

**International Strategic Management:
Managing & Competing Across Borders**

Competitive Paper

**OFFSHORING OF IT SERVICES:
A SURVEY OF THE LITERATURE AND TOWARDS A NEW RESEARCH AGENDA**

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ABSTRACT

Although international outsourcing or offshoring of information technology services by advanced industrialised countries from less developed countries is a relatively new phenomenon, a plethora of research exists on the subject. And, given the multidisciplinary nature of the subject, the literature on offshoring is often disparate and subject to confusion. This paper surveys the developments in the empirical literature on offshoring over the 1992-2007 period and identifies potential areas for future research. The main findings are that while the intensity of research on the subject has increased rapidly over a short period of time, research efforts to date have focussed mostly on offshoring decision and offshoring management particularly from the perspective of the offshorer. Future research opportunities exist in the area of offshoring strategy and performance relationship, the behaviour and performance of offshore service providers particularly within the context of firms from less developed countries competing globally, and the nature of competition among offshore service providers both within and among countries.

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1. INTRODUCTION

International outsourcing or offshoring is not a new international business activity and has been an integral competitive strategy of manufacturing firms for many years. Offshoring is supply of services from another country either through internal suppliers (international insourcing) or external suppliers (international outsourcing) while outsourcing is supply of services from external suppliers either domestically (domestic outsourcing) or internationally (international outsourcing). However, this paper uses outsourcing and offshoring as interchangeable terms as IT work is generally offshored and there is some overlapping research in these areas. Offshoring allows firms to outsource some of their once in-house activities to foreign providers as a cost saving strategy. The continuous decline in cross border trade barriers over the last two decades and the development of more affordable advanced information and communication technologies have made offshoring in general increasingly feasible and financially viable to a greater number of firms. Offshoring of IT services¹ can be traced back to the mid 1970s when firms in advanced industrialised countries started to outsource some of their IT service needs to comparatively low wage countries. However, the development of the global IT offshoring industry as we know it today is a relatively new phenomenon dating back to the late 1990. Since then, both the intensity and scale of IT services offshoring have grown rapidly to become one of the fastest growing international businesses in the world. The IT service market has been predicted to grow to approximately US\$800 billion by 2009 (Gartner, 2005) with global IT offshoring growing from US\$40 billion in 2004 to over US\$90 billion in 2008 (Nasscom, 2005). The main players on the demand side in the global IT offshoring market include the triad economies which account for 87% of the world market: USA 37%, Western Europe 35.4%, and Japan 14.2% (EITO, 2006). On the supply side or the service provider's side, India and China have emerged as preferred IT offshoring locations among multinationals (Kearney, 2006). Other smaller offshore service providers include Ireland, Israel, Philippines, Malaysia and Russia.

The main purpose of this paper is to survey the literature on offshoring particularly as it relates to IT services and identify gaps for future research. The next section explains the method and data for the study. In section 3 the paper provides an overview of the theoretical underpinnings underlying the offshoring phenomenon.

¹ IT services include software development, system services and broader range of IT supported business services commonly referred to as IT enabled services or BPO services.

Section 4 discusses the empirical studies reviewed. The conclusions and directions for future research are contained in the last section.

2. METHOD AND DATA

A sample of 55 empirical studies conducted during 1992-2007 constitutes the main data for analytical purposes for the paper. The list of studies was compiled after conducting extensive searches using academic research engines such as Proquest and Ebsco Host. Different key words such as outsourcing, offshoring, information technology services, and offshore service providers were used as locators for the studies in the sample. The first round of searches generated in excess of 20 thousand items. After further refining the search by narrowing down the search criteria to include academic publications only since 1992, a sample of 55 studies was compiled. The information in Table 1 summarises some salient features of this sample sorted out by time of publication, publication outlet and the study focus.

Table 1: Salient Features of Offshoring Literature

	1992-1995	1996-1999	2000-2003	2004-2007	Total (%)
A. Publication Outlet *					
Top Journals	1	2	2	3	08 (15)
Highly Regarded	3	6	5	5	19 (34)
Well Regarded	1	0	2	4	07 (13)
Recognised	1	1	5	4	11 (20)
Not Rated	1	1	1	7	10 (18)
Total A (%)	07 (13)	10 (18)	15 (27)	23 (42)	55 (100)
B. Research Focus					
Offshoring Decision	6	6	6	13	31 (43)
Offshoring Management	3	3	6	6	18 (25)
Offshoring Outcome	0	4	5	3	12 (17)
Offshore Service Provider	0	0	2	4	06 (08)
Cross Country Comparisons	0	0	3	1	05 (07)
Total B** (%)	09 (12)	14 (19)	22 (31)	27 (38)	72 (100)

* Journal categorisation based on ASB07 journal ratings from www.harzings.com

** Total for research focus is more than 55 as some studies focus on more than one dimension.

During the 1992 – 2007 period, the intensity of research offshoring published in academic journals has increased steadily and considerably as researchers became increasingly aware of the emerging importance of offshoring. Regarding the focus of studies in the sample, however, the majority of published work to date has focused on offshoring decision (43%) followed by offshoring management (25%). Finally, although research on offshoring has

appeared in all classes of journals considered, more than 60 percent has appeared in top tier journals (15%), highly regarded journals (34%) and well regarded journals (13%). There is visible substantial increase in research volume over time however most of the research is on OS decision followed by OS management and least on OS outcome and OSPs over the period 1992-2007.

