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The role of organizational control in outsourcing practices: An empirical study

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ABSTRACT

Recent case study research has examined the role of organization control as a critical component of outsourcing performance (Kang et al. 2012a. Journal of Business Research 65, 1195–1201). In contrast to case study methodology, this paper aims to empirically examine the relationships among outsourcing strategies and organizational control in the Chinese context and refine the theoretical and managerial implications of the current research model. Based on data collected from 158 firms operating in China, this paper examines the impact of two types of outsourcing strategies on different organizational control measures. Our findings suggest that for efficiency-seeking outsourcing, output control and process control are appropriate in creating successful outsourcing practices. As for innovation-seeking outsourcing, social control and process control are the most effective options. Theoretical and managerial implications for strategic outsourcing are also discussed.

1. Introduction

Applying proper organizational control mechanisms is essential for achieving effective inter-firm cooperation as well as for achieving intended organizational goals (Hartmann et al., 2008; Senja and Mika, 2009). Outsourcing literature has suggested that a lack of effective control over suppliers presents a crucial risk factor that may result in less than desirable outsourcing outcomes (Harland et al., 2005; Kotabe et al., 2008; Quinn and Hillmer, 1995). Organizational control as a useful governance mechanism can reduce serious outsourcing failures.

However, little research has been conducted on how firms apply organizational control in conjunction with their outsourcing strategies. Kang et al. (2012a) presented a conceptual model of organizational control. Based on case studies of five foreign manufacturing firms operating in China, Kang's research examined the relationships among outsourcing strategies, organizational control, and outsourcing performance. However, the validity and applicability of various control mechanisms require further empirical examination in larger contexts. As an extension of previous research, this paper aims to investigate how outsourcing strategies are associated with the choice of organizational control mechanisms. Our findings present a unique contribution to the organizational control literature and outsourcing theory, and illustrate that specific types of organizational control are necessary for the effective operation of both efficiency-seeking outsourcing and innovation-seeking outsourcing. By focusing on the outsourcing operations of Chinese companies, this study provides important insight into the effective use of organizational control when implementing different outsourcing strategies, and also expands understanding of the role of formal control and social control in China outsourcing practices.

2. Theoretical background and hypothesis

2.1. Outsourcing strategies

As a result of (a) the wide application of information and communication technologies, (b) the availability of global logistics, and (c) the implementation of lean management practices, firms have achieved a great deal of process rationalization, task simplification, and parts standardization. Thus, firms have achieved drastic cost reductions in their respective supply chains. Consequently, firms have deployed outsourcing arrangements in their vast arrays of business processes. More specifically, firms transfer

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non-core activities to external organizations that possess the required levels of expertise and economies of scale in order to achieve operational efficiency and cost reduction goals (Jiang et al., 2006; Kotabe and Murray, 2004). This outsourcing evolution has been the primary focus of the early period of outsourcing, which emphasized efficiency through the division of work between different firms (Hatonen and Eriksson, 2009).

In response to Prahalad and Hamel's core competence theory, which was popular in the 1990s, firms have implemented outsourcing strategies not merely as a cost reduction tool but also as a strategic initiative for securing core competitiveness (Freytag and Kirk, 2003; Kang et al., 2009; Kremic et al., 2006; Quinn, 1999). In a rapidly changing market environment, no firm can realistically expect to compete against global competitors relying exclusively on its internal capabilities. As a result, firms have expanded the scope of their outsourcing to include their key traditional functional cores (e.g., R&D, product design, and marketing) (Chen et al., 2011; Gottfredson et al., 2005; Kaipia and Tanskanen, 2003; Marshall et al., 2007). The strategic intent of outsourcing is to secure and deploy multiple competitive advantages (e.g., cost reductions, innovativeness, and flexibility) in a turbulent market environment (Kremic et al., 2006; Quinn, 1999). As the scope of outsourcing has expanded to include globally networked economies, it has become crucial for firms to achieve cost efficiencies and/or operational efficiencies and to tap into a broad set of innovation capabilities.

