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MARMARA ÜNİVERSİTESİ
SOSYAL BİLİMLER ENSTİTÜSÜ
İŞLETME ANABİLİM DALI
YÖNETİM VE ORGANİZASYON (İNGİLİZCE) BİLİM DALI

STRATEGIC OUTSOURCING AND ITS IMPACT ON FIRM PERFORMANCE

Doktora Tezi

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İstanbul, 2008

Marmara Üniversitesi
Sosyal Bilimler Enstitüsü Müdürlüğü

Tez Onay Belgesi

İŞLETME Anabilim Dalı YÖNETİM VE ORGANİZASYON(İNG) Bilim Dalı Doktora öğrencisi SELNUR GÜZEL nın STRATEGIC OUTSOURCING AND ITS IMPACT ON FIRM PERFORMANCE adlı tez çalışması ,Enstitümüz Yönetim Kurulunun 07.07.2008 tarih ve 2008-11/26 sayılı kararıyla oluşturulan jüri tarafından oybirliği/~~oyçokluğu~~ ile Doktora Tezi olarak kabul edilmiştir.

		Öğretim Üyesi Adı Soyadı	İmzası
Tez Savunma Tarihi	:	04/09/2008	
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ACKNOWLEDGEMENTS

I would like to thank to my advisor Assos. Prof. Dr. Gülruh GÜRBÜZ for her continious support and valuable supervision through every step of this dissertation. I would also like to thank the members of my committee Prof. Dr. Yonca KARAPAZAR ASLANBAY, Prof. Dr. Şule ÖZMEN, Prof. Dr. Sedefhan OĞUZ, and Doç. Dr. Aslı KÜÇÜKASLAN for their valuable contributions.

I am thankful to Dr. Hande Sinem AYKOL and Assist. Prof. Dr. Müjdelen YENER for their constant motivation and morale along the way.

I am also grateful to my father Doç. Dr. Güven ERKAN, mother Türkan ERKAN and husband Serdar GÜZEL for their guidance, patience and love.

ÖZET

Stratejik Dış Kaynak Kullanımının İşletme Performansına Etkisi

Dış kaynak kullanımı, işletmelerin yoğun olarak kullandığı yeni bir kavram olmamakla beraber, dış kaynak kullanım pazarının büyüklüğü düşünüldüğü zaman, işletme stratejisi olarak kabul gördüğü açıktır. Dış kaynak kullanımı, geçmişte iş çevreleri tarafından finansal hedefleri gerçekleştirmede bir yöntem olarak kabul edilirdi. Bu sebeple, maliyetleri düşürme, sabit maliyetleri değişkene çevirerek sermaye yaratma amacı işletmeleri dış kaynak kullanımı için tedarikçi firmalara yönelten temel nedenlerdi. Ancak günümüzde işletmeleri daha fazla zorlayan, global, rekabetçi çevre koşulları mevcuttur. Bu sebeple dış kaynak kullanımı ile ilgili kararlar üst düzey yönetimin konusu haline gelmiş, işletmelerin organizasyon yapılarını değiştiren stratejik kararlar olarak ortaya çıkmışlardır.

Bu araştırrmada, dış kaynak kullanım yoğunluğunun işletme performansına etkisi temel işletme stratejileri ve çevre dinamizmi değişkenleri vasıtasıyla analiz edilmiştir. Araştırmanın amacı çok boyutlu bir model yaratarak dış kaynak kullanımı ve işletme performansı ilişkisini incelemek ve değişik çevrelerde faaliyet gösterip farklı işletme stratejileri uygulayan firmaların dış kaynak kullanım yoğunluklarının işletme performanslarına etkilerini incelemektir. Farklı bakış açıları ve perspektifler değerlendirilerek, literatürde başka araştırmacılar tarafından az sayıda kurgulanan çok boyutlu bir model yaratılmaya çalışılmıştır.

Bu araştırmadaki en önemli bulgu işletme strategileri ve çevre dinamizminin işletme performansına direk, anlamlı bir etkisi olmadığı şeklinde ortaya çıkmıştır. Sadece, dış kaynak kullanım yoğunluğunun işletme performansında firma bazında pozitif katkılarının olduğu saptanmıştır. Araştırma sonuçlarına göre daha fazla dış kaynak kullanım yoğunluğuna sahip işletmelerde anlamlı performans etkileri görülmüştür. Ancak bu bulgu, işletme genel performansı üzerinde ölçümlenmiştir ve performansın işletme bazında finansal, innovative, müşteri/tedarikçi ve çalışan performansı boyutları incelenmiştir.

Bu çalışmada dış kaynak kullanımının işletme genel performansına etkisi sorgulanmış ve dış kaynak kullanımının performansa pozitif, anlamlı katkısı olduğu ortaya çıkmıştır. Diğer tarafta işletme stratejileri ve çevre dinamizmi, dış kaynak kullanımı ve işletme performansı ilişkisine etki eden moderatör değişkenler olarak ortaya çıkmıştır.

ABSTRACT

Strategic Outsourcing and Its Impact on Firm Performance

Outsourcing, far from being a new concept has been widely used by companies, and given the growth of the overall outsourcing market, it's clear that the strategy has gained acceptance. In the past, businesses reviewed outsourcing largely as a way to meet financial objectives. Therefore, tactical plans, such as reducing costs, transforming fixed costs to variable and liberating capital, were often the basic reasons for turnings to an outsourcing service provider. But now companies face a more challenging business environment. It is more global, competitive, networked, and unpredictable. As a result, the decision to outsource is more strategic in nature, taken by senior management and companies are relying on this strategy to tranform their businesses.

In this study, the direct affect of outsourcing intensity on firm performance was analyzed through generic firm strategies and environmental dynamism. The aim of the research was to develop a multidimensional model for analyzing the outsourcing, performance and strategy relationship and figuring out the outsourcing intensity levels for firms pursuing different generic strategies to maximize firm's financial and non-financial performance in different environments. By combining different and variety of perspectives, this dissertation aimed to develop a multidimensional model that has not been outlined by the other researchers in the field.

The most important finding in this study is that neither generic firm strategy nor environment has direct significant effect on firm performance. Only outsourcing intensity has positive contribution to firm performance at the firm level. The results indicate that firms pursuing more intense outsourcing strategies can experience significant performance effects. However, this finding was measured at the firm level. That is, outsourcing was found to have impact on financial, innovation, employee and customer/supplier relations performance of the firm overall.

In this study, a firm-level performance impact of outsourcing is detected, leading to conclusion that the outsourcing intensity has low positive contribution to firm performance at the firm level. On the other hand, generic firm strategies and environmental dynamism is found to moderate the relationship between outsourcing intensity and firm performance.

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1. INTRODUCTION

During economic booms consumers spend, investors lend, and businesses expand everywhere. The 'to-do' list of management is loaded with strategies of growing a business. Alternatively, when the economy experiences a downturn, all eyes turn toward reducing expenses, leveraging existing investments and gaining efficiency. The beginning of this century has witnessed many unforeseen business events both in Turkey and abroad – the financial and political crisis in Turkey, the Enron and WorldCom scandals and the terrorist attacks in America. Such events have led to massive uncertainity and instability in most markets. Businesses in today's turbulent environment have learnt to consider creative strategies to help them to survive in the volatile world markets. One of these strategies is outsourcing.

Outsourcing, far from being a new concept has been widely used by companies, and given the growth of the overall outsourcing market, it's clear that the strategy has gained acceptance. However, there is an evolutionary change underway in the adoption of outsourcing services. In the past, businesses reviewed outsourcing largely as a way to meet financial objectives. Therefore, tactical plans, such as reducing costs, transforming fixed costs to variable and liberating capital, were often the basic reasons for turnings to an outsourcing service provider. But now companies face a more challenging business environment. It is more global, competitive, networked, and unpredictable. As a result, the decision to outsource is more strategic in nature, taken by senior management and companies are relying on this strategy to tranform their businesses.

1.1 Definition of Core Concepts

The core concepts of this dissertation are outsourcing and firm performance. There seems to be confusion in the management litarature about what is meant by the term 'outsourcing'. From the different meanings of outsourcing, there are different

types, which may be grouped according to various criteria in the existing literature. In order to provide a clear understanding of this dissertation and outsourcing-performance relationship, these concepts are defined in this early stage of the dissertation.

Genarally, the definition of outsourcing used in studies of the subject is so broad that it includes virtually any good or service that an organization procures from outside firms. However, defining outsourcing simply in terms of procurement activities does not capture the true strategic nature of the issue. From our point of view, outsourcing is not simply, a purchasing decision. We suggest that outsourcing represents the fundemantal decision to reject to do an activity in-house and look for outside sources. In this way, outsourcing is a highly strategic decision that has the potential to cause performance effects through the organization. Giley & Rasheed (2000) proposes that outsourcing may arise in two ways: First outsourcing may arise through the substitution of external purchases for internal activities. In this way, it can be viewed as a discontinuation of internal production and an initiation of procurement from outside suppliers. To the extent that this type of outsourcing reduces a firm's involvement in production, it may be viewed as 'vertical disintegration'. This seems to be the most commonly understood and used type of outsourcing. On the other hand, outsourcing may also occur because of the absenteesim of the activity in the firm. So, outsourcing may also arise when a firm purchases goods or services from outside organizations even when those goods or services have not been completed in-house in the past. Therefore we suggest that organizations having no choice but to acquire a particular good or service from an external source are not outsourcing. In our point of view, it is important to make this substitution / abstention distinction in outsourcing since it will affect the scope and aim of our research which is to explore outsourcing and performance relationship. A totally new outsourced activity which was not held previously in firm, does not question the outsourcing – performance relationship and therefore is not in the scope of our research.

Some of the operational definitions of outsourcing found in literature are as follows:

'Outsourcing' means purchasing ongoing services from an outside company that a company currently provides, or most organizations normally provide for themselves (Linder, 2004).

'Outsourcing' is the act of transferring some of an organization's recurring internal activities and decision rights to outside providers, as set forth in a contract (Greaver II, 1999).

'Outsourcing' is purchasing from someoneelse a product or service that had been previously provided internally (Wheelen T. L., Hunger J. D., 2000).

'Outsourcing' is the purcahse of a value creating activity from an external supplier (Hitt, Ireland, Hoskisson 1995).

'Outsourcing' is the reliance on external sources for manufacturing components and other value-adding activities (Lei&Hitt, 1995).

'Firm Performance' is the other core concept in this reserach. Firm performance – organizational performance is the degree to which an organization realizes its goals. Performance is a broad concept and it is diffucult to measure in organizations. It implicitly takes into consideration a range of variables to determine a firm's financial and non-financial performance. Many of the privately held firms are unlikely to provide objective financial data, and their executives are expected to be unwilling to provide detailed accounting data. Therefore subjective measures of financial performance (sales growth, assets growth, return on assets, operating income growth, return on sales, overall financial performance) are used. Besides, our sample particially includes publicly traded firms. So together with the subjective data, we had the chance to use these firms' audited financial data. Dess and Robinson (1984) provide strong evidence of the validity and reliability of this type of subjective measures of performance. Ventatraman and Ramanujam (1986) and Giley and Rasheed (2000) use

broader meaures of firm performance to determine the effects of outsourcing on overall performance: research&development outlays, stability of employment, growth of employment, process innovations, product innovations, employee motivation, job satisfaction, customer relations, and supplier relations.

1.1 The Importance and Growth of Outsorcing as a Strategic Management Tool

Outsourcing is critical to the growth and success of a nation's economy (Corbett,2004). Harvard Business Review lists it as one of the most important new management ideas and practices of the 20th century (Sibbet,1997). Outsourcing is noted as 'one of the geatest organizational and industry structure shifts of the century (Quinnn 2002, Geaver II,2004). Many of the world's largest and most succesfull companies are also the world's top providers of outsourcing services. Companies like IBM, Delphi, General Electric, IKON, Unisys, UPS, Xerox, and many others have millions of employees in their outsourcing business. According to Peter F. Drucker, the fastest growing industry in America is 'outsourcing' (Drucker, 2002). Peter Drucker was among the first to focus the attention of business executives on the power of outsourcing. He made the prediction that 'more and more people working for the organizations will actually be on the payroll of an independent outside contractor (Drucker,1989).

The outsourcing of services enables a company's resources and capabilities to be improved by achiving better quality services and better performance (Espino-Rodrigez&Padron-Robania, 2004). While outsourcing improves the performance of areas of the business that do not provide a unique competitive differentiation, it also frees needed capital and resources for investment in those areas that do provide competitive advantage. It reduces both direct costs and opportunity costs (Corbett,2004).

In order to understand the importance and the rationale behind outsourcing, the connection between core competencies and outsourcing should be understood first. The term 'core competencies' was first introduced in 1990 (Prahalad&Hamel,1990). Prahalad and Hamel referred to core competencies as the 'collective learning' in the organization, especially how to coordinate diverse production skills and integrate multiple streams of technology. They predicted that in the coming years managers would be increasingly rewarded for their ability to identify, enhance and leverage their company's core competencies.

In 1994, James Brian Quinn and Fred Hilmer redefined the term as 'Strategic Outsourcing' (Quinn&Hilmer, 1994). Quinn&Hilmer identified the seven characteristics of core competencies as: skills and knowledge sets, not products or functions; flexible, long-term platforms capable of adoptation or evolution; limited in number with no more than two or three per organization; unique sources of leverage in the value chain; areas where the company can dominate; elements important to customers in the long run; capabilities embedded in the organization's systems.

The connection between core competencies and outsourcing was completed with Tom Peter's frequently cited quote ' Do what you do best and outsource the rest' to focus on core competencies and outsource every other part of their operation.

According to Greaver II, the outsourcing initiative becomes strategic when it is aligned with the organization's long-term strategies and when the typical outsourcing benefits will emerge over severall years, and when the results, either positive or negative, will be significant to the organization. With the redefinition of Greaver II, strategic outsourcing takes outsourcing to a higher level by asking fundemental questions about outsourcing relevance to the organization and its:

- Vision of its future
- Current and future core competencies
- Curent and future structure
- Current and future costs

- Current and future performance
- Current and future competitive advantages

There is a huge amount of research about outsourcing in management literature and outsourcing is a global industry (Corbett,2004). According to scholars and practitioners, outsourcing is nothing more and nothing less than a strategic management tool. Since no organisation can stay competitive in today's rapidly changing global economy by relying solely on its own resources, outsourcing is a neccesary response to today's hyper-competitive business environment.

So, we recognize that outsourcing is strategically important (Quinn&Hilmer, 1994; Venkatessan,1992; Jennings,1997). Like any strategic decision, outsourcing must be assessed for its effects on competitive advantage and its congruence with decisions that mean changes in the organization's environment (Rumelt,1980). The strategic approach regards outsourcing as a strategy, and as such it must form part of strategic management. Strategic management is the disipline responsible for studying how organizations formulate and implement strategies to achieve objectives (Hofer&Schendel, 1978). The classsic strategic management literature also suggest that there is a relationship of strategic action with performance (Summer et al.,1990). Bettis et al. (1992) argue that outsourcing must be seen as a component of strategy and not as an 'incremental decision'. They state that managers must treat outsourcing decisions as strategies and consider costs and quality the key variables in any production decions. Greaver (1999), points out that strategic outsourcing considers 'make or buy' decisions to be top level, with basic questions about the company arising, such as the vision of the future, core competencies, structure, costs and competitive advantage. Therefore, the decision to outsource should be included in the company strategy, remaining the processes and assessing the strategic and financial consequences.

All of these lead us to consider that, given its strategic character, outsourcing, in a broad sense, influences the firm's strategies. To be specific, it effects organizational performance, which is the central theme of our research.

1.2 The Purpose and Contributions of the Research

Regarding outsourcing as strategic and suggesting that it has an influence on the organizational performance, is something that has been done with a few emprical research in management literature. Considarable anectodal evidence suggests that an organization's use of outsourcing will have an influence on its performance. However, few emprical examinations of the outsourcing performance relationship have been conducted, and these anectodal accounts of outsourcing effects raise some fundamental questions for emprical research.

Giley and Rasheed (2000), emprically examined the extent to which outsourcing of both periphal and near core tasks influences firm's financial and nonfinancial performance. In addition, they examined the potential moderating effects of firm strategy and the environment on the outsourcing performance relationship. Results indicated that, whereas there was no significant direct effect of outsourcing on firm performance, both firm strategy and environmental dynamism moderated the relationship between outsourcing and performance.

Espino-Rodrigez and Padron-Robania (2004) studied hotel sector managers' perceptions of the influence of outsourcing on operations strategy emprically and particularly on the objectives of cost reduction related operations, improved quality, flexibility and better service. They evidenced that outsourcing significantly influences hotel performance.

Greer&Rasheed&Giley (2004) emprically analyzed the relationship between the outsourcing of human resource (HR) activities, namely training and payroll, and firm performance. They tested for the potential moderating effects of firm size. Results indicated that both training and payroll outsourcing have implications for firm performance but findings regarding a moderating effect of firm size were in conclusive.

Calabrese & Erbetta (2005) investigated whether the outsourcing strategy has positively affected the overall performance of a total of 456 automative suppliers in

Italy. They observed by means of financial statements and under different viewpoints: growth, productivity, financial dependence and profitability. Their findings pointed out that firms always characterised by low integration or that deverticalised their productive structure over time have shown the highest growth, whereas firms with high integration level or that pursued a verticalisation strategy performed better in respect of profitability and debt ratio.

Jiang (2004), the owner of outstanding doctoral research award of Emerald in 2005, analyzed a sample of publicly traded firms that outsourced parts of their operations between 1990 and 2002. Jiang used publicly avaliable acounting data to test for changes in operating performance and abnormal return rates of stock that result from outsourcing decisions. This research was one of the first emprical study to examine the outsourcing impact on firm's performance and value by audited financial data rather than subjective perceptual measures. There is no emprical evidence in Jiang's research to support that outsourcing will improve a firm's productivity and profitability. But it provides solid evidence that outsourcing can improve a firm's cost efficiency and protect, if not increase, the firm's value.

Görzig and Stephan (2002), emprically tested whether outsourcing is an important determinant for a firm's profitability. In addition, they provided estimates on the relative importance of firm, market (i.e industry), and location specific effects, as well as on the impact of organizational structure and human capital input on firm performance. Their analysis supported the view that firms tend to overestimate the benefits accruing from outsourcing of external services and / or underestimate the associated transaction costs.

In literature, it is obvious that many researhers have made arguments both for and against outsourcing as a means of sustainable competitive advantage. However, less attention has been given to those factors that influence a firm's outsourcing decisions. Previous work on the subject has examined a relatively narrow set of determinants. In addition that work has dealt with either a single industry or the outsourcing of a single activity (Giley,1997). The aim of this research is to contribute to this domain by

developing a more comprehensive set of potential determinants that drive the benefits sought from outsourcing, influence firm's outsourcing decisions and outsourcing intensity which in turn should effect firm performance and test them for firms operating in a variety of industries, pursuing different generic firm strategies in different environments. Accordingly, a critical challenge facing organizations is how to effectively organize and manage outsourcing in accordance with the direction of their generic firm strategies. With the premise that organizations with the best fit between generic firm strategy (cost leadership, differentiation or focus) and outsourcing intensity are expected to have better outsourcing benefits and organizational performance then those with such fit.

The main objective of this study is to find answers to questions like ' Are benefits sought from outsourcing different for firms pursuing different generic firm strategies?', 'Are different levels of outsourcing intensity changing according to benefits sought positively affect firm performance?', ' Is environment an effective factor in moderating this outsourcing - performance and strategy fit?'. To answer these questions, we hypothesize theoratically feasible sets of hypothesis between generic firm strategies and outsourcing intensity which lead to different achievement of outsourcing benefits and firm performance.

The aim is to develop a multidimentinal model for analyzing the outsourcing, performance and strategy relationship and figuring out the best fit of outsourcing decisions and benefits with firm strategy to maximize firm's financial and non-financial performance in different environments. By combining different and variety of perspectives, this dissertation aims to develop a multidimentional model that have not been outlined by other researchers in the field. The author aims to figure out outsourcing, performance and strategy relationship of corporate firms in Turkey.

The number of emprical studies in Turkey about outsourcing is also very few. There is a comprehensive research conducted about developing logistics outsourcing and usage patterns in Turkey which is worth to be noted. Akyıldız's (2004) research was conducted to explore how logistics concept was perceived by Turkish firms, what level

of logistics outsourcing were, what kind of logistical services were used , and what level of anticipated logistics outsourcing will there be in the next three to five years. Field survey was conducted with 800 manufacturing firms registered to the Union of Chambers and Commodity Exchanges, located in Ankara. The collected data was analyzed by using descriptive and nonparametric statistics. The results indicated that transportation and customs process are the functions most commonly outsourced. Although the level of logistics outsourcing were 77 percent, logistics partnership were at low levels sustained with very weak ties. All logistics functions, including transportation and customs brokerage at most, were anticipated to increase in the next three to five years.

Another comprehensive research about outsourcing is conducted by the joint work of IBM Turkey and Capital (a prestigious monthly periodical of business and economy in Turkey) in 2005. The field survey was presented to the CEOs, CIOs, general managers or senior information technology managers of 100 leading Turkish companies operating in a variety of sectors. According to the survey, outsourcing is growing most rapidly in information technology functions. The respondent firms intend to increase their outsourcing budgets by 35-40% in 2006. The most noted reasons to outsource are cost driven reasons like reducing costs through superior provider performance and the provider's lower cost structure and turn their fixed costs into variable costs. Another noted reason to outsource is to increase organizational effectiveness by focusing on their core competencies and outsourcing the non-core, operational functions. Total outsourcing market in Turkey is about a hundred million dollars.

In short, outsourcing is a well established business practice both in Turkey and abroad. However, academic research about outsourcing is relatively new and scattered. This dissertation aims to fill in this gap and develop a multidimentional model by combing different and variety of perspectives that have not been outlined by other researchers in the field. The aim is to deeply analyze the outsourcing, performance and strategy relationship and figure out the best fit of outsourcing decisions and benefits with firm strategy to maximize firm performance

1.3 Organization of the Dissertation

The coming chapter begins with a review of outsourcing literature. The literature review is mainly based on outsourcing's definitions and theoratical perspectives on the subject. In chapter three, an effort is made to develop a theoratical model of outsourcing. The proposed conceptual research model is presented by giving the explanation of each variable used in this study. The methodology of the research is presented in chapter four. Research questions, research design, sampling, hypothesis and measurement of variables are explained in this chapter. In the consecutive chapters, the findings of the research (chapter five) and the discussions of the findings, limitations and recommendations for future research (chapter six) are presented.

2. LITERATURE REVIEW

Over the last decade, there has been an increasing emphasis on buyer-supplier relationships in the academic community and international business (Macbeth&Ferguson,1994; Hines,1996; Olsen&Ellram,1997; Quinn, 1999; Lamming et.al, 2000). The relevant literature refers to a situation which is traditionally well-known in theory or practice as 'make or buy' decision (Arnold,2000a). Traditionally, outsourcing is an abbreviation for 'outside resource using' (Bühner&Tuschke,1997; Koppelmann,1996; Quinn&Hilmer,1994; Zahn et al., 1998). In order to find outsourcing's place in management theory, we should first understand the complementary theories about vertical integration, transaction cost economics and make or buy decisions.

2.1 Vertical Integration and Transaction Cost Economics

Vertical integration which is a topic of both management and economics literature, is defined as 'the combination of technologically distinct production, distribution, selling, and/or other economic processes within the confines of a single firm (Porter, 1980). D'Aveni and Ilinitch define vertical integration as 'pattern of diversification that combines lines of business in a way that allows a company to use the outputs of one line of business as inputs for another. Thus, vertically integrated firms link products inadjacent stages of production (D'Aveni&Ilinitch, 1992). On the other hand, Harrigan defined vertical integration as the 'in-house production of goods and services that could be purchased from outsiders' and noted that it is a way of increasing a firm's value-added margins (Harrigan,1985b).

Early examinations of the vertical integration concept, relied primarily on a transaction cost explanation. According to this view, vertical integration is an attempt to minimize the costs and uncertainity associated with market based transactions. In the absence of transaction costs, the organization of economic activity is a meaningless area of study (Williamson,1971).

Indeed, Coase was the first to address vertical integration (Coase,1937). He asserted that costs associated with transacting on the open market must be examined when addressing vertical integration. High transaction costs have been shown to lead to internalization of market- based contracts and therefore to vertically integrated firms (Williamson, 1979). In other words, profit-maximizing firms will produce in-house what is found to be more expensive to acquire through a market-based transaction (Klein, Crawford & Alchain, 1978).

In the transaction cost economics view, vertical integration decisions might be seen as make or buy decisions; decisions consisting only of the financial calculation of costs of integrating versus costs of purchasing. However, vertical integration must take into account much broader strategic issues and many vertical integration and accounting decisions are structured as make-or-buy calculations (Porter,1980). So, vertical integration decisions are often made by comparing the costs of purchasing the particular good or service on the open market against the costs associated with manufacturing the good or service in-house. Thus the make or buy decision is an application of transaction cost economics; products are made in-house if the manufacturing costs are lower than transaction costs plus the purchase price.

2.2 Outsourcing Literature

The literature on vertical integration provides a theoretical foundation upon which theories of outsourcing strategies may be built. By shifting production to outside organizations, firms are, in effect, reducing their levels of internalization. Thus outsourcing may be viewed as a mechanism that allows organizations to 'de-verticalize'. In this section, the definitions of outsourcing used in previous researches are examined. The strategic nature of the firm is examined and the following definitions of ' strategic outsourcing' concept in literature is given. Besides, outsourcing reasons and benefits sought are given together with the advantages and disadvantages of outsourcing identified in prior studies. Then, the theory-based literature on outsourcing is given to explain the theories that are applied to analyze a firm's outsourcing decision, process

and result. Finally, an overview of research to date about outsourcing is made to identify current methodologies, research scopes, and gaps in outsourcing research.

2.2.1 Strategic Outsourcing

Generally, the definition of outsourcing used in prior studies of the subject is so broad that it includes virtually any good or service that an organization procures from outside firms (Giley,1997b). From the different meanings of outsourcing, there are different types, which may be grouped according to various criteria in the literature. Some of the operational definitions of outsourcing are given with the definition of core concepts in the previous chapter. From the definitions of outsourcing given, outsourcing concerns types of activities that contribute substantially to the firm's added value. Accordingly, the outsourcing initiative becomes strategic when it is aligned with the organization's long-term strategies and when the typical outsourcing benefits will emerge over several years, and when the results, either positive or negative, will be significant to the organization (Greaver II, 1999). According to Greaver, strategic outsourcing takes outsourcing to a higher level by asking fundamental questions about outsourcing's relevance to the organization and its vision, current and future core competencies, structure, costs, performance, and competitive advantages.

This notion of strategic outsourcing was also introduced by Quinn and Hilmer (1994). However, if most firms in the same industry were to choose the same type of solution, such as outsourcing, the strategic advantage would be no longer valid, as companies would all converge to the same business mode (Porter,1996).

To be considered as a strategic choice, outsourcing must be a distinctive feature of specific firms in an industry. According to Quelin and Duhamel (2003), strategic outsourcing can be characterised by five elements:

- A close link between outsourcing processes and the key success factors of a firm in an industry (Quinn and Hilmer,1994)

- The transfer of ownership of a business function previously internalised, often including a transfer of personnel and physical assets to the service provider
- A global contract longer and denser than a classical subcontracting agreement
- A long-term commitment between the client and the service provider. Previous research, based on more than one hundred major contracts, shows an average contract duration of 6-7 years (Lacity&Hirschheim,1993; Barthelemy 2001)
- A contractual definition of service levels and of each partner's obligations (Doing et al., 2001)

Alexander and Young (1996b), challenge the conventional wisdom that core activities should be kept in house and evoke several distinctions between the different types of core activities. Activities critical to performance should be distinguished from activities that create a competitive advantage. The first type concerns activities, such as IT, logistics, or facilities management that support the core businesses, without neccesarily being a distinctive feature of a specific firm in its market. The second type refers to activities that create a current or potential competitive advantage for the firm.

Strategic outsourcing concerns both of these types of activities that contribute substantially to the firm's added value. By identifying the business functions to outsource, companies can benefit from an increased specialization in the areas on which they choose to focus, through increased learning, shared experience, professional career path incentives or other ways that enhance value (Alexander and Young,1996a).

Due to its strategic importance, outsourcing is a business decision that involves not only operational managers, but also top management. Outsourcing influences the resources allocated to business units as well as the level of vertical specialization of the firm's activities, both of which are strategic corporate decisions (Grant, 2002). Since it

deals with the modification of the firm's frontiers, strategic outsourcing, deemed as business strategy (Insinga & Werle, 2000), is also a corporate strategy issue.

2.2.2 Outsourcing Models

The relevant outsourcing literature refers to situations which is traditionally well-known in theory or practice as 'make or buy' decisions (Arnold,2000a) as mentioned before. In order to discuss the make/buy decision, several authors like Quinn and Hilmer (1994), Olsen and Ellram (1997), Venkatesan (1992), Arnold (2000) and Hunger and Wheelen (2000) have adopted models that allow the make/buy decision to be based on multiple criteria. Before proceeding with the theoratical perspectives in outsourcing literature, we think it is better to start with the proposed outsourcing models about 'make or buy'decisions of firms to give the big picture of relevant outsourcing decions.

2.2.2.1 Outsourcing Model of Arnold

The outsourcing model of Arnold (2000), consists of four major elements (See Fig. 2.1): Outsourcing subject, outsourcing object, outsourcing partner, and outsourcing design.

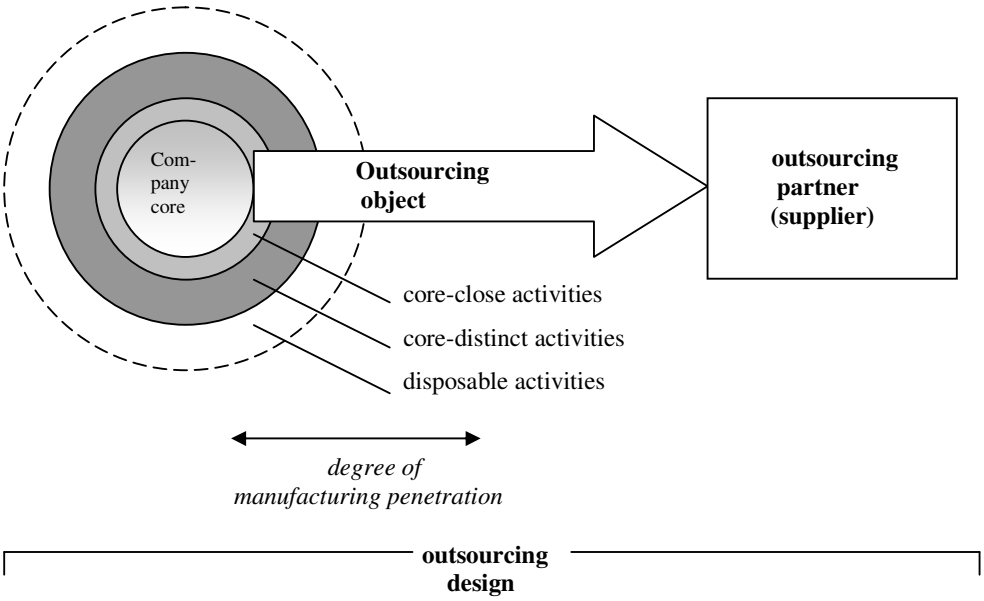


Figure 2.1 Outsourcing Model of Arnold

Outsourcing 'subject' is the economic institution which plans to outsource (or not). The subject has to make the strategic outsourcing decision. Outsourcing 'objects' are processes or process results which might be outsourced (Reichmann and Palloks,1995). With regard to activities of a company, Arnold distinguishes between:

1) The company core (all activities which are neccesarily connected with a company's existence)
2) Core-close activities (directly linked with core actvities)
3) Core-distinct activities (supporting activities)
4) Disposable activities (activities with general availability)

From an industrial perspective, the outsourcing object is closely linked with the degree of manufacturing penetration. Outsourcing 'partners' are all possible suppliers for the activities considered for outsourcing. In this case, supplier is a term in a wider sense. This supplier could also be an inhouse supplier, e.g. an independent business unit within a group of firms.

In Arnold's outsourcing model, outsourcing design alternatives for the outsourcing decision are based theoratically on Williamson's institutional economics. Developed on the ideas of Coase (1937), and Commans (1931), he sees three major 'governance structures' for economic activities (Williamson 1985; Arnold 1998):

Insourcing	**Internal Outsourcing**				**External Outsourcing**		
'make' (own manufac-turing)	'center' approach	coopera-tion	common service company	Capital investment	Formal Co-working	Co-working without formal agreement	Spot transaction

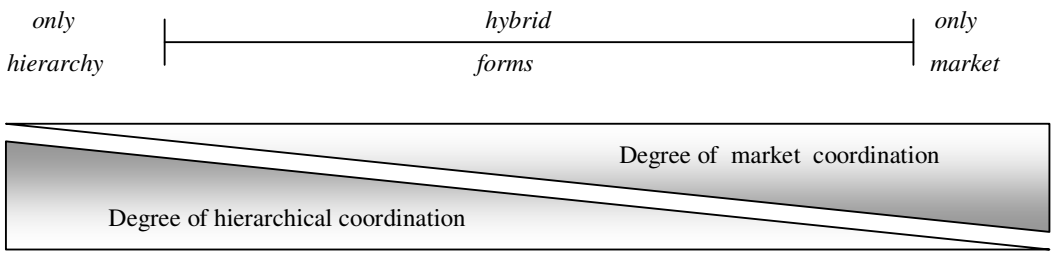


Figure 2.2 Structural Alternatives in Outsourcing Model of Arnold

Markets steer transactions by the price mechanism. There are direct incentives for all transaction partners. If a supplier can not meet customers' requirements, he will not be able to participate in economic exchanges any longer.

Hierarchies are based on the centralization of property rights by management. administrative control mechanisms within a company facilitate the orientation on one target (e.g. the production of automabiles)

There are many governance structures which are neither clear markets nor clear hierarchies. Examples are long-term contracts or strategic alliances between independent companies. All these in-between governance structures combine hierarchical and market elements (Tröndle, 1987). Therefore, they are called 'Hybrids' (Williamson, 1991).

In the outsourcing model, **'Hierarchy'** is directly linked with insourcing. All governance structures with market elements are relevant for the outsourcing design (see Figure 2.2). Arnold distinguishes between internal and external outsourcing. **'External Outsourcing'** means spot transactions or long-term relationships with suppliers. **'Internal Outsourcing'** refers to a higher degree of hierarchical steering (Zahn et.al,1998):by forming independent profit centers instead of hierarchical departments, the market element becomes relevant within a company (Krüger and Homp,1997). If for example, procurement operates as a profit center, all sourcing activities can be outsourced internally to an independent business unit. Internal outsourcing can also be organized as a horizantal cooperation of independent companies, sometimes by a general service company (joint venture) even with capital investment.

2.2.2.2 Outsourcing Model of Quinn and Hilmer

Quinn and Hilmer (1994) link many of the parameters that form both advantages and disadvantages in outsourcing collaborations, and develop two dimensions for classifying the many different activities (development/production of companies or products, service or support activities) that a firm deals with, namely 'the potential for competitive edge and the degree of strategic vulnerability. The different activities, that require different types of relationships with suppliers, are classified into three groups (Figure 2.3).

The model of Quinn and Hilmer suggests that activities with a high potential for competitive edge and a high degree of strategic vulnerability should be realized in house. Moderate strategic vulnerability and moderate potential for competitive edge represent activities that call for a range of relationships like short-term contracts, call options, long-term contracts, retainer, joint development, partial ownership or full

ownership in relation to the suppliers. Lastly, activities with low vulnerability, and low potential for competitive edge call for arm's-length relationships with the suppliers.

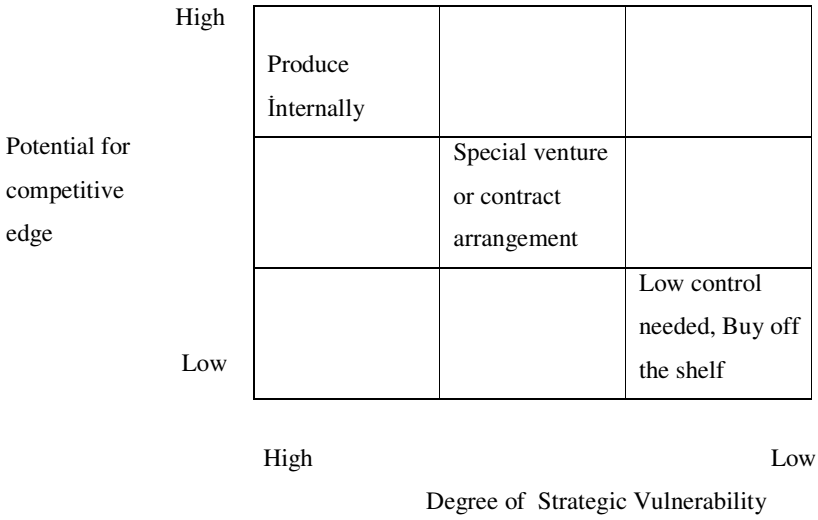


Figure 2.3 Strategic Sourcing adopted from Quinn and Hilmer (1994) by Nellore R. and Söderquist K. (2000).