3. THEORETICAL UNDERPINNINGS

Research on various aspects of offshoring to date have tended to draw from three broad streams of theoretical literature; namely (1) strategic management, (2) economics and (3) economic sociology.

3.1 Strategic Management Theories

Strategic management theories comprising the resource based view (RBV) of the firm (Barney, 1991; Barney, 1986; Coyne, 1985; Lippman & Rumelt, 1982) and the relational and resource dependence approach (Dyer & Singh, 1998) constitute the two paradigms used to explain offshoring. According to RBV a firm's competitiveness depends on its specific resources and skills which are valuable, rare, imperfectly inimitable and non substitutable. Resources and capabilities are said to be valuable when they help a firm to improve its overall efficiency and performance. They are rare when they are not held by large number of competitors and imitable when the firms not possessing the rare and valuable resources are not able to obtain them. A firm's competitiveness is sustained when there are no other strategically equivalent rare, valuable and non imitable resources available to competitors, i.e., they are non substitutable (Barney, 1991). Thus accordingly, the firm's bundle of unique resources and dynamic capabilities constitute its main source of competitiveness and help the firm to earn above normal profits.

A firm may use offshoring strategically to acquire rare resources in order to fill the gaps between its desired capabilities and its actual capabilities (Cheon et al., 1995). Offshore service providers help their clients avoid competitive disadvantage by freeing them to focus on their core competencies. Evidence of this is apparent from the results of a recent survey (Lewin & Peeters, 2006) where although cost reduction was the main reason for firms to engage in offshoring (97 % of respondents) the strategic objectives such as growth strategy (73%), competitive pressure (71%) and access to qualified staff (70%) were also cited as major factors influencing firms decisions to offshore.

With declining trade barriers and increased mobility of resources across national boundaries, firms have greater access to the global pool of rare resources regardless of their locations. However, Mahanke et al. (2005) have argued that because offshore service providers operate in an open and competitive market, their services are available to all competing firms and therefore offshoring is unlikely to be a source of sustained competitive advantage.

The relational and resource dependence approach (Dyer & Singh, 1998) also provides valuable insights into offshoring where firms engage in offshoring by forming alliances and enter into exchange relationships to acquire rare and inimitable resources. According to Dyer & Singh (1998) inter firm resources and routines may expand beyond the firm's boundaries and become critical sources of competitiveness. They identify four critical elements of inter firm relationships which may constitute sources of competitiveness namely relation specific assets, knowledge sharing routines, complementary resources and capabilities and effective governance. The management of client-vendor relationships and the context under which effective relationships lead to offshoring thus become critical elements for offshoring to succeed. In this context, alliance capitalism or strategic partnerships has been found to be beneficial in cases of very specific purpose collaborative arrangements (Dunning (2000) such as in offshoring of IT services.

Thus, by specialising, firms may enhance and sustain competitive advantage by retaining their core resources and capabilities (RBV) and offshore activities which require non core resources but which constitute core activities for the vendor (OSPs). As a result, the cost structures faced by firms are likely to decline and in a competitive environment cost saving are ultimately passed on to consumers. As such, offshoring has the potential to increase consumer welfare while also increasing productivity and efficiency through greater specialisation.

3.2 Economic Theories

The economics literature treats offshoring strictly from a cost – benefit standpoint. According to the transaction cost theory (TCT) (Coase, 1937; Williamson, 1973; 1989; 1991) minimizing transaction costs is the best strategy for firms and the decision to offshore is based on the economic benefits to the firms from such a strategy. When the transaction costs incurred in offshoring are lower

than the benefits the firm is better off with offshoring whereas when transaction costs are higher than the production costs the firm is better off with internal governance. Clients tend to internalise the service activity in case of higher uncertainty, frequency and asset specificity. TCT has been used widely in empirical research to investigate offshoring decision and offshoring management (Aubert et al., 2004; Carmel & Nicholson, 2005; Murray & Kotabe, 1999; Wang, 2002). This research stream has analysed impact of asset specificity, uncertainty, business & technical skills, frequency of transactions, and post contractual opportunism on various aspects of OS research landscape.

