

Externalising Services

Walking a Tightrope between Industrial
and Service Logics



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Industrial and Service Logics

Fredrik Nordin



STOCKHOLM SCHOOL
OF ECONOMICS
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To Bodil, Herman and Vera

Failure is in a sense, the highway to success, inasmuch as every discovery of what is false leads us to seek earnestly after what is true, and every fresh experience points out some form of error which we shall afterward carefully avoid.

John Keats

PREFACE

This report is submitted as a doctoral thesis at the Stockholm School of Economics. The research carried out forms part of the research programmes of Fenix and the Centre for Innovation and Operations Management at EFI, the Economic Research Institute at the Stockholm School of Economics.

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As usual, the author has been entirely free to conduct and present his research in his own way as an expression of his own ideas.

Stockholm, January, 2005.

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Fredrik Nordin

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CHAPTER ONE

Introduction

This thesis reports on several of the initiatives of one industrial firm (here called SysCo) to externalise the delivery of its basic product services which supplement the product offering to its customers; for example, installation, repair and training.

1.1 Prologue

"What you could help me with when I sit in anguish trying to make up my mind, which you do as a manager, concerns the issue of daring to take the step. What makes managers take the step and outsource a service?"

The citation above comes from a senior manager at SysCo's service organisation (henceforth called SysCo Services). SysCo is a leading multinational system provider at which the author of this thesis was employed during most of the research, and several years prior to it. During the study leading up to this thesis, mainly carried out between 2000 and 2003, SysCo reduced both its sales volumes and employee numbers dramatically. From the peak in 2000, sales and employee numbers decreased by more than 50% until 2003, just as they did at most of SysCo's competitors, due to a severe downturn in the industry. During the same period, product services¹ became a hot topic at SysCo, particularly the more advanced and customer-oriented services. Delivering services was seen as both a potential countermeasure to the downturn in the product business and a great opportunity.

Nevertheless, during the same period, many service processes were externalised and alliances with suppliers implemented, in particular with regard to the more basic services such as installation and repair, with the general purpose of increasing the efficiency and effectiveness of service operations. Initiatives were also undertaken to form alliances for the delivery of advanced and more customer-oriented services such as business solutions and operational services (see, for instance, Oliva & Kallenberg, 2003) in order to become more service-oriented and

¹ Services supplementing product offerings.

capable of meeting customers' changing needs, and thus differentiating itself from competitors and creating business growth.

However, many of the externalisation initiatives were problematic to carry out and many employees of SysCo Services perceived that they were counteracting the adoption of a more customer-oriented service logic at SysCo and the offering of advanced services such as solutions, full maintenance contracts, and operational services. The services covered by such a service logic, e.g. full maintenance contracts, professional services, and operational services, as well as combinations of such services, will mostly be referred to as "advanced services" in this thesis, whereas "basic services" will be used for services such as installation, repair, and training (cf. Oliva et al., 2003).²

1.2 Two paradoxical trends

For two diametrically-opposed reasons, product services are currently the object of increased attention among practitioners as well as researchers.

The *first* reason is that product services, for a few years now, have been seen as both an opportunity and a potential countermeasure for firms whose revenues from product sales are decreasing. Service businesses typically have higher margins. They can provide steadier revenue streams than product businesses, thus working as a potential counterbalance to volatility in revenues from manufacturing (e.g., Dennis, 2003, Quinn et al., 1990, Wise & Baumgartner, 1999). Many authors and many industrial firms have acknowledged this opportunity and have made services a key component of their business strategy (see, e.g., Sampson, 2000, Vandermerwe & Rada, 1988). Statistics also indicate that the change is real. For example, the business services' share of GDP in the United States has grown by 400% during the last four decades, while manufacturing has shrunk by about 40% (Davies et al., 2001). Additionally, Swedish statistics show that an increasing number of people are working with services (Öberg, 2003).

The *second* reason for the interest in services is that many firms have increased the externalisation of their services; not only manufacturing services, but increasingly also services such as design and consulting, as well as product services such as maintenance (Blumberg, 2003a). Furthermore, services are increasingly being sourced globally (Kotabe et al., 1998). More and more often, outsourcing contracts are going to low-wage countries such as India and some Eastern European nations, so called off-shoring. Reasons mentioned for the externalisation trend include faster technological development, more complex products based on several technologies, less continuous customer demand, more global competition, and a growing number of specialised and flexible outsourcing firms in the marketplace (Axelsson & Wynstra, 2002, p. 68).

² More information about different sorts of services can be found in section 1.6.1 and 2.3.1.

The move to services, or “the adoption of service logic”³, is intended to take the firm closer to the customer, while externalisation may increase the distance from the customer. One might question whether or not it is wise of industrial firms to use external resources for the delivery of product services, even in the case of the more basic ones (cf. Bettis et al., 1992), when they are also interested in creating growth by adopting service logic. On the other hand, it is sometimes argued that the externalisation of non-core areas is beneficial because it enables the firm to focus on its core areas (e.g., Kotabe & Murray, 2001, Quinn & Hilmer, 1994). The externalisation of basic services such as repair and installation is sometimes seen as a way of releasing resources for other more customer-oriented advanced services which are seen as more central to the way the firm competes and which will better be able to satisfy the overall needs of customers.

It might be expected that such externalisation projects will be problematic for reasons that are associated with this adoption (which the case stories in the next chapter will also illustrate). The reasons for such problems include the (perceived) risk that the relationship with the customer has deteriorated due to externalisation, which, rightly or wrongly, could lead to resistance on the part of the employees. It could also lead to problems regarding which supplier to contract. The perceived risk of losing the customer to the supplier can be expected to lead to problems during externalisation.

The present thesis explores problems during the externalisation of basic services at an industrial firm that is also adopting service logic.

Before the research is described in more detail, a glimpse of the studied externalisation projects is provided.

1.3 The studied externalisation projects

A sample of the studied externalisation projects is described below, acting as an introduction to the remainder of the thesis. The idea is that these authentic accounts taken from the empirical study of SysCo will make the issue of interest in this thesis somewhat more concrete. The accounts are also intended to function as an introduction to the subsequent theory chapters.⁴

The four accounts have been selected, from the different externalisation projects studied, as illustrations of the problems and challenges associated with the externalising of product services. The first three examples are about the contracting of an external supplier to deliver basic services that were previously

³ Here, adopting service logic means becoming more customer-oriented by introducing more comprehensive and customer-oriented services such as full maintenance contracts, business solutions, and managing customers' operations, instead of only more “basic services” such as repair and installation. See also sections 1.6.1 and 2.3.1.