Based on traditional outsourcing models and recent strategic outsourcing goals, Kang et al. (2012a) classified outsourcing strategies into two primary categories: (a) efficiency-seeking outsourcing strategies and (b) innovation-seeking outsourcing strategies. Using these outsourcing strategies, firms are not only able to transfer their non-core activities to specialized external experts to achieve efficiency (Harland et al., 2005; Kotabe et al., 2008), but they also try to build their innovation capabilities through inter-organizational collaboration (Chen et al., 2011; Hsuan and Mahnke, 2011; Marshall et al., 2007). Thus, strategic outsourcing goals include seeking efficiency and building innovation capabilities. In this study, outsourcing strategies (efficiency-seeking or innovation-seeking) are presented as strategic goals of outsourcing practices. Efficiency-seeking outsourcing strategies are defined as the extent of management's intent to achieve productivity and cost reduction goals by transferring normal organizational processes and routine activities to external suppliers. On the other hand, innovation-seeking outsourcing strategies are defined as the extent of management's intent to build innovative capabilities by transferring novel and customized activities to external suppliers. Table 1 summarizes the essential aspects of these two types of outsourcing strategies.

Table 1
Characteristics of outsourcing strategies.

	Efficiency-seeking outsourcing	Innovation-seeking outsourcing
Demand	Predictable	Unpredictable
Task characteristic	Routine, Standardized	Novel, Customized
Driving factors	Low cost, consistent quality, on-time delivery	Flexibility, variety, top quality
Uncertainty	Low	High
Output and process measurability	High	Relative low
Knowledge intensity	Low	High
Strategic position	Low cost based	Differentiation based

2.2. Organizational control

The strategic objective of firms that employ organizational control mechanisms in a highly uncertain business environment is to minimize potential risk factors (Han et al., 2008) and achieve intended organizational goals. The broad topic of organizational control has been widely investigated by a variety of business scholars. For example, marketing scholars have examined the influence of control on individual responses and the performance of marketing units (Jaworski, 1988), the antecedents of control selections (Lam and Chua, 2009), the effect of combined controls on the responses of marketing managers (Lam and Chua, 2009), and sales force evaluation based on control usage (Lu et al., 2006; Tan, 2001). Strategic management literature has considered organizational control as a means of achieving organizational goals by building inter-firm cooperation. This cooperation can be established by building strategic alliances (Han et al., 2008; Rooney and Cuganesan, 2009), establishing international joint ventures (Chen et al., 2009; Ebben and Johnson, 2005; Kavcic and Tavcar, 2008), and understanding the effects of organizational control on knowledge management (Turner and Makhija, 2006). Management scholars have noted the importance of using organizational control in intra-employee and inter-firm relationships to achieve organizational goals. Proper organizational control is one of the most important processes in maintaining and developing inter-firm and intra-firm collaboration.

Organizational control research has found that a well-combined set of organizational controls is more effective than using a single type of organizational control (Chen et al., 2009; Das and Teng, 1998; Jaworski et al., 1993; Ouchi, 1979). Outstanding firms apply both formal control (i.e., output control and process control) and informal control (i.e., social control) practices to achieve organizational effectiveness (Chen et al., 2009; Das and Teng, 2001b; Ouchi, 1979). Each control type features a different management focus and different measures through which firms can influence their partners to behave according to their specific requirements and thus achieve organizational goals. Table 2 shows the characteristics of three types of organizational control.

2.3. Outsourcing strategies and organizational control

Proper organizational control measures are necessary in order to implement outsourcing strategies effectively (Chen et al., 2009). Likewise, implementing outsourcing strategies successfully requires a suitable choice of organizational control strategy. An efficiency-seeking outsourcing strategy emphasizes routine and standardized activities with high measurability of outsourcing output. Control scholars have stressed that output control is available when the measurability of outcome is high; thus, output control is a useful option for effectively implementing an efficiency-seeking outsourcing strategy (Das and Teng, 2001b; Eisenhardt, 1985; Ouchi and Maguire, 1975). In order to clarify efficiency-seeking outsourcing outcome

Table 2
Characteristics of output, process and social control.

	Control focus	Control measures
Output control	Final outcomes	Clear goals, specification of outcome requirement, incentives
Process control	Behaviors during the process	Inspection, specified procedures, roles, job descriptions, reporting process
Social control	Personal interaction	Share of value and beliefs, social interaction, communication