Development of Outsourcing in Network Structure Design

This article explores inter-firm cooperation relationship with downscaling and cooperative outsourcing, and its impact on the network structures formation taking advantage of the organization’s core competencies, knowledge, innovation, and entries to new markets. Outsourcing deals with labor division, control or coordination choices, also the levels of trust, reciprocity and commitment.

Keywords: outsourcing, network structure, core competence.

Introduction

We didn’t sew the clothes we are wearing, nor did we grow the food we eat. We also didn’t manufacture our car, or perform dentistry. In other words, we outsource in our personal life. But if we tried to produce personally all or most of what our families consume, we would face a poor standard of living. A. Smith (1994 [1776 first]), the patriarch of economics, recognized this lesson two centuries ago, writing, “it is the maxim of every prudent master of a family never to attempt to make at home what it will cost him more to make than to buy.”

Modern technological developments have opened the door to outsourcing of an unprecedented type and scale. It conjures up images of low-paid workers from India taking service jobs from U.S. or European workers in a wide range of decently paid occupations: accounting departments, software maintenance and so on.

Outsourcing researches focus their interest only on some aspects of the overall outsourcing. In-depth studies have been proposed regarding economical and financial aspects, giving great attention to cost analysis, especially concerning hidden costs and moral hazards (Fill, Visser, 2000).

Sonata STANIULIENĖ – PhD, assoc. professor at the Faculty of Economics and Management, Vytautas Magnus University, Lithuania. Address: S. Daukanto St. 28, Kaunas, Lithuania. Tel.: +370 37327856. E-mail: s.staniuliene@evf.vdu.lt
In other cases, the problem has been faced from the strategic viewpoint, emphasizing risks and advantages which can arise from the practice of outsourcing, and highlighting the importance of contract management (Zhu et al., 2001). We face the lack of studies relied on the structure aspect of the outsourcing development, so it is this paper’s object.

Studying the process of network structures development in the world business, the aim of this paper purposefully was set as – to analyze the development of outsourcing in network structure design.

The theme is important to the further development of network structures’ theory. With reference to the performed analysis of today’s business conditions (for more look at Staniulienė, 2005), it was suggested the following sequence of modern networking organizational structures projects, where organization managers should design inter-organizational networks and form the flat organization hierarchy rejecting the activities of noncore competencies in the first pace.

Development of outsourcing, determining the efficient boundaries of organizations

R. Coase (1937) first tackled the question similar to A. Smith’s: if an organization can buy a certain good or service from outside the organization at a lower cost and at least the same level of quality, then it should buy; if not, then it should make.

However, the definitions display some different partial aspects, since the propositions made by the authors are based on the purpose of their research. Thus, we can classify the definitions into three types: (1) those considering that outsourcing entail a stable, long-term collaboration agreement in which the supplier becomes a strategic partner and where there are exchange relations with independent organizations; (2) those definitions that indicate the type of activity or service that can be outsourced, i.e. activities and services that are not strategic for the organization; (3) those definitions that consider that outsourcing is an action that transfers planning, responsibility, knowledge and administration of activities, all through contracts (Greaver, 1999).

The review of the different works revealed that most authors agree that outsourcing means going outside the organization to acquire determined activities that are not processed internally.

Organizations make choices about the types of employment systems they use to allocate work. Some place reliance on internalized arrangements based on long-term commitments and the utilization of bureaucratic employment practices while others draw more heavily on externalized forms of employment incorporating outsourcing and other market-based practices (Kinnie, 2001). Since the mid of 80s there has been a discernible shift towards the externalization of employment in the form of outsourcing and the subcontracting of work (Lepak et al., 2003).

The first focus has been on determining the efficient boundaries of organizations. Outsourcing decision is usually analyzed as a “make or buy” dilemma. On the one hand, following the initial contribution by R. Coase seventy years ago, market imperfections such as measurement problems and difficulties to control the collaboration between the customer and the provider, increase the complexity in arm’s-length contracts and favor the “make” option. On the other hand, there are other arguments that favor the “buy” option. Among them,
cost reduction is very commonly considered one of the main reasons to justify outsourcing strategies. Besides, specialized providers can be more efficient than vertically integrated organizations not only for scale economies but, also due to other efficiency advantages as those related to knowledge or flexibility.

