Global Sourcing of Services and Manufacturing Activities: Is It Any Different?

Peter D. Ørberg Jensen & Bent Petersen

Copenhagen Business School
Center for Strategic Management
Frederiksberg, Denmark

International sourcing strategies and operations of firms are usually described distinctively for manufacturing and services. In this conceptual paper we question the strategic relevance of this distinction. As an alternative, we present an activity-based theoretical framework for exploring the linkages between the attributes of the globally sourced activities and the international sourcing strategies and operations of firms. The framework includes three key attributes of the sourced activity: (1) the degree of discretionary judgment allocated to the local operator in carrying out the activity; (2) the degree of site specificity of the assets enabling the local activity; (3) the degree of interdependence between the local operator and the other units of the parent organization in implementing the activity. We argue that these attributes in common, rather than differences between manufacturing and services activities, defines firms’ sourcing is the key determinant of the sourcing process and outcome. Finally, we discuss the implications for research and managers.

1. Introduction

Managers in client and supplier/provider firms are under pressure to adopt global sourcing strategies and operations, but are at the same time challenged by evidence that indicates that many international sourcing operations fail to achieve the expected benefits (see e.g. Kumar et al, 2009; Lacity and Rottman, 2008). The purpose of the paper is to explore the linkages between the nature of different types of activities in the firm value chain and the international sourcing strategies and operations of firms. We take an activity-based perspective on global sourcing (Johnson et al, 2003) and suggest that an enhanced understanding of the specific nature of the activities in the firm value chain can help firms identify more realistic expectations and inform the organization and implementation of international sourcing operations.

The past decade’s international business research on the global sourcing of services is based on the – explicit or implicit – premise that international sourcing of services is different from the earlier waves of manufacturing sourcing. This premise is consistent with a traditional distinction between manufacturing and services activities as two qualitatively different types of activities. In this paper we challenge this premise and
discuss to what extent and how services and manufacturing activities are really different, or whether they share some similarities. We draw on the literatures on international business, innovation, strategy and organization to develop a theoretical framework to define the nature of activities in the firm value chain. In the final part of the paper we discuss the implications for research and the global sourcing strategies of firms and we outline the contents of what we see as a new generation in global sourcing.

We contribute to the international business research literature on global sourcing by taking an integrative approach that builds on extant research and propose a novel perspective on global sourcing strategy and operations. We place the nature of the activity as the unit of analysis and the key determinant of the sourcing process and the outcome and we present a theoretical framework with three different and defining attributes of the activity. This approach is different than mainstream research on global sourcing which mostly remains at the level of the firm and rarely takes a more detailed perspective. Our framework goes beyond the conventional divide between manufacturing and services activities and outlines similarities and differences between various types of services and manufacturing activities. We specifically intend to contribute further to the findings of a number of recent contributions on global sourcing that take their point of departure in the specific value chain activities in question (Jensen, 2009; Karmarkar, 2004; Kumar et al, 2009; Sako, 2006; Stringfellow et al, 2008).

In the sections below we first examine prior contributions in the literatures on strategic management, organization and global sourcing with a particular emphasis on contributions which do take a more detailed perspective on the nature of the activities subjected to foreign sourcing, and which therefore provide the foundation for our arguments. Next, we suggest and outline the proposed theoretical framework with the three activity attributes. In the final section we discuss the implications for research and firm strategy.

2. Theory

2.1. Global sourcing of manufacturing and services

Global sourcing of business activities is addressed throughout the international business literature in the seminal works of Buckley and Casson (1976), Dunning and Lundan (2008), Hennart (1982), Vernon (1966) and Kotabe (1992), as well as in other strands of literature most notably supply chain management (e.g. Trent & Monzcka, 2003, 2005). Despite the classic roots, recent authors have pointed out that there seems to be a shortage of research that seeks to contribute to the development of a coherent theory able to capture recent years’ evolution in global sourcing of business activities (Mol et al, 2005), that there is a need to revisit existing theories of the international business in view of global sourcing (Doh, 2005), and that a framework drawing on many theoretical perspectives is needed to understand global sourcing (Kedia and Lahiri, 2007; Kedia and Mukherjee, 2009; Hansen et al, 2008). International sourcing of various services activities is a more recent phenomenon,
but, as argued by Lewin et al (2009) in particular the foreign sourcing of more advanced, high-value services is presently not well understood (Lewin et al, 2009). Yet in view of the rapid evolution of services offshoring since the late 1990s, Dossani and Kenney (2007) suggest that this business practice will evolve and deepen during the coming decade.

Despite the existence of a substantial body of literature on the subject, several authors have stressed that something “new” is happening, that offshoring is going into its “next” phase (Dossani and Kenney, 2007; Lewin and Peeters, 2006; Manning et al, 2008). This new trend in global sourcing includes that foreign sourcing increasingly encompasses research and innovation activities, design, engineering or similar types of advanced business activities (Lewin and Couto, 2007). This trend is not merely underpinned by lower wages in the destination country, but driven by a different set of strategic drivers, such as a competitive race for talented employees (Lewin et al, 2009), it influences the organizational and geographical configuration of the firm across firm boundaries and national boundaries (Contractor et al, 2010; Mudambi and Tallman, 2010) and it also affects the location choices and patterns for various activities (Demirbag and Glaister, 2010) where, for example, more advanced manufacturing activities are relocated to different destinations than more simple manufacturing activities (Jensen and Pedersen, 2011).