⁴ These accounts can also be found in Paper V.

conducted in-house. The fourth one is about broadening the service offering by aligning with partners as a means of becoming more customer-oriented. Together, they illustrate some of the problems associated with the externalising of product services. They also represent the range of product services studied. More information about the empirical base of the study can be found in Chapter 4.

1.3.1 Externalising product training

In a pilot project conducted between 2001 and 2002, SysCo Services had an external training firm, based in the US, sell and deliver IT-related courses directly to its customers. The general purpose of the project was to learn about alliances, and to develop an alliance strategy. The specific purpose was for SysCo Services to reach new markets with its present services, increase its sales, and potentially also develop new services.

The externalisation project created much frustration and conflict at SysCo Services, which hampered its progress. One reason for the conflict was the different views held at SysCo Services, and whether or not it was wise to use external firms for these courses. Many employees saw externalisation as “foolish” and were of the opinion that IT training, instead, was an area where SysCo Services should further develop its own competence; thus internal support for externalisation at SysCo Services was very low. They thought that externalisation entailed a risk of losing IT competence, which they felt to be an area that was too close to SysCo’s core business. As a result, they thought that SysCo would lose business to its partner. Other employees saw it as an opportunity to access competence in the sale and supply of IT training.

The project also caused frustration among some of the customers, who had not been informed about the changes in advance. Some customers wondered whether or not SysCo had the necessary competence in-house, and this meant a risk of reduced credibility for SysCo.

The project was terminated after the initial pilot project. Although the official reason for this was the general downturn in the economy and the rather unlucky market conditions; the correctness of the externalisation is still being debated.

1.3.2 Externalising product installation

Another example is the installation of SysCo’s products. Around 2000, this was completely externalised to a global construction firm with its head office in Europe (henceforth called Global Service Corp), including the project management part. However, this did not turn out very successfully for several reasons.

First, Global Service Corp conducted very few installation projects because local SysCo employees deemed this more expensive than locally-sourced alternatives, preferring to collaborate with firms which they had already established bonds with.

Secondly, many local customers wanted to have installation firms from their own domestic market, with their own language and culture. Thus, neither the local customers nor the local employees of SysCo were committed to using Global Service Corp. *Finally*, some installation providers were not satisfied with merely conducting installation services on behalf of SysCo, and were increasingly offering supplementary services directly to the customers of SysCo, including different solutions and even management of the customers' operations. In other words, they were trying to climb the value chain towards more advanced and customer-oriented services just like SysCo. Building on their experience of conducting installation work and other operational services for SysCo, as well as for SysCo's competing System Providers, they were able to offer a complete bundle of services and solutions to their customers, with some customers actually contracting them to manage, for instance, their systems.

In view of the negative experiences arising from externalising installation work, SysCo Services' strategy changed. Instead of externalising installation completely, managed from SysCo's head office and including the operational parts as well as the project management part, installation resources would be sourced locally and project management kept at SysCo. Strong suppliers such as Global Service Corp would not be used at all.

1.3.3 Externalising hardware repair

Repair was gradually externalised to external service firms, starting in around 1997, with the purpose of decreasing costs and facilitating a focus on other areas. When a new repair re-structuring and externalisation project, initiated in 2003, had found a preferred supplier, which it wanted to contract for repair work in one or more of its regions, management suddenly halted the selection process and the second-choice supplier had to be contracted instead. The project had made its decision, based on the rigorous formal evaluation of several suppliers, but the managers of SysCo had gradually realised over the years that this specific supplier had become too strong. They were suddenly afraid that it would benefit too much from being awarded the repair contract. This specific supplier happened to be one of the suppliers that had also been contracted for installation services, for instance. The emerging awareness of this firm's ambitions to compete with SysCo led to a temporary halt to the project, and the selection of a less dangerous supplier.

1.3.4 Partnering for full-services

In around 2002, SysCo started to discuss partnering with firms that it believed could help it expand its service offering and cover a broader range of its customers' products. This, and an expansion into more advanced services such as solutions and taking over customers' operations, was seen as critical to SysCo's service business when many of the basic services had been externalised to specialised service firms for efficiency reasons. In spite of the terminology used by

SysCo Services, i.e. “partnering”, the partnering manager and other employees at SysCo Services said that SysCo should always face the customer in these alliances. Otherwise, he said, there would not be a deal with the supplier. In other words, they were determined to stay close to their customers by owning the contract and the relationship with the customer and by being the intermediary between the customer and the partners. The customer relationship was deemed too important to leave to, or share with, another firm.

However, the restrictions imposed by this strategy were gradually relaxed as SysCo realised that both the potential alliance partners and the customers had different opinions, and that there were also technological reasons for not always fronting the customer. Thus, the initially very firm statement about always fronting the customer in horizontal alliances was replaced by a pragmatic view where the preferred structure was dependent on each specific case, e.g. the customers’ wishes and the partners’ competence. Gradually, a more detailed partnering strategy was developed whereby the structural question of who would be closest to the customer was formulated for each of SysCo Services’ different service areas, e.g. Systems Integration, Installation, and Product Support. For example, when the external partner firm had expertise in one of the customer’s applications, e.g. Business Management Systems such as SAP, they realised that it would not typically be viable to have SysCo fronting the customer. SysCo did not have any core competence in this area, and neither did it have any history of delivering and supporting applications such as SAP vis-à-vis its customers.

Besides formulating a partnering and sourcing strategy, or rather guidelines for the make-or-buy decision for the different service areas, the prime contractor role was also developed. The Manager of SysCo Services explained:

“We will always be the prime contractor and retain the responsibility for services for products, from transmission up to the service-layer. Over and above that, we can let other firms handle things.”

A new organisational unit was also set up for centrally coordinating partnering and sourcing matters at SysCo Services.

1.3.5 Recurring problems and the focus of this thesis

The preceding stories provide a glimpse of a number of problems that were identified during the research which are associated with externalising the delivery of product services, problems which may also appear when other firms do the same thing.

The project concerning the externalisation of product training contained a lot of internal trouble, and the internal change process became a significant problem. The installation and full-service projects both indicate the importance of the relationship with the customer. The repair project indicates that “no alliance project is an island” (cf. Engwall, 2003) but needs to be linked to other alliances

and other services. These and other problems will be described and discussed in more detail in the remainder of this thesis. Generally speaking, the simultaneous adoption of service logic influenced the externalisation projects because it caused, for instance, resistance among the employees to allowing external firms to deliver services.