A second focus has been on how patterns of transactional or embedded relationships between organizations affect organization performance (Gilley, Greer, Rasheed, 2004) and organization-level learning (Matusik, Hill, 1998). These studies have shown that organizations benefit from outsourcing peripheral activities when they operate in dynamic environments (Matusik, Hill, 1998). More importantly, embedded relationships among contracting parties often allow superior knowledge transfer and trustworthy exchanges, which lead to higher organization performance (Uzzi, 1997). The effective management of information processes across inter- and intra-organizational boundaries is extremely challenging as a result of several factors: volatility in customer requirements and external market conditions, lack of suitable infrastructure, information security, and the lack of common standards or processes to facilitate seamless knowledge transfer.

Keeping such functions external can be vital for organizations with highly competitive market niches, requiring frequent product improvements, where rationalizations of scope and scale are a routine component of strategy-making (Suarez-Villa, Fischer, 1995). Increasing the specialization by outsourcing of less essential functions can also provide greater internal flexibility, allowing management and production to become more focused in areas of greater priority (Suarez-Villa, Karlsson, 1996).

Downsizing has been one of the most prevalent business trends of the past two decades. Achieving greater specialization, targeting market niches more competitively, increasing productivity, and developing continuous streams of innovations are considered to have been some of the more important benefits of reduced size (Acs, Audretsch, 1993). The term downscaling may perhaps be more representative of the kinds of transformations that have accompanied reduced size, such as the redefinition of scope, the targeting for continuous innovation, the development of new trans-active relationships with suppliers, or the participatory engagement of labor in production. Scope reductions through outsourcing may allow a more effective use of resources, if savings can be redeployed to enhance the organization's internal advantages. Segmenting operations into smaller units or subsidiaries can also result in downscaling, inducing greater specialization, more autonomy and operational flexibility. Changes in the intra-corporate division of labor allow the segmented operations to deepen their innovative capabilities (Susman, 1992). Although the segmentation of large organizations has provided many benefits, it can be argued that outsourcing among independent or partner organizations has been the more important source of downscaling. In many cases cooperative outsourcing has helped to keep small organizations small, by allowing high quality and specialized operations to remain independent and external.

Outsourcing also provides organizations with greater flexibility in the deployment of resources in the face of rapidly changing technologies and increasing complexity of product development.
We have come to believe that bureaucracy is bad and flexibility is good. And so it follows that a company that invests in as little as possible will be more responsive to a changing marketplace and more likely to attain global competitive advantage.

Several macroeconomic factors, including globalization, competitive pressures, and the need to leverage availability of the talent pool across national boundaries led to the emergence of outsourcing as an important vehicle for plants to contract their business processes to external providers.

Worldsourcing, as global outsourcing, is benefiting a number of developing and transition economies and also fundamentally changing the structure of organizations. Some economies have recorded local improvements in living standards by supplying the industrial world with products and services that are no longer profitable in high cost labor economies. Current trends are for organizations in industrial countries to move from outsourcing to offshoring, even to worldsourcing.

However, outsourcing means very different things to different people. From a European manufacturing perspective outsourcing is often, and increasingly, directly associated with moving component production to low cost countries, such as China. In service industries, the trend towards setting up operations, such as call centers in India, is likewise considered the way forward for companies to remain competitive.

**Outsourcing management leaps**

Relationship and network researchers have tended to take the view that in practice neither outsourcing decisions themselves, nor the management of outsourcing, is ever simple. Executives must make tremendous managerial leaps to understand, implement, and master outsourcing process networks.

The last decade showed an evolution in outsourcing processes from traditional to strategic. Outsourcing is considered traditional if there is outsourced a process not considered “critical” for the organization. This is the case for activities that do not require specific competencies by the supplier, like canteen services or cleaning services. Strategic outsourcing is “when companies outsource everything except those special activities in which they could achieve a unique competitive edge” (Quinn, Hilmer, 1994).

This definition has three important characteristics. The first is that it states that outsourcing has to be a strategic decision that forms part of the organization’s strategy and must be aimed at the pursuit and maintenance of competitive advantage (it has been already discussed above).

The second is so as it considers that the organization must be able to identify which activities or business processes are candidates for outsourcing and must be developed by suppliers, whose capabilities and skills are superior to those of the organization. Outsourcing pioneers are urging managers to subcontract anything and everything. Make-or-buy decisions should directly follow from the core competence analysis and only those activities that are definitely non-core should be considered for outsourcing. A study highlighted that most frequently-outsourced processes are related to salaries and taxes calculation, building administration and claims management. In recent times, executives in charge of “back office” functions such as human resources, informa-
tion technology, indirect procurement, finance, and accounting have been advised to adopt “front office” mentalities by operating their functions as a business within a business.