In a review of the literature on the offshoring of services, Jensen (2008) noted that vast majority of journal articles discussed the foreign sourcing of services at a general level of analysis. Only few articles addressed services offshoring at a more specific level where a focus on the activities in question was taken into consideration. In the relatively few cases where journal articles at the time had adopted a more specific focus on the nature and type of business activities, such a focus mainly concerned information technology (IT) but other types of services were not addressed in great detail or not addressed at all. Bearing in mind that the field of IT encompasses a vast subset of different activities with e.g. different levels of complexity, coordination needs between home and offshore teams and other characteristics (which we discuss later in this paper), this leads us to one of the key messages in our paper. We argue that research on global sourcing to a much greater extent needs to adopt a detailed perspective concerning the nature of the business activities – manufacturing as well as services – involved in foreign sourcing operations. We shall elaborate this argument below. Interestingly, this argument seems to be shared in some recently published articles (Doh et al, 2009; Kedia and Mukherjee, 2009; Kumar et al, 2009; Mudambi and Tallman, 2010) whose authors through different approaches analyze and discuss how the characteristics of business activities relate to other variables in global sourcing arrangements.

2.2. Towards and activity-based view on global sourcing

During the past decade especially, a number of scholars in strategic management and organization have argued strongly for the need to change the level of analysis from a “macro-level” to a “micro-level” that takes into consideration the motives and behavior of individuals and the nature and characteristics of activities (Felin and Foss, 2005; Felin and Hesterly, 2007; Foss, 2009; Johnson et al, 2003; Priem and Butler, 2001; Rouse and Daellenbach, 1999; Whittington, 2003). In their introductory article to a special issue on an activity-based view on strategy in the Journal of Management Studies, Johnson et al (2003) have argued for a shift in the strategy debate
towards a micro perspective on strategy. According to the editors of this special issue, this includes an increased emphasis on the detailed processes and practices which constitute the day-to-day activities of organizational life and which relate to strategic outcomes. This activity-based perspective on strategy proposes, first, that value lies increasingly in the micro activities of managers and others in organizations, and second, that a macro-perspective, which the authors see as dominant in the literature, is too remote from the action in organizations. As Johnson et al (2003) note: “Quite simply, a strong instrumental reason for the importance of a more micro activity based view of strategy, therefore, is that managers manage activities” (ibid., p. 5). Foss (2009) presents similar arguments and sees the “macro bias” in strategic management and organization research as problematic because it fails to capture skills, motives and actions at the individual level which shape organizational-level or industry-level outcomes. According to Foss (2009), a more promising research approach is to take a fine grained view on organizations that focus on individuals, including the actions and transactions in which these individuals are involved.

Whereas the above authors do not specifically relate their arguments to the field of global sourcing, we extend the micro-perspective on activities to global sourcing research. However, before we outline our own proposition we highlight key points from previous authors in the strategic management literature and in the global sourcing literature which provide some foundations for an activity-based perspective on global sourcing.

2.3. The nature of activities

For a start, we may use James D. Thompson’s (1967) seminal work to better understand some fundamental distinctions between different activities. Thompson (1967) defined three different technologies – respectively, long-linked, intensive and mediating technology – where each technology is related to different types of activities and rely on different types of interdependencies, which is “... the extent to which the performance and the outcome of one task is affected by, or needs interaction with, the performance and outcome of other tasks.” (Kumar et al, 2009, p. 645). Thompson (1967) distinguished between three types of interdependencies: First, pooled interdependence – here individuals or work units work independently of each other and need not be aware of the other actors performing activities. They exist, operate and create value in themselves. Second, sequential interdependence – here individual work units are directly linked to each other in a linear fashion. Each work unit adds value incrementally to the work in a serial manner. Third, reciprocal; work flows back and forth between two work units, and the work of one unit is continuously dependent on the other unit. For our purpose the two first types of technology appear as the most relevant. Thompson’s definitions were later used by Stabell and Fjeldstad (1998) to construct separate models for value-creation in firms and here Stabell and Fjeldstad (1998) use the different technologies to denote the characteristics of, respectively, manufacturing and services firms and activities within these firms. Long-linked technology is the assembly-line, highly codified work process in manufacturing firms, or, as Thompson wrote:

“A long-linked technology involves serial interdependence in the sense that act Z can be performed only after successful completion of act Y, which in turn rests on act X, and so on. The original symbol of technical rationality, the mass production assembly line, is of this long-linked nature. It approaches instru-
mental perfection when it produces a single kind of standard product, repetitively and at a constant rate” (Thompson, 1967, p. xx)

