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The impact of management capability on the resource–performance linkage: Examining Indian outsourcing providers[☆]

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ABSTRACT

The increase in offshore outsourcing of information technology-enabled business processes has renewed scholarly attention to better understand the dynamics of service provider firms. In this study, we examine how offshore outsourcing service providers' internal and relational resources and capabilities jointly predict their economic performance. Analysis of data collected from a sample of 105 Indian service providers suggest that rent generation from firm-specific, idiosyncratic resources is positively moderated by the level of management capability possessed by such firms. Theoretical and managerial implications of the findings are discussed and avenues of future research are offered.

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1. Introduction

Offshore outsourcing occurs when firms hand over their value chain activities to foreign, independent service providers (Bunyaratavej, Hahn, & Doh, 2008; Doh, 2005). Research delving into the intricacies of this phenomenon stress that offshore service providers are important ally in the value creation mechanism (Kedia & Mukherjee, 2009; Zaheer, Lamin, & Subramani, 2009) and that success of offshore outsourcing is largely contingent on their performance. Very little attention, however, has been accorded to understand the context of offshore service providers (Lahiri & Kedia, 2009; Zaheer et al., 2009). In particular, research focusing on their internal assets and overall performance has remained inadequate so far. In this paper, we attempt to examine the empirical linkages among provider firm-specific resources, capabilities, and performance, and shed light on the competitive dynamics of Indian offshoring service providers.

Resource-based view (RBV) of the firm suggests that ability to attain higher performance is determined by the nature of strategic resources possessed and utilized by firms (Barney, 1991; Wernerfelt, 1984). Extending this view to the current context suggests that performance of offshore outsourcing provider firms should be a function of various strategic resources that are possessed and deployed by these firms. Indeed, several firm-specific resources, such as human capital, organizational capital, client-provider partnership quality etc., have been highlighted in the literature as crucial determinants of provider firm performance (Feeny, Lacity, & Willcocks, 2005; Lahiri & Kedia, 2009). These resources, in addition to being possessed, need to be strategically deployed and leveraged (Sirmon, Gove, & Hitt, 2008; Sirmon & Hitt, 2003) by firms in order to generate superior performance and competitive advantage. More specifically, while a provider firm's idiosyncratic resources and innovative knowledge assets may contribute to its performance (He & Wang, 2009), such resources must be managed and deployed effectively to realize competitive advantage. International business (IB) and strategic management scholars have called for studies that identify firm-level capabilities needed to effectively manage various organizational resources (Manning, Lewin, & Massini, 2008; Sirmon, Hitt, & Ireland, 2007). In responding to such calls, this study intends to fill an important research void by exploring the moderating influences of *management capability* on the degree to which firm-specific resources are able to contribute to firm performance. We propose that improving provider performance through rent generating resources requires an emphasis on management capability, defined as the ability to assemble, integrate, and deploy various firm-specific resources, in particular human, organizational and relational, to fulfill diverse client-related business requirements (Lahiri & Kedia, 2009).

We studied 105 Indian business process offshoring (BPO) service provider firms to examine our central research question. Empirically, we showed that performance effects of two firm-level resources (human capital and organizational capital), and one

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relational resource (partnership quality) improve in the presence of a firm level capability (management capability). The Indian BPO industry presented a perfect setting for our investigation for several compelling reasons. First, India remains the top choice among various offshoring destinations for western client firms (Luo, Zheng, & Jayaraman, 2010; Zaheer et al., 2009). Findings from this setting are thus likely to have crucial impact on the offshore outsourcing clients and providers from other emerging countries. Second, Indian BPO industry has evolved from low-value added services (e.g., call centers) to high-value added knowledge-based services. This helps to examine the research question across a broad range of high-value business processes. Finally, as one of the world's largest and most dynamic economies, India-based studies add value to our overall understanding of the global business environment (Lahiri, in press; Malik & Kotabe, 2009).

This analysis contributes to the growing body of offshore outsourcing literature and focus attention on the relatively under-explored Indian BPO industry that caters to more than 35% of the global BPO market and has been growing at the rate of more than 35% per annum for the last several years (Nasscom-Everest Study, 2008). Our empirical analysis of the providers' context and the resultant findings generate important theoretical and practical insights that add to the scholarship that focuses on the performance implications of valuable firm assets. We also contribute by enhancing the applicability of RBV in a new industry and its participating firms. Furthermore, we respond to calls in the resource-based literature to illuminate how organizational capabilities may moderate the resource attributes to generate improved performance (Priem & Butler, 2001; Sirmon et al., 2008) for offshore outsourcing providers. Finally, by focusing on offshore service providers we enrich the IB literature since performance dynamics of these emerging market firms may determine the viability of offshore outsourcing of IT-enabled business processes as a strategic tool. Indirectly, our analysis also sheds light on the central question in IB—what determines the international success and failure of (offshore outsourcing client) firms? (Peng, 2004).

