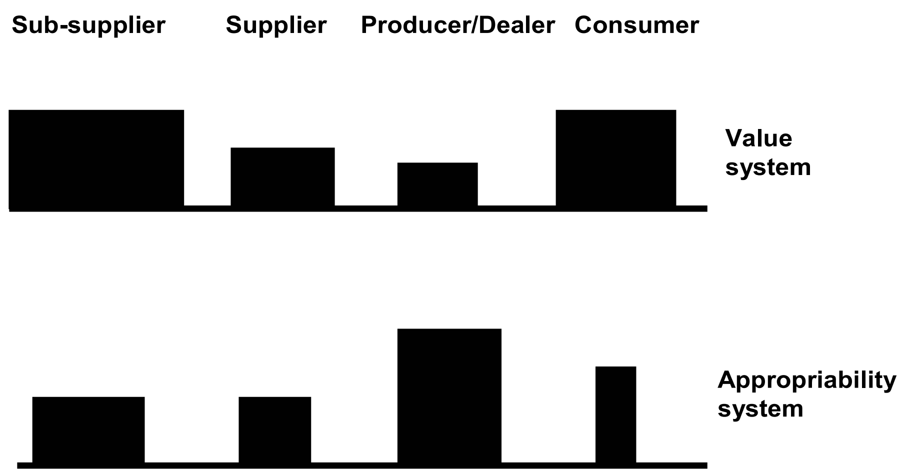

Figure 4: Appropriability system (Hermans et al. 2004)

According to Hermans et al. (2004), it is possible to find imbalance in the value system of a product or service. The system is unstable if there are imbalances originating from the fact that value is created at one location and appropriated at a different one. This is illustrated in figure 4. Vertical integration could be seen as a solution for removing the imbalances.

<u>Hybrids</u>

Many governance structures are neither markets nor hierarchies, but combine elements from both. They are called hybrids. Partnership solutions between independent companies can best be regarded as a hybrid. Partnerships are most preferable when there are factors which speak both for vertical integration and for outsourcing. Blomqvist et al. (2002) have pointed out that partnerships emerge in a business environment with high volatility, high degree of uncertainty and high degree of asset specificity. It is clear that a partnership-type arrangement in above conditions is more viable than vertical integration or the market option. It must be remembered, however, that partnership is not an easy resolution in any conditions. It is usable when it really creates some extra value compared with markets and vertical integration. In partnerships there might arise problems with asymmetric information and opportunism. Trust and reciprocity among partners are needed to avoid these kinds of problems.

According to Karhunen and Kosonen (2002), problems arisen during a partnership may be divided to task-related and partner-related ones. The most common task-related problems are associated with the quality of the product and delivery times. Partner-related problems include misunderstandings between the partners, such as unrealistic perceptions considering the company's own contribution to the relationship. Partner-related problems are more serious than task-related ones, because they may lead to dissolution of the alliance, or may be an obstacle for the creation of it.

2.4.3 Characteristics of different governance structures

Virolainen (1998:133-134) has compared the governance structures in different circumstances as illustrated in table 2. The selection of a suitable governance structure is affected by asset specificity, transaction uncertainty, frequency of transactions, flexibility, strategic risks and qualification of suppliers. To be successful in outsourcing, the company must have both competitive and partnership strategies because different activities require different sourcing means.

	Asset specificity	Trans-action uncertainty	Frequency of interaction	Flexibility	Strategic risk	Qualification of supplier
Market	Low	Low	Low / High	High	Low	Low
Partnering	Medium	Low / Medium	High	Medium / High	High / Medium	High
Vertical integration	High	High	High	Low	High	Low

Table 2: Procurement strategy decision associated with a combination of different circumstances (Virolainen 1998: 133)

In table 3 Blomqvist et al. (2002) summarize a list of different benefit-generating factors and mechanisms provided by markets, partnership and vertical integration.

Markets	**Partnership**	**vertical integration**
* economies of scale * lesser risk * less investment in specific assets * increased flexibility * increased variety * high-power incentives * efficiency through fierce competition	* focus on core competencies in the value chain * ability to coordinate disperse knowledge * ability to create incentives for coordination e.g. trust * risk sharing through separate ownership of assets * investments in relation-specific assets * communication and information sharing * improved quality * shorter time-to-market	* economies of scope * economies of scope through learning * effective management and control through ownership * cost-efficiency through economies of joint ownership * competence-enhancing innovations * exploitation of monopoly power * efficient internal communication network

Table 3: Benefits provided with different governance structures (Blomqvist et al. 2002)

Although the partnership option makes it possible to combine the benefits of markets and vertical integration, it is a more challenging governance structure to manage. As already mentioned, it must be kept in mind that partnership is not an easy resolution in any conditions.

2.5 Reasons to outsource and to avoid outsourcing

Quelin and Duhamel (2003) have found that the three most important criteria when making outsourcing decisions are: to lower operational costs, to focus on core activities, and to gain flexibility. Jackson et al. (2001) also agree with these three, and in addition they list access to technology and market discipline as criteria affecting the outsourcing decision.

The first reason cited for outsourcing is saving money. Economies of scale can be achieved when the supplier concentrates on one area and provides this service to many corporations. Savings typically result because the outsourcing partner can access a cheaper, more flexible work force and the latest, most efficient technology. The other reason is cost control. When the supplier charges for each activity, as opposed to the “free” in-house activity, people benefiting from the activity may be more cautious. Outsourcing also makes sense when the use of an activity is variable or unpredictable. An organization may for example recruit staff with special skills on an irregular basis if in-house work is not economically reasonable. (Jackson et al. 2001, Belcourt 2006)

Focusing frees internal resources and allows the organization to concentrate on its core activities. The move of secondary activities of the organization to suppliers whose core activities these functions are, make it possible for the organization to exploit relative advantage to maximize total value. By outsourcing non-core activities, managers hope to be able to focus on value-added roles. (Jackson et al. 2001, Belcourt 2006)

In efforts to manage business volatility optimally, organizations realize outsourcing as a means to gain flexibility that is impossible to achieve internally. Using outside suppliers can improve the scalability of a company's production capacity at a far lower cost. Outsourcing can enhance three kinds of flexibility: functional (i.e., labor can be redeployed to cover new work tasks or methods), wage (i.e., pay linked to performance), and numerical (i.e., headcount is adjusted to demand). (Jackson et al. 2001, Quelin & Duhamel 2003)

Functions are often outsourced because organizations need reliable access to new technologies. Certain suppliers may have proprietary access to technology or other intellectual property which the company would not otherwise have access to. This new technology may improve efficiency and the long-term total cost structure. (Jackson et al. 2001, Belcourt 2006)

The fifth criterion affecting the outsourcing decision is market discipline. By putting certain functions out to bid, companies increase their choices and gain greater insights as to the true costs and benefits of these activities. Transparency and accountability are enhanced. Market-based contracts focus on output, not input, and they promote innovative work practices. (Jackson et al. 2001)

Outsourcing does not always turn out well. According to Jackson et al. (2001), approximately 20 to 25 percent of outsourcing agreements fail within two years, and half fail within five years. Service-level failures, scope disagreements, cost disputes, and personality clashes are the most common problems in relationships with outsourcing partners. Jack and Raturi (2002) describe in their study a company that did not use outsourcing as a source of volume flexibility. This was particularly because the company had tried outsourcing before with some poor results. Four main problems were identified in this case: (1) inability to adequately specify requirements and volume levels to get good prices in the contract; (2) high costs of outsourcing; (3) poor quality levels; and (4) delivery reliability problems.

3 RISKS RELATED TO OUTSOURCING

Increased co-operation of companies in a supply network causes transfer of risks between the companies; some risks may increase and others may decrease. All different types of risks in the network can seldom be controlled by one action. Disturbances and unexpected events have different consequences on different companies in the network. Thus several risk management strategies are needed in supply networks.

The company's position in the network is a remarkable factor, because it can for example influence access to the resources of other network members. The position needs to be considered when assessing and managing risk. Sharing the risks and benefits depends on the type of collaboration. In joint ventures or strategic alliances there are often formal written agreements of risk and benefit sharing, or the sharing is a natural consequence of joint ownership. There may not be such clarity of risk and benefit sharing in less formal types of collaboration. In these cases it is consequential to form an agreement to ensure long-term commitment to allow sharing of sensitive information, knowledge and competences. (Harland et al. 2002)

3.1 Risk classification in the literature

Generally, risk is understood as a possibility to loose something in consequence of some unexpected event, and the probability of that event. Randomness or contingency are characteristics of risk. Risk can also be unforeseeable, but often organizations are prepared for the realization of the risk. (Eerola & Louto 2000: 23)

Zsidisin (2003) defines supply risk as the probability of an incident associated with inbound supply from individual supplier failures or supply market occurring, in which its outcomes result in the inability of the purchasing firm to meet customer demand, or cause threats to customers' life and safety. It is essential that supply management professionals understand both the sources and the outcomes which incorporate supply risk, because the effects of negative supply events can have ramifications throughout the network.

Risks related to external suppliers have been grouped in several ways in different studies. According to Chopra and Meindl (2007: 424-426), when transferring the activities to an external supplier, companies must evaluate the following risks: the process is broken, underestimation of the cost of coordination, reduced customer/supplier contact, loss of internal capability and growth in third-party power, leakage of sensitive data and information, and ineffective contracts. Hallikas and Virolainen (2004) have listed four categories of sources of risks emerged in the network context: asset specificity -related "hold up" risks, competency markets -related "inefficiency" risks, nature of knowledge -related "spill-over" or "appropriability" risks, and time horizon -related "timing" risks. Among others, Quelin and Duhamel (2003) and Hallikas et al. (2002b) have also mentioned quality risk. These risks will be discussed in the following subchapters.

