Challenges of hotel outsourcing in Ghana: A transaction cost perspective

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Abstract

Outsourcing is one of the many business strategies adopted by hotels due to the many opportunities that it provides. These opportunities notwithstanding, there are teething challenges with outsourcing. This study sought to find out from hotel managers in the Accra Metropolis of Ghana some of the challenges they face with outsourcing from a transaction cost perspective. Eight in-depth interviews were conducted in six hotels that outsourced. After capturing and transcribing data, a three-tier coding system was employed to group responses under thematic networks. The global themes that emerged within and across cases were inductively analysed. It was realised that poor quality of outsourced staff, lack of product knowledge by hoteliers, monopolistic tendencies by a few outsourcers, lack of commitment on the part of outsourced staff and cost involved in outsourcing were some of the challenges faced by the hotels in the Accra Metropolis of Ghana.

Keywords: accommodation, Accra Metropolis, Ghana, challenges, outsourcing, transaction cost, economic theory

Introduction

The business environment within the hospitality and tourism industry has been evolving just like any other industry. Globalisation, technological advancement, fierce competition and the changing customer have been cited as driving this change (Espino-Rodriguez & Padron-Robaina, 2005). Some businesses have been slow to change while others have been quick to act or react. But in the current global business environment, it is no longer good and healthy for a business entity to sit idle and wait for any contingency. Businesses need strategies in order to effectively compete and many are turning to outsourcing. Outsourcing can provide opportunities for an organisation to become competitive by accessing the knowledge, skills, and economies of scale and experience of specialist firms. These benefits notwithstanding, many organisations have failed to achieve the desired benefits envisaged in the decision to outsource and have subsequently experienced the consequences of outsourcing failure or have run into challenges that were not envisaged. This is as a result of industry practitioners adopting and embracing outsourcing strategies without necessarily taking the time to assess whether the concept is applicable to their businesses or not (Lam & Han, 2005).

McIvor (2005) is of the view that many outsourced functions are failing because of the misapplication of the concept by practitioners. Additionally, many of the organisations that have experienced outsourcing failure or poor results often had limited knowledge or experience in outsourcing and were outsourcing activities that they were having problems with without looking within to see what was internally wrong. This clearly shows that outsourcing is not all that rosy as there are challenges that firms will face no matter how well-crafted their outsourcing
strategies are. This study sought to explore challenges of outsourcing in hotels within the 3 and 4 Star categories in the Accra Metropolis of Ghana.

Overview of the accommodation sub-sector of Ghana’s tourism industry

Ghana’s tourism industry has seen tremendous growth in recent years. The accommodation sub-sector which is seen as the most obvious and physical form of tourism development anywhere in the world (Mensah, 2009; Akyeampong, 2007) is diverse with all the accommodation types such as hostels, resorts, spas and multinational hotels visible in the national stock (Mensah, 2009). The development of tourism in post-independence Ghana can be categorised into three periods (Akyeampong, 2007). These are the era of socialism-inspired development (1957-1973), constrained development (1973-1986) and market-oriented development (1986-to date). The third era is an important watershed in the development of tourism in Ghana since it marked the beginning of a period when a greater impetus was given to tourism development in Ghana. The beginning of the market-oriented period marked the start of the structural adjustment programme and the opening up of the Ghanaian economy for private and multinational investment. The liberalisation of Ghana’s economy which started in 1986 can be seen as contributing to the increase in demand for and supply of commercial accommodation in Ghana as more businessmen/women came into the country.

Transaction cost economics theory

Transaction cost economics (TCE) theory is the most influential theory on outsourcing (McIvor, 2009 & 2005; Lamminmaki, 2008; Holcomb & Hitt, 2007; Espino-Rodriguez & Padron-Robaina, 2005; Espino-Rodriguez & Gil-Padilla, 2005). This theory was put forward by Williamson in 1975 although according to Arnold (2000) and Lamminmaki (2005), Coase had earlier used it in 1937. The theory combines economic theory and management theory (McIvor, 2009) to determine the best type of relationship a firm should develop in the market place. The ultimate aim of a firm is to minimise total cost comprising transaction costs and production costs. This forms the basis for organising an economic activity either within the boundaries of the firm or using the open market (Grune-Yanoff, 2007). In any organisation, decisions on how to produce are made more difficult and costly due to the characteristics of players within the organization’s industry and the environment in which they operate (Donada & Nogatchewsky, 2009). The difficulties include bounded rationality, information asymmetry, opportunism and the presence of few suppliers (Donada & Nogatchewsky, 2009; McIvor, 2009).

