

Managing Outsourcing Strategy in a Complex Project: A Case Study of a complex of Four Residential Towers Project

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Executive Summary

Outsourcing became a usual practice for organizations which seek rapid business transformation, neglecting the consequences in long term duration. The case study of this paper is a complex project, where decisions to outsource irrationally lead to increase cost, potential risks and conflicts between outsourcing partners significantly, which lead to low project performance and coordination difficulties.

The purpose of this study is to explore the key factors to effectively managing the coordination mechanisms between more than hundred and eighty external service providers and a main contractor of a complex of four residential towers project “Complex1”, in addition, to focus on the significance of decision-making process prior to outsource.

This paper develops an approach built on sharing information, building trust and commitment, and managing interdependencies, it examines the coordination mechanisms in “Complex1” and the success or failure of the outsourcing decision via conducting a questionnaire-based survey among the outsourcing partners.

Moreover, the study argues that based on “Resource Based View Theory”, organizations may consider implementing a decision-making process to choose outsourcing as a procurement strategy for their projects, rather than deciding irrationally based on short-term benefits. Hence, it proposes an approach for the decision-making process of outsourcing developed from the literature by emphasizing on make-or-buy analysis.

The framework attempts to guide decision makers to gain the competitive advantage of outsourcing, moreover, to guide project managers to avoid potential risks and achieve the required mutual goals in quality, innovation and customer satisfaction.

Introduction

(Grover *et al.*, 1994) Defined Outsourcing as requesting a service from external service provider. (Lankford & Parsa, 2006) Also defined Outsourcing as “The procurement of services from sources that are outside of the organization which generally involves the relocation of operational control to the external service provider”. In the other hand, (Weil & Dalton, 1992) defined complex projects as vulnerable to project performance issues, which projects tend to be “complex” due to multiple changes in design stages, procurement, testing and construction and other sequence activities involved.

Moreover, it is changing in customer requirements and project performance in terms of schedule, time and cost, in addition of the delays in discovering rework.

Outsourcing, which is called in the literature “Contracting-Out”, “Strategic Partnering”, or “External Service Provider”, nowadays became a fashionable strategy for organizations which seek a rapid business transformation in short-term duration (Linder *et al.*, 2002).

(Embleton & Wright, 1998) Stated that outsourcing market is increasing every year, showing that in 1992 58 % of the organizations reported outsourcing compared to 86% in 1995 in USA. (Hui *et al.*, 2008) Agreed, that Outsourcing became a usual organizational practice with very little research of the impacts of managing this strategy on outsourcing partners in complex projects.

However, the consequences of choosing outsourcing irrationally as a procurement strategy can significantly impact the effective coordination management, that is; in complex projects uncertainty increases and forecasting tend to be not easy due to high interdependencies between activities as a result coordination and controlling of suppliers tend to be more complex (Hui *et al.*, 2008).

Problem Definition

The case study of this report is a complex of four residential towers project in UAE which is called “Complex1” worth 400M AED (108.9M US\$) , it includes 2000 units, three basement levels, ground floor and two parking levels, the area of the project is approximately 180,000 m².

The contractor is a subsidiary company from a well-known cooperation which has more than 25,000 employees worldwide with more than 2.353 Billion revenues in the construction field. According to the main contractor’s project manager, the number of suppliers contracts exceeded 180 contracts, they chose outsourcing as a procurement strategy due to the project’s low revenue, which was estimated 3% of the total amount at the time, hence, the main reason of this strategy of procurement according to the project manager, was to decrease costs of operations, share risks with suppliers, and concentrate on the progress.

However, the project manager claimed that due to this large number of suppliers, they faced a lot of issues and conflicts in sequence of work, quality, payments, subcontractors slow work and inefficiency, as a result the project is now 750 days

delayed from its original handing over date and loses of the main contractor reached 100M AED (27.23M US\$). (The main contractor Project Manager)

This paper is going to propose a model to effectively managing the coordination and relationships between the suppliers and the contractor. Moreover, it is going to emphasize on the significance of decision-making process prior to decide outsourcing as a procurement strategy using an appropriate model built from the literature, then “Complex1” management capability is going to be examined in terms of coordination mechanisms, trust and information sharing between suppliers and the contractor.

Literature review

Schedule, Cost and quality, the three components which motivate organizations to outsource (Simmonds & Gibson, 2008), however (Auzair *et al.*, 2013); (HRMID, 2007); (Zhang, 2006); (Willcocks, 2012) Argued that outsourcing might impact managing those variables significantly.

Some organizations take outsourcing as a style to gain profit, cost saving, greater productivity, or to concentrate on core business...etc. (Lankford & Parsa, 2006). There are many advantages and disadvantages of outsourcing in literature and practice, see Table 1 Advantages and disadvantages of Outsourcing. However, this report will concentrate on key opportunities and challenges of two key management variables which impact the success of this procurement strategy; a decision-making process and an effective coordination management in terms of managing interdependencies, sharing information and trust, that should be implemented between suppliers and contractors.

<i>Outsourcing Opportunities</i>	<i>Challenges of Outsourcing</i>
Cost Saving	Controlling issues
Time Saving	Loss of flexibility
Transferring hidden costs to suppliers	Reversibility
Concentrating on core business	Quality of service
Greater productivity	Coordination difficulties

Table 1 Advantages and disadvantages of Outsourcing

Outsourcing opportunities

Many researches focused on the opportunities to engaging in outsourcing, (Kavc̃ic̃ & Tavc̃ar, 2008) found in the initial stage of their research which based on quantitative and qualitative data collection that outsourcing can increase the organizational financial gains in the short-term period. (Hui *et al.*, 2008) Discussed that cost saving through

outsourcing can be achieved as a result of numerous studies on transaction cost economics, they also stated that it is cheaper for organizations to contract out resources or human capital that the organization need. (Linder *et al.* , 2002; Linder, 2006; Lankford & Parsa, 2006; Embleton & Wright, 1998) Agreed that most companies consider outsourcing as a strategy to cut cost, entering new talented abalities and gaining better financial flexibility.