The third characteristic of strategic outsourcing is that it includes the concept of business processes, since resources can only be a source of competitive advantage if they are exploited through business processes (Ray et al., 2004). A process of outsourcing should start a benchmarking procedure to evaluate the best practice for its specific case (Yasin, 2002). Its model is organized in four main steps (see Table 1):

The two main actors of outsourcing processes are the “outsourced” and the “outsourcer”. The first, the “customer”, outsources his processes, while the second, the organization (vendor), delivers outsourced services.

To analyze relationships between “outsourced” and “outsourcer”, we investigate two main characteristics:
- **Specificity** refers to the level of reutilization of the considered goods/process for many different uses. Usually, they do not allow different uses (Van Mieghem, 1999).
- **Complexity** refers to the difficulty of monitoring and defining contract terms and conditions of the outsourcing process (Vining, Globerman, 1999).

Apart from the strategic importance of the appropriate core competence analysis, the need appears for careful development and management of outsourcing relationships. The problem is that many companies that have undertaken outsourcing projects have found themselves struggling to control the activity they once controlled in-house (Greaver, 1999). As a consequence many organizations have ended up either bringing the activity back in house (Gadde, Håkansson, 2001) or managing the supplier or service provider to such an extent that the latter no longer has the flexibility to deliver the expected results. The root of many outsourcing problems is that often many companies fail to recognize the importance of balancing control and independence between the parties in the relationship.

Tightly coupled processes are often inflexible; such companies limit the value that innovative thinking might yield. Managing their processes more loosely would permit them to unlock the full value of specialization for themselves and their partners and to gain more strategic value of flexibility. Finally, companies may choose to focus on the setting of business standards by learning how to define standards for coordinating activities across a number of organizations and how to get these standards accepted. They

---

**Main steps of the outsourcing processes**

| Internal analysis | 1. Core competence identification  
|                   | 2. Identification of processes to be outsourced  
|                   | 3. Type of relationship (network?)  
|                   | 4. Outsourcing design  
| External analysis | 5. Outsourcer search  
| Contract          | 6. Contract negotiation  
| Outsourcing management | 7. Outsourcing planning, organizing, leading and controlling  

**Table 1**

Source: composed by the author with reference to Yasin (2002).
are also beginning to understand the challenges involved in building and maintaining loose relationships based on trust and long-term incentives, not on the control of activities within a process. Outsourcing also has pitfalls. Poor vendor management skills may lead to a loss of management control, resulting in higher costs, loss of institutional knowledge, and the risk of becoming too dependent on vendors to perform routine operational tasks. Other risks may include the loss of flexibility due to contractual lock-in arrangements that could prevent upgrades to new technologies and a potential increase in costs (Lacity, Wilcocks, Feeny, 1995).

Many companies who have tried outsourcing view it as a difficult process that does not often end as initially planned. Indeed, the failure rate for outsourcing relationships remains incredibly high. In a Deloitte Consulting (2005) survey of 25 world-class organizations covering various industries, the conclusions about outsourcing were not encouraging. One-quarter of the companies had brought business functions back in-house after realizing that they could do the work themselves more successfully and at lower costs. 44 percent of the companies surveyed reported that outsourcing didn't save any money and nearly half identified hidden costs as the most common problem when managing outsourcing projects. Hence, though initially motivated to outsource in order to cut costs, simplify projects, and tap expertise not found in-house, many companies learned that unexpected complexity, lack of flexibility among outsourcing providers, and other unforeseen conditions.

Companies that are disappointed with their current outsourcing deals tend to be in the traditional vendor relationships of the past. So, the need of new structuring opportunities for companies to begin outsourcing appears.

Refashioning organizational boundaries: outsourcing structure design

While prior research has shown that there are advantages to engaging in outsourcing (Lacity, Willcocks, Feeny, 1996), very little research has focused on the nuances of outsourcing arrangements, such as how activities are best divided up among outsourcing partners under one governance structure.

From the organization’s perspective, outsourcing strategies are part of the reorganization process. It fits in the set of downsizing strategies and the diversification decrease that many organizations have adopted. Organizations have carried out a vertical disintegration process in many manufacturing activities, with an increasing use of the sub-contractors’ components. Exploring the structure of outsourcing arrangements (i.e. the division of responsibility and authority over performing sets of activities) between organizations is important for several reasons.

Firstly, outsourcing rarely involves a focal organization completely relocating an entire process or set of activities from within its boundaries to a sole outsourcing partner, particularly when it comes to complex projects. Rather, it is frequently the case that complex activities are subdivided into discrete portions and distributed among multiple outsourcing partners, making these parties interdependent with each other and with the focal organization.
Second, organizations are increasingly outsourcing activities that are core and integral to their own operations, often relying on inter-organizational systems to coordinate relationships with their contractors. Yet there is evidence that outsourcing increased some organizational dysfunctions as increased interpersonal conflict (Kochan, et al., 1994) and so on. This evidence suggests the need for a more careful investigation of how complex activities should be divided among organizations in outsourcing arrangements.

At last, little research has focused on understanding how the structure of outsourcing arrangements affects the overall performance. Outsourcing work to contractors can speed the development through the division of labor and reduction of costs, by having contractor employees perform work that is beyond the normal capacity of a focal organization, and increase efficiency and effectiveness by allowing specialized contractor employees and a focal organization’s employees to focus on activities related to their own core competencies. However, outsourcing activities also complicates the organization’s ability to coordinate and control that work, potentially hindering overall performance. The structure of outsourcing also influences the extent to which conflicts can be resolved by contracts or by existing routines within the focal organizations’ structures.

Outsourcing has generally been of two types:

1) The competitive mode, relying on hierarchical arrangements, minimal cost objectives, and on rigid or preordained performance expectations; it still prevails among many organizations in some of the more traditional industries;

2) The cooperative mode, relying on tacit performance agreements, trust, and reciprocal adjustment; it has been more common in high technology sectors, where short product cycles and continuous innovation are imperatives.

F. Franceschini et al. (2003) propose four types of relationships of the outsourcing process actors:

- Traditional vendor;
- Temporary relationship;
- Strategic alliance;
- Network organization.

A detailed map of the main characteristics of “outsourced”-“outsourcer” relationships is reported in Table 2:

Organizational researchers have been long dealing with the problem of balancing the distribution and integration of tasks across the work unit boundaries (Thompson, 1967; Galbraith, 1974). A central argument is that, when work is distributed among different social entities, the control and coordination of work is hampered. Control refers to the organization’s ability to manage or direct distributed activities such that their outcomes match the organization’s expectations. Coordination refers to an organization’s ability to integrate these distributed activities. When activities are tightly controlled they are more likely to yield outcomes that meet the expectations of the parties involved, while well-coordinated activities are more likely to result in smooth workflow among the parties carrying them out (i.e. minimal backlogs, accidents, mistakes, and wastes).

Agency issues aside (Jensen, Meckling, 1986), coordination and control become more difficult when there is a mismatch between the information-processing requirements of the distributed activities and the information-processing capac-
Table 2

Main characteristics of different types of outsourced-outsourcer relationships

<table>
<thead>
<tr>
<th>Objective</th>
<th>Traditional vendor</th>
<th>Temporary relationships</th>
<th>Strategic alliance</th>
<th>Network organization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Resolution of an immediate problem</td>
<td>Reach better competencies</td>
<td>Joined value creation</td>
<td>Better future market position</td>
<td></td>
</tr>
<tr>
<td>Time</td>
<td>Short-term</td>
<td>Medium/long-term</td>
<td>Long-term</td>
<td>Long-term</td>
</tr>
<tr>
<td>Strategy</td>
<td>Little</td>
<td>Joined to objective of &quot;outsourced&quot; process</td>
<td>Follows strategy of the company</td>
<td>Joined company vision</td>
</tr>
<tr>
<td>Trust</td>
<td>No essential</td>
<td>About competencies</td>
<td>High and reciprocal</td>
<td>Maximum and reciprocal</td>
</tr>
<tr>
<td>Evaluations</td>
<td>Productivity, cheapness, reaction time</td>
<td>Effectiveness, process improvement</td>
<td>Competitive advantage, profit</td>
<td>Innovation, new market creation</td>
</tr>
<tr>
<td>Price model</td>
<td>Cheapness</td>
<td>Based on cost and shared risk</td>
<td>Win-win</td>
<td>Win-win</td>
</tr>
</tbody>
</table>

Source: F. Franceschini et al. (2003).

ity of the organizational structure. When activity interdependence is high, coordinating and controlling activities across work units demand a tremendous amount of information-processing capabilities (Thompson, 1967; Galbraith, 1974). In such situations, how organizations structure activities has a large influence on overall task performance.

Structural contingency theory speaks mostly about the structure of activities within organizations’ boundaries, but the same principles apply in inter-organizational relationships where activities flow among different social entities creating inter-organizational interdependence. Much like units within an individual organization, a set of organizations engaging in exchange relationships as part of the same project form a social system in which goals can be identified and disseminated, resources regulated, and roles and functions governed (Aldrich, 1999). And, as within organizations, the effective performance of distributed activities requires a match between the structure of inter-organizational relationships and the information demands required for the activities.

The myriad quasi-organization structures, strategic alliances and other organization “umbrellas” are developed over the years. The boundaries of the organization have become fuzzy in recent decades, particularly due to the compulsions of innovative activity, where “strategic alliances can facilitate complex coordination beyond what the price system can accomplish, while avoiding the dysfunctional properties sometimes associated with hierarchy”.

So, we propose a network type of the structure of different types of outsourced-outsourcer relationships, which may be, as seen in Table 2, the best structure form for controlling and coordinating outsourced production or services rendering processes. An organization today should seek to tailor its organization structure to the
needs of its activities. The modern organization should build a network of locational advantage for every activity comprising the spectrum of business processes; a network which is internally consistent and compatible with the overall objectives of the organization. The purpose is to marry the capabilities at the headquarters to the locational, comparative advantages in a different country and market, in order to achieve an innovational, competitive structure for a truly global organization.

The rapid spread of outsourcing activity has led organizations to face complex issues of organizational structure. Due to competition pressures and the increased complexity companies try to create flatter, more flexible and responsive organizations as opposed to the diversified conglomerates of notably the 1970s. Companies “stick to their knitting”, since any one company simply cannot master and execute all functions in a competitive manner (Burnes, 1992). In addition, human intellect and resources are becoming even more essential to corporate survival and it’s more difficult to manage them through hierarchical chains of command and rigid structures. Outsourcing can be an excellent way to improve processes, but at the same time, if improperly used, it might lead companies to lose their skills and knowledge, which are difficult to recover. So, the competence market is also an important motive behind outsourcing.

A company cannot develop an outsourcing strategy and implement it discretely, without an understanding of the embeddedness of individual relationships within wider networks (Gadde, Håkansson, 2001).

Linking up a network with research institutions may also provide for the sort of fertilization of ideas and discoveries that only the practical and cumulative knowledge of the various organizations involved in the network can provide. By enhancing the non-tradability of embodied knowledge assets as an integral, component network of the organization through work organization, work structuring and tacit knowledge sharing, organizations can seek to magnify their internal value to the organization while ensuring that their external market value is not enhanced as atomized, individual, knowledge asset components; the value of the networked knowledge assets is enhanced because of their connections to other parts of the organization.

A network can also tailor cooperation to better support continuous innovation, when R&D collaboration is involved. This can lead to more rapid testing and product development through the use of additional or more skilled personnel, or more sophisticated equipment and facilities, all of which might be too costly for an organization to maintain on its own. Many attributes of the markets for innovation goods and services are characterized by the network or demand side externalities and cooperation needs to become an integral part of a competitive strategy in order to achieve growth objectives.

Joining a network may expand the resource horizons of participating organizations considerably, offering access to supportive aspects that surpass those offered by outsourcing (Håkansson et al., 1993).

At the national or international scales, a network can also make it easier for any participating to enter new markets or deal effectively with institutional regulation. Organizations attempting to expand to international markets may find a network of similar organizations to be the only
viable vehicle to establish market niches independently (Dunning, 1993).

Networks can also help secure international licensing agreements, or marketing distribution arrangements, by linking up with a foreign partner, in ways that any individual organization might find very difficult to do on its own (Gates, 1995).

Better access to capital markets may also benefit participation in networks. If many or all of the organizations in a network are geographically concentrated, the very existence of the network may provide a “critical mass” that can help attract external capital investment to local.

Technology enables buyers and sellers of services to exchange information in real time and to embed themselves deeply in each other’s companies. Organizations can thus move away from command and control structures to sense and respond forms of collaboration. Buyer and seller are separated by boundaries that are porous and constantly shifting; it’s impossible to tell where one boundary ends and the other begin.

**Developing outsourcing networks**

Our perspective on outsourcing is derived from the network theory. P. Håkansson et al. (1993) propose a network model formed by actors, activities and resources, where companies develop networks of relationships through connected activities, linked resources and bonds between actors, all of the elements being interconnected and interdependent. The actors in a network are defined by the activities they perform and by the resources they possess. Through exchange processes with other organizations’ activities and resources, bonds are created and developed.