Intensive technology is fundamentally different and, according to Stabell and Fjeldstad (1998), may be used to describe a certain type of service activities. Intensive technology is characterized by a high level of uncertainty about how best to produce intended outcomes. The problem-solving process in value shops is iterative and cyclical with a high degree of reciprocal interdependence between activities, since the perception of the problem and adequate solutions influence each other and may well change along the way. Examples include work done in hospitals, educational institutions and professional services firms in medicine, law, IT, architecture, engineering and hospitals. In Thompson’s description:

“The intensive technology is most dramatically illustrated by the general hospital. At any moment an emergency admission may require some combination of dietary, x-ray, laboratory, and housekeeping or hotel services, occupational therapies, social work services, and spiritual or religious services. Which of these, and when, can be determined only from evidence about the state of the patient. (...) The intensive technology is a custom technology. Its successful employment rests in part on the availability of all the capacities potentially needed, but equally on the appropriate custom combination of selected capacities as required by the individual case or project” (Thompson, 1967, p. xx).

Therefore, an important distinction between long-linked and intensive technology is that the content and configuration of the outcome (i.e. either a tangible product or an intangible solution) is known from the beginning in processes relying on long-linked technology whereas it is not known, or known only in rudimentary form, in intensive technology processes.

Interestingly, however, and central to the purpose of this paper, is that this seemingly clear distinction between manufacturing and services activities appears to be changing. This influences the viability of the global sourcing strategies of firms. In economics, products are tangible and storable items and in accordance with Thompson’s (1967) long-linked technology, they can be manufactured efficiently with standardization and automation processes. By contrast, services are traditionally conceptualized as intangible, non-storable, and co-produced with customers with instant consumption, which traditionally has made standardization and automation of service delivery difficult. According to Sako (2006), however, such definitions do no longer apply to all firm activities across sectors. This is because any firm in the economy is now likely to have a combination of products and service activities. As Sako (2006) describes it: “This hybrid is on the rise owing to the phenomena of ‘productizing’ services and ‘servicizing’ products” (p. 509). Due to the advances in information technology, services are becoming more like manufacturing as processes can be standardized and data stored (a similar point is made by Karmarkar; 2004). On the other hand, “servicizing” of manufacturing activities appear where firms are offering services which are complementary to the products firms sell, in the form of e.g. after-sales maintenance, or systems integration solutions (Sako, 2006, p. 510). According to these authors, the important distinguishing feature of an activity is therefore not whether it belongs to the categories of manufacturing or services activities, but lies elsewhere. Sako (2006) sees the main distinctions as whether the execution of an activity requires low-skilled or high-skilled labour and whether that activity is standardized or customized. For services, Karmarkar (2004) also stresses the key distinction between
standardized vs. customized services and furthermore notes the distinction between “simple” and “complex” processes. Importantly, such features have strategic implications: “The strategies that service organizations select will depend on the work they do and whom they serve” (Karmarkar, 2004, p. dd).

In a recent article, Stringfellow, Teagarden and Nie (2008) have presented a theoretical model of the creation of the “invisible” costs of foreign sourcing, in which the nature of the sourced activities is a key determinant. The authors’ key argument is that there must be a fit between the attributes of the offshored activity and the attributes of the offshore location in order to realize intended benefits. Conversely, if there is a mismatch between the two types of determinants, then the intended benefits are unlikely to materialize. The authors’ framework captures the nature of different services, the work process and different dimensions of the distance between the onshore and offshore locations. Stringfellow et al (2008) argue that the influence of these factors, and the linkages between them, determine the “invisible” costs of offshoring services. Invisible costs include a range of costs such as replacing the customers who reduce or stop their purchases from firms that use foreign service providers, and costs that are caused by the unique characteristics of services. The latter stem from the fact that services often come with a high degree of intangible components with tacit knowledge embedded, require interaction with the customer and different agents in the firm, or in the partnering firm, which may be located onshore and offshore.

Such definitions underpin the conceptual model by Stringfellow et al (2008). Central to their model is a theoretical construct labeled as “interaction intensity”. Building on Thompson’s (1967) definitions of long-linked technology and intensive technology combined, interaction intensity means the degree to which customers interact with services providers. This is determined by, respectively, the content of the service and the process. Content refers to what is offered, either tangible (a hamburger, a report), or intangible (advice, IT services) services. The essence of this model is that there must be a fit between the attributes of the offshored activity and the offshore location in order to realize intended cost savings, and hence also to make offshoring operations profitable and ensure high quality output. The point made by Stringfellow et al (2008) concerning the need for a fit between these factors is an important foundation for our framework. However, bearing in mind the arguments by Sako (2006) regarding the blurring boundaries between manufacturing and services we see the interaction intensity construct and the importance of fit as points that relate not merely to services but also to manufacturing activities.

3. Attributes of Strategic Sourcing

Following the activity-based view on strategy described earlier we suggest that the nature of the activities in foreign sourcing is a key determinant of how foreign sourcing operations and workflow should be organized in order to achieve a successful long-term outcome in the home firm. By placing the nature of the activity as the key determinant, we also propose that it is less important to categorize an activity as manufacturing or service and that certain activities have shared attributes that make the manufacturing-service distinction less relevant for global sourcing research and practice. We further propose that three attributes of the activity, and the combination of these attributes, shape the specific nature of an activity. These attributes are, first, the degree of exploration on the part of the home firm combined with the discretio-
nary judgment allocated to host firms; second, the degree of specificity and irreversibility of the activity; and third, the degree of interdependence between home and host firms in the implementation of the activity.

