Outsourcing: transferring services and processes to external service providers

Outsourcing refers to the transfer of company functions, processes or manufacturing services to external service providers. In industry, it frequently concerns contract manufacturing, logistics, IT or commercial processes, which are carried out by suppliers instead of being produced in-house. This gives procurement a new role: instead of steering internal departments, it manages suppliers through contracts, metrics and audits. The term is closely related to insourcing, nearshoring and make-or-buy decisions.

As of October 2026 · amplifa-marketplace.ai/en/glossary/outsourcing

Key facts at a glance

01 Outsourcing is the permanent transfer of tasks or processes to external service providers on a contractual basis.

02 The fundamental decision is made through a structured make-or-buy analysis based on a sound requirements analysis.

03 In practice, industrial companies typically outsource contract manufacturing, logistics, IT, facility services and parts of indirect procurement.

04 Successful outsourcing requires clear specifications, measurable SLA/KPIs and defined handover processes.

05 Typical risks include dependencies (vendor lock-in), quality deterioration, hidden follow-up costs and loss of know-how.

06 Regulatory and data protection aspects as well as contract for work and supply terms must be reviewed before contract award.

Definition: Outsourcing

Outsourcing is the strategic decision to permanently transfer services previously performed in-house to external providers. It is not a one-off order but a long-term supply-related partnership with contractually

agreed services, volumes and quality requirements. Outsourcing must be distinguished from pure external procurement, which does not presuppose the transfer of one's own resources.

Distinguishing from insourcing and nearshoring

Insourcing describes the repatriation of outsourced services into one's own company, often after quality problems or changed cost situations. Nearshoring relocates services to geographically close countries in order to shorten supply chains and spread risks. Both concepts are reactions to outsourcing experience and part of the same strategic make-or-buy discussion.

Functions affected in industry

In manufacturing companies, outsourcing frequently concerns the contract manufacture of components and assemblies, the complete logistics operation including warehousing and picking, IT services and indirect areas such as facility management or payroll accounting. Within procurement itself, purchase order release, supplier chasing and master data maintenance are increasingly outsourced to business process providers, while strategic tasks such as technology assessment remain in-house.

Degree of outsourcing as a steering metric

The degree of outsourcing measures the share of externally delivered services in total value creation. It serves portfolio steering and shows how dependent a company is on external partners. A high degree reduces fixed costs but increases the importance of supplier management and contract design.

Methods and approach in outsourcing decisions

An outsourcing project typically follows a multi-stage process from requirements analysis via supplier selection to transition. The quality of preparation largely determines later success: unclear specifications and missing handover concepts are the most common causes of subsequent cost increases.

Make-or-buy analysis and requirements analysis

The starting point is a sound requirements analysis that precisely captures the type, volume, quality and time structure of the service. Building on this, the make-or-buy analysis compares internal costs with offer prices – including transaction costs, transition effort and capital tied up. A cost breakdown of one's own production costs is helpful, as it establishes comparability with provider offers and makes later price deviations from the order apparent early on.

Invitation to tender and award decision

Supplier selection takes place via a structured request for proposal with defined award criteria such as price, capacity, quality capability, location and sustainability credentials. For close decisions, a Best and Final Offer (BAFO) procedure can form the final negotiation stage. The award readiness of the request itself – i.e. how clearly specification, volumes and terms are worked out – determines the informative value of the incoming offers.

Transition and contract design

The transition phase includes knowledge transfer, machinery and tooling relocation, ramp-up qualification and defined milestones. The contract governs SLAs, prices with adjustment mechanisms (typically material price indexation), liability, exit clauses and audit rights. For manufacturing services, declarations of conformity, first article inspection and documentation obligations must additionally be agreed.

Key KPIs for steering outsourced services

Outsourced processes can only be steered if performance is agreed in measurable terms and regularly evaluated. The KPIs are typically fixed in service level agreements and consolidated in regular supplier evaluations.

Delivery and process metrics

Core metrics are on-time delivery, PO Cycle Time from requirement to order confirmation, and the results of the available-to-promise (ATP) check at the service provider. For contract manufacturing, scrap rates, rework share and schedule adherence in batch allocation are added. These metrics are typically discussed in joint operations meetings on a monthly basis.

Quality and cost metrics

Goods receipt inspection provides the data basis for acceptance rate, complaint rate and 8D processing times. Cost steering is carried out via price deviation from the order, index adjustments and plan-actual comparisons of the agreed cost breakdown. Volume discounts should be contractually fixed as volume rebates and regularly reviewed for achievement.

Structuring service level agreements

SLAs define the metric, measurement method, data source, target value and consequences in case of deviation. Agreement on a common data basis is important, as divergent measurements between client and service provider are a frequent point of dispute. An escalation path with graduated response times belongs in every SLA toolkit.

Risks and controls in outsourcing

Outsourcing shifts responsibility, not accountability: the client remains responsible to its customers for quality and security of supply. Risks must therefore be identified systematically and safeguarded through contractual and operational controls.

Dependence and vendor lock-in

Knowledge, tooling and processes transfer to the service provider – a later repatriation or change of provider can be expensive and lengthy. Countermeasures are exit clauses with defined handover obligations, contractual securing of tooling ownership, data return and – where possible – dual sourcing

strategies for critical services.

Quality assurance and audits

For outsourced services, quality management in procurement relies on defined inspection plans, goods receipt inspection and regular supplier audits. A structured audit checklist ensures comparability across locations and points in time. For chemical-technical requirements, certificates of analysis and complete documentation form part of every delivery.