The agency cost theory (Mitnick, 1975; Ross, 1973) highlights the conflicting goals between agent (OSPs) and the principal (clients), and the intrinsic problems in such relations. Offshoring decisions are also based on agency costs namely monitoring costs by the client, bonding costs by the outsourcer and the residual loss to the client. Like TCT, ACT also helps deciding OS decision choice: outsource or to insource, decision depends upon agency costs. The TCT and ACT are based on similar assumptions as to self interest seeking behaviour, goal conflict, bounded rationality, information asymmetry, pre-eminence of efficiency (Eisenhardt, 1989). Risk aversion and information as commodity are additional assumptions underlying ACT (Eisenhardt, 1989). The OS success lies in managing these client vendor relationships through contracts and/or relations. The RBA and TCT are also complementary. The former is the theory of firms earning extra rents and the later is that of its existence (Barney et al., 2001).

3.3 Economic Sociology Theories

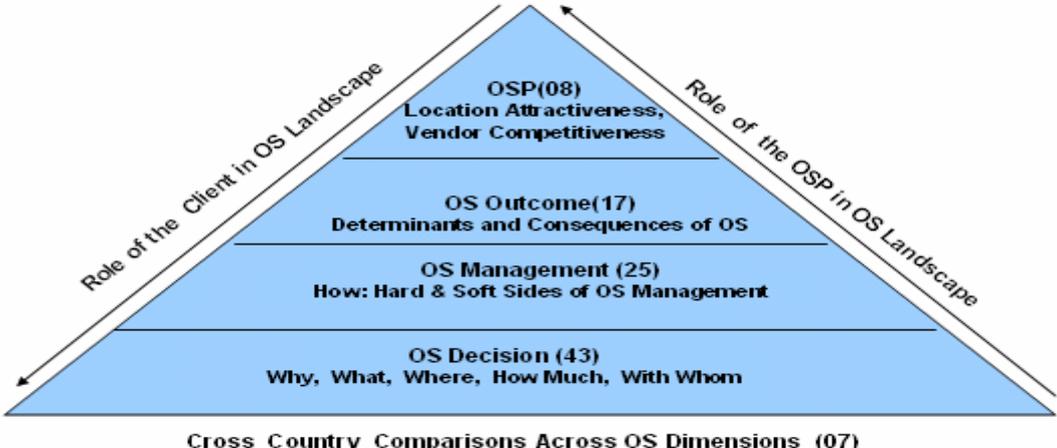
The economic sociology literature (Granovetter, 2005)) asserts that firm's economic behaviour is closely embedded into structures of social relations for three reasons: information, ability to punish or reward and trust. People rely on information from the people they know and not on others and thus social relationships influence the flow and the quality of information. Trust emerges from such relationships and the ability to reward or punish as information comes from the personally known people. However he cautioned that the social relations might be a necessary condition for trust and trustworthy behaviour but are not sufficient to guarantee that (Granovetter, 1985). In the case of future uncertainties, human inability to foresee future, long contracts, and self interest seeking behaviours,

embeddedness may provide competitiveness. OS empirical literature support complementing contract based OS management with relational management (Barthelemy, 2003; Lacity et al., 2004; Poppo & Zenger, 2002; Willcocks & Kern, 1998).

4. EMPIRICAL INVESTIGATIONS

This paper builds on Mahnke et al. (2005) pioneering literature review on outsourcing of IT services to provide a more comprehensive survey of the offshoring literature in three ways: First, the paper extends Mahnke et al. (2005) work to explicitly focus on offshoring of a broader range of IT services and IT enables services; second perspectives of the offshore service provider’s or vendors are taken into consideration and third, the review of literature covers a longer time frame and draws from a larger sample of empirical studies. The paper draws from a sample of 54 empirical studies published between 1992-2007, a period during which offshoring has experienced rapid growth. The studies in the sample were grouped into different categories according to their main focus and generally fall into the following five categories: offshoring decision (OSD), offshoring management (OSM), and offshoring outcomes (OSO) and offshore service providers (OSP). In addition a small number of cross country comparisons on offshoring were also identified (Figure 1). Each of these categories is discussed below.

Figure 1: OS Research Landscape and Client - Vendor Roles



Note: Figures in parenthesis denote proportion of studies undertaken in each dimension during the period 1992-2007

4.1 Offshoring Decision

The decision to offshore is neither a business strategy (Quelin & Duhamel, 2003) nor simply purchase or contract out decision but is a strategic decision to reject internalisation of the activity (Gilley & Rasheed, 2000) and depends upon each firm's unique requirements and circumstances (Grover & Teng, 1992). As such, studies on offshoring decision have been concerned with three main questions.

