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Nexus Between Risk in Outsourced Activities and Operational Performance of Electricity Distribution Company in Nigeria

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Abstract

The emergence of globalization has made outsourcing become one of the most used corporate strategies for providing top-notch services to various service industry which the electricity distribution sector is not left out. The study aims at examining the outsourced risk and operational performance of electricity distribution company in Nigeria using Benin Electricity Distribution Company (BEDC) as a case study. The study employed survey research design with a sample size of 14 business managers who were selected purposively. The data collected were analyzed using correlation analysis to determine the risk inherent outsourced activities posed are associated with operational performances. The findings of the study shows that the Pearson correlation value $r = 0.333$ between security & privacy risk and operational performance indicates a positive and low relationship at ($P=0.245$; $P>0.05$) significant level, the Pearson correlation value $r = 0.311$ between operational risk and operational performance indicates a positive and low relationship at ($P=0.279$; $P>0.05$) significant level , and the Pearson correlation value $r = 0.543$ between financial risk and operational performance indicates a positive and moderate at ($P=0.045$; $P<0.05$) significant level in the study area. In line with the findings, the study concludes that all risks factors are contributing element to operational performance except for financial risk having a moderate influence on operational performance in the study area and recommends that as much as risk is an important factor in business, the services of outsourced vendors should be cautioned so as not to expose the organization to too much of risk.

Keywords: Outsourcing, Risk, Operational performance, Distribution company, Electricity

1. Introduction

Outsourcing is said to be the process of hiring third parties to conduct services that were typically performed by the company and it is frequently employed so that a business can concentrate on its core functions. Adeleke, Olajide, and Bolanle, (2014) observed that due to the various costs of human and material resources and other issues that may arise from the production cost of goods and services, many organizations in Nigeria have adopted outsourcing as a tool to improve their corporate performance. Similarly, in today's worldwide interconnected world, businesses both in the private and public sectors simply rely on outside sources to fulfill their supply chain demands either for software, information technology, services, products, or partial components of these deliveries (Al Harrack, 2021). Similar to newly established organizations, they will continue to exist for all time with the sole intent of making a profit and keeping costs to a minimum. This as well is accomplished through the process of outsourcing by reducing staff maintenance costs, which helps organizations save a lot of money by contracting out work to outside workers (Adeleke, et al., 2014). Outsourcing as a function appears to be one of many ways to improve an organisation's performance. Generally outsourcing ensures that organization focuses on core businesses such as resources in the form of investment, people, and infrastructure used in developing the core business (Muhammad & Abubakar, 2019). In light of the above, outsourcing has evolved from a traditional concept to a strategic one that can significantly help organizations use their skills and resources to achieve greater competitiveness in the context of today's growing global competition (Prince, Irene, Osei & Anita, 2014).

Risk management has traditionally been responsible for assisting management in comprehending the potential effects of changes to corporate strategy, new products, market developments, and the overall business environment (Felix et al., 2016). The goal of outsourcing should be to free up management and give them the confidence to take on more risk in the core business operations that bring the most value. Al Harrack, (2021), argued that with the fundamental incentive to outsourcing being cost reduction and specialized knowledge at lower-value or peripheral operations, there is an increasing risk that an enterprise's capabilities might be exceeded by one or more of its providers in a data and intelligence driven environment. Also, IEAS (2021) concur that due to the inherent risks of third-party arrangements and the untransferable ultimate accountability of the entity using third-party services, effective management of outsourcing services is a must for both the private and public sectors.