Network structures condition and reflect the internal division of labor existing between organizations in a network. Such functional divisions help determine the role each organization may play, including, for example, the “nodal” responsibilities involving coordination, resource allocation for shared projects, gatekeeping, or even arbitration. The internal division of labor of a network also helps determine the disparities that may occur among organizations, involving, for example, access to internal resources within the network, and the external links that may be developed through the network.

The view of networks (Gadde, Håkansson, 2001) is of individual relationships as parts of a larger whole – a network of interdependent relationships. Relationships are connected since what happens in one relationship affects positively or negatively the interaction in others. Hence, what happens in a relationship between two companies does not only depend on the two parties involved in the relationship, but also on a number of other direct or indirect relationships. This approach to networks suggests that as a result of the complex interdependencies of networks, organizations may only manage, rather than control or co-ordinate in networks.

Business relationships and network connections are tools through which companies can have access to others’ capabilities and resources. In addition, these authors suggest that those resources acquire value when they are used by and become useful to other organizations.

Is order to enable a company to capture the benefits of outsourcing one should integrate its supplier relationships more closely, even to the extent that they be considered ‘quasi-organizations’ (Lamming, 1993). However, close relationships
require investment and are thus costly. So the balance of advantage in increasing the scope of a company’s suppliers by outsourcing may depend both on the structure of the company’s supply network, and on its ability to develop and manage its supplier relationships effectively. This in turn highlights the need for development of two key relationship variables: trust and commitment.

Many companies with superior capabilities have prospered as the dominant player in a network. Japanese keiretsu are structured that way. Toyota’s successful lean production system - a truly systemic innovation-required tremendous coordination with its network of suppliers. Because Toyota was much larger than its suppliers, and because, until recently, it was the largest customer of practically all of them, it could compel those suppliers to make radical changes in their business practices. In a more egalitarian network, suppliers can demand a large share of the economic benefits of innovations, using what economists call holdup strategies.

Although networks—with their high-powered incentives - may be effective over the short term for an unchanging technology, they will not adapt well over the long term as technology develops and companies must depend on certain internal capabilities to keep up. The popularity of networked companies and decentralization arises, in part, from observations over a time the massive investments in manufacturing, management, and distribution that were needed to realize the gains from innovation.

Trust and reciprocity are bound to be the vital lubricant of any cooperation involving research activities (Hansen, 1992). The level of trust involved in such cooperation may also depend on the degree of commitment that any of the engaged organizations have to the network, and their embeddedness in it.

According to P. Ring and A. van de Ven (1992), trust primarily emerges on the basis that the other party will fulfill its commitments. Repeated personal interaction discourages attempts to behave in an opportunistic manner and to gain short-term advantages and thereby increases the level of trust. Trust has three forms:

• **Contractual trust** is defined as the trust that the other party will adhere to the explicit and implicit points of the contract as agreed. Contractual trust is based on moral standards of honesty and ‘keeping your word’. It rests on the expectation that the other party will fully honour the agreements, whether put down in writing or not.

• As relationships evolve, **competence trust** becomes more important than the written formal agreement. Competence trust revolves around faith that the other party has the competence to be able to produce what is required. Competence trust may be acquired by purchasing an existing competence or by investing in its development.

• Ultimately, **goodwill trust** is the decisive factor in highly evolved relationships; it is the trust that the other party will perform tasks in excess of the agreed terms and conditions. Goodwill trust is based on the expectations that parties have an open commitment to each other. Shared values and norms are a necessary but not a sufficient condition for developing goodwill trust. What is needed is a norm of open commitment and reciprocity.

Social bonding can often contribute to higher levels of trust and commitment in a relationship. However, trust and commitment may also be influenced by the
level of the investment in the relationship and the quality of available alternatives.

The literature related to business networks suggests that more and more companies are outsourcing non-core activities (Greaver, 1999). The network approach suggests that companies are specialized in fewer the activities that are necessary to meet the requirements of their customers, presenting potential problems in demonstrating and communicating the company’s capabilities in customer relationships. Indeed this is supported by the core competence perspective on outsourcing. Core competencies (Quinn, Hilmer, 1994) should not be outsourced, as this would be detrimental to the development of the company’s unique capabilities and its ability to leverage these capabilities in its business relationships. Therefore, the activities that may be considered as outsourcing possibilities should therefore be those, which do not constitute the company’s unique capability (Quinn, 1999). However, the boundary between competencies developed and nurtured in-house and those deployed through external relationships becomes blurred (Gadde, Håkansson, 2001). Hence, the question of core competencies becomes more difficult as it is no longer an either/or decision; external actors may play a key role in core competence development and maintenance. The management of the network relationships that form part of and add value to core competencies and core technologies becomes critical. Indeed, it has been suggested that the ability to leverage a complex network of companies – or ‘network competence’ – is by itself a critical core competence (Ritter, Gemünden, 2003).