3.1.1 Broken process

Strategic issues and operational problems need to be properly addressed by the executive management. There will not be any improvement simply by handing a problem over to a supplier. If the company outsources the activity in which it has lost control of the process, there will certainly be problems. Before planning to outsource the broken process, the first step is to get it under control. This is not the time to do a decision whether to outsource or not before the process is restored as before. (Chopra & Meindl 2007: 424, Hughes et al. 1998:43)

3.1.2 Underestimation of the total cost of outsourcing

It is usual that the outsourcing company underestimates the necessary effort to coordinate outsourced activities. This often happens when the company outsources activities to several suppliers. This kind of outsourcing can be very effective if the company realizes that being a coordinator among external suppliers is one of its core activities. In case of insufficient coordination, there might follow financial losses. (Chopra & Meindl 2007: 424)

Cost management is more challenging in networks than in a single company. Companies must be able to manage their costs; both fixed and variable. The increasing responsibilities often require growing investments; thus the risks of investments often increase. In high demand business cycles companies may endanger their ability to control their cost structures and investments. (Hallikas et al. 2004)

3.1.3 Spill-over risk / Appropriability risk

A company must usually share significant information when using an external supplier. If the same supplier also belongs to another competitive network, there is always risk of leakage of sensitive information to competitors. (Chopra & Meindl 2007: 425)

Spill-over risk is in question when knowledge spill-over between the company and the supplier causes a risk for the company. Products and production technologies cause a lot of spill-over uncertainty. The best way to manage this kind of risk is to develop clear contract policies and property rights. To avoid leakage of sensitive information, companies produce strategically highly important products by themselves (Hallikas et al. 2002b). According to Hallikas and Virolainen (2004), the more appropriable (i.e. easier to protect) the new knowledge is, the smaller are the risks related to outsourcing and vice versa.

Also if outsourcing substantially increases the supplier's power compared to the company, it may be recommended that the company keeps the function in-house. It is also possible to keep a part of a function in-house if a complete loss of capability importantly strengthens the supplier's bargaining position. (Chopra & Meindl 2007: 425)

3.1.4 Inefficiency risk

Chopra and Meindl (2007: 426) have processed the inefficiency risk from the viewpoint of ineffective contracts, whereas Hallikas et al. (2002b) emphasize defective supply market information. Ineffective contracts may cause deactivating the outsourcing partner. If a certain income is guaranteed, this might eliminate incentives for the outsourcing partner to innovate cost reducing. Contracts should be based on a desired service level and leave the outsourcing partner freedom to work at an optimal level. (Chopra and Meindl 2007: 426)

A potential risk in outsourcing is that the company has chosen a wrong outsourcing partner. That is the reason why companies try to be as aware of the markets as possible. If the company has chosen a single sourcing strategy, there may be a lack of awareness of the possible competitive sources. The strategy of multiple sourcing ensures that there is some knowledge about the markets available all the time. If there are only a few possible suppliers in the markets, and the products or services are of high specificity, the long-term partnership arrangement can reduce the inefficiency risk. (Hallikas et al. 2002b)

3.1.5 Hold-up risk

The hold-up risk is understood as a dependency or lock-in on a certain supplier or technology. The specificity of a source is the main factor in the hold-up risk category. The dependency on the supplier matters especially in unsuspected changes in the business environment. An important issue is the company's ability to replace the supplier if risk occurs. The supplier can take advantage of this lock-in by renegotiating the terms of the contract or by insisting on different terms next time around. This post-contractual dependency causes the power relation between the two parties to change — the supplier may take over the dominance. This risk appears to be the root of a majority of the problems companies have experienced. It is even more significant than that of outsourcing core competencies. The hold-up risk can be reduced by maintaining competition between the suppliers. (Hallikas et al. 2002b, Lonsdale 2001)

The hold-up risk may come true also vice versa. If the supplier becomes too dependent on a single customer, it may in the long run lead to the supplier's diminished innovation and product development capabilities. (Hallikas et al. 2002b)

3.1.6 Timing risk

If the outsourcing subject and outsourcing partner operate with different time scopes and expectations from the cooperation, timing risk may become evident. The partner may behave opportunistically and operate on fast profit seeking and short term focus, whereas the outsourcing subject aims at long-term strategic collaboration. (Hallikas et al. 2002b)

3.1.7 Quality risk

The risk of loosing the control of quality is also a major concern in outsourcing. Is the outsourcing partner capable to offer activities which in the long term will satisfy the company's own and the end customers' requirements? By outsourcing the company takes the risk of no longer holding the necessary know-how and controlling the evolution of an outsourced activity. It is difficult to change the supplier or bring the outsourced activity back in-house after signing an outsourcing contract. (Quelin & Duhamel 2003)

It is more effective if the quality risk identification and analysis of causes and effects are conducted together with the supplier. If there are many suppliers available, the strategy of multiple sourcing is a recommended alternative also in reducing the quality risk. (Hallikas et al. 2002b)

3.2 Risk management

The consequences of risk are not always easy to manage in the network environment. Critical incidents may influence also other network members heavily. As a member of a network, each company operates at its own risk and should manage the risks itself. However, it is useful to share the risk management process partially and to develop collaborative means to manage the risks. This is because the interconnections of the companies in the network make them dependent on each other. Some network members may be highly risk-averse whereas others are risk-takers. The attitude changes with experience; a company or sector used to taking risks may change its attitude after experiencing heavy losses. Risk management has to be holistic and it has to be accepted that multiple approaches are compulsory if risk is to be avoided. (Harland et al. 2002, Hallikas et al. 2004)

In this chapter risk management is discussed from two different points of view. The first viewpoint is risk management in the network environment; this means the risk management process during the period after the outsourcing decision has been done. Lallukka (2005) has described risk management as a combination of supply market influence, selected supplier strategy and management of a relationship. The second viewpoint is risk management during the outsourcing decision making process.

3.2.1 Risk management process in the network environment

Harland et al. (2002) have introduced a supply network risk tool for helping to identify, asses, and manage risks (figure 5). The tool is divided into six boxes. Box number 1 involves mapping the supply network. This involves understanding who owns what, and clarifies the roles and responsibilities of the network members. This is often a difficult task, because all the key elements have to be identified and others ignored. In box number 2 there is information concerning the type of risk and its location. The specific risks that will be considered for the particular activity should be identified through brainstorming with other actors in the supply network. At this stage only those risks with a significant potential loss to any actor in the network should be considered. Box number 3 includes the chosen types of risk. They are assessed for the likelihood of their occurrence, exposure in the network, potential triggers of the risk, at what stage in the life cycle the risk is likely to be realized, and what likely potential losses might occur. What is the likelihood that a risk will occur and what is the notability of the consequences and losses are the main questions which must be answered when assessing the risk.

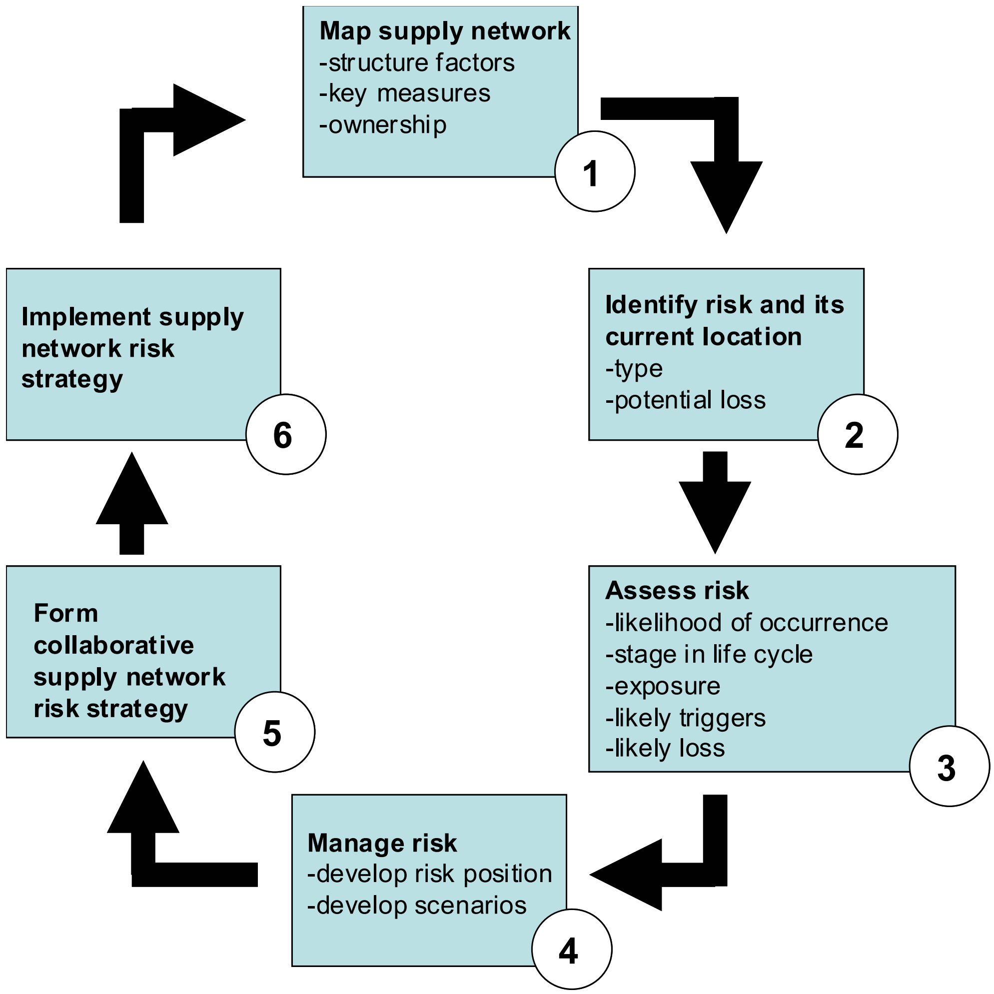

Figure 5: Supply network risk tool (Harland et al. 2002)

Risk management itself takes place in box number 4. The assessment information is analyzed and alternative risk management actions are recommended. The risk position is predicated on the particular problem and the actors involved. This position can be reactive, defensive, prospective or analytical. Schemes of alternative network structures and relationship strategies are possible to be developed, depending on the risk position. In the last two boxes of the tool, the chosen redesign of the network and relationship strategies within it are executed through an updated common supply network risk strategy. This new strategy is brought into effect and evokes a remapping of the network. The tool brings the decision makers back to box number 1. (Harland et al. 2002)

According to Hallikas et al. (2004), the identification and evaluation of the common goals of the network is a ground for a successful mutual risk management process and common network risk management strategy. The risk management process in the network environment is described by Hallikas et al. as action with four phases: risk identification, risk assessment, decision and implementation of risk management actions, and risk monitoring. The four phases are discussed below.