Bounded rationality, according to Grune-Yanoff (2007) and Mansourain and Ford (2007), was first used in 1955 by Herbert Simon and later in 1956 by Herbert Simon and James March (Jones & George, 2006). It is based on the assumption that human decision making is limited by the ability of the person to process information and anticipate the future. Thus, in real life there is nothing like absolute rationality but rather human beings are only rational enough or partly rational (Mansourian & Ford, 2007). This hampers an individual’s ability to make optimum decisions. Due to this, it becomes difficult to make complete contracts which in turn increase the cost of every transaction.

Information asymmetry is based on the assumption that even if information is available to all parties involved in a contract one party may have more information than the other and will try to keep it away from the other (McIvor, 2005). Incomplete information comes about due to the inability of the decision maker to have full range of alternatives available and the consequences of the known alternatives. The reasons for this are risk and uncertainty, ambiguous information and time constraints and costs (Jones & George, 2006).
Opportunism in a transaction is the tendency for the parties involved in a contractual relationship to behave unscrupulously. This happens if they have information that other parties do not have. Opportunism refers to “the incomplete or distorted disclosure of information, especially calculated attempts to mislead, distort, disguise, obfuscate or otherwise confuse” (Vasquez, Iglesias & Rodriguez-del-Bosque, 2007, p. 500). When investments require specific assets, a partner may have information or know the weakness of the investing firm and might bargain “opportunistically” to appropriate more rent from the transaction. Also, since specific assets can be used in just one relationship the partner firm may encourage investment knowing that at the end of the contract, they would be in a better position to have control or use for the asset (Vasquez et al., 2007).

The presence of few suppliers creates market inefficiencies that can create high switching costs and increase opportunistic behaviour (Holcomb & Hitt, 2007). Because there are a limited number of suppliers in the open market, the only ones available turn to have more bargaining power which adds to the cost of a transaction. Also, if transactions are infrequent and small, the cost of getting additional information is high and this hinders the ability of firms to look for more information from suppliers before deciding on which one to choose (Mclvor, 2005). Mclvor (2005) postulates that costs in any transaction come as a result of the type of governance structure which is a major criterion in the decision to outsource. He also notes that cost and transactional difficulties increase if the transaction is associated with certain characteristics. These characteristics are what Williamson (1985) refers to as the dimensions of transaction cost: asset specificity, uncertainty and frequency.

**Asset specificity**

Williamson (1985) notes that asset specificity is the most prominent and widely studied dimension of transaction cost economics theory. This dimension distinguishes transaction cost economics from other transactions of an organisation. In transactions, goods and services that are highly specificity cannot be outsourced without incurring high costs. These costs come as a result of the need to write and negotiate contracts and monitor such contracts. Low specificity transactions require little monitoring and cost and can, therefore, be organised through external sources (Holcomb & Hitt, 2007).

An asset is specific when it cannot be relocated to another use without incurring significant costs (Espino-Rodriguez et al., 2008). This means that the asset is only important in a specific transaction; therefore, there is a high probability of hold-up if one party decides to renge on its duties. Lamminmaki (2005) using Williamson’s (1985) six typologies of asset specificity found that site specificity, temporal asset specificity and brand capital were the most pertinent reasons why hotels outsource.

**Site specificity** relates to investments that require that assets are located in close proximity to a supplier, which in this case is a hotel. In the hotel business, Hammington and King (2000) found that hotels outsource their food and beverage operations due to under performance. The restaurants cannot be located on other premises although some hotel guests prefer outside restaurants (Hammington & King, 2000). But once the hotel has added F&B to its operations the restaurant would have to locate on the premise of the hotel.