The development of nodal functions in a network may be inevitable, as organizations become more embedded or the possibility of greater gains becomes enticing. The need for an outreach function may similarly become necessary, if a need to seek additional partners with new capabilities arises. Seeking new distribution or service arrangements may also require a nodal function to be delegated, especially when all or many of the member organizations’ products, differentiated as they may be, can nevertheless share distribution and servicing opportunities.

Among the various typologies, the circuit (non-nodal) network structure is more likely to occur among independent small organizations. The lack of hierarchy may provide for fluid transactional patterns, where cooperative relations are established as needs arise, and where reciprocity may be a tacitly expected feature of inter-organization relations. In this network structure, reciprocity may lead to two-way subcontracting, whereby organizations outsource some of their production or research needs within the network, while they are also subcontracted by partner organizations for specific production or research tasks (Suarez-Villa and Fischer, 1995). Such a strategy, which may lead some organizations to over-externalize some of their functions in order to accommodate requests from network partners, may be engaged in to build up cooperative relationships. The reciprocity obtained in this way may be especially helpful during hard periods.

As some organizations take up a coordinating function within the network, it can produce the nodal circuit variant. The empowerment of an organization to develop a unique decision-making function within the network may occur for specific projects, or for definite or unspecified periods of time, and may be the result of a need to specialize, to manage a complex
project, or because of a growing number of member organizations. An expanded division of labor can raise questions about inter-organization disparities in decision-making powers within the network, leading to more limited trust, however. An increasing division of labor may therefore result in greater gains and efficiency for the network (Harrigan, 1988).

A hierarchical network populated by small organization dependent on a large organization, or by its subsidiaries and spun-off units, is more likely to be of the branch form. Nodal organizations are necessarily an integral part of the branch network, unlike in the previously discussed circuit structure. The very structure of the branch network may lead to significant inter-organization disparities in access to resources, information, or in the decision-making prerogatives that accompany any nodal function. Disparities may also tend to become stronger as the division of labor deepens and the hierarchy develops levels. In this context, therefore, cooperation is more likely to be “programmed”, or organized, by the main organization (or organizations) in the network; as such, the interests of the smaller participants may well be subordinated to those of the organizations that take up major coordinating roles. Exit from the branch network structure may become more difficult for any participating unit, and especially for the smaller organizations, because of this network’s organization and the highly specialized roles that may be developed over time. More difficult exit may well translate into greater commitment to the network, especially when opportunities to join other networks in a similar role, or to diversify and grow unilaterally, are very limited. Thus, commitment to a network can become a function of its structure and division of labor, as well as of the alternative opportunities available.

Hybrid network structures should also be considered in multilateral network formation. The types of organizations involved (independent or subsidiaries), their sizes (SMEs, large, very large) and their geographical range (local, regional, national, multinational) can produce diverse combinations. Two hybrid structures possibly deserve more attention: the circuit-barrier and the circuit-branch networks. The circuit-barrier structure essentially shields or segments a portion of the network, for strategic or functional reasons (Suarez-Villa et al., 1992). Hierarchy is a characteristic of this structure, where a controlling function is exercised by one or more major nodal organizations; in the case of a network of subsidiaries, a major nodal organization would likely be the parent organization. The control function of the nodal organizations in the circuit-barrier and circuit-branch structures therefore acquires greater relevance for the network than in any of the previous network types. Such control need not be associated with lesser inter-organization cooperation, although the inevitably hierarchical structure of these networks can induce greater specialization, thereby limiting or segmenting inter-organization relations. Also, greater control over a network’s members need not have an adverse effect on commitment, to the extent that continuing in the network is perceived to be more advantageous than exiting it. For organizations operating in a highly specialized production niche within these hybrid networks, however, the possibilities for survival and growth may be more closely linked to the fortunes of a network, since the exit and readjustment to a new role outside the network may carry great risks and uncertainty.
Conclusions

The paper deals with structural approach to the outsourced activities development observed over recent years. Consequently, the transfer of ownership of a business process to a supplier is an important and complex strategic decision and makes outsourcing a challenging process.

The network structure type for outsourcing was proposed as it best matches the outsourcing actors’ benefits. A network among various independent organizations can provide a collective sort of invention or innovation, where each of the allied producers nevertheless retains the initiative to apply the results in ways that benefit its own strategic aims. Gains can be in the form of direct access to knowledge, inventive resources.