2.2.2.3 Outsourcing Model of Venkatesan

Venkatesan (1992) indicate that there are two types of products, namely core (there are strictly produced in-house, because they are critical for the performance of the end product and the company is distinctively good at making them), and non-core (they are produced with the help of suppliers, because they are less critical and the company lacks the expertise for producing them efficiently). The core products of Venkatesan, correspond to the in-house products Quinn and Hilmer as both the core and in house products are produced internally withhout any supplier involvement. However, Venkatesan does not specify the type of relationships that could be used when engaging suppliers for the non-core products.

2.2.2.4 Outsourcing Model of Olsen and Ellram

Olsen and Ellram's (1997) model, does not discuss the outsourcing decision. It focuses on products where the decision to outsource is already taken. However, it provides an interesting analysis of the types of relationships that could be used in the collaborative mode (corresponding to the intermediate situation in Quinn and Hilmer's model).

According to Olsen and Ellram, parts that are outsourced can fall into four different categories; strategic, bottleneck, leverage, and non-critical. These products are classified based on the difficulty of managing the purchasing situation and the importance of the project to the companies. Strategic products are highly important and highly diffucult to manage. Non-critical products are at the other extreme and thus are low on the importance and are easy to manage. Bottleneck products are diffucult to manage and the importance of bottleneck projects is low. Finally, leverage products are easy to manage and the importance of the leverage products is high. All the identified product categories with the exception of the non-critical products require some form of collaboration between the outsourcing partners.

2.2.2.5 Outsourcing Model of Hunger and Wheelen

Hunger and Wheelen's (2000) model also discusses the make or buy decision. According to Hunger and Wheelen, an outsourcing decision depends on the fraction of total value added that the activity under consideration represents and by the amount of potential competitive advantage in that activity for the company or business unit. A proposed outsourcing matrix by Hunger and Wheelen (2000) is figured as below:

Activity's Total Value Added to Firm's Prducts and Services /
Activity's Potential for Competitive Advantage

Taper Vertical Integration: Produce some internally	**Full Vertical Integration:** Produce all internally
Outsource Completely: Buy on open market	**Outsource Completely:** Purchase with Long-term contracts

Figure 2.4 Proposed Outsourcing Matrix adapted from Hunger J.D and Wheelen T.L (2000).

According the proposed matrix, a firm should consider outsourcing any activity or function that has low potential for competitive advantage. If that activity constitutes only a small part of the total value of the firm's products or services, it should be purchased on the open market (assuming that quality providers of the activity are plentiful). If, however, the activity contributes highly to the company's products or services, the firm should purchase it through long-term contacts with trusted suppliers or distributors. A firm should always produce at least some of the activity or function (taper vertical integration) if that activity has the potential for providing the company competitive advantage. Full vertical integration should only be considered, however, when that activity or function adds significant value to the company's products or services in addition to providing competitive advantage.

The five models discussed above show that there is a clear correspondence between the categories for classifying activities proposed in different models. Each model categorizes the company's core and non-core activities to give the make or buy

decion of that activity in relation to each activity's strategic importance and explain the degree of supplier relations specified according to each category of activity.

2.2.3 Theoratical Perspectives on Outsourcing

In this section, theoratical perspectives based on outsourcing transactions in literature will be explained. In order to give a clear picture of outsourcing determinants when firms rely on outsourcing, the theoratical perspectives which are the foundations for these determinants will be explained.

There are several theories that are applied to explain or analyze a firm's outsourcing decions, processes or results. So far, the early theory-based literature on outsourcing draws heaviliy from the theory of transaction cost analysis, core competency theory, and agency theory.

2.2.3.1 Outsourcing from Transaction Cost Perspective

Coase (1937) was the first to discuss transaction costs as mentioned before. The theory of transaction cost analysis, pioneered by Coase, and developed principally by Williamson (1975, 1979, 1985, 1991), posits that there are costs in using a market. These costs include operational costs (e.g. serarch costs) and contractual costs (e.g. costs of writing, monitoring and enforcing a contact). This theory argues that activities of the firm either will be internalized or market-mediated, depending on relative transaction costs conducting the activities. It combines economic theory with management theory to determine the best type of relationship a firm should develop in the marketplace. While most microeconomic theories of the firm regard the firm as an abstract construct, the theory of transaction cost analysis, however, deliberately attempts to describe the firm as a set of internal (bureaucratic) activities and external market (contract) relations. It defines the boundary of the firm as the limit of transactions governed by internal processes. Any transactions that occur via markets are by definition external to the firm. Furthermore, it attempts to predict which activities are internalized and which are transacted via market exchanges. This has laid the foundations for the purchasing

discipline that uses an analysis of the factors that determine the internal and external boundaries of the firm. (Jiang, 2004).

The theory of transaction cost analysis hypothesizes that firms seek to minimize costs of operations. The theory assumes that individuals are boundedly rational and opportunistic implying that (1) contracts can not be complete because all contingencies can not be foreseen, and (2) individuals will exploit contract ambiguities to their advantage – even going so far to misrepresent contract performance. These 'costs of making each contract' appear because of information asymmetry, bounded rationality and opportunism. Such costs arise from activities which include: evaluating suppliers, negotiation, control function, etc. (Picot,1991). They appear not only in markets but also in hierarchy. If a company has to invent and to run a system to control the productivity of its workers, hierarchy costs are inevitable. The basic idea is to find a governance structure with the lowest costs for each transaction.

'Transaction Cost Economics' proposes that vertical integration is more efficient than contracting for goods and services in the marketplace when the transaction costs of buying goods on the open market become too great. However, when highly vertically integrated firms become excessively large and bureaucratic:

The costs of managing the internal transactions (Vertical Integration)	>	*The costs of providing needed goods externally* (Outsourcing)

So, outsourcing appears as a rational way when the consecutive costs are compared. During the 1990's, there has been a movement away from vertical growth strategies (thus vertical integration toward cooperative contractual relationships with suppliers and even with competitors). These relationships range from 'outsourcing' to strategic alliances, in which partnerships, technology licensing agreements and joint ventures taht supplement a firm's capabilities (Wheelen T., Hunger J.D, 2000).

From the transaction cost perspective, outsourcing creates a market-contracting, interorganizational relationship between a firm and its external service provider, and requires the firm to incur substantial costs of negotiating, monitoring, and supervising external contractual parties. Transaction costs are exacerbated of specific assets, uncertainity, and frequency of transactions (Jiang,2004):

2.2.3.1.1 Specific Assets

Specific assets are physical and human assets that are specialized and unique to the extent that they generate less value outside the contractual relationship (Wiliamson,1985). Given high asset specificity, the desired way to source is through internal sourcing (Williamson 1979). No matter how unique a firm's business operations are, however, it still needs certain standard supports, such as financial accounting, human resource management or inventory control, which may be outsourced. But according to transaction cost analysis: assuming that parties to an exchange will perform efficiently and forgo opportunistic behavior is imprudent. (Anderson and Coughlan, 1987). As a result, specific assets cause problems because an outsourcing firm's continued use of such assets depends on the good-faith behavior or forbearance of the vendor. For example, outsourcing firms are exposed to the possibility of 'opportunistic expropriation' if the vendor chooses to capitalize on the transaction (Klein et al., 1978).

2.2.3.1.2 Uncertainity

Uncertainity is at the root of all market failures or transactional diffuculties (Aubert et. al, 1996). Detailed contracts can be drawn specifying the obligation of each party and the allocation of costs and benefits in every conceivable state of nature. Writing and enforcing complete contracts is even more costly for highly complex and uncertain transactions. Indeed, a typical outsourcing contract is highly complex. For example, Brandon and Segelstein (1984) prescribe a checklist of more than 170 essential contracting elements for use in negotiating an IT outsourcing contract. The elements include technical and monetary details such as price adjustments when volume changes, quality standards, site access, turnaround time for batch work, response time for online

work, hardware configuration, staff expenses, costs of termination or cancellation, and dispute resolution mechanisms.

2.2.3.1.3 Frequency of transactions

Low frequency transactions are likely to be organized through market interactions or with the help of any general governance mechanism available in the community. For low-frequency transactions, the firm will prefer to bear the risk associated with opportunism and uncertainity rather than support the cost of creating a new governance mechanism or expanding an existing one. When parties interact frequently, it may be more economical to design a governance mechanism that is specifically adapted to a specific situation. Thus internalization of transactions by the firm is only efficient for recurrent transactions. For example, software development projects vary in complexity and area of application. Different sytems require different skills. Even if a firm conducts software development projects on a regular basis, it may not have the required skills in its regular workforces: the firm will use consultants whenever it believes that these skills will not be required on a regular basis. Here, 'frequency' refers to to the use of different skills rather than software development projects. For a given project, the required skills and their frequency refers to the use of different skills rather than software development projects. For a given project, the required skills and their frequency of use must be identified. For frequently used skills, the firm should conduct the development in-house; but for special skills, a contract (outsourcing) should probably be used. Aubert et al. (1996) investigate seven outsourcing firms and find: they are using external vendors to provide expertise that was only needed for a limited period. When the expertise was expected to be needed on a regular basis, the personnel were hired permanently.

Transaction cost theory assumes that each of the above factors create potential costs. According to Williamson (1979), the decision of whether or not to outsource and the extent of outsourcing, depends on the transaction costs associated with outsourcing versus internalization. If the costs are very high, complete vertical integration may be the answer. However, there is usually a contractual solution somewhere between vertical

integration and complete free market forces that will better satisfy the organization's needs. For example, the level of customized equipment or materials involved in the transaction relates to the degree of asset specificity. When asset specificity and uncertainity are low, and transactions are relatively frequent, transactions will be governed by markets. High asset specificity and uncertainity lead to transactional difficulties with transactions held internally within the firm – vertical integration. Medium levels of asset specificity şlead to bilateral relations in the form of co-operative alliances between the organizations. Therefore, there is a degree of dependence that one or both organizations in the co-operative alliance can take advantage of.

2.2.3.2 Outsourcing from Core Competence Perspective

The term 'core competencies was fisrt introduced in 1990 by Prahalad&Hamel and described as 'the collective learning' in the organization, especially how to coordinate diverse production skills and integrate multiple streams of technology. As a result of this thinking, many large corporations began to focus on the 'core competence' (Prahalad and Hamel, 1990) that distinguished them from their competition. This led many corporations to divest themselves of divisions that did not fall witin the core competence.

Core competencies combine three elements (Krüger and Homp,1997):

- In the eyes of the customers, their characteristics must be relevant. They differentiate between the company and its competitors.
- To gain competitive advantage, resources and know-how for the product must be unique over time. It must be possible to protect it against imitation by competitors over time. So a competitive advantage must be sustainable.
- Only if these resources are usable for multiple purpose, they are core competencies and should remain within a company and should not be outsourced.

Indeed, this line of thought was feeded by analyses such as Porter's value chain (Porter,1985) which helps managers focus on the way value is added by various organizational activities.

Quinn (1992) and Quinn and Hilmer (1994) take this approach further by suggesting outsourcing activities that fall outside the core intellectual properties that distinguish the enterprise from others, since specialist intellect is the core resource of most organizations through which they deliver a superior service to the customer. Most activities in the value chain can be defined as services (Cronk and Sharp, 1995). Each service can be examined from a customer perspective to see if it is one which the organization knows how to perform better than anyone else in the world. If it is, it should be retained and the intellectual resources surronding it should be protected by any possible means. Any services that the organization is unable to perform better than anyone else should be outsourced. The basis of this argument is that the success of an organization is the product of all the elements of the value chain. The better each of these is, the better the whole (Jiang,2004).

There are two schools of thought for the core competency theory which are **'resource based view'** and '**collective learning view'**.

Resource-based view concentrates on the firm's specific resources and argues that these resources can provide competitive advantage to the organization.(Khatri,2000). In other words, internal resources enable the firm to survive and compete in the market (Teece et al., 1997; Wernerfelt, 1984). The resources can only create sustainable competitive advantage for the firms if they employ four attributes. These attributes are; being valuable, rare, diffucult to imitate and having no substitutes. According to this approach each firm has different type of resource and capability and has to live with or without it for sometime. Resource-based perspective assumes that these resources provide sustainable competitive advantage for the organization only if these resources employ the above mentioned four characteristics (Barney, 1991). .

Resource-based view adds another important perspective to outsourcing. Outsourcing to meet the unique needs of a firm have the potential to create resources that may allow for sustainable competitive advantage as mentioned above. When the activity supposed to outsourcing has the potential to create such resources, outsourcing these activities may well increase the risk of imitation by competing firms. So an important concern raised by the resource based view is that the outsourcing of firm activities may make it diffucult to develop core competencies that lead to competitive advantage. Core competencies develop through a complex process requiring high degrees of social capital and the ability to draw-in ways that are diffucult to specify in advance – on a variety of sources of intellectual capital (Hamel and Prahalad 1989; Prahalad and Hamel,1990). As a result, the learning and collaboration required by this complex process is thought to be more likely to occur when all parties are part of the organization (Corner and Prahalad,1996).

Collective-learning view has entered literature when Prahalad and Hamel (1990) defined core competencies in terms of 'the collective learning in an organization, especially how to coordinate diverse production skills and integrate multiple streams of technologies' which gives it a competitive advantage over its competitors. Researhers following collective learning view use the terms 'competency' and 'capability' interchangeably. The focus of this view is on the determinant of skills and know-how possessed by an organization. This school of thought is appropriate for studying today's competition as more recent studies indicate that differences in starting resource positions may be less important than differences in abilities to leverage corporate resources (Prahalad, 1993).

In fact, many theories and perspectives in management literature complement each other. For instance, Quinn and Hilmer's (1994) outsourcing model mentioned before proposes a framework that encompasses insights from both Transaction Cost Perspective and Resource-Based View of the firm (Wernerfelt, 1984; Barney,1991; Grant, 1991). According to Quinn and Hilmer, companies should 'outsource everything except those special activities in which they could achieve a unique competitive edge'

but also take transaction costs into account as 'most supplier markets are impect (and) outsourcing entails unique transaction costs – searching, contracting, controlling, and recontracting – that at times may exceed the transaction costs of having the activity directly under management's in-house control' (Quinn and Hilmer, 1994).

Recently, scholars have presented resource-based perspectives of integration that augment transaction-based views and sharpen the focus on firms' relative advantages. (Combs and Ketchen, 1999; Leiblein and Miller, 2003; Poppo and Zenger, 1998). The resulting convergence between these two theories has stimulated a number of emprical studies, which has created a more effective understanding of what derives strategic outsourcing. For example, in recent years, transaction cost scholars have accepted that transaction-based and resource-based perspectives 'deal with partly overlapping phenomena, often in complementary ways' and that capability endowments matter to boundary decisions (Williamson, 1999). Combs and Ketchen (1999) found evidence that firms often place resource-based concerns ahead of exchange-economics when deciding on potential interfirm cooperation. Complementary to this view, Madhok (2002), pursued the question of how firms should organize production given certain resource-based conditions (e.g pre-existing strenghts and weaknesses). He suggested that boundary decisions depend not only on the conditions surrounding the transaction, but also on capability attributes, and the governance context that it creates. Thus, substantial emprical support exists for the proposition that capability considerations trade-off with economizing constraints in the decision to outsource (e.g. Hoetker, 2005; Jacobides and Winter, 2005; Poppo and Zenger, 1998).

2.2.3.3 Outsourcing from Agency Theory Perspective

Agency theory is essentially concerned with the delegation of work by one party (the principal) to another (the agent) via a contract (Eisenhardt, 1989), whether or not they are both within the same organization.

Fundemantally, agency theory focuses on controlling the behavior of agents to ensure that it is consistent with the objectives desired by the party paying for the agent's

services, the principal (Jensen & Meckling, 1976). The contract is the core idea in agency theory. It may be explicit signed contract with an outside consultant or contract programmer, or it may be implicit., as with in-house employees. In either case, a contract can have two types: compensation based on behaviors or on outcomes. A behavior- based contract compensates agents for performing certain tasks or behaving in a certain way. The agent is paid a salary or hourly rate for performing the tasks, regardless of the outcome. This type of contract is more common with in-house employees than it is with outside contractors. An outcome-based contract compensates agents for achieving certain goals or outcomes. Thus, the tying of performance evaluations and merit bonus payments to meeting project deadlines and staying within budget illustrates an outcome-based contract (Lederer and Prasad, 2000). Such a contract is commonly used with both in-house employees and with outside contractors.

The choice of contract type depends on agency costs, which include the principal's effort in assessing the agent's performance and the agent's efforts in assuring the principal of his commitment (Cheon et al., 1995). Iholds that human beings act through self-interest and therefore, as contracting parties, they may have divergent goals. An important aspect of the theory is that both outsourcing firms and vendors wish to avoid risk whendealing with each other. The outsourcing firms may prefer to place risk with the vendor via an outcome-based contract, whereas the vendor may prefer to avoid risk by having a behavior-based contract (Eisenhardt, 1989). Outcome-based contacts are claimed to reduce vendor opportunism because the rewards of both vendor and outsourcing firm depend on the same actions. Behavior-based contracts need the outsourcing firm to have sufficient information to identify two possible dangers: first, whether there is adverse selection (the vendor does not possess the skills he claims); second, moral hazard – 'the vendor is shirking' (Eisenhardt,1989).

2.2.3.4 Summary of Outsourcing Researh to Date Based on Theoratical Perspectives

After reviewing outsourcing literature and the theoratical perspectives based on the subject, the representative research studies reviewed for this study based on each perspective are summarized in Table 2.1:

Table 2.1: Outsourcing Researh to Date Based on Theoratical Perspectives

Theoratical Perspective	Representative Work
Transaction Cost Perspective	Arnold (2000);Ellram and Billington (2001); Evans (2000); Greer et al (1999); Hendry (1995); Jennings (2002); Maltz and Sautter (1995); Tayles and Drury (2001); Teng et al (1995); Venkatraman (1997), Widener and Selto (1999) Aubert et al (1996); Barthelemy (2001); Cachon and Harker (2002); Coman and Ronen (2000); DiRomualdo and Gurbaxani (1998); McCarthy and Anagnostou (2004); Ngwenyama and Bryson (1999); Rao and Young (1994);
Core Competence Perspective	Hunger and Wheelen (2000); Venkatesan (1992); Jones (1994), Lee (2001); Lonsdale (1999); Mc Dermott and Handfield (2000); Nellore and Soderquist (2000); Pinnington and Woolcock (1995); Welch and Ranganathan (1992) Canez et al (2000); Chesbrough and Teece (2002); Earl (1996); Fuller et al (2000); Granstrand et al (1997), Insinga (2000); Sharpe (1997); Shy and Stenbacka (2003); Wasti and Liker (1997);
Agency Theory Perspective	Olsen and Ellram's (1997); Johnson and Schneider (1995); Kaipia and Tanskanen (2003); Kim (2003); Kim and Smith (2003); Knemeyer et al (2003); Hines and Rich (1998); House and Stank (2001); Mean and Kiu (2002); Richmond et al (1992); Sabherwal (2003); Sink et al (1996); Spencer et al (1994); Yost and Harmon (2002) Boyson et al (1999); D'Amours et al (1993); Dapiran and Lieb (1996); Ekanayaka et al (2003); Fernie (1999); Harland et al (2003).

2.2.4 Theoretical Foundation for Strategic Outsourcing

In the previous sections, we have given the operational definitions of outsourcing and the theoretical perspectives on which the concept is build. In this section, we begin with a concise review of the literature to derive a more complete definition of 'strategic outsourcing'. Next, transaction-based and resource-based arguments are reviewed for strategic outsourcing. Building on these two perspectives, a theoretical model of strategic outsourcing by Holcomb&Hitt that uses transaction and capability-based factors to examine a firm's decision to outsource is presented.

2.2.4.1. Strategic Outsourcing Redefined

Holcomb & Hitt (2006) define strategic outsourcing as the organizing arrangement that emerges when firms rely on intermediate markets to provide specialized capabilities that supplement existing capabilities deployed along a firm's value chain. Holcomb & Hitt suggest that strategic outsourcing creates value within firm's supply chains beyond those achieved through cost economics. Intermediate markets that provide specialized capabilities emerge as different industry conditions intensify the partioning of production. As a result of greater information standardization and simplified coordination, clear administrative demarcations emerge along a value chain (Jacobides, 2005). Partioning of intermediate markets occur as the coordination of production across a value chain is siplified and as information becomes standardized, making it easier to transfer activities across boundaries (Richardson, 1972). Accordingly, an orientation toward strategic outsourcing evolves, as specialized capabilities emerge, resulting in a greater dependence on intermediate markets for production (Fine and Whitney, 1999; Quinn, 1999).

The decision to outsource 'existing' production represents the simplest form of 'strategic outsourcing' (Holcomb & Hitt, 2006). As mentioned before, Giley and Rasheed (2000), refer to this organizing form as 'substitution-based outsourcing' where firms discontinue internal production and replace existing activities and/or factors of production with capabilities provided by intermediate markets. On the other hand, Giley

& Rasheed, refer to the opposite of this form as 'abstention-based outsourcing', which occurs when firms acquire capabilities from intermediate markets, rather than incur the neccesary investments to internalize production.

An important distinction introduced in this section is how resource-based perspective influence the decision to strategically outsource more effective specialized capabilities along a value chain. More effective capabilities can enable firms to increase inventory turns, shorthen product development cycles, and reduce the time-to-market for new products (Clark and Fujimoto, 1992; Petersen et al., 2005). In other words, strategic outsourcing not only creates cost economies by shifting production activity from a focal firm to intermediate markets, but also creates economic value, especially when production involves the use of potentially more valuable specialized capabilities (Fine and Whitney, 1999; Mowary et al. 1996). Holcomb and Hitt (2006), argue that strategic outsourcing not only allows firms to reduce costs, but also enhance their portfolio of capabilities and value creation potential, especially when firms produce unique combinations using capabilities provided by those markets.

2.2.4.2. A Theoretical Model for Strategic Outsourcing

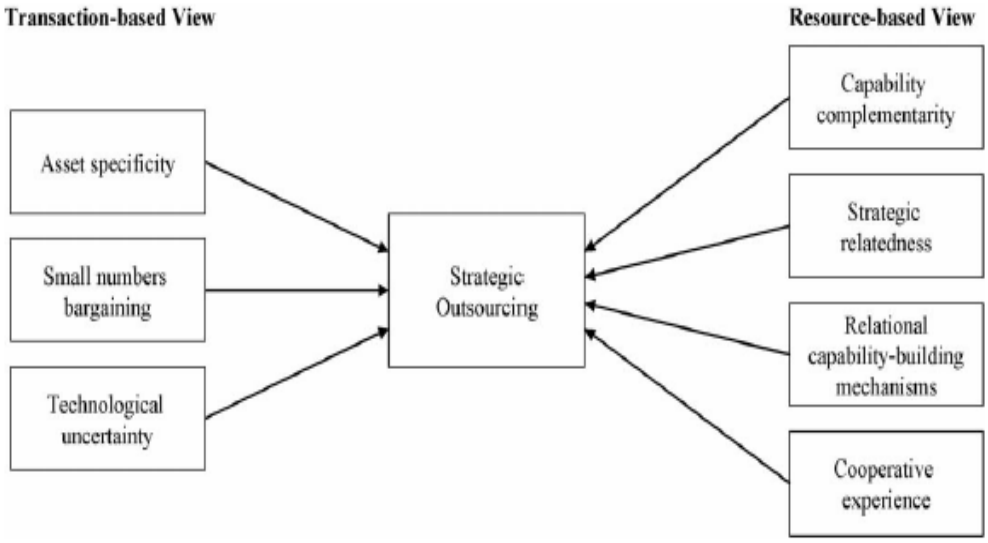


Figure 2.5 A Theoretical Model for Strategic Outsourcing

Source: 'Toward a Model of Strategic Outsourcing', Journal of Operations Management, Tim R. Holcomb, Michael A. Hitt (2006).

Figure 2.5 summarizes Holcomb & Hitt's model for strategic outsourcing. This model depicts conditions for value creation integrated with economizing arguments for strategic outsourcing. Building on two perspectives for strategic outsourcing, they present a model of strategic outsourcing that uses transaction and capability-based factors to examine a firm's decision to outsource.

For better understanding of Holcomb and Hitt's model, it is better to distinguish the relationships between resources and capabilities. Capabilities result from a complex pattern of actions and a positive synergy among various resources (Grant 1991; Nanda 1996). They are invisible and manifested within organizational activities and processes and enable firms to provide products or services to customers (Hammer and Champhy

1993; Collis 1994). Penrose (1959) points out that capabilities are the actual and active inputs to production function. Capabilities of a firm may be developed indigenously or collaboratively with the help of the firm's stakeholders. For Wernerfelt (1984) firm resources are "anything which could be thought of as a strength or weakness of a firm". Under this definition, capability is considered part of resource and firm competence could either be a resource or capability. On the other hand, many authors do not include capabilities within the definition of firm resources because of their dynamic or "doing" nature. For example, Nanda (1996) suggests that resources and capabilities should be defined differently: if resources are defined in terms of what they do rather than what they are, it becomes impossible 'to distinguish among them the strategic and the non-strategic resources'.

A relatively clear description of resources and capabilities is due to Grant (1991) who defines; "resources are inputs into the production process — they are the basic unit of analysis capability is the capacity for a team of resources to perform some task or activity". Therefore, firm capabilities are determined as the direct source of competence. Some examples of firm capabilities are given in Figure 2.6:

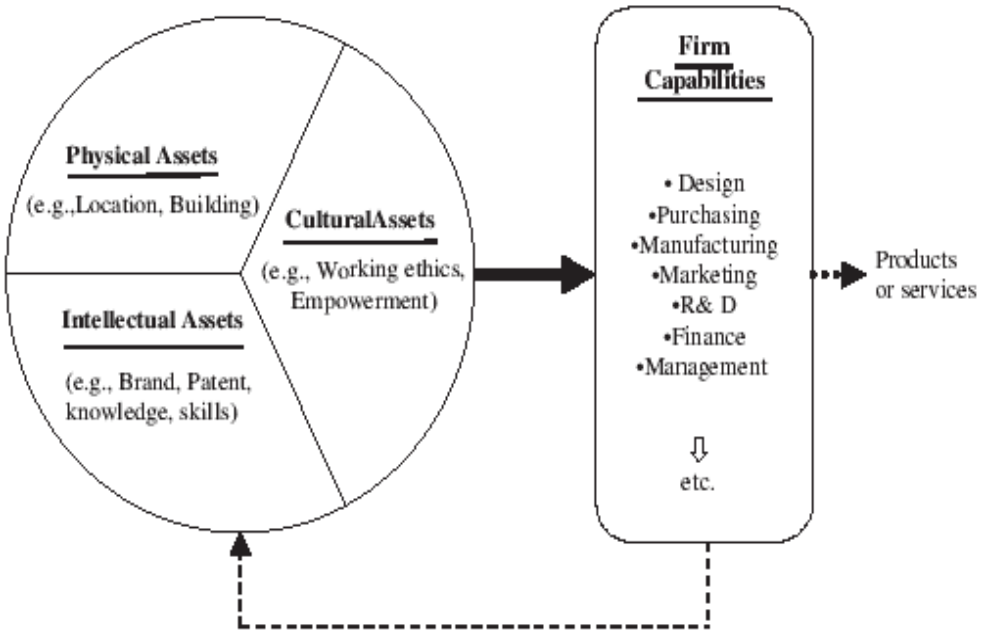


Figure 2.6 Relationship Between Resource and Capability

Source : Adapted from Hafeez K., Malak N. and Zhang Y.B. (2006)

Holcomb and Hitt (2006) suggest three assumptions that underlie resource-based views about strategic outsourcing:

- Strategic outsourcing relationships form within a social context. Ties, both direct and indirect, with firms in intermediate markets create a network (Uzzi, 1997), and become an importany source of information about the reliability and performance of current and future exchange partners (Granovetter, 1985).
- Selection determines gains available to firms from capabilities accessed in the intermediate markets and then intensifies the effect of these capabilities on firm performance. Complementarity and relatedness creates uniquely valuable synergy, especially when specialized capabilities are effectively combined and when no other combination can replicate the resulting value chain (Harrsion et al. 1991, 2001; Prahalad and Bettis, 1986; Richardson 1972; Tsai, 2000).

- Firms enhance their ability to leverage specialized capabilities by developing and refining mechanisms that strengthen the synergies such capabilities provide. These mechanisms are referred as relational capability-building mechanisms (Dyer and Singh, 1998; Makodok, 2001) which allow firms to enhance the potential value of specialized capabilities deployed along a value chain.

In sum, Holcomb & Hitt contend that specialized capabilities accessed by strategic outsourcing may allow firms to achive greater performance gains.

2.2.4.3 Transaction Based Arguments for Strategic Outsourcing

Efficiency assumptions in TCT drive the classical reasoning for strategic outsourcing. With this view, diffuculties that emerge from market-based exchanges generate transaction costs. Such costs include negotiation, contracting, monitoring, and enforcement costs, as well as costs incurred when resolving disputes. Based on this perspective, the performance implications of outsourcing and thus the decision criteria firms apply are based on the alignment of different governance structures with attributes of the exchange and the underlying contracting environment. For example, a firm that selects a sample governance structure lacking adequate safeguards and controls is exposed to moral hazard, and hold-up risks when the contracting enviroment is complex or when it involves transaction-specific investments (Leiblein, et al., 2002). By contrast, selecting an excessively complex governance structure for a simple contracting environment unneccesarily intensifies bureaucratic complexity., which reduces decision-making speed, decreases strategic flexibility, and increases overall costs (Williamson, 1985). Accordingly, cost economics as a consequence of effective governance structures represent important criteria in the decision to strategically to outsource. In the theoretical model of Holcomb & Hitt (2006) given before, three transaction-based considerations for strategic outsourcing are presented as : asset specificity, small numbers bargaining, and technological uncertainity.

2.2.4.4. Resource Based Arguments for Strategic Outsourcing

Transaction-based perspectives of strategic outsourcing can be extended by focusing attention on the role of specialized capabilities obtained through intermediate markets (Holcomb and Hitt, 2006).

The ability to access new and potentially more valuable capabilities is a critical driver of strategic outsourcing because these actions can fundementally alter a firm's capability endowments (Morrow et al. 2005), making it easier to pursue new opportunities in the market. Holcomb and Hitt maintains that different conditions affect the value of capabilities sourced from intermediate markets. In particular, four resource-based considerations for strategic outsourcing are described briefly in their model, namely complementarity of capabilities, strategic relatedness, relational capability-building mechanisms, and cooperative experience as shown in the model.

According to Holcomb and Hitt, the value creating potential of the firm is at the heart of the theory of the firm, and by adopting a model of strategic outsourcing, scholars and practitioners can understand the strategic, operational, and financial motivations and incentives behind this organizing arrangement. They assert that if outsourcing is pursued strategically, firms can achieve above normal returns, and examining the different conditions in which value creation occurs can extend management's view of strategic outsourcing and provide a new paradigm for supply chain practitioners to demonstrate the practical benefits of strategic outsourcing.

2.2.5 The Theoretical Research Model

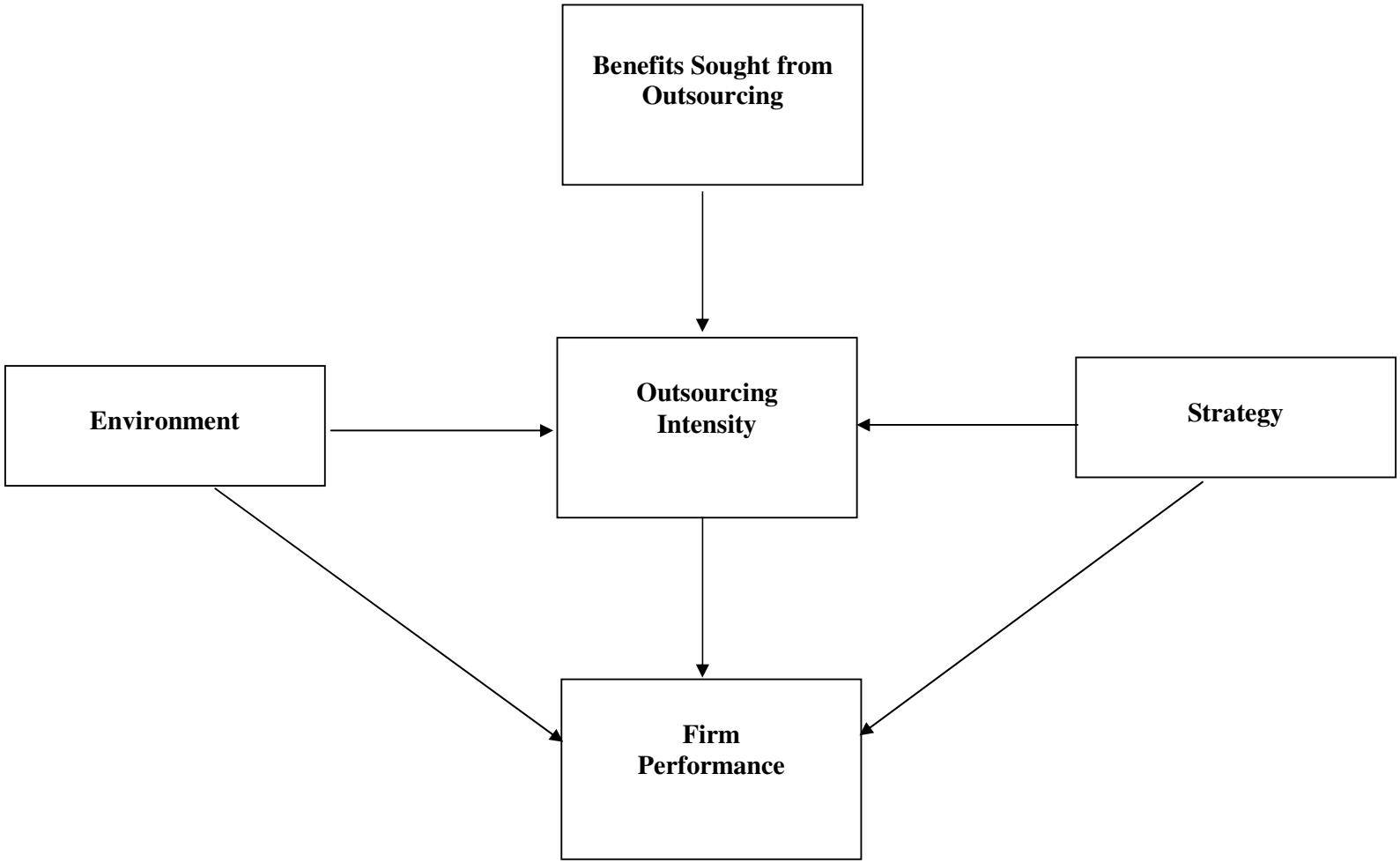
The combination of three perspectives, together, transaction cost economics, the core competence perspective and the agency theory perspective help us to develop an integrated model for outsourcing decisions. This theoratical model is based on several researchers but mainly influenced by the works of Giley (1997) and Jiang (2004).

The main objective of this study is to find answers to questions like ' Are benefits sought from outsourcing different for firms pursuing different generic firm strategies?', 'Are different levels of outsourcing intensity changing according to benefits sought positively affect firm performance?', ' Is environment an effective factor in moderating this outsourcing - performance and strategy fit?'. To answer these questions, we hypothesize theoratically feasible sets of hypothesis between generic firm strategies and outsourcing intensity which lead to different achievement of firm performance.

The aim is to develop a multidimentinal model for analyzing the outsourcing, performance and strategy relationship and figuring out the best fit of outsourcing decisions and benefits with firm strategy to maximize firm's financial and non-financial performance in different environments. The detailed proposed research model is explained in the next chapter by providing dimensions and definitions of each variable within the related perspective.

In this study, the direct affect of strategy on firm performance will be analyzed through outsourcing intensity. Strategy of the firm is proposed to directly affect the performance of the firms (Porter, 1980; Weinzimmer, 2000) and the performance is the outcome of the fit between several factors as strategy, capabilities and environment (Bergeron, Raymond and Rivard, 2004).

Figure 2.7 Proposed Theoretical Research Model



2.3. Research Focuses of Current Outsourcing Research

Research focuses of outsourcing can be identified by many areas: definitions of outsourcing, the outsourcing framework, the outsourcing methodology, the benefits and risks of outsourcing, global outsourcing, best practice outsourcing, popular organizational fuctions to outsource, trends in outsourcing, and organizational performance implications of outsourcing. In this section, the intention is to get a big picture of what the outsourcing researchers are doing. By examining a variety of research foci, we would like to identify current outsourcing research scopes and gaps in outsourcing research.

2.3.1 Definitions of Outsourcing

There seems to be confusion in the management literature about what is meant by the term 'outsourcing'. Generally, the definition of outsourcing used in prior studies is so broad that it includes virtually any good or service that an organization procures from outside firms. Different operational definitions of outsourcing are examined in previous sections but we would like to address to Giley and Rasheed's (2000) definition one more since it calls attention to the strategic nature of the concept.

Giley and Rasheed (2000) believe that defining outsourcing simply in terms of procurement activities does not capture the true strategic nature of the issue. Outsourcing is not simply a purchasing decision ; all firms purchase elements of their operations. They suggest that outsourcing is less common and represents the fundemental decision to reject the internalization of an activity. In this way, outsourcing is a srategic decision and has the potential to cause performance effects throughout the organization. According to Giley and Rasheed, outsourcing may arise through the substitution of external purchases for internal activities. In this way, it can be viewed as a discontinuation of internal production and an initiation of procurement from outside suppliers and may be reviewed as vertical disintegration. Sometimes, a firm also purchases goods or services from outside organizations when those goods or services have not been completed in-house in the past. In this case, organizations have no choice

but to outsource that particular good or service from a supplier. Giley and Rasheed define this situation as 'abstention' in contrary to the former situation which they define as 'substitution'. Similiar to Giley and Rasheed, Jiang (2004) also accepted this opinion and made this substitution / abstention distinction in defining outsourcing in his research while examining the outsourcing impact on the whole firm's value and performance.