3.1. Degree of exploration and discretionary judgment allocated to host firms

March’s (1991) influential distinction between exploration and exploitation in organizational learning is also relevant for our purpose. March (1991) defines exploration as: “search, risk taking, experimentation, play, flexibility, discovery and innovation”, and exploitation as: “refinement, choice, production, efficiency, selection, implementation and execution” (March, 1991, p. 71). While each of the two constructs represents different strategies for the acquisition and use of knowledge/capabilities, they are also highly complementary. Thus, as March (1991) notes, it is necessary to have an appropriate balance between the two elements. Too much exploration without exploitation leads to high costs of experimentation without reaping the subsequent benefits; conversely, exploitation without exploration leads the organization to a suboptimal equilibrium (March, 1991, p. 71). March (1991) further argues that an organization should not seek to establish full standardization of its processes, but leave room for exploration, since it will foster innovation (a similar point was made later by Nonaka, 1994). March’s distinction between the dimensions of exploration and exploitation is central here because it is connected to the home firm’s underpinning motives for global sourcing. The exploration-exploitation distinction is a recurrent theme in literature strands that are related to the topic of this paper, albeit under slightly different terms. Notably, there seems to be an increased emphasis on the exploration dimension relative to exploitation as firms’ global sourcing strategies and operations evolve into new forms.

First, a similar discussion exists in the field of R&D internationalization. Gammeltoft (2006) summarizes these different approaches when he describes a “traditional view” versus a “new view” as regards R&D internationalization. The traditional view, dominating until the late 1970s, describes the R&D activities of MNCs as mainly located in the home base. R&D outside the home base predominantly consists of minor, local adaptations connected with sales and production in the foreign markets. The new view emphasises the ways in which knowledge and innovation processes are becoming increasingly globally polycentric, i.e. where the R&D located outside the Triad (i.e. US, EU, Japan) is no longer merely local adaptation but a wider range or R&D activities including some high-value R&D functions. Based on studies of foreign direct investments in the pharmaceutical and electronics industries, Kuemmerle (1999) identified two strategies for R&D investments at foreign locations. In a home-base exploiting strategy, firms seek to exploit specific capabilities of the host country. In this situation, as firms become aware of differences in local needs and local demand becomes more advanced, local R&D partners may help the firm to adapt existing products. In contrast, the main driver of a home-base augmenting strategy is the firm’s need to knowledge that is not location-specific.

Second, within the innovation literature Archibugi and Iammarino (1999) have argued that MNCs tend to move beyond the international exploitation of nationally produced innovations to also engage in global generation of innovation and techno-scientific collaborations. Similar to Kuemmerle (1999), Archibugi and Iammarino (1999) argue
that firms seek to augment their knowledge capability, and will seek this knowledge wherever it is best created. Other authors within the innovation literature describe global and “open” sourcing of knowledge as an increasingly important competitive strategy for modern firms (Cantwell 2003; Chesbrough 2003a, 2003b, 2006; Christensen 2006; Laursen and Salter 2006). An open innovation strategy implies that firms recognize that knowledge is distributed globally and possessed by a range of public and private agents with whom firms must seek to collaborate because it is financially and practically difficult, even for large MNCs, to possess cutting-edge knowledge and capabilities in every field. One implication is that the home firm will seek to develop an extensive collaboration with the partnering firm/institution in order to explore and benefit from strategically important partner capabilities. An open innovation strategy differs from a more traditional strategy which emphasizes control and protection of firm specific capabilities above other priorities. Hence, partnerships with other firms will also be less extensive.

Certain tasks have a low degree of codification and therefore necessitate that the staff in the destination firm is able to exercise independent judgment in the execution of the tasks based on their educational background and professional experience. This is particularly the case for activities relying on intensive technology where the understanding of problems and solutions are defined and redefined throughout the iterative and co-evolutionary work process. Such activities are expert knowledge activities where full responsibility of the problem definition and activity execution is given to individuals/units who possess knowledge and skills at a high level. At the other end of the spectrum, activities that are sourced to the host firm with a precise and detailed set of specifications demand a much lower degree of independent judgment and decision-making on the part of the host firm. Such activities include basic, assembly-line activities with little or no demand for host firm staff to exercise judgment. A type of activity, which we may call rule-based activities, also requires a limited need for independent judgment, albeit it is slightly higher than the basic activities. Such activities are found e.g. in customer service centres where front level personnel try to solve customer problems based on manuals and standard operating procedures. In other words the definitions of problems as well as solutions are predefined and rely on routines. In such organizations complications occur when a customer problem has a unique character and does not fit into the pre-defined categories and hence are difficult to solve with pre-defined solutions. These situations require a much higher degree of knowledge and independent judgment, but often such organizations are ill equipped to tackle the problems and there is a mismatch between the nature of the problem (unique) and the applied solution (standardized).

