

Do outsourcing and non-outsourcing New Zealand SMEs perform and perceive international outsourcing differently?

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Abstract

International outsourcing of goods and services has become an integral part of the value chain of many firms. However, most outsourcing research relates to MNEs, with little emphasis on SMEs. This study aims to address this significant gap in research by focussing on international outsourcing perception and performance differences between outsourcing and non-outsourcing manufacturing SMEs in New Zealand. Based on a sample of 74 New Zealand SMEs within the manufacturing sector, the findings suggest that SMEs engaged in international outsourcing perform significantly better than non-outsourcing SMEs. Both outsourcing and non-outsourcing SMEs have similar perceptions regarding outsourcing challenges. However, the former perceive outsourcing benefits more favourably. The findings are discussed in the light of resource based view and core competency theory of the firm.

Key words – Outsourcing, Performance, Small and medium enterprises, New Zealand

1. Introduction

International outsourcing of business activities is perceived to stay, grow and present challenges in the foreseeable future (Beaumont and Sohal, 2004; Chadee and Raman, 2009; Doh, 2005). Firms are disintegrating their low and high end manufacturing functions to reconfigure their value chain activities (Contractor et al., 2010). Declining trade barriers, rapid diffusion of information and communication technologies and enhanced management capabilities provide firms with opportunities to seek factors of production across the globe at competitive prices. Globalisation has provided an opportunity to arbitrage country differences (Mudambi and Venzin, 2010). Firms outsource internationally to seek cost reductions, access cheap labour, meet competitive pressures, and mimic industry practices for future growth (Lewin and Peeters, 2006). This enables firms to channelize their resources to their core competencies and source non-core value chain activities from vendors abroad (Prahalad and Hamel, 1990).

International outsourcing occurs when firms disaggregate some of their value chain activities to leverage the comparative advantage of geographical locations in order to complement their own resources and capabilities for achieving sustained competitiveness (Contractor et al., 2010). Outsourcing can be understood from location and control perspectives (Chadee and Raman, 2009). Firms sourcing value chain activities from locations other than the home country (location aspect) are engaged in offshoring and if these are sourced from third party providers and not firms' own affiliates (control aspect) then it is outsourcing. However, if firms are engaged in sourcing business activities from third party providers located abroad, it is called international outsourcing or offshore outsourcing – which is the focus of this paper.

Firms engaged in international outsourcing face additional set of international management and organisational challenges such as increased task complexities, interdependencies, hidden costs and institutional differences (Larsen et al., 2012). Thus, the need to study offshoring firms, in general. Further, SMEs need to be examined as 1) there is little research on SMEs & outsourcing; 2) SMEs constitute significant part of national economies; 3) face similar competitive pressures as that of MNEs; and 4) face additional challenges of knowledge and resource constraints. Though a good amount of literature has emerged on understanding offshoring firms, most of the current research focuses on multinationals, with little focus on SMEs (Carmel and Nicholson, 2005; Di Gregorio et al., 2009). Focus on MNEs is understandable, as they are bigger and more visible players in the global economy and their actions are likely to create or lose jobs based on their outsourcing decisions (Di Gregorio et al., 2009). However, SMEs also constitute a significant part of national economies and are not just engaged in domestic business. For instance, the share of SMEs in gross domestic product is about 50% for high income countries (Ayyagari et al., 2007). Firms from high income countries typically outsource to low or middle income countries. SMEs are also likely to engage in outsourcing as practiced by their larger counterparts as they face similar pressures to outsource from low cost destinations (Gupta et al., 2007). Moreover, SMEs face additional challenges of resource constraints and engaging in international outsourcing is likely to help channelizing limited resources to their core competencies.

Moreover, most studies on outsourcing performance, decision and reasons are from a US or European perspective, with a few studies from Australasia (Al-Qirim, 2003; Beaumont and Costa, 2002; Beaumont and Sohal, 2004; Fisher et al., 2008). Factors such as cost savings, focus on core capabilities and improved service quality emerged as the key drivers of information technology outsourcing in three Australian studies (Beaumont and Costa, 2002;

Beaumont and Sohal, 2004; Fisher et al., 2008). This is in alignment with studies conducted at other places. The focus of Australasian studies is on patterns of outsourcing and the electronic commerce issues of SMEs (Al-Qirim, 2003); reasons, impediments and outsourcing success factors (Beaumont and Costa, 2002; Beaumont and Sohal, 2004). Al-Qirim (2003) find that most of the information technology outsourcing in New Zealand is in maintenance and major concerns relate to the suppliers, such their selection and performance.