2.3.2 The Outsourcing Framework and Methodology

Corbett M. F. (2004) presents the outsourcing framework which results in a list of potential areas where competitive and operational improvements are possible in his book 'The Outsourcing Revolution'. According to Corbett, the outsourcing framework is a starting point for listing and categorizing the activities that take place in an organization and by seeing activities across the organization under a common framework, it becomes much easier to evaluate each in terms of its relationship to others, to rate and rank its contribution to the organization's competitive advantages and to maintain focus on how it is sourced.

Greaver II (2004), suggests the seven steps to successful outsourcing which are summarized in the Table 2.2. The steps can and should be modified to fit the specific organization and outsourcing situation. According to Greaver, many of the steps are interrelated and should run somewhat parallel. This is important because,

- There is constant learning, testing, and adjustment to the outsourcing project as it progresses. The value of this new information would be lost for the earlier steps if the steps were rgidly followed sequentially.
- If there is not continuous referral to the early steps, it is possible for the project's purpose (reasons to outsource) to blur and wander on to undesired purposes.
- Running in parallel reduces overall project cycle time, getting to a go/no go decision quickly, which is very important to overall project success.

Table 2.2 Seven Steps to Successful Outsourcing

Planning Initiatives	Exploring Strategic Implications	Analyzing Costs and Performance	Selecting Providers	Negotiating Terms	Transitioning Resources	Managing Relationships
Assess risks. Announce initiative. Form project team. Engage advisers. Train the team. Acquire other resources. Address issues: • Resource management • Information management • Project management Set objectives.	Understand organization's: • Vision • Core competencies • Structure • Transformation Tools • Value Chain • Strategies Determine: • Decision rights • Contract lenght • Termination Date. Align initiative	Measure activity costs. Project future costs. Measure performance: • Existing and future • Cost of poor performance Benchmark costs/performance. Determine: • Specific Risks • Asset values • 'Make' total costs • Pricing models • Final Targets.	Set qualifications. Set evaluation criteria. Identify providers. Screen providers. Draft RFP. Evaluate proposals: • Qualifications • Costs Perform due diligence Determine: • 'Buy' total costs • Short-list providers • Finalist provider • Review with senior management.	Plan negotiations. Address: • High-level issues • Deal breakers Prepare term sheets. Negotiate contract: • Scope • Performance standards • Pricing schedules • Terms and conditions Announce relationship.	Adjust team roles. Compare/merge transition plans. Address transition issues: • Communication • Human resources • Other production factors Meet with employees: • Organization • Provider Make offers/termination Provide counselling. Physically move.	Adjust management styles. Set up oversight council Communicate Define and design: • Meeting agendas • Meeting schedule • Performance reports Perform oversight role. Confront poor performance. Solve problems Build the relationship.

Source: Adapted from 'Strategic Outsourcing – A Structured Approach to Outsourcing Decisions and Initiatives', Maurice F. Greaver II (1999).

2.3.3 Benefits and Risks of Outsourcing

Although the results of outsourcing have not fully proven by archival data, there are many potential benefits and risks identified in the literature. These are mostly improved financial performance and non-financial performance effects. Jiang (2004) classified and explained the benefits and risks of outsourcing as in the following:

Main benefits associated with outsourcing are as follows:

2.3.3.1 Cost Savings and Profitability

Outsourcing firms often achieve cost advantages relative to vertically integrated firms (Bettis, et al., 1992; Kotabe, 1992; Lei & Hitt, 1996; Quinn, 1992). Through outsourcing noncore activities, manufacturing costs decline and investment in plant and equipment can be reduced (Bettis et al., 1992). This reduced investment, in manufacturing capacity lowers fixed costs and leads to a lower break-even point. The short-run cost improvement swiftly reinforces the outsourcing desicion. Thus, outsourcing may be an attractive method of improving a firm's financial performance, especially in the short-run.

2.3.3.2 Access to State-of –the-Art-Technology

The volatility of technology can quickly make current skills obsolete. For example, software is updated and replaced very rapidly – by the time an entity invests in and trains its full-time staff, the technology may no longer be state-of-the-art. Outsourcing specialists must be well trained and up-to-date to survive. Firms focusing on outsourcing can switch suppliers as new, more cost effective technologies become available.

2.3.3.3 Quality, Productivity and Flexibility

Outsourcing may contribute to other advantages as well. In-house production increases organizational commitment to a specific type of technology and may constrain flexibility in the long-run (Harrigan, 1985). In addition, outsourcing allows for quick response to changes in the environment (Dess, et al., 1995) in ways that do not increase costs associated with bureaucracy (D'Aveni & Ravenscraft, 1994). Vendors often can tap a wide range of resources, skills and capacities while internal staff may have limited capabilities. One additional advantage of outsourcing is that it tends to promote competition among outside suppliers, thereby ensuring availability of higher-quality goods and services in the future (Kotabe&Murray, 1990). Quality improvements may also be realized by outsourcers, because they can oftentimes chooses suppliers whose products or services are considered to be among the best in the world (Dess et al., 1995; Quinn,1992). Thus, firms that outsource may achieve long-run advantages compared to firms relying on internal production. As noted by Quinn, 'virtually all staff and value chain activities are activities that an outside entity, by concentrating specialists and technologies in the area, can perform better than all but a few companies for whom that activity is only one of many' (1992).

2.3.3.4 Focus on Core Competency

An increased focus on a firm's core competencies is another important benefit associated with outsourcing (Dess et al.,1995; Kotabe&Murray, 1990; Quinn, 1992; Venkatraman, 1997). Outsourcing noncore activities allows the firm to increase managerial attention and resource allocation to those tasks that it does best and to rely on management teams in other organizations to oversee tasks at which the outsourcing firm is at a relative disadvantage. Giley and Rasheed (2000) use two examples to explain this benefit: Honda's core competence is in small engine production and, therefore, the domain of Honda's activities can be seen as any business in which this core competence finds an application. Nike's core competencies are in the design and marketing of shoes rather than in their manufacture. Therefore, Nike has focused on these aspects of the

athletic shoe industry and has relied on outside firms for virtually all manufacturing activities.

On the other hand, Jiang (2004) explained the main risks of outsourcing as lack of innovation and organizational learning, supplier ethics, high switching costs, loss of control, and bad for employee morale:

2.3.3.5 Lack of Innovation and Organizational Learning

One of the most serious threats resulting from a reliance on outsourcing is declining innovation by the outsourcer. Outsourcing can lead to a loss of long-run research and development competitiveness (Teece, 1987) because it is often used as a substitute for innovation. As a result, firms that outsource are likely to lose touch with new technological breakthroughs that offer oppertunities for product and process innovations. (Kotabe,1992).

2.3.3.6 Supplier Ethics

In addition, as suppliers gain knowledge of the product being manufactured, they may use that knowledge to begin marketing the product on their own (Prahalad & Hamel, 1990). In fact, firms from the Pacific Rim, have a well-established pattern of market entry based on outsourcing partnerships (Willar & Savara, 1988). Many Asian firms have made their initial entrance into U.S markets by first entering supplier arrangements with U.S. manufacturers, and subsequently marketing their own brands aggressively. In this way, many Asian firms have achieved market dominance.

2.3.3.7 High Switching Costs

A shakeout has taken place among IT vendors, with mergers and takeovers becoming commonplace. It is like that fewer suppliers will survive in the future, making it more difficult to shop for the right price. Furthermore, IT professionals argue that outsourcing allows the user to become a 'hostage' of the vendor – the company may lose

technical staff and be locked into the vendor's proprietary software and hardware. In a long-term contract, the customer has more leverage in negotiations, but the vendor has more leverage after outsourcing is under way.

2.3.3.8 Loss of Control

Critics or outsourcing argue that no outside vendor can match the responsiveness and service levels offered by an in-house function, largely because the outsider is not subject to the same management direction and control as employees. Some managers come to regret that the vendor's employees – often working full-time inside the user organization – do not display the same commitment and dedication shown by the inside staff (Lacity and Willcocks, 1996). Bryce and Useem (1998) analogize this problem as: 'a mercenary may shoot a gun the same as a soldier, but he will not create a revolution, build a new society, or die for the homeland'.

2.3.3.9 Bad For Employee Morale

Outsourcing often results in layoffs or the transfer of existing employees to the vendor. Such displacement can set morale into a tailspin and cause even talented staff to fear for their employment security.

2.3.4 Global Outsourcing

It is also worth mentioning the increase in the number of articles focusing on Offshore or Global Oousourcing. Global sourcing strategy has been one of the most hotly debated management trends in the last 20 years. The use of cheaper communications technology, the Internet, economic globalization, and easy access to IT professionals with lower salaries are some of the reasons for this (Khan and Fitzgerald, 2004). In its early years, global sourcing was examined mostly from 'in-house' development and procurement perspectives; and in the last several years, research focus has shifted to 'outsourcing' activities. Along with this shift from internal to external

focus on global sourcing, many researchers and business preactioners have applied a core competency argument to justify increased levels of outsourcing activities on a global basis. Although the beneficial aspects of outsourcing are assumed in most cases, no consensus exists in reality as to the effect of outsourcing. Furthermore, the increased instability of the exchange rate environment in the last several years has also led to increased difficulties in managing globally scattered operations that were once fashionable in the 1980s-90s under the rubric of global strategy (Kotabe and Murray, 2003).

2.3.5 Best Practice Outsourcing

The pursuit of outsourcing best practice is related to achieving superior performance on behalf of the host organization. However, a variety of views exist as to the nature of best practice and even what is best practice through the various stages of an outsourcing contract (Kakabadse &Kakabadse, 2000). With the potential to realize extensive gain in the pursuit of competitive adavntage but with hte equal possibility of inflicting considerable damage to the organization, best practice outsourcing is becoming a focal point of attention (Kakabadse and Kakabadse,2002).

An analysis of the literature emphasizes the variety of interpretations of best practice from the planning stage of outsourcing to the selection of suppliers, to the implementation and monitoring of the contract (Table 2.3).

Table 2.3 Perspectives on Best Practice Outsourcing

Authors	Stage of Outsourcing	Best Practice Issues and Questions
Manion et al. (1993)	**Planning**	**Questions:** • What are the proposed savings measured against? • Can the outsourcer achieve economies of scale that the client could not? • Is the guaranteed price a good deal? • Can the outsourcer buy equipment and hardware cheaper? • Does the client have a process to determine if outsourcing is the correct strategy to pursue? • Overall, should the client leave support operations to specialists?
Gamble (1995)	**Planning**	**Questions:** • What will be the net gain or loss in performance quality through outsourcing? • What will be the net effect on the strength, versatility and resourcefulness of the organization if the activities in question are outsourced? • What is the level of dependence on third parties? • How vulnerable would the organization become if that third party were unable to perform as expected?
Kelly (1995)	**Planning**	**Key issues:** • Determine what business you are in • Look for outsourcing opportunities • Evaluate costs of outsourcing • Monitor • Be flexible • Don't jump on the bandwagon
May (1998)	**Managing**	**Technical competencies:** * Costing * Contract Law * Organization and Management (O&M) analysis * Purchasing **Behavioural Competencies:** * Listening skills * Communication skills * Lateral Thinking * Persuasiveness * Cultural awareness

		* Systems design * Team working * Probabilistic forecasting * Loss evaluation * Benchmarking * Market and economic research * Decision taking * Negotiating
Quinn (1999)	**Planning**	**Key issues:** • Define few core competencies (two to four) • Outsource everything that is not core or does not protect core competencies
Lankford and Pars (1999)	**Planning**	**Considerations:** • Competence factors utilized in evaluating suppliers (e.g. flexibility, understanding the company's business. • Bid evaluation procedures including specifiic evaluation of low bids. • Precisely defined scope of work, detailing the nature and xtent of collaboration between buyer and supplier. • Safeguards for performance and cost control.
Insigna and Werle (2000)	**Strategy**	**Considerations:** • Alignment of the outsourcing with the business strategy of the enterprise. • Clarification of core capabilities and competencies (value or potential value of an activity should be established on the basis of market principles, not operational principles). • Identification of strategic gaps and specific strategies for cost saving and asset shedding. • Recognition of the enterprise's significant dependencies and vulnerabilities.
McIvor (2000)	**Framework for evaluating outcomes**	**Considerations:** • Define the core activities of the business on two levels – formal and reactionary • Evaluate the 'value add' of relevant value chain activities. • Total cost and benefit of activities – both internal and estrimate of external cost. • Relationship of analysis.

Useem and Harder (2000)	**Implementation**	Management Capabilities • Strategic thinking • Deal making • Partnership management • Leading through change
Gay (2000)	**Implementation and monitoring**	Need to have • Clear objectives • Work towards agreed objectives • Agreed frequency of review • Agreed dates and submissions for review • Agreement on arbitration • Feedback and learning sessions.
Bendor-Samuel (2001)	**Selecting Supplier**	Supplier considerations • Best in class leverage • Scale • Expertise • Access

Source: Adapted from Kakabadse A. and Kakabadse N. (2003), 'Outsourcing Best Practice: Transformational and Transactional Considerations' , Knowledge and Process Management, Vol 10, Number 1, pp 60-71.

2.3.6 Popular Organizational Functions to Outsource

Among the popular organizational functions to outsource, particular emphasis has been given to IT outsourcing in the academic and more popular business press literature. (Murray and Kotabe, 1999).Global competition, downsizing, the move to flatter organization, the search for greater flexibility, rapid changes in technology and the emphasis on concentrating on core competencies, are cited as the major drivers for the upsurge in IT outsourcing. In the IT industry, data storage capability has dramatically increased in quality and at the same time has undergone considerable price reduction, to the extent that data storage services are being charged on a cost-per-megabyte-per-month basis, in a similiar way that clients pay for utilities such as

electricity and water (Nairn, 1999). Further, outsourcing suppliers are looking beyond running IT systems to business process management (BPM). It is the move to outsourcing BPM that has equally provided a stimulus for the emergence of shared service centers (SSCs). SSCs provide a range of IT services across particular sectors through the adoption of common technology systems and infrastructure, all to enhance economies of scale (Heikkila, 2000).

An international survey of outsourcing was undertaken in 2001 by Cranfield School of Management researchers to figure out current outsourcing practices between US and European companies. The study was undertaken in two stages; initial interviews with a sample of service purchasers and service providers in order to ascertain the key issues and trends in outsourcing. The interviews (whereby 747 respondents of senior managers returned) were followed by an emprically based survey of European (including UK) and US based organizations. In contrast to the emphasis given to IT outsourcing in the literature, the Cranfield survey, places basic services above IT services as the most popular area of outsourcing activity (Figure 2.5). Third are human resource (HR) activities and related processes. US companies pay greater attention to outsourcing basic services (a variety of services ranging from canteen facilities to office services), whereas European companies give marginally greater attention to IT, HR, and manufacturing outsourcing. Lower in the rankings, but considered as being of substantial importance to US and European companies is technology-based outsourcing, particularly in telecommunication services and e-commerce related activities, with the US companies displaying marginally greater preference in this area. In-keeping with the theme of outsourcing basic services, US companies report they give greater attention to facilities management outsourcing than do European companies. Moreover, the survey results indicated that US companies are identified as pursuing more value adding sourcing strategies while European companies are more focused on gaining economies of scale through outsourcing. Both European and US companies consider ousourcing as critical to their organizational strategy. (Kakabadse&Kakabadse, 2002).

After reviewing articles in this area to investigate the most popular functions to outsource, we see that particular emphasis has been given to HR outsourcing and

logistics outsourcing together with IT/IS outsourcing. We would like to give short reviews about each functional outsourcing area to cover literature to date.

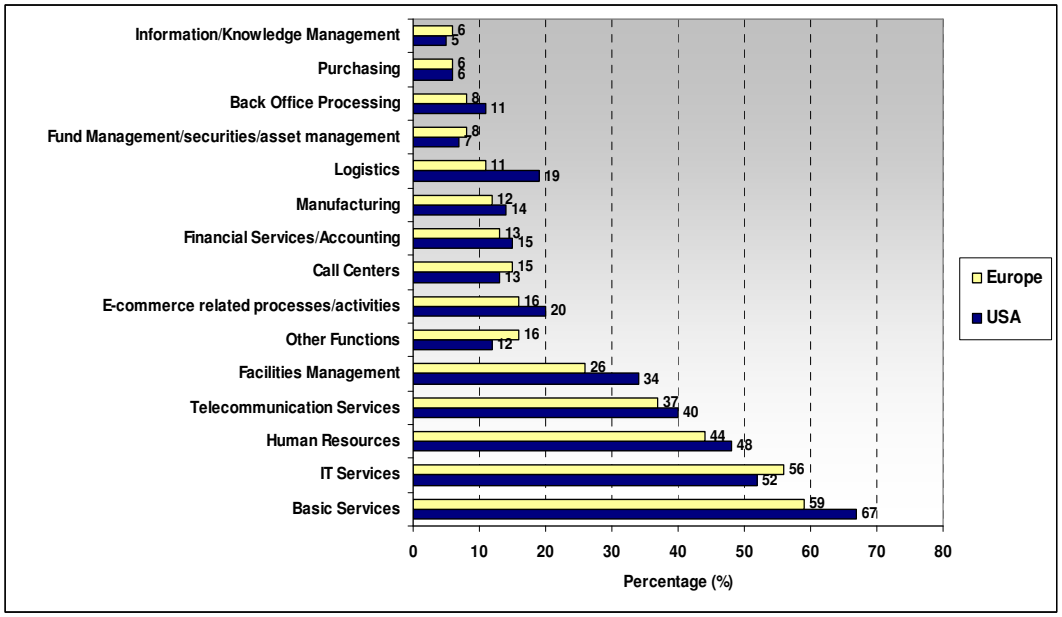


Figure 2.8 Business Processes/Functions Outsourced: International Comparison - adapted from Kakabadse & Kakabadse (2002), 'Trends in Outsourcing: Contrasting USA and Europe'.

2.3.6.1 Information Technologies / Systems Outsourcing

Outsourcing has become a basic strategy of the Information Systems field (Akomoge, Less, Irgens, 1998) and has experienced considerable growth in recent years. Forrester, forecasts that European enterprises will spend over EUR 128 billion on computer outsourcing in 2008 (Forrester, 2004) and the Gartner Group has estimated that the worldwide IT outsourcing market will grow from the US $ 180.5 billion revenues in 2003 to US $ 253.1 billion revenues in 2008 at a compound annual growth rate of 7.2%. Some of the largest IS outsourcing providers are IBM, EDS, CSC, Hewlett Packard, Oracle, General Electric, and HSBC (Gartner, 2005).

Based on a literature survey made by Gonzalez & Gasco & Llopis (2006), articles on IS outsourcing have been published for 18 years, the earliest dating back to 1988, and the most modern ones being published in 2005. No articles on IS outsourcing were published between 1988, when one article was released, and 1992. However, since then, the number of publications has soared as a result of the Kodak effect in 1989 (Loh & Venkatraman, 1992), after the Eastman Kodak Company outsourced its DP function to four vendors led by IBM and including DEC, Business Land and Anderson Consulting, too. This deal signaled the start of information systems outsourcing megadeals and also legitimized outsourcing. Prior to this outsourcing had apparently raised little interest (Hirschheim&Dibbern, 2002 ; Jurison, 1995). It is interesting to note that the article published in 1988 (Owen & Aitchison, 1988), did not use the term outsourcing anywhere in the text but used 'Facilities Management' instead. The term 'outsourcing' can be traced back to the 1990s (Tayntor, 2001), and in 2005 the largest number of articles (19) was published (Gonzalez & Gasco & Llopis 2006).

2.3.6.2 Human Resources Outsourcing

Two types of human resources activities, namely training and payroll are the most popular activities subject to outsourcing. Studies such as those by Frayne and Geringer (2000) and Harel and Tzafrir (1999), have found that training function can yield positive firm performance.Training efforts can be phenomenally expensive and because of such costs, HR profesionals have reported greater pressure to produce returns on investments in training (Bassi and McMurrer, 1998; Morrow et al., 1997). It appears that many HR departments are using outsourcing to enhance the value received from training expenditures, as a past survey found that 32% of companiesoutsource training (HR Focus, 1997). Similarly, survey results indicate that 38.4% of firms outsource their payroll functions (HR Focus, 1997). However, there have been a few emprical investigations of the performance effects of HR Outsourcing. Giley & Greer & Rasheed's emprical work in 2004 indicated that both training and payroll outsourcing have implications for firm performance (Giley & Greer & Rasheed, 2004). Lepak and Snell's (1998) model of virtual HR provides guidance to help determine which HR activities should be outsourced. In this model, unique and high value activities make up

the category of core HR activities, which are not candidates for outsourcing. In contrast, peripheral HR activities (low uniqueness and low value), idiosyncratic HR activities (low value and high uniqueness), and traditional HR activities (high value and low uniqueness) are all candidates for outsourcing.

Another emprical research for the performance effects of HR outsourcing is Butler's investigation in 2006. Butler's emprical doctoral dissertation examined the impact of the managerial decision to outsource human resources services on operating and capital market performance. The business strategy model and transaction cost economics provide a theoratical basis for examining this relationship. The decision to outsource involves, among other factors, choices concerning core competencies, organizational structure shifts, attributes of the outsourced function, and the trade off between production and transaction costs. Using archival accounting and financial data, Butler's research builds upon the limited and primarily survey method human resource outsourcing literature. Butler examined the performance effects of outsourcing from the perspectives of both the outsourcing or client firm and the human resource service provider. In making the decision to outsource human resource services, client firms consider the organizational factors and strategic goals potentially influenced by outsourcing HR services, the attributes of the specific HR functions and the cost trade-off between production and transaction costs, and other organization.Client firms expect improved performance as a result of outsourcing either through decreasing costs or increasing revenue from focusing on core competencies or value creating activities.

In contrast, specialized human resource services consider attributes of specific HR functions from a risk, cost and potential compensation perspective. Once a firm enters this market, performance is driven by its ability to provide profitable services to client firms and to maintain a sufficient client base. HR service providers offer a broad range of services including HR management, HR technology, regulatory compliance, risk management and payroll processing which encompass tasks that vary in complexity, uncertainity, frequency, asset specificity. These attributes determine, in part, the revenue available to HR service providers. Other factors that influence the profitability of human resource service providers are the benefits offered to client firms such as reducing costs

associated with HR services, allowing HR managers to focus on strategic HR issues by reducing the burden of performing some HR tasks internally, improving service to employees, and increasing efficiency in HR operations.

In view of these two stakeholders in the outsourcing contract, the overall results in Butler's investigation suggest that human resource outsourcing has a long run impact on operating performance and that investors value the contract announcements for both outsourcing firms and providers in the short term and in the long run. More specifically, a significant relation between HR outsourcing and firm operating and HR performance as return on assets, returns, and market value of equity, three years after the outsourcing announcement is reported by Butler. Additionally, outsourcing firms and human resource service providers experience significant and positive abnormal returns in a 2-day event window immediately following the outsourcing announcement. Butler, also reported that these firms experience significant and positive cumulative abnormal returns two and three years after the announcement suggesting that investors reward firms for initiating outsourcing agreements and anticipate increased cash flows as a result of this strategy in the short and long run. Outsourcing HR services is negatively related to cost of equity capital one and two years after the announcement implying that this additional disclousure is valued by investors. However, this benefit subsides, over time as the incorporation into the financial statements of the changes associated with implementing the outsourcing contract is delayed or the expected increased cash flows do not materialize.

Butler's research also provides an incremental contribution to the limited outsourcing research by incorporating several considerations not previously addressed in the literature. This research is most closely related to Giley's work in 2004, where the relation between two types of human resource outsourcing (payroll and training) and firm performance is investigated. This dissertation also examines the relation between HR outsourcing and firm performance, but includes all types of human resource services and uses archival financial data to measure firm performance. While most outsourcing research is approached from the perspective of the outsourcing firm, Butler's work considers not only the outsourcing firms'operating and market performance, but also the

human resource service provider's market performance. Finally, this research is important among other outsourcing studies is that it investigates the cost of equity capital implications of HR outsourcing because the implications of the outsourcing contacts affect firm performance.

Additional research for which HR activities to outsource is provided by a strategic typology developed by Alan Speaker (Greer, 2001). The two-by-two typology classifies HR activities on two dimensions: (1) type of activity, and (2) strategic value of activity. The model incorporates the evolving wisdom of strategic HR that the greatest performance impact can be obtained with relationship-oriented-high strategic value activities. Activities in this category include performance enhancement, consulting within the firm, employee relations, labor negotiations, and executive compensation. In contrast, transactional-low strategic value activities, such as payroll, benefits administration, employee records, and retirement administration, are clearly candidates for outsourcing. Outsourcing these activities enables the firmto achieve more efficient workforce, utilization by focusing on higher value activities. Thus, HR executives should see an imperative to move toward activities in the relationship-high strategic value category where they can make the most impact on organizational performance (Giley, Greer, Rasheed, 2004).

In addition to the theoratical rationales provided by transaction cost economics, the concept of competency, and the strategic HR perspective, there are additional rationales for HR outsourcing. These include specialized expertise, cost savings, reductions in liability or risk, and temprorary expansion of HR capabilities to meet extraordinary circumtances (Greer et al., 1999). However, there are exceptions to these rationales, such as when outsourcing an HR activity would make the firm vulnerable to being held hostage by a vendor. Another exception occurs when an activity can not be outsourced without compromising critical information that would make a firm vulnerable if it outsources its executive compensation function and confidential information is leaked to competitors that may then conduct raids on its executive talent. In addition, HR departments, get into trouble very quickly when outsourced activities

such as payroll, employee records, and retirement administration are not handled well (Speaker, 1999).

2.3.6.3 Logistics Outsourcing

Logistics outsourcing has faced significant growth in the last decades due to companies looking to reduce costs, improve service reliability, and increase inventory visibility. If well implemented and managed, such growth reflects the economic potential from logistics outsourcing. Logistics providers bring in value added services by streamlining the supply chain, they make logistics processes more effective by reducing transportation and warehousing needs (Facanha and Horvath, 2005).

As international competition intensifies, technological improvements and worldwide deregulation enable the creation of more sophisticated logistics systems and processes (Sheffi, 1990). Manufacturers have also been concentrating on their core business functions, which typically include product design, development, production, marketing and sales. This puts logistics processes in the category of support functions that can be outsourced to organizations whose core business is logistics-itself-third party logistics providers (3PLs).

From 1992 to 2000, the global logistics outsourcing industry has grown from $10 billion to $56 billion (Lynch, 2002). The current market size is approximately $65 billion, and net revenues for 3PLs increased 7% from 2001 to 2002 (Armstrong&Associates, 2003). Among the main functions outsourced are transportation management and warehousing, but third party logistics providers also handle customs brokerage, freight forwarding, vendor management, customer service, freight payment and quality control, among others. The complexity of those functions vary widely, ranging from simple domestic distribution programs to complex international programs involving intermodel-transportation, several distribution centers, and just-in-time manufacturing facilities. By outsourcing logistics functions, manufacturers and retailers are looking to focus on their core competencies while achieving cost savings brought by 3PLs.

A number of advantages and disadvantages of outsourcing logistics functions rather than performing them in-house have been identified in the literature. A user can reduce capital investment in logistics facilities, focus on core activities, reduce inventory, improve response rates to customers, and reduce logistics costs through outsourcing (Crum and Allen 1997; Lieb and Miller, 2002). There are, however, some factors that may work against outsourcing, such as loss of control, losing touch with important information, failure to select or manage providers properly, and lack of confidence in outside providers (Razzaque and Sheng, 1998). Previous studies have indicated that the outsourcing and non-outsourcing firms may differ in some firm-spesific characteristics, such as firm size, account size, degree of centralization, and degree of corporate control (Murphy and Poist 1998; Razzaque and Sheng 2002).

2.3.7 Trends in Outsourcing

There are two new trends encountered in literature associated with outsourcing – transformational outsourcing and business process outsourcing – both of which are strategic in nature.

2.3.7.1 Transformational Outsourcing

Transformatinal outsourcing is a special variety of outsourcing. It involves ongoing services that are critical to the performance of the business. In transformational outsourcing, 'what' is outsourced matters, and 'how' the initiative is structured is also important. But what matters more is the purpose of the initiative – the 'why' of outsourcing (Linder,2004). According to Linder, transformational outsourcing is defined most clearly by the objective of the initiatice as 'using outsourcing to achieve a rapid, sustainable, step-change improvement in enterprise-level performance' and transformational outsourcing is very different from conventional – tradiotional – outsourcing.

This conventional view of outsourcing holds that:

1. Outsourcing is appropriate only for noncore activities.
2. The primary benefit of outsourcing is reduced cost.
3. When executives outsource a function or process, they can turn their attention to more strategic matters.

However, transformational outsourcing holds a very diffrent set of precepts from conventional outsourcing. It is entirely appropriate for any activity that is critical to performance or growth. Whether these are core or not is a seperate question. Cost is and is always should be a factor that managers consider in any initiative, but transformational outsourcing targets a broader value equation since it is a tool of top management to achieve the company's strategic objectives.

Similiarly, Mazzawi (2002) makes the traditional and transformational distinction of outsourcing and describes transformational outsourcing as combining consulting, technology and outsourcing to stimulate and facilitate business change, helps to create and sustain the adaptive enterprise. Transformational outsourcing focuses on shedding non-core services and adding value by accessing best-practice and economies of scale in non-complex and non-core areas. It is about focusing on avoiding doing internally what others can do more efficiently and effectively. Mazzawi (2002) makes the traditional versus transformational distinction of outsourcing as in the following table:

Table 2.4 Traditional and Transformational Outsourcing

Traditional Outsourcing	Transformational Outsourcing
Operational Focus	Business focus
All about cutting costs	All about creating value
Helps impose control	Helps manage uncertainity
Aligns with fundementally unchanged business processes	Aligns with the business processes that change in line with strategic goals
Based on external IT specialists achieving higher performance than a non-specialist company economy	Based on the creation of a network of partnerships in the new connected
Removes non core functions from the business to	Business change and cost re-
engineering enable	
Provide a one-time release of capital	sustained value creation

2.3.7.2 Business Process Outsourcing

When process thinking is applied to outsourcing, it becomes business process outsourcing, BPO. BPO shifts the focus of traditional outsourcing and the way the relationships with outside specialists are defined and implemented – within discrete departments – toward a process-centric, end-to-end view of the business's activities.

Business process outsourcing represents an important expansion in where and how organizations are using outsourcing. Instead of focusing exclusively on neatly defined departments of work, business process outsourcing looks across the company to improve it, working in from the customer's perspective. It combines a process-centric view of the business with reengineering, technology, and supply chain consolidation to deliver not only a more efficient operation but a higher-value outcome for the customers.

Business process outsourcing fundementally repositions outsourcing from its traditional role as a tool for cost-cutting to one for process improvement, better customer service, and creation of new sources of revenue and business growth (Corbett, 2004).

2.3.8 Organizational Performance Implications of Outsourcing

To date, little is known about the firm-level outcomes of outsourcing decisions and the performance implications of varying levels of outsourcing intensity appear uncertain as mentioned before. Many authors (Giley&Rasheed 2000; Rodrigez&Robania 2004;Quelin &Duhamel 2003; Kakabadse&Kakabadse 2002; Barthelemy&Geyer 2001; Giley&Greer&Rasheed 2004; Arnold 2000; Kotabe&Murray 2004) have discussed the issue and have supported their positions with anectodal evidence. However, little systematic emprical work has been conducted to determine the influence of outsourcing decisions on firm's organizational performance.

By outsourcing to specialist organizations services not generated by core competencies, companies can see an improvement in their organizational performance (Bettis1992; D'Aveni&Ravenscraft 1994; Kotabe 1989; Lei&Hitt 1995; Quinn 1992). Giley and Rasheed state that there are three reasons for this. Firstly, the acquisition of non-strategic services allows the organization to centre on what it really can do well, that is on the services whose resources have a high strategic value. Such a focusing on services not included in the core competencies can increase performance and allow the company to be more flexible. Secondly, increasing the outsourcing of non-strategic services can improve both the quality and the service (Dess, 1995). This is because specialist organizations concentrate their efforts on a reduced set of functions, thus obtaining a better result than if the company carried them out internally. Lastly, the outsourcing of services of low strategic value enables the company to reduce costs and improve its competitive position (Giley&Rasheed, 2000).

After analyzing the outsourcing literature and the related theoratical perspectives on the concept, we see that the performance implications of varying levels of outsourcing appear uncertain.

2.4 Current Global Trends in Outsourcing

It is apparent from the literature that outsourcing (both supply chain and traditional back office functions) has been a regular feature of business life for many years. Global consultancy firm PricewaterhouseCooperhouse has conducted a global CEO Survey in 2006 where CEOs have indicated a marked shift in their motivation for using external suppliers, from simply as a mechanism to lower cost to a means of achieving a more strategic, collaborative framework. In tandem, CEOs pointed out of an increasing trend to expand the scope of activity that is covered by outsourcing arrangements, from the traditional component supplies and IT infrastructure to other activities that, in the past, were held sacrosanct, including human resource management and research and development.

Initially intended primarily to reduce costs, outsourcing is evolving into an integrated element in a strategy to increase companies' competitive advantage. This trend is underscored by the findings of this survey. Only 15% of CEOs interviwed claim that their relationship with suppliers is based entirely on lowest cost.

Recenty, the Economist Intelligence Unit (EIU) surveyed 187 senior executives on the subject of collaboration in November 2006. According to the report, more than one-half of all executives polled say collaboration will either form an important part of their firm's competitive advantage or will actually be central to its survival over the next three years. In today's economy, effective value chain management is increasingly about collaboration – that is, full alignment of business objectives and incentives among partners in the value chain. This is further validated in PricewaterhouseCoopers' Global CEO survey. When asked to describe their relationships with current suppliers, 29% of survey respondents reported that they were already fully aligned with their partners in the value chain. Interestingly, only small differences exist between developed economy company CEOs and their emerging economy counterparts in the assesment of outsourcing supplier relationships. According to the survey, the same is true regionally, with one exception: Central and Eastern European CEOs are far more likely to describe their relationships with suppliers as

based entirely on cost or lowest price. These companies that source more than 30% of their business from low-cost countries, are most likely to see themselves as fully aligned with their suppliers in cost and business benefit objectives (Figure 2.9). CEOs from emerging economies, Latin America, large companies and the retail sector report higher propensity to outsource a larger part of their businesses.

Propensity to Outsource	Global CEOs	Developed Economies	Emerging Economies	Latin America	Large Companies >$10 bn	Retail
Less than 10%	35%	42%	25%	19%	40%	48%
11-20%	12%	14%	9%	11%	19%	10%
21-30	6%	6%	6%	7%	8%	3%
31-40	4%	4%	4%	4%	4%	8%
41-50	2%	2%	3%	4%	1%	5%
More than 50%	11%	4%	22%	30%	8%	15%
Do not outsouce/have business in low-cost countries	24%	24%	23%	17%	13%	8%
Between 11-50%	26%	26%	22%	26%	32%	26%
Base	1,084	653	431	139	72	40

Figure: 2.9 Percentage of Business Currently Outsourced From, or Located in Low-Cost Countries

Source: Adapted from PricewaterhouseCoopers Global CEO Survey, 2006.

As outsourcing ceases to be purely a low-cost strategy, a shift is occuring in the elements of the value chain being outsourced and in what is perceived as adding value. Hints of a new value chain model in which even core functions are being outsourced are beginning to appear. PricewaterhouseCoopers survey notes a small but significant number of CEOs who derive competitive advantage from outsourcing activities that were traditionally perceived to be too strategically important to outsource, including R&D (12%) , human resources (11%), and even marketing and sales (9%), a trend that runs through a number of the CEO in-depth interviews. This willingness to allow normally tightly protected activities to migrate outside the company is a convincing signal of the degree to which the nature of outsourcing is changing.

On the other hand, when CEOs are asked about the geographic location of their current outsourcing activities in the survey, mixed responses are provided. As Figure 2.10 indicates, 35% of respondents reported that more than 10% of their current value chain is sourced from, or located in, low-cost countries. In three years time, this number is expected to have increased to 47%.

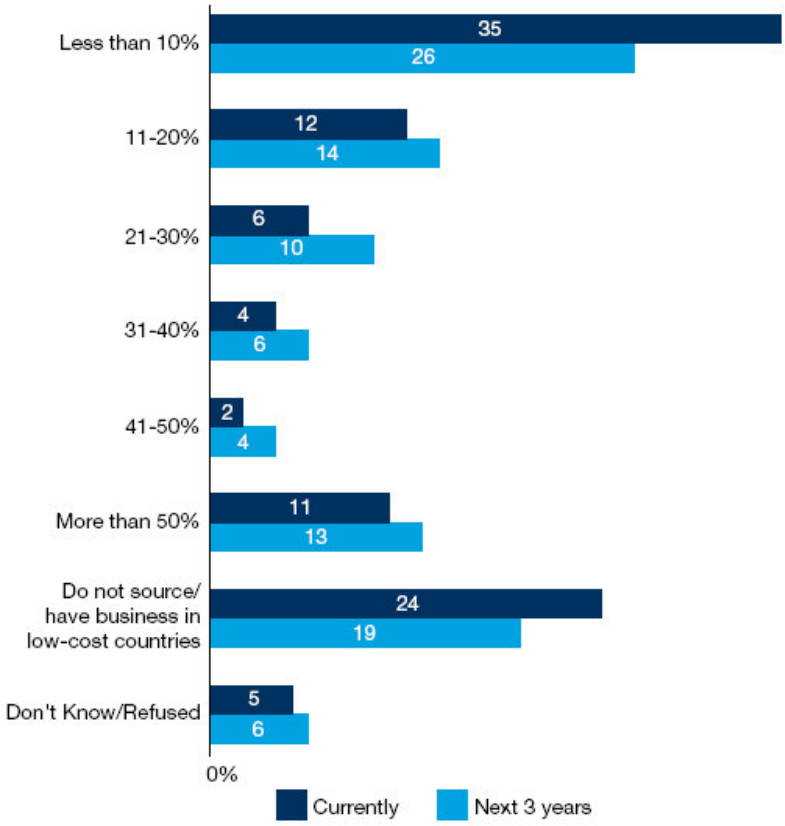


Figure: 2.10 Percentage of Business Currently Outsourced From, or Located in Low-Cost Countries (e.g Brazil, Malaysia, China and Ukraine currently and in the next three years)

Source: Adapted from PricewaterhouseCoopers Global CEO Survey, 2006.