In this thesis, externalisation problems are explored and advice is given to managers responsible for such changes regarding the way in which the externalisation should be carried out. The thesis is primarily based on a longitudinal case study at the service organisation of an industrial firm in the high technology industry (SysCo), and has been reported upon in five papers, which are appended to this thesis. In particular, this thesis integrates the findings of these five papers, reports upon the problems encountered during the externalisation of product services, and discusses the underlying reasons for these problems. Externalising basic services such as repair and installation, while at the same time adopting a service logic that involves offering and delivering more customer-oriented and advanced services such as solutions, will lead to a number of important challenges that may lead to problems during the externalisation. These challenges, as well as examples of externalisation problems, will be described. Conclusions will also be drawn regarding how and why the context and the change-approach influence the process of externalising basic product services.

Before the purpose is formulated, some previous contributions central to the issue of interest in this thesis are reviewed in order to assess the current state of knowledge in the area.

1.4 Previous studies on the externalising of services

Knowledge gained through systematic research into the problems and challenges associated with the externalising of basic services in tandem with the adoption of service logic is limited, even though this could potentially be studied empirically. While it may be difficult to say a lot about the long-term effects, on welfare and employment for instance, of externalising basic services at this stage, it is easier to say something about the process of externalising basic services concurrently with service logic being adopted, including the problems associated with it. Nevertheless, only a very limited number of studies have focused specifically on this issue.

In fact, there are only a limited number of studies in each of the two separate areas (the externalisation of product services and the adoption of service logic), at least when studies focusing more narrowly on services such as logistics and helpdesks are excluded. The latter studies are excluded here since the focus of this thesis is product services that are more technological in nature and more closely related to central activities at industrial firms, e.g. R&D and manufacturing.

Because of the growing level of interest in services, among industrial firms too, it can be expected that extraordinary managerial efforts will be needed to manage the change process associated with externalising services at industrial firms when the firm is also trying to “climb the value chain” and adopt a more customer-oriented service logic that includes more advanced services.⁵

While much work has gone into describing the meaning of different sorts of services; there has recently been particular interest in services such as “complete solutions” and the like (e.g., Board, 2001, Brown, 2000, Davies et al., 2001, Galbraith, 2002, Miller et al., 2002, Sandberg, 2003); less has concentrated on the peculiarities and difficulties associated with the process⁶ of externalising services. No previous empirical studies were found which explicitly address how the adoption of a service logic whereby more complete and advanced services are delivered affects the process of externalising basic services. Furthermore, while much work has gone into service management and service operations in general (e.g., Blumberg, 1991, Fitzsimmons & Fitzsimmons, 2000, Heskett et al., 1990, Hope & Mühlemann, 1997, Johnston & Clark, 2001, Normann, 2000, Van Looy et al., 1998), less has focused explicitly on product services at industrial firms (Armistead and Clark (1991, 1992) and Mathe and Shapiro (1993) being notable exceptions). There is also some important published work on *buying business services* (e.g., Axelsson et al., 2002, Fitzsimmons et al., 1998), which broadly covers the area, providing an excellent and more general overview of the field, but a little too general to be called the research frontier of the topic of the externalisation of product services and containing little advice concerning the change process associated with externalising product services.

Given this lack of studies focusing on the particular issue of interest in this thesis (i.e. the simultaneous adoption of service logic and the externalisation of basic services), further investigation of the topic might be justified. There are, however, two studies which are closely associated with the issue. Both of them deal, to some extent, with the change process associated with the externalising of services while service logic is being adopted. Thus, they can be seen as representatives of the discourse and knowledge to which this thesis intends to contribute.

⁵ As an employee of SysCo for more than ten years, and as a member of several service externalisation projects, e.g. the externalisation of repair and logistics functions, I experienced at close hand some of the problems associated with the externalising of services. This triggered my research interest of focusing on this change process.

⁶ “Process” refers to how things are done rather than what is done (Schein, 1987), to the interrelated activities, or behaviours of individuals, extended in time (Stymne, 1970), or to a “collection of tasks and activities that together – and only together – transform inputs into outputs” (Garvin, 1998). In this thesis, the term refers to the way in which the externalisation process is carried out, i.e. the change approach.

The first study was carried out by **O'Farrell and Wood (1999)**, and primarily focuses on *strategic alliances* for the delivery of business services.⁷ Nevertheless, since it provides interesting ideas that are presumably also of relevance to the area of externalising services into more operational alliances, it is seen here as a central contribution to that area. More specifically, the authors claim that most previous literature on alliances has a manufacturing perspective and that there is a need to incorporate the role of alliance clients into the alliance literature. As they put it, "business service SAs require client sanction". Furthermore, the authors also say that one difference between service alliances and manufacturing alliances is that it is easier to define the scope of a manufacturing alliance, typically in terms of a physical output, than to define the scope of a service alliance. This study indicates a challenge for externalisation projects that may potentially lead to problems if not handled properly. The authors draw on their previous articles on business services and emphasise that business service firms must work closely with client staff in joint production relationships and that the quality of many business services depends not only upon the performance of the supplier, but also on how well the customer performs in interaction with the supplier.

Another stream of research focuses on the *outsourcing* of services. In this research stream, the *second* study of interest can be found, written by **Allen and Chandrashekar (2000)**. This theoretical study describes what service outsourcing means and how the outsourcing relationship can be managed. The authors emphasise, among other things, the need to start outsourcing on the basis of clear goals and expectations and to choose suppliers which have both technically and managerially competent suppliers. The importance of a sufficiently clear, but also flexible, contract is emphasised, and justified by the difficulty of predicting future events in services. One potential problem emphasised is the risk of negative feelings among internal employees as a result of outsourcing. One way of counteracting this is to define core competencies clearly and to document the reasons for outsourcing, as well as involving employees in the formulation of the outsourcing strategy. According to the authors, negotiations and supplier assessments should preferably be handled by a central function within the organisation.