Outsourcing Management Challenges

Supply Chain Coordination and controlling

Coordination and controlling efforts as a result can be the major challenge that organizations may face (Magid, 2007). Coordination is defined as managing interdependencies associated with activities to analyze and redesign organization (Simatupang *et al.*, 2004). (Kanda & Deshmukh, 2007) Defined supply chain coordination as managing dependent activities between several supply chain partners and efforts of all supply chain participants to achieve mutual goals; they defined the common goals in quality, innovation, and customer satisfaction.

Researchers have developed number of modes for coordination with suppliers such as; Interdependence, information sharing, logistics synchronization, incentive alignment, collective learning, and decision synchronization...etc.

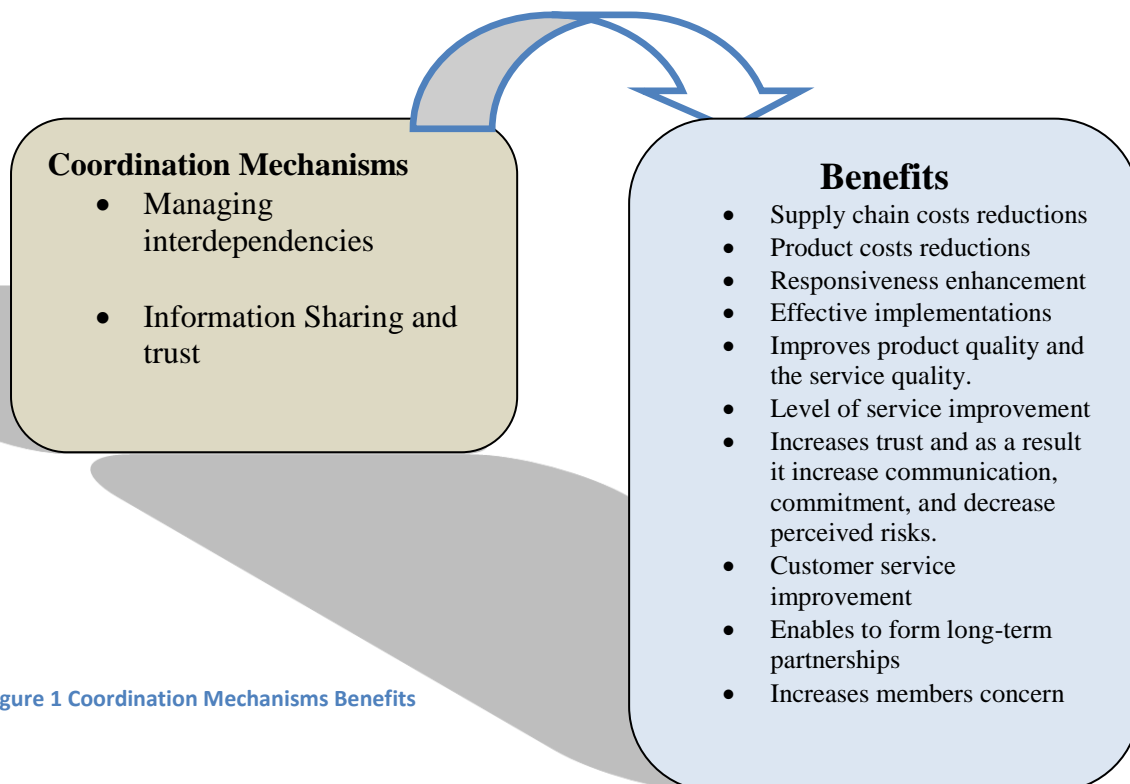


Figure 1 Coordination Mechanisms Benefits

Contractor/Supplier Conflict Management

Conflicts between suppliers and contractors happen when certain actions prevent one or both parties to achieve their common goals, disagreement in performance, incentives or measures, and differences in perceptions (Simatupang *et al.*, 2004). To avoid conflicts occurrence, parties are concerned in sharing information and confronting with each other to solve problems (Victor & Blackburn, 1987).

(Acharya & Im, 2006) Defined Conflict as a major difference between two or more parties in interests, ideas, or beliefs, they described conflicts as a result of transformed potential risks which is called “Critical Conflicting factors”, however, conflicting factors that may be involved in procurement as their claim are; Not clear scope of work, excessive amount of change orders and negotiation, quality, payments, contractor slow work, and subcontractor inefficiency.

If those potential risks were not managed clearly nor resolved, they may transfer to conflicts and as a result dispute may occur which require resolution process by third party intervention, (Acharya & Im, 2006) recommended resolution model to reduce conflicts which include four major processes :

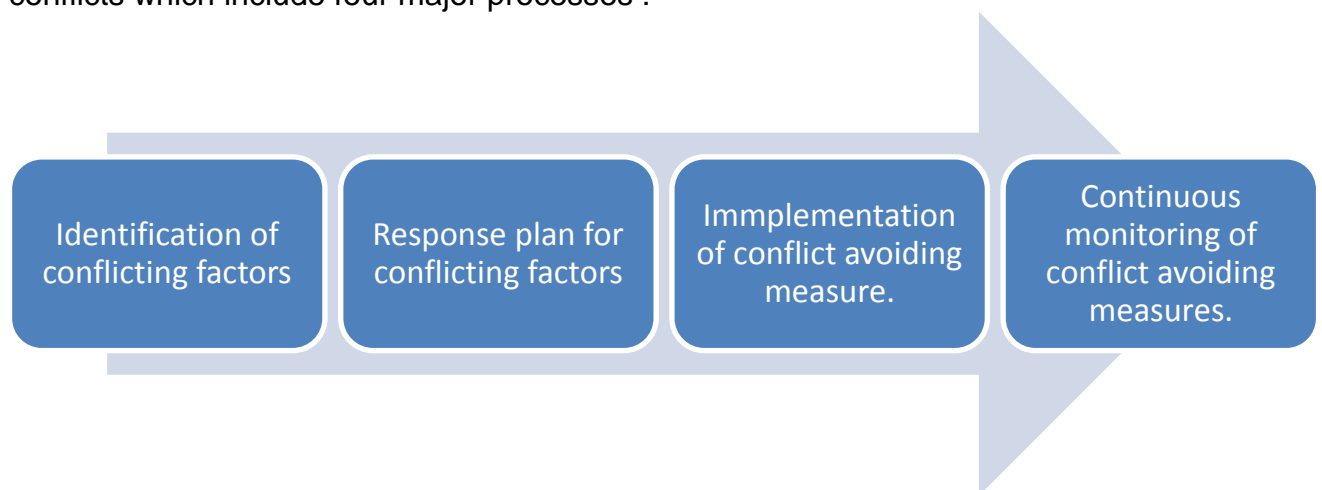


Figure 2 (Acharya & Im, 2006) Conflict resolution model

Decision making

The decision whether to outsource or no faced all organizations, with a limited number of resources, some organizations cannot afford to use in-house resources which increases the possibilities to take outsourcing as a procurement strategy for their projects, however, to retrieve the best results of such decision, organizations need to take into account the necessarily processes and measures to end up with the right decision that satisfies the organization strategic direction and core business.