Due to this fact, hotels can sometimes become opportunistic when it comes to negotiations. They may demand custom made fittings for their restaurants which can only be used for that hotel. Another area that Lamminmaki (2005) has noted is customised laundry equipment. Reusing it elsewhere becomes difficult and the operator is locked up in the contract. She gives another dimension to the issue by arguing that hotels ask contractors to
locate on their premise in order to secure their commitment. In this regard, hotels are willing to give subcontractors long term contracts for committing to the hotel and making asset specific commitments.

**Temporal asset specificity** - timing and coordination of activities is the hallmark of the hospitality industry. The various departments in a hotel work in unison to deliver value for guests. The timely cleaning of rooms by housekeepers depends on the timely delivery of linen and other products. How early rooms are made available to front office by housekeeping also affects the timely check-in of guests. There are other areas within the hospitality industry that require timing and coordination. The delivery of food items to the food and beverage department also has implications on the timely delivery of food orders. So, in a situation where a partner or supplier holds up delivery, this will affect the operations of the hotels. Therefore, hotels are reluctant when it comes to outsourcing such functions (Lamminmaki, 2005).

**Human asset specificity** is knowledge or experience of the outsourcer’s personnel that is specific to the requirements of dealing with the hotels (De Vita, Tekaya & Wang 2011). Hotels are not just looking for any other personnel to engage but people or companies with specific skills that is lacking internally. De Vita et al. (2011) are of the view that human asset specificity is the most widely investigated dimension of the asset specificity construct, hence the most widely used. The authors note that human asset specificity can be characterised as unique technical skills and experience required in carrying out the activity being transacted. This also has to do with using the services of specialised suppliers.

**Brand capital** - Brand reputation is very important in the hospitality and tourism industry and in all other industries. Many international hotel brands such as Accor, Holiday Inn, Best Western, Hyatt, Shangri-La, and Marriott and in Ghana brands such as Golden Beach Hotels and Coconut Grove Hotels have built a reputation which they protect all the time. Lamminmaki (2008) concludes that hotels would not go into any contractual relationship with another firm or company if they see that such arrangements would adversely affect their brand reputation. Hotels tend to perform functions that directly relate to their brand in house than to outsource them.

**Uncertainty**

Contracts are inherently incomplete all the time due to the bounded rationality concept. Therefore, the harder it is to anticipate what would impinge on a relationship, the greater the uncertainty and greater the potential for incomplete contracting and opportunistic behaviour (Lamminmaki, 2008). In order to avoid the costs associated with incomplete contracts, TCE theory holds that the presence of greater uncertainty with a particular transaction, the greater the likelihood that it will be done internally. Environmental uncertainty and behavioural uncertainty can be identified here.

Environmental uncertainty affects the ability of the organisation to make predictions about the future concerning a particular activity (Watjatakrul, 2005). When there is uncertainty surrounding a particular activity, partners may withhold information from each other. They tend to act in an opportunistic manner. This uncertainty may force organisations to in-source rather than outsource such activities.

Behavioural uncertainty looks at monitoring the performance of subcontractors. Watjatakrul (2005) raises the argument that exchange partners may sometimes act with guile to create hidden costs by underperforming. When this happens, the cost of monitoring performance becomes high, so, many organisations would rather perform such activities internally than to outsource.
Frequency

This has to do with how often an activity is done or carried out by an organisation. When activities are carried out very often, the greater the likelihood it would be done in-house and vice versa (Lamminmaki, 2008).

According to McIvor (2009 & 2005), the fundamental question associated with TCE theory is when should a firm use market governance, hierarchy governance or intermediate governance. He opines that by looking at both the cost of governance and the threat of opportunism organisations can make the right decisions with regards to their boundaries. In some cases, it becomes necessary to invest in transaction specific assets.

Weaknesses of transaction cost economics theory

It is argued that TCE relies on single transactions as the unit of analysis. Multiple transactions with the same vendor or supplier are not taken into account. Another weakness is the over reliance on market and hierarchical governance. There are other governance mechanisms or structures such as expected transaction, the dynamic evolution of governance and transaction, the role played by trust and equity in an inter-organisational relationship. These are ignored in TCE theory (McIvor, 2005).