Mutual risk identification

In a network environment, due to the interdependencies between the organizations, mutual risk identification must be taken into consideration. The risks that have not significant impacts for an individual company but may affect seriously the whole network or other network members' operational capability are to be identified. There are potential benefits of sharing information, opinions and visions within the network, between the partners. Different views help in recognizing and understanding common threats in a more holistic way. The supply network structures including the risks are often very complex and difficult to perceive, and this makes many risks remarkably difficult to identify. Interruptions, quality failures and delivery fluctuations are common strong signals of risks in the supply network and in production systems. As each member of the network is responsible for its own risks, it must identify the risks also from its own viewpoint. (Hallikas et al. 2004)

According to Hillson (2002), there is no single best method for risk identification. He has listed plenty of different techniques for risk identification, like brainstorming and workshops, checklists and prompt lists, and questionnaires and interviews. The appropriate risk identification method according to Hillson is a combination of different techniques.

Mutual risk assessment

Hallikas et al. (2004) have assessed two components of risk, the probability and the consequences, separately in a five-class scale as illustrated in tables 4 and 5. These classifications answer the two main questions posed by Harland in his tool in figure 5, box 3: 1) what is the likelihood that a risk will occur, and 2) what is the notability of the consequences and losses.

Rank	Subjective estimate	Description
1	Very unlikely	Very rare event
2	Improbable	There is indirect evidence of event
3	Moderate	There is direct evidence of event
4	Probable	There is strong direct evidence of event
5	Very probable	Event recurs frequently

Table 4: Risk probability assessment scale (Hallikas et al. 2004)

When assessing the subjective probability and the impact of the risk, the company's own experience and other companies' performance are utilized.

Rank	Subjective estimate	Description
1	No impact	Insignificant in terms of the whole company
2	Minor impact	Single small losses
3	Medium impact	Causes short-term difficulties
4	Serious impact	Causes long-term difficulties
5	Catastrophic impact	Discontinue business

Table 5: Risk impact assessment scale (Hallikas et al. 2004)

An event or change which is harmful to one company in a network may have no or positive effects to another company in the same network. Thus the possible effects of the risks should be assessed from the viewpoint of the company. Other than financial consequences to be considered are also immaterial consequences, such as trust and reputation. These can cause financial losses in the long run. In a network environment a final consequence may be that the company loses its position in the network. (Hallikas et al. 2004)

Decision and implementation of risk management actions

In the network environment, risks can be managed by developing a collaborative network strategy. In network-wide analysis the basic idea is to find the optimal risk management strategies to share and balance risks at network level. The risk strategies are normally grouped according to their intended effect towards the risk. Four different groupings are used: risk elimination, risk transfer, risk reduction, and risk taking. Risk elimination as a risk strategy seeks to eliminate the uncertainty by making it impossible for the risk to occur. When transferring the risk there is an ambition to find another actor in the network to whom the responsibility for action can be passed. This may reduce the total risk of the supply network if the company taking the risk can cope with it better than the company transferring it. Risk reduction means actions which reduce the size of the risk to make it more acceptable for the network. It is possible to reduce both the probability and the impact of the risk. When taking the risk the idea is to accept that risk exists. It is possible to respond to risk either actively by allocating appropriate actions, or passively by monitoring the status of the risk. (Hillson 2002, Hallikas et al. 2004)

Mutual risk monitoring

According to Hallikas et al. (2004), the company and its environment are in a state of change all the time, and thus also the risk status can not be permanent. Monitoring the changes in the network, customer needs, technology, partner strategies and competitors and updating the risk assessment in keeping with changes is essential. Mutual risk management at the network level, as well as risk management at the company level are continuous processes. This is also the idea behind the risk management tool in figure 5, in which the tool brings the decision makers from box number 6 back to box number 1.

3.2.2 Risk management model for outsourcing

Lonsdale (1999) has constructed a risk management model for outsourcing. The first issue in the model, illustrated in figure 6 is whether the activity planned to be outsourced is responsive for competitive advantage or not. If the answer is affirmative, the activity is better to keep in-house, otherwise outsourcing is an alternative. This has already been discussed in chapter 2.3, “core competency”. In the second phase the decision makers must avoid monopolistic or oligopolistic supply markets. In the third phase the asset-specificity of an activity is categorized in three different categories: high, medium, and low. The issue here is how to manage the risk of post-contractual dependency. As mentioned in chapter 2, if the asset-specificity is high, it is better to keep this kind of activity in-house. In case the asset-specificity is medium, outsourcing with a bilateral contract with the supplier is recommended, and when the asset-specificity is low, outsourcing with a short-term contract is suitable.

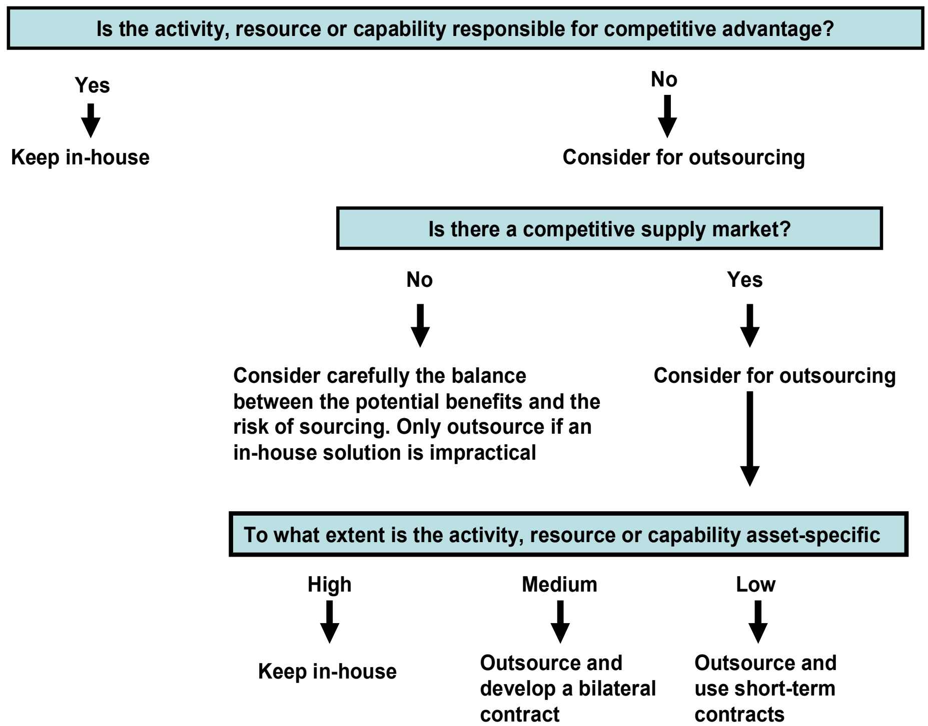

Figure 6: Risk management model for outsourcing (Lonsdale 1999)

According to a literature review related to commercial banks' outsourcing information systems compiled by Adeleye et al. (2004), there are several different methods used in risk management during the outsourcing process. Identification of the risks in outsourcing an activity can be done by reviewing of documentation of an existing system and circulating the list of existing problems. Risks that can be found in the history are possible to come true in the future as well. Also interviews with appropriate in-house users and managers can be useful. The impacts of risk on outsourcing are to be investigated in advance; transaction flows are to be documented, and joint meetings of systems people, operators and end users are to be held. Recommendations designed to avoid or prevent risk from occurring are collected.

4 RUSSIA AS AN OUTSOURCING ENVIRONMENT

The Russian market is still in the phase of transition from a collapsed state-run economy to a free market. This is to say that the Russian economy is still adapting to the new political system which changed in the early 1990's. Lack of freedom and control by authorities are a special feature in doing business in Russia. It is impossible to forecast the political decisions and regulations, and this makes Russia an unstable and testing business environment. In the former state-run economy there was neither business legislation nor the ownership concept in use, and in today's Russia the laws and rules are still inconsistent. Inexperienced bureaucratic authorities facing emerging free markets for the first time, together with the old-fashioned legal system with frequent changes and the absence of an independent judiciary system make corruption an issue. Nepotism, gifts, bribes and price fixing are accepted as traditional business behavior, and non-adherence to laws and judicial decisions are common practices. (Barnes et al. 1997, Johanson et al. 2000, Darkow et al. 2006)

Communism prevailed in Russia for more than seventy years. During this period, under the control of the Soviet Union, economic structures were distorted. It was not significant whether the costs would be covered by later earnings and whether the investments brought any profit. Lack of inter-organizational competition was a clear difference between the central planning system and the western system. Companies were not independent organizations either, but operated as production units whose performance was only measured in terms of the physical quantities produced. (Johanson et al. 2000, Tiusanen & Jumpponen 2001)

Corruption and Bureaucracy

Russia is a demanding business environment, where the most significant problems are related to bureaucracy and corruption. There are several plans for anti-corruption made by different authorities. According to official criminal statistics from year 2007, the expenses originating from corruption were more than a billion rubles. The real expenses are estimated to be 2000 times more. Also a supporting package for small and medium sized enterprises, aiming to decrease the time and expenses related to official supervision, bureaucracy and corruption is in progress. (Tekniikka & Talous 16.5.2008, SVKK 19.2.2008, SVKK 26.6.2008)

Lack of labor

The labor has always been a problem in Russia. Since the Soviet Union collapsed the labor has been available, but the skills are not stable and the work ethic is poor. A new phenomenon in today's business in Russia is lack of labor, especially with technical education. The problem is no longer a poor work ethic but a high turnover of workers. Especially younger managers are willing to change the employer to get even a small rise in salary. The labor shortage and tightened competition are signs of a normalized operational environment. (Tekniikka & Talous 16.5.2008, Talouselämä 7.4.2008)

Infrastructure

Many infrastructure facilities have deteriorated since the economy slowed down in the beginning of the 1990's, and not many investments have been made during the last twenty years. Now infrastructure improvement is ongoing, and the Russian government has set the target of solving the infrastructural problems in the foreseeable future. For example an investment program to develop the traffic infrastructure has been presented. The idea is to build roads, railways and runways and to improve harbors with nearly 370 billion euro during the years 2010 – 2015. (Kauppalehti 23.7.2008, Tekniikka & Talous 6.6.2008)

4.1 Outsourcing in Russia

In Russian enterprises there is still the strong tradition that all the functions are kept inside the company. This is completely different from the specialization and concentration on the key advantages which is the trend in western markets. The business culture where the services are bought from external suppliers is emerging little by little. The reason for this is the lack of resources, which is a consequence of the growing competition that has forced many manufacturers to specialize also in Russia. It is expected that this tendency will become stronger in the future. When outsourcing, the Russian enterprises are quality conscious and appreciate a good reputation of the supplier. Price is not the most decisive criterion when comparing the outsourcing candidates. (Kauppalehti 26.5.2008)