Resource Based View Theory

Definition

(Wernerfelt, B., 1990) Defined resource based view as an approach to receive competitive advantage, considering resources important for organizations performance.

Scholars argued that firms must look inside the organizations to receive the sources of competitive advantage instead of searching at the competitive environment for it. See Figure 3 Resource based view Model, which explains the model key criteria.

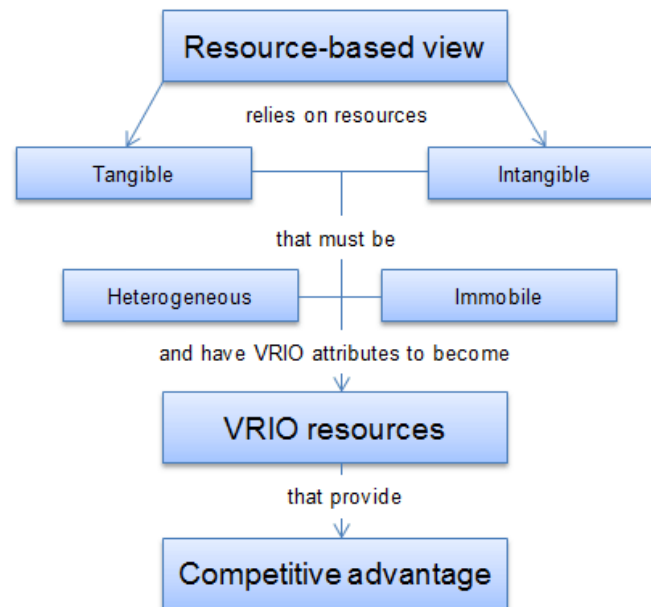


Figure 3 Resource based view Model

Make or Buy Analysis

“Make or Buy” decision considered to be complicated at the heart of outsourcing (Woodall *et al.*, 2009), yet, (Cáñez *et al.*, 2000) focused on the significance of make or buy approach as being important for many decades, because of its multidisciplinary nature, they developed a comprehensive frame work of make or buy decision by combining models from the literature; vertical integration, transaction cost, and strategic resourcing.

Several scholars studied the “make or buy” strategies from different perspectives like; strategic view, core or non-core activities and competitive advantage, this paper is going to combine the three perspectives, and asks the following questions before taking the decision to outsource:

Q1: Is the activity to be outsourced core or non-core activity?

Q2: Does outsourcing provide the competitive advantage of the organization?

Q3: Does the activity which is going to be outsourced achieve the strategic direction of the organization?

Q4: To which degree the benefit of the outsourced activity is less than the cost?

Conceptual Model Development

In order to build a conceptual model for effectively managing outsourcing strategy, efforts from theory and literature have been considered; resource based theory, effective management of interdependencies, and information sharing and trust management throughout the project. Moreover, with the aim of making the right decision to outsource, a decision-making process is considered to be essential.

Coordination Management Model

Interdependencies

Scholars argued that outsourcing is unsuitable strategy for long-term durations. (Hui *et al.*, 2008) Stated in complex projects, activities are subdivided into multiple external service providers, making these activities interdependent which impact each other within stage or between stages. They concluded that it depends on activities interdependence and how they are distributed in terms of sequence to be beneficial.

Information sharing and Trust

(Simatupang *et al.*, 2004) Studied the degree of involvement of supply chain members in information sharing, which offers visibility into supply chain procedures in coordinating the sequence of activities, it includes customer needs, product related information, customer demand, process related data and performance data, they proposed that actors do not have to share private information but they should find different solutions to the problems they face.

Trust is meant to be an important qualitative factor due to suppliers' capability to participate with organizations as partners and ability to share data from costs to schedules, it integrates suppliers in projects activities according (Kanda & Deshmukh, 2007), as a result it maintains a good relationship, build a commitment, and a smooth communication between parties to achieve the common goals required.

Trust can be another perceived risk absorption method to information sharing taking into account that it doesn't prohibit the actual risk (Tomkins *et al.*, 2001). Thus, uncertainties between parties can be mitigated through control or trust (Salonen, 2004). However, if the relationship between the contractor and suppliers in terms of trust and information sharing went to downstream, potential risk may increase leading to conflicts and as a result claims and dispute may occur. See Figure 4 Outsourcing Suppliers Coordination Management Model (Source: The Author) which illustrates the coordination mechanisms for an effective management developed from the literature and practice.