Though outsourcing is expected to add to firm performance, there is little and mixed evidence that outsourcing leads to better firm performance (Gilley and Rasheed, 2000; Gorg and Hanley, 2004; Massini et al., 2010; Mol, 2005). Outsourcing firms are likely to perform better than non-outsourcing firms as it enables them to leverage from global factors of production and thus save costs. Recent developments in globalisation and technologies have enabled firms to disintegrate their value chain activities: focus on core activities and outsource non-core activities to offshore locations. Thus, we expect that the SMEs which outsource some of their value chain activities and thus focus on their core activities and utilise their limited resources optimally are likely to perform better than non-outsourcing SMEs. Moreover, as firms engage in international outsourcing, managers face additional challenges and complexities which need to be managed for getting the expected outcomes (Larsen et al., 2012). The managers who achieve the expected outcomes are likely to perceive international outsourcing more favourably than others (Ocasio, 1997). Thus successful firms leverage from the available benefits and manage the outsourcing challenges at the same time. Accordingly, international outsourcing can be another tool in the hands of SMEs to utilise their limited resources and thus, enhance their performance.

As there is a limited research on international outsourcing from the perspective of SMEs who play a critical role in national economies and are not smaller versions of MNEs, this paper aims to address this important gap in research. The paper focuses on SMEs in the New Zealand manufacturing sector to investigate whether there are any differences between outsourcing and non-outsourcing firms in terms of firm performance and perceptions of international outsourcing factors. The paper does not aim to test the causality relationships because of the nature of data collected. However, based on findings of this study and the relevant theoretical literature, we intend to derive relationships between outsourcing decisions, perceptions, and firm performance.

The paper contributes to the outsourcing literature by providing evidence to what is known anecdotally; that significant differences exist between outsourcing and non-outsourcing SMEs in terms of performance, outsourcing motivators and firm characteristics such as size and age. This is one of the few studies focussing on outsourcing from SMEs' perspective. The paper argues that as SMEs face resource and knowledge constraints, international outsourcing could be one of the strategic tools available to enable focus on their core competencies and leverage globally available factors of production. The paper also calls for further research to establish the context in which international outsourcing could add to the performance of SMEs. As the study is based on a small sample size of New Zealand SMEs in the manufacturing sector, the findings are expected to be indicative only, calling for further research in the field.

2. Hypotheses development

Strategy, economics and international business theories shed light on outsourcing drivers and performance implications. As a firm's bundle of resources and capabilities enable it to earn above normal profits, gaps in capabilities can be filled by strategically outsourcing to acquire

the needed resources (Cheon et al., 1995). This makes outsourcing a strategy decision where a firm strategically rejects in-house production to acquire from outside vendors. Outsourcing is also an economic decision where potential transaction costs are compared with outsourcing benefits emerging from specialisation which are not always realisable (Coase, 1937; Williamson, 1989, 1991). Firms outsource to take benefits of disintegration, location and externalisation (Dunning, 2001; Kedia and Mukherjee, 2009). Firms disintegrate some value chain activities and source from outside vendors located at destinations with competitive factors of production. The convergence of wages of outsourcing locations, labour regulations, environmental standards and corporate codes of conduct provide some challenges to international business and management theory where firms can easily relocate operations and employment from place to place (Doh, 2005). Thus outsourcing entails both benefits and challenges to firms engaged in outsourcing to seek sustained performance.

2.1 Outsourcing and firm performance

Though outsourcing is believed to improve firm performance through specialisation, there is limited and mixed evidence on the impact of outsourcing on performance (Bertrand, 2011; Bryce and Useem, 1998; Gilley and Rasheed, 2000; Gorg and Hanley, 2004; Massini et al., 2010; Mol, 2005). Large US multinationals sustain their global profitability levels by strategically leveraging technology transfers and international outsourcing (Kotabe and Swan, 1994). International outsourcing leads to improved performance of firms by enabling firms to focus on their core competencies and sourcing supplementary goods or services from outside vendors (Kotabe et al., 1998). Gilley and Rasheed (2000) find no direct effect of outsourcing on firm performance and suspect that outsourcing benefits are overstated. However, they argue that the firm strategy and environment moderate the relationship between outsourcing and firm performance. Firms following cost leadership strategy in stable environments enjoyed better

performance by outsourcing some business activities. However, in a study of 200 manufacturing firms in the Netherlands, Mol, Tulder and Beije (2005) find no performance effects of international outsourcing. This may be due to dynamic environments and relatively higher transaction costs than production costs (Gilley and Rasheed, 2000; Mol et al., 2005; Williamson, 1989).