The popularity of vertical integration in Russia is a heritage from the Soviet period when the industrial plants did everything themselves to secure production. No possible subcontractors were available because it was forbidden to found private companies. Firms were forced to solve their resource dependence problems within their own organizations because there was no freedom to buy and sell. Therefore securing supplies was maybe the most important task for the Soviet economy organizations. Nowadays many large companies are beginning to concentrate on their core areas and want to outsource some of their activities, but the lack of subcontractors is a problem in Russia. (Johanson et al. 2000, Dudarev et al. 2004)

Although small enterprises have emerged in Russia, most of them are not suitable to operate as subcontractors, but operate in consumer markets. In addition, the fact is that in today’s Russia establishing any kind of business is a bureaucratic process. Tens of different licenses and permits are needed, and the average time for the establishing process is about two months. The banking sector in Russia has not been able to establish structures to promote emerging enterprises, either. The banking sector itself has functioned poorly, and only a small number of the banks in Russia operate like the banks in the western market economies. If any credits are delivered to small and medium sized enterprises, they are usually short-term with high interest rates. (Tiusanen & Jumpponen 2005, Helanterä & Ollus 2004: 118)

4.2 Business management culture in Russia

Russian managers traditionally concentrate on internal matters within the company. To attain and maintain power and control within the own organization is the main idea in the Russian management culture. External inter-firm relationships are not seen equally important. This behavior comes from the Soviet period as well. Withholding information from others gave individuals an advantage, so sharing knowledge was not seen necessary like today. It was out of the ordinary for Soviet managers to develop any relationships outside the company. The company staff focused only on production issues inside the own company. This incurred a high degree of centralization, and thus a low degree of initiative in improving business relationships. This was harmful to the build-up of inter-organizational trust and commitment. (Barnes et al. 1997, Johanson et al. 2000)

Mashkina et al. (2006) have analyzed the differences in understanding the Russian business norms between Finnish and Russian business partners. According to their study, the Russians think that it is almost impossible to avoid corruption in Russia and from the Finns' point of view it must be realized that corruption exists in Russia. The Russians see it difficult and the Finns impossible to predict changes in the Russian legislation. According to the Finns, in Russia agreements are signed but they might not be implemented. For the Russians, problems with non-payment or breaking the agreement are solved by personal negotiations, and agreements are needed mainly for the bureaucracy. The Russians see that the Finns plan everything very carefully and therefore it takes time for them to make a decision. The situation is changing so rapidly in Russia that it is difficult to make long term plans, and the Finns do not understand this. The Finns for their part see planning and organizing as the foundation of efficient business everywhere, and Russian firms could save time and money by planning. In addition, from the Russians' point of view good personal connections are needed in Russia, but one should separate friendship and business. From the Finns' point of view it is difficult for a foreigner to get the connections that are needed in Russia.

Russia is a country with comparatively weak formal institutions; more importance is given to informal institutions, like personal relationships. Personal trust and informal agreements among managers are emphasized. For managers it is important to pay attention to these when forming business relationships in Russia. According to the authoritarian governance in Russia, there must be a reliable relationship with a manager to reach a reliable relationship between the companies. The manager is the real decision maker, and he/she does not trust anybody but the "own" people, i.e. people he/she is familiar with. In many cities and regions in Russia there is a managerial elite who know each other. A typical phenomenon is an elite rotation in which the managers move from one company to another and the elite remains the same. When it is not possible to trust the legal system, the business managers trust each other. It is said that you can never be sure if somebody conforms to a law, but you can always be sure that the partner you know is reliable. It often happens that the relationship between the companies ends if the essential person leaves the company. (Bäckman 1997: 45, 61, Darkow et al. 2006)

On the other hand, the importance of informal structures like personal relationships in Russia has often been highlighted. It is not free of charge to maintain institutions like these, as they also cause transaction costs. This hampers the development of business enterprises as well. (Tiusanen & Jumpponen 2005: 20)

5 OUTSOURCING IN THE INTERVIEWED COMPANIES

This empirical part of the study is based on interviews done in three companies operating in Russia. All the three case companies operate in the food industry; company A in the confectionary business, and companies B and C in the bakery business. Companies A and B are local Russian actors, and company C is an international firm. The questions asked from the interviewees are based on the theory part of this study. The questions are grouped in four topics: 1) operation of the company in Russia, 2) make or buy, 3) outsourcing risks, and 4) risk management. The questions are presented in appendix 1. The risk ranking (see appendix 2) is based directly on theory chapter 3.1, risk classification in the literature. The analyses are done by comparing the given answers with each other and with the relevant part of the theory.

The chapter is divided into eight subchapters: special characteristics of the business environment in Russia, core activities and supporting activities, reasons to outsource and outsourcing benefits, activities already outsourced and possible to outsource, organizing the outsourcing decision, supplier relationships, outsourcing risks, and risk management. The answers of the companies are presented in the beginning of each subchapter. All the opinions come straight from the respondents: the development manager on behalf of company A, marketing director on behalf of company B, and sourcing manager on behalf of company C. The analyses are conducted in the end of each subchapter.

5.1 Special characteristics of the business environment in Russia

Company A

The real problem in the business environment in Russia from the business development point of view is the infrastructure provided by the government. It is not developed enough for business requirements. For example in case of trying to find a new location for a new production line, the company will face several problems related to infrastructure. Finding a place with all infrastructure facilities and services is very difficult, and because there is shortage of sites with total infrastructure capacity, the price of sites is very high. In the real world this means that if a road to a suitable site exists, there is no gas available, and if there is gas available, then there is not enough electricity capacity. All the other areas of businesses can be managed, but the problems in infrastructure are not under the control of the company.

Company B

When comparing Russia's bakery business to Finland, in Finland the market of bakery products is more stable and already divided among players. In the Russian bakery market, the phase of growth has been completed, and now the phase of consolidation is on the way. If for Finnish companies the direction of development is in customers and products, for Russian companies the direction of development is in acquisition of other companies, e.g. competitors.

Company C

The challenges in the business environment are seen as a part of the business, and in Russia the challenges are only slightly different compared to anywhere else. Some things might be even easier to handle in Russia than for example in the Swedish business culture. One good example is the decision making which can be notably faster in Russia than in Sweden. Therefore it must be easier for Finns than for Swedes to operate in Russia.

One challenge for foreign companies operating in Russia might be that in Western markets the companies are adjusted to operate freely so that the main focus can be in the real business. There is no need to think every week or every month about changes in the business environment depending on a new president or parliamentary election etc. Political decisions in Russia, both nationwide and at the local level might be remarkable and have significant impacts on entrepreneurship. Uncertainty is characteristic for entrepreneurship and for attitudes towards work in companies as well.

There is one challenge stemming from history that differentiates Russia from other business environments: the sellers' market. In the old days, also in the West, to run for example a bakery business, the bakeries were forced to make purchases from wherever the products or services were available. This still is reality in many cases in Russia. Suppliers dictate the terms of contracts, and then it is a ”take it or leave it” –situation.

In the Russian business environment also positive changes happen rapidly. The companies must be all the while ready to react and to seize an opportunity, or some other company will react sooner. The company must be really reactive to succeed in Russia. Requirements in Russian markets are booming all the time, and therefore acting with old time management is not possible anymore. The company must find the best know-how and knowledge in use.

Analysis

The interviewed companies saw the Russian business environment from different viewpoints. The biggest challenge for company A was the underdeveloped infrastructure, for company B the phase of bakery markets and the direction of the future development of the market, and for company C the common uncertainty. These special characteristics are summarized in table 6.

<u>Company A</u>	<u>Company B</u>	<u>Company C</u>
underdeveloped infrastructure	direction of development	uncertainty

Table 6: Special characteristics of the business environment in Russia

The underdeveloped infrastructure is an inheritance of the ending of the Soviet era in the 1990's when the economy in Russia slowed down. Solving the infrastructural problems is one of the main missions of the Russian government (See chapter 4).

Both company B's and company C's concerns are related to the markets. Like company B stated, several companies aim to expand by acquisitions. Contrary to company B's estimation, the growth in the bakery business is not considered to be completed. For example company C in its annual review expects the growth to be continued. The buying habits of the Russian consumers are developing and the buying power is increasing. At the same time, the prices of raw materials and the salaries are rising. On the other hand, company C stated that the Russian administration hampers the markets. Frequent changes in legislation and the absence of an independent judiciary system are among other things seen as problems of the Russian market.

5.2 Core activities and supporting activities

<u>Company A</u>

Company A perceives the development of a new style and new taste of traditional products to be its core activity in the confectionary business. The company is developing modern style cookies and ginger bread by adding new ingredients to traditional products. In addition to development, also quality assurance and building new brands to support the products are seen as core activities.

Manufacturing is understood as a supporting activity of the company. It is not considered as the main activity of the company even though the company has own production in two production lines: modern style cookies and ginger bread. Also logistics is seen as a supporting activity.

Company B

Company B perceives producing fresh and wholesome bread to be its core activity. Logistics is seen as a supporting activity.

Company C

Versatile supply of bakery products, technological know-how and mastery of demand and supply are seen as the core activities of company C. It is not enough that company has excellent products, but the customers must agree with that also. It is important to introduce the right products in right time to the markets, so that the customers are ready to pay a bit more for the products of company C. It is also important to make sure that the resellers are willing to take the products of company C to their selection as high level products.

All the productive machinery and technology which make it possible to run the core activities are seen as supporting activities in company C. Also continuous development of human resources is essential to make it possible to reach the given targets. With human resources it is not meant only baking know-how but also project management, leadership and motivation of people.

Analysis

The core activities and supporting activities of the interviewed companies are summarized in table 7. Although all the three companies operate in the same industry, their core activities and supporting activities differ. So the understanding of the areas which are important to the customers and in which the companies can perform activities better than others is company-dependent.

	Company A	Company B	Company C
Core activity	Product development	Production	Technological know-how and mastery of demand and supply of bakery products
Supporting activities	Manufacturing Logistics	Logistics	Mastery of productive machinery and technology Development of human resources

Table 7: Core activities and supporting activities

Company B considers production to be its core activity, whereas company A understands production to be a supporting activity. Company C has a more strategic approach to the matter of core and supporting activities. When only the activities which are considered to be core activities of the company should be kept in-house and protected against imitation by competitors, the interviewed companies have dissimilar activities as candidates to be outsourced. However, understanding of the roles of own activities give a good readiness to run outsourcing in the interviewed companies.

5.3 Reasons to outsource and outsourcing benefits

Company A

From company A's viewpoint, the main reason to outsource is the fact that the company is not an expert in the activities which are the suppliers' core activities. Also when there is no need to invest on outsourced activities, the capital can be used for developing the core activities of the own company. However, in Russia it is difficult to find partners who can ensure a sufficient quality level for high quality products.

In company A the outsourcing benefits are seen as financial. The price may become a bit higher when an activity is bought from another company, but the return of equity (ROE) will also be higher.

Company B

Outsourcing activities which are the suppliers' core competencies and not the company's, is efficient. It is for example possible to handle more retail stores at the same time when some marketing activities are outsourced. When marketing is outsourced, the company may get more versions of doing marketing activities than in the case of developing the marketing in the own company. The external supplier conducts promotion actions, and there may be hundreds of promoters working for the company. It would be impossible for the company itself to gather, train and control such a number of promoters.

In some cases also price can be decisive in the outsourcing decisions. Marketing agents of external suppliers often come to the wholesale firm in order to maintain for example five different groups of products for the needs of different companies. This means that also the expenses can be divided between five client companies of the external supplier. In case the agent is working only for company B, all the expenses are naturally connected with company B. Another example is transportation. For company B it is not possible to posses and maintain trucks to serve all the customers by vehicles of their own. The company has so many customers that it would become too expensive.

In addition to financial benefits, also flexibility is seen as a benefit of outsourcing in company B. Activities can be bought when they are needed and if they are not needed, there will be no costs, either.

Company C

There are two main reasons why company C has not done much outsourcing yet. The first is lack of experience. This is to say that company C is not yet aware enough of which would be the activities possible to outsource and which activities need to be kept in-house. The second reason is the uncertainty of whether there are suitable suppliers in the Russian markets available or not. At the moment company C is not aware of suppliers capable enough in Russia.

One of the outsourcing benefits from the viewpoint of company C is getting skilful and trained people for the company’s purposes. Companies are competing for trained labor already now, and in the future the situation will tighten. By outsourcing there is no need to hire all the labor to the company’s own pay list. Also the company does not have to be the best in everything if the know-how needed is available from external suppliers. In addition to skilful labor and flexibility, cost savings are perceived as an outsourcing benefit.

Analysis

The reasons to outsource and the outsourcing benefits from the viewpoint of the interviewed companies are summarized in table 8. Companies A and B have a conception of reasons to outsource, whereas company C as a foreign actor in the Russian markets is still in a situation where outsourcing is not current, and therefore it only underlines the reasons of why not to outsource. However, all the companies are able to mention several benefits originating from outsourcing.

	Company A	Company B	Company C
Main reasons to outsource (+) or not to outsource (-)	+ activity not company's core + no need to invest - difficult to find capable supplier	+ activity not company's core + coverage + price	- not clear which activities to outsource - difficult to find suitable suppliers
Benefits received by outsourcing	Financial benefits	Financial benefits Flexibility	Skilful labor availability Flexibility Financial benefits

Table 8: Reasons to outsource and outsourcing benefits

On the basis of the answers, companies A and B have realized that it is reasonable to transfer non-core activity of the company to an external supplier who conducts this activity as its core activity. This is a tendency in today's business, and it naturally frees up internal resources to concentrate on the core activities of the organization. The answers show also that it is difficult to find capable/suitable suppliers in the Russian markets. This can be seen as a constraint on outsourcing.

The interviewed companies are very aware of outsourcing, and all the companies are aware of the financial benefits. Company B especially mentioned economies of scale that can be achieved when the supplier concentrates on one area and provides this service to many corporations. B and C also saw flexibility (headcount adjusts to demand) as a benefit. Using outside suppliers will improve the scalability of the companies' production capacities at lower cost. Company C's mention of the availability of skilful labor can be seen also as access to certain intellectual property or technology, which the company would not otherwise have access to. This is generally known as one of the most important criteria when making outsourcing decisions.

By outsourcing the companies gain greater insights to the true costs and benefits of certain activities. Even if the financial benefits were recognized, the interviewed companies did not mention the improved cost control. This comes true when suppliers charge for each activity, as opposed to the in-house activity which is thought to be free. People benefiting from the activities become more cautious. As a conclusion, the interviewed companies are not so well aware of their transaction costs, but are more interested in unit prices.

5.4 Activities already outsourced and possible to outsource

Company A

Company A has outsourced logistics services like transporting and distribution. The company also uses external sales offices that take care of selling the products.

Following the tradition in Russia, company A decided to establish their own factory in the beginning although now more and more manufacturing activities can be outsourced. If the quality level is high enough and price suitable, it is possible to outsource the whole manufacturing of the company.

Company B

Company B has outsourced some logistics, R&D, and marketing. Firstly, the company has so many customers that it is not possible to possess and maintain own trucks for delivery transportation. Serving all customers by own vehicles would be too expensive. However, the company has some vehicles of their own. Secondly, research and development activities have been every now and then bought from external suppliers. The procedure has been that if some company has offered new products or new ingredients, it has sent a technologist to company B's factory to design and make the named product. Thirdly, in marketing the company outsources practically all the design at the moment. Also external promoters are in use when launching new products.

In the future more marketing, especially branding could be a candidate for outsourcing in company B. The reason for this is that branding is not a core competency of the company and the aim is to buy the outsourced activities from companies whose core competencies it belongs to.

Company C

In company C some production in St. Petersburg and selling and delivering in Moscow are done by other companies. Firstly, one small bakery produces bakery products for company C with a shared recipe. These products are sold under the trademark of company C. Secondly, in the Moscow area there are wholesale firms in use which take care also of the distribution of the products to the resellers, whereas distribution to resellers in the St. Petersburg area is organized by using own vehicles and straight pick ups from the company's warehouse.

From company C's viewpoint the operations in Russia are still in the phase where all efforts are needed in organizing the functions inside the company to a satisfying level. The next step is to think which of the functions should be done by the company itself and whether it would be more profitable to outsource something. The main question is especially whether there are suppliers available who are capable enough to do the named function. No strategically important functions will be outsourced.

Analysis

The outsourcing decision is always based on a make-or-buy question. All the interviewed companies have done some outsourcing so far. The decision to outsource is a strategic choice between executing the necessary activities internally or buying them externally. Table 9 is a summary of the outsourced activities in companies A, B and C.

	Company A	Company B	Company C
Already outsourced activities	* transport * distribution * selling	* logistics * R&D * some marketing	* some production * selling and distribution (in Moscow)
Possible to outsource in the future	* production	* some marketing, like branding	* nothing that is strategically important will be outsourced

Table 9: Outsourced operations in the case companies

When comparing the outsourced activities to the companies' core and supporting activities mentioned in chapter 5.2, it is worth noticing that core activities have been kept in-house and not planned to be outsourced. Like company C defined, nothing that is strategically important will be outsourced. Although company C is reserved about outsourcing in the foreign business environment, it still has a subcontractor producing some products under the trademark of the company. So it can be said that this local subcontractor operates as a contracting manufacturer for company C. As a conclusion, all the companies see it possible to carry out outsourcing also in the future.

Companies B and C also use a so-called gray zone in outsourcing of transportation between 100 percent make and 100 percent buy. Company B has outsourced transportation, but it also has some own vehicles for deliveries. Company C has outsourced distribution in Moscow, but kept transportation in St. Petersburg inside the company. Its customers also pick up the products straight from the warehouse in St. Petersburg. These kinds of solutions are useful for testing and learning, because there is no need to do the final make-or-buy decision.

5.5 Organizing the outsourcing decision

Company A

In company A two product directors (cookies and ginger bread) are in charge of making the decision to buy own manufacturing services or to find a partner outside. The quality director is involved in ensuring the quality of potential partners, and the logistics director to find out if there are enough transport connections between the company and the planned partner.

There is no purchasing director in company A, but purchasing activities are under the logistics department and the logistics director is in charge there. However, the purchasing activities in company A only cover the ingredients, not any services.

Company B

The whole marketing department of company B is involved in decision making when outsourcing for example marketing activities, like design. It is also possible that some other departments, like the sales department would take part in the decision. However, the final decision is made by the general manager.

In company B there are special written standards for outsourcing. The company has an action rule (standard) for outsourcing, which is applied in case of buying all kinds of services or products from outside the company.

Company C

In company C the purchasing department would not be necessarily involved when for example a bakery production is outsourced. The managers responsible for e.g. sales or logistics would sort out the facts of outsourcing of the planned function. After that the case would be discussed in the executive group of the company. Consequently, the outsourcing process would start from the departments, but it depends on the meaning and the scale of the function planned to be outsourced, who would do the final decision.

Analysis

All departments that contribute to the outsourcing decision, or will be affected by it, should be involved in making the decision. In all the interviewed companies there are several actors in advisory role in the outsourcing decisions (table 10). The outsourcing decision is prepared and planned together between the departments. This leads to a situation in which the departments will undertake the outsourcing decision. These kinds of decision-making committees are in a strong position to determine which activities give the competitive edge and whether the critical competence is in-house or with external suppliers.

	Company A	Company B	Company C
Involved in decision making	Product director, quality director, logistics director	The whole marketing department, sales manager, possible other departments as well (in case of marketing issues)	Sales manager, logistics manager, executive group of the company
Final decision maker	Product director	General manager	Depends on the meaning and the scale of the function

Table 10: Organizing the outsourcing decision

Although many actors are involved in the decision making in the interviewed companies, the decision-making committees will not be involved in the final decision. When doing the final decision there is a difference between the companies of Russian origin and the international company operating in Russia. In the interviewed Russian companies the final decision maker is the product director in company A and the general manager in company B. In company C the meaning and the scale of the outsourced function is decisive for who will do the final decision. However, the whole executive group of the company is somehow involved in the decision making.

Purchasing as a function does not have a significant role in outsourcing decisions in the interviewed companies. Purchasing is understood mainly as a function in charge of buying raw materials. So the purchasing function is seen in a very traditional way in the interviewed companies.

5.6 Supplier relationships and the significance of personal relationships

<u>Supplier relationships</u>

<u>Company A</u>

From company A's point of view, lack of trust is a real problem when looking for a suitable supplier. For example in transportation services the company must have 5-10 companies to take care of the distribution. Only one partner would not be possible.

The key factor of a reliable supplier is workable quality management. In Russian markets it is possible to find capable suppliers of both suitable price and quality, but the problem is that the qualities and prices of the offered services are not stable. For example the interviewee of company A mentioned that the easiest way for the suppliers to solve their own problems is to raise the prices regardless of contracts.

Company A has its own program to improve the reliability. The aim is to improve also the quality of suppliers' operations, not only to manage the own company's quality. The method used by company A consists of visits to suppliers' sites and consulting the suppliers on how they can improve quality and how to invest in quality management.

<u>Company B</u>

For company B it is not easy to find reliable suppliers, and because of that the company has several suppliers competing with each other. Choosing only one supplier could be a threatening situation for the company. The company often changes the suppliers to keep up competition between them. If there was only one supplier, the prices would be higher and the service level would be lower.

Trust as such is not a problem for company B. The question is more about low predictability. When signing a new contract with a new supplier the company assumes that the contract will be fulfilled only for example in 50 % of the cases. That is because the supplier may declare something in the contract, but in reality the situation may be completely different.

Company C

For company C it is not easy to find reliable partners. These kinds of business relationships have not become stable in Russia yet. It is important that ownership is under own control to make sure that nobody will take it away. It is also risky to operate as a subcontractor, because continuity is uncertain. Who is ready to invest in machinery and know-how in the situation where nothing is certain? When operating with locals in Russia it has been noticed that people live in a state of short-sightedness. Even one year is too long a period for planning.

Lack of trust is not seen as the most significant problem for company C. The main problem is the instability of the development of the Russian society. How people have the courage to take risks and make investments depends on that development. The decisions and prevailing practices of the authorities are changing arbitrarily back and forth, and this kind of atmosphere does not encourage people to try new things. Rather, everything is kept under own control, and if something negative happens, it is seen important that the investments can be easily turned to cash. For example Finns are ready to invest in Russia, but are the Russians themselves ready to do so?

The ideal situation would be that there were capable long-term partners available in Russia. In that kind of situation there would be no need to use time and energy in searching for suitable suppliers. The problem is that it is not possible to trust the suppliers fully, and it is never certain that the contracts will be followed. At the moment there is not any supplier in Russia that would be capable to operate as a single sourcing partner from the viewpoint of company C.

Significance of personal relationships

Company A

Personal relationships are the key factors in inter-firm relationships. For example the general manager of one of the logistic partners of company A is a co-student in the same MBA program from which the development manager of company A has graduated. This helps them to understand each other. For example it is easy to find a common understanding on the sufficient level of quality, how to improve it, and what the goals are. In Russia there is lack of modern style managers. If in some company there is a manager from a very good school, it is possible to speak a common language with him or her and be sure that the company provides good services.

As a conclusion, the significance of personal relationships originates from the Russian culture and it is possible to move the inter-firm business relationship from a company to another to follow a known manager.

Company B

Personal relationships are important to some extent and at a certain level in business. With personal relationships it is possible to pressure suppliers to do a certain job, but if the supplier cannot do the job due to his business, good personal relationships cannot help.

If the pricing is reasonable, it is possible to follow the known manager to another company because with this manager predictable quality is ensured. In many cases personal relationships are the greatest guarantee that contracts will be fulfilled. It is possible to trust a friend.

Company C

According to common understanding, personal relationships are really significant in the Russian business culture. The respondent has been working as a purchasing manager for only a few months, and has had several meetings with locals. All the meetings have so far been positive experiences, but it is impossible to say what the locals really think about the newcomer.

As a foreign actor in the Russian markets it is important to behave neutrally. This means to avoid provocative language or acting, which could lead to the situation that the company is not anymore a desired customer in the suppliers' eyes. This is a challenge when new people are hired to the company all the time and the way of action is changing. For example how do the locals react to the new method in which all the functions have own people in charge and they can do decisions on the company's behalf? Previously there was a general manager involved in almost all the decisions in company C, but not anymore.

One big issue when operating in Russia is knowledge of the Russian language. If it is possible to communicate with locals in their own language, it makes things a lot easier. The foreigner is more accepted in Russia if he or she can speak Russian. The respondent has started studying the Russian language, but must still use an interpreter in all the challenging cases.

Analysis

All the interviewed companies agreed that they face difficulties in finding suitable outsourcing partners. Companies B and C think that the finding itself is not easy, whereas company A's point of view is that it is possible to find capable suppliers, but unstable quality and pricing are the main problems in supplier relations. None of the companies is ready to organize outsourcing by the strategy of single sourcing. At the moment it is not even seen as an alternative in the Russian markets. The companies have several suppliers competing against each other. Thus there is an opportunity to receive lower unit prices, but dealing with several suppliers requires more transactions, and this increases transaction costs and may also delay schedules.

Lack of trust is seen as a problem in Russia. In today's business, a limited number of suppliers or even one supplier are favored in order to develop a long-term partnership with the suppliers, but in Russia it is difficult to do any long-term planning together with suppliers when there is no guarantee that the contracts between the contracting parties will be followed. Company B has a different approach to this problem: it is not a question of unreliability but of low predictability. So breaches of contracts are more or less appropriate. A summary of the different factors realized in the interviewed companies is presented in table 11.

The number of suppliers needed is the first issue in designing the supplier structure. The second is the way the suppliers are organized. On the basis of the interviews, the companies in Russia seem to use vertical integration and the market option. To be successful in outsourcing, the companies should have both competitive and partnership strategies, because different activities require different sourcing means, but co-operative partnerships (hybrids) are not favored at the moment in the interviewed companies.

	Company A	Company B	Company C
Availability of capable suppliers	possible to find capable suppliers; the prices and qualities of the offered services are not stable	not easy to find reliable suppliers; the company uses several suppliers competing with each other	not easy to find reliable partners
Single vs. multiple sourcing	5-10 companies taking care of distribution, only one partner would be impossible	several suppliers competing with each other, only one could be a threat	no supplier capable of being a single sourcing partner available
Lack of trust	lack of trust is a real problem	trust as such is not a problem; the question is more about low predictability	lack of trust is not the most significant problem, but it is not possible to trust the suppliers fully

Table 11: Supplier relationships

It can be said that the level of vertical integration in the interviewed companies is rather high, especially in company C. This is to say that the companies perform most of the activities by themselves, from producing the raw materials to delivering the final products to the end users. This is understandable, because vertical integration is seen as the best alternative when the level of uncertainty is high, the quality of the suppliers is low, and trust between the partners is lacking. These are the features which according to the interviewed companies belong to the Russian business environment.

In the market option, if a company's requirements cannot be met by a certain supplier, the supplier will be easily changed. Especially company B is active in changing the suppliers, and getting efficiency through fierce competition. Even if it is not easy, it is still possible to find suppliers in the Russian business environment, but the quality of suppliers is low. The outsourced activities of the interviewed companies do not need any specific investments. Thus also using the market option is preferred.

The best solution for a business environment with a high degree of uncertainty and volatility would be the partnership option. Partnering would make it possible for example to focus on the core competencies, coordinating dispersed knowledge, and risk sharing through separate ownership of assets. However, the problem in Russia seems to be the quality of suppliers that should be high in partnering, but at least the interviewed companies realize the quality as low. Trust among the partners would also be mandatory.

Personal relationships are in a significant role in the Russian business. On the basis of the interviews it can be said that these kinds of informal structures are essential in the Russian business. Keeping up these informal institutions also causes transaction costs, and this may hamper the business development.

It was mentioned above that contracts are not always followed, but like company B described, it is possible to trust a friend. The Russian-origined companies A and B saw it possible that the business relationship would follow the personal relationships to a new partner company. Company C as a foreign actor in the Russian markets considered knowledge of the Russian language very necessary. Provocative acting must also be avoided in the foreign business culture from viewpoint of company C. Personality clashes are recognized to be common problems in relationships with the outsourcing partners. This may become critical especially in Russia.

5.7 Outsourcing risks and ranking of risks

The respondents had time to get prepared also for questions about outsourcing risks. The questions “what kinds of risks are there related to outsourcing from your company’s point of view?” and “what is the most significant one of them?” were included in the questionnaire that was sent to gather preliminary data (see appendix 1). The ranking of risk in the second subchapter is based on risk classification which was not given in advance (see appendix 2). Outsourcing of a broken process is discussed in the third subchapter.

Outsourcing risks

Company A:

Stable quality is seen as a very significant challenge in company A. When having own manufacturing it is possible to control the standards of quality more easily than with an external provider, though the ISO9000 quality standard and other standards for food industry quality are in use in the manufacturing.

A too high price without any reason can also be a possible risk when outsourcing. When starting the relationship, the price can be reasonable, but when the supplier faces some unexpected challenges, the easiest way to solve the problem is to raise the price. The company invests in building the relationships, but suddenly it must find another provider due to remarkable changes in pricing.

Company B:

Quality risk is the main risk for company B, especially the quality level of a new supplier. Consequently, when having a new supplier, strong control is needed. The other question is whether the supplier is able to fulfill the contract in a given time. Of these two risks, the quality risk is more significant.

Company C:

From company C’s viewpoint, challenge number one is how to ensure supply. That is because everything is founded on a workable supply. The second challenge is the control over quality. How to ensure that the defined quality requirements will be fulfilled? For example when talking about concrete raw materials, control over quality in the whole chain is a problem. Raw materials are purchased from many different suppliers, and there is no stable system in ensuring the quality.

The third challenge is what the expenses will be when the function is no longer under own control. Understanding the total cost is not a strength of Russians, but people are more interested in unit prices. When outsourcing, it is possible to face extraordinary expenses like customs duties, changes in taxation and other expenses originating from the authorities.

The most significant risk of the above three is how to ensure supply. It is possible to control this by giving enough information of the requirements, amounts and quality criteria. Also signing a contract which puts both sides under an obligation is important, though it is not certain that the contracts are followed.

Ranking of risk

The respondents were asked to rank six different outsourcing risks in the scale from 1 (not significant at all) to 5 (very significant). The list of the risks was shown to the interviewees for the first time during the interviews, it was not sent as preliminary data. According to the risk ranking, the most significant risk was again the quality risk (as in table 13) and the least significant risk was the hold-up risk. Although companies A and C mentioned the cost risk as remarkable in the previous open risk question, in risk ranking the meaning of underestimation of total cost was not seen to be as significant as would have been expected.

	A	B	C
Quality risk:	5	5	4
Spill over risk:	3/1	4	4
Inefficiency risk:	4	5	2
Timing risk:	3	3	4
Underestimation of total costs:	4	1	3
Hold up risk:	1	2	3

Table 12: Risk ranking among interviewed companies (1: not significant at all, 5: very significant)

In addition to risk ranking in table 12 company B commented separately on the underestimation of total costs and the timing risk. Firstly, the cost of outsourcing can not be more than estimated, because price rise is not included in the contract. Secondly, company B wants to have short contracts, normally one-time services, but the suppliers assume to have longer collaboration. Also the hold-up risk was covered from the marketing function's point of view. Company A for its part understood that the spill-over risk is function-related; 3 was given to manufacturing, and in case of logistics the estimation was 1.