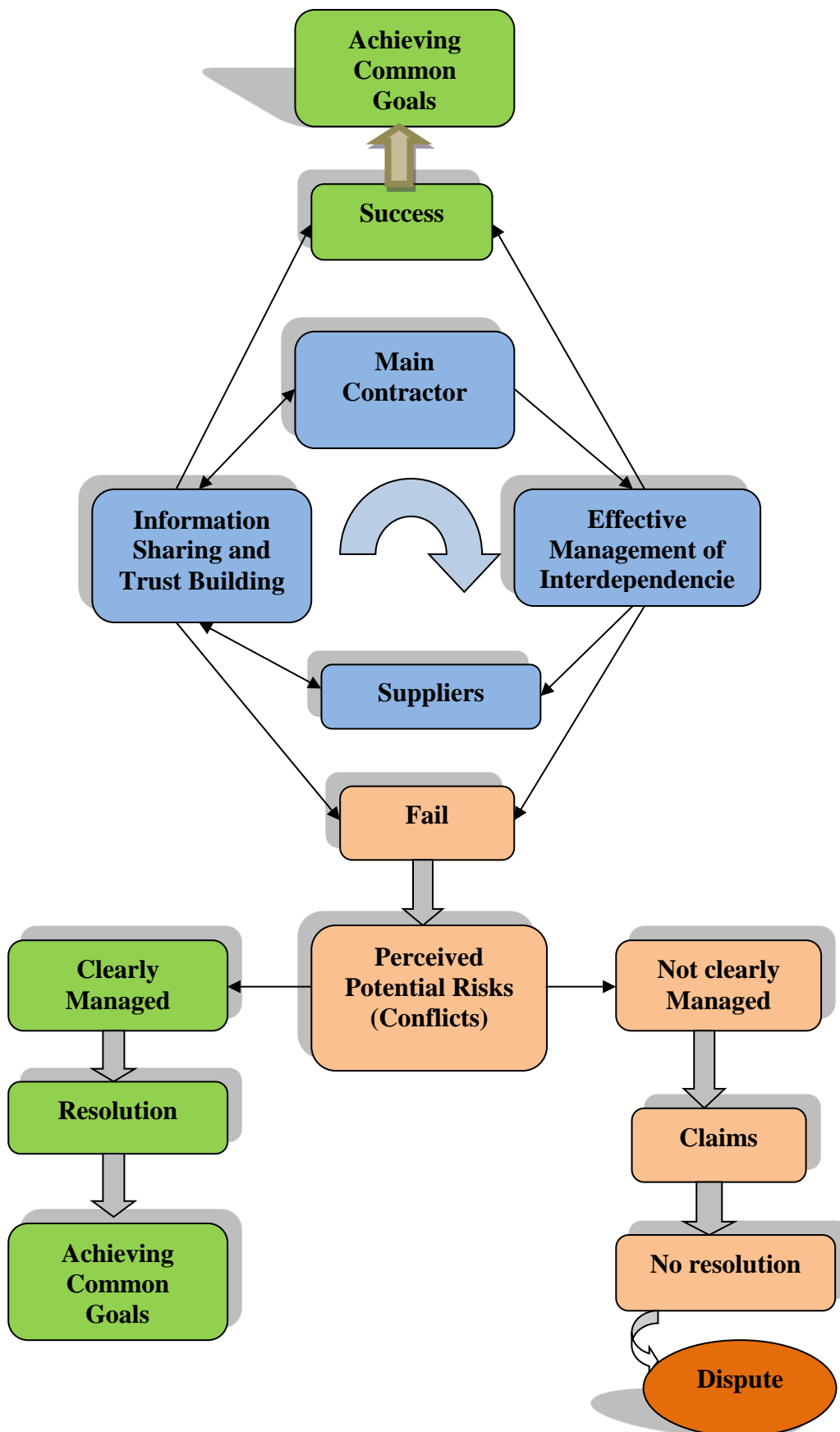


Figure 4 Outsourcing Suppliers Coordination Management Model (Source: The Author)

Decision-Making Process Model

Competitive Advantage

Resource Based View Theory

Criteria

Resource based view suggests that it is more useful to take advantage of external opportunities using available resources inside the organization rather than acquiring external skills to achieve performance required. This theory is based on two types of resources; Tangible and intangible (Rothaermel, 2012; Barney, 1991).

Tangible assets

Tangible assets are physical objects like; machineries, buildings, lands, capital and equipments, organizations can take advantage of these assets in the long run.

Intangible assets

Intangible assets are the resources which have no physical meaning but organizations can still own them, like; brand names, intellectual property and trademarks. This kind of asset is built over time, and it is the main sustainable resource that brings competitive advantage.

As a result, RBV suggests that any activity that cannot achieve, deliverability, inimitability, durability, and non-substitutability should be outsourced.

Strategic Direction

Organizations adopt the short-term profit and short-term cost reduction, however, it is argued that make or buy decision is made by organizations who seek long-term profit. (McIvor *et al.*, 1997) Illustrated that make or buy analysis is a strategic decision, that has influences on overall organization strategy. Their paper described a model that includes a four stages analysis for an effective make or buy decision which are; defining the core activities, profiling the appropriate value chain links, total cost analysis; analysis of potential suppliers for partnership. and analyzed number of strategic factors. They presented key problems that face organizations to end up with an effective make or buy decision. See Figure 5 Hierarchy of strategic Importance (McIvor *et al.*, 1997).