2. Offshore outsourcing of information technology enabled business processes: role of service providers

Business processes are 'actions that firms engage in to accomplish some business purpose or objective. Thus, business processes can be thought of as the routines or activities that a firm develops in order to get something done.....' (Ray, Barney, & Muhanna, 2004, p.24). When clients engage in BPO they essentially disaggregate their firms' value chain and hand over parts thereof to providers for successful execution and delivery of the executed processes. Although cost savings remain the major inspiration for initiation of BPO moves, other advantages accrue to the clients as well e.g., increased focus on core business activities, added flexibility of business operations, greater risk spreading, and reduced time to market (Kedia & Mukherjee, 2009; Luo et al., 2010). Most recent estimate suggests that global market for BPO may reach US $975 billion by 2012 (BPO Watch, 2008).

To effectively partake in the rapidly growing market, BPO providers continue to offer a wide variety of value-added services using expertise arising from and embedded in different internal assets. In the process they generate revenues, learning and increased competitiveness (Budhwar, Luthar, & Bhatnagar, 2006; Feeny et al., 2005). The role of providers becomes crucial owing to several unique features of BPO as a strategic business practice. First, conceptualizing and handling intricacies related to transition, management, execution and delivery of business processes is complex than dealing with migrated discreet activities as in traditional outsourcing. Second, BPO requires significant amount of *domain knowledge* than managing routinely outsourced activities that are more repetitive in nature. Domain knowledge refers to information and skill-sets associated with distinct processes such as banking, capital market or mortgage that enable providers to cater to specific client needs. Third, handling BPO contracts requires greater amount of *industry expertise* than other forms of outsourcing. This entails thorough understanding of the requirements and challenges of different industries (often called "verticals") in which clients operate. Finally, BPO contracts generally tend to be long-term in nature than in traditional offshore outsourcing contracts requiring business partners to remain focused on building and sustaining value creating relationships (Lahiri & Kedia, 2009).

In summary, we suggest that offshore outsourcing of IT enabled business processes is relatively more complex and greater partnership-focused than other forms of offshoring (e.g., standardized IT), and requires greater dependence on the performance of providers in fulfilling various business expectations of clients. Consequently, the role of different internal and relational firm assets are more pronounced in BPO than in other forms of offshore outsourcing. In the next section we offer theoretical justification for this study's constructs and develop our hypotheses.

3. Theoretical background

Inherent in BPO partnerships is clients' dependence on the expertise of providers and the latter's ability to utilize such expertise in providing valuable services to the former (Kedia & Lahiri, 2007; Sen & Shiel, 2006). Although business expectations of clients and providers vary, the source of success for both partners hinge on the providers' resource-base and how expertise arising from such resource-base is suitably utilized. In this context, RBV seems to be the appropriate theoretical perspective to explain and justify the various constructs used in this study. According to RBV, firms are viewed as portfolio of distinctive resources and capabilities. RBV assumes that firms are fundamentally heterogeneous in resources and capabilities and when resources are not perfectly mobile across firms, heterogeneity can be sustained (Barney, 1991; Wernerfelt, 1984). A resource is an "asset or input to production (tangible or intangible) that an organization owns, controls or has access to on a semi-permanent basis" and organizational capability "refers to the ability of an organization to perform a coordinated set of tasks, utilizing organizational resources, for the purpose of achieving a particular end result" (Helfat & Peteraf, 2003, p. 999).

Resources and capabilities form the basis of firm's improved performance and competitive advantage when they are valuable and rare. RBV further postulates that firms can obtain sustained competitive advantage over rivals when their assets are inimitable and non-substitutable in addition to being valuable and rare. By utilizing useful assets, firms capitalize on environmental opportunities and neutralize threats that exist, and are able to obtain competitive edge over those firms that do not possess similar resources or are unable to capitalize on them. RBV-based examination of resources, capabilities and superior firm performance has impacted scholarship in various disciplines including strategy and IB (Barney, Wright, & Ketchen, 2001; Newbert, 2007; Peng, 2004).

Although some scholars often use *resources* and *capabilities* synonymously, theoretically they are different. The former is relatively independent, simple and static, while the latter is collective, complex and dynamic. Related business literature suggests that dynamic capabilities are definite strategic and organizational processes that create value for firms by altering firm resources into new rent-creating resources in changing environments (Eisenhardt & Martin, 2000). More formally, dynamic