

# Chapter 9

## The Impact of Outsourcing on Performance and Competitive Priorities among Malaysian SMEs

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### ABSTRACT

*The objective of this research is to examine the influence of outsourcing on financial performance and competitive priorities of Malaysian SMEs. A data sample of 100 SMEs was analyzed to examine these relationships. The analysis was conducted via Partial Least Squares. Based on the findings, while outsourcing has significant influence of SMEs financial performance in Malaysian context, outsourcing activities do not have an impact on competitive priorities. Outsourcing approach emphasizing on the establishment of core competitive advantage, allows Malaysian SMEs to get the numerous benefits such as overall sales growth, market share, net profit, return on investment, and financial liquidity.*

### INTRODUCTION

Small and medium-sized enterprises (SMEs) are predicted to progress tremendously although they have to face continuous challenges to survive in a turbulent market (Kumari et al. 2015). From the context of Malaysia, SMEs are expected to continue their imperative role in pushing Malaysia to become a developed and inclusive nation. As reported in a recent report in 2015, Malaysian SMEs have contributed 98% of businesses and 59% of employment to the nation's economy. Given that more than 99% of businesses in

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Malaysia are SMEs, it is crucial to retain a proper economic growth, in the means of employing a large portion of Malaysia's labour force of 12 million people (EPU, 2015). Consistent with this circumstance, the Malaysian government agreed that SME is a fundamental sector which acts as a catalyst in spurring investments and transforming Malaysia into a developed economy by 2020. Nevertheless, SMEs are not achieving superior performance and this is evidenced by the SMEs' contribution to GDP at only 32% (SMEs Master Plan 2010-2020). SMEs often face difficulties in achieving economies of scale and scope as larger companies do (Raman & Ahmad, 2013). Moreover, SMEs have inadequate resources and a limited market share, mainly within the national market. Because of these limitations encountered by the SMEs, they have to craft and execute strategies relevant to the new episode of severe competition in order to sustain in the market place. Progressively, many SME entrepreneurs are embarking on outsourcing as a new mechanism in which, SMEs outsource activities that are either not important to their core or simply too expensive to be performed in-house (Isaksson & Lantz, 2015).

Since the industrial revolution, the outsourcing phenomenon has been around (Patil et al., 2015). The trend towards outsourcing has become one of the strongest and most sustained developments over the last ten years (Fill & Visser, 2000; Solakivi et al; 2011). Operating in the given the dynamic and hostile business environment, organisations are being exposed to many challenges that posed adverse impacts on the survival and development of the businesses. As such, organisations have sought to restructure, build flexibility and reduce cost by contracting out functions and activities traditionally performed in-house. This scenario also has given impact to the development and growth of SMEs. In fact, from the context of Malaysia, SMEs have been at the front line of the economic expansion and considered as the powerhouse of the country's economy which, if properly nurture and groom, could leapfrog Malaysia from a developing to a developed nation (Abdul-Halim, et al. 2012). Moreover, the era of globalisation has required SME entrepreneurs to face massive changes regarding how they operate their businesses. In line with this, it has marked the end of the usual way of doing business, mandating new approaches into the forms of strategies that entrepreneurs need to adopt in order to ensure business sustainability (Shane & Venkataraman, 2000; Raman & Ahmad, 2013).

One of the many challenges is to get access to reasonably cost-effective financing and mostly venture capitalists do not see the potential of SMEs, as many SMEs do not have the track record that a stable or large organisation does (Brewer et al. 2013). Apart from that, many SMEs do not have skilled manpower because they could not afford to pay high salaries to get the skilled employees. SMEs cannot be competitive, innovative and creative without the skilled employees. On top of that, SMEs also experience lack of technological capability in which they do not have sufficient financing to acquire technology that may be actually be very pertinent for them to be competitive and have a strong market position (Butler & Callahan, 2014). It can be surmised from past researchers that the main obstacles surround SMEs are lack of financial and technical resources, insufficient relevant market information and government support and inability to deal with international affairs to execute the business successfully. Also, the new era of customers are looking for quality products at lower prices and superb delivery (Kumari et al. 2015; Unal & Dontu, 2014; Edvardsson, 2011).

The challenges above faced by the SMEs have encouraged entrepreneurs to establish and execute strategies relevant to the new episode of intense competition in order to survive in the market place. Increasingly, many SME entrepreneurs are turning to outsourcing as a new management strategy (Yang, et al. 2016). Previously, SMEs often purchase only raw materials from outside vendors and perform rest of the manufacturing activities in-house. Thus, in order to compete in current market scenario, SMEs have to outsource some of their business activities. As such, if an organisation decides to perform activities

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