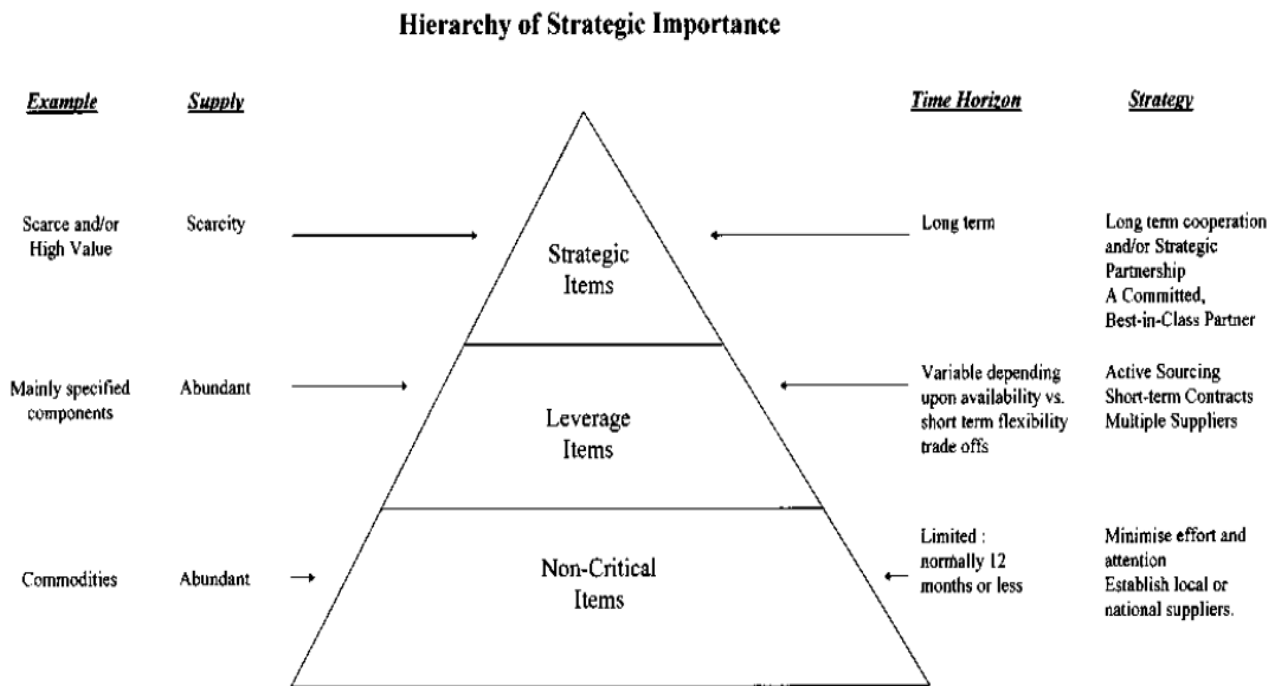


Figure 5 Hierarchy of strategic Importance (Mclover *et al.*, 1997)

Defining Core or none-core Activities

The emphasis on core and strategic activities outsourcing categories has been increasing since 1980s. (Ramacha & Natarajan, 2011; McCormack, 2003) emphasized on risks attached to outsourcing core or none-core activities. However, in order to achieve the competitive advantage and customer satisfaction, organizations must differentiate between core and none-core activities prior to decide whether to outsource or to use in-house resources, the first step forward to for choosing to outsource is defining core and none-core activities (Mclvor *et al.*, 1997). (Boer *et al.*, 2006) Mentioned three main basic outline for make or buy decision, they emphasized as well on defining core or none-core activities, assessments of costs, and analyzing suppliers relationship.

As a result, in order to maintain the competitive advantage of organizations, core activities are advised to stay in-house and outsource none-core activities after implementing a cost-benefit analysis.

Cost Analysis

Organizations have always assumed that outsourcing reduces costs, and exploit the implicit financials by the potential suppliers (Ramacha & Natarajan, 2011; Woodall *et al.*, 2009). However, calculating and identifying all potential and actual cost involved in activities is important in deciding to make or buy including uncertainty costs according to (Woodall *et al.*, 2009) , yet, there are two types of cost estimation according to (Mclvor *et al.*, 1997); cost estimation associated with internal production and cost estimation associated with suppliers, whereas, total internal cost is difficult to be

estimated which include costs that can be traced to the main outsource location and secondary costs.

Prior to outsource, organizations may consider, cost-benefit analysis of outsourcing activities including the potential costs of monitoring and controlling costs, uncertainty costs, and other costs associated with the activities and to which degree costs of the outsourced activities stay within limits, please see Figure 6 Outsourcing Decision-making Process Model (Source: The Author) which illustrates the decision-making process that can be used prior to outsource for an effective coordination management of outsourcing partner.