Holcomb and Hitt (2007) aver that the assumption that at equilibrium all firms will behave in a similar manner is untenable with governance theories. They also add that the portfolio of firms involved in any transaction is not taken care of under TCE.

Study area

The profile of Accra as the capital and seat of government of Ghana and in addition to the fact that it hosts all the diplomatic missions in Ghana as well as being the headquarters of many organisations and enterprises operating in Ghana makes it a magnet that attracts the establishment of high quality commercial accommodation (Akyeampong, 2007). Commercial accommodation distribution in Ghana is spatially skewed with the Accra Metropolis enjoying the lion’s share (GTA, 2009). It has the highest concentration of all the categories of hotels that can be found in Ghana.

In recent times, Accra has seen the proliferation of firms providing services such as security management, catering, Information Technology and laundry to most service sector businesses such as banks and hotels. Outsourcing of services in an area or locality depends to a greater extent on the availability of such services in that area (Ono 2007; Corbett 2004). Therefore, the Accra Metropolis provided the setting for carrying out the study.

Methodology

The study adopted a qualitative exploratory research design to investigate outsourcing strategy among the hotels. This was done with the aim that after exploration variables that could be measured will be identified (Creswell, 2007& 2002). This was necessary due to the paucity of literature on hotel outsourcing in Ghana. At the time of conducting the study a total of thirteen (13) hotels could be identified within the 3 and 4 Star categories of hotels in the Accra Metropolis (GTA, 2009). Six outsourcing hotels comprising three 4-Star hotels, three 3-Star hotels out of this total participated in the study. General managers (GMs) or senior managers who run the hotels on a daily basis and are involved in [outsourcing] strategy formulation and implementation (McIvor, 2009; Mensah, 2009; Benamati & Rajkumar, 2008), and therefore better placed to provide responses to the various questions that were asked were contacted. In-depth interviews were conducted, using a semi structured interview guide. The interviews lasted for more than an hour although in one instant forty minutes was recorded.
Findings and discussion

Challenges of outsourcing emanate either from within the organisation or from the subcontractor. Some of the challenges cited by the managers included poor quality of outsourced staff, lack of product knowledge by hoteliers, monopolistic tendencies by a few outsourcers, lack of commitment on the part of outsourced staff, differences in the organisational culture of hotels and contractors and cost involved in outsourcing.

Most of the managers involved in the study cited poor quality of staff from the outsourced companies as a major concern. Workers that were brought in by the hotels through the Temporary Work Agencies (TWAs) did not meet the criteria set by these hotels. The hotels, therefore, needed to give them extra training upon arrival at the hotels. There were other instances where some staff had the technical skills needed to perform a function but because they did not have work experience in the hotel industry they had to be given extra training just to equip them for the hotel-specific task.

The concern expressed by the managers in this study are similar to the findings of Knox (2010) concerning the use of temporary workers in hotels in Sydney, Australia where managers complained of low quality standards of outsourced staff. Lack of experience and inefficiency were associated with many temporary staff due to inadequate training by TWAs and this poor quality affected standards within the hotels:

The challenge I have come to know about outsourcing, as I said, is the inexperienced people they dump on the hotel. Because you know the work needs expertise, everywhere, from the kitchen to the front desk, they all need expertise. So if I tell you I need four people for the restaurant and you just grab people from the street and give them to me and it turns out that they are not waiters or waitresses, it becomes frustrating [Supervisor- 4 Star hotel].

Lack of product knowledge by management of the hotel is another challenge associated with outsourcing. Some suppliers are “cashing in” on the limited knowledge that managers have with regards to equipment delivery and servicing by not providing ample education on how to use the machines and equipment purchased from them. What this means is that the suppliers have information that is not known to the hotels. Due to this information asymmetry, opportunistic behaviours are exhibited by these suppliers to the detriment of the hotels. In TCE theory, information asymmetry and opportunism increases the cost of every transaction. Firms are, therefore, careful with suppliers who are perceived to be opportunistic. The machines break down easily and quickly only for a subcontractor to come in and charge more to fix them. This finding is affirmed by the experience of a manager in a 3 Star hotel:

The bigger challenge is when you do not have the product knowledge. If I do not know what I am expecting, and I am sourcing it out, how do I even evaluate what has been given. The contractors take advantage of not training the users, so the equipment does not become user-friendly. The more the machines break down, the more money they make. We have come to realise that most people bring products and because they sort of want to rip you off, they eliminate the training aspect [Manager- 3 Star hotel].