According to A.T Kearney's research about top 10 outsourcing destinations as Figure 2.11 indicates in the following, India leads the way as the major outsourcing destination, followed by China. While India is significantly ahead, both destinations are regarded by CEOs as having the right elements to provide good services – a sound but low-cost business environment, complemented by the availability of skilled labour.

Asia dominates as the most desirable outsourcing region. However, it is expected that over the long term, outsourcing will increase significantly in Latin America, central and eastern Europe, and the Middle East.

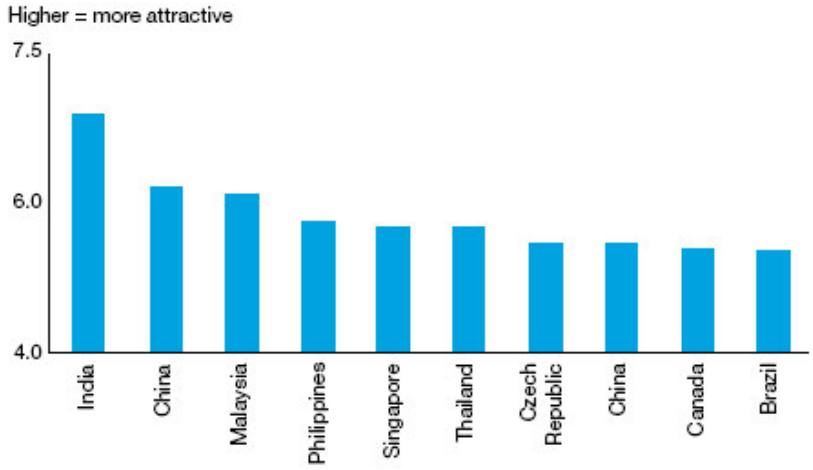


Figure: 2.11 Top 10 Outsourcing Destinations
(next three years)

Source: Adapted from A.T Kearney's Annual Global Services Location Index, November 2005.

Outsourcing is clearly a strategy that has been widely accepted by global companies, and that acceptance is growing as the current global trends indicate.

3. THE SPECIFICATION OF THE PROPOSED CONCEPTUAL RESEARCH MODEL ON PERFORMANCE IMPLICATIONS OF OUTSOURCING

In the previous section the proposed theoratical research model is given by combining the three theoratical perspectives namely; transaction cost , core competence and agency theory perspective. In this section, the detailed proposed research model is explained by providing dimensions and definitions for each variable and by comparing the model with other researchers' models.

Theorists in economics and managerial accounting deal with make-or-buy decisions and they approach the decision to outsource as a purely financial one and do not consider the context within with such decisions are made (Welch&Nayak, 1992).Our aim, on the other hand, is to analyze the outsourcing decision of a firm as an organizational process and thus begin with deeply analyzing the organization's strategies in conjunction with the firm's benefits sought from outsourcing. To determine a firm's overall reliance on outsourcing, a measure called 'outsourcing intensity', which lies in fact at the center of our model , is used. Firm performance, generic firm stragety, benefits sought from outsourcing and environmental dynamism are the other variables presented in our theoratical research model.

Outsourcing Intensity

To determine a firm's overall reliance on outsourcing, a measure called 'outsourcing intensity' is used (Table 3.1). Giley (1997) suggests that a firm's dependence on outsourcing can not be measured simply by the number of activities that the firm outsources. According to Rasheed, examining a firm's level of outsourcing only in terms of breadth (the number of activities outsourced as a percentage of the total number of activities in which the firm could be engaged) misses an important aspect of the phenomenon: how much of those activities are outsourced. He suggests that only when a firm's breadth and depth (the extent to which a firm outsources a higher portion of that activity on average) of outsourcing are combined does an accurate picture of the

firm's reliance on outsourcing emerge. Giley calls this combined construct as ' outsourcing intensity' and two types of outsourcing intensity are proposed in his model: peripheral and core. The first type occurs when firms acquire less strategically relevant, peripheral activities from external suppliers. The second category occurs when firms acquire activities that are considered highly important to long-run success in their industry from outside suppliers.

Table 3.1 Outsourcing Intensity Measure

Variable	Operational Definition	Source
Outsourcing intensity	a measure constructed to determine a firm's overall reliance on outsourcing (the larger a firm's value of outsourcing intensity, the greater is the role that outsourcing plays in its strategy making and calculated separately for core and non-core activities)	Giley (1997); Giley&Rasheed (2000)

Our outsourcing intensity measure is constructed similarly to Giley's. We use the American Management Association's outsourcing survey instrument to list the distinct activities in functional business categories of a firm. This list is subsequently cross-checked with several items discussed by Porter (1985) in defining the value chain activities. This list does not include all activities in which organizations are engaged but serves for an adequqate job of capturing the main business activities present in firms opearating in any sector.

Table 3.2 List of Activities in Organizational Functions of a Firm

Organizational Functions	Activities
Finance and Accounting Functions	• Bookkeeping • Clerical Functions • Data Processing
General and Administrative Functions	• Building Maintenance and Cleaning • Clerical Functions • Mailroom Activities • Moving&Storage • Office Design • Office Supply
Human Resources Functions	• Benefits Administration • Payroll • Recruiting • Regular Staffing (Employee Leasing) • Temprorary Staffing • Training - Functional • Training – Management & Supervision
Information Systems Functions	• Batch Processing • Data Communication • Voice Communications • Installation / Maintenance • PC Supply / Maintenance • Photocopying • Systems Design
Marketing Functions	• Advertising • Customer Service • Publicity & Promotion • Sales - Direct Mail • Sales - Representative • Sales- Telemarketing
Transportation & Distribution Functions	• Employee Business Travel • Intra Office Delivery • Product Service Delivery
Manufacturing Functions (Manufacturing Firms Only)	• Component Design • Packaging • Product Assembly • Product Design

Source: Listed here are 37 activities in the AMA questionnaire. Eric Rolfe Greenburg and Carol Canzoneri, 'Outsourcing: The AMA Survey', American Management Association Research Reports, 1997, New York.

To measure '**the outsourcing intensity'** of the listed activities, respondents are asked to indicate the level of outsourcing intensity on a 6 – point Likert type scale, with 1 indicating '**not outsourced'** and 6 **'totally outsourced'.**

To better understand the nature of the activities that are being outsourced and their contribution to competitive advantage of the firm (similiar to Giley's peripheral and core activity distinction) respondents will be asked to indicate the extent to which each activity listed in the table is important to profitability, superior performance and sustainable competitive advantage in their industry. Respondents are asked to indicate the significance of each activity on a separate 6 point scale (1= not at all important to 6= extremly important). Activities receiving scores above the median, will be categorized as activities related to core business functions of the firm which serve for sustaining competitive advantage.

Firm Performance

Firm performance has long been the primary dependent variable in strategic management research. However, prior firm performance can not be looked upon only as an outcome of organization-environment interactions. Rather it must also be viewed as an important input to managerial decision making. As a result, a firm's historical performance may be an important independent variable that influences a number of managerial decisions, including outsourcing strategies (Giley, 1997). Child (1974) provides a discussion of the importance of firm performance as an independent variable and states that the performance levels achieved by an organization constitute a vital input of information to its managers that is likely to stimulate them to make adjustments in polies and modes of operation. Child states that it is unrealistic to regard performance only as a variable dependent on other factors.

When faced with declining business performance, firms may seek to restructure their operations through a redeployment of their assets (Harrigan,1980). One way in which organizational assets may be redeployed is through outsourcing arrangements with outside suppliers. Bettis et al. assert that pressure for improved returns often causes managers turn to outsourcing as a 'quick fix'for their inefficiencies. This is likely a result of a focus on short-run cost reduction as opposed to long-run technological superiority. (Hayes & Abernathy, 1980). Because higher levels of internalization can cause inefficiencies to develop due to problems of coordination and control, managers may use greater levels of outsourcing during periods of performance decline (Giley, 1997).

In line with the arguments above, we will hypothesize this firm performance and outsourcing relationship. Many of the privately held firms are unlikely to provide objective financial data, and their executives are expected to be unwilling to provide detailed accounting data. Therefore, we find it appropriate to use subjective measures of financial performance and ask firm performance questions based on Dess and Robinson (1984). Dess and Robinson (1984) provide strong evidence of the validity and reliability of this type of subjective measures of performance. Each respondent will be asked to rank his/her firm's performance compared to other similiar firms in their industry on sales growth, after tax return on sales, after tax return on total assets, and overall financial performance over the last 12 months.

Following Ventatraman and Ramanujam's (1986) and Giley and Rasheed's (2000) suggestion, broader measures of firm performance will be examined to determine the effects of outsourcing on overall organizational performance. Cameron (1978) and Chakravarty (1986) have both used multiple measures to reflect the multidimentionality of the performance construct.

To determine each firm's non-financial performance, respondents are asked to rate their firm's R&D outlays, stability/growth of employment, process innovations,

product innovations, employee compensation, employee morale/job satisfaction, customer relations, supplier relations relative to their competitors. For both financial and nonfinancial performance, responses are coded on a 6-point scale (1=at the bottom of similiar firms in the industry to 6=at the top of similiar firms in the industry. Survey question is 'Please rate your firm's performance relative to similiar firms in your industry over the last 12 months).

Table 3.3 Firm Performance Measure

Variable	Operational Definition	Source
Sales Growth	The percentage change in gross sales (change in gross sales/ gross sales)	Dess&Robinson (1984)
Assets Growth	The percentage change in total assets (change in total assets / total assets)	McGulre& Sundgren&Schneeweis, (1988), Dess&Robinson (1984)
Return on Assets	A measure of operating performance of how well assets have been employed since being received by a firm	McGulre& Sundgren&Schneeweis, (1988), Dess&Robinson (1984)
Operating Income Growth	The percentage change in operating income (which is net sales less cost of goods sold and operating expenses before deducting non-cash expenses)	McGulre,&Sundgren&Schneeweis, (1988)
Return on Sales	The ratio of net income to total sales of the firm	Dess&Robinson (1984)
Overall financial performance	Accounting-based performance measured by ROA, total assets, sales growth, assets growth, operating income growth	McGulre& Sundgren&Schneeweis, 1988), Gilley&Rasheed (2000)
Research& Development Outlays	The amount of money spent for product and process innovation & improvement	Cameron (1978), Chakravarty (1986), Ventatraman& Ramanujam (1986), Giley& Rasheed (2000)
Stability of Employment	Keeping an effective workforce within an organization	Cameron (1978), Chakravarty (1986), Ventatraman& Ramanujam (1986), Giley& Rasheed (2000)
Growth of Employment	The percentage change in number of total employess	Cameron (1978), Chakravarty (1986), Ventatraman& Ramanujam (1986), Giley& Rasheed (2000)
Process Innovations	The introduction of new technological processes such as improved manufacturing facilities, increasing product quality, and faster distribution	Cameron (1978), Chakravarty (1986), Ventatraman& Ramanujam (1986), Giley& Rasheed (2000)
		Cameron (1978), Chakravarty (1986),

Process Innovations	The introduction of new products or products' physical atributes and capabilities	Ventatraman& Ramanujam (1986), Giley& Rasheed (2000)
Employee Compensation	Monetary payments (wages, salaries) and non-monetary goods/commodities (benefits,vacations) used to reward employees	Cameron (1978), Chakravarty (1986), Ventatraman& Ramanujam (1986), Giley& Rasheed (2000)
Employee Motivation	Forces either within or external to employees toward the accomplishment of organizational goals	Cameron (1978), Chakravarty (1986), Ventatraman& Ramanujam (1986), Giley& Rasheed (2000)
Job satisfaction	A positive attitude toward one's job	Cameron (1978), Chakravarty (1986), Ventatraman& Ramanujam (1986), Giley& Rasheed (2000)
Customer Relations	Relations with the people and organizations in the environment who acquire goods or services from the firm	Cameron (1978), Chakravarty (1986), Ventatraman& Ramanujam (1986), Giley& Rasheed (2000)
Supplier Relations	Relations with the people and organizations who provide the raw materials the organization uses to produce its output	Cameron (1978), Chakravarty (1986), Ventatraman& Ramanujam (1986), Giley& Rasheed (2000)

Firm Strategy

A key principle of strategy is to concentrate resources in selected areas that have the potential to provide competitive advantage (Henn, 1985). By applying this principle to outsourcing, it can be argued that to increase performance, firms should concentrate on activities providing a source of competitive advantage, such as improved quality of service or innovation, and outsource all other activities that outside firms can do better and more efficiently. In management literature, there are three main levels of strategies; corporate, business and functional. A firm's business-level strategy may have an important influence on the intensity with which it chooses to outsource its activities.

Therefore, this study will mainly focus on the business level strategies of the outsourcing firms.

Porter (1980) proposes three generic strategies for organizations to gain competitive advantage. These strategies are; cost leadership, differentiation, and focus.

Firms following a cost leadership strategy produce and sell products or services at a lower price than competitors and hence become low cost producers in an industry (Rauch and Frese, 2000). A cost leadership strategy is distinguished by an organizational focus on having the lowest costs in the industry. The primary goal of a cost leader is reducing total costs by increasing efficiency. A cost leadership strategy is characterized by incremental improvements in production and distribution that are directed at cost minimization (Porter, 1980). This strategy does not ignore quality, service or innovation but focuses on producing at the lowest cost compared to competitors (Dess&Davies, 1984). Products become more standardized and production runs become longer the more a firm emphasizes cost leadership. This allows organizations pursuing cost leadership strategy to take full advantage of economies of scale. It will be hypothesized that a cost leader will attempt to reduce total costs by outsourcing many activities. Thus, a cost leader is supposed to pursue intense outsourcing strategies by keeping in-house only those activities at which it has an absolete cost advantage.

On the other hand, firms following a differentiation strategy, aim to create and sell products or sevices that are unique to customers in terms of innovation, quality or style (Miller and Toulouse, 1986).Differentiators distinguish themselves by providing higly unique products or services. For differentiators, cost containment is important, but is secondary to delivering a distintive product. This uniqueness allows the firm to set prices higher than the industry average (Dess and Davies, 1984). The uniqueness of products/services can be achieved through severalactivities like creating a design or brand image, offering innovative technology or providing superior customer service. The main aim of differentiation strategy is to create loyalty among buyers. This will lead to higher sales margin. The differentiation strategy requires extensive expenditure on R&D activities and marketing (Miller and Friesen, 1986). Miller (1986) noted that there are at

leat two types of differentiation strategies: marketing differentiation and innovative diffrentiation. First one focuses on image management through marketing efforts and the second one strives for creating the most attractive products. In our study, both types of differentiators are proposed to approach outsourcing in the same way.

To maintain control over their sources of differentiation, differentiators are supposed to pursue less intense outsourcing strategies. Harrigan (1984) suggests that it is important for differentiators to understand the complex interorganizational exchanges that drive the firm's differentiation and retain those activities inhouse. Thus, despite cost advantages that may arise from shifting production of many activities to outside suppliers, differentiators are proposed to maintain higher levels of internalization to keep control over their diffrentiation-enhancing internal transfers (Barney, 1997). So, cost leaders are supposed to pursue more intense outsourcing strategies than do differentiators.

The focus strategy, the third generic strategy, on the other hand uses either of these strategies on a narrow geographic market, certain group of customers or a specialized product line (Miller and Toulouse, 1986). Porter (1980) argues that firms should not try to apply these strategies at the same time. Otherwise, the firm will 'stuck in the middle'. These strategies are alternatives to each other in dealing with environmental forces.

Firm strategy will be measured by using three subscales: cost-leadership, differantiation and focus following Porter's generic competitive strategies. Porter lists some of the commonly required skills and resources, as well as organizational requirements (Porter, 1980). In light of Porter's requirements for generic competitive strategies, we will develop our strategy items.

Table 3.4 Generic Firm Strategy Measure

Variable	Operational Definition	Source
Cost Leadership	Producing and selling the products or services at a lower price than the competitors	Baum et al. (2001), Pelham (1999)
Differentiation	Creating and selling products or services that are unique to customers in terms of innovation, quality or style.	Baum et al. (2001), Pelham (1999)
Focus	Focusing on a narrow geographic market; certain group of customers or a specialized product line	Baum et al. (2001), Vorhies & Harker (2000)

Environment

The strategies are the systems through which organizations try to fit their environment (Baum et al., 2001; Covin et al., 1990; Porter 1985) and in the studies of strategy, environment is a vital component (Covin et al. 1990). Environmental impacts on organizational strategies, structures, processes and performance have been the subject of many studies in the literature in the last four decades (Bourgeouis, Mc Allister, & Mitchell, 1978; Burns & Stalker, 1961; Dess & Beard, 1984; Downey, Hellriegel,& Slocum, 1975; Duncan, 1972; Emery & Trist, 1965; Fredrickson, 1984; Hitt, Ireland & Palia, 1982; Hrebeniak & Joyce, 1985; Jauch & Craft, 1986; Koberg & Ungson, 1987; Lawrence & Lorcsch, 1967; McCabe, 1990; Milliken, 1987; Prescott, 1986; Tosi, Aldag, & Storey, 1973; Giley 1997). Therefore, in the presence of strategy, the environment of the organization is usually taken into consideration. None of these studies have specifically addressed the relationship between environmental dynamism and outsourcing strategies except for Giley (1997). In Giley's work, there were significant

results. The relationship between outsourcing and firm performance was positive in stable environments, but negative in dynamic ones.

The relative dynamism in a firm's external environment may have important effects on outsourcing intensity (Giley; 1997). 'Environmental dynamism' is defined as 'the rate of change and innovation in an industry as well as the uncertainity or predictability of the actions of competitors and customers' (Miller and Friesen, 1982). Environmental dynamism is especially useful as an exploratory variable in organizational studies. The dynamic environment is influential on variety of management practices from strategy formation to performance (Miles et al., 2000). For instance, it is proposed that in dynamic environments organizations have to be innovative. Otherwise, they will have difficulties in keeping their market share (Miller,1988). Dynamic environments provide opportunities for the organizations. In dynamic environments, the diffrentiation strategy which mainly focuses on the adaptability to the environment is more beneficial. Cost leadership strategy, on the other hand, which is inflexible and requires rigid production and management practices may lower the performance levels of organizations. (Miller and Toulouse, 1986).

Harrigan (1983) found that internalization of tasks is ideal for firms in stable environments. Conversely, D'Aveni and Ravenscraft (1994) argue that, when industry demand is uncertain, internalization can lead to higher administrative costs and lower margins as a result of coordination and information processing costs. Also, uncertainity with respect to demand makes outsourcing attractive because it allows firms to shift much of the risk associated with declining demand (such as idle equipment and head count reductions) to supplier firms. Finally, the changes in technology that accompany high levels of environmental dynamism can make what was once a very valuable organizationaltechnology to become suddenly obsolete. By increasing their reliance on outsourcing during times of high environmental dynamism, managers may have the flexibility to change suppliers as technological advancements warrant (Giley, 1997).

In line of the arguments above, we will propose that firms operating in dynamic environments will pursue more intense outsourcing strategies.

Table 3.5 Environmental Dynamism Measure

Variable	Operational Definition	Source
Environmental Dynamism	the rate of change and innovation in an industry as well as the uncertainity or predictability of the actions of competitors and customers are dynamic	Miller & Friesen (1982)

Benefits Sought from Outsourcing

There has been a large volume of reserach about the disadvantages and advantages of outsourcing. The most often discussed are improved financial performance and various nonfinancial performance effects, such as heightened focus on core competencies. An increased focus on an organization's core competencies is the most noted benefit associated with outsourcing. (Dess 1995, Kotabe & Murray 1990, Quinn 1992) and outsourcing non-core activities allows the firm to increase managerial attention and resource allocation to those tasks that is does best. Although outsourcing's potential benefits are many, Bettis (1992) and Kotabe (1992) argue that reliance on outside suppliers is likely to lead to a loss of overall market performance. Declining innovation by the outsourcer, a loss of long-run R&D are most serious threats (Kotabe,1992).

Jiang (2004) classified and explained the benefits and risks of outsourcing as mentioned in the previous section. Maurice F. Greaver II. summarizes the benefits sought from outsourcing more comprehensively in six categories as in the following in his book 'Strategic Outsourcing – A Structured Approach to Outsourcing Decisions and Initiatives (1999). Greaver II notes that the critical point is to undertand the reasons and the benefits sought for considering outsourcing. According to Greaver II (1999), just as the probability of another person's suit of clothes fitting the other exactly

is remote, so too is the probability of another organization's resons to outsource fitting the other equally remote.

Organizationally Driven Benefits:

- Core competencies (enhance effectiveness by focusing on what you do best)
- Flexibility (increase flexibility to meet changing business conditions, demand for products and service, and technologies)
- Organization structure (transform the organization)
- Product or service value (increase)
- Customer satisfaction (increase)
- Shareholder value (increase)

Improvement Driven Benefits:

- Operational performance (increase operational performance through higher quality, increased productivity, shorter cycle times, increased outputs, greater profits)
- Technology and knowhow (obtain expertise, skills, and technologies that would not otherwise be available)
- Risk management (improve risk management)
- Innovation (acquire innovative ideas)
- Credibility and image (improve credibility and image by associating with superior providers)

Financially Driven Benefits:

- Cash generation (generate cash by transferring assets to the providers)
- Asset management (reduce investments in assets and free up these resources for other purposes)

Revenue Driven Benefits:

- Market share (gain market access and business opportunities through the provider's network)
- Sales and production capacity (expand sales and production capacity during periods when such expansion could not be financed)

Cost Driven Benefits:

- Cost structure (reduce costs through superior provider performance and the provider's lower cost structure, turn fixed costs into variable costs)

Employee Driven Benefits:

- Employee commitment (give employees a stronger career path, increase commitment in non-core areas)

This list may not include all benefits sought from outsourcing as it changes in every organization as mentioned before but we think it serves for an adequqate job of capturing the main benefits sought from outsourcing for firms opearating in any sector. A description of each benefit is presented in Table 3.6.

Table 3.6 Benefits Sought from Outsourcing Measure

Variable	Operational Definition	Source
Core competencies	Business activities that an organization does particularly well in comparison to competitors	(Greaver II, 1999)
Flexibility	Increasing flexibility to meet changing business conditions, demand for products and service, and technologies	(Greaver II, 1999)
Organization structure	The framework in which the organization defines how tasks are divided, resources are deployed, and departments are coordinated	(Greaver II, 1999)
Product or service value		(Greaver II, 1999)
Customer satisfaction		(Greaver II, 1999)
Shareholder value		(Greaver II, 1999)
Operational performance	Increasing performance through higher quality, increased productivity, shorter cycle times, increased outputs, and greater profits	(Greaver II, 1999)
Technology	The knowledge, tools,	(Greaver II, 1999)

	techniques, and activities used to transform the organization's inputs into outputs	
Knowhow	The knowledge of the methods or techniques of doing business activities	(Greaver II, 1999)
Risk management		(Greaver II, 1999)
Innovation	The tendency of a firm to engage and support new ideas, novelty, experimentation and creative processes that may result in new products, services or technological processes	(Greaver II, 1999)
Credibility and image	Improving credibility and image by associating with superior providers	(Greaver II, 1999)
Cash generation	Generating cash by transferring assets to the providers	(Greaver II, 1999)
Asset management	Reducing investments in assets and freeing up these resources for other purposes	(Greaver II, 1999)
Market share	Gaining market access and business opportunities	(Greaver II, 1999)

	through the provider's network	
Sales capacity	Expandibg sales capacity during periods when such expansion could not be financed	(Greaver II, 1999)
Production capacity	Expandibg production capacity during periods when such expansion could not be financed	(Greaver II, 1999)
Cost structure	Reducing costs through superior provider performance and the provider's lower cost structure, turn fixed costs into variable costs	(Greaver II, 1999)
Employee commitment	Giving employees a stronger career path, increase commitment in non-core areas	(Greaver II, 1999)

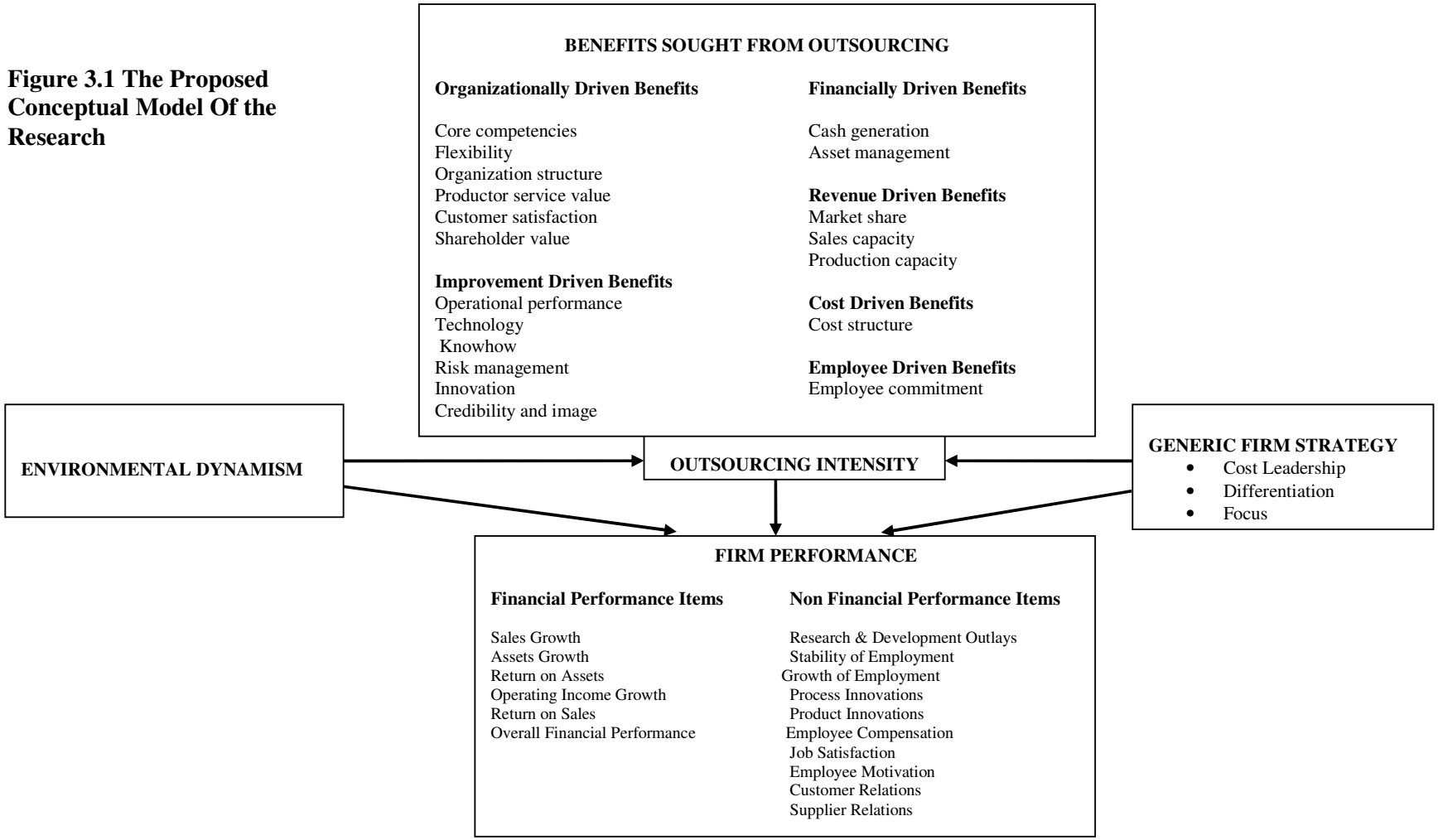
The Proposed Conceptual Model of the Research

The theoratical research model is based on several researchers but mainly influenced by the works of Giley (1997) and Jiang (2004) as mentioned before. The combination of three perspectives, together, transaction cost economics, the core competence perspective and the agency theory perspective help us to develop an integrated model for outsourcing decisions. The proposed research model is inspired by the work of Giley (1997) and Jiang (2004) but the model is enriched by involving the benefits sought from outsourcing measure.

Specifically, this model draws on transaction cost economics (Coase, 1937; Williamson, 1975, 1985) and the resource based perspective. The transaction cost theory perspective suggests that activities that are not firm-specific are more likely to be outsourced, while the resource-based perspective suggest that activities not critical to core competencies should be outsourced.

In this study, the direct affect of outsourcing intensity on firm performance will be analyzed through generic firm strategies and environmental dynamism. Strategy of the firm is proposed to directly affect the performance of the firms (Porter, 1980; Weinzimmer, 2000) and the performance is the outcome of the fit between several factors as strategy, capabilities and environment (Bergeron, Raymond and Rivard, 2004). The aim is to develop a multidimensional model for analyzing the outsourcing, performance and strategy relationship and figuring out the outsourcing intensity levels for firms pursuing different generic strategies to maximize firm's financial and non-financial performance in different environments. By combining different and variety of perspectives, this dissertation aims to develop a multidimensional model that has not been outlined by the other researchers in the field.

Figure 3.1 The Proposed Conceptual Model Of the Research



4. RESEARCH DESIGN AND METHODOLOGY

The research design and methodology of this dissertation are explained in this chapter. Initially, the research objectives and research questions will be discussed to develop the hypothesis based on our literature review and proposed research model given. Afterwards, the sample characteristics are analyzed and the development of the survey instrument is described together with the explanation of data analysis methods.

4.1Research Objectives

In the literature review, it is mentioned that many researchers have made arguments both for and against outsourcing as a means of sustainable competitive advantage. However, less attention has been given to those factors that influence a firm's outsourcing intensity. Previous works on the subject have examined a relatively narrow set of determinants (Giley 1997, Giley&Rasheed 2000, Rodrigez&Robania 2004, Greer&Rasheed&Giley 2004, Calabrese&Erbetta2005, Jiang 2004, Görzig&Stephan 2002). In addition, those works have dealt with either a single industry or the outsourcing of a single activity.

The aim of this research is to contribute to this domain by developing a more comprehensive set of potential determinants that drive the benefits sought from outsourcing decisions and outsourcing intensity which in turn should affect firm performance and test them for firms operating in different sectors, pursuing different generic firm strategies. Accordingly, a critical challange facing organizations is how to effectively organize and manage outsourcing in accordance with the direction of their generic firm strategies. With the premise that organizations whose generic firm strategies (cost leadership, differentiation or focus) are compatible with their outsourcing intensity are expected to have better outsourcing benefits and organizational performance. By combining different and variety of perspectives, this dissertaion aims to develop a multidimentional model that have not been outlined by other researchers in the field. The author aims to figure out outsourcing, performance and strategy relationships of corporate firms in Turkey.

The specific research questions are listed as in the following:

1. How are the corporate firms' overall reliance on outsourcing – outsourcing intensity – in Turkey for different functional business activities? How important is each business activity subject to outsourcing to the competitive advantage (namely to profitability, superior performance and sustainable compatitive advantage) of the firms operating in different industries / environments?

2. What is the relationship between outsourcing intensity of organizational activities of a firm and their importance to competitive advantage? Do these relationships differ according to the industry or environment firm operates?

3. What are the organizationally driven benefits sought from outsourcing practices in corporate firms in Turkey?

4. How do these organizationally driven benefits of outsourcing affect the outsourcing intensity of a firm?

6. How do generic firm strategies affect the outsourcing intensity of an organization?

7. What is the relationship between environmental dynamism and outsourcing intensity of a firm?

8. What is the relationship between outsourcing intensity of organizational activities, and firm performance? Does different levels of outsourcing intensity affect firm performance?

9.Does the impact of outsourcing intensity on firm performance dependant to environmental dynamism or generic firm strategies?

4.2 Hypotheses

Based on the literature review, the proposed research model and research questions, the following hypothesis are developed:

Hypothesis 1a: There is a relationship between benefits sought from outsourcing and industry/sector of a firm it operates.

Hypothesis 1b: There is a relationship between environmental dynamism and industry/sector of a firm it operates.

Hypothesis 1c: There is a relationship between generic firm strategies and industry/sector of a firm it operates.

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Hypothesis 1d: There is a relationship between firm performance and industry/sector of a firm it operates.

Hypothesis 1e: There is a relationship between outsourcing intensity of a business activity and industry/sector of a firm it operates

Hypothesis 2: There is a relationship between generic firm strategies and outsourcing intensities of firms.

Hypothesis 3: There is a relationship between outsourcing intensity of an organizational activity and activity's importance to compatitive advantage of the firm.

Hypothesis 3a: There is a relationship between outsourcing intensity of finance and accounting activities of a firm and finance and accounting activities' importance to compatitive advantage of the firm.

Hypothesis 3b: There is a relationship between outsourcing intensity of general and administrative activities of a firm and general and administrative activities' importance to compatitive advantage of the firm.

Hypothesis 3c: There is a relationship between outsourcing intensity of human resources activities of a firm and human resources activities' importance to compatitive advantage of the firm.

Hypothesis 3d: There is a relationship between outsourcing intensity of information systems activities of a firm and information sytems activities' importance to compatitive advantage of the firm.

Hypothesis 3e: There is a relationship between outsourcing intensity of marketing activities of a firm and marketing activities' importance to compatitive advantage of the firm.

Hypothesis 3f: There is a relationship between outsourcing intensity of logistics activities of a firm and logistics activities' importance to compatitive advantage of the firm.

Hypothesis 3g: There is a relationship between outsourcing intensity of manufacturing activities of a firm and manufacturing activities' importance to compatitive advantage of the firm.

Hypothesis 4: There is a relationship between benefits sought from outsourcing and outsourcing intensity of a firm.

Hypothesis 4a: There is a relationship between organizationally driven benefits sought from outsourcing and outsourcing intensity of a firm.

Hypothesis 4b: There is a relationship between improvement driven benefits sought from outsourcing and outsourcing intensity of a firm..

Hypothesis 4c: There is a relationship between financially driven benefits sought from outsourcing and outsourcing intensity of a firm.

Hypothesis 4d: There is a relationship between revenue driven benefits sought from outsourcing and outsourcing intensity of a firm.

Hypothesis 4e: There is a relationship between cost driven benefits sought from outsourcing and outsourcing intensity of a firm..

Hypothesis 4f: There is a relationship between employee driven benefits sought from outsourcing and outsourcing intensity of a firm.

Hypothesis 5: There is a relationship between outsourcing intensity of a firm and firm performance.

Hypothesis 5a: There is a relationship between outsourcing intensity of a firm and its financial performance.

Hypothesis 5b: There is a relationship between outsourcing intensity of a firm and its non-financial performance.

Hypothesis 6: There is a relationship between environmental dynamism and outsourcing intensity of a firm.

Hypothesis 7: There is a relationship between generic strategies of a firm and firm performance.

Hypothesis 8: There is a relationship between generic strategies of a firm and outsourcing intensity of a firm.

Hypothesis 9: There is a relationship between benefits sought from outsourcing and firm performance.

Hypothesis 9a: There is a relationship between organizationally driven benefits sought from outsourcing and financial firm performance.

Hypothesis 9b: There is a relationship between organizationally driven benefits sought from outsourcing and non-financial firm performance.

Hypothesis 9c: There is a relationship between improvement driven benefits sought from outsourcing and financial firm performance.

Hypothesis 9d: There is a relationship between improvement driven benefits sought from outsourcing and non-financial firm performance.

Hypothesis 9e: There is a relationship between financially driven benefits sought from outsourcing and financial firm performance.

Hypothesis 9f: There is a relationship between financially driven benefits sought from outsourcing and non-financial firm performance.

Hypothesis 9g: There is a relationship between revenue driven benefits sought from outsourcing and financial firm performance.

Hypothesis 9h: There is a relationship between revenue driven benefits sought from outsourcing and non-financial firm performance.

Hypothesis 9i: There is a relationship between cost driven benefits sought from outsourcing and financial firm performance.

Hypothesis 9j: There is a relationship between cost driven benefits sought from outsourcing and non-financial firm performance.

Hypothesis 9i: There is a relationship between employee driven benefits sought from outsourcing and financial firm performance.

Hypothesis 9j: There is a relationship between employee driven benefits sought from outsourcing and non-financial firm performance

Hypothesis 10: There is a relationship between environmental dynamism and firm performance.

4.3 Sample

Data for this study were collected from a sample of 94 corporate firms operating in two major sectors, namely manufacturing and service sector, in İstanbul, Turkey. Regarding outsourcing as strategic and suggesting that it has an influence on organizational performance, is something that has to be done with emprical research in big sized, corporate firms. The criteria for being a corporate firm differ in different sources. There are methods, structures or mechanisms like 'corporate governance', by which a corporation is directed, administered or controlled. It includes the framework of Rules; such as internal or external rules of corporation, Relations; between all parties, Systems&Processes; delegation of authority, performance measures, assurance mechanisms, reporting requirements and accountabilities. The principle participants in corporate firms are the shareholders, management and the board of directors. Other participants include regulators, employees, suppliers, partners, customers, and the general community. According to Greaver (1999), strategic outsourcing takes outsourcing to a higher level by asking fundemental questions about outsourcing's relevance to the organization and its vision, structure, current and future core competencies, costs, performance and competitive advantages. To be considered as a strategic choice, outsourcing must be a distinctive feature of specific firms in an industry and can be characterised by five elements as mentioned by Quelin and Duhamel (2003). So, taking into consideration this notion of strategic outsourcing, the field survey is presented to the CEOs, CIOs, or senior managers of companies listed in 'Capital 500' list of year 2006. Capital is a prestigious monthly periodical of business and economy in Turkey.

The questionnaire to be used in the field survey was developed in order to investigate the strategic outsourcing practices in Turkey and their impact on firm performances. Data was collected through face to face interviews and mail surveys in Internet. Of the 500 firms in Capital 500 list, 94 firms returned usable surveys in time to

be included in this study. So, 19% of the population has been covered during the course of sampling. The firms in the sample included many industrial sectors, such as chemistry, textile, automative, food, retail, cement, rubber and others. In order to get statistically more reliable results and analyze the big picture, industrial sectors in the sample are also grouped under two distinct sectors: manufacturing and service.

The characteristic of the sample and descriptive data (company and respondent information details) are provided in **Table 4.1a, 4.1b** and **Table 4.2.**

Table 4.1a Sample Distribution by Sector

Sector	Frequency	Percent
Manufacturing	60	63.8
Service	34	36.2
Total	**94**	**100**

Table 4.1b Sample Distribution by Industry

Industry	Frequency	Percent
Press	2	2.1
Chemistry/Medicine	9	9.6
Rubber	3	3.2
Textile	6	6.4
Commerce/Service	15	15.9
Electric/Electronics	3	3.2
Furniture	0	0
Energy	4	4.3
Information Technologies	5	5.3
Beverage	4	4.3
Retail	3	3.2
Telecom	2	2.1
Iron-Steel	2	2.1
Metal	0	0
Health	0	0
Automative	11	11.7
Food	9	9.6
Gold	0	0
Plastic	1	1.1
Cement	3	3.2
Machinery	1	1.1
Tobacco	1	1.1
Packing	2	2.1
Glass / Seramic	2	2.1
Tourism	1	1.1
White Goods	2	2.1
Others	1	1.1
Total	**94**	**100**

Table 4.2 Sample Disribution by Respondent Information

Respondent Information	Whole Sample		Manufacturing Sector		Service Sector	
	Frequency	Percent	Frequency	Percent	Frequency	Percent
Age						
20-30 years old	2	2.1	2	3.3	0	0
31-40	62	66.0	38	63.3	24	70.6
41-50	29	30.9	19	31.7	10	29.4
>50 years old	1	1.1	1	1.7	0	0
Total	94	100	60	100	34	100
Gender						
Female	34	36.2	17	28.3	17	50.0
Male	60	63.8	43	71.7	17	50.0
Total	94	100	94	100	34	100
Education Level						
High School	3	3.2	3	5.0	0	0
University	65	69.1	39	65.0	26	76.5
Master's Degree	26	27.7	18	30.0	8	23.5
PHD. Degree	0	0	0	0	0	0
Total	94	100	60	100	34	100
# of years worked for the company:						
0-1 year	4	4.3	4	6.7	0	0
2-5 years	30	31.9	19	31.7	11	32.4
6-10 years	33	35.1	18	30.0	15	44.1
>10 years	27	28.7	19	31.7	8	23.5
Total	94	100	60	100	34	100

# of years worked in the sector:						
0-1 year	1	1.1	1	1.6	0	0
2-5 years	11	11.7	7	11.5	4	12.1
6-10 years	38	40.4	25	41.0	13	39.4
>10 years	44	46.8	28	45.9	16	48.5
Total	94	100	61	100	33	100

4.4 Instrument

The measurement of variables is explained in this section. The structured questionnaire (see Appendix 1) has 173 items in total and composed of 6 parts which are general information about the firm and respondent, outsourcing intensity, firm performance, firm strategies, benefits sought from outsourcing and the environmental dynamism.

4.4.1 General Information About the Firm and the Respondents

Descriptive statistics such as the industrial sector in which the firm operates, the respondents' gender, age, education level, number of years worked for the company, number of years worked in the sector are asked in this part.

4.4.2 Outsourcing Intensity

Outsourcing intensity is measured by a scale developed similar to Giley's (1997). American Management Association's outsourcing survey instrument (1997) is also used to list the distinct activities in functional business categories of a firm. This list is subsequently cross checked with several items discussed by Porter (1985) in defining the value chain activities. This list does not include all activities in which organizations are engaged but serves for an adequate job of capturing the main business activities present in firms operating in any sector.

To measure 'the outsourcing intensity' of the listed activities, respondents are asked to indicate the level of outsourcing intensity on a 6 point Likert type scale, with 1 indicating 'not outsourced' and 6 'totally outsourced'. To differentiate between 'low outsourcing intensity' and 'high outsourcing intensity', as a cut off point is chosen so that only those firms having outsourcing intensity level of 4 or more in each activity are supposed to have high outsourcing intensity. Those below that level are considered to have low outsourcing intensity for that activity.

To better understand the strategic significance of the activities that are being outsourced and their contribution to competitive advantage of the firm (similar to Giley's peripheral and core activity distinction) respondents are asked to indicate the extent to which each activity listed in the table is important to profitability, superior performance and sustainable competitive advantage in their industry. Respondents are asked to indicate the significance of each activity on a separete 6 point scale (1= not at all important to 6= extremely important). Activities receiving scores above 3, will be categorized as activities related to core business functions of the firm which serve for sustaining competitive advantage.

4.4.3 Firm Performance

Many of the privately held firms are unlikely to provide objective financial data, and their executives are expected to be unwilling to provide detailed accounting data. Therefore, it is found appropriate to use subjective measures of financial performance and ask firm performance questions based on Dess and Robinson (1984). Dess and Robinson (1984) provide strong evidence of the validity and reliability of this type of subjective measures of financial performance. Each respondent is asked to rank his or her firm's performance compared to other similar firms in their industry on sales growth , after tax return on total assets and overall financial performance over the last 12 months.

To determine each firm's non-financial performance, respondents are asked to rate their firm's R&D outlays, stability/growth of employment, process innovations, product innovations, employee compensation, employee morale/job satisfaction, customer relations, supplier relations relative to their competitors. For both financial

and nonfinancial performance, responses are coded on a 6-point scale (1=at the bottom of similiar firms in the industry to 6=at the top of similiar firms in the industry. Survey question is 'Please rate your firm's performance relative to similiar firms in your industry over the last 12 months).

4.4.4 Firm Strategy

Generic firm strategies are measured by using three subscales: cost-leadership, differentiation and focus following Porter's generic competitive strategies. In light of Porter's requirements for generic competitive strategies, firm strategy is measured using an amended form of Miller's (1988) scale. Miller (1988) reported estimated reliabilities (Cronbach, 1951) of these subscales as .64, .47, and .50, respectively. In our scale, Miller's (1988) risk-related items are not used to measure strategy; however, several items are added to Miller's (1988) subscales in attempt to improve their reliability. Responses were made on a 6 point scale (1 = we never this strategy to 7 = we always use this strategy).

4.4.5 Environment

The relative dynamism in a firm's external environment may have important effects on outsourcing intensity (Giley, 1997). As stated in literature, 'environmental dynamism' is defined as 'the rate of change and innovation in an industry' as well as 'the uncertainty or predictability of the actions of competitors and customers' (Miller and Friesen, 1982).

Environmental dynamism is measured using a scale developed by Miller and Friesen (1982) and amended by Giley (1997). Responses are coded on a 6 point scale (1 = strongly disagree to 6= strongly agree). Miller reported a reliability of this measure of .59. To increase the reliability, two additional questions were included by Giley (1997), increasing the number of items in this scale to seven and the internal reliability coefficient of the dynamism measure to .79.

4.4.6 Benefits Sought from Outsourcing Measure

Benefits sought from outsourcing measure are constructed by using Greaver II's (1999) categorization of benefits sought from outsourcing. According to Greaver II (1999), just as probability of another person's suit of clothes fitting the other exactly is remote, so too is the probability of another organization's reasons to outsource fitting the other equally remote. This list gategorizes the benefits in six dimensions and has 17 items. This list may not include all benefits sought from outsourcing as it changes in every organization as mentioned before, but it may serve for an adequate job of capturing the main benefits sought from outsourcing for firms operating in any sector.

4.5 Data Analysis Methodology

The collected data is initially analyzed by reliability and factor analysis. The internal consistency of each scale is measured by the recomputation of Cronbach's alpha after the extraction of items with low reliabilities. Factor analyses are conducted in order to eliminate the items with low reliabilities. After the factor and reliability analysis have been conducted, the new factors are replaced with the old ones and the proposed conceptual model is modified to be tested for the impact of outsourcing on firm performance. Further analyses are conducted with these new factors on the modified model.

The differences between firms operating in manufacturing and service sectors are calculated through Independent Sample t-Tests (independent sample t-tests for generic strategies questionnaire, environmental dynamism questionnaire, benefits sought from outsourcing questionnaire and outsourcing intensity scale).

The direct, indirect and combined relationships between dependent and independent variables are tested by multiple regression analysis. In this study, the direct effects of independent variables are analyzed first. Firm performance is dependant on outsourcing intensity whereas outsourcing intensity is dependant on the benefits sought from outsourcing. The strategies that affect the benefits sought from outsourcing and outsourcing intensity are figured out. On the other hand, the impact of environmental dynamism is figured out as another independent variable on firm performance. Then

the combined effects of independent variables on firm performance will be analyzed. In the combined models, the aim is to find out whether the benefits sought from outsourcing differ under certain strategies and environments and affect outsourcing intensity of a firm, which in turn affect firm performance.

The direct, indirect and combined effects of independent variables of strategy and outsourcing intensity on firm performance are also analyzed for manufacturing and service industries. In this part, the aim is to find whether the concepts are better in explaining firm performance when they act together. The combined effects of generic firm strategies, environmental dynamism and outsourcing intensity (independent variables) are analyzed on firm performance.

5. RESEARCH FINDINGS

Research findings are presented in this section. Five steps are followed as in the following:

(1) Obtaining reliability and factor analysis of the dependent and independent measures,

(2) Independent sample t-Test in order to figure out the differences between two industries / sectors.

(3) Investigating the outsourcing intensity levels of different organizational functions and their contribution to competitive advantage through paired sample t-Test

(4) Investigating the determinants of outsourcing intensity level – through linear regression analyses

(5) Investigating the direct and mediator/moderrator effects of independent variables on firm performance - through linear regression analyses

(6) Testing for combined models of the outsourcing intensity and firm performance relationship – through hierarchical regression analyses in two different industries/sectors

5.1Reliability and Factor Analysis

To test the reliabilities of the scales, Cronbach's alpha reliability analysis was conducted. Two tests, Barlett's Test of Sphericity and Kaiser-Meyer-Olkin Measure of Sampling Adequacy (KMO-MSA) are considered important in determining the appropriateness of the data for factor analysis. In order to conduct factor analysis, KMO has to be more than 0.50 and Barlett's Test of Sphericity has to be significant ($p<0.001$). For factor analysis, principle components analysis and Varimax rotation are performed.

5.1.1 Reliability and Factor Analysis of Generic Firm Strategies Scale

Generic firm strategies scale originally consisted 25 items. The KMO value was 0.874 and significance of Barlett test was 0.000, so factor analysis could be conducted. When principle component analysis with varimax rotation was performed, 4 factors were extracted. The items that had factor loadings lower than 0.60 were eliminated except for one factor, which had a loading of 0.597. After eliminations, the factor analysis resulted in 4 factors and 21 items. These four factors were similar to the generic strategies of Porter, so they were labeled as 'Differentiation Strategy ', 'Focus Strategy', 'Cost Leadership Strategy for Manufacturing Functions'' and 'Cost Leadership Strategy for Marketing Functions'. Differentiation strategy had 0.898, focus strategy had 0.893, cost leadership strategy for manufacturing functions had 0.852, and cost leadership strategy for marketing functions had 0.829 Cronbach's alpha value.

Table 5.1 Reliability and Factor Analysis of Generic Firm Strategies Scale

	Factor Loadings	Variance Explained	Cronbach Alpha	# of Items
Differentiation		**38.331**	**0.898**	**7**
We differentiate our products to satisfy different customer needs.	0.720			
We add features to our products to be technically competitive.	0.733			
We use prestige pricing.	0.780			
We charge a premium price for our products' brand image.	0.707			
We charge a premium price for our products' technology and features.	0.795			
We have a corporate reputation for technological leadership.	0.687			
Our products' perceived quality is high.	0.610			
Focus		**16.667**	**0.893**	**5**
We don't use market segmentation.	0.885			
We have a wide area of dealer network.	0.878			
We have a wide area of customer service.	0.866			
We use market segmentation to serve for special needs of a narrow strategic target.	0.829			
We avoid of marginal customer accounts.	0.690			
Cost Leadership for Manufacturing Functions		**8.214**	**0.852**	**4**
Our focus is on cost minimization.	0.705			
We standardize our products to lower costs.	0.702			
We have tight cost control mechanisms.	0.651			
We have products designed for ease of manufacture.	0.767			
Cost Leadership for Marketing Functions		**5.202**	**0.829**	**5**
We minimize our advertising expenses.	0.637			
We often review our pricing policies and launch campaigns.	0.597			

We minimize our R&D costs in areas like new product and process development.	0.682			
We minimize our costs in areas like customer service.	0.750			
We minimize our costs in managing our dealer network.	0.633			
Total Variance Explained		**68.415**	**0.517**	**21**
Kaiser-Meyer-Olkin Measure of Sampling Adequacy	**0.838**			
Barlett's Test of Sphericity				
Approx. Chi-Square	**1246.715**			
df	**210**			
Sig.	**0.000**			

5.1.2 Reliability and Factor Analysis of Benefits Sought from Outsourcing Scale

Benefits sought from outsourcing measure originally consisted 17 items. The KMO value was 0.668 and significance of Barlett test was 0.000, therefore factor analysis could be conducted. When principle component analysis with varimax was performed, 4 factors extracted. Four items (asset management, organization structure, cost structure, and credibility & image) which had factor loadings lower than 0.6 were eliminated. After elimination, the factor analysis was run again and resulted in 4 factors and 13 items.

Table 5.2 Reliability and Factor Analysis of Benefits Sought from Outsourcing Scale

	Factor Loadings	Variance Explained	Cronbach Alpha	# of Items
Organization Driven Benefits		**29.552**	**0.787**	**5**
Cash generation	0.766			
Core competencies	0.744			
Technology & Know-how	0.711			
Operational Performance	0.715			
Flexibility	0.611			
Employee-Customer Driven Benefits		**14.248**	**0.714**	**3**
Employee Commitment	0.784			
Customer Satisfaction	0.715			
Product / Service Value	0.710			
Improvement Driven Benefits		**12.913**	**0.699**	**3**
Innovation	0.832			
Sales Capacity / Production Capacity	0.770			
Market Share	0.691			
Market Driven Benefits		**9.142**	**0.563**	**2**
Risk Management	0.839			
Shareholder Value	0.753			
Total Variance Explained		**65.855**	**0.774**	**13**
Kaiser-Meyer-Olkin Measure of Sampling Adequacy	**0.657**			
Barlett's Test of Sphericity				
Approx. Chi-Square	**421.061**			
df	**78**			
Sig.	**0.000**			

5.1.3 Reliability and Factor Analysis of Environmental Dynamism Scale

Environmental dynamism scale, which originally consisted 7 items, resulted in one factor when factor analysis was performed (KMO value was 0.921 and significance of Barlett test was 0.000). When the factor analysis was run, there was not any item with a factor loading less than 0.60 to be eliminated. The factor is labeled as 'Environmental Dynamism' in line with its operational definition.

Table 5.3 Reliability Analysis of Environmental Dynamism Scale

	Cronbach alpha	# of Items
Environmental Dynamism	**0.943**	**7**
We often change our sales and marketing strategies		
Product life cycle is short.		
Our competitors' actions are easy to predict. (R)		
Consumer demand and needs are easy to predict. (R)		
Production technology changes continuously.		
Technology changes are easy to predict. (R)		
Consumer demand and market shares change continuously.		

5.1.4 Reliability and Factor Analysis of Firm Performance Scale

Firm performance scale originally consisted 15 items and when principle component analysis with varimax rotation was performed, 4 factors were extracted (The KMO value 0,803 and the significance of Barlett's Test was 0.000). One item, stability of employment, which had factor loading lower than 0.60, eliminated. After elimination, the analysis was run again and resulted in 4 factors and 14 items.

Table 5.4 Reliability and Factor Analysis of Firm Performance Scale

	Factor Loadings	Variance Explained	Cronbach Alpha	# of Items
Financial Performance		**40.682**	**0.854**	**7**
Sales Growth	0.783			
Assets Growth	0.746			
Return on Sales	0.644			
Return on Assets	0.722			
Growth of Employment	0.644			
Operating Income Growth	0.645			
Overall Financial Performance	0.741			
Innovation Performance		**14.722**	**0.762**	**3**
Product Innovations	0.825			
Process Innovations	0.782			
Research and Development Outlays	0.793			
Employee Performance		**8.612**	**0.983**	**2**
Employee Motivation	0.915			
Job Satisfaction	0.910			
Customer and Supplier Relations Performance		**7.260**	**0.848**	**2**
Customer Relations	0.831			
Supplier Relations	0.825			
Total Variance Explained		**71.277**	**0.879**	**14**
Kaiser-Meyer-Olkin Measure of Sampling Adequacy	**0.815**			
Barlett's Test of Sphericity				
Approx. Chi-Square	**803.220**			
df	**91**			
Sig.	**0.000**			

5.1.5 Reliability and Factor Analysis of Outsourcing Intensity Scale

Outsourcing intensity scale originally consisted of 36 items that represented organizational activities in seven different functional business categories of a firm namely, finance & accounting functions, human resources functions, general & administrative functions, marketing functions, logistics functions, manufacturing functions, and information systems functions. Considering the small sample size, factor analysis conducted separately for each organizational function.

5.1.5.1 Reliability and Factor Analysis of Finance and Accounting Functions' Outsourcing Intensity Scale

Finance and accounting functions consisted of four items and when principle component analysis with varimax rotation performed, 2 factors were extracted. (The KMO value was 0.474, and the significance of Barlett's Test was 0.000). None of the items had factor loadings lower than 0.60.

Table 5.5 Reliability and Factor Analysis of Finance and Accounting Functions' Outsourcing Intensity Scale

	Factor Loadings	Variance Explained	Cronbach Alpha	# of Items
Operational Finance Activities		**31.847**	**0.533**	**2**
Bookkeeping	0.845			
Procurement, Import & Export, Treasury Operations	0.803			
Managerial Finance Activities		**42.084**	**0.655**	**2**
Data Processing & Management	0.857			
Statutory & Management Reporting	0.897			
Total Variance Explained		**73.931**	**0.529**	**4**
Kaiser-Meyer-Olkin Measure of Sampling Adequacy	**0.474**			
Barlett' s Test of Sphericity				
Approx. Chi-Square	**55.406**			
df	**6**			
Sig.	**0.000**			

5.1.5.2 Reliability and Factor Analysis of Human RelationsFunctions' Outsourcing Intensity Scale

Human relations functions consisted of seven items and when principle components analysis with varimax rotation performed, 2 factors extracted (KMO value was 0.534 and the significance of Barlett's Test was 0.000). One of the items, fringe benefits, had factor loadings lower than 0.6.

Table 5.6 Reliability and Factor Analysis of Human Relations Functions' Outsourcing Intensity Scale

	Factor Loadings	Variance Explained	Cronbach Alpha	# of Items
Primary Human Relations Activities		**46.005**	**0.770**	**3**
Payroll Activities	0.836			
Recruiting	0.879			
Employee Research	0.763			
Secondary Human Relations Activities		**21.903**	**0.643**	**3**
Temporary Staffing	0.703			
Training – Functional	0.874			
Training – Management and Supervision	0.657			
Total Variance Explained		**60.611**	**0.731**	**6**
Kaiser-Meyer-Olkin Measure of Sampling Adequacy	**0.518**			
Barlett's Test of Sphericity				
App. Chi-Square	**210.268**			
df	**15**			
Sig.	**0.000**			

5.1.5.3 Reliability and Factor Analysis of General and Administrative Functions' Outsourcing Intensity Scale

General and Administrative functions consisted of six items and when principle components analysis with varimax rotation performed, 3 factors extracted (KMO value was 0.602 and the significance of Barlett's Test was 0.000). None of the items had factor loadings lower than 0.6.

Table 5.7 Reliability and Factor Analysis of General and Administrative Functions' Outsourcing Intensity Scale

	Factor Loadings	Variance Explained	Cronbach Alpha	# of Items
General Activities		**49.344**	**0.688**	**2**
Building Maintenance & Cleaning	0.859			
Photocopying	0.855			
Administrative Activities		**20.142**	**0.809**	**2**
Office Supply Management	0.908			
Mailroom Activities	0.851			
Support Activities		**17.334**	**0.739**	**2**
Office Design & Decoration Employee Catering & Transportation Services				
Total Variance Explained		**86.820**	**0.780**	**6**
Kaiser-Meyer-Olkin Measure of Sampling Adequacy	**0.602**			
Barlett's Test of Sphericity				
Approx. Chi-Square	**264.076**			
df	**15**			
Sig.	**0.000**			

5.1.5.4 Reliability and Factor Analysis of Marketing Functions' Outsourcing Intensity Scale

Marketing functions consisted of seven items and when principle components analysis with varimax rotation performed, 2 factors extracted (KMO value was 0.744 and the significance of Barlett's Test was 0.000). None of the items had factor loadings lower than 0.6.

Table 5.8 Reliability and Factor Analysis of Marketing Functions' Outsourcing Intensity Scale

	Factor Loadings	Variance Explained	Cronbach Alpha	# of Items
Marketing Activities		**51.639**	**0.850**	**5**
Advertising	0.778			
Customer Relationship Management	0.897			
Call Center Operations	0.642			
Public Relations	0.730			
Marketing Research	0.871			
Sales Activities		**23.440**	**0.889**	**2**
Wholesales Activities	0.950			
Retail Sales Activities	0.910			
Total Variance Explained		**75.079**	**0.829**	**7**
Kaiser-Meyer-Olkin Measure of Sampling Adequacy	**0.744**			
Barlett's Test of Sphericity				
Approx. Chi-Square	**361.378**			
df	**21**			
Sig.	**0.000**			

5.1.5.5 Reliability and Factor Analysis of Logistics Functions' Outsourcing Intensity Scale

The result of factor analysis of 3 item logistics functions' outsourcing intensity scale resulted in one factor. The item with low reliability excluded (Outbound logistics activities). The factor was labeled as inbound logistics activities with reliability of 0.707.

Table 5.9 Reliability Analysis of Logistics Functions' Outsourcing Intensity Scale

	Cronbach Alpha	# of Items
Inbound Logistics Activities	**0.707**	**2**
Inbound Logistics Activities Intra Office Delivery		

5.1.5.6 Reliability and Factor Analysis of Manufacturing Functions' Outsourcing Intensity Scale

The result of factor analysis of 3 item manufacturing functions' outsourcing intensity scale resulted in one factor. None of the items had low reliabilities. The only factor with 3 items labeled as 'manufacturing functions' was used with reliability of 0.643.

Table 5.10 Reliability Analysis of Manufacturing Functions' Outsourcing Intensity Scale

	Cronbach Alpha	# of Items
Manufacturing Activities	**0.643**	**3**
Product / Component Design Product / Process Research Development Product Assembly / Packaging / Quality Control		

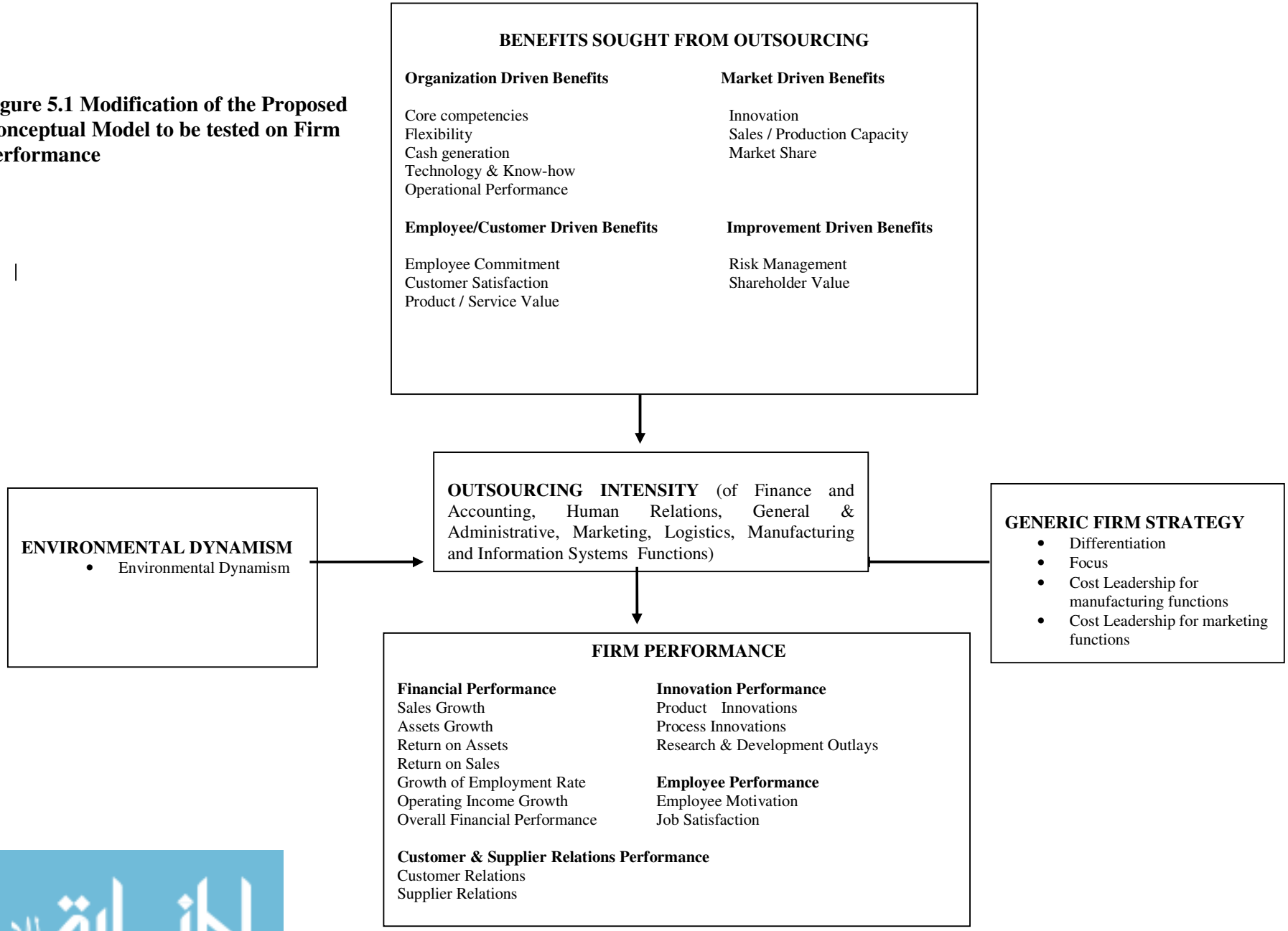
5.1.5.7 Reliability and Factor Analysis of Information Systems Functions' Outsourcing Intensity Scale

The result of factor analysis of 6 item information systems functions' outsourcing intensity scale resulted in one factor. None of the items had low reliabilities. The sole factor with 6 items was labeled as 'information systems activities' with reliability of 0.772.

Table 5.11 Reliability Analysis of Information Systems Functions' Outsourcing Intensity Scale

	Cronbach Alpha	# of items
Information Systems Activities	**0.772**	**6**
Batch Processing Management Installation / Maintenance Server and Data Management IT Helpdesk Activities PC Supply / Maintenance Application Development & Maintenance		

Figure 5.1 Modification of the Proposed Conceptual Model to be tested on Firm Performance



5.2 Independent Sample t-Test

Independent sample t-Tests were conducted in order to figure out the differences between two industries / sectors.

5.2.1 Independent Sample t-Test for Firm Performance Questionnaire

Independent sample t-Test to firm performance factors (total firm performance, financial performance, employee performance, innovation performance and customer-supplier relations performance) was conducted in order to find out if there is a relation between sector and firm performance or not. The result of independent sample t-Test has shown that there is no significant difference between firm performance factors of firms in different industries / sectors. Therefore, it can be concluded that industry / sector does not have an effect on firm performance of firms.

Table 5.12 Independent Sample t-Test Results for Firm Performance Questionnaire

Total Firm Performance		N	Mean	Std. Dev		t	p
	Manufacturing	60	17.475	3.165	Equal Variances assumed	-0.726	0.469
	Service	34	17.910	1.942	Equal Variances not assumed	-0.825	0.412
	Levene's test for Equality of variances					F 4.979	P 0.028
Financial Performance		N	Mean	Std. Dev		T	p
	Manufacturing	60	4.264	0.795	Equal Variances assumed	-0.431	0.668
	Service	34	4.331	0.602	Equal Variances not assumed	-0.465	0.643
	Levene's test for Equality of variances					F 1.087	P 0.300
Employeee Performance		N	Mean	Std. Dev		T	p
	Manufacturing	60	3.792	1.412	Equal Variances assumed	-0.591	0,556
	Service	34	3.956	1.054	Equal Variances not assumed	-0.640	0,524
	Levene's test for Equality of variances					F 2,640	P 0,108
Innovation Performance		N	Mean	Std. Dev		T	p
	Manufacturing	60	4.594	0.692	Equal Variances assumed	0.103	0.918
	Service	34	4.578	0.779	Equal Variances not assumed	0.100	0.921
	Levene's test for Equality of variances					F 1.093	P 0.299
Customer-Supplier Relations Performance		N	Mean	Std. Dev		T	p
	Manufacturing	60	4.825	1.203	Equal Variances assumed	-0.948	0.345
	Service	34	5.044	0.801	Equal Variances not assumed	-1.057	0.294
	Levene's test for Equality of variances					F 5.164	P 0.025

5.2.2 Independent Sample t-Test for Generic Firm Strategy Questionnaire

Significant differences were found between generic strategies of firms in two different sectors. The firms in the service sector apply more differentiation strategy then the firms in manufacturing sector (t=-2.745, p=0.007, mean (manufacturing) =3.37, mean (service) =3.95 for differentiation strategy and t=-2.115, p=0.037, men (manufacturing)=4.01, mean (service)=4.51. On the other hand, the firms in manufacturing sector apply more cost leadership strategies.

Table 5.13 Independent Sample t-Test Results for Generic Firm Strategies Questionnaire

Differentiation Strategy		N	Mean	Std. Dev		t	p
	Manufacturing	60	3.371	0.847	Equal Variances assumed	-2.745	0.007
	Service	34	3.954	1.199	Equal Variances not assumed	-2.499	0.016
	Levene's test for Equality of variances					F 15.437	P 0.000
Focus Strategy		N	Mean	Std. Dev		T	p
	Manufacturing	60	4.013	1.036	Equal Variances assumed	-2.115	0.037
	Service	34	4.506	1.166	Equal Variances not assumed	-2.046	0.045
	Levene's test for Equality of variances					F 0.031	P 0.861
Cost Leadership for manufacturing functions		N	Mean	Std. Dev		T	p
	Manufacturing	60	4.266	0.886	Equal Variances assumed	3.332	0.001
	Service	34	3.558	1.151	Equal Variances not assumed	3.101	0.003
	Levene's test for Equality of variances					F 8.897	P 0.004
Cost Leadership for marketing functions		N	Mean	Std. Dev		T	p
	Manufacturing	60	3.930	0.805	Equal Variances assumed	2.200	0.030
	Service	34	3.482	1.160	Equal Variances not assumed	1.994	0.051
	Levene's test for Equality of variances					F 15.424	P 0.000

5.2.3 Independent Sample t-Test for Outsourcing Intensity Questionnaire

The only activities that had significant results for outsourcing intensity between two sectors were marketing activities and information systems activities.

Table 5.14.1 Independent Sample t-Test Results for Outsourcing Intensity Questionnaire

Operational Finance Activities		N	Mean	Std. Dev		t	p
	Manufacturing	60	1.950	0.779	Equal Variances assumed	-0.521	0.603
	Service	34	2.044	0.940	Equal Variances not assumed	-0.495	0.622
	Levene's test for Equality of variances					F 1.230	P 0.270
Managerial Finance Activities		N	Mean	Std. Dev		T	p
	Manufacturing	60	2.208	1.139	Equal Variances assumed	-0.175	0.861
	Service	34	2.250	1.046	Equal Variances not assumed	-0.180	0.858
	Levene's test for Equality of variances					F 0.100	P 0.753
Primary HR Activities		N	Mean	Std. Dev		T	p
	Manufacturing	60	3.922	1.292	Equal Variances assumed	0.948	0.345
	Service	34	3.647	1.451	Equal Variances not assumed	0.918	0.362
	Levene's test for Equality of variances					F 1.639	P 0.204
Secondary HR Activities		N	Mean	Std. Dev		T	p
	Manufacturing	60	4.6611	0.886	Equal Variances assumed	0.456	0.650
	Service	34	4.568	1.042	Equal Variances not assumed	0.436	0.665
	Levene's test for Equality of variances					F 2.314	P 0.132

The outsourcing intensity of marketing and information systems activities were higher for firms in the service sector (t=-2.048, p=0.043, mean (manufacturing)

=3.050, mean (service) =3.617 for marketing activities and t=-2,067, p=0.042, mean (manufacturing) =3.144 and mean (service) =3.754 for information systems activities).

Table 5.14.2 Independent Sample t-Test Results for Outsourcing Intensity Questionnaire

General Office Activities		N	Mean	Std. Dev		t	p
	Manufacturing	60	5.000	1.432	Equal Variances assumed	-1.508	0.135
	Service	34	5.441	1.229	Equal Variances not assumed	-1.573	0.120
	Levene's test for Equality of variances					F 2.850	P 0.095
Administrative Activities		N	Mean	Std. Dev		T	p
	Manufacturing	60	3.641	1.859	Equal Variances assumed	0.911	0.365
	Service	34	3.264	2.045	Equal Variances not assumed	0.887	0.379
	Levene's test for Equality of variances					F 0.176	P 0.676
Support Activities		N	Mean	Std. Dev		T	p
	Manufacturing	60	5.441	0.957	Equal Variances assumed	1.277	0.205
	Service	34	5.102	1.617	Equal Variances not assumed	1.115	0.271
	Levene's test for Equality of variances					F 11.376	P 0.001
Sales Activities		N	Mean	Std. Dev		T	p
	Manufacturing	60	2.483	1.182	Equal Variances assumed	-0.007	0.994
	Service	34	2.485	1.294	Equal Variances not assumed	-0.007	0.993
	Levene's test for Equality of variances					F 1.408	P 0.238

Table 5.14.3 Independent Sample t-Test Results for Outsourcing Intensity Questionnaire

Marketing Activities		N	Mean	Std. Dev		t	p
	Manufacturing	60	3.050	1.316	Equal Variances assumed	-2048	0.043
	Service	34	3.617	1.245	Equal Variances not assumed	-2.079	0.041
	Levene's test for Equality of variances					F 0.164	P 0.687
Logistics Activities		N	Mean	Std. Dev		T	p
	Manufacturing	60	3.675	1.528	Equal Variances assumed	1.097	0.275
	Service	34	3.308	1.600	Equal Variances not assumed	1.083	0.283
	Levene's test for Equality of variances					F 0.657	P 0.420
Manufacturing Activities		N	Mean	Std. Dev		T	p
	Manufacturing	60	4.661	0.886	Equal Variances assumed	0.456	0.650
	Service	34	4.568	1.042	Equal Variances not assumed	0.436	0.665
	Levene's test for Equality of variances					F 2.314	P 0.132
Information Systems Activities		N	Mean	Std. Dev		T	p
	Manufacturing	60	3.144	1.364	Equal Variances assumed	-2.067	0.042
	Service	34	3.754	1.395	Equal Variances not assumed	-2.054	0.044
	Levene's test for Equality of variances					F 1.216	P 0.273

5.2.4 Independent Sample t-Test for Environmental Dynamism Questionnaire

Significant differences were found for environmental dynamism between manufacturing and service sector. Environmental dynamism was higher for firms operating in service sector.

Table 5.15 Independent Sample t-Test Results for Environmental Dynamism Questionnaire

		N	Mean	Std. Dev		t	p
Environmental Dynamism	Manufacturing	60	3.254	0.983	Equal Variances assumed	-3.512	0.001
	Service	34	4.058	1.201	Equal Variances not assumed	-3.323	0.002
	Levene's test for Equality of variances					F 1.476	P 0.228

5.2.5 Independent Sample t-Test for Benefits Sought from Outsourcing Questionnaire

There are no significant differences between organization driven benefits, employee-customer driven benefits, or market driven benefits sought from outsourcing in two different sectors. A significant difference was only found for improvement driven benefits sought from outsourcing. Improvement driven benefits sought from outsourcing was higher for firms operating in service sector (t=-3.040, p=0.003, mean(manufacturing)=2.383, mean(service)=3.058).

Table 5.16 Independent Sample t-Test Results for Benefits Sought from Outsourcing Questionnaire

Organization driven benefits		N	Mean	Std. Dev		t	p
	Manufacturing	60	4.708	0.691	Equal Variances assumed	-1.065	0.290
	Service	34	4.858	0.587	Equal Variances not assumed	-1,113	0.269
	Levene's test for Equality of variances					F 0.063	P 0.803
Employee/Customer driven benefits		N	Mean	Std. Dev		T	p
	Manufacturing	60	3.294	0.944	Equal Variances assumed	-1,072	0.286
	Service	34	3.490	0.647	Equal Variances not assumed	-1,187	0.239
	Levene's test for Equality of variances					F 7.425	P 0.008
Improvement driven benefits		N	Mean	Std. Dev		T	p
	Manufacturing	60	2.383	0.971	Equal Variances assumed	-3.040	0.003
	Service	34	3.058	1.139	Equal Variances not assumed	-2.908	0.005
	Levene's test for Equality of variances					F 2.313	P 0.132
Market driven benefits		N	Mean	Std. Dev		T	p
	Manufacturing	60	4.200	0.866	Equal Variances assumed	-0.384	0.702
	Service	34	4.264	0.613	Equal Variances not assumed	-0.422	0.674
	Levene's test for Equality of variances					F 5.988	P 0.016

5.3 Paired Samples T-test

In order to figure out differences between the firm activities' outsourcing intensity levels and these activities' importance to competitive advantage of the firm, paired sample t-test was conducted.

Table 5.17 Paired Sample t-Test Results for Firm Activities

	Pair	Mean	T	p
Operational Finance Activities	Outsourcing intensity level	1.984	-8.889	0.000
	Importance to competitive advantage	3.090		
Managerial Finance Activities	Outsourcing intensity level	2.223	-5.824	0.0000
	Importance to competitive advantage	2.994		
Primary HR Activities	Outsourcing intensity level	3.822	4.479	0.000
	Importance to competitive advantage	2.989		
Secondary HR Activities	Outsourcing intensity level	4.627	10.158	0.000
	Importance to competitive advantage	3.432		
General Office Activities	Outsourcing intensity level	5.159	22.934	0.000
	Importance to competitive advantage	1.329		
Administrative activities	Outsourcing intensity level	3.505	8.940	0.000
	Importance to competitive advantage	1.436		
Support Activities	Outsourcing intensity level	5.319	18.285	0.000
	Importance to competitive advantage	1.707		
Marketing Activities	Outsourcing intensity level	3.250	-7.158	0.000
	Importance to competitive advantage	3.950		
Sales Activities	Outsourcing intensity level	2.484	-13.908	0.000
	Importance to competitive advantage	4.404		
Logistics Activities	Outsourcing intensity level	3.542	3.844	0.000
	Importance to competitive advantage	2.755		
Manufacturing Activities	Outsourcing intensity level	4.627	10.158	0.000
	Importance to competitive advantage	3.432		
Information Systems Activities	Outsourcing intensity level	3.365	7.648	0.000
	Importance to competitive advantage	2.072		

There are significant differences between outsourcing intensity of firm activities and these activities' importance to profitability and sustainable competitive advantage of the firm. A graphical visualization of the analysis is shown in figure 5.2

Figure 5.2 Graphical Visualization of Paired Sample t-Test Results for Firm Activities for Manufacturing and Service Firms

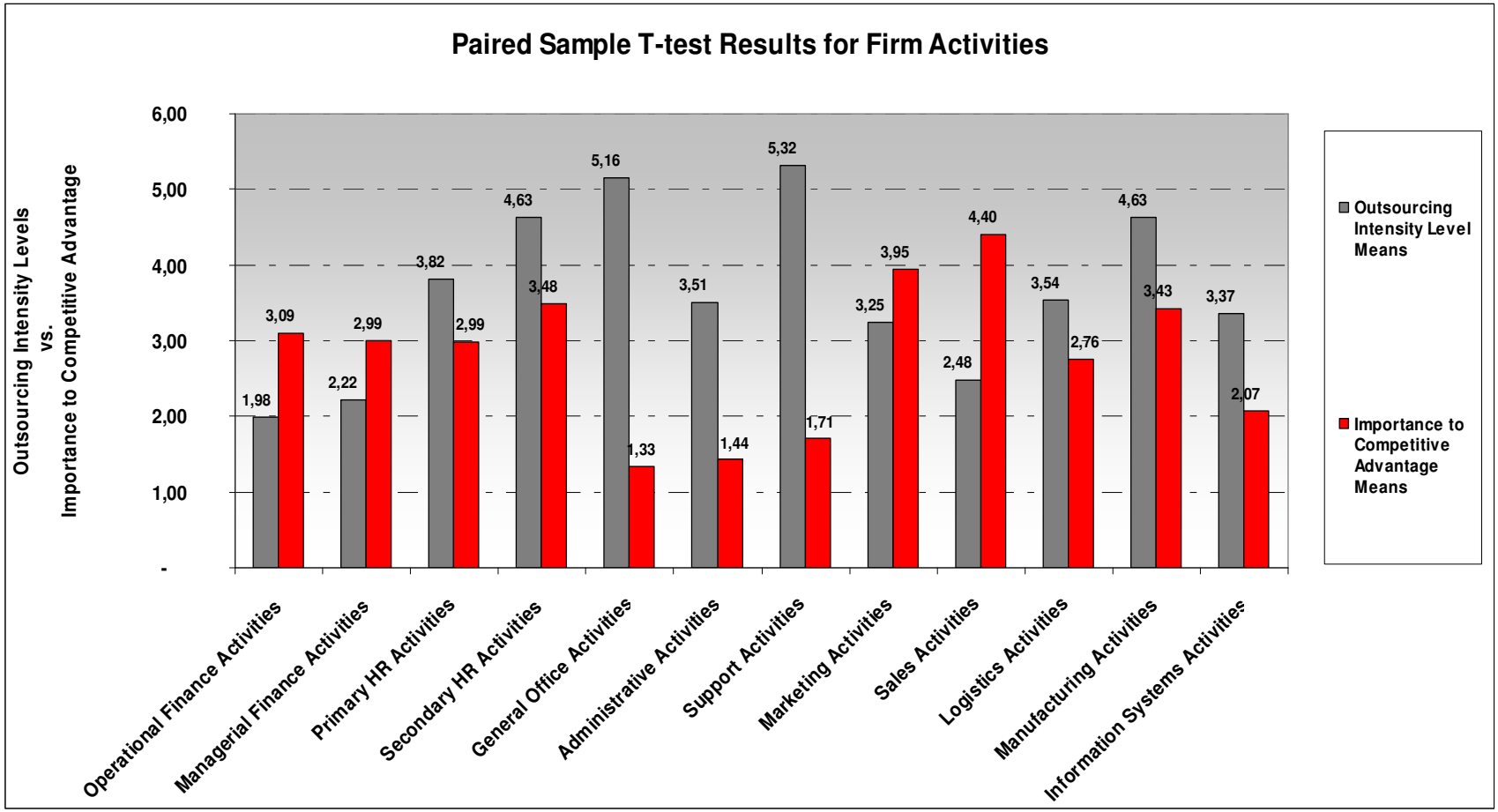


Figure 5.3 Graphical Visualization of Paired Sample t-Test Results for Firm Activities in Manufacturing Sector

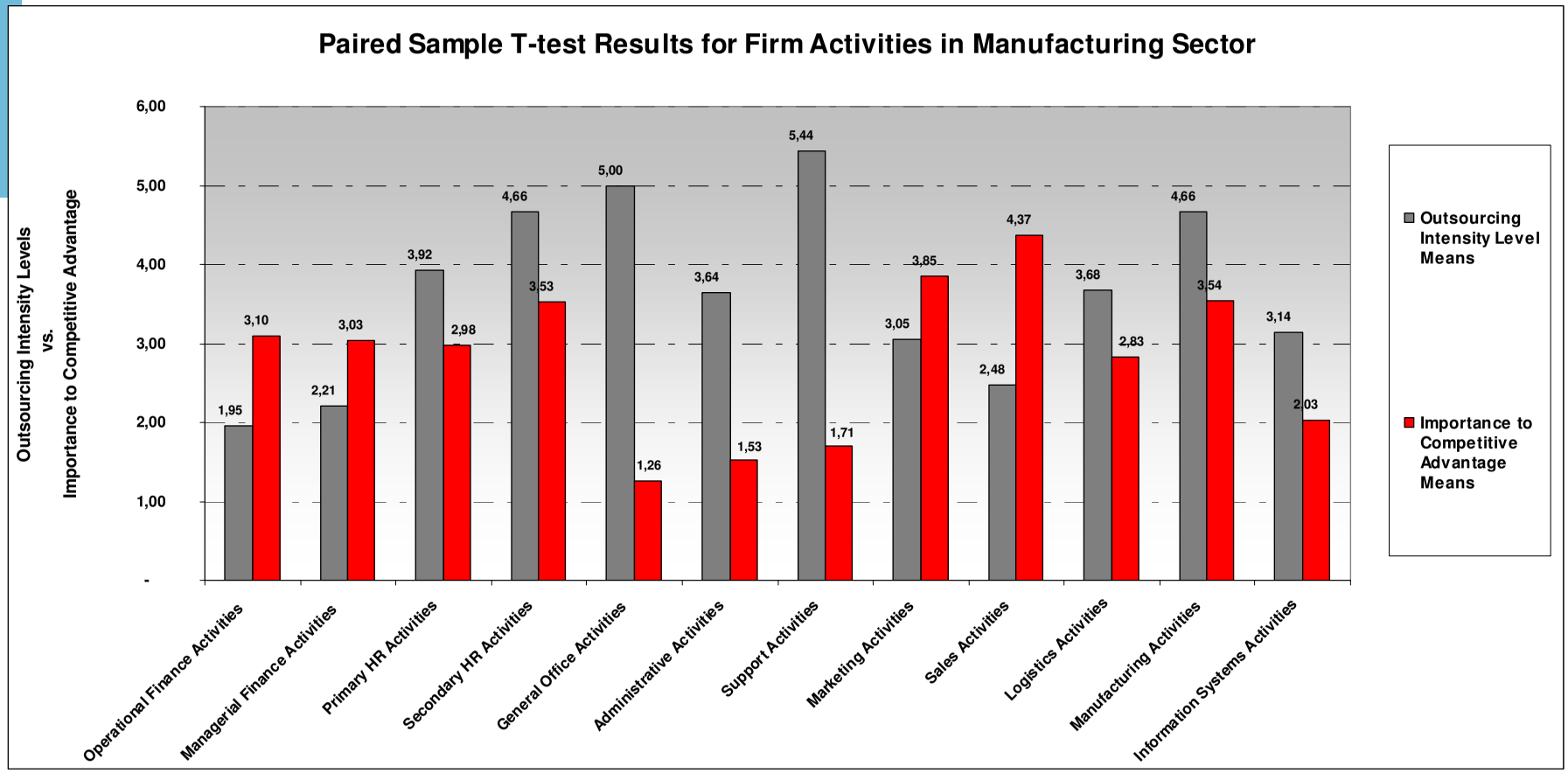
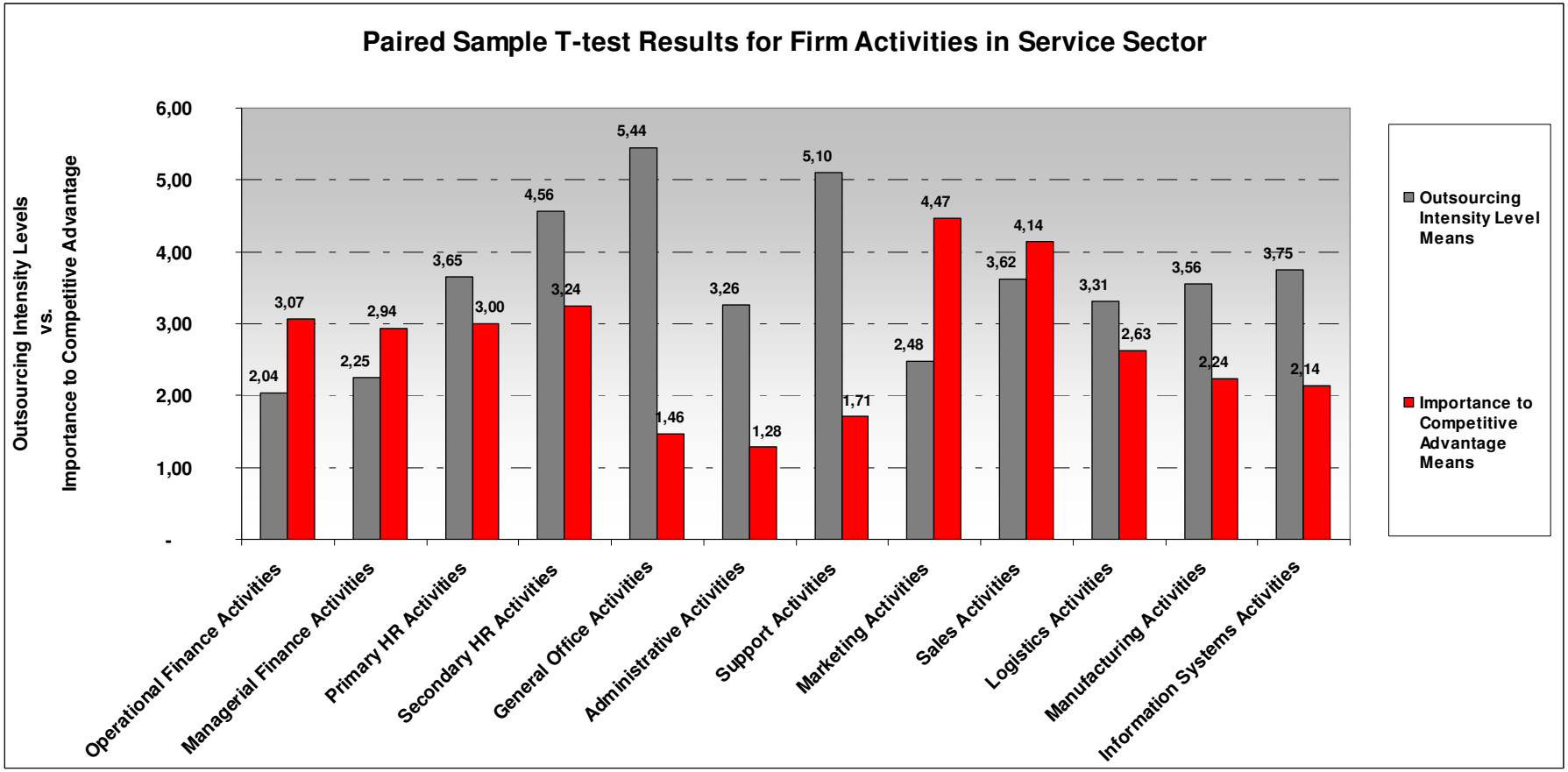


Figure 5.4 Graphical Visualization of Paired Sample t-Test Results for Firm Activities in Service Sector



When we analyze the paired differences between the means of related firm activity's importance to competitive advantage of the firm and the outsourcing intensity level of the activity, the analysis indicate that:

Operational finance activities' importance to competitive advantage of the firms are **higher** than the outsourcing intensity levels of the activities (t=-8.889, p=0.000, mean outsourcing intensity= 1.984, mean importance to competitive advantage=3.090).

Managerial finance activities' importance to competitive advantage of the firms are **higher** than the outsourcing intensity levels of the activities (t=-5.824, p=0.000, mean outsourcing intensity= 2.223, mean importance to competitive advantage=2.994).

Primary HR activities' importance to competitive advantage of the firms are **lower** than the outsourcing intensity levels of the activities (t=4.479, p=0.000, mean outsourcing intensity= 3.822, mean importance to competitive advantage=2.989).

Secondary HR activities' importance to competitive advantage of the firms are **lower** than the outsourcing intensity levels of the activities (t=10.158, p=0.000, mean outsourcing intensity= 4.627, mean importance to competitive advantage=3.432).

General office activities' importance to competitive advantage of the firms are **lower** than the outsourcing intensity levels of the activities (t=22.934, p=0.000, mean outsourcing intensity= 5.159, mean importance to competitive advantage=1.329).

Administrative activities' importance to competitive advantage of the firms are **lower** than the outsourcing intensity levels of the activities (t=8.940, p=0.000, mean outsourcing intensity= 3.505, mean importance to competitive advantage=1.436).

Support activities' importance to competitive advantage of the firms are **lower** than the outsourcing intensity levels of the activities (t=18.285, p=0.000, mean outsourcing intensity= 5.319, mean importance to competitive advantage=1.707).

Marketing activities' importance to competitive advantage of the firms are **higher** than the outsourcing intensity levels of the activities (t=-7.158, p=0.000, mean outsourcing intensity= 3.250, mean importance to competitive advantage=3.950).

Sales activities' importance to competitive advantage of the firms are **highe**r than the outsourcing intensity levels of the activities (t=-13.908, p=0.000, mean outsourcing intensity= 2.484, mean importance to competitive advantage=4.404).

Logistics activities' importance to competitive advantage of the firms are **lower** than the outsourcing intensity levels of the activities (t=3.844, p=0.000, mean outsourcing intensity= 3.542, mean importance to competitive advantage=2.755).

Manufacturing activities' importance to competitive advantage of the firms are **lower** than the outsourcing intensity levels of the activities (t=10.158, p=0.000, mean outsourcing intensity= 4.627, mean importance to competitive advantage=3.432).

Information systems activities' importance to competitive advantage of the firms are **lower** than the outsourcing intensity levels of the activities (t=7.648, p=0.000, mean outsourcing intensity= 3.365, mean importance to competitive advantage=2.072).

5.4 Multiple Regression Analysis

The multiple regression test results are presented in this section. The proposed conceptual model was modified in line with the results of the factor analysis (see figure 5.1).

In this section, the following steps are discussed:

(1) Investigating the determinants of outsourcing intensity level – through linear regression analyses

(2) Investigating the direct effects of independent variables on firm performance - through linear regression analyses

(3) Testing for mediator/moderator variables for the relation between outsourcing intensity and firm performannce

(4) Testing for combined models of the outsourcing intensity and firm performance relationship – through hierarchical regression analyses in two different industries/sectors

5.4.1 Multiple Regression Results for the Determinants of Outsourcing Intensity Level

Besides, from the analysis of proposed research model, the focus of this research is to find the determinants of outsourcing intensity of firms. Therefore, multiple regression analysis were conducted to test if benefits sought from outsourcing, generic firm strategies, environmental dynamism are all unique predictors of outsourcing intensity of firms. Multiple regression analysis was conducted for each independent variable and outsourcing intensity as the dependent variable.

5.4.1.1 Multiple Regression Model for Benefits Sought from Outsourcing and Outsourcing Intensity Level

When regression analysis were conducted for all of the benefits sought from outsourcing scale in order to find out their impact on the outsourcing intensity, three significant results were obtained (R^2 =0.340, F=11.319, p=0.000). These three results in fact explain 34% of outsourcing intensity meaning that there is a significant linear relationship between benefits sought from outsourcing and outsourcing intensity. Organization driven benefits had the highest and positive contribution to outsourcing intensity and therefore the strongest predictor of outsourcing intensity with β=0.511 meaning that organization driven benefits sought from outsourcing lead firms to increase outsourcing intensity levels. Employee/Customer driven benefits had a slightly lower negative contribution (β=-0.389). Market driven benefits had a lower and positive contribution to outsourcing intensity (β=0.170) meaning that market driven benefits sought from outsourcing does not lead firms to increase outsourcing intensity levels.

Table 5.18 Multiple Regressions Significant Results for Benefits Sought from Outsourcing and Outsourcing Intensity Level

Independent Variables		Dependent Variable	
	β coefficients	Outsourcing Intensity Level	R^2 =0.340 F= 11.319 P=0.000
Organization driven benefits	0.511		
Employee/Customer driven benefits	-0.389		
Market driven benefits	0.170		

5.4.1.2 Multiple Regression Model for Generic Firm Strategy and Outsourcing Intensity Level

When regression analysis were conducted for generic firm strategies scale in order to find out their impact on the outsourcing intensity, only three significant results were obtained (R^2 =0.113, F=2.845, p=0.000). These three results in fact explain 11% of outsourcing intensity. Cost leadership strategy for marketing functions had the highest and positive contribution to outsourcing intensity and therefore the strongest predictor of outsourcing intensity with β=.280 meaning that cost leadership strategy for marketing functions lead firms to increase outsourcing intensity levels. Cost leadership strategy for manufacturing functions had a slightly lower negative contribution (β=-0.238). Focus strategy had a lower and positive correlation with outsourcing intensity as its β=0.224.

Table 5.19 Multiple Regressions Significant Results for Generic Firm Strategy and Outsourcing Intensity Level

Independent Variables		Dependent Variable	
	β coefficients	Outsourcing Intensity Level	R^2 =0.113 F= 2.845 P=0.02
Cost leadership strategy for manufacturing functions	-0.238		
Cost leadership strategy for marketing functions	0.280		
Focus strategy	0.224		

5.4.1.3 Regression Model for Environmental Dynamism and Outsourcing Intensity Level

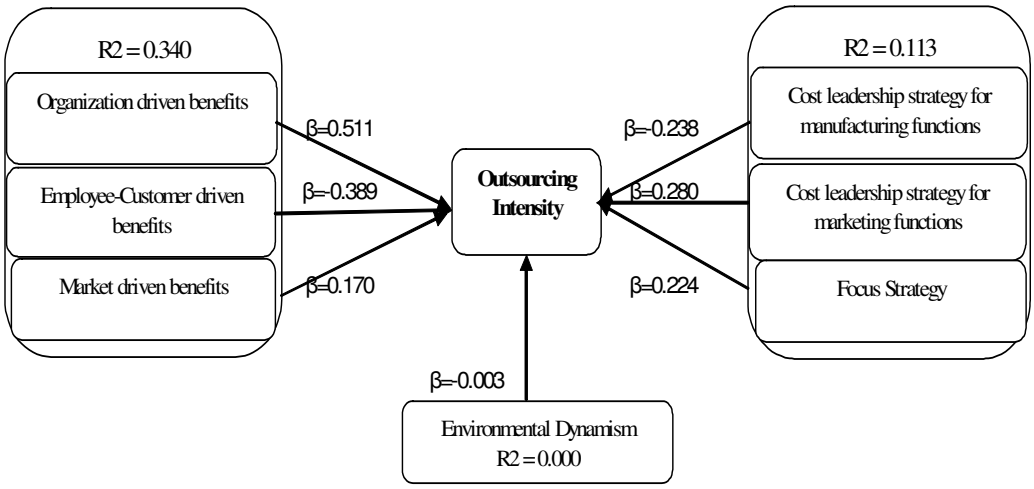
When regression analysis were conducted for environmental dynamism scale in order to find out its correlation with outsourcing intensity, no significant result was obtained (R^2 =0.000, F=0.001, p=0.980).

Table 5.20 Regression Analysis Results for Environmental Dynamism and Outsourcing Intensity Level

Independent Variables		Dependent Variable	
	β coefficients	Outsourcing Intensity Level	R^2 =0.000 F= 0.001 P=0.980
Environmental Dynamism	-0.003		

A summary of the direct effects of benefits sought from outsourcing, generic firm strategy, and environmental dynamism on outsourcing intensity is given in Figure 5.2.

Figure 5.5 Determinants of Outsourcing Intensity Level - Direct Effects of Independent Variables



5.4.2 Multiple Regression Results for Direct Effects of Independent Variables on Firm Performance

In order to determine the influence of outsourcing intensity on firm performance and explore the linear relationships of generic firm strategies and environmental dynamism on firm performance, regression analysis was conducted.

5.4.2.1 Multiple Regression Model for Generic Firm Strategies and Firm Performance

When multiple regression analysis was conducted, none of the generic firm strategies had significant relationships to firm performance.

5.4.2.2 Regression Model for Environmental Dynamism and Firm Performance

When regression analysis was conducted, environmental dynamism did not have any direct significant relationship to firm performance.

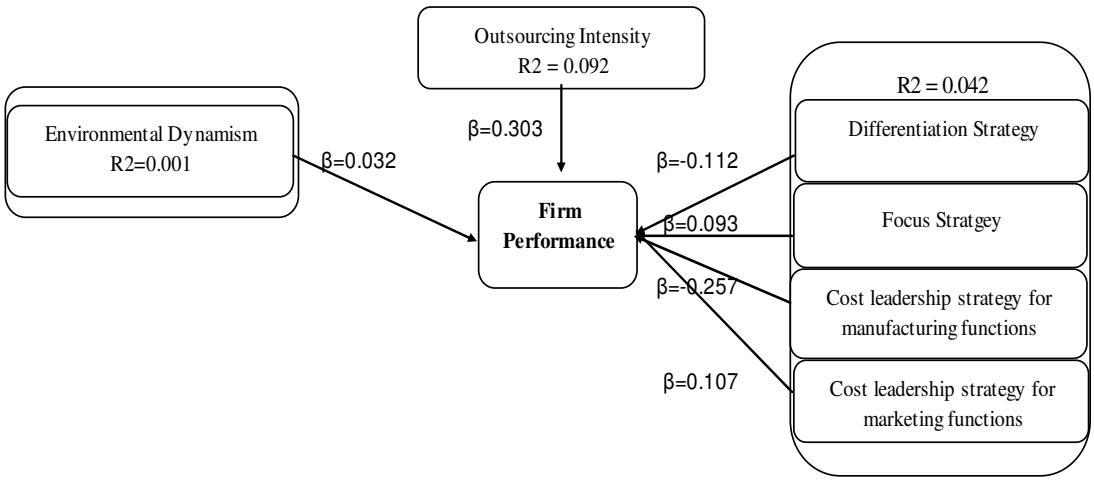
5.4.2.3 Regression Model for Outsourcing Intensity and Firm Performance

When regression analysis was conducted in order to find out the impact of outsourcing intensity on firm performance, a significant result was obtained (R^2 =0.092, F=9.320, p=0.003).Outsourcing intensity had a slightly low positive contribution (β=0.303) to firm performance.

Table 5.21 Regression Analysis Results for Outsourcing Intensity and Firm Performance

Independent Variables		Dependent Variable	
	β coefficients	Firm Performance	R^2 =0.092 F= 9.320 P=0.003
Outsourcing Intensity	0.303		

Figure 5.6 Direct Effects of Independent Variables on Firm Performance

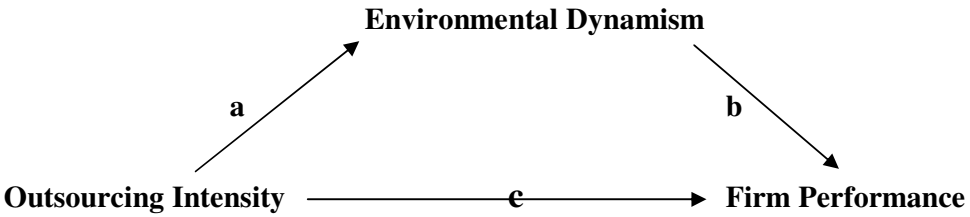


5.4.3 Regression Results for Testing Mediator / Moderator Variables for the Relation Between Outsourcing Intensity and Firm Performance

5.4.3.1The Mediator Model and Regression Results for Testing Mediators

To explore the mediator variables in outsourcing intensity and firm performance relationship, the following mediation models were constructed:

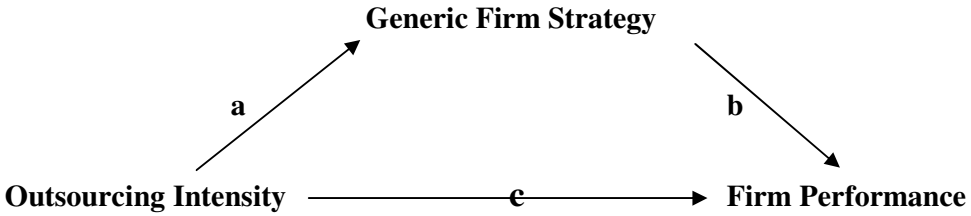
Figure 5.7 Mediator Model for Testing Environmental Dynamism as a Mediator in Outsourcing Intensity and Firm Performance Relationship



In general, a given variable may be said to function as a mediator to the extent that it accounts for the relation between the predictor and the criterion. This model assumes a three-variable system such that there are two causal paths feeding into the outcome variable (firm performance): the direct impact of the independent variable (path c) and the impact of the mediator – environmental dynamism (path b). There is also a path from the independent variable – outsourcing intensity – to the mediator – environmental dynamism (path a).

On the other hand, a second mediator model is constructed for testing generic firm strategies as a mediator in outsourcing intensity and firm performance relationship:

Figure 5.8 Mediator Model for Testing Generic Firm Strategy as a Mediator in Outsourcing Intensity and Firm Performance Relationship



In this model, again, a three variable system is assumed. Similar to the first model, there are two causal paths feeding into the outcome variable (firm performance): the direct impact of the independent variable – outsourcing intensity (path c) and the impact of the mediator – generic firm strategy (path b).

A variable functions as a mediator when it meets the following conditions: (a) variations in levels of the independent variable significantly account for variations in the presumed mediator (i.e path a), (b) variations in the mediator significantly account for variations in the dependent variable (i.e path b), and (c) when paths a and b are controlled, a previously significant relation between the independent and dependent variables is no longer significant, with the strongest demonstration of mediation occurring when path c is zero (Baron&Kenny,1986). So, from a theoretical

perspective, a significant increase/decrease demonstrates that a given mediator is indeed potent.

Since there is no need for hierarchical or stepwise regression or the computation of any partial or semipartial correlations (Baron&Kenny, 1986), the following three regression equations were tested for both mediators: First, regressing the mediator (environmental dynamism/generic firm strategy) on the independent variable (outsourcing intensity), second regressing the dependent variable (firm performance) on the independent variable (outsourcing intensity), and third, regressing the dependent variable (firm performance) on both the independent variable and on the mediators. These three regression equations provide the tests of our mediation models. Theoratically, to establish mediation, the following conditions must hold: First the independent variable must effect the mediator in the first equation; second the independent variable must be shown to affect the dependent variable in the second equation; and third; the mediator must effect the dependent variable in the third equation.If these conditions all hold in the predicted direction, then the effect of the independent variable on the dependent variable must be less in the third equation than in the second (perfect mediation holds if the independent variable has no effect when the mediator is controlled).

Because the independent variable is assumed to cause the mediator, these two variables should be correlated first to talk about a mediator relationship. In our models, the presence of such a correlation did not exist when the regression analysis were run (Figure 5.6 & 5.7). So, neither environmental dynamism nor generic firm strategies do act as mediator variables in outsourcing intensity and firm performance relationship.

Figure 5.9 Dirrect Effects of Environmental Dynamism as a Mediator on Outsourcing Intensity and Firm Performance

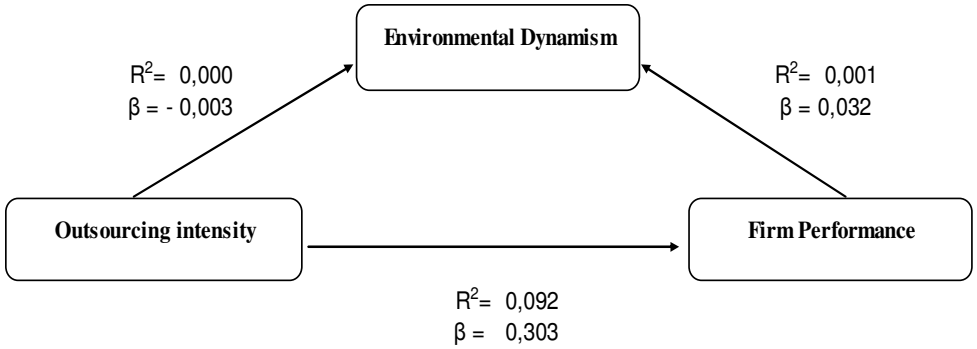
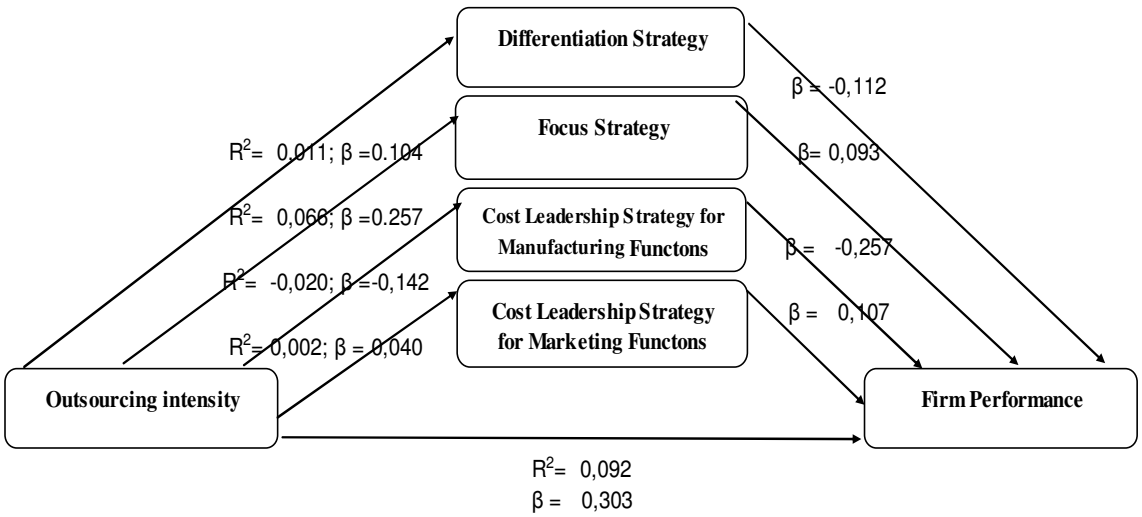


Figure 5.10 Dirrect Effects of Generic Firm Strategy as a Mediator on Outsourcing Intensity and Firm Performance



5.4.3.2 The Moderator Model and Regression Results for Testing Moderators

As shown in the previous section, to demonstrate mediation, one must establish strong relations between (a) the predictor and the mediating variable and (b) the mediating variable and the predictor. In contrast to mediation, there is no need for strong relations between the predictor and the moderator to establish moderator relationships.

Figure 5.11 Moderator Model for Testing Environmental Dynamism as a Moderator in Outsourcing Intensity and Firm Performance Relationship

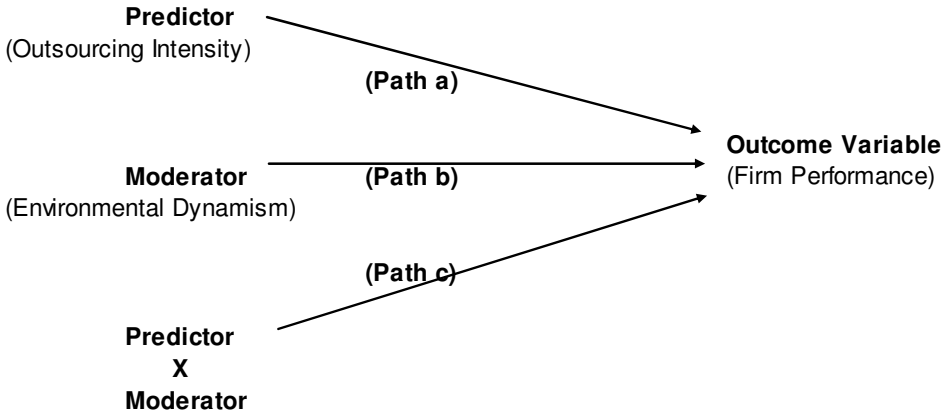
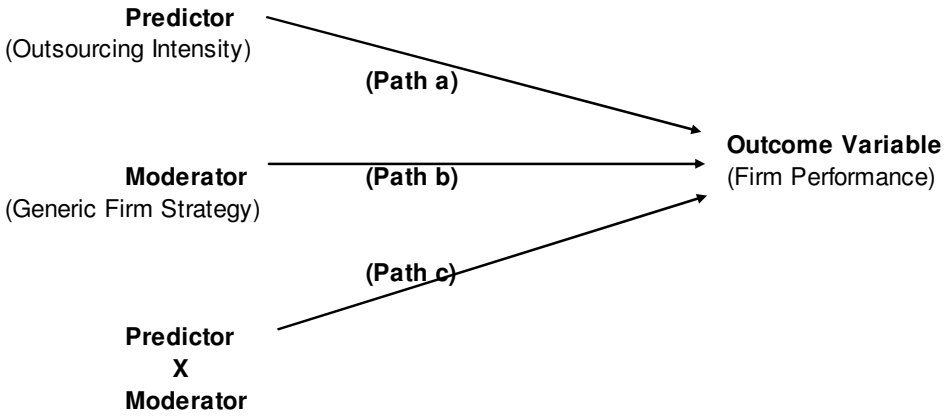


Figure 5.12 Moderator Model for Testing Generic Firm Stratey as a Moderator in Outsourcing Intensity and Firm Performance Relationship



The models diagrammed in Figure 5.8 and Figure 5.9 have three causal paths that feed into the outcome variable of firm performance: the impact of the outsourcing intensity as a predictor (Path a), the impact of environmental dynamism or generic firm strategy as a moderator (Path b), and the interaction of these two with the outcome (Path c). The moderator hypothesis is supported if the interaction (Path c) is significant. There may also be significant main effects for the predictor and the moderator (Paths a and b), but these are not directly relevant conceptually to testing the moderator hypothesis (Baron&Kenny, 1986).

In addition to these theoretical considerations, it is desirable that moderator variable be uncorrelated with both the predictor and the criterion (dependent variable) to provide a clearly interpretable interaction term. Another property of moderator variable is that unlike the mediator – predictor relation (where the predictor is correlated to the mediator), moderators and predictors always function as independent variables. In order to test our proposed moderator models for environmental dynamism and generic firm strategy as moderator variables in outsourcing intensity and firm performance relationship, regression analysis were conducted. The results are demonstrated in the following figures:

Figure 5.13 Moderator Model for Testing Environmental Dynamism as a Moderator in Outsourcing Intensity and Firm Performance Relationship

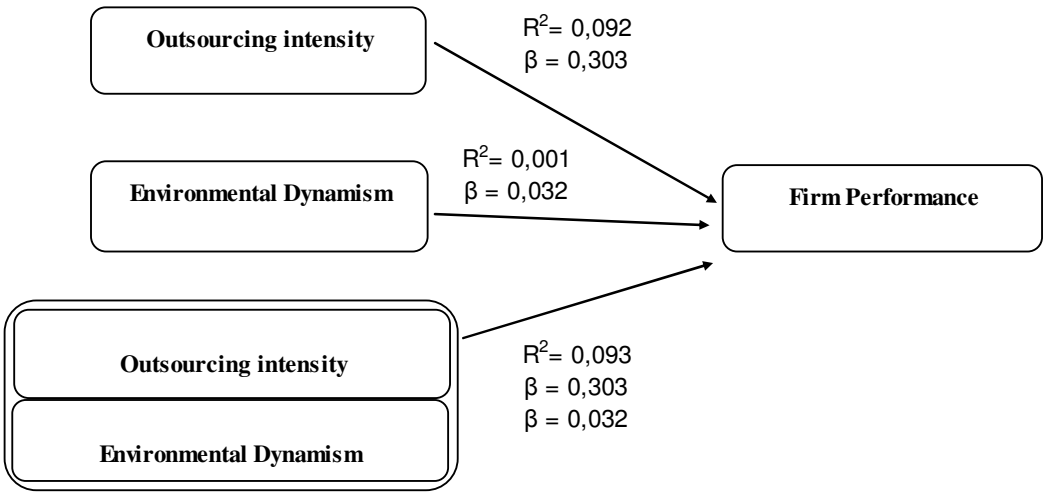
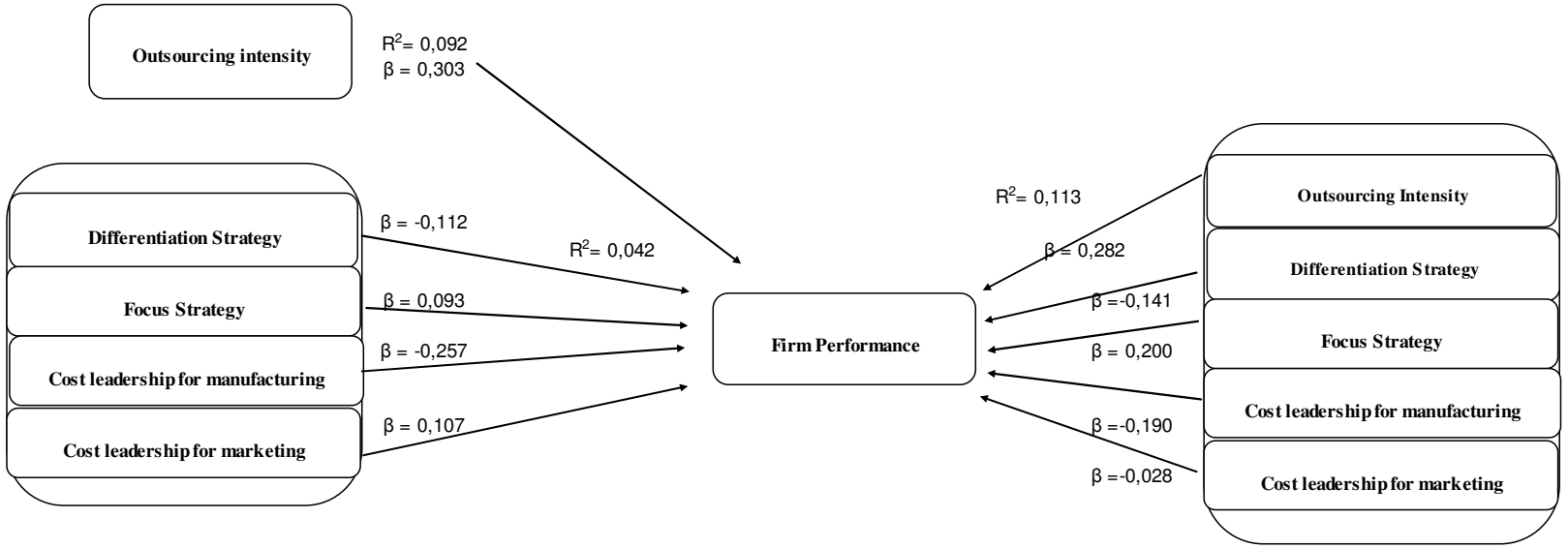


Figure 5.14 Moderator Model for Testing Generic Firm Stratey as a Moderator in Outsourcing Intensity and Firm Performance Relationship



In order to support a moderator relationship, the interaction of independent and moderator variable together on the dependent variable should be significant as mentioned before. In both of our suggested moderator models, there is a significant but weak relationship (R^2= 0.0993, R^2= 0.113). It is also desirable that moderator variables be uncorrelated to the predictor and criterion variable to talk about a clearly interpretable relationship. In the moderator model that we tested for generic firm strategy, there is a weak positive correlation between generic firm strategy and firm performance (R^2= 0.042). In conclusion, environmental dynamism and generic firm strategy act as weak moderators in outsourcing intensity and firm performance relationship.

5.4.4 Regression Analyses Results for Combined Models

In this section, the objective is to explore if the independent variables are more accountable in explaining firm performance when they act together. In order to reach this objective, hierarchical regression analyses are conducted. We developed three combined models where

1) The combined effect of outsourcing intensity and environmental dynamism on firm performance
2) The combined effect of outsourcing intensity and generic firm strategy on firm performance
3) The combined effect of outsourcing intensity and benefits sought from outsourcing on firm performance

are investigated for the whole sample, manufacturing firms and service firms consecutively.

5.4.4.1 Combined Effects of Environmental Dynamism and Outsourcing Intensity on Firm Performance

When hierarchical multiple regression analysis was conducted to analyze the combined effects of environmental dynamism and outsourcing intensity on firm performance, the combined model was significant with p=0.012 resulting in an F ratio of 4.668 although about a total of 9.3% of the variance in firm performance was explained by environmental dynamism (0.1%), and outsourcing intensity (9.2%). In other words, environmental dynamism alone accounts for 0.1% of the variance in firm performance and outsourcing intensity alone accounts for 9.2% of the variance in firm performance after controlling for environmental dynamism. The R square change associated with environmental dynamism (0.1%) is very small with β= 0.032 meaning that environmental dynamism is not a good predictor of firm performance. Outsourcing intensity, on the other hand, had a higher and positive contribution to firm performance with β= 0.303 and R square change of 9.2%.

Table 5.22 Hierarchical Regression Analysis Results for Combined Effects of Environmental Dynamism and Outsourcing Intensity on Firm Performance

Models / Independent Variables		**Dependent Variable / Combined Model**	
Models / Independent Variables	β coefficients / R^2 change		
Model 1: Environmental Dynamism	β =0.032 R^2 change = 0.01	Firm Performance	Combined Model: R^2 =0.093 F= 4.668 P=0.012
Model 2: Outsourcing Intensity	β =0.303 R^2 change = 0.092		

Table 5.23 Hierarchical Regression Analysis Results for Combined Effects of Environmental Dynamism and Outsourcing Intensity on Firm Performance in Manufacturing Sector

Models / Independent Variables		Dependent Variable / Combined Model	
Models / Independent Variables	β coefficients / R^2 change		
Model 1: Environmental Dynamism	β =0.056 R^2 change = 0.000	Firm Performance	Combined Model: R^2 =0.134
Model 2: Outsourcing Intensity	β =0.369 R^2 change = 0.134		F= 4.397 P=0.017

Table 5.24 Hierarchical Regression Analysis Results for Combined Effects of Environmental Dynamism and Outsourcing Intensity on Firm Performance in Service Sector

Models / Independent Variables		Dependent Variable / Combined Model	
Models / Independent Variables	β coefficients / R^2 change		
Model 1: Environmental Dynamism	B=-0.025 R^2 change = 0.000	Firm Performance	Combined Model: R^2 =0.071 F= 1,188 P=0.318
Model 2: Outsourcing Intensity	β =0.269 R^2 change = 0.071		

5.4.4.2 Combined Effects of Generic Firm Strategy and Outsourcing Intensity on Firm Performance

When hierarchical multiple regression analysis was conducted to analyze the combined effects of generic firm strategies and outsourcing intensity on firm performance, the combined model was significant with p=0.05 resulting in an F ratio of 2.238 although about a total of 11.3% of the variance in firm performance was explained by generic firm strategies (4.2%), and outsourcing intensity (7.1%). In other words, generic firm strategies alone accounts for 4.2 % of the variance in firm performance and outsourcing intensity alone accounts for 7.1% of the variance in firm performance after controlling for generic firm strategies. The R square change associated with generic firm strategies (4.2%) is slightly small meaning that generic firm strategies alone do not have a significant contribution to firm performance when they act alone. Outsourcing intensity, on the other hand, had a higher and positive contribution to firm performance with β= 0.282 and R square change of 7.1%.

Table 5.25 Hierarchical Regression Analysis Results for Combined Effects of Generic Firm Strategies and Outsourcing Intensity on Firm Performance

Models / Independent Variables		**Dependent Variable / Combined Model**	
Models / Independent Variables	β coefficients / R^2 change		
Model 1: Generic Firm Strategies -Differentiation Strategy - Focus Strategy -Cost leadership for manufacturing - Cost leadership for marketing	R^2 change = 0.042 β = -0.141 β = 0.030 β = -0.190 β = 0.028	Firm Performance	Combined Model: R^2 =0.113 F= 2.238 P=0.05
Model 2: Outsourcing Intensity	β = 0.282 R^2 change = 0.071		

Table 5.26 Hierarchical Regression Analysis Results for Combined Effects of Generic Firm Strategies and Outsourcing Intensity on Firm Performance in Manufacturing Sector

Models / Independent Variables		**Dependent Variable / Combined Model**	
Models / Independent Variables	β coefficients / R^2 change		
Model 1: Generic Firm Strategies -Differentiation Strategy - Focus Strategy -Cost leadership for manufacturing - Cost leadership for marketing	R^2 change = 0.053 β = -0.181 β = -0.001 β = -0.194 β = 0.128	Firm Performance	Combined Model: R^2 =0.178 F= 2.345 P=0.053
Model 2: Outsourcing Intensity	β =0.387 R^2 change = 0.125		

Table 5.27 Hierarchical Regression Analysis Results for Combined Effects of Generic Firm Strategies and Outsourcing Intensity on Firm Performance in Service Sector

Models / Independent Variables		**Dependent Variable / Combined Model**	
Models / Independent Variables	β coefficients / R^2 change		
Model 1: Generic Firm Strategies -Differentiation Strategy - Focus Strategy -Cost leadership for manufacturing - Cost leadership for marketing	R^2 change = 0.209 β = 0.514 β = 0.348 β = -0.125 β = 0.433	Firm Performance	Combined Model: R^2 =0.227 F= 1.646 P=0. 181
Model 2: Outsourcing Intensity	β = 0.142 R^2 change = 0.018		

5.4.4.3 Combined Effects of Benefits Sought from Outsourcing and Outsourcing Intensity on Firm Performance

When hierarchical multiple regression analysis was conducted to analyze the combined effects of benefits sought from outsourcing and outsourcing intensity on firm performance, the combined model was significant with p=0.000 resulting in an F ratio of 15.008. 46.3% of the variance in firm performance was explained by benefits sought from outsourcing (45.7%), and outsourcing intensity (0.6%). In fact, benefits sought from outsourcing alone accounts for 45.7 % of the variance in firm performance and outsourcing intensity alone accounts for 0.6% of the variance in firm performance after controlling for benefits sought from outsourcing. The reason behind the small R square

change associated with outsourcing intensity (0.6%) is the multicollinearity. High correlation was detected between benefits sought from outsourcing and outsourcing intensity and there was a significant linear relationship between benefits sought from outsourcing and outsourcing intensity. Considering that such high correlations cause problems when trying to draw inferences about the relative contribution of each independent variable to the success of the model, and adding the second variable does not significantly increase the predictive power of the model, it is meaningful not to use this model.

Table 5.28 Hierarchical Regression Analysis Results for Combined Effects of Benefits Sought from Outsourcing and Outsourcing Intensity on Firm Performance

Models / Independent Variables		**Dependent Variable / Combined Model**	
Models / Independent Variables	β coefficients / R^2 change		
Model 1: Benefits Sought from Outsourcing - Organization driven benefits - Employee/Customer driven benefits -Improvement Driven benefits - Market driven benefits	R^2 change = 0.457 β =0.417 β =0.134 β =0.221 β =0.151	Firm Performance	Combined Model: R^2 =0.463 F= 15.008 P=0.000
Model 2: Outsourcing Intensity	β =0.096 R^2 change = 0.006		

Table 5.29 Hierarchical Regression Analysis Results for Combined Effects of Benefits Sought from Outsourcing and Outsourcing Intensity on Firm Performance in Manufacturing Sector

Models / Independent Variables		**Dependent Variable / Combined Model**	
Models / Independent Variables	β coefficients / R^2 change		
Model 1: Benefits Sought from Outsourcing - Organization driven benefits - Employee/Customer driven benefits -Improvement Driven benefits - Market driven benefits	R^2 change = 0.502 β =0.545 β =0.038 β =0.207 β =0.158	Firm Performance	Combined Model: R^2 =0.512 F= 11.210 P=0.000
Model 2: Outsourcing Intensity	β =0.132 R^2 change = 0. 012		

Table 5.30 Hierarchical Regression Analysis Results for Combined Effects of Benefits Sought from Outsourcing and Outsourcing Intensity on Firm Performance in Service Sector

Models / Independent Variables		**Dependent Variable / Combined Model**	
Models / Independent Variables	β coefficients / R^2 change		
Model 1: Benefits Sought from Outsourcing - Organization driven benefits - Employee/Customer driven benefits -Improvement Driven benefits - Market driven benefits	R^2 change = 0.395 β =0.262 β =0.024 β =0.400 β =0.249	Firm Performance	Combined Model: R^2 =0.402 F= 3.765 P=0.010
Model 2: Outsourcing Intensity	β =0.116 R^2 change = 0. 007		

6. DISCUSSION AND CONCLUSION

In this section, a summary of the overall findings of the research is presented and related discussions of these findings are explained.

6.1 Summary of the Findings

In the literature review, it is mentioned that many researchers have made arguments both for and against outsourcing as a means of sustainable competitive advantage. However, less attention has been given to those factors that influence a firm's outsourcing intensity and previous works on the subject have examined a relatively narrow set of determinants. In addition, those works have dealt with either a single industry or the outsourcing of a single business activity. The aim of this research is to contribute to this domain by developing a more comprehensive set of potential determinants that drive the benefits sought from outsourcing decisions and outsourcing intensity which in turn should affect firm performance and test them for firms operating in different sectors/environments pursuing different generic firm strategies. In order to reach these objectives several analyses were conducted. In this section, the summary of the overall analyses and findings are presented.

6.1.1 Findings of Reliability and Factor Analyses

In general, the reliability and factor analyses were consistent with the literature. Generic firm strategies scale revealed four factors that were similiar to the generic strategies of Porter except for the cost leadership strategy. Cost leadership strategy were grouped into two factors and named as: cost leadership for marketing functions and cost leadership for manufacturing functions. The other two strategies generated from the analyses were labeled the same as Porter's generic strategies: differentiation and focus strategy.

In the benefits sought from outsourcing measure, four factors were emerged Employee and customer driven benefits were emerged as one dimension and grouped together. Organization driven benefits, improvement driven benefits and market driven benefits were labeled similar to literature. In this scale, asset management, organization

structure, cost structure, and credibility & image were omitted. Four main benefits were emerged and labeled as organization driven benefits, employee-customer driven benefits, improvement driven benefits and market driven benefits. Organization driven benefits factor included cash generation, core competencies, technology & know-how, operational performance and flexibility. Employee –Customer driven benefits included employee commitment, customer satisfaction, and product / service value. Improvement driven benefits included innovation, sales capacity / production capacity and market share. Lastly, market driven benefits included risk management and shareholder value. Our scale may not include all benefits sought from outsourcing as it changes in every organization as mentioned before but we think it may serve for an adequate job of capturing the main benefits sought from outsourcing for firms operating in any sector.

In the environmental dynamism scale, only one factor emerged and labeled same as the literature.

The firm performance scale, which originally constructed as financial and nonfinancial performance in literature, emerged with four factors named as: financial performance, innovation performance, employee performance and customer and supplier relations performance. Only stability of employment item was eliminated. Non- financial performance in literature was enriched with three factors labeled as innovation performance, employee performance and customer and supplier relations performance.

Outsourcing intensity scale grouped organizational activities in seven different functional business categories of a firm namely; finance and accounting functions, human resources functions, general and administrative functions, marketing functions, logistics functions, manufacturing functions, and information systems functions. A few items were eliminated from the scales, and some of the activities were divided into sub-activities. American Management Association's outsourcing survey instrument was used to list the distinct activities in functional business categories of a firm and this list was subsequently crosschecked with several items discussed by Porter (1985) in defining the value chain activities. Factor analyses results does not include all activities

in which organizations are engaged but serves for an adequate job of capturing the main business activities present in firms operating in any sector.

6.1.2 Findings of Independent Sample t-Tests

Independent sample t-Tests were conducted to analyze the differences between two industries, which are manufacturing and service. Research questions were also aimed to explore the industry differences of outsourcing industry and firm performance relationship for firms operating in different environments pursuing different generic strategies. Hypotheses 1a through 1e were tested to examine the industry differences for each scale.

Independent sample t-Test results for firm performance indicated that there was no significant difference between firm performance factors of firms in different industries. This result indicates that firms operating in manufacturing or service industries do not experience significant performance differences. Hypothesis 1d formed to test if there is a relationship between firm performance and industry/sector of a firm it operates was rejected. This finding, however, should not be interpreted as meaning that industry has no effect on firm performance. In the current study, performance was measured at the firm level for two industries only. However, it may be possible that industry can have impact on firm performance factors in many other industries.

Significant differences were found between generic strategies of firms in two different industries. The firms in the service industry apply more differentiation strategy than firms operating in manufacturing industry. Hypothesis 1c formed to test if there is a relationship between generic firm strategies and industry/sector of a firm it operates was accepted. On the other hand, firms in manufacturing industry apply more cost leadership strategies. Significant differences were also found for environmental dynamism in manufacturing and service sectors. Environmental dynamism was higher for firms operating in service sector. Hypothesis 1b formed to test if there is a relationship between environmental dyanmism and industry/sector of a firm it operates was accepted as well.

According to independent sample t-Test results indicating industry differences for outsourcing intensity scale, the only activities that had significant results for outsourcing intensity levels between two industries were marketing activities and information systems activities. The outsourcing intensity of marketing and information systems activities was higher for firms in the service sector. Therefore, hypothesis 1e formed to test if there is a relationship between outsourcing intensity of a business activity and industry of a firm it operates was accepted.

There were no significant differences between organization driven benefits, employee customer driven benefits, or market driven benefits sought from outsourcing in two different sectors. A significant difference was only found for improvement driven benefits sought from outsourcing. Improvement driven benefits sought from outsourcing were higher for firms operating in service sector. Hypothesis 1a formed to test if there is a relationship between benefits sought from outsourcing and industry of a firm it operates was accepted.

6.1.3 Findings of Paired Sample T-test

In order to figure out differences between firm activities' outsourcing intensity levels and these activities' importance to competitive advantage of the firm, paired sample t-test was performed. Hypothesis 3a through 3g were formed to test if there is a relationship between outsourcing intensity of an organizational activity and activity's importance to competitive advantage of the firm.

When paired differences between the means of related firm activity's importance to competitive advantage of the firm and the outsourcing intensity level of the activity for the whole sample was analysed, the analyses indicated that:

- Operational finance activities' importances to competitive advantage of the firms were higher when compared with the outsourcing intensity levels of those activities.

- Managerial finance activities' importances to competitive advantage of the firms were higher when compared with the outsourcing intensity levels of those activities.
- Primary and secondary human resources activities' importances to competitive advantage of the firms were lower when compared with the outsourcing intensity levels of those activities.
- General office activities' importances to competitive advantage of the firms were lower when compared with the outsourcing intensity levels of those activities.
- Administrative and support activities' importances to competitive advantage of the firms were lower when compared with the outsourcing intensity levels of those activities.
- Both marketing activities' and sales activities' importances to competitive advantage of the firms were higher when compared with the outsourcing intensity levels of related activities.
- Logistics activities' importances to competitive advantage of the firms were lower when compared with the outsourcing intensity levels of those activities.
- Manufacturing activities' importances to competitive advantage of the firms were lower when compared with the outsourcing intensity levels of those activities.
- Information systems activities' importances to competitive advantage of the firms were lower when compared with the outsourcing intensity levels of those activities.

These findings indicate that only managerial and operational finance activities in addition to sales and marketing activities were supposed to be core business functions receiving high scores on importance to competitive advantage and firms tend to outsource them less with lower outsourcing intensity levels.

Paired sample t-test results were similar for all business activities in both manufacturing and service industries.

6.1.4 Findings of Multiple Regression Analyses for the Determinants of Outsourcing Intensity Level

Besides from the proposed research model, this research aimed to find the determinants of outsourcing intensity of firms. Multiple regression analyses were conducted to test if benefits sought from outsourcing; generic firm strategies and environmental dynamism are all unique predictors of outsourcing intensity of firms.

Hypotheses 4a through 4f were constructed to test if there is a relationship between benefits sought from outsourcing and outsourcing intensity of a firm. Specifically for benefits sought from outsourcing scale, significant results for organization driven benefits, employee/customer driven benefits and market driven benefits were obtained. Organization driven benefits had the highest and positive contribution to outsourcing intensity and therefore the strongest predictor of outsourcing intensity meaning that organization driven benefits sought from outsourcing lead firms to increase outsourcing intensity levels. On the other hand, employee/customer driven benefits had a slightly lower negative contribution and market driven benefits had a lower and positive contribution to outsourcing intensity. All together, these three dimensions explained 34% of outsourcing intensity meaning that there is a significant linear relationship between benefits sought from outsourcing and outsourcing intensity.

Hypothesis 8 was formed to test if there is a relationship between generic firm strategies and outsourcing intensity of a firm. The findings for generic firm strategies scale indicate that only three generic strategies in fact explain 11% of outsourcing intensity. In this study, cost leadership for marketing functions had the highest and positive contribution to outsourcing intensity levels among other strategies and therefore the strongest predictor of outsourcing intensity meaning that cost leadership strategy for marketing functions lead firms to increase outsourcing intensity levels. Cost leadersip for manufacturing strategy and focus strategy also had a slightly lower contribution to outsourcing intensity levels. These results also indicate that firms pursuing strongest cost leadership and focus strategies have more intense outsourcing relative to firms following other strategy types.

Hypothesis 6 was formed to test if there is a relationship between environmental dynamism and outsourcing intensity of a firm. Environmental dynamism was found to have no significant effect on outsourcing intensity levels of firms.

6.1.5 Findings of Multiple Regression Analyses for Direct Effects of Independent Variables on Firm Performance

When the multiple regression analyses were conducted for the direct effects of generic firm strategies, environment and outsourcing intensity on firm performance, the only variable with significant explanatory power was outsourcing intensity. Therefore, no support was found for hypothesis 7 and hypothesis 10. Neither generic firm strategies, nor environment did have any significant impact on firm performance. Only 9,3 % of firm performance was explained by outsourcing intensity where outsourcing intensity had a slightly positive contribution to firm performance. Hypothesis 5 formed to test if there is a relationship between outsourcing intensity of a firm and firm performance was not rejected.

6.1.6 Findings of Regression Analyses for Testing Mediator Variables of the Outsourcing Intensity and Firm Performance Relationship

To explore the mediator variables in outsourcing intensity and firm performance relationship, two mediator models were constructed where the mediator effects of environmental dynamism and generic firm strategy were questioned. In general, a given variable may be said to function as a mediator to the extent that it accounts for the relation between the predictor and the criterion variable. In other words, a mediator effect would be detected for environmental dynamism or generic firm strategy if the following conditions were met:

a) Variations in levels of outsourcing intensity significantly account for variances in the mediator (environmental dynamism / generic firm strategy)

b) Variations in the mediator (environmental dynamism / generic firm strategy) significantly account for variations in firm performance

c) When the variations in a&b are controlled, a previously significant relationship between outsourcing intensity and firm performance is no longer significant.

Theoratically, to establish a mediator relationsip, the independent variable (outsourcing intensity) is assumed to cause the mediator (environmental dynamism / generic firm strategy). Therefore, outsourcing intensity and environmental dynamism or generic firm strategy should be correlated first to talk about a mediator relationship. In the current model, the presence of such a correlation did not exist. The results indicate that neither environmental dynamism nor generic firm strategies do act as mediator variables in outsourcing intensity and firm performance relationship.

6.1.7 Findings of Regression Analyses for Testing Moderator Variables of the Outsourcing Intensity and Firm Performance Relationship

In order to support a moderator relationship, the interaction of outsourcing intensity and environmental dynamism or generic firm strategy (moderators in the current model) together on firm performance should be significant. In both of suggested moderator models, there is a significant but week relationship. In the current study, environmental dynamism and generic firm strategy act as weak moderators in outsourcing intensity and firm performance relationship.

Firm strategy and environmental dynamism were found to moderate weakly the relationship between outsourcing intensity and firm performance. Therefore, the results of this study indicate that the influence of outsourcing on firm performance is not the same for firms operating in different environments or following different strategies.

6.1.8 Findings of Regression Analyses of Combined Models

The objective in developing combined models was to explore if the independent variables were more accountable in explaining firm performance when they act together.

When hierarchical multiple regression analyses was conducted to analyze the combined effects of environmental dynamism and outsourcing intensity on firm performance, the combined model was significant where a total of 9.3% of the variance in firm performance was explained by environmental dynamism (0.1%) and outsourcing intensity (9.2%). In other words, environmental dynamism alone accounts for 0.1% of the variance in firm performance and outsourcing intensity alone accounts for 9.2% of the variance in firm performance after controlling for environmental dynamism. This result indicates that environmental dynamism is not a good predictor of firm performance. Outsourcing intensity, on the other hand, has a higher and positive contribution to firm performance.

When the combined effects of generic firm strategies and outsourcing intensity on firm performance were analysed, the combined model was also significant where a total of 11.3% of the variance in firm performance was explained by generic firm strategies (4.2%), and outsourcing intensity (7.1%). Therefore, generic firm strategy alone accounts for 4.2% of the variance in firm performance and outsourcing intensity alone accounts for 7.1% of the variance in firm performance after controlling for generic firm strategy. Generic firm strategies alone do not have a significant contribution to firm performance when they act alone. Outsourcing intensity, on the other hand, has a higher and positive contribution to firm performance.

The combined effects of benefits sought from outsourcing and outsourcing intensity on firm performance were also analysed. The combined model was significant where 46.3% of the variance in firm performance was explained by benefits sought from outsourcing (45.7%) and outsourcing intensity (0.6%). Benefits sought from outsourcing alone accounts for 45.7% of the variance in firm performance and outsourcing intensity alone accounts for 0.6% of the variance in firm performance after controlling for benefits sought from outsourcing. The reason is the multicollinearity existing between benefits sought from outsourcing and outsourcing intensity. High correlation was found to exist between benefits sought from outsourcing and outsourcing intensity.

6.1.9 Findings of Regression Analyses of Combined Models for Industrial Differences

In order to see the industrial differences, the combined models were analysed seperately for manufacturing and service industries.

When the whole data was analysed to investigate the combined effects of environmental dynamism and outsourcing intensity on firm performance, the combined model was significant where 9.3% of the variance in firm performance was explained by two variables. Specifically for manufacturing industry, 9.3% of the variance in firm performance increased to 13.4% where outsourcing intensity alone accounted for the whole variance of 13.4% in firm performance. However, in service industry, 7.1% of the variance in firm performance was explained alone by outsourcing intensity. This finding indicates that outsourcing intensity is a better predictor of firm performance in manufacturing industry than it is in service industry.

Generic firm strategies' and outsourcing intensity's effects on firm performance differentiated as well when seperately analysed for manufacturing and service industries. In manufacturing industry, both variables' combined effects on firm performance were higher (17,8%) where outsourcing intensity effects were more dominant (with 12.5% accountability) than generic firm strategies.

In the service industry, on the other hand, the finding was more interesting. The combined effects of both variables on firm performance were even higher (22.7%). Generic firm strategies alone explained 20.9% of the variance in firm performance where as outsourcing intensity had a relatively low effect of 1.8% in explaining the dependent variable.

It is meaningful to state that generic firm strategies are more dominant and effective than outsourcing intensity in explaining firm performance in service sector. On the other hand, outsourcing intensity is a better predictor than generic firm strategies in explaining firm performance in manufacturing industry. The combined effect of outsourcing intensity and generic firm strategies on firm performance

decreases to 17.8% in manufacturing sector where outsourcing intensity has a total accountability of 12.5% on the combined model.

To explore the industrial differences of combined effects of benefits sought from outsourcing and outsourcing intensity on firm performance, industry differences were also analysed. The combined model's accountability was higher (51.2%) in manufacturing industry when compared with service industry (40.2%).

6.2 Conclusion

In the literature review, it is mentioned that many researchers have made arguments both for and against outsourcing as a means of sustainable competitive advantage. However, less attention has been given to those factors that influence a firm's outsourcing intensity. Previous works on the subject have examined a relatively narrow set of determinants (Giley 1997, Butler 2006, Felton 2005, Giley&Rasheed 2000, Rodrigez&Robania 2004, Greer&Rasheed&Giley 2004, Calabrese&Erbetta2005, Jiang 2004, Görzig&Stephan 2002). In addition, those works have dealt with either a single industry or the outsourcing of a single activity.

Giley and Rasheed (2000), emprically examined the extent to which outsourcing of both periphal and near core tasks influences firm's financial and nonfinancial performance. In addition, they examined the potential moderating effects of firm strategy and the environment on the outsourcing performance relationship. Results indicated that, whereas there was no significant direct effect of outsourcing on firm performance, both firm strategy and environmental dynamism moderated the relationship between outsourcing and performance.

Espino-Rodrigez and Padron-Robania (2004) studied hotel sector managers' perceptions of the influence of outsourcing on operations strategy emprically and particularly on the objectives of cost reduction related operations, improved quality, flexibility and better service. They evidenced that outsourcing significantly influences hotel performance.

Greer&Rasheed&Giley (2004) emprically analyzed the relationship between the outsourcing of human resource (HR) activities, namely training and payroll, and firm performance. They tested for the potential moderating effects of firm size. Results indicated that both training and payroll outsourcing have implications form firm performance but findings regarding a moderating effect of firm size were in conclusive.

Calabrese & Erbetta (2005) investigated whether the outsourcing strategy has positively affected the overall performance of a total of 456 automative suppliers in Italy. They observed by means of financial statements and under different viewpoints: growth, productivity, financial dependence and profitability. Their findings pointed out that firms always characterised by low integration or that deverticalised their productive structure over time have shown the highest growth, whereas firms with high integration level or that pursued a verticalisation strategy performed better in respect of profitability and debt ratio.

Jiang (2004), the owner of outstanding doctoral research award of Emerald in 2005, analyzed a sample of publicly traded firms that outsourced parts of their operations between 1990 and 2002. Jiang used publicly avaliable acounting data to test for changes in operating performance and abnormal return rates of stock that result from outsourcing decisions. This research was one of the first emprical study to examine the outsourcing impact on firm's performance and value by audited financial data rather than subjective perceptual measures. There is no emprical evidence in Jiang's research to support that outsourcing will improve a firm's productivity and profitability. But it provides solid evidence that outsourcing can improve a firm's cost efficiency and protect, if not increase, the firm's value.

Görzig and Stephan (2002), emprically tested whether outsourcing is an important determinant for a firm's profitability. In addition, they provided estimates on the relative importance of firm, market (i.e industry), and location specific effects, as well as on the impact of organizational structure and human capital input on firm performance. Their analysis supported the view that firms tend to overestimate the

benefits accruing from outsourcing of external services and / or underestimate the associated transaction costs.

On the other hand, the number of emprical studies in Turkey about outsourcing was also very few. There is a comprehensive research conducted about developing logistics outsourcing and usage patterns in Turkey which is worth to be noted. Akyıldız's (2004) research was conducted to explore how logistics concept was perceived by Turkish firms, what level of logistics outsourcing were, what kind of logistical services were used , and what level of anticipated logistics outsourcing will there be in the next three to five years. Field survey was conducted with 800 manufacturing firms registered to the Union of Chambers and Commodity Exchanges, located in Ankara. The collected data was analyzed by using descriptive and nonparametric statistics. The results indicated that transportation and customs process are the functions most commonly outsourced. Although the level of logistics outsourcing were 77 percent, logistics partnership were at low levels sustained with very weak ties. All logistics functions, including transportation and customs brokerage at most, were anticipated to increase in the next three to five years.

Another comprehensive research about outsourcing was conducted by the joint work of IBM Turkey and Capital (a prestigious monthly periodical of business and economy in Turkey) in 2005. The field survey was presented to the CEOs, CIOs, general managers or senior information technology managers of 100 leading Turkish companies operating in a varity of sectors. According to the survey, outsourcing is growing most rapidly in information technology functions. The respondent firms intend to increase their outsourcing budgets by 35-40 % in 2006. The most noted reasons to outsource are cost driven reasons like reducing costs through superior provider performance and the provider's lower cost structure and turn their fixed costs into variable costs. Another noted reason to outsource is to increase organizational effectiveness by focusing on their core competencies and outsourcing the non-core, operational functions. Total outsourcing market in Turkey is about a hundred million dollars.

In short, outsourcing is a well established business practice both in Turkey and abroad. However, academic research about outsourcing is relatively new and scattered. The aim of this research was to contribute to this domain by developing a more comprehensive set of potential determinants that drive the benefits sought from outsourcing decisions and outsourcing intensity which in turn should affect firm performance and test them for firms operating in different sectors, pursuing different generic firm strategies. A critical challange facing organizations is how to effectively organize and manage outsourcing in accordance with the direction of their generic firm strategies. With the premise that organizations whose generic firm strategies (cost leadership, differentiation or focus) are compatible with their outsourcing intensity were expected to have better outsourcing benefits and organizational performance. By combining different and variety of perspectives, this dissertaion aimed to develop a multidimentional model that have not been outlined by other researchers in the field. The author aimed to figure out outsourcing, performance and strategy relationships of corporate firms in Turkey.

Specifically, the proposed research model has been drawn on transaction cost economics (Coase, 1937; Williamson, 1975, 1985) and the resource based perspective. The transaction cost theory perspective suggests that activities that are not firm-specific are more likely to be outsourced, while the resource-based perspective suggest that activities not critical to core competencies should be outsourced. In this study, direct effects of outsourcing intensity on firm performance have been emprically investigated through generic firm strategies and environmental dynamism. Strategy of the firm is proposed to directly affect the performance of firms (Porter, 1980; Weinzimmer, 2000) and the performance is the outcome of the fit between several factors as strategy, capabilities and environment (Bergeron, Raymond and Rivard, 2004).

In summary, the measures constructed and emprically tested in this dissertation are aimed at attempting to bridge literature findings. The theoratical measures proposed have been partly validated by the related findings of the analyses which are summarized as in the following.

There has been a large volume of research about benefits sought from outsourcing in literature as noted before. The most often discussed were improved financial performance and various nonfinancial performance effects, such as heightened focus on core competencies. An increased focus on an organization's core competencies was the most noted benefit associated with outsourcing (Dess1995, Kotabe & Murray 1990, Quinn 1992) and outsourcing non-core activities allowes the firm to increase managerial attention and resource allocation to those tasks it does best. Although outsourcing's potential benefits noted are many, Bettis (1992) and Kotabe (1992) argue that reliance on outside suppliers is likely to lead to a loss of overall market performance. Declining innovation by the outsourcer, a loss of long-run R&D are most serious threats (Kotabe, 1992). Maurice F. Greaver II. (1999) summarizes the benefits sought from outsourcing more comprehensively in six categories as we constructed in our scale. Greaver II noted that the critical point was to understand the reasons and the benefits sought for considering outsourcing. According to Greaver II, just as the probability of another person's suit of clothes fitting the other exactly is remote, so too is the probability of another organization's reasons to outsource fitting the other equally remote.

In our environmental dynamism measure, only one factor emerged and labeled same as the literature. We have noted that environmental impacts on organizational strategies, structures, processes and performance have been the subject of many studies in literature in the last four decades and therefore in the presence of strategy, the environment of the organization is usually taken into consideration. Some of these studies have specifically addressed the relationship between environmental dynamism and outsourcing strategies and one of these researchers were Giley (1997). In Giley's work, the relationship between outsourcing and firm performance was positive in stable environments, but negative in dynamic ones. As noted before, the relative dynamism in a firm's external environment may have important effects on outsourcing intensity. Environmental dynamism was defined as 'the rate of change and innovation in an industry as well as the uncertainity or predictability of the actions of competitors and customers.

The firm performance measure, which originally constructed as financial and nonfinancial performance in literature, emerged with four factors named as: financial performance, innovation performance, employee performance and customer and supplier relations performance. Only stability of employment item was eliminated. Non- financial performance in literature was enriched with three factors labeled as innovation performance, employee performance and customer and supplier relations performance. This finding is in fact very important for today's organizations where non-financial measures like innovation performance are considered very important parameters in today's everchanging business markets. On the other hand, employee performance emerged as another important factor in assessing non-financial performance in today's organizations where human capital is regarded among the most important intellectual capital resources of companies.

Generic firm strategies scale revealed four factors that were similiar to the generic strategies of Porter except for the cost leadership strategy. Cost leadership strategy were grouped into two factors and named as: cost leadership for marketing functions and cost leadership for manufacturing functions. The other two strategies generated from the analyses were labeled the same as Porter's generic strategies: differentiation and focus strategy.

In this research, we empirically tested if there is a relationship between generic firm strategies and outsourcing intensity of a firm. In this study, cost leadership for marketing functions had the highest and positive contribution to outsourcing intensity levels among other strategies and therefore the strongest predictor of outsourcing intensity meaning that cost leadership strategy for marketing functions lead firms to increase outsourcing intensity levels. Cost leadersip for manufacturing strategy and focus strategy also had a slightly lower contribution to outsourcing intensity levels. These results also indicate that firms pursuing strongest cost leadership and focus strategies have more intense outsourcing relative to firms following other strategy types. This finding is contrary to prior research done by Giley (1997). Giley's results indicate that firms pursuing stronger differentiation strategies have higher outsourcing intensity levels relative to other strategy types. According to Giley's research,

differentiators are more likely to outsource their firm activities than are cost leaders. In fact, Giley's finding was contrary to prior research on the strategy-internalization relationship. Specifically, Harrigan (1984) and Barney (1997) noted that differentiators should retain in-house those activities that add to the firm's level of differentiation. Therefore, differentiators would suppose to have less outsourcing intensity levels for their core business activities.

It is also empirically tested if there is a relationship between environmental dynamism and outsourcing intensity of a firm. Environmental dynamism was found to have no significant effect on outsourcing intensity levels of firms. This finding is contrary to most of the prior research. For example, Harrigan (1983), found that stable environments are ideally suited for internalization of activities. Similiarly, D'Aveni and Ravenscraft (1994) argued that internalization is more effective in stable environments. Thus, firms should, theoratically, outsource more in environments that are more dynamic. Therefore, the finding in this research that environmental dynamism has no effect on outsourcing intensity levels of firms is a divergence from prior research. According to literature, environmental dynamism is especially useful as an exploratory variable in organizational studies. The dynamic environment is influential on variety of management practices from strategy formation to performance (Miles et al., 2000). For instance, it is proposed that in dynamic environments organizations have to be innovative. Otherwise, they will have difficulties in keeping their market share (Miller,1988). Dynamic environments provide opportunities for the organizations. In dynamic environments, the diffrentiation strategy which mainly focuses on the adaptability to the environment is more beneficial. Cost leadership strategy, on the other hand, which is inflexible and requires rigid production and management practices may lower the performance levels of organizations. (Miller and Toulouse, 1986). Harrigan (1983) found that internalization of tasks is ideal for firms in stable environments. Conversely, D'Aveni and Ravenscraft (1994) argue that, when industry demand is uncertain, internalization can lead to higher administrative costs and lower margins as a result of coordination and information processing costs. Also, uncertainity with respect to demand makes outsourcing attractive because it allows firms to shift much of the risk associated with declining demand (such as idle equipment and head count reductions) to

supplier firms. Finally, the changes in technology that accompany high levels of environmental dynamism can make what was once a very valuable organizationaltechnology to become suddenly obsolete. By increasing their reliance on outsourcing during times of high environmental dynamism, managers may have the flexibility to change suppliers as technological advancements warrant (Giley, 1997). In line of these arguments above, we proposed that firms operating in more dynamic environments would pursue more intense outsourcing strategies, however our finding in this research that environmental dynamism has no effect on outsourcing intensity levels of firms is a divergence from prior research.

Firm performance has long been the primary dependent variable in strategic management research. However, prior firm performance cannot be looked upon only as an outcome of organization-strategy-environment interactions. Rather it must be viewed as an important input to managerial decision making. Keeping in mind that a firm's historical performance may be an important independent variable that influences a number of managerial decisions, we have built our model to explore the direct effects of strategy and outsourcing intensity on firm performance.

The performance implications of outsourcing have been widely debated as mentioned before in literature. However, little research has been conducted to determine whether and to what extent outsourcing influences firm performance. In the current study, the impact of outsourcing intensity on firm performance was examined. The results indicate that firms pursuing more intense outsourcing strategies experience slightly positive performance impacts. This finding should not be interpreted as meaning that outsourcing has significant effect on firm performance. In the current study, performance was measured at the firm level. Thus, outsourcing was found to have low positive contribution on the financial, innovation, employee and customer and supplier relations performance of the firm overall. However, it is possible that outsourcing has an impact on the individual functional areas in which it occurs. For example, a firm's manufacturing operations may experience cost reductions as a result of outsourcing, or a firm may improve its customer service by shifting it to an outside specialist organization. Therefore, individual functional areas may experience

performance improvements (or declines) because of outsourcing. In the current study, only a firm-level positive performance impact of outsourcing was detected.

For moderator effects, firm strategy and environmental dynamism were found to moderate weakly the relationship between outsourcing intensity and firm performance. Therefore, the results of this study indicate that the influence of outsourcing on firm performance is not the same for firms operating in different environments or following different strategies. As stated by the literature also, firm strategy and environmental dynamism both moderate the relationship between outsourcing intensity and firm performance.

The overall results of the above analyses indicate that the influence of environment, outsourcing intensity and generic firm strategies on firm performance is not the same for firms operating in manufacturing and service industries. The impact of outsourcing intensity on firm performance varies with different levels of environmental dynamism and firm strategies and this effect is more apparent and higher in manufacturing industry.

When generic firm strategies' and outsourcing intensity's combined effects were analysed on firm performance, there was a considerable difference in service industry. Generic firm strategies have significant effects on firm performance in service sector when analysed together with outsourcing intensity.

It is meaningful to state that generic firm strategies are more dominant and effective than outsourcing intensity in explaining firm performance in service sector. On the other hand, outsourcing intensity is a better predictor than generic firm strategies in explaining firm performance in manufacturing industry

The combined models actually prove that the joint effects of our independent variables (environmental dynamism, generic firm strategy, outsourcing intensity) on firm performance are more beneficial for our understanding of firm performance effects than their direct effects. When they are combined, the explanatory power of these combined models increase. In the industrial analyses, the explanatory power of the

models increases even more when outsourcing intensity accomplished by environmental dynamism and generic firm strategies.

In conclusion, this study has investigated the determinants and performance implications of outsourcing decisions in light of generic firm strategies and environmental dynamism variables. The emprical research suggest that:

- Firms in service industry apply more differentiation strategy than firms in manufacturing industry and firms in manufacturing industry apply more cost leadership strategies.
- Environmental dynamism is higher for firms operating in service industry.
- The outsourcing intensity of marketing and information systems activities are higher for firms operating in the service sector.
- Especially improvement driven benefits sought from outsourcing is higher for firms operating in service industry.
- Managerial and operational finance activities in addition to sales and marketing activities receive high scores on importance to competitive advantage and firms tend to outsource them less with lower outsourcing intensity levels.
- Organizational driven benefits, employee/customer driven benefits and market driven benefits lead firms more to increase outsourcing intensity levels.
- Firms pursuing stronger cost leadership and focus strategies have more intense outsourcing relative to firms pursuing differentiation strategies.
- Environmental dynamism has no significant effect on outsourcing intensity levels of firms.
- Neither generic firm strategy nor environment has direct significant effect on firm performance. Only outsourcing intensity has low positive contribution to firm performance at the firm level.

- Neither environmental dynamism nor generic firm strategies do act as mediator variables in outsourcing intensity and firm performance relationship.
- Generic firm strategies and environmental dynamism moderate weakly the relationship between outsourcing intensity and firm performance. The influence of outsourcing on firm performance is not the same for firms operating in different environments or following different firm strategies.
- The combined effects of both environmental dynamism / generic firm strategy and outsourcing intensity on firm performance is significant. When they act alone (environmental dynamism/generic firm strategy), they do not have a significant contribution to firm performance. When they act together with outsourcing intensity, all together they have a higher and positive contribution to firm performance.
- The overall results of combined models also indicate that the influence of environment, outsourcing intensity and generic firm strategies is not the same for firms operating in manufacturing and service industries. The impact of outsourcing intensity on firm performance varies with different levels of environmental dynamism and firm strategies and this effect is more apparent in manufacturing industry.

6.3 Overall Discussion

The most important finding in this study is that neither generic firm strategy nor environment has direct significant effect on firm performance. Only outsourcing intensity has positive contribution to firm performance at the firm level. The results indicate that firms pursuing more intense outsourcing strategies can experience significant performance effects. However, this finding was measured at the firm level. That is, outsourcing was found to have impact on financial, innovation, employee and customer/supplier relations performance of the firm overall. As stated by literature, it is

possible that outsourcing has significant effects on individual functional areas in which it occurs. For instance, a firm's manufacturing operations may experience cost reductions as a result of outsourcing, or a firm may improve its customer service by shifting it to an outside specialist organization. Therefore, individual functional areas may experience performance improvements as a result of outsourcing. In our study, a firm-level performance impact of outsourcing is detected, leading to conclusion that the outsourcing intensity has low positive contribution to firm performance at the firm level.

On the other hand, generic firm strategies and environmental dynamism is found to moderate the relationship between outsourcing intensity and firm performance. Specifically, firms pursuing stronger cost leadership and focus strategies have more intense outsourcing relative to firms pursuing differentiation strategies. The finding that firms pursuing cost leadership strategies have more to gain from outsourcing is intuitively appealing. As predicted, by outsourcing tasks, cost leaders may be able to incrementally lower their costs, thereby improving their cost position relative to their industry rivals. The finding that firms pursuing focus strategies have more intense outsourcing and therefore more to gain from outsourcing is also interesting. Cost leadership for manufacturing strategy and focus strategy in the current study had a slightly lower contribution to outsourcing intensity levels. The finding that firms pursuing strongest cost leadership and focus strategies have more intense outsourcing relative to firms following other strategy types is contrary to prior research done by Giley (1997). Giley's results indicate that firms pursuing stronger differentiation strategies have higher outsourcing intensity levels relative to other strategy types. According to Giley's research, differentiators are more likely to outsource their firm activities than are cost leaders. In fact, Giley's finding was contrary to prior research on the strategy-internalization relationship. Specifically, Harrigan (1984) and Barney (1997) noted that differentiators should retain in-house those activities that add to the firm's level of differentiation. Therefore, differentiators would suppose to have less outsourcing intensity levels for their core business activities.

Environmental dynamism is found to have no significant effect on outsourcing intensity levels of firms. This finding is contrary to most of the prior research. For example, Harrigan (1983) found that stable environments are ideally suited for internalization of activities. Similiarly, D'Aveni and Ravenscraft (1994) argued that internalization is more effective in stable environments. Thus, firms should, theoratically, outsource more in environments that are more dynamic. Therefore, the finding in this research that environmental dynamism has no effect on outsourcing intensity levels of firms is a divergence from prior research.

This study employed the concept of 'Strategic Outsourcing' and by concerning strategic outsourcing, we considered firm performance effects of an organization's outsourcing decisions. In this context, firm performance effects include both the direct and the strategic effects. It is mentioned that more traditional approaches towards outsourcing have focused solely on the direct effect. Traditional approaches suggest that the production of goods or a servive should only be outsourced if this helps cutting costs, at least in the long run. Hence, their focus is only on the direct effect of outsourcing. In order to question strategic effects of outsourcing, we can also focus on modern approaches on strategy as well.

Today, if a decision or an action is considered as being 'strategic', this may mean that it involves the selection of an organization's goals, that it affects the organization beyond the short-run, that is taken rationally, weighing the costs and benefits of various alternatives, or that the rivals' actions and potential reactions are accounted for (Rumelt, Schendel & Teece, 1994). Modern views usually employ a concept of strategy based on modern game theory. In a game theoratic sense, a decision is strategic if that decision affects other players' decisions or actions and if the decision maker is aware of this interaction and takes it into account in the decision process (Baye, 2003).Consequently, game theorists distinguish between an action's direct effect and its strategic effect. The direct effect measures the immediate impact an action has on an organization's performance. Cutting costs for example, directly increases a company's profits (as long as everthing remains the same). The strategic effect is the impact that an action has on the rival's decisions, and thereby on the organization's

own performance. For example, cost cutting may not only have a direct effect on one's own profits, but it may also induce price changes, which may encourage rivals to change their prices as well, which then effects one's own profits again. This indirect chain of causation is what is called as 'strategic effect' according to game theorists. In our study, we questioned the firm performance levels of firms relative to similar firms in their industry but we have not questioned the strategic effect of outsourcing on rivals' behaviours. According to game theorists, if outsourcing decisions of firms affect the rivals' outsourcing decisions, we can speak of strategic outsourcing. Accordingly, outsourcing concept in our study is strategic in the sense that it questions organization's strategy, environment and performance in the long run.

After all, the conducted survey contains useful information with its indepth literature review about strategic outsourcing decisions and their impact on firm performance for the executives considering outsourcing as well as to the service providers who are considering relationships with firms planning to enter into the Turkish market. In fact, Turkey is at the epicenter of transport corridors connecting Europe to the Caucasus and Asia, as well as to the Middle East. This is important not only for Turkey's foreign trade relations and economic development but also for regional and interregional economic cooperation. In the aftermath of the cold war, Turkey has moved from the periphery of Europe to the edge of a new political and economic reality called Eurasia. This region, broadly defined as including Central Asia, the Caucasus and the Black Sea countries, attracts increasing attention not only because it constitutes one of the world's most potentially important energy-producing regions, but because it is also a crucial trade and transport corridor linking East and West. While there is still evidence that a high percentage of firms do not use outsourcing as a management tool in Turkey, the conducted survey shows that manufacturing and service industries in Turkey have potential for further development of the outsourcing sector. The vision of developing Turkey among top outsourcing destinations in the region will further enhance the use of the outsourcing service providers in the coming years. India is the major outsourcing destination, followed by China in the world. While India is significantly ahead, both destinations are regarded as having the right elements to provide good services – a sound but low-cost business environment, complemented by the availability of skilled labour.

Considering that Turkey has the similiar characteristics with its availability of low cost skilled labour and its location in the most desirable outsourcing region of Asia, Turkey is also a primary candidate to be listed among top outsourcing destinations in the world.

6.4 Implications

In our research, there is nothing totally new for business and management ideas. Supposedly, we have built our hypothesis on the belief that 'new ideas always consist of previously known components', and the basic intention in this research is to shape and recombine these business ideas to find new implications for researchers and policy makers – both in Turkey and abroad.

Using outsourcing for increasing organizational performance is not a new concept and the idea of strategic outsourcing is hardly new. But taken together, they represent a management approach that is quite unprecendented. Plenty of organizations outsource, but they typically do so for marginal or nonstrategic processes that do not matter to their business success, and plenty of those organizations are unaware of the performance implications of their outsourcing decisions. Only experienced companies know how to use outsourcing effectively and outsourcing providers know how to deliver sophisticated services effectively. The key idea in this research is to create awareness about 'strategic outsourcing' concept both for experienced and in-experienced companies in using outsourcing as a management tool and present them the findings about organizational performance implications of outsourcing strategies in Turkish companies.

6.4.1 Implications for Researchers

Most prior research has focused on outsourcing concept in isolation to examine its effects on performance outcomes of organization. In contrast, this study focus on the simultaneous pursuit of strategic outsourcing and organizational performance. Our baseline proposition is balancing strategic outsourcing decisions in the pursuit of proper firm strategies and environmental dynamism, which in turn contributes to overall firm performance. We derived a set of detailed hypothesis, and

tested them over 94 corporate firms operating in the manufacturing and service industries in Turkey. The research results support that firms pursuing more intense outsourcing strategies can experience significant positive performance effects.

While the sample in this research is representative of the population of 500 corporate firms list in Turkey, there is a need to test the theoratical model in other industry settings to establish the generalizability of our findings. In addition, future research should study time periods characterized by incremental firm performance effects and focus on outsourcing intensities of specific business functions and their performance effects. These effects would help in strengthening the external validity of the theoratical model developed and tested herein. In addition, the measure of outsourcing intensity provides a methodological contribution to researchers. More importantly, we hope that the literature review about the 'strategic outsourcing' subject to date and the findings in the emprical research create interest for researchers on this important pheonomenon.

The theoratical implications and contributions of the studies are significant across the conceptual, substantive, and methodological domains. The significant conceptual contribution of this study is the development of a theoratical framework for the strategic outsourcing of firm activities and their impact on firm performance. This is done by explicitly incorporating the benefits sought from outsourcing decisions and analysing firm's outsourcing intensities to explore firm performance levels. At a broader level, this study attempts to integrate generic firm strategies and environment effects to explain the effect of outsourcing on firm performance in the context of the transaction cost analysis literature, the core-competency argument-based literature and the literature on management. A second conceptual contribution of this study is the classicification sheme proposed for types of firm activities that can be performed within firms operating in any sector.

There are two significant methodological contributions of these studies. The measurement of outsourcing intensity and the core and non-core distinction made through exploring strategic significance of the activities and their contribution to competitive advantage of the firm have been a challenge for researchers. This

dissertation has drawn from the theoratical conceptualizations of these concepts to measure them explicitly by using multiple-item scales.

On the substantive domain, this study has extended the conceptual issue of strategic outsourcing to the area of manufacturing and service industries. At a broader level, the study have sought to explore the role of outsourcing in both industries.

6.4.2 Implications for Policy Makers

This study also provides some relevant managerial implications for policy makers. In particular, a policy maker in a managerial level frequently needs to determine the degree of vertical integration and the extent of strategic outsourcing simultaneously. Here, the challenge for policy makers is to balance this relationship to strive for superior firm performance. While finding the appropriate balance between outsourcing intensity of appropriate organization functions and measuring firm performance effects can be difficult, maintaining the right balance overtime can be even more challenging because the competitive landscape is often highly dynamic. We therefore suggest that matching the appropriate level of outsourcing intensity for a firm's selected functions with the industry environment and firm strategies is a dynamic firm capability to survive in rapidly changing business environments. Discovering and maintaining this balance between strategic outsourcing, environmental dynamism and firm strategy is a critical and challenging, but potentially rewarding task for managers in achieving superior firm performance.

7. LIMITATIONS AND RECOMMENDATIONS

This study has several limitations. First, the sample size of 94 corporate firms is too small to test the study's propositions with much power. Cohen's (1988) recommendation is to get approximately 180 responses in statistical power analysis for the behavioral sciences and 198 responses is needed for the moderator hypotheses. Further insight would likely be gained from such an increase in the sample size.

Second, the sample is drawn from two industries and the research is applied to 94 firms. Therefore, the generalizability of our findings are limited with these firms in two industries. Stage of industry development is another important factor, which has not been taken into consideration in our study. The impact of strategic outsourcing decisions on firm performance may be different for firms in introduction-stage industries or decline stage industries. Thus, the outsourcing behaviour of firms in either the youngest or the most mature industries should be studied as well.

Additionally, firm size may be an issue. It is conceivable that large firms outsource more activities. In the current study, the average firm size is greater than 500 employees. Thus, extremely large (like corporate firms in the current study) or extremely small firms may have may have determinants and performance implications of outsourcing that conflict with this study's findings. Another issue may be firm age. Young firms may be more willing to outsource some of their functions in the set-up period to control their overheads. In the current study, none of the firms in the sample were in the set-up period.

Finally, because most of the firms in the sample were manufacturers (64 firms), and service firms were less in number (30 firms), generalizing the findings of service firms may be inappropriate. It is possible that the pattern of outsourcing may be very different for service firms than it is for manufacturers, because service industries are characterized by less tangible outputs, simultaneous consumption and production, and so on (Boddewyn, Halbrich, & Perry,1986). Future research should attempt to gather outsourcing information from firms in introduction and decline-stage industries, those in different industries, and those with different firm age.

Another limitation concerns some of the measures in this study, which are perceptional. For those variables, it was rather impossible to obtain the actual data therefore subjective data was preferred. For example, objective measures of performance were not available for the majority of firms in the sample because they are privately held.

Future research should attempt to further develop the outsourcing intensity measure. Outsourcing intensity of an activity was measured by asking the outsourcing level of specific activity on a 6-point Likert scale. Altering this threshold may reveal other unique relationships like measuring outsourcing dichtomously where an activity is either provided on contractual basis or not.

Because outsourcing strategies and their perfpormance implications evolve over time, future research should also be directed toward collecting longitudial data. This is especially important for the relationship between outsourcing and firm performance. For example, in the past, one of the strongest arguments against outsourcing is that it transfers critical knowledge to supplier firms. This may take many years to develop and therefore examined more effectively through longitudial research.

The effect of outsourcing on the performance of firm's different functional areas should be examined as well. Although, firm level performance impact was found in this study it is quite likely that individual functional areas, like human resources and information systems functions in literature, that are outsourced see dramatic changes in their performance levels.

In addition, other variables that may have an impact on outsourcing strategies should be examined. Specifically, public and private firms' attitudes toward outsourcing may be different. Public firms may outsource to a greater extent than privately-held firms.

Soon, there will likely be new reasons why companies are looking to outsource, new types of outsourcing relationships, and new reasons why certain providers are chosen. Growth in global outsourcing will transform the countries'

workforce. Managers will need to have increased awareness of the client and the vendor employee groups about why and how cross-cultural differences in relationships, culture and attitude, and expectations affect work interactions and effectiveness. New research will be required to develop a framework for adoption of these policies, practices, and strategies for addressing these issues in order to maximize firm profits and future growth.

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APPENDICES

T.C
MARMARA ÜNİVERSİTESİ
SOSYAL BİLİMLER ENSTİTÜSÜ
İNGİLİZCE İŞLETME BÖLÜMÜ
DOKTORA PROGRAMI

Sayın İlgili;

İşletmelerin gittikçe artan ölçüde, sadece kendi faaliyet alanları içerisinde sahip oldukları yetenek ve becerileri esas alan işleri yapmak istemeleri ve bunlar dışındaki diğer işlerini organizasyon dışındaki başka işletmelerden almak eğilimi yaygın bir 'outsourcing – dış kaynaklardan yararlanma' uygulamasını ortaya çıkarmıştır. Yurdumuzda esasen yıllardır özelllikle inşaat sektöründe görülen 'taşeron kullanma' veya imalat konularında 'fason üretim' olarak bilinen işletmecilik uygulamaları birer 'outsourcing' örneğidir. İlişikteki ankette dış kaynak kullanımı ile ilgili sorular bulacaksınız. Bu anket dış kaynak kullanımının işletme performası üzerine etkilerini araştırmak amacıyla hazırlanmıştır.

Bu anket, ekonomik açıdan farklı bir sürecin içinde olan yurdumuzdaki işletmelerin dış kaynak kullanımdaki yaklaşımlarının ortaya konması ve işletme performanslarına etkilerinin incelenmesi ile outsourcing uygulamalarının daha iyi tanınmasını ve sağlıklı yerleşmesini sağlayacaktır.

Bu anketten elde edilen veriler Marmara Üniversitesi' nde yapılan bir doktora tezi için kullanılacak olup toplu halde değerlendirilecek ve firma bazındaki bilgiler kesinlikle gizli tutulacaktır. Araştırmaya ilişkin sonuçlar arzu ettikleri takdirde katılımcılar ile paylaşılacaktır.

Katıldığınız için teşekkürler.

Lütfen tablodan firmanızın hangi sektörde faaliyet gösterdiğini (x) ile işaretleyiniz.			
Ağaç – Orman	*Enerji*	*Otomotiv*	*Ambalaj*
Basın	*Bilişim*	*Gıda*	*İnşaat*
Kimya İlaç	*İçecek*	*Kuyumculuk*	*Cam-Seramik*
Lastik	*Perakende*	*Plastik*	*Reklamcılık*
Tekstil	*Telekom*	*Çimento*	*Madencilik*
Ticaret- Hizmet	*Demir-Çelik*	*Makine*	*Turizm*
Elektrik – Elektronik	*Metal*	*Tütün*	*Beyaz Eşya*
Mobilya	*Sağlık*	*Medya*	*Diğer*

Cinsiyetiniz:	*Kadın*	*Erkek*
Yaşınız:		
Eğitim Seviyeniz:	*Lise*	*Üniversite*
	Yüksek Lisans	*Doktora*
Kaç yıldır bu firmada çalışıyorsunuz?		
Kaç yıldır bu sektörde çalışıyorsunuz?		

Aşağıda sıralanan iş süreçlerini gerçekleştirmek için '*dış kaynaklardan*' ne kadar yararlanıyorsunuz?						***İŞ SÜREÇLERİ***	Aşağıda sıralanan iş süreçleri karlılığınızı arttırmaya katkıda bulunarak, rakiplerinize karşı sürdürülebilir rekabet üstünlüğü ve üstün performans sağlamada ne kadar önemlidir?					
Hiç Yararlanmıyoruz					**Tamamen Yararlanıyoruz**		**Hiç Önemli Değil**					**Kesinlikle Önemli**
1	**2**	**3**	**4**	**5**	**6**		**1**	**2**	**3**	**4**	**5**	**6**
						1) Muhasebe Kayıtlarının Tutulması (Faturalama, Borç ve Alacak İşlemleri, Sipariş Alma, vb.)						
						2) Satın Alma, İthalat-İhracat, Nakit ve Kredi İşlemleri, Hazine Operasyonları						
						3) Veri İşleme ve Yönetimi						
						4) Yasal ve Yönetimsel Raporlama						
						5) İşgörenlerin Ücretlendirilmesi ve Bordro Faaliyetleri						
						6) İşgörenlere Yapılan Ayni Yardımlar						
						7) İşgören Seçme						
						8) Personel Araştırmaları						
						9) Geçici İşgören Tedariki						
						10) İşgören Eğitimi (Fonksiyonel Eğitimler)						
						11) İşgören Eğitimi (Yönetici ve Liderlik Programları)						
						12) Bina Bakımı ve Temizliği						
						13) Fotokopi						
						14) Ofis Yönetimi (Ofis Malzemeleri Tedariki, Dağıtımı)						
						15) Posta Odası, Muhaberat (Taşıma, Saklama, Arşiv vb.)						
						16) Ofis Tasarımı ve Dekorasyonu						
						17) Personelin Yemek ve Servis Hizmetleri						
						18) Reklam ve Tutundurma Faaliyetleri						

Aşağıda sıralanan iş süreçlerini gerçekleştirmek için '*dış kaynaklardan*' ne kadar yararlanıyorsunuz?						***İŞ SÜREÇLERİ***	**Aşağıda sıralanan iş süreçleri karlılığınızı arttırmaya katkıda bulunarak, rakiplerinize karşı sürdürülebilir rekabet üstünlüğü ve üstün performans sağlamada ne kadar önemlidir?**					
Hiç Yararlanmıyoruz					**Tamamen Yararlanıyoruz**		**Hiç Önemli Değil**					**Kesinlikle Önemli**
1	**2**	**3**	**4**	**5**	**6**		**1**	**2**	**3**	**4**	**5**	**6**
						19) Müşteri İlişkileri Yönetimi						
						20) Çağrı Merkezi Operasyonları						
						21) Halkla İlişkiler						
						22) Toptan Pazarlama Faaliyetleri						
						23) Perakende Pazarlama Faaliyetleri						
						24) Pazar Araştırmaları						
						25) İçe Yönelik Lojistik (Girdilerin Temini, Depolaması, Stok Yönetimi, Fiziki Dağıtımı)						
						26) Dışa Yönelik Lojistik (Ürünlerin Müşteriye Fiziki Dağıtımı)						
						27) Ofis / İşletme İçi Dağıtım, Ulaşım						
						28) Ürün / Parça Tasarımı						
						29) Ürün ve Süreç Geliştirmeye Yönelik Araştırma / Geliştirme						
						30) Ürün Montajı, Paketleme, Kalite Kontrol						
						31) Veri Merkezi Yönetimi						
						32) Altyapı Yönetimi						
						33) Sunucu ve Veri Depolama Yönetimi						
						34) Yardım / Hizmet Masası						
						35) PC Tedariki ve Bakimi						
						36) Uygulama Yazılımı Yönetimi / Bakımı						

Geçmişteki 12 aylık dönemi göz önünde bulundurarak, aşağıda sıralanan *'örgütsel performans göstergelerinizi'* rakiplerinizle kıyaslayarak değerlendiriniz.	**Rakiplerimize kıyasla çok düşük**	**Rakiplerimize kıyasla oldukça düşük**	**Rakiplerimize kıyasla düşük**	**Rakiplerimize kıyasla çok az düşük**	**Rakiplerimize kıyasla düşük değil**	**Rakiplerimize kıyasla kesinlikle düşük değil**
1) Satışlardaki Büyüme						
2) Varlıklardaki Büyüme						
3) Faaliyet Karındaki Büyüme						
4) Satışların Geri Dönüş Oranı (Dönem Net Karı / Toplam Satışlar)						
5) Varlıkların Geri Dönüş Oranı (Dönem Net Karı / Toplam Varlıklar)						
6) Genel Finansal Performans						
7) Ürün / Süreç Geliştirme Kapsamında Harcanan Araştırma ve Geliştirme Giderleri						
8) Ürün Geliştirmeye Yönelik Buluşçuluk Faaliyetleri						
9) Süreç Geliştirmeye Yönelik Buluşçuluk Faaliyetleri						
10) Çalışan Devir Hızı						
11) Çalışan Sayısındaki Büyüme						
12) Çalışanların Motivasyonu						
13) Çalışanların İş Tatmini						
14) Müşteri İlişkileri Gücü						
15) Tedarikçi İlişkileri Gücü						

Lütfen aşağıda sıralanan stratejik faaliyetleri ne derece kullandığınızı kutucukları işaretleyerek belirtiniz.	**Hiç kullanmıyoruz**	**Çok az kullanıyoruz**	**Az kullanıyoruz**	**Oldukça kullanıyoruz**	**Çok kullanıyoruz**	**Tamamen kullanıyoruz**
1) Müşterilerimizin değişik beklentilerini karşılamak amacıyla ürünlerimizi rakip ürünlerden farklılaştırmaya çalışırız.						
2) Yeni ürün geliştirme faaliyetlerine önem veririz.						
3) Rakiplerimize teknik üstünlükler sağlamak amacıyla ürünlerimizde ek donanımlar geliştirriz.						
4) Ürünlerimiz için yüksek fiyatlar ödemeye hazır müşteriler yaratmaya çalışırız.						
5) Sık sık reklam kampanyaları düzenleriz.						
6)Pazardaki tüm müşteriler bizim için hedef müşteridir.						
7)Ürünlerimizin müşterilerimiz tarafından benzersiz olarak algılanmasına çalışırız.						
8) Ürünlerimizin marka bilinirliğine karşılık yüksek fiyatlandırma politikaları uygularız.						
9) Ürünlerimizin teknolojik özelliklerine karşılık yüksek fiyatlandırma politikaları uygularız.						
10) Faaliyet gösterdiğimiz sektörde firmamızın teknoloji lideri olarak algılanmasına çalısırız.						
11) Ürünlerimizin müşterilerimiz tarafından algılanan kalitesi rakiplerimize kıyasla yüksektir.						
12) Geniş bayi teşkilatı ile faaliyet gösteririz.						
13) Yaygın ve gelişmiş müşteri hizmetleri faaliyetlerimiz vardır.						
14) Müşteri segmentasyonu yaparak belirli müşteri gruplarına ulaşmaya çalışırız.						
15) Maliyetlerin minumuma indirilmesi her zaman ana hedefimizdir.						
16) Maliyetlerimizi düşürmek amacıyla ürünlerimizi standartlaştırırız.						
17) Sık sık fiyatlandırma politikamızı gözden geçirir, kampanyalar düzenleriz.						
18) Reklam bütçemizi asgari düzeyde hazırlarız.						
19)Çok sıkı maliyet kontrol mekanizmalarımız vardır.						
20) Ürünlerimiz seri üretime yönelik tasarlanmıştır.						
21) Lojistik faaliyetlerimiz düşük maliyetlidir.						
22) Büyük boyutlarda müşteri hesapları ile çalışmaktan sakınırız.						
23) Yeni ürün ve süreç geliştirmeye yönelik araştırma ve geliştirme bütçemizi asgari düzeyde hazırlarız.						
24) Müşteri hizmetleri maliyetlerimizi asgari düzeyde tutmaya çalışırız.						
25) Bayi yönetimi alanında maliyetlerimizi asgari düzeyde tutmaya çalışırız.						

Aşağıda işletmelerde dış kaynaklardan yararlanma tekniğinin tercih edildiği durumlarda beklenen faydalara ilişkin örnekler sıralanmıştır. İşletmenizdeki dış kaynaklardan yararlanma uygulamalarını düşündüğünüzde lütfen aşağıdaki örneklerden her birine ne derece katıldığınızı belirtiniz.						
Dış Kaynak Kullanımı;	**Hiç katılmıyorum**	**Çok az katılıyorum**	**Az katılıyorum**	**Oldukça katılıyorum**	**Çok katılıyorum**	**Tamamen katılıyorum**
1) Ana faaliyet alanlarımıza odaklanarak işletmemizin temel yeteneklerini geliştirmemizi sağlar.						
2) Değişen teknolojiye, yeni ürün ve servislere olan taleplere ve çevre koşullarına uyum için organizasyonel esneklik kazanmamızı sağlar.						
3) Örgüt yapımızda arzu edilen organizasyon değişikliklerini yapmamızı sağlar.						
4) Ürün / Servis değerlerimizi arttırmaya yardımcı olur.						
5) Müşteri tatminimizi arttırmada rol oynar.						
6) Hissedarlarımızın değerini arttırmada rol oynar.						
7) Artan kalite, üretimde verimlilik ve karlılık ile operasyonel performansımızı arttırmamıza yardımcı olur.						
8) Gelişmiş teknolojilere bilgi birikimimizi arttırmak ve yeteneklerimizi geliştirmek suretiyle sahip olmamızı saplar.						
9) Risk yönetimi uygulamalarımızı geliştirmemize yardımcı olur.						
10) Yaratıcı fikirler üretmemize katkıda bulunarak işletmemizde buluşçuluk yeteneklerimizi geliştirmemize katkı sağlar.						
11) Kendi konularında uzmanlaşmış tedarikçi firmalarla işbirliği yapmamızı sağlayarak firma imajımızı arttırmamızı sağlar.						
12) Varlıklarımızı tedarikçi firmalara transfer etmek suretiyle işletmemize nakit yaratmamızı sağlar.						
13) Yatırımlarımzı azaltmamızı ve kaynaklarımızı başka alanlarda kullanmamızı sağlayarak varlık yönetimimizi geliştirmemizi sağlar.						
14)Tedarikçi firmalar aracılığıyla yeni pazarlar ve iş fırsatları yakalamamıza ve pazar payımızı arttırmamıza yardımcı olur.						
15) Üretim ve satış kapasitemizi arttırmada kaynak sıkıntısı yaşadığımız durumlarda tedarikçi firmalar ile işbirliği yaparak kapasite arttırımına gitmemizi sağlar.						
16) Tedarikçi firmaların düşük maliyet yapıları ile maliyet yapımızı değiştirmede esneklik kazanmamızı sağlar.						
17) Çalışanlarımıza ana faaliyet alanlarımızla ilgili olmayan iş süreçlerimizde daha iyi kariyer fırsatları sunmamızı sağlar.						

Aşağıda işletmenizin faaliyet gösterdiği sektördeki çevre koşullarını tanımlayabilecek maddeler sıralanmıştır. Lütfen işletmenizin faaliyet gösterdiği sektördeki çevre koşullarını değerlendiriniz.

Faaliyet gösterdiğimiz sektörde;	**Hiç katılmıyorum**	**Çok az katılıyorum**	**Az katılıyorum**	**Oldukça katılıyorum**	**Çok katılıyorum**	**Tamamen katılıyorum**
1) Pazarlama ve Satış Yönetimi ile ilgili stratejilerimizi sıklıkla gözden geçirmek gerekir.						
2) Mamül hayat eğrisi kısadır.						
3) Rakiplerimizin stratejilerini tahmin etmek güç değildir.						
4) Müşteri taleplerini ve ihtiyaçlarını tahmin etmek güç değildir.						
5) Üretim teknolojisi sürekli değişim içerisindedir.						
6) Değişen teknoloji uygulamalarını takip etmek güç değildir.						
7) Müşteri talepleri ve firmaların pazar payları sürekli değişim içerisindedir.						
8) Fiyat rekabeti ciddi bir tehdit oluşturur.						
9) Devlet müdahaleleri ciddi bir tehdit oluşturur.						
10) Nitelikli işgücü ve kaynakların kısıtlı olması ciddi bir tehdit unsurudur.						
11) Müşterilerin satınalma alışkanlıkları sürekli değişim içerisindedir.						