Support for research and production involving continuous innovation may depend greatly on the nodal or coordinating role that one or more participating organizations play, regarding the sharing of the research and development secrets and strategies. Also the circuit (non-nodal) network structure is likely to occur among independent organizations or other hybrid forms of network structure.

Without access to an established marketing and service network an organization may find it difficult or impossible to obtain such gains independently or on their own, because of the higher risks involved, their inability to obtain venture capital, a lack of market power, or insufficient production capacity.

Organizations will enter a network up to the point where the perceived costs, such as giving up knowledge, facilities or capital, equal or surpass the expected gains. Even when a network does not produce the desired benefits, it may nevertheless be kept in expectation of future gains or out of relational value. Trust that builds up over time may in itself lead to unforeseen benefits, even when the expected gains are not fully realized over a given time period. Trust and the temporal, qualitative and community dimensions of a network are therefore important factors in determining commitment, over and above any strict cost-benefit accounting, particularly among small and medium-size producers.

Many outsourcing relationships experience problems which have been attributed to issues such as control, internal resistance, poor communication or inflexibility with changing business needs. The literature on outsourcing suggests that a vital characteristic of strong outsourcing relationships is that a significant commitment exists between the customer and the outsourcer. Both parties in an outsourcing relationship may be required to make significant time and resource investments in the relationship, adapt to new, more collaborative business relationships and build interpersonal capabilities. Outsourcing relationships require continuous coordination and communication between the parties involved.

Commitment may also be an important determinant of the “embeddedness” of organizations in a network. The embedded quality of a network can, in turn, help “anchor” the engaged organizations to a locality, providing advantages that may be difficult to match by other competing areas or nations. The commitment and embeddedness of organizations in a network can also go a long way toward developing the culture that can provide resilience in times of stress, or enlist institutional support to develop commonly needed resources making a network without boundaries.
Organization managers particularly need a better understanding of their own company’s core skills and technologies and those of their suppliers, customers and service providers. Indeed, without these companies’ unique competencies and capabilities, their strategic position in the network would be short-lived.

There is a need for future studies to examine a wider range of characteristics of relationships that could potentially influence the conditions in which outsourcing relationships evolve. Therefore, it would be important for future research to empirically examine different outsourcing relationship situations across a variety of industries and countries. Furthermore, the importance of aligning the different cultures involved in the outsourcing relationship is an aspect that deserves further investigation.

References


The paper submitted: May 31, 2009

Prepared for publication: November 30, 2009


Organizacijos bus įsitraukusios į tokį tinklą toli, kol jų patiriamus žinių skleidimo ir daliøjimo pajėgumais kaštai neviršius naudos gaunamos iš veiklų/ os iškėlimo. Net kai tinkle dar nėgaunama pageidaujama nauda, narystę gali būti pratešiama laukiant būsimos naudos ar verslo vertės didėjimo.

Vienas pagrindinių veiklos valdymo uždavinių yra išskirti savo organizacijos vystomaes esmines kompetencijas ir įvardinti kitas veiklas, kuriose šios kompetencijos nenaudojamos su tikslo perleisti tas veiklas vykdyti subrangovui, sudarant su juo kontraktą, kuriame apsvarstyti dalyvių tarpusavyne santykiai, numatomos atlikti veiklos ir būsimos naudos.

Tokiių nepriklausomų organizacijų santykių pleta griauna tradicines organizavimų ribų suvokimą ir padeda pagrindus organizacinių tinklinių struktūrų formavimui, pasauliniu mastu kuriant tinklinius veiklos struktūrą nepriklausomai už buvusias konkurentais, tiekėjais, vartotojais ar kitų interesų turinčiomis organizacijomis.

Veiklos iškėlimas už organizacijos ribų susiduria su darbo pasidalijimo, kontrolės ar koordinavimo problemomis, nes skirtingai nuo tradicinių rinkos santykių, tinklėje struktūroje būtina pasitikėjimo atmosfera, reikia nuolatos balansuoti tinkles nariams tarpusavyje sėkmingai veikti dėl centrines padėties, t. y. teisės koordinuoti viso tinkle veiklą ir net kontroliuoti kitų narių atliekamas funkcijas. Pasitikėjimas ir šiapareigojimas yra tinklinių struktūrų vienos svarbiausių sąlybių, o kartu ir narių, esančių tinkle, veiklą koordinuojančių bruožų.