Embedded in this dimension is also the level of managerial control applied by the home firm in the day-to-day operations of the host firm. To illustrate the variance involved, an extremely high level of discretion delegated to the host firm would represent a management-by-objectives approach where the home firm upfront would define the problem to be solved but would leave it to the host firm to decide how to solve the problem and which output/solution would be the best to solve the problem at hand. Moreover, this could even include a breakdown and detailing of the problem due to the nature of the problem-solving process in intensive technology processes. In contrast, the other end of the continuum would signify a model where the home firm maintains full control of operational management (e.g. through expatriate managers stationed at the premises of the host firm) and with great detail makes all management decisions which are then implemented by host firm staff.
3.2. Degree of specificity and irreversibility of the activity

To what extent an activity is ‘strategic’ or ‘operational’ very much depends on the degree of reversibility of the invested assets. Strategy is essentially about irreversible decisions (Ghemawat, 1991) - to what extent an investment is sunk (Baumol and Willig, 1981). What interests us in a sourcing context, however, is the extent to which the local assets are location-specific. If the assets enabling the local activity can be redeployed elsewhere at low costs then the sourcing decision is more operational than strategic. The standard example is the sourcing of cheap labor employed in footloose textile and garment factories (Gereffi and Memedovic, 2003). These “screw driver” factories are designed for cost-less dismantling in case the local factor costs rise (or favorable trade agreements expire) and makes relocation pertinent.

Williamsonian transaction cost economics puts another label - namely site-specificity - on basically the same phenomenon, (Williamson, 1983). Site specificity is one out of several types of asset specificity and usually connected to natural resources. However, other types of asset specificity, such as human asset specificity and dedicated asset specificity (Williamson 1983) are likely to increase the site-specificity as well inasmuch as the assets are rather immobile and rare. Williamson’s definition of specificity revolves around the extent to which the assets that enable the transactions in question can be employed in other relationships with the same payoff. If the site-specificity of the local operator is high the implication is that the assets of the operator are rendered useless in case the exchange partner (the foreign buyer, client) terminates the relationship. This type of specificity was described by Alfred Marshall (1890) in his seminal article on the hold-up phenomenon. In Marshall’s classical case example a steel mill is located next to a power plant in a remote and isolated part of the country. The steel mill is movable only at great costs and completely dependent on the delivery of electricity from the power plant – which is the only adjacent supplier. Hence, the steel mill cannot operate profitably if the power plant raises the price on electricity (exploiting its monopoly). In other words, the site specificity of the steel mill renders it vulnerable to a hold-up (Williamson, 1983) by the exchange partner - the power plant owners. In TCE the degree of reversibility is measured in terms of the quasi-rent, i.e. the difference between the first and second best use of the assets. The second best use of the steel mill assets – namely steel production based on expensive power supplies from a remote power plant - is considerable worse than the best. An alternative calculation of the degree of site specificity is to measure the switching or relocation costs, that is, the costs of relocating the assets (Kogut and Kulatilaka, 1994). Using Marshall’s power plant – steel mill example, the measurement would be the costs of relocating the steel mill to a power plant that does not hold a monopoly position.

3.3. Degree of interdependence between home and host firms in the implementation of the activity

For this third element in the framework we mainly build on the framework outlined by Kumar et al (2009). Global sourcing can be examined at two levels, respectively the strategic and the operational level. At the operational level, Kumar et al (2009) argue that companies have retreated from offshoring due to lack of efficient implementation on the operational level. That is, after the strategic decisions have been made, the operational problems and costs of work transfer and interaction communication and
coordination outweigh the forecast savings and benefits foreseen at the strategic level. For managers, the problem lies in management expertise on an operational level. Building on Thompson (1967), Van de Ven et al (1976) and other contributions in the organization literature, Kumar et al (2009) see the degree and type of inter-task interdependence as a key operational determinant of intersite interaction and communications in offshoring. It follows that the greater the interdependence, the greater the amount of communication and coordination effort required, the greater the chance of breakdown and the greater the likelihood of loss of control, especially when tasks are located across global distances.

Kumar et al (2009) extend extant theory with three types of interdependence in order to better understand and manage task interdependence. First, integration interdependence, which adds on Thompson’s (1967) and Van de Ven’s (1976) scale of interdependence intensity. Kumar et al (2009) position this between sequential and reciprocal interdependence. Integration interdependence is characterized by the overall task being subdivided and with different actors working separately, but in parallel. This creates a need for continuous fit or integration process in order to acquire value as a whole. Second, hand-offs, which illustrates the existence of an interface when work segments are handed off to actors performing parallel tasks and when outcomes are delivered to the fitting or integration process. Hand-off functions as a foundation for the interaction between sequential and reciprocal interdependence. It is therefore necessary to differentiate between tasks requiring minimal hand-off efforts and hand-offs requiring high levels of information sharing and knowledge exchange. Third, stickiness, where the authors distinguish between normal, non-sticky tasks such as routine and standardized work, and sticky forms of task interdependence. The degree of stickiness in information and knowledge transfer depends on the characteristics of the sender, the receiver, the organizational context of information transfer and the content of the information. Transfer stickiness will be high “...for large volumes of tacit, ambiguous, equivocal, uncertain and complex tasks” (Kumar et al, 2009, p. 655).

We find that these constructs form a more elaborate understanding of what is included under the distinction between relatively simple activities vs. relatively advanced activities in global sourcing which we touched upon earlier. It follows that the advanced activities are characterized by a high level of integration interdependence, they require significant hand-off efforts to transfer information and knowledge, and they contain a high degree of sticky information and knowledge. Managers can apply a range of techniques to ease such transfers, simply interfaces and make sticky information and knowledge more transparent and accessible (see Grant et al, 2000, for an overview of such techniques) which helps turn advanced activities into more simple activities over time (a process sometimes referred to as commoditization). However, because an advanced activity at that point in time is driven by an exploration motive it comes with such attributes because it is positioned at the front end of known knowledge or in the borderland between known and not yet known knowledge.

The three dimensions – degree of discretionary judgment, site specificity, and interdependency - are summarized in Figure 1. Visually, the three dimensions together form two triangles: The inner triangle (the shadowed area) represents lower degrees of discretionary judgment, site specificity, and interdependency; the outer triangle higher degrees. Operational sourcing – “old generation sourcing” - is contained in the inner triangle, whereas strategic sourcing – “new generation sourcing” - fill out the
4. Discussion and Conclusion

4.1. Some implications of an activity-based view on global sourcing

In addition to the activity-based framework described above we also propose that while the foreign sourcing operation may be regarded as an outcome of strategy (or if not a comprehensive strategy then at least strategic decisions, see Heijmen et al, 2008, for a discussion), the nature of the activity in foreign sourcing also has strategic implications that follow in the wake of implementing sourcing operations.

So, what are the implications of an activity-based view on global sourcing, and how might it evolve in future years? Inspired by Kakabadse and Kakabadse’s (2000) argument a decade ago that a new outsourcing paradigm is emerging, we pursue this line of thinking and suggest that it may be beneficial to consider a new generation of global sourcing of manufacturing and services activities. Based on the framework outlined earlier we find that the pertinent distinction for global sourcing operations in modern organizations has less to do with a categorization of activities as services or manufacturing but primarily relates to whether the activities are relatively simple and routinized (i.e. the basic and rules-based activities described above) or relatively advanced and high-value (i.e. activities that require discretionary judgment, have a high degree of site specificity, and are highly interdependent). A new generation of global sourcing is related to similar terms used by several authors to describe recent years’ trend in global sourcing (e.g. Bryson, 2007; Dossani and Kenney, 2007; Lewin and Couto, 2007; Manning et al, 2008). It fundamentally assumes that the foreign sourcing of more advanced activities is the manifest action which is related to a coherent set of interrelated elements. It is, so to speak, the tip of the iceberg where the foreign sourcing of advanced business activities is the only part visible, but is one part of an underlying greater whole.

Kakabadse and Kakabadse (2000) argued that a “new outsourcing paradigm” was emerging and they outlined what they saw as the characteristics of this paradigm. They observed that companies by means of outsourcing are rapidly ‘devolving’ from self-contained, vertically integrated organizations to more virtual entities that rely on business partners to fulfil major parts of their supply and value chain requirements. This effort to externalize and become an extended enterprise bears remarkable resemblance to the Japanese keiretsu model. They argued that as a consequence Western managers need to move from arm’s length business relationships towards long-term, collaborative, strategic partnerships with external business partners. They concluded that some organizations have purposely started building integrated value chains with their suppliers and electronic trading communities and as a result, “outsourcing has become a lever of business transformation and new organizational forms exemplified by joint venture spin-offs and shared service consortia where the

outer space. In reality, it is not always either-or. It is a continuum and sourcing of some activities may have both high and low degrees on the three axes.

*** INSERT FIGURE 1 ABOUT HERE ***
focus is on competing for value and not effectiveness in the back office” (Kakabadse and Kakabadse, 2000, p. 716).

In keeping with the points made by Kakabadse and Kakabadse (2000), we outline some central parts of a new generation of global sourcing in the following. First, compared to Kakabadse and Kakabadse (2000) whose discussion evolved around the ownership dimension (the make-or-buy decision), a new generation of global sourcing logically must have the cross-border transfer of business processes as the focal point. Table 1 below summarizes the characteristics of an “old” generation of global sourcing and compares with the suggested “new” generation of global sourcing of advanced activities within manufacturing and services. We compare the two generations regarding their implications for firm strategy, organization, and business linkages in the following.

4.2. Implications for firm strategy

A main responsibility for top management is to formulate firm strategy, set the performance targets accordingly and ensure strategy execution. As noted by Mintzberg and Waters (1985) this is the deliberate strategy (closely related to a classic scientific management perspective) as opposed to the emergent strategy, which occurs over time as “a pattern in a stream of decisions” (Mintzberg and Waters, 1985, p. 257). In the new generation of global sourcing such important tasks still prevail but the management role is complemented with additional challenges. When activities are advanced, creative and innovative, hard to codify and rely on a high level of tacit knowledge, reciprocities between the different stakeholders (experts, managers, clients/end-users) are needed in the implementation process to achieve the best result. To make this process succeed, communication, integration and coordination of the resources in the network are required to ensure that the parties involved, and located in different countries, act in a coherent way. Mastering such activities will be a central competence for managers in order to create competitive advantages through advanced services offshoring. Jensen (2009) observed that experiences from the foreign sourcing process had a catalytic effect on the strategic learning of home firms that eye new business opportunities as foreign sourcing operations evolved. This strategic change in the home firms followed the pattern of an emergent strategy described by Mintzberg and Waters (1985) where firms embark on the offshoring collaboration with one set of strategic intentions, but these intentions are sufficiently flexible to adapt to the learning that occurs along the way and new strategic motives are added.

The notion of value creation logic mentioned in Table 1 is taken from Stabell and Fjeldstad’s (1998) proposition for a theory on value creation in firms. Using this line of thinking, the understanding of a new generation of offshoring goes beyond the “old” generation’s logic of specialization and optimization through disaggregation of the activities in the firm’s value chain: The logic in the new generation is to create value from knowledge exploration and reengineering of the value chain across borders to establish an integrated global value chain. We agree with the argument made earlier by Doz et al. (2001) that in the future competitive advantage will not arise from cross-
ing borders in search of lower factor costs. Rather, it will come from transcending national boundaries to identify and mobilize critical knowledge, technology, market intelligence and capabilities scattered around the world.

As shown in numerous studies, the primary incentive for foreign sourcing of the old generation of sourcing is cost-seeking. In the new generation, the primary incentive for the offshoring firm is different. Cost advantages are still important, but the predominant motive for offshoring firms is to improve competitiveness through access to different types of knowledge and skills located elsewhere than in the home country. Jensen and Pedersen (2010) show that while the cost saving motive drives a firm’s offshoring of less advanced tasks (which are mainly related to unskilled, labour-intensive processes), experienced and knowledge-intensive firms offshore more advanced tasks because they seek more knowledge abroad. These firms follow a different strategy as they seem to offshore advanced tasks for the purpose of making broader and deeper use of their global knowledge network, as they use offshoring to tap into sources of new knowledge or large pools of talented people abroad.

The findings presented by Maskell et al. (2007) portray foreign sourcing as a dynamic process where experience is a key determinant in firms’ offshoring decisions and behavior and where the classic cost-saving offshoring strategy is complemented or even superseded by other strategic motives. Precisely because of this dynamic process, the “new” generation perspective on global will not totally replace the “old” generation perspective. The two will continue to coexist, as there seems little doubt that, in many cases, firms will continue to engage initially in offshoring due to the expected cost advantages. This is particular the case for some basic and routinized activities. But once firms have started the learning process, the offshoring experience they gain may function as a bridge they can use to cross the line between the “old” and the “new” offshoring generation. In line with the findings of Maskell et al (2007) and Carmel and Agarwal (2002), we suggest that experience will be the key determinant that enables firms to transcend the old generation of foreign sourcing and change strategy and practice towards the new generation of foreign sourcing.

4.3. Organizational implications

The main difference between the old and new generation of foreign sourcing concerning the organization of the firm lies in the firm’s configuration of its global value chain. While neither foreign sourcing of advanced business activities nor foreign sourcing in general is confined to MNCs, different organizational models of the MNC in the international business literature are helpful as one explanation of the link between offshoring and firm organization. A traditional model of the organization of the MNC is the “multi-domestic MNC” (Bartlett and Ghoshal, 1998) which implies a dispersed value chain, where the foreign subsidiaries are mini-replicas of the parent firm (see also e.g. Pearlmutter, 1969, who refers to this model as the “ethnocentric” MNC). In contrast, the concentrated value chain configuration (Porter, 1986) is driven by the fundamental idea to build critical mass and specialization in regional, or global, clusters, e.g. with “centres of excellence” in the firm or shared services centres. This configuration of the global value chain is also connected to a network-based view of the MNC where there is a more equal, and hence more complex, balance of power and division of responsibilities between the parent company and foreign subsidiaries. The international business literature refers to this organizational model with different constructs, such as the network-based MNC (Forsgren et al., 2005; Nohria and Ghoshal, 2000).
shal, 1997), the MNC heterarchy (Hedlund, 1986), the meta-national MNC (Doz et al., 2001) or the transnational MNC (Bartlett and Ghoshal, 1998). For the new generation of foreign sourcing, the point is that when MNCs change their global organization from the multi-domestic model to the transnational (or any similar) model, offshoring of company functions becomes a product of this organizational change. Our research with firms from Denmark and other countries during a number of years suggest that this trend of change towards the concentrated value chain configuration is underpinning a significant portion of the cross-border relocation of value chain functions (see also Beugelsdijk et al, 2009), and for more advanced activities the data indicate that the desire to create global or regional clusters/centres with critical mass and specialized know-how is an important driver in this respect.

4.4. Implications for inter-firm linkages

The change in inter-firm linkages included in the new generation of offshoring may be characterized by two related dimensions, respectively the nature of the business linkage and the degree of power asymmetry.

While the old foreign sourcing generation’s business linkage between client and supplier/service provider is the arm’s length principle, the new foreign sourcing generation entails a different type of linkage with increased partnership between the two parties, where the supplier/service provider gets deeper involved in the client organization, which could also imply some level of formal or de facto integration between the client and the service provider. The new model for client/service provider business linkage is labelled the “extended organization” by Kakabadse and Kakabadse (2000) or the “extended enterprise” by Aron and Singh (2005), and both terms essentially cover the same elements.

As a consequence of the change from the arm’s length principle to partnership, the power relations change accordingly. In their theory of the governance in global value chains, Gereffi et al. (2005) present five different models of the relationship between the clients and the suppliers/service providers in global production networks. In each model, the degree of power asymmetry between client and supplier/service provider is different and is used to characterize the relationship and the relative influence of each party. In line with this thinking, the old generation of global sourcing has a high degree of power asymmetry, meaning that the power in the relationship is unequally distributed and clearly rests with the client. In contrast, the new generation of global sourcing has a much lower degree of power asymmetry, meaning that power is more equally distributed between the client and the service provider. The value of the partnership in the new generation of offshoring is very much due to the nature of that relationship as a non-zero-sum-game, with a resulting flow of important synergies. Turning the relationship into a zero-sum-game would be a loss for both parties.

We suggest that an activity-based view on global sourcing implies that the characteristics of the activities exchanged (low degree of codification, high degree of tacit knowledge) and a work process relying on intensive technology (Kumar et al, 2009; Stringfellow et al, 2008; Thompson, 1967) increase the complexity of managing the process. As a consequence the power distribution and the governance of the business linkage between the home and host units differ from those related to the foreign sourcing of less advanced activities and match the relational model as described by Dyer and Singh (1998) and Gereffi et al (2005). The complex exchange of tasks be-
tween clients and foreign suppliers/service providers opens the relationship to a bar-
gaining process since the client firm’s critical resources increasingly span firm 
boundaries and become embedded in inter-firm resources and routines. This contrib-
utes to the equalization of power between the two firms. Notably, while power in the 
literature on global value chains above all appears to be rooted in the firm size of the 
dominant firm in the chain, this is not always the case in the new generation of global 
sourcing. Instead the key to power in these relationships lies elsewhere, such as the 
capabilities possessed by each firm and the potential strategic advantages each firm 
might gain from a continued cooperation.

4.5. Implications for international business research

In this paper we have advocated for a more detailed perspective on the attributes of 
the specific value chain activity. The intention is to contribute to the development of 
an activity-based perspective on global sourcing and thus advance a better scholarly 
and managerial understanding of the activities involved in global sourcing and the 
related global sourcing strategies and operations. We suggest that this more fine-
grained distinction of the nature of offshored activities is needed because it is an im-
portant determinant of the success or failure of foreign sourcing operations. Based on 
the three-dimensional framework we argue that the important distinction between 
various types of activities in global sourcing lies not between manufacturing and ser-
dvices activities, but may be found in the three dimensions of the framework.

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6. Author Address

Peter D. Ørberg Jensen, PhD, Assistant Professor
Center for Strategic Management and Globalization
Copenhagen Business School
Porcelaenshaven 24
Email: poe.smg@cbs.dk
Telephone: +45 3815 2658
Fax: +45 3815 3035
2000 Frederiksberg
Denmark

and

Bent Petersen, PhD, Professor
Center for Strategic Management and Globalization
Copenhagen Business School
Porcelaenshaven 24
Email: bp.smg@cbs.dk
Telephone: +45 3815 2510
Fax: +45 3815 3035
2000 Frederiksberg
Denmark

We do not want our paper published as a working paper
Figure 1: Three dimensions of Strategic Sourcing

Degree of Discretionary Judgment

Operational Sourcing ("Old Generation")

Strategic Sourcing ("New Generation")

Degree of interdependency

Degree of Site Specificity
### Table 1: From an “Old” Generation of Global Sourcing to a “New” Generation of Global Sourcing of Advanced Business Activities

<table>
<thead>
<tr>
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<th>&quot;Old Generation Offshoring&quot;</th>
<th>&quot;New Generation Offshoring&quot;</th>
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<tr>
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<td>Strategy formulation, planning and setting of performance targets</td>
<td>Communication, team and process integration and coordination at international/global level</td>
</tr>
<tr>
<td><strong>Value creation logic</strong></td>
<td>Specialization and optimization through disaggregation of the value chain</td>
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</tr>
<tr>
<td><strong>Primary strategic driver of offshoring</strong></td>
<td>Competitiveness through cost reduction</td>
<td>Competitiveness through knowledge and skill seeking across borders</td>
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<td><strong>Organizational Implications:</strong></td>
<td></td>
<td></td>
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<td><strong>Global firm value chain configuration</strong></td>
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<td><strong>Level of global integration</strong></td>
<td>The multi-domestic MNC with relatively little global integration</td>
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<td><strong>Implications for inter-firm linkages:</strong></td>
<td></td>
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<tr>
<td><strong>Type of business linkage</strong></td>
<td>Arms length</td>
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<td><strong>Degree of power asymmetry</strong></td>
<td>High degree: Lead firm dominates</td>
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