Legal, tax and data protection aspects

Relevant topics are temporary agency work and false self-employment in personnel outsourcing, delivery terms under Incoterms CIP or other clauses, warranty and liability, and data protection requirements for IT services. These points must always be reviewed on a case-by-case basis with the legal and tax departments; general statements do not replace legal advice.

Current developments: resilience, nearshoring and digitalisation

The outsourcing debate has shifted: cost saving is no longer the sole objective; supply chain security and flexibility have joined it as equals. Companies increasingly evaluate outsourcing decisions from a resilience and compliance perspective.

Resilience and nearshoring instead of pure cost optimisation

Supply failures and geopolitical uncertainties have meant that distance, transport risk and degrees of dependence now feed into the make-or-buy analysis. Nearshoring and multi-stage supply concepts complement or replace classic offshore outsourcing models. Price is thus supplemented by risk costs – a holistic total cost comparison has become standard.

Sustainability and reporting obligations

Outsourced services increasingly fall under sustainability and supply chain due diligence obligations. Frameworks such as the GRI Standards as well as customer requirements for carbon accounting make the service provider's environmental and social performance an award criterion. Corresponding evidence and audit rights should be contractually anchored early on.

Digitalisation of steering

Digital procurement platforms with mobile approval (P2P), automated supplier chasing and integrated procurement data models reduce the steering costs of outsourced processes. A consistent procurement data model enables transparency on service, volume and cost developments across all outsourced areas and makes multi-provider comparisons possible.

Typical metrics

Metric	Typical value
Supplier on-time delivery	> 98 % *Customary SLA target value for outsourced manufacturing services*
Goods receipt inspection acceptance rate	> 99 % *Share of defect-free deliveries; below this, complaint processes apply*
PO Cycle Time	< 3 working days *From requirement to order confirmation by the service provider*
Scrap rate in contract manufacturing	< 1.5 % *Industry-dependent; significantly stricter for safety-relevant parts*
Price deviation from the order	< 2 % *Indicates contract discipline regarding the invoiced price*

Practical example

A medium-sized mechanical engineering company with around 400 employees faced the decision of whether to outsource sheet metal working and welded assembly production in order to expand capacity for final assembly. Following a structured requirements analysis and make-or-buy analysis, the company decided to outsource to two regional contract manufacturing partners. The transition took around nine months and included machine relocation, tooling transfer and qualification of the partners following first article inspection.

- Invitation to tender with weighted award criteria (quality 30 %, capacity 25 %, price 25 %, location/logistics 20 %) and a BAFO round with the three finalists
- SLA with an on-time delivery target above 98 %, a scrap limit below 1.5 % and monthly review of goods receipt inspection
- Annual supplier audit based on a standardised audit checklist, plus contractually fixed exit clauses and tooling ownership
- Digital connection via a portal for purchase order release and supplier chasing to reduce PO Cycle Time

Conclusion

Outsourcing is far more than a cost reduction measure: it shifts a company's value creation, responsibility and risk structure and must therefore be prepared strategically. Success comes to those who make the decision on reliable data, specify services precisely and organise steering through measurable SLAs. Procurement takes on the key role here as contract partner, quality guardian and risk manager. At the same time, outsourcing remains reversible: regular make-or-buy reviews ensure

that the outsourcing decision continues to fit cost, quality and resilience objectives. Those who actively manage dependencies and maintain control mechanisms secure their company's long-term value creation.

Frequently asked questions

? What does outsourcing mean in simple terms?

Outsourcing means that a company permanently transfers tasks that were previously performed in-house to external service providers – for example manufacturing, logistics or IT. The service provider takes over personnel, machinery and process responsibility, while the client steers the service and handles settlement. The opposite is insourcing, where services are brought back into the company.

? What are the advantages and disadvantages of outsourcing?

Advantages typically include lower fixed costs, access to specialist expertise, greater flexibility in handling capacity fluctuations and a focus on core competences. Disadvantages include dependence on the service provider, loss of know-how, coordination effort and quality risks. Whether outsourcing pays off is determined by a thorough make-or-buy analysis including transaction and transition costs.

? What is the difference between outsourcing and external procurement?

With external procurement, a company purchases services it has never performed itself – such as standard parts. Outsourcing, by contrast, requires that the service was previously produced in-house and that resources such as personnel, machinery or knowledge actually transfer to the provider. Outsourcing is therefore a strategic structural decision, while external procurement is a routine purchasing decision.

? Which tasks are typically outsourced?

In industry, contract manufacturing, logistics and warehousing, IT services, facility management and commercial processes are frequently outsourced. In procurement, it affects operational activities such as purchase order release, supplier chasing and master data maintenance. Strategic functions such as supplier selection and contract negotiation usually remain in-house.

? How does an outsourcing project proceed?

Typically in five phases: requirements and make-or-buy analysis, request for proposal and supplier selection based on defined award criteria, contract negotiation with SLAs, transition with knowledge and resource transfer, followed by ongoing operational steering with KPI reviews and audits. The transition phase is, in experience, the most critical and should be planned with clear milestones and responsibilities.

? When is outsourcing manufacturing a sensible choice?

It makes sense when internal costs permanently exceed market prices, capacities are needed for

core processes, or specialist technologies are lacking that a provider can handle more economically. It is often not sensible for highly sensitive know-how, very small batch sizes with high coordination effort, or when security of supply is extremely critical. The decision should always include a total cost view including risk costs.

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