Analysis

All the interviewed companies were aware of the risk of loosing control of quality when outsourcing (table 13). It can be said that this risk was seen as the most significant. The companies cannot be sure whether the suppliers are capable to offer activities which satisfy the company's own and the end customers' requirements. The strategy of multiple sourcing of companies A and B is a common tool in reducing the quality risk.

Company A	Company B	Company C
Quality risk Price risk	Quality risk	Ensurance of supply Quality control Total cost of outsourcing

Table 13: Most significant outsourcing risks

Company C's main concern was the ensurance of supply, but both companies A and C were also aware of the risk of increasing costs. Company A was worried about the possibility that the suppliers solve their own problems by raising the prices regardless of the contracts, whereas company C was worried about the possibility of different kinds of extraordinary expenses, like expenses originating from authorities. None of the companies was concerned with the effort and costs needed in coordination of the outsourced activities. According to the theory, cost management is more challenging in networks than in a single company.

Company B's attitude to the timing risk was interesting. Normally it is understood that companies aim at long-term collaboration, and the suppliers may behave opportunistically and operate with a short-term focus. Company B, however, wants to have short contracts which are not in the interest of its suppliers. This is seen as a timing risk. Also, company B saw underestimation of the total cost as not significant at all. From company B's viewpoint the only thing that matters is the price, and if the rising of price is not included in the contract, they do not pay it. None of the transaction costs, like costs related to supplier searching, contract follow-up and reclamations are perceived significant at all for company B.

Company A saw a dependency or lock-in on a certain supplier or technology not significant at all. The hold-up risk can be reduced by maintaining competition between the suppliers, and company A uses the strategy of multiple sourcing. This is to say that company A has succeeded in executing its strategy in this respect. Company A also understood the fact that different risks interact with different functions in various ways.

Outsourcing a broken process

When asked about broken processes and outsourcing of them, the interviewed companies had different kinds of approaches. The approaches are summarized in table 14. Companies B and C perceived outsourcing as a possible tool in fixing the process. From company A's point of view, the first step was to improve the broken process inside, and outsource after fixing, when the process is under control of the company.

Company B's reason for outsourcing the broken process is that the process must be outsourced, because the company itself can not handle the process. Company C saw that outsourcing might be the problem-solving method if there really is a capable supplier available. In this kind of situation, outsourcing might be the way to improve the company's internal effectiveness.

Company A	Company B	Company C
must be fixed before outsourcing	must outsource if company can not handle it	outsourcing might be the solution

Table 14: Broken process outsourcing

Company A has understood that there will not be any improvement simply by handling problems over to suppliers. If the interviewed companies outsource the activities in which they have lost control of the processes, they will most likely face problems. The first step is to get the matter under control, as company A answered.

5.8 Risk management

Company A

Company A does not perceive itself as professional in risk management. Naturally all the top managers are aware that they must identify risks, and estimate the consequences and probabilities. But for example no mathematical theories are in use. However, it is mandatory to plan continuously what the necessary actions are if the risks come true.

Risk management is mandatory when doing something new. The company must use simple risk management tools in project management, when for example the company is developing a new product and finding a new supplier. Risk management is also needed in operational activities, but in a smaller scale. Risk management activities are mainly carried out with external suppliers. Company A's viewpoint is that external factors are all the time more risky than factors inside the company.

Company B

In company B there is no planned risk management in use related to external suppliers. However, multiple sourcing is one way to minimize risks. Especially when there is an important project in question, company B does not give it to one supplier, but to two or three in order to secure the operations.

Company C

All the insurances and financial risk management are taken care of at the group level in company C. In addition, the company aims for multiple sourcing when trying to minimize availability risk and cost risk. Using only one supplier is seen as an especially risky situation. This balance of terror is in use not only in Russia but in all the countries where company C runs business. At the moment there is no supplier in Russia which would be capable to operate as a single sourcing partner, according to the interviewee in company C.

Ensuring the quality is a big issue for company C, and there is still a lot to do with it. International retail sale chains follow all the time how company C takes care of the quality issues of subcontracted work. Luckily no big quality failures have happened so far. There are a lot of different kinds of certificates in use, but that is not a guarantee of stable quality of products and services in Russia. It is a challenging duty to ensure the quality matters with all the suppliers. To make sure that the suppliers understand the requisite quality level and how to produce the services and products with sufficient quality, is one of the main missions of company C.

Impacts of the risks

When asked which of the risks illustrated in table 12 would have catastrophic impacts for the company, all the respondents were unanimous. The most dangerous risk when becoming materialized is the quality risk. It was mentioned that it is possible to loose a lot of money because of the tight contracts with resellers. With quality failures the company will also loose its reputation, and re-convincing customers is very difficult. In the grocery business the actors cannot afford to risk that the products include something that does not belong there. So it is vital to become convinced about the quality of the supplier as well. For example if some agency will make a market research which does not describe the real market situation and the buying company will follow that off-beam research, it would be a catastrophe.

The viewpoints on the most common risks mentioned in table 12 differed in the companies. Company A found the timing risk and company B underestimation of the total cost as the most common ones. However, company B did not see underestimation of the cost as a very dangerous risk, because this kind of risk is fully under the control of the company. From company C's point of view, the most common was the hold-up risk, because changing the supplier is not easy.

Analysis

None of the interviewed companies perceived themselves especially skilful in risk management. In company B there is no planned risk management in use, and Company C has risk management actions only at the group level. Risks in networks are often very complex and remarkably difficult to identify. Only in company A the identification is somehow organized. However, none of the different techniques for risk identification, like brainstorming and workshops were mentioned in the interviews.

Also risk assessment was organized somehow in company A. The most common (very probable) risks and the most notable risks (catastrophic consequences and losses) that may lead to discontinuity of business from the interviewed companies' viewpoints are summarized in table 15.

	Company A	Company B	Company C
Most common	Timing risk	Total cost	Hold-up risk
Catastrophic impacts	Quality risk	Quality risk	Quality risk

Table 15: The most common risk and the risk with catastrophic impacts

The quality risk with catastrophic impacts has also other than financial consequences. Loosing the reputation in the eyes of the customers causes financial losses in the long run.

Company A has also planned how to react if the risks come true. Company C has many certificates in use, but in Russia they are not workable methods in avoiding risks. As mentioned above all the companies prefer the strategy of multiple sourcing. Companies B and C named multiple sourcing as a tool to minimize risks. This reduces both the probability and the impact of risk. Company C is also training the suppliers to produce the services and products with sufficient quality. These actions mean that the companies try to reduce the risks but also accept that risks exist.

The risk monitoring should be a continuous process. The companies should monitor organized customer needs, technology, partner strategies and competitors, but it can be said that in risk monitoring there is still a lot to do in the interviewed companies.

6 CONCLUSIONS

When comparing the theory described in the theory part of this study with the outsourcing practices in the interviewed companies, it may be noticed that both similarities and discrepancies exist. This comparison is made in the beginning of this chapter. After the comparison, transaction cost analysis is discussed separately, and then four conclusions are made. With the conclusions it is possible to understand how the objective of this study was reached, i.e. how this study clarifies the outsourcing decision making in companies operating in Russia. Further research needs are mentioned in the end of this chapter.

Similarities between the theory and the outsourcing practices in the interviewed companies

Even though the division of activities in the interviewed companies to core activities and supporting activities differ, all the respondents see the importance of keeping their core activities in-house. These kinds of activities have not been outsourced so far and are not planned to be outsourced in the future. This is also in accordance with the theory in the literature. The core activities should not be outsourced, because they provide long-term competitive advantage for business enterprises.

Also the reasons to outsource and the outsourcing benefits in the interviewed companies follow essentially the guidelines given in the literature. When companies specialize in their core activities by outsourcing non-core activities, flexibility and financial benefits are gained. The availability of skilful labor was also mentioned and it is possible to be seen also as access to certain intellectual property or technology, which the company would not otherwise have access to. This is also mentioned in the literature as an important criterion when making outsourcing decisions. The so called gray zone of outsourcing is also in use. This is to say that companies are testing and learning outsourcing without doing complete outsourcing.

The outsourcing decisions in the interviewed companies are prepared by so called outsourcing committees consisting of representatives from different departments. According to the literature these kinds of committees are needed and are in a strong position to determine which of the functions give competitive edge to the companies, and whether critical competence lies in-house or with external suppliers.

Supplier relationships in the interviewed companies are organized on the basis of multiple sourcing strategies to ensure supply at a reasonable price and quality. This is also mentioned in the literature: the traditional attributes of price, quality, and delivery are emphasized in the case of multiple sourcing. The interviewed companies perceive the suppliers as unreliable (the quality of the suppliers is low), so also according to the theory it is understandable to choose either the market option or vertical integration as the governance structure. Partnering as the governance structure presumes that the quality of the suppliers is high. None of interviewed companies has a supplier which would be capable to be a single sourcing partner.

The risk of loosing control of quality is according to the literature a major concern in outsourcing. The interviewed companies are all aware of the quality risk. Underestimation of the total cost of outsourcing is a known risk in the literature, and was mentioned as a concern in the interviewed companies as well.

Discrepancies between the theory and outsourcing practices in the interviewed companies

In the literature the make-or-buy process is divided into three phases: preparation, data collection, and analysis and results. Although decision-making committees could be identified, none of the respondents mentioned any planned process behind the outsourcing decision. It can be concluded that the companies operating in Russia have not much experience in outsourcing. This is to say that there is need for outsourcing professionals like consultants in Russia.

According to the theory, different activities would need different sourcing means. This is to say that companies would need both competitive and partnership strategies in outsourcing. In the interviewed companies there were mainly competitive strategies in use. Only the international company had one contracting manufacturer as a partner.

