Supply chain integration and shareholder value: Evidence from consortium based industry exchanges

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Abstract

Recent trade and academic literature point to the importance of supply chain integration among partners as a key determinant of value creation. This paper analyzes the shareholder value effects of setting up industry exchanges, a prominent mechanism used to achieve supply chain integration. Shareholder value effects are estimated by measuring the stock market reaction (abnormal returns) associated with announcements to form or join industry exchanges. We find that abnormal returns from participation in industry exchanges are positive but only marginally significant in the whole sample of 144 firms in 18 exchanges formed during 2000–2001. In the sub-sample of 88 exchange founders who were part of the original announcements to form the exchange, the abnormal market reaction is about 1% and significant. We also find that firms with greater bargaining power and higher process efficiency benefit more from participation in industry exchanges.

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1. Introduction

Recent practitioner and academic literature (Magretta, 1998; Sahin and Robinson, 2005; Watson and Zheng, 2005; Kulp et al., 2004; Frohlich, 2002; Frohlich and Westbrook, 2001; Cua et al., 2001), emphasize the role of supply chain integration among partners as an important determinant of value creation. Higher levels of product variety, global marketplaces, shorter product life cycles, and the demand for better customer service have significantly increased the need for integration with supply chain partners. At the same time, firms are outsourcing more activities and developing long-term relationships with a stable set of partners who perform critical functions such as component design, manufacture, assembly, and distribution (Parker and Anderson, 2002). Recent technological innovations have also facilitated the use of the Internet to support inter-firm business processes. Consequently, the dominant belief is that the most successful companies are “those that have carefully linked their internal processes to external suppliers and customers in unique supply chains” (Frohlich and Westbrook, 2001, pp. 185).

To facilitate the integration of supply chains among many firms within an industry, the last few years have witnessed the creation of several consortium based, business-to-business (B2B), industry-specific electronic exchanges (we henceforth refer to them as industry exchanges). Unlike public exchanges that are third party operated and owned, industry exchanges are set up by the trading partners themselves, with typically one or
two dominant exchanges in each industry. Further, unlike other Internet-based business models based on the matching and aggregation of buyers and sellers, the primary purpose of industry exchanges is to facilitate the integration of supply chain related business processes among existing trading partners (Christiaanse, 2005). Table 1 summarizes the prominent industry exchanges set-up in the US during 2000–2001, the primary years when such industry exchanges were established in various industries.

As a mechanism to achieve supply chain integration, industry exchanges have many advantages. The exchange founders listed in Table 1 demonstrate that industry exchanges are usually set-up either by a few prominent buyers (e.g. the Covisint exchange in the auto industry) or a few prominent sellers (e.g. the Healthcare Exchange for hospital supplies). Consequently, they have instant buy-in from the major industry players and have the potential to achieve critical volume of transactions rapidly. Further, the exchange makes it less expensive to participate, as proprietary one-to-one links between partners are replaced with a single, less expensive connection to the industry exchange (Christiaanse, 2005). The
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