4.1.1 Why and why not to offshore:

Gaps in capabilities, and the dimension of firm's resources and strategy (strategic management theories) and production costs compared to transaction and agency costs (economic theories) may motivate firms to consider offshoring some of their activities (Cheon et al., 1995). Hence, the motivating factors and barriers to offshoring may be categorised as strategic, financial, environmental and technological.

Strategic motivators may include firm's decisions to concentrate core activities while leaving operational commoditized operations to specialised service providers, liquefying of IT assets and converting fixed overheads into variable overheads. The result is that through offshoring, a firm's resources can be freed allowing thereby allowing it to deploy limited resources on other strategic aspects (McFarlan & Nolan, 1995). Additionally offshoring allows vendors and clients to share business risks (Quelin & Duhamel, 2003), and protect their core assets and capabilities by raising market barriers for them and commoditising the outsourced activities (Levy, 2005). Offshoring also leads to greater flexibility and allows clients to have access to more innovative solutions from specialised OSPs (Quinn, 2000). Competitive pressures from the external markets (Pinnington & Woolcock, 1995) and strong supplier marketing efforts (McFarlan & Nolan, 1995) accompanied by management attitudes and beliefs (Pinnington & Woolcock, 1995) also drive the firms to outsource. However, while attempting to gain strategic benefits, firms may also be exposed to strategic risk like loss of core competencies and critical skills, mismatch of client vendor priorities (Quinn & Hilmer, 1994), loss of know how and innovation capability (Earl, 1996; Hoecht & Trott, 2006), loss of flexibility with outsourcers, and feeling of 'locked in' or 'hostage' or 'dependency' (Antonucci &

Tucker, 1998; Quelin & Duhamel, 2003). Weak management capabilities also act as barrier to outsource (Earl, 1996).

Cost savings have been identified as one of the main motivators for offshoring (Barthelemy & Geyer, 2001; Kakabadse & Kakabadse, 2002). For example in a survey carried in the US and UK in 1996, 85 % of managers interviewed identified cost savings as major motivator for IT outsourcing (Lacity & Willcocks, 1996). And the magnitude of cost savings through outsourcing can also be substantial without affecting the quality of the services rendered. Serapio (2005) found that 44 % of firms in his study realised cost savings of up to 40 % and 50 % of firms rated the productivity and quality of offshore service providers as being almost the same as in the US (Serapio, 2005). Thus, OSPs are able to provide professional services at corporate standards of quality to their clients at lower costs by having leaner overhead structures, using low cost pool of knowledge workers, realising economies of specialization and scale (McFarlan & Nolan, 1995).

Firms also have to routinely face and manage change to their external environment and in some cases resort to offshoring as a response to external pressures. The imitative behaviour of firms (Loh & Venkatraman, 1992) where firms follow their competitors is a good example of how pressure from external sources may change the behaviour of firms. Other changes in the external environment which may motivate firms to offshore IT services include changes in the macro economy, including a country's laws (Apte et al., 1997) and its economic and political landscape (Bahli & Rivard, 2003). Such changes may also act as inhibitors to offshoring if there are uncertainties about the economic, legal and political landscape of in the offshoring location.

Technological motivators include client's failure to meet service standards and IT failures, and access to specialised IT skills of OSPs (McFarlan & Nolan, 1995). Aubert et al. (2004) found a significant positive relationship between the level of technical skills required in performing activities. Difficulties in retaining skilled IT staff and its availability through outsourcing activities are the top motivator found in an Australian survey (Beaumont & Costa, 2002). Though vendors are a good source of technological competencies they could also be a source of potential risks (Antonucci & Tucker, 1998; Jennings, 2002; Quelin & Duhamel, 2003).

Cost savings, focus on core competencies and access to high quality skills are the most cited offshoring motivators (Beaumont & Costa 2002). In a US based survey 67 % of companies were willing to outsource globally if they could realise cost savings (Apte et al., 1997). More recently, research by (Lewin & Peeters, 2006) suggests that 97 % of companies surveyed cite cost reduction as the main reason to outsource followed by growth strategy (73%), competitive pressure (71%) and access to qualified staff (70%). However, research by Espino-Rodríguez & Gil-Padilla, 2005; Loebbecke & Huyskens, 2006 have also failed to establish any significant relationship between offshoring decision and financial factors.

Lacity & Hirschheim (1993) rebuffs three commonly cited outsourcing logics namely that (1) outsourcers are strategic partners, (2) outsourcers are inherently more efficient and (3) outsourcing results in 10 to 50 % cost savings. They termed these as myths on the grounds that the outsourcers do not share profit motive and internal IT departments can also provide cost effective services and savings. Though outsourcing is a well accepted strategy in search of desired objectives its benefits are not necessarily universal to all who undertake such activities.