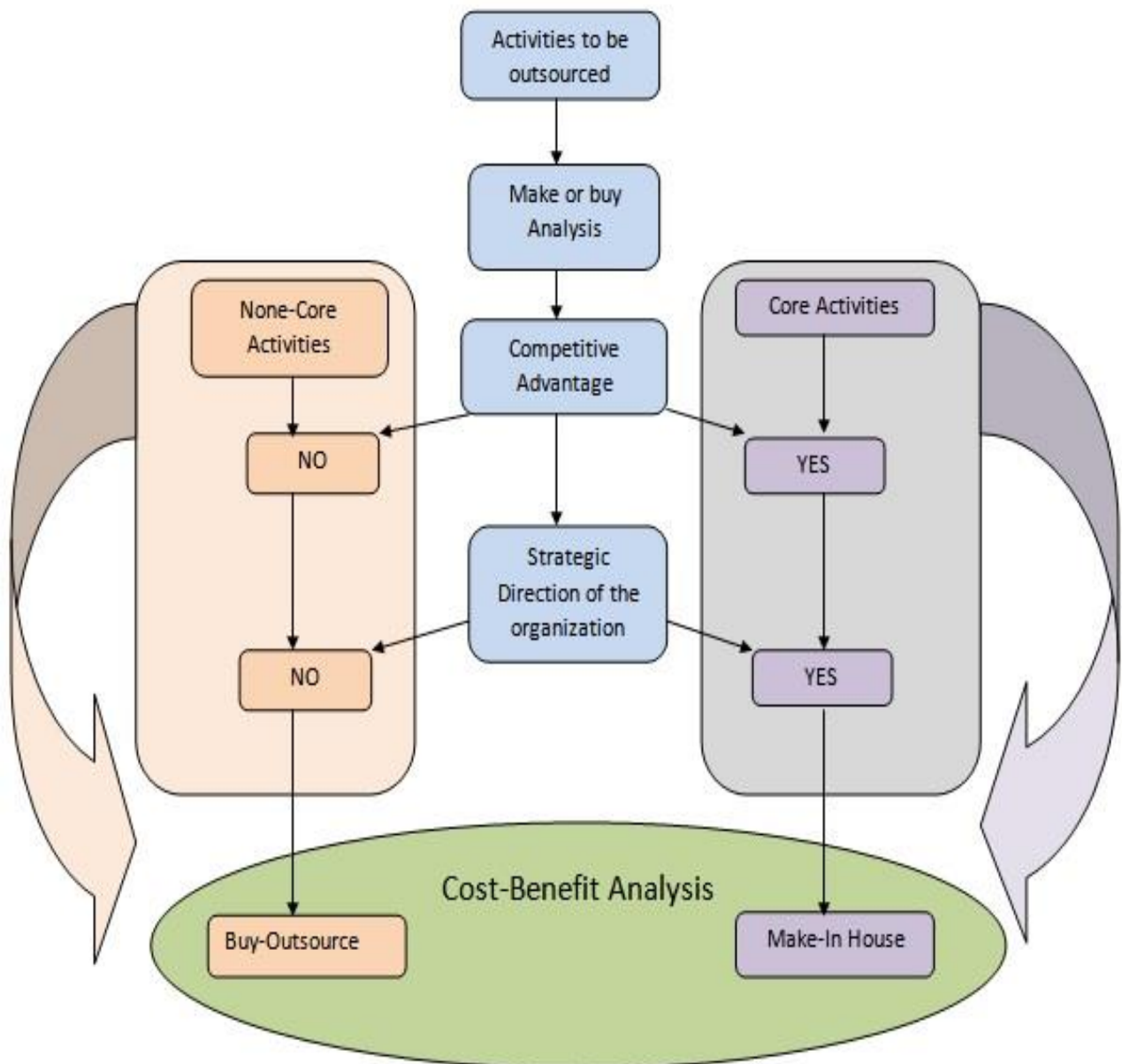


Figure 6 Outsourcing Decision-making Process Model (Source: The Author)

Data Collection and Analysis

Case Study

The data collected using a questionnaire-based survey to examine the coordination mechanisms between several suppliers and the contractor of “Complex1”, the questionnaire included five key managers in the project from the main contractor side, and five suppliers of both core and non-core activities, while the analysis is used to evaluate the relationship, information sharing and trust among the outsourcing partners. Finally, more data were also collected to examine the success or failure for using outsourcing strategy in “Complex1”.

Contractor/Supplier Coordination management Analysis

Coordination

- A- Are the employees aware of supply chain coordination?
- B- Is there flexibility in coordination mechanisms?
- C- Are there barriers observed while coordinating with each other?

Relationship and information sharing

- D- Is the relationship with Contractor/suppliers long-term?
- E- Are the Contractor/suppliers motivated for close relationship with each other?
- F- Are members ready to do all operations collaboratively?
- G- Is the relationship with members built on trust and commitment?
- H- Do Contractors/suppliers share Information?

Conflict Management

- I- Are the outsourced interdependent activities coordinated well to avoid conflicts?
- J- Are there conflicts between suppliers and contractors?

Assessment/Contractor	Project Manager	Procurement Manager	Sr. Construction manager	Commercial Manager	Technical Manager	Total
A	Yes	Yes	Yes	No	No	60%
B	No	Yes	Yes	No	No	40%
C	Yes	No	Yes	Yes	Yes	80%
D	No	Yes	No	No	No	20%
E	Yes	No	Yes	No	Yes	60%
F	Yes	Yes	Yes	Yes	Yes	100%
G	Yes	Yes	Yes	Yes	Yes	100%
H	Yes	No	No	No	No	20%
I	Yes	No	Yes	No	Yes	60%
J	Yes	Yes	Yes	Yes	Yes	100%

Table 2 Contractor Response on Coordination Management

Assessment/Suppliers	Supplier 1	Supplier 2	Supplier 3	Supplier 4	Supplier 5	Total
A	No	No	No	Yes	No	20%
B	No	No	No	Yes	No	20%
C	Yes	Yes	Yes	No	Yes	80%
D	Yes	No	No	Yes	Yes	60%
E	Yes	No	No	Yes	No	40%
F	Yes	Yes	Yes	Yes	Yes	100%
G	Yes	No	No	Yes	Yes	60%
H	No	Yes	No	No	No	20%
I	No	No	No	Yes	No	40%
J	Yes	Yes	Yes	NO	Yes	80%

Table 3 Contractor/Suppliers response to the relationship and information sharing

Case Study Analysis

Response to Coordination Management

In “Complex1”, it is noted that there is a gap in understanding the coordination methodology and implementation between the contractor and the suppliers, in the same time, it seems the flexibility in coordination among the outsourcing partners is likely to be low, moreover, all partners believe that there are barriers observed in the coordination system, please see Figure 7 Contractor/Suppliers response on Coordination Management.

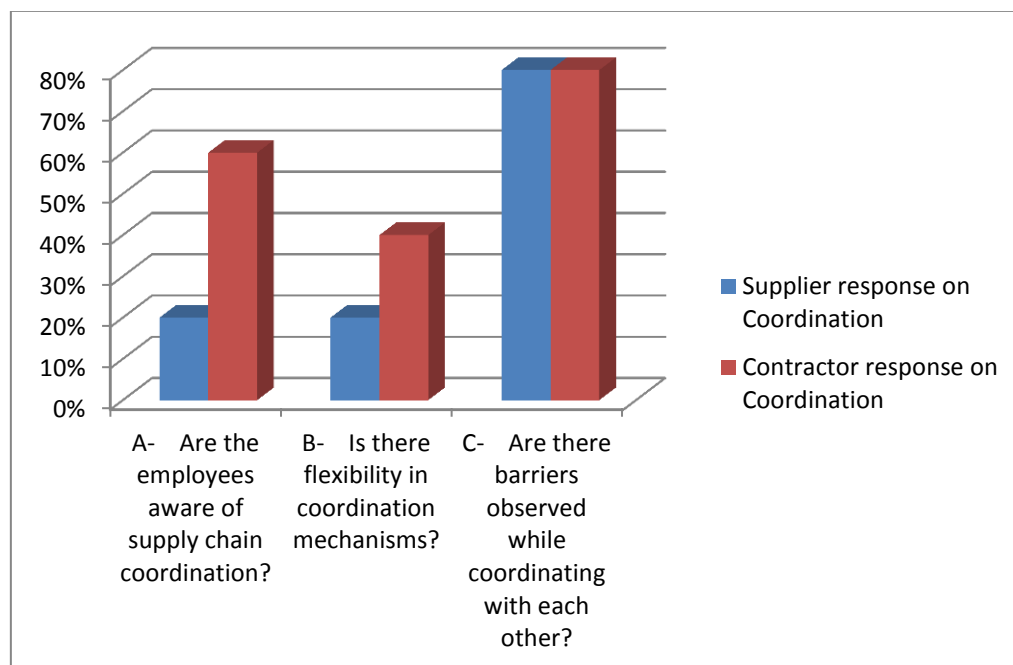


Figure 7 Contractor/Suppliers response on Coordination Management

Response on relationship and information sharing

It is seen that suppliers have a higher expectation of long-term relationship with the contractor. Although the main contractor has less significant initiative to keep none-core activities suppliers' relationships for long-term duration, the results showed that the main contractor is still motivated for a closer relationship with the core activities suppliers. A significant response from all parties to collaborate in all operations, however, it is found the sharing information between the outsourcing partners is pretty much weak, please see Figure 8 Contractor/Supplier response on relationship and information sharing.