Performance effects also vary for firms, whether engaged in exporting or not – exporting firms enjoy positive effects of outsourcing on their performance as compared with non-exporting firms (Görg et al., 2008). Bertrand (2011), in a study of 2000 French MNEs finds that international outsourcing enhances the export performance of firms by reducing their costs, providing them with new resources and market knowledge and enhancing their flexibility. The knowledge of offshore markets helps reduce transaction costs and thus enhances the performance of exporters. International outsourcing enhances productivity by discharging operational tasks more efficiently (Beaumont and Sohal, 2004; Görg et al., 2008)

Most of the studies to date focus on outsourcing from the perspective of MNEs and only a handful of studies have focussed on outsourcing–performance relationships for small firms (Di Gregorio et al., 2009; Gorg and Hanley, 2004). In an analysis of the impact of outsourcing on the profitability of the electronics sector in Ireland, Gorg and Hanley (2004) find outsourcing of materials lead to higher profitability within larger plants. They did not find any effect of services outsourcing on the profitability of smaller plants. Larger firms gain more from outsourcing because of their relative higher bargaining power, lower transaction costs and higher knowledge base than their smaller counterparts (Gorg and Hanley, 2004). But on the other hand, small firms that are more entrepreneurial and resource constrained might see outsourcing as a tool to overcome their constraints. The findings of a SME study in the US

suggest that international outsourcing of services by SMEs leads to greater extent and scope of internationalisation of sales (Di Gregorio et al., 2009).

Despite limited and mixed evidence of the impact of outsourcing on firm performance, it is widely believed that outsourcing leads to improved firm performance. We expect that SMEs engaged in international outsourcing perform better than those not outsourcing. By outsourcing some of their business activities, SMEs are likely to save costs and focus on their core areas and competencies (Fisher et al., 2008; Prahalad and Hamel, 1990). As SMEs face resource constraints, international outsourcing might enable them to channelize their limited resources. Moreover, contacts in overseas markets are likely to provide access to those markets and thus firms are able to overcome the limitation of small domestic market size which is often cited as a key reason for early internationalisation (Freeman and Cavusgil, 2007). Hence the following hypothesis:

Hypothesis 1: Outsourcing SMEs are likely to perform better than non-outsourcing SMEs.

2.2 Outsourcing factors

International outsourcing is a strategic decision where a firm rejects internal production of some value chain activities and source it from outside vendors located abroad. The outsourcing factors can be understood in terms of drivers of and barriers to international outsourcing decisions. The literature suggests factors such as access to cheap capital, cost savings, competitive pressures and access to competitive factors of production and industry practice as the key motivations to outsource (Lewin and Peeters, 2006). Similarly, outsourcing also entails challenges such as hidden costs, vendors becoming competitors, vendor inefficiencies and relationship management with the vendors (Barthelemy, 2001; Levina and Ross, 2003; Rao et al., 2006).

Firms outsource for strategic, financial, environmental and technological reasons (Chadee and Raman, 2009). Focussing on core competencies, deploying scarce resources strategically, sharing business risks and the existence of competitive pressures motivate firms to outsource (Lewin and Peeters, 2006; McFarlan and Nolan, 1995; Quelin and Duhamel, 2003; Quinn, 2000). However, there is also a likelihood of being locked into strategic dependency with the vendors (Quelin and Duhamel, 2003). Financial factors, including cost savings, are also well advocated in the literature (Lacity and Willcocks, 1996; Lewin and Peeters, 2006). When making outsourcing decisions, firms need to be careful of hidden costs that may not be immediately apparent. However, some studies (Espino-Rodríguez and Gil-Padilla, 2005; Loebbecke and Huyskens, 2006) found no empirical evidence for the impact of cost savings on outsourcing decisions. In a recent study, Massini, et al. (2010) establish a 'U' shape relationship with cost saving and outsourcing. They argue that cost savings, after declining at a certain stage of outsourcing, start rising again once firms develop capabilities and strategies to manage outsourcing. Environmental factors such as imitative behaviour (Loh and Venkatraman, 1992) and the internal business environment also influence outsourcing decisions. The technological reasons to outsource include internal IT failures, the availability of technical skills and technological infrastructure (Aubert et al., 2004; McFarlan and Nolan, 1995).