4.1.2 What and how much to offshore:

“If supplier markets were totally reliable and efficient, rational companies would outsource everything except those special activities in which they could achieve a unique competitive edge i.e. their core competencies” (Quinn & Hilmer, 1994 p.47). As the degree of perfection and reliability vary across offshore service provider and the strategic question which arises is: what functions can the firm offshore and how much to offshore? Strategic offshoring depends on the firm’s competitive edge, transaction costs, its vulnerability, degree of control and flexibility (Quinn & Hilmer, 1994). Activities which are deemed to be core business and are subject to strategic vulnerability may be better produced internally or insourced rather than outsourced. Traditional strategy models suggest that non core activities can be successfully outsourced (Grote & Taube, 2007) while the outsourcing of core activities could be risky as the firms may lose core competencies (Prahalad & Hamel, 1990). Grote & Taube (2007) argue that outsourcing is feasible when organisational proximity is not essential whereas offshoring may be feasible when there are cultural and professional proximities with offshore service

providers. They found that in the case of investment bank research offshoring, only non-core activities such as junior tasks or support type tasks are strong candidates for offshoring. None of the participating banks offshored their main research activities being their core competency. However, outsourcing of core activities could also be good for firms provided the right approach is taken (Baden-Fuller et al., 2000). There can be erosion of core competencies of the firm because of competition, alteration in value chain or development of new technologies, and thus when the core competencies are declining, outsourcing adds value.

The level of outsourcing also depends upon transaction attributes such as the degree of asset specificity, uncertainty and business and IT skills required to perform IT activities adequately. Aubert et al. (2004) found asset specificity, uncertainty and technical skills to be significant in explaining the level of offshoring in IT companies. If more investment in specific assets is required, level of uncertainty is high and more business skills are required, firms may prefer to insource and not to outsource. However greater requirements of IT skills may result in higher degree of outsourcing to leverage specialised IT service providers' knowledge and skills.

4.1.3 From where and with whom to offshore:

The third question which IT firms have to address when considering offshoring relates to the location and choice of offshore service providers. OLI framework for explaining FDI (Dunning, 1980; 1988; 1995; 2000; 2001), addresses the "where" of FDI of MNE activities and, can be applied even to non-FDI based MNE activities such as in offshoring. The location advantages (L) are external to the firm and relate to the geography and location attractiveness (external environment) of particular country and / or region. The importance of the choice of location for offshoring can be further exemplified by the amount of commercially oriented research on the subject by professional consulting firms such as Gartner, AT Kearney, McKinsey, and Forester..

The choice of a particular location and the selection of an appropriate service provider from the chosen location for offshoring purposes is a critical decision as 'one size may not fill all' and the decision depends on many factors such regulatory and political environment, factor endowments such as human capital and infrastructure (Graf & Mudambi, 2005; Kshetri, 2007; Palvia, 2004) cultural

compatibility (Kshetri, 2007; Mol et al., 2004; Palvia, 2004), vendor capabilities (Beulen et al., 2005; Feeny et al., 2005) and nature of services to be outsourced. For example, Ireland is a preferred offshoring destination for high value software services whereas the Philippines is better suited for call centre activities while India caters for low to middle end software and services. Kearney (2004) has devised a location attractiveness index based on a multiplicity of factors including business environment, financial structures and human capital.

Another issue to consider while offshoring is whether the firm should outsource externally to third parties or insource, by setting up its own offshore subsidiaries. Insourcing (IS) by IT firms is preferable when there is high asset specificity and when the firm's IT division is a profit centre (Barthelemy & Geyer, 2005). The choice between insourcing and outsourcing also varies across countries. For example, it has been found that German firms prefer quasi outsourcing whereas French firms prefer outsourcing (Barthelemy & Geyer, 2001) and the difference in strategy has been attributed to the existence of powerful labour unions in Germany. The setting up of subsidiaries may include significant costs of doing business abroad and firms have to undertake cost benefit analyses of offshoring to different locations. Although cost saving is often cited as major driver for services offshoring, firms tend to locate their offshore service facilities in locations where they have greater cultural similarity, and high education levels (Bunyaratavej et al., 2007). Thus, firms may not necessarily outsource to cheapest locations abroad.

Firms tend to offshore as opposed to outsource (domestically) when asset specificity is high, volume uncertainty is low and clients have better coordination capability (Mol et al., 2004). In case of high assets specificity firms may be ready to outsource from any part of the world wherever the specialised services are available. Moving to offshore locations also depends on the stability and consistency of supply of services and service provider's coordination and management capabilities. The selection of an appropriate service provider is critical in order to realise the benefits of offshoring and the relationship between the client and the vendor often goes beyond pure contractual arrangements.