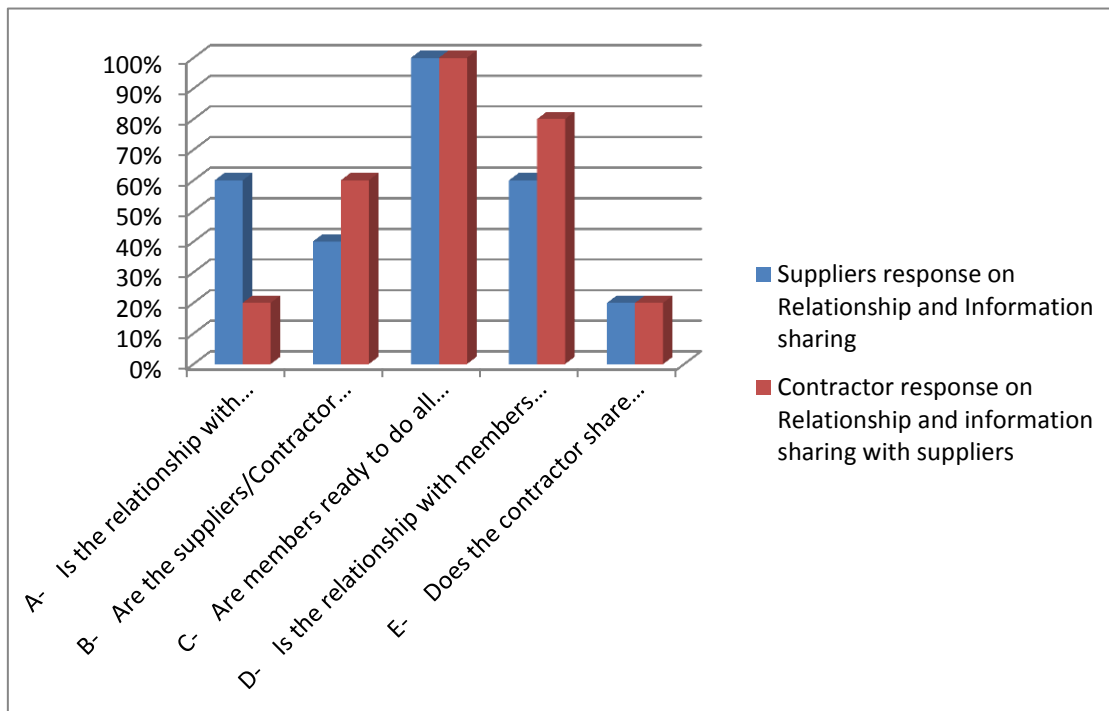


Figure 8 Contractor/Supplier response on relationship and information sharing

Contractor/suppliers response to potential risk and conflicts

The results found that in “complex1”, suppliers have lower expectations to having conflicts with the main contractor, moreover, it is shown that all parties believe there are potential risks to have conflicts between them, see Figure 9 Contractor/Suppliers response on Potential risk and conflict.

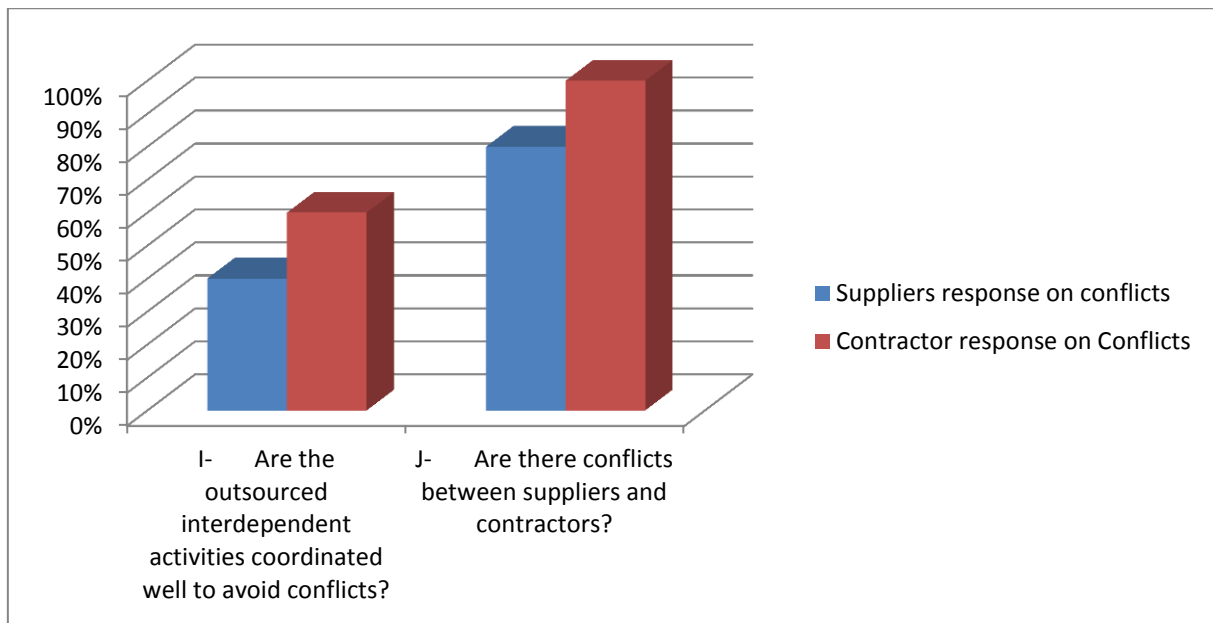


Figure 9 Contractor/Suppliers response on Potential risk and conflict

Outsourcing decision-making process assessment in "Complex1"

Data Collected from five key managers from the main contractor side in "Complex1" to examine the success or fail of the outsourcing strategy.