About transaction cost analysis

There are always transaction costs when making an economic exchange. When the transaction costs of using markets are higher than the managing costs of using own recourses, a transaction should be organized within the company and vice versa. Only the foreign company operating in Russia mentioned that it would be the ideal situation if there were capable long-term partners available in Russia, because in that kind of a situation there would be no continuous need to use time and energy in searching for suitable suppliers. Nevertheless, it can be said that the significance of transaction costs is not fully understood in any of the interviewed companies. Firstly, none of the respondents mentioned improved cost control as a financial benefit of outsourcing. According to the literature, this benefit comes true when suppliers charge for each activity, as opposed to the in-house activities which are thought to be free. Secondly, when companies use the strategy of multiple sourcing by dealing with several suppliers, this naturally requires more transactions compared to the single sourcing strategy. None of the respondents mentioned costs related to keeping up the supplier relationships. The same phenomenon is found in the significance of informal structures, i.e. personal relationships. All the respondents saw these kinds of relationships essential in the Russian business life, but none of them identified the costs spent for these kinds of informal institutions. Thirdly, none of the companies was concerned with the effort and costs needed in coordination of the outsourced activities. As a good example is the company that considers underestimation of total cost not significant at all, because if the too high price of the outsourced activity is not included in the contract, the problem is solved by not paying the invoice. None of the transaction costs, like costs related to supplier searching, contract follow-up and reclamations are perceived significant at all in that company.

According to the literature, the level of transaction costs depends on the external and internal uncertainty, the frequency of the transactions, and the level of transaction-specific investments.

Uncertainty

It can be concluded on the basis of the interviews that environmental uncertainty and a small number of potential trading partners are typical features of the Russian markets. These are factors that cannot be influenced by the companies. They can be seen as the main external transaction cost factors in Russia. According to the interviewees, also behavioral uncertainty seems to be high in Russia. This is to say that the situations involving transactions are such that the contracting parties cannot be sure if the other party has fulfilled its obligation or not. If the level of uncertainty is high, the likelihood of vertical integration increases. This seems to be the prevailing practice also in the interviewed companies.

Monitoring costs and coordinating costs are closely related to uncertainties. Monitoring the partners' capabilities to produce the suitable quality seems to be difficult in the interviewed companies. Also strict coordination of the activities with possible external suppliers would be mandatory.

Frequency of transactions

There seems to be no difference between occasional and recurrent transactions for the interviewed companies. The likelihood that all transactions between companies will create contractual problems seems to be high, and this naturally involves extra costs. Business contacts normally decrease opportunistic behavior, but according to the interviewees, breaches of contracts are common in Russia.

Specificity

If particular skills or services have high specificity, then these activities must be kept inside the company. If activities that require transaction-specific investments are outsourced, the company becomes more locked-in to its supplier, and the transaction costs become higher. According to the interviews, lock-in is not experienced significant at all in the interviewed companies. This is due to the fact that none of the interviewed companies has outsourced any activities with high specificity.

Objects with low specificity can be outsourced and the economies of scale can be exploited by using external outsourcing partners, but as only a few suppliers are available for the interviewed companies in the Russian markets, gaining large scale effects seems to be difficult.

Conclusion 1: The purchasing function has no role in the interviewed companies when making the outsourcing decision

According to the interviews, decision-making committees are favored when making the outsourcing decision. So the decision is a result of cooperation of different actors in the companies. Even if there are different departments involved in the outsourcing decision making, the purchasing function has no role in it. Purchasing as a function in the interviewed companies is mainly in charge of purchasing raw materials, it is not used in managing external resources.

The difference between the interviewed local companies in Russia and the foreign operator is in the final decision maker. In the Russian-origined companies the final decision maker is either the general manager or the product manager. In the international company the decision maker depends on the meaning and scale of the outsourced function.

Conclusion 2: The difficulty of finding suitable suppliers seems to be a main constraint on outsourcing in Russia

According to the interviews, the companies operating in Russia are willing to outsource their non-core activities, and they understand several benefits originating from outsourcing. Financial benefits and flexibility are the main stimulants for outsourcing. However, from the viewpoint of the respondents, it is difficult to find a suitable supplier in the Russian markets. If there are suppliers available, they may often not be capable of operating as outsourcing partners. The problems faced are unstable quality and arbitrary pricing.

The low reliability of possible suppliers is also recognized as a significant factor on the basis of the interviews. It is difficult to do long-term planning together with the suppliers when there is no guarantee that the contracts between the contracting parties will be followed. Breaches of contracts are accepted as an existing phenomenon, and the companies must take it into consideration in all decision making.

The so called gray zone between 100 percent make and 100 percent buy is also in use in some functions. This kind of solution is useful for testing and learning to outsource. This is understandable when outsourcing is experienced as a new and foreign way of action.

On the basis of the interviews, it may be concluded that the local companies are more courageous in their attitude towards outsourcing than the international operator in Russia, despite the fact that the international company was the only one among the interviewed companies that used one Russian supplier as a contracting manufacturer.

Conclusion 3: Quality risk is the most significant risk related to outsourcing in Russia according to the interviewees

Besides benefits, the interviewed companies are also aware of risks related to outsourcing in Russia. All the interviewed companies are most worried about loosing the control of quality when outsourcing. Whether the suppliers are capable to offer activities which satisfy the company's own and the end customers' requirements seems to be a big concern in the interviewed companies. The companies also agree that the realization of quality risk would have catastrophic impacts. Especially in the food industry, where all the interviewed companies operate, loosing the reputation in the eyes of Russian consumers due to quality failures would have fatal consequences.

Of other risks, also underestimation of the total cost of outsourcing is a concern in the companies. Costs are expected to originate either from the outsourcing partner (breaking the contract by raising prices) or from authorities (extraordinary expenses).

On the basis of the interview, when the list of different outsourcing risks was given to the respondents, quality risk was still ranked as the most significant. In addition to the risk of underestimation of the total cost of outsourcing, the next most significant ones were the risk of leakage of sensitive information to competitors or other unwanted actors and the risk of choosing an inefficient partner.

Conclusion 4: Organized risk management does not exist in the interviewed companies

On the basis of the interviews, the companies have no organized risk management with their suppliers. When analyzing the interviews as a whole, it can be said that companies either accept the existence of the risks in the supplier relationships or try to reduce the risks. All the interviewed companies have prepared themselves for the realization of outsourcing risks mainly by keeping the functions under own control inside the company.

Organizing supplier relationships on the basis of multiple sourcing can be seen as a risk management tool for reducing risks related to outsourcing. This strategy is a common tool in reducing the quality risk, which is the most significant risk among the interviewed companies. The strategy of multiple sourcing is one way of being updated of the market situation as well, and this way also the inefficiency risk can be prevented.

Normally the leakage of sensitive information can be prevented by developing clear contracts between the parties. Since breaches of contracts are very common in Russia, as mentioned above, this tool is not useful.

Topics for further research

According to the present study, quality risk is perceived as the most critical outsourcing risk. It is understandable that especially in the grocery business, quality failures become the most significant concerns. It would be interesting to find out what the situation is in other industries in Russia. The questionnaire used in this study could be sent to companies operating for example in the automotive or metal industry.

According to the findings of this research, the companies in Russia have positive thoughts about outsourcing. This willingness of Russian companies to outsource is contrary to common understanding for example in Finland. It can be concluded that there is a big demand for reliable and capable suppliers in Russia. Outsourcing could also be seen as a possible solution to Russia's increasing labor shortage. Hence it would be interesting to study the Russian companies' demand for capable suppliers and foreign companies' interest to operate in Russia.

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OTHER SOURCES OF INFORMATION:

Interview in company A: Outsourcing / Ahola 10.4.2008
Interview in company B: Outsourcing / Ahola 11.4.2008
Interview in company C: Outsourcing / Ahola 21.4.2008

Dear Madam / Sir,

I am in the final stages of my master's studies (Econ.) at Lappeenranta University of Technology. My master's thesis is a part of a larger research project of risk management in supply networks. The project is conducted in co-operation with St Petersburg State University Graduate School of Management (Russia), the European Business School (Germany), and the School of Business and NORDI at Lappeenranta University of Technology (Finland). NORDI (The Northern Dimension Research Centre) is a research institute run by Lappeenranta University of Technology. NORDI coordinates research into Russia and Eastern and Central Europe.

This questionnaire is a part of my master's thesis study. The study deals with the key factors in outsourcing from the viewpoint of an original equipment manufacturer (OEM) operating in Russia. The focus is directed to the risks resulting from the outsourcing decision. Also the risk management process will be studied.

The objective of the study is to understand the special characteristics of outsourcing in the Russian business environment. Your company has a strong experience in the Russian business environment and therefore your contribution to this questionnaire is highly appreciated. On the basis of your answers, it is possible to pose more detailed questions.

Sincerely yours, Iivari Ahola

<u>BASIC INFORMATION</u>

Name of the company:

Line of business:

Operating in Russia since:

Number of employees (total / in Russia):

Annual revenue (total / in Russia):

Name of respondent:

Position in the company:

INTERVIEW QUESTIONS

1. Operations of the company (in Russia)
    - **Describe shortly the operations of your company.**
    - **What is the core activity (core competency) of your company? If more than one, list all.**
    - **What kind of core-distinct (supporting) activities does your company carry out?**
2. Make or buy
    - **Are there any activities outsourced (in Russia)? If affirmative, which? Why were they decided to be outsourced?**
    - **If there are none, why?**
    - **Which activities would it be possible to outsource (still)?**
    - **How is the outsourcing decision organized? Who are involved? Who is in charge?**
    - **How easy was it (will it be) to find a reliable supplier?**
    - **Is the lack of trust a significant problem?**
    - **How to improve reliability?**
    - **What kinds of benefits are / can be achieved by outsourcing?**
    - **What makes Russia especially challenging as a business environment? Or is Russia especially challenging?**
3. Outsourcing risks
    - **What kinds of risks are there related to outsourcing (in Russia) from your company's point of view? List all.**
    - **What is the most significant of them? How to manage this risk?**
4. Risk management
    - **How is risk management organized in your company?**
    - **How has outsourcing effected (would effect) risk management in your company?**

Outsourcing risks / additional questions

- **How does your company experience the following outsourcing risks (5: very significant – 1: not significant at all)? How to manage them?**
  - **Underestimation of total costs of outsourcing?**

    1 2 3 4 5

  - **Spill-over risk (leakage of sensitive data and information)?**

    1 2 3 4 5

  - **Inefficiency risk (choosing an inefficient outsourcing partner)?**

    1 2 3 4 5

  - **Hold-up risk (a dependency or lock-in on a certain supplier or technology)**

    1 2 3 4 5

  - **Quality risk (the supplier is not capable in the long term to offer activities which satisfy your company's and the end customers' requirements)?**

    1 2 3 4 5

  - **Timing risk (the supplier may operate on a fast-profit-seeking and short-term focus when your company aims at long-term strategic collaboration)?**

    1 2 3 4 5

- How to outsource an activity where your company has lost control of the process?