4.2 Offshoring Management

Once the decision to offshore has been taken, the next issue which arises relates to the successful management of offshoring activities. Numerous offshoring management issues need to be considered but the initial ones are related to the nature and form of the vendor/client contract and the management of the offshoring deal through contracts and/or relations or some combination of these. Barthelemy (2003) used the terms 'Hard' and 'Soft' sides for 'development and enforcement of a good contract' and 'development of relationships based on trust' respectively in managing offshoring relationships.

4.2.1 Hard side of offshoring management

Offshoring contracts may take various forms; including fixed price contracts, time and material contracts or incentive based contracts. Fixed price contracts are characterised by fixed fees for the contract with vendor bearing the major risk. For time and material contracts, the vendor charges fee at a certain rate and the client becomes the risk bearer. The choice of the nature of the contract significantly determines the project's profit with the time and material contracts resulting in higher profits to vendors (Gopal et al., 2003). The contract choice depends on the risk associated with the activities under consideration, client knowledge set, bargaining power of parties involved and market conditions. In case of software development which is considered to be more risky, risk averse OSP would prefer time and material contracts than fixed price contracts. However, in general, clients prefer fixed price contract while vendors prefer time and material contract to minimise their risks. The actual decision depends upon their respective bargaining powers and with the size of the vendor and the client and the extent of competition among OSPs bearing significant influence on the nature of the contractual outcome.

By offshoring certain IT activities, it does not necessarily imply that the firm loses its knowledge base for those activities. Client's peripheral knowledge is significant in outcome based formal controls but not on process based controls and help in governance of alliance (Tiwana & Keil, 2007). Clients may still possess and develop peripheral knowledge to better manage offshoring alliance and leave the processing with the service providers to perform them independently. Competitive tendering of contract is also not necessarily cheaper than negotiating pricing and has been

found not to impact on the offshoring outcome which is influenced by contract specifications (Domberger et al., 2000). Repeat contracts are cheaper than initial contracts as there develop interactions, communication and trust between the client and the service provider. Therefore it may be argued that it is not the pricing variation of contract but it is the contract specifications that lead to better offshoring outcome. A detailed contract is also an essential tool to manage effectively the offshoring relationships (Barthelemy, 2001; Lacity & Hirschheim, 1993; Shepherd, 1999; Willcocks & Choi, 1995; Willcocks & Kern, 1998) with short term and detailed contracts leading to higher offshoring success (Lacity & Willcocks, 1998).

4.2.2 Soft side of offshoring management

Undue contractual complexities may also prove counterproductive (Shepherd, 1999) but since contracts can never be complete, there are bound to be future uncertainties which necessitates the role of relationships. Research has also established strong link between partnership quality and offshoring (Grover et al., 1996; Lee, 2001; Lee & Kim, 1999). This legitimises the role of the so called 'soft side' contract based on trust, cooperation and commitment of management to offshoring. Relationship that goes beyond contractual arrangements has been found to be particularly critical in resolving disputes between client and OSPs. Contracts are 'necessary but not sufficient' for the success of offshoring and it is believed that the partnership philosophy is an effective tool for managing offshoring relationships (Elmuti et al., 1998; Grover et al., 1996; Lee, 2001; Lee & Kim, 1999). Both clients and OSPs may gain through partnerships with clients gaining better innovative solutions as relationships help service providers gain a better understanding of their client's business and requirements. Similarly, better relationships may help OSPs in retaining their clients, get referrals to attract new clients, build on their capabilities and competencies. However the extent of client-vendor relationships depends upon the client's needs and purpose of offshoring and the skills and experience of the service provider (Kedia & Lahiri, 2007). Kedia & Lahiri (2007) argue that the intensity of client-vendor relationship increases as they move from cost reduction objective to core competence focus objective and enhance flexibility and risk sharing. The degree of skills and experience of OSPs also influence the degree of

relationships. Clients may not prefer a high intensity relationships with less specialised OSPs as higher degree of relationships involve sharing of clients' critical knowledge as well.

Client-vendor relationships can be also be improved by active participation, better communication and information sharing, and senior management support (Lee & Kim, 1999). As mutual dependency rises and the age of the relationship grows, the partners also need to be careful. In the case of rising dependency, there may be chances of opportunism (Williamson, 1973, 1989) and a clear contract may be helpful in avoiding this. Successful partnership relationships depend on managing knowledge flows, mutual dependencies and organisational linkages (Willcocks & Choi, 1995). Client-vendor relations in offshoring experience additional complexities including cultural incompatibilities at corporate, professional, organisational and national levels (Willcocks & Choi, 1995), an area which has not received much attention in the literature.