Concerning the articles summarised above, a few observations can be made. For example, O'Farrell and Wood emphasise the need to take the relationship with the customer into account during the externalisation of services, as this may be critical to the success of the alliance. Their study is, however, just like most of the others

⁷ O'Farrell and Wood write about Strategic Alliances (SAs), but their definition of an SA is relatively vague - "an agreement between autonomous firms to collaborate in future in pursuit of mutually beneficial goals. The agreement may be formal or informal but a key element is the intention to maintain the alliance, although it may be terminated at any time". Thus, the interpretation is that the findings of the article are also valid for the externalisation projects of interest in this thesis (O'Farrell et al., 1999).

reviewed, theoretical. The article by Allen and Chandrachekar suggests a linear model wherein clear goals are set early on during the externalisation process. It also addresses the potential internal problems associated with externalisation. Furthermore, none of the reviewed studies explicitly addresses the relationship between the adoption of service logic and how the process of externalising services should be carried out. Neither do the authors account for any empirical evidence leading to their advice. Moreover, they do not explicitly address the issue of externalising basic services simultaneous to service logic being adopted, although they do touch on the issue indirectly. The present study addresses this more explicitly.

In the next chapter, the overall purposes of this study are formulated.

1.5 Purposes

This thesis is concerned with two simultaneous and intentional changes; the externalisation of basic services and the adoption of a service logic that involves the offering and delivering of more advanced and customer-oriented services. The main issue of interest in this study is problems encountered during such externalisation projects which are being carried out while service logic is being adopted at the same firm. How the adoption of service logic influences the externalisation and how the externalisation of product services can be managed when service logic is also being adopted are issues that have been largely neglected by previous empirical research. Thus, the main purpose of this thesis is;

P1: to explore problems, as well as their sources, associated with the externalising of basic services at an industrial firm while service logic is simultaneously being adopted.

A more practitioner-oriented purpose is also stated:

P2: to suggest how externalisation should be carried out in order that externalisation problems may be moderated.

1.6 Some central definitions and delimitations

1.6.1 Services

This thesis focuses on **product services**, which can be defined as “the set of all potential additional services a supplier can supplement his product offering with, in order to differentiate his offering relative to the competitors’ as perceived by (potential) customers and distributors” (Frambach et al., 1997). This includes, for instance, installation, after-sales service, and training services (Mathieu, 2001a). Customer service, after-sales service, and maintenance are similar terms (although after-sales service excludes services rendered before and during sales). Product services can be contrasted with “pure services”, which are services that are marketed in their own right without necessarily being associated with a physical product (Hutt & Speh, 2004, pp. 328-329). Closely related terms are customer

support, product support, technical support and service (Goffin & New, 2001), and industrial services (Johansson, 2003). Product services can be divided into *basic* and *advanced* services, where the former include installation, repair, and training while the latter include professional services, maintenance services, and operational services (Oliva et al., 2003). For more details, see Section 2.3.1 on page 2.

Furthermore, in this thesis, the term **service logic** is used. In this thesis, developing a service logic within the organisation broadly means that customers' needs and wishes are increasingly seen as business opportunities, in contrast to, for instance, the "industrial logic" where cost minimisation is the focus (Kingman-Brundage et al., 1995). This means collaborating with and learning from customers and being adaptive to their individual and dynamic needs (Vargo & Lusch, 2004).⁸ Here, the term service logic refers to a situation where a firm not only delivers *basic* services, such as repair and installation, but also the more comprehensive and customer-oriented *advanced* services, such as business solutions and full maintenance contracts (Oliva et al., 2003) which cover support for a greater share of the customers' product portfolio and a greater share of the customers' needs. While basic services are product-oriented and focus on single service transactions, advanced services focus on improving the customers' processes or creating longer lasting relationships with them. **Adoption of service logic** is another expression used, with adoption here meaning to "take up and practice or use". In this thesis, the term adoption is used to emphasise "the necessity of adaptation, not just deployment or adherence to a plan" and "the lack of end point" (Åhlström, 1997, p. 12).

1.6.2 Externalising and related terms

Alliance is a generic term that has many alternative interpretations, and several synonyms. In this thesis, the term is broadly defined as "a long-term relationship between two firms falling somewhere between market and hierarchy". This is intentionally a loose definition because examining differences between different sorts of alliances is not the focus of the thesis. The intention is rather to seek commonalities for the different sorts of alliances being implemented. However, one noteworthy empirical delimitation of the present study is that it primarily focuses on non-equity alliances, i.e. contractual agreements without equity sharing. This means that equity-based alliances such as Joint Ventures, i.e. alliances involving joint ownership, are largely excluded from the research. This is an important delimitation since the risks that are of interest in this study (e.g. the risk of losing the values related to having the customer relationship) are seen as more evident in non-equity based alliances. In equity-based alliances, the risk is lower because of the joint ownership. Another delimitation worth noting is that the

⁸ Vargo and Lusch use the concept "service-centered logic".

alliances studied here are mostly fairly operational in character, with a focus on reducing costs and improving efficiency and effectiveness, rather than, for example, dramatically improving or changing the firm's competitive position through the development of new technology, new products, and/or new markets. The latter type of alliance is often called "strategic" (see, for instance, Hellman et al., 1993)

This thesis explores several initiatives to externalise the delivery of basic product services to suppliers and partners. Here, the term **externalising services** means turning over to external suppliers the delivery of services required by the customers. The externalisation results in alliances between the buyers and sellers of services. The externalisation can be; (1) a means of vertically disintegrating an activity, or (2) an alternative to vertical integration (cf. Barthélemy, 2003), although the empirical base of this study is mainly (but not only) constituted by the first type. Furthermore, the conceptions "implementing a service alliance", "implementing a service supply relationship", and "outsourcing services" are all closely related and used, for instance, in some of the articles. In this thesis, the main focus is on the transfer stage, or the stage where the decision to externalise services is implemented.

Implementation traditionally means "putting into practical effect; carrying out". In this thesis, the term "implementation" refers to the process of progressing, not necessarily linearly, from an exploration stage, where the discussions and negotiations are about to start, to an operational alliance. Using Ford's terminology for buyer-seller relationships, the stages studied in this thesis primarily correspond to the exploratory and developing stages, i.e. the stages before the stable stage where routine has been achieved and after the pre-relationship stage where the negotiation is yet to start (Ford et al., 1998). In this thesis, implementation is not seen as a sequential process, following on from and shaped by strategy formulation. The term is used more broadly here, being seen as a complex and iterative process with overlapping stages where strategy is formed, to some extent, in parallel with the implementation.