In an outsourcing market where there are few service providers and suppliers in the area of equipment maintenance, the few ones that are available tend to act in ways that have the semblance of monopoly. Because hotels do not have options with regards to repairers of machines, they have to fall on the original suppliers who act with guile, delaying the repairs to the
detriment of the hotels. This issue is addressed by small numbers bargaining attribute of TCE theory as described by a manager from a 3 Star hotel:

*It becomes a problem when companies become monopolies. Before I got this new company to supply our generators, the previous company said once I have bought my generators from them, I only have to bring Company D in to service it. That put me in a fix because I could not do anything. These are some of the peculiar problems and huge challenges that you face when you outsource, especially when contractors become sole agents and they do not have competitors* [Manager- 3 Star hotel].

Cost of outsourcing is another challenge faced by the hotels. It is expected that outsourcing would lead to cost reduction, but that is not always the case. Some firms demand what is beyond the means of the hotels even if permanent staff are employed. But that is not surprising since the contractor comes in with people with the necessary expertise. Though that could only be a logical explanation, some of the hotels complained that the charges of some vendors or service providers were far higher than what in-house staff would take for the same job. Another challenge relating to cost is the cost of renegotiating contracts. When an agreement is not reached on such contracts, they are sometimes abrogated due to the differences as the following expressions would support this claim:

*The cost involved in contracting a vendor. Others too, when the contract comes to an end and we want to renegotiate, they increase their charges. So these are some of the challenges* [Supervisor- 4 Star hotel].

**Conclusion**

This paper explored the challenges faced by hotels that outsource in the Accra Metropolis of Ghana from a transaction cost economic perspective. The findings indicate that some of the challenges were explainable by the transaction cost economics theory. Firstly, the poor quality of outsourced staff being supplied by the TWAs is an indication that the skill set of those employees are not highly specific to needs of the hotels. These are general skills that do not necessarily add value to the hotels. If the skills were highly specific and according to the human asset specific dimension of the TCE the hotels would gone in for highly skilled staff. But as it has turned out, not all the staff have the specific skills being looked for. Human asset specificity is knowledge or experience of the outsourcer’s personnel that is specific to the requirements of
dealing with the hotels (De Vita, Tekaya & Wang 2011).

Secondly, cost has always been a factor to consider in outsourcing decision making across the globe; where the cost of outsourcing is low organisations will embark on it and where costs are high even functions that have been outsourced are brought in-house. The findings show that the cost of outsourcing is high for some of the hotels and this coupled with the high cost of renegotiation could bring most of the outsourced functions in-house or prevent some of the hotels from further embarking upon outsourcing all together.

Thirdly, lack of product knowledge on the part of some of the managers is attributable to the information asymmetry element of TCE. Some organisations deliberately withhold information that could be beneficial to other partners in a transaction in order to gain unthawed advantage over the other. Some of the suppliers to the hotels deliberately refuse to give information on products or cross train employees from the hotels. In this case important information that could be beneficial to the hotels.

Fourthly, the lack of commitment on the part of some outsourced workers is an attribute of the behavioural uncertainty attribute of TCE. Some workers will deliberately act with guile just to stifle the progress of the hotels. This is an issue since the behaviour of staff of the outsourced company can be determined by the outsourcing firm from the onset of the transaction. This raises the cost of contract negotiation and monitoring which adversely can affect how future outsourcing by the hotels.

Finally, because there are a few suppliers in the outsourcing market in Ghana, it is possible for the few one to behave as monopolies. Few suppliers in the outsourcing market make fair bargaining impossible which eventually will lead to high cost of transaction.

References:


