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Global marketing and procurement of industrial products: Institutional design of interfirm functional tasks

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Abstract

Marketing and procuring component parts in the global marketplace can pose such significant trading hazards that industrial transactions often must be embedded in protective governance. This article identifies key forces influencing the institutional designs that best safeguard exchanges between international trading partners for such industrial tasks as the design, fabrication and delivery of component parts. The effectiveness of designs such as market contracting, alliances, and international joint ventures are shown to be a consequence of the transactional characteristics of a given task, the governance risks experienced by both buyer and supplier, and the differences between the institutional environments of the partners' countries. In addition to a comprehensive institutional design model, several propositions are developed to serve as a guide to future empirical research in the areas of global industrial marketing and procurement.

Keywords: Global marketing; Industrial procurement; Governance; Institutional design

1. Introduction

In a global business-to-business setting, original equipment manufacturers (OEMs) rely on international networks of suppliers to furnish key component parts (Bello & Zhu, 2006). For each of these components, crucial functional tasks such as design, fabrication, and delivery are required prior to assembly of the finished product at an OEM's factory (see Fig. 1). OEM's face the classic "make or buy" decision regarding each task since designing, fabricating, and delivering components can be performed in-house or outsourced to upstream suppliers. For any given component part, an OEM may arrive at a unique institutional arrangement for each task: design may be outsourced, fabrication performed in-house, and JIT delivery to final assembly performed by a trusted third-party logistics provider (3PL). Hence, tasks such as designing and fabricating parts can be managed using alternative institutional designs or governance mechanisms ranging from simple market contracting to vertically integrated ownership (Carson, Devinney, Dowling, & John, 1999). Between market contracting and ownership are a variety of intermediate (i.e., hybrid) governance institutions employing social–relational elements such as partnerships, alliances, and joint ventures that can be used to organize the conduct of interfirm tasks.

Analysts (Bello, Lohtia, & Dant, 1999) recognize that several strategic, production and transaction cost factors affect institutional designs, and Williamson (1985) in particular details the dominant role played by important exchange attributes in determining organizational form. In spite of this rich literature, several gaps remain. First, researchers tend to examine governance issues from either the industrial supplier or buyer's perspective. Scant studies have employed a comprehensive approach to the transacting hazards and governance risks experienced by both industrial buyers and suppliers. Second, the level of aggregation for studies of organizational form often occurs at the firm-level rather than at the task-level. A focus on tasks permits a more fine-grained analysis of institutional design at a fundamental level of organizational structure. Third, the range of design options considered in many studies is limited to a simple choice between outsourcing or in-house production. Often ignored is the rich set of intermediate design options that reflect unique hybrid combinations of markets and hierarchies. Finally, an overwhelming majority of studies are conducted in

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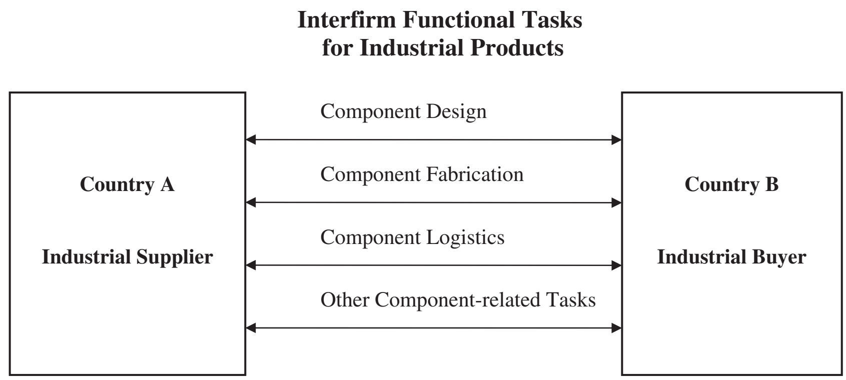

Fig. 1. Interfirm functional tasks: Global marketing and procurement of industrial products.

domestic settings. Cross-border, macro-environmental forces that may weaken and otherwise interfere with industrial governance arrangements between global trading partners have been given little attention.

The purpose of this article is to specify the design of institutional arrangements for interfirm functional tasks associated with marketing and procurement of industrial products in a global business-to-business context. Fig. 2 introduces a model detailing the connections between transactional characteristics of a functional task, governance risks for both the buyer and supplier, and the impact of institutional environmental differences between international markets. The article makes three contributions to our understanding of global industrial buyer–seller relationships. First, the source of governance risks involved in industrial component transactions is identified as flowing from key characteristics of the interfirm functional task. Based on transaction cost theory, three exchange attributes (i.e., asset specificity, uncertainty, and performance ambiguity) of a given component-related task are demonstrated to be the foundation of governance difficulties. Second, industrial buyer's and supplier's negotiation preferences for a particular governance arrangement are shown to be driven by the governance risks experienced by each party. Different combinations of risk allocation drive the particular governance preferences for a given task. Third, environmental differences between the partners' home countries are shown to condition the preferences of the trading partners for institutional arrangements. Regulatory, normative, and cultural differences are identified as strengthening or weakening the preferences of partners for particular institutional solutions to governance problems.

The article proceeds by analyzing various institutional arrangements for interfirm functional tasks involved in global industrial markets, exchange attributes in terms of governance risks, and implications for a task's institutional design across focal interdependent dyads as well as external operating environments. Three propositions are developed to summarize the theory presented and to serve as a guide to future empirical research in the area of global industrial marketing and procurement.

2. Institutional arrangements for interfirm functional tasks

Defined as rules of exchange, institutional arrangements (IAs) are the specific forms of governance through which global exchange partners manage cross-border, buyer–supplier relationships to perform component-related tasks. As the organizational form governing the conduct of a task "an IA can consist of various formal and informal components and will possess contractual, ownership, and social characteristics" (Carson et

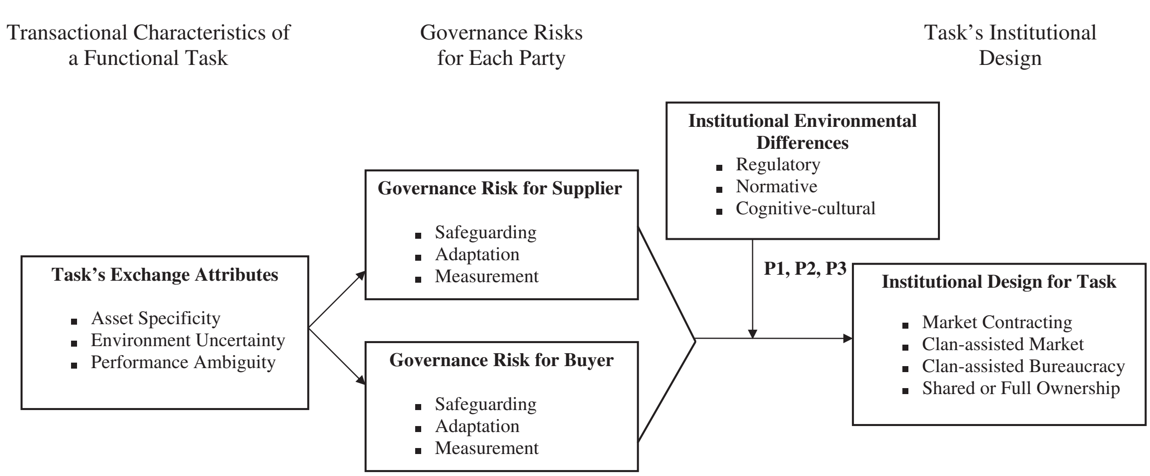

Fig. 2. Institutional design for an interfirm functional task: Global marketing and procurement of industrial products.