1.7 Preview of the thesis

This thesis consists of five original publications with an integrated synthesis, discussion, and extension. Here, the latter is called the thesis. I am the principal author of four of the original publications. When the thesis goes to print, two of them will have been accepted for publication in journals, while the rest will have been accepted for review in journals. Previous versions of all the papers have been presented at refereed international conferences (see the details in the footnotes).

The remainder of this thesis is organised as follows. In Chapter 2, a broader review of previous research associated with the issue of interest is presented. Chapter 3

contains the theoretical frame of reference. The frame of reference is summarised in a research model used when interpreting the empirical data. This is followed by the methodology in Chapter 4 and a summary of the papers in Chapter 5. Chapter 5 concludes with a summary of the identified externalisation problems. In Chapter 6, the empirical results are discussed. More specifically, the externalisation problems are first synthesised and then the impact on the problems associated with the change context and the change approach is discussed, in line with the research model. Chapter 7 contains a summary of the contribution and implications. At the end of the thesis, the five papers are appended in full, see the summary in the table below.

Several externalisation problems have been identified and the contextual features and change approach that seem to influence them are described. Lessons concerning how the change process should be carried out are also provided.

Table I. Papers included in the thesis

Paper	Title	Comment
Paper I	Implementing service supply relationships (Co-authored with Pär Åhlström) ⁹	This paper will be revised and submitted for a second review in <i>Journal of Purchasing and Supply Management</i> . ¹⁰
Paper II:	Identifying Intraorganisational and Interorganisational Alliance Conflicts	Accepted for publication in <i>Industrial Marketing Management</i> . ¹¹
Paper III	Managing the challenges of adopting service logic in collaboration with suppliers	Published in the <i>Journal of Change Management</i> , Vol. 4, No. 4, 2004. ¹²
Paper IV	Searching for the optimum product service distribution channel	Under review in the <i>International Journal of Physical Distribution and Logistics Management</i> . ¹³
Paper V	Managing the challenges of outsourcing services	Under review in the <i>International Journal of Service Industry Management</i> . ¹⁴

⁹ For this paper, I had the main responsibility for collecting and analysing the data, and for the literature review. I also wrote much of the text in the article, as input for Pär who was responsible for compiling the complete paper.

¹⁰ An earlier version of this paper was presented at the 8th International Annual Conference of EurOMA held in Bath, UK, June 3-5, 2001 (Åhlström & Nordin, 2001).

¹¹ An earlier version of this paper was presented at the 12th Annual IPSERA Conference in Budapest, Hungary, April 14-16, 2003 (Nordin, 2003).

¹² An earlier version of this paper was presented at the 11th Annual International EurOMA Conference 2004, Fontainebleau, France, June 27-30 (Nordin, 2004a).

¹³ An earlier version of this paper was presented at the British Academy of Management Annual Conference, St. Andrews, UK, Aug 30-Sept 1 (Nordin, 2004c).

¹⁴ An earlier version of this paper was presented at the British Academy of Management Annual Conference, St. Andrews, UK, Aug 30 - Sept 1 (Nordin, 2004b).

CHAPTER TWO

Theoretical Background

The main idea of this chapter is to review theories associated with the studied phenomena, and to provide an overview of results and conclusions closely related to the research issue of this study. The review serves as a broad basis for the research question and the research model presented in the next chapter.

2.1 Introduction

This chapter is divided into three sections which review studies associated with (1) managing change, (2) adopting service logic, and (3) externalising services.

The review is selective and focuses on literature that is relevant to the issue of interest in this thesis. This chapter provides a starting point for identifying challenges and problems associated with externalising basic product services and simultaneously adopting service logic, and for developing a frame of reference that is presented in the next chapter. It concludes with a discussion about the differences and potential challenges of adopting service logic and simultaneously externalising services, as an introduction to the research model and research question presented in the following chapter.

2.2 Managing change

Two generic approaches to managing change are *top-down* and *bottom-up*. Central management drives a top-down approach. The reason for using this approach is often the belief that major changes cannot be managed by employees on the lower levels of the organisation because of their narrower perspective, their lack of resources, and their lack of political power to bring about system-wide changes (Conger, 2000). The second approach is based on the perspective that modern organisations are so complex and sophisticated that it is impossible for a small group of top leaders to grasp all the knowledge needed to reach decisions about

and implement the necessary changes. Instead, a distributed leadership is needed where the diverse voices from within the organisation are consciously used (Bennis, 2000). Although these perspectives might seem completely different at first sight, they are not. The top-down approach, as described by Conger, also acknowledges the need to involve lower levels of the organisation. The advantage of the top-down approach lies in senior managers' ability to implement changes that cross organisational borders within the organisation, due to their position. However, the bottom-up approaches more strongly emphasise the need to change the values of the organisation rather than just driving change from the top and, to some extent, involving junior managers. It is a matter of having willing and committed followers.

Service organisations may be particularly sensitive to the type of change employed, because of the nature of service organisations, with their competence located close to the customer in the service delivery organisations and the best understanding of customer needs often located far from top-management. To succeed in bringing about change, an alliance between the top and the bottom of the organisation may be needed, whereby the knowledge of the customer-interfacing employees in the service organisation, for instance, is exploited while a course is set at the top. Dunphy, for example, suggests an approach to change which is both top-down and bottom-up, and which can solve the paradox of the need for strong leadership with regard to difficult strategic decisions and the need to make decisions close to the customer. Strategy must be formed on the basis of the knowledge possessed by the employees of the organisation and on the broader perspective of management. Particularly during turbulent times, management must gather knowledge from employees and others relating to changes as well as other aspects of the context (Dunphy, 2000).

Another important aspect concerns whether the change is systematically *planned* in detail before being implemented, or if it is *evolving and emergent*. For example, Ghoshal and Bartlett (2000) claim that successful change requires the internal performance of each individual unit involved to be improved before any synergies can be achieved on an overall level. According to them, the transformation process must be divided into the stages of; (1) rationalisation — strengthening the individual units, (2) revitalisation — linking individual units and searching for synergies and economies of scale, and (3) regeneration — ensuring continuous learning and maintaining momentum during the change process. Weick (2000), on the other hand, emphasises that change should be emergent in the parts of the organisation where knowledge and the operational business are occurring. Strategy implementation should be replaced by strategy making. The benefits of emergent change are its sensitivity to local contingencies and its suitability for experimentation and learning. However, it may also be slow and less well-suited to responding to threats rather than to opportunities, and less well-suited to firm-level change rather than to operational change. Emergent change whereby the strategy

takes shape over time is similar to the adaptive strategy mode described by Mintzberg (1978). In the adaptive mode, strategy is formed over time in an emergent and complex process containing many decision-makers and conflicting goals. This mode prevents control but fosters learning. The strategy planning mode is based on the often false assumptions of full information and a stable environment, leading to the conclusion that strategy formation is rather a learning process that is modified en route. Stating a strategy explicitly may sometimes be risky since it prevents those involved from learning and adapting to their environment.