4.2.3 Balancing hard and soft side of offshoring management

Balancing the contractual (hard) and relationship (soft) side arrangements in an offshoring venture may lead to effective OS management and thus to OS success. Wang (2002) argues that high mutual dependency created by investments by both the parties result in increased opportunity costs of contract termination for both parties, and thus, reduces the opportunistic behaviour and increases the outsourcing success. As regards the positive effect of degree of uncertainty on the extent opportunism perceived by the client, he argued that this relationship is stronger with a higher degree of asset specificity. Barthelemy (2003) argues that offshoring arrangements that are managed by soft sides do well on performance dimension while those focused on hard side management perform well on cost dimension. Offshoring ventures with a balance of soft and hard side are generally more successful because a good contract provides the basis for the development of trust. Tight contracts may be helpful in the case of commodity type services while relational aspects become important in case of innovative type of services outsourcing (Beaumont & Costa, 2002). Contractual and relational governance complement each other and have positive relationship with exchange performance (Poppo & Zenger, 2002). Effective management of offshoring depends an understanding of the partner's culture (Beaumont & Costa, 2002) and the influence of culture is bidirectional (Nicholson & Sahay,

2001). Clients' understanding of vendors' cultural and political issues may help in better management of the offshoring relationship and vice versa.

4.3 Offshoring Outcomes

It is interesting that despite the tremendous hype in the popular press about offshoring and in particular about its dangers, there is little empirical evidence to support either the benefits or dangers of offshoring at the firm level. The review of the conceptual and theoretical literature on offshoring of IT services point clearly that through specialisation, offshoring has the potential of adding value to the client's activities thereby enhancing its international competitiveness (Bryce & Useem, 1998). However, there is hardly any empirical evidence that Offshoring really adds value to clients in the long run. Investigation of the outcome of offshoring in general has been addressed in a few studies (Gilley & Rasheed, 2000; Gorg & Hanley, 2004; Grover et al., 1996; Kotabe et al., 1998; Murray & Kotabe, 1999) with inconsistent findings. Grover et al (1996) found that that an effective sourcing strategy may lead to improved market performance and argue that core services should be internalised as it gives further innovation and that non core activities be sourced from independent suppliers. Murray & Kotabe (1999) advocate sourcing of none core services from domestic external suppliers to improve market performance. They argued that external sourcing of non core services reduce client's investments and enhance operational flexibility. This finding does not seem to fit to offshoring of IT based services as such services are separable and can be stored, shipped and transferred across national boundaries in real time. Therefore it would be informative to assess whether sourcing strategy of IT based services improve or hamper market performance.

Gorg & Hanley (2004) have found no relationship between offshoring and profitability for services although they established a positive relationship for manufacturing firms. Similarly Gilley & Rasheed (2000) found no direct effect of offshoring on the overall performance of firms and argue that this may be as a result of the overstated benefits of outsourcing. They also refute the commonly held argument that outsourcing may lead to loss of R&D competitiveness. The influence of outsourcing varies for firms operating in different environments following different strategies (Gilley & Rasheed,

2000). Cost leadership firms and innovative differentiators have positive relationship between offshoring and performance particularly in stable environments.

4.4 Offshore Service Provider's Perspectives

Most of the empirical literature to date has tended to focus on the offshoring decision, management and outcome of the client. Research on the offshore service provider is almost non existing despite the fact that the success of the client is intricately linked to the success of the OSP and the behaviour and performance of the OSP is critical to the overall offshoring venture. The success of an offshoring venture depends not only on the client's needs and objectives but also on the vendor (OSPs) capabilities (Feeny et al., 2005) as the OSPs are integral parts of value chain of outsourcers. The clients must ensure that their vendors are growing well (Quinn, 2000). In this respect, issues related to OSPs are an integral part of the offshoring process and need to be understood.

Although parallels can be drawn from the export performance literature (Aaby & Slater, 1989; Chetty & Hamilton, 1993; Katsikeas et al., 2000; La et al., 2005; Zou & Stan, 1998) and competitiveness literature (Dunning, 1988; Porter, 1990), the offshoring of information technology is a recent phenomenon and the nature of the offshoring activities cannot be compared to standard exporting activities. International competitiveness (IC) at the level of the firm, sector and nation has received plenty of attention from researchers over the last 25 years largely because of the rapid growth in cross border merchandise trade over this period as a result of trade liberalisation. Despite being controversial, the debate on the subject has contributed to our understanding of why some firms are successful in international market while others are not, particularly for the manufacturing sector. The implicit assumption that IC of service firms is similar to that of manufacturing firms is misleading (Bunyaratavej et al., 2007; Lindsay et al., 2003). Graf and Mudambi (2005) argue that OSPs are high touch – high tech firms where knowledge professionals play a key role in their competitiveness. Coviello et al. (1997) identify the nature and skill of personnel, contacts and relationships in key markets, the nature of organisational structures and relationships in networks as key determinants of international competitiveness of SME service export firms. Amin and Hagen (1998) found internal organisation of industries such as strategic alliances, cooperate to compete, and good collaborative

relationships with suppliers, technology, quality, and customer satisfaction as highly significant contributors to competitiveness. They also identified employee skills, education system, corporate culture and foreign competition as significant factors of competitiveness.

A few attempts to understand the service providers side has been undertaken at the industry or national level as for India (Arora et al., 2001; Athreye, 2005) , China (Kumar et al., 2005; Qu & Brocklehurst, 2003; Yang et al., 2005) , Russia (Bardhan & Kroll, 2006; Hawk & McHenry, 2005), Ukraine (Zatolyuk & Allgood, 2004), and country comparisons (Chadee & Pang, 2007; McManus & Floyd, 2004). However, there are very few empirical studies that have investigated supply side issues at firm level. Currie (2000) suggests that OSPs may strengthen their strategic positioning by providing a range of services and consolidating their strengths through mergers, acquisitions and joint ventures. Hussey & Jenster (2003) identifies domain knowledge, expectations management, open communication & culture, setting up structures for each contract and relationship management as key issues for service providers. They argue that because service providers deal with different firms from various organisational and national cultures it becomes a challenge to manage all this in a comprehensive way. OSPs may enhance their competitiveness through effective management of people and technology (Shee & Pathak, 2005), knowledge transfer, embeddedness and industry clustering (Dayasindhu, 2002). Innovations are critical for success for knowledge intensive firms that come mainly through human capital and not from R&D investments (Leiponen, 2005). Chadee & Pang (2007) found significant positive relationship between technology strategy and performance of IT service providers. They argued that technology competence of employees also help improve their financial performance as IT service providers with quality people are more flexible and responsive to the changing environment.

Managing relationships with the client is crucial for offshoring success (Oza & Hall, 2005) particularly those involving cultural differences, client expectations and language. Cultural issues identified by Oza and Hall (2005) study of Indian OSPs include religious issues, food habits, the way different people perceive work and interpersonal communication and interpretation skills. Expectation mismatch is another difficulty faced by service providers despite the presence of effective contracts. Service providers find it hard to satisfy the hidden expectations. The other difficulties identified by

Oza and Hall relate to language difficulties, managing transition and lack of client experience. Since the reputation of OSPs has significant impacts on the success of the offshoring venture (Wang, 2002) OSPs need to focus on improving their reputation.

Given that offshoring is a relatively recent phenomenon involving firms from less developed countries quickly becoming global players, an interesting question arises as to how these firms develop and compete in international markets. The literature on international competitiveness to date has tended to focus mostly on manufacturing firms from advanced industrialised countries. Generally, these firms are well endowed in resources and have developed within more or less similar institutional environments. However, firms from developing countries are generally resource poor and their establishment, development and international expansion have taken place within an environment different from those found in western economies. As OSPs are mostly and increasingly from developing countries, opportunities exist for greater enquiry of the sources of their international competitiveness.

5. SUMMARY AND AGENDA FOR FUTURE RESEARCH

Despite the rapid growth in offshoring activities in general and in offshoring of IT services in particular, research on the subject has not kept pace with developments in this rapidly growing international business activity. There has been a significant but asymmetrical research on various aspects of offshoring. Offshoring decision and offshoring management have received particular attention. To date, most research on offshoring is based on the client's perspectives and it is becoming imperative to include the perspectives of the OSPs in offshoring management research as offshoring activities mature and the management of offshoring activities become more complex. OSPs are integral partners in offshoring ventures and as strategic partners, their health is critical to the success of the venture. Based on the review of the empirical studies in this paper, several areas of research are identified.

The first area of research relates to the motivators and barriers to for offshoring. While many of these motivators and barriers have been identified in the literature, there is no empirical investigation of their influence on the offshoring ventures' performance. Which of the motivators

result into benefits in real forms, and to what extent? Which of the barriers are real and how can the associated risks be minimised? How do firms decide on the extent of offshoring activities, from where, and from whom? These are possible questions to investigate.

Substantial research exists in the area of offshoring management through contracts or relationships or a combination of the two. This area of research may be further explored to investigate the implications of incentive and non incentive based contracts, comparison of contract types, how client and OSPs learn during offshoring relationships, what the possible risk factors in such relationships are and how these can be minimised, how and to what extent cross cultural differences influence offshoring management, how local and global players interact and influence each other and the influence of the depth of relationships on effective management of offshoring ventures.

There is also an increasingly pressing need for empirical testing of the impact of offshoring decision variables on firm performance. This area is still neglected and requires more attentions. Questions worth investigating include: How relational and structural embeddedness effect offshoring performance? Does offshoring success vary across cultures or countries and why? Does offshoring enhance or reduce value in the long run? Last but not the least the sources of competitiveness for OSPs need to be explored and tested across countries and cultures.

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