Systems for distributing electricity is an essential component of modern society's infrastructure and as such electricity distribution is by definition a "natural monopoly," which means that creating rival parallel infrastructures to deliver this service would not be socioeconomically advantageous. Authorities heavily regulate this sector of the economy to prevent the abuse of monopolistic power (Nordgård & Wangensteen, 2009). However, the inability of distribution companies to meet its intermediation obligations introduces some vulnerability into their system. In Nigeria, the first electrical power plants were established in 1886 to supply the Lagos Colony, which was still a separate colony. The Electricity Corporation of Nigeria (ECN) was created by an Act of Parliament in 1951, and the Niger Dams Authority (NDA) was also established for the production of hydroelectric power in 1962. The National Electric Power Authority (NEPA), which was created in 1972 as a consequence of the merging of the two (2), was renamed Power Holding Company of Nigeria (PHCN) in 2005 as a result of unbundling and the power reform process. Benin Electricity Distribution Company is one of the successor distribution companies created following the unbundling and privatization of the state-owned power utility "PHCN". BEDC is responsible for retail distribution of electricity in four states: Delta, Edo, Ekiti and Ondo States with geographical coverage of 55,770 square kilometers. The company operates from twenty (25) business districts with approximately 350 offices located across the four (4) states with about 13 million people and about 4 million households.

Outsourcing company operations creates serious risk-related problems as a result of operational changes involving people, things, technology, and business procedures, which create operational risk exposures. Also, it brings about doubt since the new connection between outsourced vendor and the firm still signifies untested agreement since it is difficult to ascertain whether the outsourced vendor will perform the task better than that of internal staff (Kamanga & Ismail, 2017). Although, several studies (Akinbola, et al., 2013; Mwelu et al., 2014; Olannye & Okoro 2017; Agburu et al., 2017) on outsourcing has received remarkable attention most especially in the fast-food industry, manufacturing sectors, banking sector, communication sectors and the likes. However, such studies have not been conducted on outsourcing risk inherent and operational performance of the electricity distribution companies of Nigeria, hence there is a need to fill the gap for this study. The study therefore aims at examining the outsourced risk and operational performance of Benin Electricity Distribution Company (BEDC) in Nigeria.

2. Literature Review

2.1. Outsourcing

While outsourcing is not a new concept, there has been a remarkable amount of discussion regarding it in recent years. Many different viewpoints on outsourcing have been presented by various authors. According to Gabriel, Marek, and Milos (2015), outsourcing as a concept comes from the American economic life and represents a combination of the words outside, resource (s) and using as one artificial word known as outsource. The United Nations organizations, referred outsourcing as “common”, “shared” or “support” services which is guided by strategic decision-making, historical precedent, a hiring process, or a mix of all (IEAS, 2021). Also, Outsourcing is defined in the UN Procurement Practitioner's Handbook as “the process of contracting out a business process, which an organization may have previously performed internally or which the organization deems necessary or important, to an independent company, supplier or contractor where the process is purchased as a service.” Maurice, (2017) defined outsourcing as the tactical organizational means which involves giving out an organization’s none-core and non-revenue generating activities to outside vendor popularly known as service provider.

According to Corbett (2004), outsourcing involves a long-term partnership between the supplier and the beneficiary and a significant amount of risk sharing. Corbett idea about outsourcing implies that risk is inevitable for any organization that wish to entrust her business to an outside vendor.

2.2. Risk

Risk as a term is common and it is widely used in nature and in practice. Aven et al., (2011) was of the view that the concept of risk has changed over time and is still changing. According to Adam (2014), it is a word that has various meaning to many people. It is also a word that causes the feeling of urgency because it addresses detrimental, sometimes catastrophic outcomes (Aleksandar & Radenko, 2015). Risk is defined in several ways, depending on various factors like probability, expected values, uncertainty, and objectives. Some of the definition of risk includes: IRGC, (2005) they observe risk as an uncertain consequence of an event or activity related to something of human value. Also, risk equals expected damage (Campbell, 2005).

Risk refers to uncertainty about and severity of the events and consequences (or outcomes) of an activity with respect to something that humans value (Aven & Renn, 2009).

Traditionally the role of risk management in outsourcing is to assist management understand the potential impact of changes in business strategy, new products and market changes as well the entire business environment. There have been multiple suggestions for the type of outsourcing risk (Corbett, 2004; Bi, 2007; Shi, 2007; Juras, 2007; Gefen, Wyss & Lichtenstein 2008; Gonzalez, Gasco, Llopis 2009) but as such, the following risk categories can be highlighted using Corbett's (2004) strategy:

Transaction Risk: refers contract provisions, such as rules governing the resolution of disputes, commitments made by both parties, guarantees, the transfer of assets, the payment terms, and the terms under which penalties for non-performance or improper performance of the contract must be paid.

Operational risk: refers to the effects of outsourcing on the principal's employees, both those who remain with the company and those who may join the service provider as employees. This type of risk is also connected to the service provider's adaptation to the client's requirements, as well as the potential for changes to the laws governing such cooperation.

Strategic risk: refers to the long-term negative effects of collaboration, such as: loss of control over outsourced activities, knowledge loss, changes in provider activity, negatively affecting the client (examples: restriction of the range of services rendered, changes in the characteristics of transport, inadequate adaptation to changing legal requirements concerning, for example, the movement of hazardous materials).

Felix et al., (2016) observed that other risks associated with outsourcing and which may directly or indirectly affect the firm performance include: Lack of strategic clarity before entering into the contract, and/or failure to take into account the strategic change in the future which might change the nature of the outsourcing relationship; loss of control, loss of critical skills and knowledge, loss of intellectual property, loss of security, drop in service quality, and costs may increase as well as loss of innovative capability.

2.3. Theoretical Review

A variety of theories including Resource Based Theory, Transaction Cost Economics Theory, Core Competence Theory, and Contractual Theory, are the foundations for outsourcing. Nevertheless, this study is anchor on the Transaction Cost Theory. This theory provides an explanation that demonstrates the connection between the cost involved in contracting and the risk that may arise therein.

2.3.1. Transaction Cost Theory

This theory takes a look at the opportunity cost in monetary terms of outsourcing before taking decision whether to outsource or not. Transaction cost economics was first introduced by Coase in 1937 explaining that resources are allocated according to price mechanism and this allocation is dependent on conditions outside the firm and direct production and price movements which are routed via a series of exchange transactions with the market.

Transaction costs arise from the fact that it is not possible for a firm to completely contract while incomplete contracts create renegotiations when the balance of power between the transacting parties shifts (Williamson, 1979). The attribute of a firm's transactions positively associated with transaction costs include the necessity of investment in durable, specific asset, inefficiency of transacting, task complexity and uncertainty, difficult in measuring task performance and interdependence with other transactions.

Transaction cost economics (TCE) theory is based on a rational decision made by firms after considering transaction related factors such as asset specificity, environmental uncertainty and other types of transaction cost. Activities conducted under conditions of high uncertainty require specific assets e.g., human and physical capital. Asset specifically refers to the nontrivial investments in transaction i.e., specific assets. The central question of TCE is whether a transaction is more efficiently performed within a firm or outside it. The choice of producing in-house or buying from outside should be made on the basis of costs involved in both the operations. While producing in-house may incur higher production costs, buying from the market incurs higher transaction costs (Audu et al., 2017)

Reuben et al, (2007) were of the view that transaction cost economics (TCE) or theory view the relationship between service receiver and service provider as a model that allows economic transactions to take place. Transaction costs include time, money, human resources, contract issues negotiation matters, risks e.tc. Hence the relationship between service receiver and service providers is closely integrated due to cost considerations (Shaharudin et al., 2014). However, according to Mclvor et al., (2008), the transaction cost theory and resource based view theory can be combined to form a combined view through which outsourcing decisions can be based upon as transaction cost theory and resource based view theory complement each other. Therefore, in the process of making outsourcing decisions, it is not only important to consider the internal and external costs of providing the good/service but also the cost of managing the transaction in-house and outside (Klaas, McClendon & Gainey, 2001).

2.4. Empirical Review

Over time, researchers have empirically investigated the connection between outsourcing and organizational performance among which include the study on cybersecurity risks in outsourcing strategies by Al Harrack (2021) which discusses outsiders' threats in outsourcing strategies without neglecting the existence of insiders' threats providers to fulfill an organizational need either for software, information technology, services, products, or partial components of these deliver. The study identifies that in a world driven by data and intelligence, where cost savings and specialized expertise are the primary drivers of outsourcing, there is a higher danger that one or more of an organization's providers may be able to outperform it in terms of skills.

The study highlighted various cybersecurity risks from various authors ranging from piracy, vandalism, sabotage, untrustworthiness of the contractor and riots arguing that external threat actors can procure support from insiders by breaching security frameworks and providing password authentications for illicit actions. In summary, the study conclude that outsourcing strategies are a major source of cyber risks. This study also considers that the outsiders' threats are embedded in outsourcing strategies and also that when companies outsource IT or other functions, they change their risk profile to assume the providers' risks incorporated in the extended supply chain along with the uncertainties and opacities that constitute an intrinsic part of it. The study finds out that a client-provider trust relationship can improve the management of cybersecurity risks in the supply chain and mitigate the risks in the outsourcing decision-making process

Muhammad and Abubakar, (2019) study on benefits and challenges of outsourcing on service delivery: lessons for Nigerian public organizations. The study examines the benefits and challenges of Nigerian public organizations. The study pointed out that outsourcing is getting mileage across the world and many organizations can be transformed using the system as it will save cost, ease access to skilled human resources, enhance risk management, minimize corruption and accelerate migrating to new technologies. Part of the risk element the study finds out was that it can create over-reliance on external hands, shrink organization's talent pool and expose organization's confidential information. The study recommended that governments and managers of public organizations should ensure that only qualified and trusted firms be given such contracts, state of the art equipment be employed and operations of outsourced staff be adequately monitored so as to minimize the risk level of contracting out their services.

The study of Rehema and Rugami (2018) on effect of outsourcing on organization performance south to determine the influence of outsourcing risks, outsourcing costs, quality of service and functional department on the performance of commercial banks in Mombasa County Kenya. The study adopted the descriptive research design among the targeted population for the study which are strategy managers in all commercial banks in Mombasa County. The study sample was 90 strategy managers who were selected through census survey. Descriptive statistics such as (mean and standard deviation) were used to analyses quantitative data. The study established that outsourcing risks had a positive and significant effect on the performance of Commercial Banks in Mombasa County, Kenya and concludes that risks in outsourcing may arise due to possibility of weak management, inexperienced staff, business uncertainty, outdated technology skills, environmental uncertainty, hidden costs, lack of organizational learning and loss of innovative capacity. The study therefore recommends that commercial banks when drafting a contract should make sure to include all the expected services, and read carefully for any surcharges or extra charges. Before negotiations even begin, they should have providers sign a confidentiality agreement promising to safeguard the banks' secret

Wachira (2016), investigated the impact of outsourcing practices conducted by organizations in Nairobi. Questionnaires were distributed to management of 85 profit-making organizations in Nairobi. Data was collected from primary sources through survey method by use of questionnaires. The data was quantitatively analyzed based on research objectives. The quantitative data was analyzed through descriptive statistics and inferential analysis by use of statistical package for social sciences (SPSS) version 21 software. Findings suggested that outsourcing can yield positive and/or negative outcomes depending on the risks encountered by the business environment, company policy, function/s to be outsourced, and the competence and commitment of the outsourcing vendor. The study argued three improvements to enhance the positive impact of outsourcing. These are; the formulation of standard outsourcing policies, price regulations for outsourcing, and the commitment of outsourcing firms in adhering to set contract deadlines. The study implies that outsourcing opens markets for free trade and development to take place.

A study by Gadzekpo and Amos (2016) discussed the conceptual view on potential risk and threat of outsourcing of facilities management services in Commercial Banks in Ghana. The study identifies that in recent times, commercial banks have outsourced numerous non-core services such as ICT, janitorial services, security, and even part of bank's human resources and that outsourcing comes with some comparative advantages for the banks, but there are still fears of some uncertainties. Focusing on literature on outsourcing and authors own perspective from the banking sector in Ghana, the study identifies anticipated cost not realized, selection of wrong vendor & contract writing, overreliance on vendor/outsourced service provider, confidentiality risk, differences in working culture, and losing control over in-house activities as the key risks likely to come with outsourcing. The study therefore presents a theoretical framework for outsourcing. This implies that as outsourcing has its advantages, it also comes with a lot of risk factors.