According to Quinn (1999), there is evidence that a formal systems-planning approach cannot handle the implementation of a strategic change process by itself. Besides the hard data decisions that dominate the literature, a number of soft change factors must be taken in account when implementing strategies, e.g. external relations, organizational structure, and management style. These factors are difficult to handle using formal planning models alone. However, formal planning is not just bad since it encourages long-time perspectives and facilitates evaluation of plans. It is not possible to combine all simultaneous strategic decisions into one single matrix in order to achieve an optimised solution, for cognitive and timing reasons.

2.2.1 Critical perspectives on research into managing change

Managing change is a complex matter, but, according to Collins (1998), most literature on change management is simplified, e.g. it neglects contextual factors. In spite of the fact that people and organisations often know what to do, often nothing happens. Implementing alliances is one example that many practical cases and researchers point out as being difficult, e.g. Boddy and colleagues (2000) who contend that we know very little about the practical implementation and management of alliances. Similarly, the outsourcing literature generally views implementation as unproblematic, Wasner (1999) being a notable exception. Moreover, the advice of consultants is seldom implemented; the problem being one of implementation rather than strategy (Pfeffer & Sutton, 1999).

Kanter (1983) calls large functionally-differentiated organisations, with complex hierarchies and departmental subcultures, “segmentalist” organisations. These organisations are often resistant to change due to institutionalised behaviour (Hannan & Freeman, 1984). Coordination between departments within organisations very often involves organisational politics and power struggles (Gandz & Murray, 1980), and the more complex the organisation - the more political things will probably be.

Several authors have tried to describe the ideal change process using a number of steps to be taken when implementing change, so called N-step guides (Collins, 1998). N-step change models can at best be used as guidance for the change agent,

although they are seldom sufficient for the complex and political reality that major changes imply (Buchanan & Badham, 1999). Collins (as do many others) contends that these models are generally too simplified to be of very much use in reality, neglecting contextual factors, the need for active management, and the ability to play the political game and deal with complexity and contradiction. Also, project management models generally assume that there will be linearity in the change, forgetting the negative reactions of people, e.g. resentment. Organisational development models, on the other hand, rely on involvement, consensus and alignment, and restraining the use of creativity and flexibility (Buchanan et al., 1999). Participative change models such as the OD models often work poorly in situations where there are many conflicting wills (Reason, 1984).

Instead of following a generic “off-the-shelf” recipe for change, a successful change approach (e.g. top-down or bottom-up, revolution or evolution, participative or directive) should be adjusted to the change context, i.e. the organisational features pertinent to a change situation. The features to consider before and during any change initiatives at an organisation include (1) time; how quickly is change needed? (2) scope; breadth and depth of change, e.g. realignment or transformation¹⁵, (3) preservation; assets, characteristics, and practices to be maintained and protected, (4) diversity within the organisation in terms of values, norms and attitudes, (5) capability; organisational, managerial, and personal ability to implement change, (6) capacity; cash, people and time available for the change, (7) readiness for change; aware and motivated employees? and (8) power; latitude of unit needing to change and of the change leader (Balogun et al., 2004, Hope Hailey & Balogun, 2002).

2.2.2 Factors hindering change

There are several potential reasons why an intended change may be difficult to implement, and an emerging body of research is focusing on the reasons for such difficulties.

Based on research at several large firms, Beer and Eisenstat (2000) have suggested six core reasons (“killers”) for failing to implement strategy: (1) ineffective senior management teams, (2) unclear strategies and conflicting priorities, (3) a top-down *laissez-faire* senior management style, (4) poor vertical communication, (5) poor co-ordination across businesses or borders, (6) inadequate down-the-line leadership skills and development. Reasons 1-3 are about “quality of direction”, reason 4 is about “quality of learning”, and reasons 5 and 6 are about “quality of implementation”. Together, these “killers” create a vicious circle which blocks strategy implementation and learning.

¹⁵ Realignment means changing the way of doing things but does not involve a fundamental reappraisal of the central assumptions and beliefs of the organisation. Transformation means a fundamental change within the organisation requiring a shift in strategy, structure, systems, processes, and culture. (Balogun & Hope Hailey, 2004, p. 20).

Resistance to change within organisations, as well as the reasons for this resistance, is the focus of an article by Ford and colleagues (2002). Their literature overview suggests that resistance occurs because; (1) it threatens the status quo, (2) it increases fear and anxiety regarding real or imagined consequences, (3) it threatens the way people make sense of the world, (4) people hold previous resentment towards those leading the change, (5) people have different understandings or assessments of the situation, and (6) people are protecting established social relations that are perceived to be under threat. According to the authors, change and resistance to it are a function of the socially constructed reality. The type of resistance is dependent on the type of reality that people construct. Background conversations, or implicit unspoken “backgrounds” for the “foreground conversations”, can be seen as a contextual factor for change resulting from the experiences and traditions of those involved in the change. Three generic resistance-promoting backgrounds are suggested: complacent (“nothing new or different is needed”), resigned (“this probably won’t work either”), and cynical (“this is just more of the same old stuff”). One way of dealing with these backgrounds is reinvention, or undoing what is and creating something new.

Kothandaraman and Wilson (2000) have suggested a research framework for the implementation of a relationship strategy which is related to adopting service logic. According to them, successful implementation requires broad involvement in the internal organisation. In general, the literature on relationship marketing treats the internal organisation and its individuals as black boxes. They argue that internal factors can affect the outcome of the implementation. For example, they mention the following potential hindrances to implementation: (1) the refusal of functional departments to coordinate effectively in order to deliver the goods, resulting in poor performance that can potentially ruin the relationship, (2) conflicts in inter-functional relationships, (3) the orientation of managers based on arms’-length type relationships. The authors suggest the following model for the effects of intra-organisational (internal) factors on the inter-organisational (external) factors leading to relationship performance. Internal factors, or managers’ “alignment with the relationship paradigm, ARP” are attitudes towards cooperation, trust, and interdependence. External factors, or “relational behaviour”, are flexibility, information exchange, and solidarity. Internal moderators are resource dependence, domain similarity, and reward structure. External moderators are dependence structures and transaction-specific investments.