Assessment Criteria

- 1- Does outsourcing provide the competitive advantage of the organization?
- 2- Are the outsourced activities core activities?
- 3- Does outsourcing provide the benefits required to the organization?

Question	Contractor Project Staff					Total
	Project Manager	Procurement Manager	Sr. Construction Manager	Commercial Manager	Technical Manager	
1	No	Yes	No	No	Yes	40%
2	No	Yes	No	No	No	20%
3	No	Yes	Yes	No	Yes	60%

Table 4 Contractor Response on Outsourcing Decision Making

Contractor's Response to Outsourcing Decision Making Validity

The results showed that there is a less significant competitive advantage in dealing with this amount of suppliers in the project whether core or none-core activities. However, the management believes, if there was an effective decision-making strategy prior outsourcing, the coordination management with outsourcing partners would be more successful. See Figure 10 Contractor's Response on Outsourcing Decision Making.

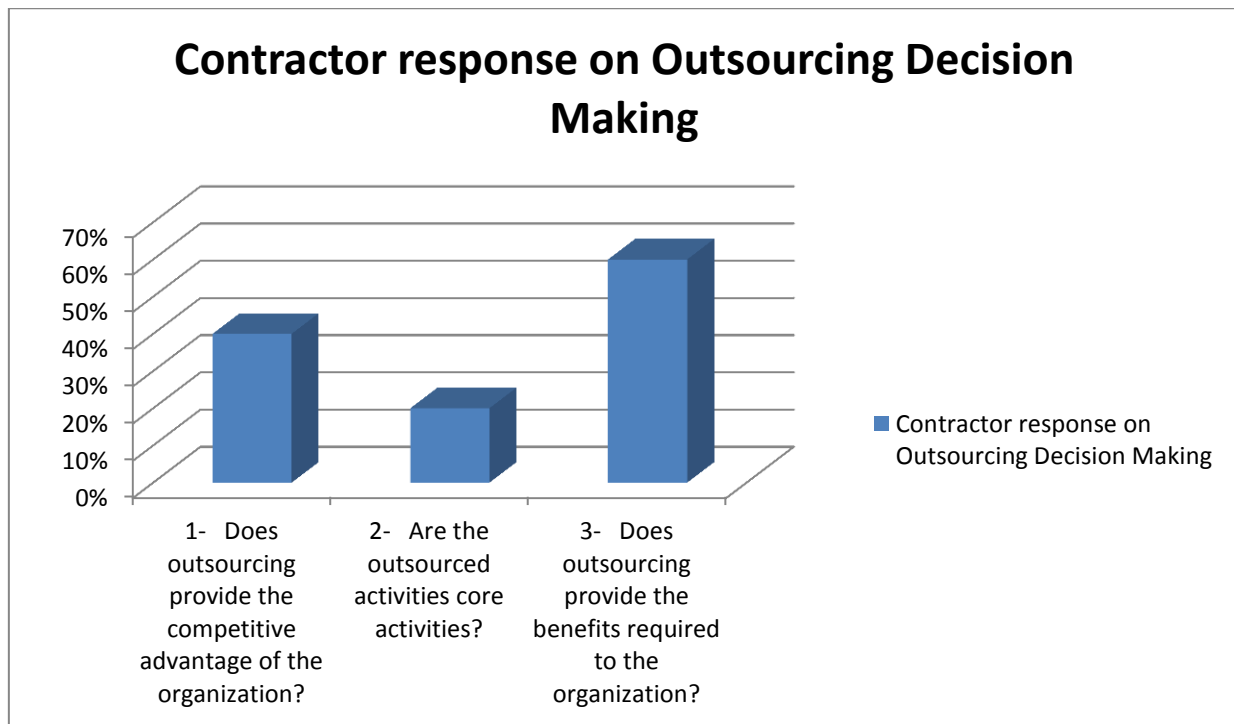


Figure 10 Contractor's Response on Outsourcing Decision Making

Conclusion and Recommendations

In order to effectively manage the coordination mechanisms among outsourcing partners in a complex project, a decision-making process is extremely essential to be implemented prior to outsource activities.

In “Complex1”, deciding to outsource irrationally led to severe consequences in terms of managing coordination effectively among one hundred and eighty suppliers. The model of coordination management proposes that in order to achieve the common goals of the outsourcing strategy among all outsourcing partners in “Complex1”, the main contractor needs to effectively manage interdependencies among all suppliers, whether activities within stage or between stages and sequence of activities, it is recommended that small numbers of contractors to be used but higher concentration on the contractor effort to enhance the controlling and coordination.

In addition, sharing information like, customer needs, service related data, process, and performance is extremely important to gain trust between suppliers and the main contractor, whereas, trust can play a major role in risk mitigation and controlling potential risks “Conflicts” and since conflicts have negative impacts on project performance, outsourcing partners need to identify the sources of the conflicts to overcome disagreements by understanding the common goals of the project, however, the model recommends effective management of potential risks to avoid dispute.

On the other hand, decision-making process model suggests that based on “Resource based theory”, organizations may consider using available sources inside the organization, furthermore, it suggests a make-or-buy analysis for the outsourcing

activities, that is; in order to outsource, activities should not be core activities, nor strategic, however, it is highly recommended that a cost-benefit analysis to be initiated to identify potential, uncertainty, and actual costs prior to decide whether to outsource or to use in-house.

Outsourcing provides organizations expertise and access to concentrate on productivity, innovation, and core business, however, organizations need to decide based on their ability to manage the coordination and controlling mechanisms using a comprehensive decision-making process to achieve the best outcome.

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Ramaz S. Issa is a Civil Engineer, is studying for a Master of Science degree in project management at the British University in Dubai, and is a PMP candidate. Ramaz S. Issa is a Civil Project Engineer at Gulf Technical Construction Company, a Drake & Scull International PJSC Company in Dubai, UAE. He has participated in managing three multi-million dollar projects which include, complex of four residential buildings, container terminal works building package that includes offices & various Industrial buildings, and four stars hotel. Ramaz earned his bachelor's degree in civil engineering from the University of Sharjah and aims to finish his MS degree in project management from the British University in Dubai in 2016.

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