Felix et al, (2016) sought to study the effects of outsourcing on organization performance in manufacturing sector of Kenyan firms. The objectives of the study were to determine whether cost, quality, technology adaptation and risk affect organization performance at Del Monte Kenya Limited. Data were collected through survey method by use of questionnaires. The data was quantitatively analyzed through descriptive statistics and inferential analysis which was based on the research objectives. Both correlation and regression analysis were done and the results reviewed that cost, quality, technology adaption had a significant strong positive relationship on organization performance. There result also discovered that there was an insignificant positive weak relationship between risks and organization performance. The study therefore recommended that organizations should not outsource an activity fully until they have confirmed beyond doubt that the service provider is capable of handling the activity. This implies that not all activities within an organization can be outsourced to outsourcing firms.

Moja et al, (2016) study on hazard and risk assessment in electricity sector of Swaziland Electricity Company identify the hazards and risks associated with the various processes involved in each step and suggest possible measures to control the identified risks. The top three significant hazards identified included; exposure to live wires, road hazards and the use of uncertified/serviced/ defective/wrong equipment and/or machinery. The distribution department was observed to have the most hazards and fatalities when compared to the other departments. This work determined hazards associated with the electricity sector and developed a simplified tool for hazard identification which can be used by other sectors. The data obtained in the hazard registers act as baseline information for other electricity utilities wishing to implement health and safety systems. The study provides information on currently used control measures and proposes additional measures that could help improve the safety performance of Swaziland Electricity Company and facilities of similar kind.

3. Methodology

The study was carried out at Benin Electricity Distribution Company who is one of the leading electricity distribution companies in Nigeria with a geographical coverage of 55,770 square kilometers operating with twenty (25) business districts with approximately 350 offices located across the four (4) states with about 13 million people and about 4 million households. The study was limited to areas in Ondo and Edo State Nigeria. Ondo axis consist of 4 business units while Edo state consist of 10 business units. The choice of the two areas was based on geopolitical zone (South west and South south) areas of Nigeria. The method used in this study is the survey type which involves the selection and studying the sample chosen from the total population of 14 business managers in order to determine the risk inherent outsourced activities posed are associated with operational performances of BEDC. 1 business manager represent each axis of the business units in Ondo and Edo axis respectively of Benin Electricity Distribution Company. A sample size of 14 business managers was selected from the two axis of BEDC using the purposive sampling techniques as each manager represent each of the business units within the two axis under study. The study makes use of primary data. The primary data was obtained through the instrumentality of constructed questionnaire which was distributed among the business managers. Questionnaire used as research instrument was validated by applying the questionnaire to business manager of Ikeja Electricity Distribution Company with a Cronbach Alpha coefficient result of 0.831 for risk. The data collected was analyze using the correlation analysis.

4. Data Analysis and Discussion of Findings

This objective of the study seeks to determine the relationship between risk inherent in outsourced activities and operational performance in Benin Electricity Distribution Company and this was achievable through correlation analysis. A Pearson moment correlation analysis helps to measure the relationship between two or more variables and also help to describe the strength and direction of the linear relationship between the two variables A Pearson moment correlation coefficient value "r" from 0.10-0.30 indicates a very low positive/negative relationship, 0.30-0.50 indicate a low positive/negative relationship, 0.50-0.70 indicate moderate positive/negative relationship, 0.70-0.90 indicates high positive/negative relationship and 0.90-0.99 indicate very high positive/negative relationship. Also, a positive (+1) Pearson correlation value shows that the relationship between the variables are positive while a negative (-1) Pearson correlation shows that there is a negative relationship i.e. an increase in one variable bring about a decrease in the other variable. Table 1 shows the correlation matrix among the study variables (i.e. risk inherent and operational performance) in the study area.

From the table, it is shown that there was an insignificant low negative relationship between security &privacy risk and operational risk (r= -0.200, p=0.492). Security & privacy risk and financial risk as well have an insignificant positive low relationship as explained by the Pearson correlation coefficient of 0.342 and a p value of 0.231. The Pearson moment correlation value r, 0.333 indicates that there is positive and low relationship between security & privacy risk and operational performance at (P=0.245; P>0.05) in the study area. This interprets that out of many other possible elements, security and privacy risk in the study area is a contributing element to the operational performance in the region however it is said to note that this has only had less minimal influence on operational performance in the study area due to the weak relationship between the variables.