Finally, Szamosi and Duxbury’s (2002) research suggests that; (1) inadequate communication and participation (e.g. not asking employees if there are better ways of doing things), and (2) bureaucratic resistance and favouritism (e.g. allowing departments to protect themselves from change) result in by an organisation that does not support change.

2.3 Adopting service logic at industrial firms

Adopting service logic means starting to see the customers' needs and wishes as business opportunities, in contrast to, for instance, the "industrial logic" where cost minimisation is the focus (Kingman-Brundage et al., 1995). A firm that has adopted service logic typically sees the repeat business of satisfied customers as the key to long-term revenue and profitability, and the customer is treated both as an asset to be nurtured and as a partner. Employees are not just seen as error-prone cost generators who need to be supervised. They are instead seen as important and knowledgeable resources possessing experience that can be used to improve the business. It is not only salespeople who are seen as valuable, but also the employees working at the support interface, for instance.

Although there is no clear distinction between services and products, several authors have previously described the differences between services and products. Cooper and Jackson (1988), for instance, summarise the more commonly recognised characteristics as; (1) the *intangibility*; meaning that they cannot be felt, tasted, or touched in the same way as goods can, (2) the *inseparability*; meaning that production and consumption are simultaneous and force the buyer to be in intimate contact with the production process, (3) the *heterogeneity*; entailing a potentially high variability in the performance of services, in particular as regards people-based services, and (4) the *perishability*; meaning that services, in particular professional services (Bowen et al., 1989), cannot be stored. Intangibility implies perishability while simultaneity implies heterogeneity. Others (e.g., Sampson, 2000) emphasise that all services act on something which is provided by the customer, i.e. that service supply chains are *bidirectional*. In service businesses, customers are also suppliers and there is a *customer-supplier duality*. In the repair case, the customer provides a broken television set.

Many industrial firms try to exploit the opportunities of service logic by adding services as a key component of their business strategy and by moving from manufacturing physical goods to delivering services. One of the first to predict this change was Theodore Levitt who described how manufacturing firms should integrate services into their offerings and focus on nurturing their customer relationships (1983), recommending a production-line approach to services (1972). This change has later been designated "servitisation" (Vandermerwe et al., 1988), "going downstream" (Wise et al., 1999), or "servification" (Normann, 2001), and basically means that service management is positioned as a strategic opportunity (Dennis, 2003).

According to Christian Grönroos, the focus on services is increasing partly due to customers' increasing need for comfort, industrial firms' intentions to increase the value of their customer offerings, and technological developments (for example IT) facilitating the creation of services, e.g. through the Internet. Others claim that there is an increasing dependence on the sourcing of technologies from several

suppliers (Karlsson, 2003) and an increasing number of technologies per product (Howells, 1999). This increases the technological complexity for many industrial customers, leading many of them to look for integrated single-source services, or integrated solutions (Davies et al., 2001), which can make their day-to-day business operations easier (Blumberg, 1991). From a buyer's perspective, by purchasing more comprehensive service packages where, for instance, one single supplier takes over the management of the customer's operations or assumes responsibility for a broader range of services and products, the buyer can simplify its operations, and perhaps also reduce its costs (Miller et al., 2002). For the supplier, offering a higher level of services than competitors is a way of differentiating (Desmet et al., 2003). Since the copying of services is often easy for competitors to do (Vandermerwe, 2000), merely offering basic services is often not enough and better ways of creating value for the customer must be sought. On a more general level, it is now generally recognised that services can provide organisations with important competitive advantages and that the level of customer services strongly influences the customer's choice of supplier (see, for instance, Grönroos, 2000, Lambert et al., 1998, Vandermerwe et al., 1988).

Thus, service offerings are increasingly of a more customer-oriented, comprehensive, and tailored nature, sometimes designated "integrated solutions" (Davies et al., 2001, Wise et al., 1999), "customer solutions" (Sandberg, 2003, Vandermerwe, 1996), "turnkey solutions" (Frambach et al., 1997), "advanced services" (Oliva et al., 2003), or "full-services" (Stremersch et al., 2001). According to Wise and Baumgartner, "integrated solutions" entail products and services being combined into seamless offerings. A "customer solution" is an integrated offering characterised by customisation (i.e. based on the unique requirements of each customer) and typically, but not necessarily, co-creation (i.e. co-developed with the customer) (Sandberg, 2003). According to Frambach and colleagues (1997), industrial customers increasingly want turnkey solutions instead of products that partially solve their needs. This means suppliers having to offer tangible products augmented with product services. Finally, "full service" is defined as "comprehensive bundles of products and/or services that fully satisfy the needs and wants of a customer related to a specific event or problem" (Stremersch et al., 2001).

Moreover, the closer relationship between buyer and seller that is typically rendered possible by being a full-service, solutions or systems provider (Gadde & Jellbo, 2001) often leads to a number of strategic advantages. The advantages are related, for example, to faster innovation and learning in direct interaction with the customer (Gupta & Wilemon, 1990, Prahalad & Ramaswamy, 2000, Von Hippel, 1988) and better control of the actual service delivery. Another advantage for organisations located downstream or close to the customers, e.g. full-service providers or consultants, is that they typically have a relatively good understanding of the customers and their needs (Storer et al., 2002).

Examples of firms for which success has been reported after turning to services include SKF (Vandermerwe, 1993), ABB (Desmet et al., 2003, pp. 47-49), and Nokia (Foote et al., 2001), while, according to Foote and colleagues, Hewlett-Packard and Rank Xerox have had significant trouble (Foote et al., 2001), and Intel and Boeing have been less fortunate and returned to their focus on the product business (Sawhney et al., 2004). Perhaps the best-known example of a firm that has successfully transformed itself from a product-oriented firm into a full-service provider is IBM (Mills, 1996). IBM also provides full-services on products which it has neither manufactured nor sold (Mathieu, 2001b).

The focus of this thesis is industrial firms that are trying to expand their service offering from basic services to advanced services, e.g. solutions and full-maintenance contracts (Oliva et al., 2003). This is defined in the next section by means of introducing four basic transitions.