For the purpose of this study, we have grouped outsourcing factors (drivers and barriers) into four categories: strategic resources, strategic challenges, competitive pressures and home country job losses. Strategic resources and challenges include the key benefits and challenges at the firm level as highlighted in the extant literature. Competitive pressures factor relates to the extent of competition out in the external environment. Outsourcing has been widely

recognised as resulting in job losses in the home country, which is the fourth factor for this study. It is likely that the managers who perceive outsourcing as a strategic resource are likely to undertake outsourcing decisions. In other words, SMEs engaged in outsourcing are likely to perceive outsourcing as a strategic resource. This is according to the attention-based view of the firm, which states that managers' decisions depend on the issues on which they focus their attention (Ocasio, 1997). Moreover, the current research suggests that outsourcing enables firms to save costs, improve cash flows, and channelize the scarce resources to core competencies (Lewin and Peeters, 2006; Prahalad and Hamel, 1990). On the other hand, the literature also highlights strategic challenges firms face such as hidden costs (Larsen et al., 2012), supplier dependency (Quelin and Duhamel, 2003), and threat of losing critical business skills and quality. Similarly, other challenges such as the existence of competitive pressures and job losses in home countries are also a reality. Both outsourcing and non-outsourcing firms are likely to accept the existence of these challenges. Hence the following hypotheses:

Hypothesis 2: Outsourcing SMEs are likely to perceive outsourcing as a strategic resource more favourably than non-outsourcing SMEs.

Hypothesis 3: Both outsourcing and non-outsourcing SMEs are likely to equally recognise outsourcing challenges such as strategic challenges, competitive pressures and home country job losses.

The study also investigates whether outsourcing and non-outsourcing SMEs differ in their characteristics, such as size and age. We do not hypothesise size, age and outsourcing decision associations. As these are the most commonly used control variable in business studies, we intend to explore whether any such differences exist between outsourcing and non-outsourcing SMEs.

3. Methods

The scant literature on international outsourcing from an SME perspective provides impetus to this research. The key question this paper intends to answer is whether there are any differences in performance and perceptions for outsourcing factors between outsourcing and non-outsourcing SMEs in New Zealand. As there is little and mixed evidence for the impact of outsourcing decisions on firm performance, we attempt to investigate this empirically within a New Zealand setting.

3.1 Context of the study

New Zealand is a small developed geographically isolated economy with a sizeable number of SMEs. New Zealand SMEs are relatively small and constitute a significant part of the economy. According to the New Zealand Ministry of Economic Development (MED, 2010), SMEs account for 97% of all the firms, 31% of the total employment and a significant proportion of the country's GDP. Over 99% of them are domestically owned and face challenges of high mortality rates, resource constraints and relatively small firm size. Global recession has impacted New Zealand SMEs. This is evidenced by more number of enterprise deaths than births for the first time in 2009 since 2001. Moreover, the percentage of high growth enterprises, defined as firms with 10 or more employees having average annual sales growth rate of 20% or more, has declined since 2008. More than 40% of SMEs reported decrease in profitability while about 30% reported increase in profitability in 2009 as compared to the last year. New Zealand SMEs also face challenges of lack of human and social capital, strategy planning and implementation, and financial resources (Horsley and Ahmed, 2011).

3.2 Data

In order to achieve the study objectives an industry-wide web questionnaire survey of SMEs in the manufacturing sector in New Zealand was undertaken. Kompass NZ was used to obtain the contact details of senior management teams and information on firm characteristics such as year of establishment, number of employees, ANZSIC codes and expected turnover. The 15-minute survey was pre-tested on a class of postgraduate international business students and minor adjustments were made as suggested by the pilot survey participants. The link to the questionnaire survey was emailed to 1500 manufacturing SMEs in New Zealand. We received 105 questionnaires in all. After deleting the incomplete questionnaires, the useable sample is reduced to 74 New Zealand SMEs in the manufacturing sector. During the survey, a 7-point magnitude earthquake struck Christchurch, New Zealand on September 4, 2010 (BBC, 2010) which we suspect was one of the reasons for the low response rate.

Table I shows sample characteristics as compared with the industry over two dimensions, namely size and age. As the sample did not contain any zero employee SMEs, the industry level data is also adjusted to exclude such SMEs. The sample distribution for size as measured by the number of employees is relatively similar to the country level distribution, with 47% of the sample being respondents from micro SMEs. More than half of the manufacturing SMEs are less than 10 years old, while about 50% of the sample firms are more than 20 years old. This indicates a higher proportion of older firms in the sample, as compared with the manufacturing sector in New Zealand.

Insert Table I about here

3.3 Measurement

A number of questions relating to performance, drivers, problems and challenges of outsourcing were asked to the respondents. The respondents were asked to rate these items on a five point scale ranging from 'strongly disagree' to 'strongly agree' and 'very dissatisfied' to

'very satisfied'. The items used in measuring the dependent and independent variables are summarised in Table II. The offshoring construct items are borrowed from the recent literature on factors influencing outsourcing decisions (Chadee and Raman, 2009). Performance is measured by commonly used performance items such as growth in sales, profits and overall business. The use of subjective measures of performance is well relied in the literature as it gives similar results as that of objective measures (Wall et al., 2004) To develop operational constructs for variables such as firm performance and outsourcing factors, an exploratory factor analysis (EFA) with varimax rotation using principal components is undertaken. The iterative process of EFA reduced the number of items used for factor constructions. For example, any item loading on more than one factor is removed to run EFA again. The constructs are finalised based on a scree test, the proportion of variance explained and interpretability criteria (Hatcher, 2009). This results in five constructs as shown in Table II.

All the factor constructs meet the reliability, convergent validity and unidimensionality criteria. None of the alpha values and item-to-total correlations is less than 0.70 and 0.50 respectively, except for the competitive pressures (COPR) construct. The relatively low alpha for COPR is also not a serious concern as alpha of 0.60 level can be used when constructs are not already well established (Hair et al., 2010). The questionnaire covers the commonly cited reasons influencing outsourcing decisions; however the grouping into relevant constructs is new and relevant for the current study. The five explanatory variables consist of firm performance over last 2–3 years (PERF), outsourcing factors i.e. strategic challenges (STCH), strategic resources (STRE), competitive pressures (COPR) and home country job losses (HCJL). A simple average of the factor items is undertaken to construct factor-based scales (Hatcher, 2009). This helps to explain the factors construct differences between outsourcing and non-outsourcing firms on a 5-point scale as in the original questionnaire.

Insert Table II about here

The independent variable ‘outsourcing decision’ (OSD) is a binary variable where 1 is ‘yes’ and 0 is ‘no’. SMEs are asked whether they are outsourcing any of their business activities abroad. Firm characteristics, namely ‘Size’ and ‘Age’ are measured by the number of employees and the number of years since establishment as at December 2010. Industry type as measured by standard industrial classification (SIC) codes is another commonly controlled variable. However, because of the relatively small sample size and a wide spread of sub-industries at 2 level ANZIC 2006, it is not practical to control for this in the present study – which we recognise as a limitation of the study. Information for both the predictor and criterion variables is collected from the same respondents in the questionnaire, thus the threat of common method bias exists (Podsakoff et al., 2003). However, since Harman’s single-factor test produced all the five factors, it can be safely assumed that the common method bias is not a major threat to our findings.

4. Results

As the independent variable (outsourcing decision) is of a dichotomous nature (yes/no) and the aim is to test performance and perception differences in outsourcing and non-outsourcing firms, independent t-tests available in Statistical Analysis System (SAS) are used for hypotheses testing (SAS, 2003). The independent t-tests are compare two means when they come from different groups, in this case outsourcing SMEs and non-outsourcing SMEs (Field and Miles, 2010).

Pairwise correlations and a summary of results are presented in Table III and Table IV, respectively. None of the pairwise correlations are significant and more than 0.60, leading us

to safely argue for an absence of multicollinearity (Gujarati, 1988). All of the 'Folded F' values are non-significant except for 'Age'. Folded F as produced by SAS, 2003, is equivalent to Leven's test to check for the homogeneity of variance assumption (Field and Miles, 2010). The non-significant 'Folded F' values imply that the assumption is satisfied for all the constructs except for the 'Age' construct. In the case where a homogeneity assumption is violated, Field and Miles (2010) suggest using a Satterthwaite corrected t-test (instead of the Pooled method) which we have used for the 'Age' construct. This implies that variances are roughly equal and the assumption of homogeneity of variance is met. Effect size 'r' is reported to demonstrate the effect size of the models.

Insert Table III and IV about here

On average, outsourcing SMEs ($M = 3.12$, $SE = 0.13$) are more satisfied with their performance than non-outsourcing SMEs ($M = 2.65$, $SE = 0.17$). This difference is significant, $t(72) = -2.18$, $p = 0.03$; and represents a medium sized effect $r = 0.25$. This implies that outsourcing and non-outsourcing SMEs differ significantly in performance, as measured by growth in sales, profits and overall business. In other words, outsourcing SMEs have significantly higher performance satisfaction than non-outsourcing SMEs. In addition, outsourcing SMEs ($M = 3.65$, $SE = 0.11$) perceive international outsourcing as a strategic resource more favourably than non-outsourcing SMEs ($M = 3.25$, $SE = 0.15$) with a medium sized effect $r = 0.25$. This implies that outsourcing SMEs perceive more benefits from international outsourcing than non-outsourcing SMEs and perform better. However, for other outsourcing factors, we did not find any significant differences in perceptions between outsourcing and non-outsourcing SMEs. It indicates that both outsourcing and non-outsourcing SMEs perceive international outsourcing as causing home country job losses and posing strategic challenges for them. Both outsourcing and non-outsourcing SMEs feel higher competitive pressures. This implies that both

outsourcing and non-outsourcing firms are equally aware of factors influencing outsourcing decisions but some of them still outsource while others do not.

Significant differences exist in firm characteristics, specifically the age of outsourcing and non-outsourcing firms. On average, outsourcing firms are relatively younger than non-outsourcing firms younger firms with a mean age of 22 years. This relates to the period when the New Zealand economy was opened up. Thus on average, SMEs that came into existence during the open economy regime tend to outsource internationally as compared with the ones existing before that. However, we did not find any differences in size between outsourcing and non-outsourcing SMEs.

5. Discussion

The results suggest that outsourcing SMEs perceive outsourcing as strategic resource more favourably than non-outsourcing SMEs. Moreover, they are significantly more satisfied with their performance than non-outsourcing SMEs. Both outsourcing and non-outsourcing SMEs have similar perceptions regarding strategic challenges, extent of competition, and job losses in the home country. Both outsourcing and non-outsourcing SMEs agree that outsourcing poses strategic challenges and job losses in the home country. They also agree for the existence of competitive pressures in the environment. Despite of their perceptual similarities for strategic challenges, home country job losses and competitive pressures, some SMEs outsource and others don't. Those who outsource are significantly more satisfied with their performance and perceive outsourcing as a strategic resource. Overall, the findings support all the hypotheses.

The finding of outsourcing firms performing significantly better than non-outsourcing firms aligns with the positive impact of outsourcing in achieving organisational outcomes by large

MNEs (Bertrand, 2011; Kotabe et al., 1998; Kotabe and Swan, 1994). Empirical evidence exists for outsourcing resulting in saving costs (Fisher et al., 2008; Massini et al., 2010) and improving productivity and profitability (Gorg and Hanley, 2004; Görg et al., 2008). Outsourcing is also found to create a prevalence of increased hidden costs (Barthelemy, 2001), and increased dependency on vendors (Quelin and Duhamel, 2003). This is also evidenced in the findings as both outsourcing and non-outsourcing SMEs agree with the challenges posed by international outsourcing and the existence of competitive pressures.

The differences in the benefits of outsourcing between outsourcing and non-outsourcing SMEs can be explained with an attention-based view of the firm (Ocasio, 1997). However, the causality is not clear in the current study – whether managers who give attention to the benefits of outsourcing tend to outsource or their outsourcing decision and experience leads them to perceive its higher benefits. It is interesting to note that both outsourcing and non-outsourcing SMEs perceive that international outsourcing is accompanied by its challenges and competitive pressures, but some still outsource and other do not. Challenges such as supplier dependency, hidden costs, fear of loss of quality and critical business skills and home country job losses are commonly cited in literature and the business press. Literature cites strategic challenges and resources as critical reasons to outsource offshore (Lewin and Peeters, 2006). As globalisation and free trade has caused increased competition and firms mimic industry trends (Loh and Venkatraman, 1992), it is natural for SMEs to outsource to locations with cheap labour in order to save costs and improve performance.

The findings of higher performance of outsourcing SMEs indicate that small firms can use outsourcing as a strategy to maintain and enhance their performance. This relates back to the theoretical logic behind international outsourcing. By outsourcing internationally, firms get

access to global resources at competitive rates and an opportunity to serve those markets (Dunning, 2001; Kedia and Mukherjee, 2009). Firms are likely to leverage locational advantages of competitive factors of production, specifically human resources available at other destinations (Dunning, 2001; Graf and Mudambi, 2005; Porter, 1990). Though SMEs are not smaller version of MNEs, they still face similar challenges of globalisation. However, they face additional challenges such as scarce resources and lack of market knowledge. Outsourcing some of the business activities is likely to allow limited resources to be deployed in other core areas. Thus international outsourcing of some business activities might be a strategic tool enabling SMEs to enhance their performance. In utilising globalisation opportunities, SMEs may use international outsourcing to overcome resource and size constraints and to access foreign markets. This might enable SMEs to redeploy their limited resources in core areas and outsource non-core activities to low-cost destinations abroad (Prahalad and Hamel, 1990). Outsourcing is a widely-practiced strategy where firms source some of their business activities elsewhere in order to maintain and enhance their competitiveness (Kotabe and Swan, 1994; Massini et al., 2010).

The clearly-defined performance differences between outsourcing and non-outsourcing SMEs is expected to ring bells with SMEs. It can be inferred that SMEs engaged in outsourcing are leveraging the benefits of specialisation and competitive factors of production available at other locations. This makes sense in light of the more open New Zealand economy and the prevalence of free trade agreements. For example, New Zealand has a free trade agreement with China and expects to save costs by manufacturing or sourcing, some goods from China and exporting from there, thus also mitigating the costs of geographic isolation. SMEs that are not outsourcing perceive fewer benefits from outsourcing and tend to produce everything domestically.

Conclusion, Implications and Limitations

The study focuses on investigating whether outsourcing and non-outsourcing SMEs differ in terms of performance, perceptions to outsourcing drivers and barriers and firm characteristics such as size and age. The findings support all the three hypotheses. Firstly, outsourcing SMEs perform significantly better than non-outsourcing SMEs. Secondly, outsourcing SMEs perceive higher benefits from outsourcing business activities offshore than non-outsourcing SMEs. Thirdly, both outsourcing and non-outsourcing SMEs have similar perceptions of the challenges posed by international outsourcing. This implies that although both outsourcing and non-outsourcing SMEs equally recognise outsourcing challenges, outsourcing SMEs still perceive the benefits and perform better than non-outsourcing SMEs. Lastly, outsourcing SMEs are relatively younger than non-outsourcing SMEs. However, they do not differ in terms of their size.

The study offers some important implications to SMEs and researchers. First, we provide evidence that outsourcing SMEs are more satisfied with their performance than non-outsourcing SMEs. It is widely accepted that SMEs face resource constraints. Thus, SMEs may use international outsourcing as a strategic tool to utilise their limited resources. By outsourcing their non-core activities, SMEs can leverage from their core competencies by channelizing the limited resources to the more important areas. Second, SMEs need to realize that though outsourcing poses challenges, yet it offers benefits too. Both outsourcing and non-outsourcing SMEs perceive that outsourcing poses challenges. Outsourcing SMEs see more benefits than non-outsourcing SMEs and they perform better. In the current business environment where international outsourcing has become a norm, the need is to manage outsourcing challenges and leverage from its benefits. Lastly, the findings are likely to provide initial food for thought

for researchers to examine further how SMEs can leverage more from international outsourcing.

The findings are useful as they provide initial evidence that SMEs can leverage international outsourcing to enhance their performance. This is one of the few studies focussing on relevance of outsourcing for SMEs. However, the findings should be considered as indicative only and may not be generalised, considering the limitations of the study such as small sample size and common method bias. The study contributes being exploratory in nature and the first of its kind in a New Zealand setting. The study also contributes by establishing empirically that SMEs engaged in international outsourcing perform significantly better than non-outsourcing SMEs. It also paves the way for more robust studies to explore outsourcing–performance relationships for SMEs, which is a neglected area of research so far. A critical research question for future research is to investigate the context in which SMEs can gain more from international outsourcing. Also, what exactly motivates SMEs to outsource and how much they gain or lose needs to be empirically investigated. A wider survey across industries and firm size (SMEs and MNEs) to explore the impact of outsourcing strategy of their performance is called for in order to understand international outsourcing implications.

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Table I Sample characteristics

	New Zealand %	Sample %
TYPE		
Micro (1-5 Employees)	74	47
Small (6 – 9 Employees)	15	20
Medium (10 – 19 Employees)	11	33
AGE		
1 – 5 years	37	3
6 – 10 years	22	14
11 – 20 years	23	34
> 20 years	18	49

Table II Operational measures of the exploratory variables (n = 74)

Factors Constructs	Reliability (Alpha)	Convergent validity (Item to total correlations)	Unidimensionality		
			Factor Loadings	% of Var. Explained	Cum. % of Var. Explained
<i>Performance (PERF)</i> Sales growth Profitability growth Overall business growth	0.91	0.79 0.79 0.87	83 83 91	1.08	1.08
<i>Strategic Resources (STRE)</i> Cost savings Improved cash flows Spare funds for investments Focus on core competencies	0.87	72 77 73 67	77 84 80 71	0.88	0.88
<i>Competitive Pressures (COPR)</i> Competition for access to cheap labour Lot of competitive pressures	0.62	0.46 0.46	55 64	0.25	1.13
<i>Strategic Challenges (STCH)</i> Loss of perceived quality Suppliers becoming competitors Supplier incapability Increased supplier dependency Hidden costs Loss of critical business skills	0.86	69 60 62 72 69 59	60 53 65 82 66 52	0.93	0.93
<i>Home Country Job Losses</i> Loss of jobs in the home country Feeling guilty for transferring jobs abroad	0.72	0.57 0.57	72 64	0.14	1.07

Table III Pairwise correlations (n = 74)

Variables	Mean	SD	PERF	STRE	STCH	COPR	HCJL	AGE	SIZE
PERF	2.97	0.92	1						
STRE	3.52	0.77	0.18 (0.12)	1					
STCH	3.58	0.71	-0.06 (0.62)	-0.18 (0.11)	1				
COPR	3.70	0.81	0.04 (0.71)	0.17 (0.15)	0.15 (0.21)	1			
HCJL	3.89	0.77	0.04 (0.73)	-0.14 (0.24)	0.55 (0.00)	0.13 (0.26)	1		
AGE	26.04	20.85	0.26 (0.02)	-0.09 (0.43)	-0.04 (0.74)	0.14 (0.24)	-0.06 (0.62)	1	
SIZE	8.72	5.64	0.06 (0.60)	-0.20 (0.09)	-0.08 (0.47)	0.03(0.77)	0.16 (0.17)	0.25 (0.04)	1

Note: Figures in parenthesis denote significance levels

Table IV Summary of results (n = 74)

Variable	Overall		Outsourcers			Non-Outsourcers			T Test			Effect Size (r)
	Mean	SD	Mean	SD	SE	Mean	SD	SE	df	tValue	Pr > t	
Performance	2.97	0.92	3.12	0.93	0.13	2.65	0.85	0.17	72	-2.09	0.04	0.24
Outsourcing factors												
Strategic Resource (STRE)	3.52	0.77	3.65	0.75	0.11	3.25	0.76	0.15	72	-2.18	0.03	0.25
Competitive Pressures (COMP)	3.70	0.81	3.78	0.78	0.11	3.56	0.87	0.18	72	-1.09	0.28	0.13
Strategic Challenges (STCH)	3.58	0.71	3.58	0.69	0.10	3.59	0.75	0.15	72	0.06	0.95	0.01
Home Country Job Losses (HCJL)	3.90	0.77	3.86	0.77	0.11	3.96	0.78	0.16	72	0.51	0.61	0.06
Firm Characteristics												
Firm Age	26.04	20.8	22.90	18.30	2.59	32.58	24.5	4.99	36	1.72	0.09	0.27
Firm Size	8.73	5.6	8.68	5.8	0.81	8.83	5.5	1.11	72	0.11	0.91	0.01

Notes:

1. SD stands for standard deviation and SE for standard error
2. Performance is measured on 5 point scale where 1 is very dissatisfied and 5 is very satisfied
3. Outsourcing factors are measured on 5 point scale where 1 is strongly disagree and 5 is strongly agree
4. Age is measures in 'number of years since establishment' as on 2010 and size by number of employees