Similarly, operational risk and financial risk as well have an insignificant very low positive relationship since the Pearson correlation coefficient is 0.138 and p value is 0.637. Likewise, the Pearson correlation value r of operational risk, 0.311 also indicates that there is still a positive and low relationship between the operational risk and operational performance in the study area. The figures also show that there is an insignificant relationship between the variables at (P=0.279; P>0.05). This as well interprets that out of other elements, operational risk in the study area is also a contributing element to the operational performance in the study area. However, it is said to note that it also has less minimal influence on the operational performance in the study area.

Lastly, the Pearson correlation value r, 0.543 indicates that there is positive and moderate relationship between financial risk and operational performance in the study area. Also, the figures show that there is a significant relationship between the variables at (P=0.045; P<0.05) which implies there is a link between the variables. This interprets that out of many other possible elements, financial risk in the study area is the major contributing element to the operational performance in the region however it is said to note that this has only had moderate influence on operational performance in the study area. The above findings are in connection with Wachira (2016) who disclose that outsourcing can yield positive and/or negative outcomes depending on the risks encountered by the business environment, company policy, function/s to be outsourced, and the competence and commitment of the outsourcing vendor. In the same vein, the study was in line with the study of Gadzekpo and Amos (2016) that though outsourcing comes with some comparative advantages, but there are still fears of some uncertainties such as anticipated cost not realized, selection of wrong vendor & contract writing, overreliance on vendor/outsourced service provider, confidentiality risk, differences in working culture, and losing control over in-house activities as the key risks likely to come with outsourcing.

Table 1. Correlation of risk inherent in outsourced activities on operational performance

Correlations					
		Security & Privacy Risk	Operational Risk	Financial Risk	Operational Performance
Security & Privacy Risk	Pearson Correlation	1	-.200	.342	.333
	Sig. (2-tailed)		.492	.231	.245
Operational Risk	Pearson Correlation		1	.138	.311
	Sig. (2-tailed)			.637	.279
Financial Risk	Pearson Correlation			1	.543*
	Sig. (2-tailed)				.045
Operational Performance	Pearson Correlation				1
	Sig. (2-tailed)				

*. Correlation is significant at the 0.05 level (2-tailed).
N=14
Source: Field Survey (2023)

5. Conclusion and Recommendation

The study seeks to determine the relationship between risk inherent in outsourcing and operational performance of BEDC. After successful data collection for the study, in which survey research design was adopted and the data was analyzed using the correlation analysis, the study established that there is a significant relationship among all the variables under study. The study concludes that security and privacy risk in the study area is a contributing element to the operational performance in the region however it worthy of note that it had less minimal influence on operational performance in the study area with an insignificant relationship between the variables at ($P=0.245$; $P>0.05$). More so, the Pearson correlation value r of operational risk, is 0.311 indicates that there is still a positive and low relationship between the systemic risk and operational performance in the study area which is also a contributing element to the operational performance in the region but has a less minimal influence on the operational performance in the study area with an insignificant relationship between the variables at ($P=0.279$; $P>0.05$). Lastly, the financial risk has a moderate influence on operational performance in the study area as the Pearson correlation value r, 0.543 indicates that there is positive and moderate relationship between financial risk and operational performance in the study area. This show that there is a significant relationship between the variables at ($P=0.045$; $P<0.05$) which is also a contributing element to the operational performance in the study area. Every business organization that outsourced are likely to be exposed to risk and this varies depending on the size and nature of their operation. The study therefore recommends that as much as risk which is an important factor in business should be factored in, electricity distribution companies and service industries should caution the services rendered by the vendors so as not to expose the organization to too much of risk. The study has contributed to the areas of activities to outsourced by services industries and the risk associated with outsourcing for better performance of an organization. Further studies should investigate the comparative analysis of outsourcing activities in the other two link in the value chain of the power sector (generating and transmission).

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