2.3.1 Transitions during the adoption of service logic

Adopting a service logic broadly means that customers' needs and wishes are seen as business opportunities, in contrast to, for instance, the "industrial logic" where cost minimisation is the focus (Kingman-Brundage et al., 1995). Adopting service logic, or a service management perspective, changes the focus of organisations in several ways. Grönroos (2000, p. 196) summarises the changed perspective using four points: (1) from product-based value to total value in the customer relationship, (2) from short-term transactions to long-term relationships, (3) from core product (goods or services) quality to total customer perceived quality in enduring customer relationships, and (4) from the production of technical solutions as the key process to developing total perceived quality and value as key processes.

The change associated with adopting service logic at industrial firms can also be described as a number of basic transitions between "service spaces", which is what Oliva and Kallenberg, for instance, do when they describe three transitions (2003). The last two transitions are not necessarily sequential.

- T1. Entrance onto the service market of the delivered goods (Oliva et al., 2003). This is the first basic step when service logic is adopted and typically means starting to offer and deliver basic services
- T2. From product-oriented services to the end-user's process-oriented services, (Oliva et al., 2003) or from a service supporting the customer's product to a service supporting his actions (Mathieu, 2001a). Product-oriented services are, for instance, maintenance services. Process-oriented services are professional services and operational services such as managing operations. As the service provider moves along this dimension, the product becomes part of the offering as opposed to being the centre of the value proposition (Oliva et al., 2003)

T3. From transaction-based services to relationship-based services. Transaction-based services include basic services such as documentation, repairs/spares, upgrades/updates. Relationship-based services include maintenance services such as preventive maintenance and spare-parts management, for which a fixed price is typically paid, covering all services over an agreed period (Oliva et al., 2003)

These transitions are illustrated in Figure 1. The different sorts of services are called “Basic Services” (service space A), “Professional Services” (B), “Maintenance Services” (C), and “Operational Services” (D) by Oliva and Kallenberg, the last three categories of which are also called “advanced services”. In this thesis, the term “advanced services” also refers to complete bundles of services from all the service spaces.

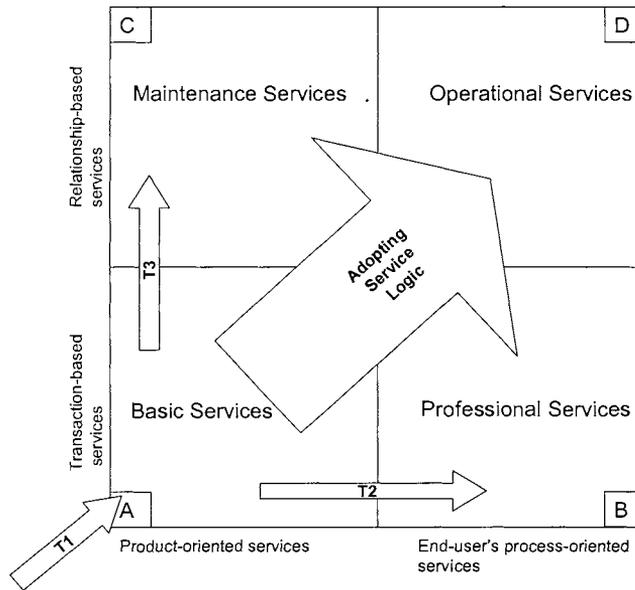


Figure 1. Transitions during the adoption of service logic (based on Oliva and Kallenberg (2003)).

With their position relatively close to the customer, firms that have adopted service logic and undergone transitions T2 and T3 can typically act as intermediaries between the customer and the suppliers of products and more basic services. Being an intermediary is typically associated with more power and opportunities to influence the design of the delivery system (Light, 1986, Stern & Weitz, 1997).

Furthermore, adopting a service logic in line with Figure 1, or adopting a full-service or solutions strategy, is typically interrelated with a number of strategic changes on the supply side of firms (Gadde & Snehota, 2000). Examples include

the externalisation of non-critical activities and the establishment of close relationships with suppliers (Gadde & Håkansson, 2001), reducing the number of suppliers (Lamming, 1993), and implementing alliances with partners and suppliers in order to satisfy customers and provide the total customer experience (Vandermerwe, 1996). Thus, another transition can be formulated, which, according to many authors, can be seen as both a precondition for, and a consequence of, the adoption of service logic.

T4. The externalisation of service processes at various points in the service distribution channel and at the different service spaces in Figure 1

This is the transition which this thesis focuses on, in particular with regard to the basic services in service space A, including how the transition is affected by transitions T1-T3.

2.3.2 Problems during the adoption of service logic

The transition from manufacturer to service or solution provider constitutes a major managerial challenge (Oliva et al., 2003) and evokes significant tensions between what is good for the client and the capabilities needing to be developed to meet customer needs (Miller et al., 2002). The transition process is thus likely to encounter problems.

One example of an empirically-grounded study that focuses on problems and challenges related to this transition process has been made by Oliva and Kallenberg (2003), and is based on interviews with senior managers and archival data from eleven equipment manufacturers relatively early on during the adoption process. A few other studies have suggested problems and challenges based on studies of archival data, interviews with top-management, or without referring to any empirical data at all.

Although the empirical evidence is sparse, a number of problems and challenges suggested in previous research will now be summarised:

- Infrastructure, i.e. building and managing the systems and infrastructure for services (Oliva et al., 2003), e.g. the capabilities, processes, and resources necessary for managing the service organisation
- Service Skills, i.e. developing skills in, for instance, providing services (operational, relationship-based, and process-oriented), pricing, and risk management. (Davies et al., 2001, Mathe et al., 1993, Mathieu, 2001b, Oliva et al., 2003)
- Change Management, i.e. managing internal resistance and cultural change when moving from products to services (Davies et al., 2001, Mathieu, 2001b, Oliva et al., 2003)

- Establishing appropriate collaboration within the service distribution channel in order to become more efficient and customer-oriented (Davies et al., 2001, Oliva et al., 2003)
- Establishing an ongoing customer relationship and a reputation as a service provider (Oliva et al., 2003)

Of the studies referred to, the one by Davies and colleagues (Davies et al., 2001) focused on a transformation corresponding to transitions T2-T4, while the others primarily focused on transition T1.

More recently, Söderström (2004) examined obstacles to adopting service logic, focusing on functional sales, i.e. the selling of functions consisting of products, services, financing, education, and information. His conclusions regarding the difficulties of doing this include the fact that it requires a paradigm shift in the existing business logic and supporting structures; above all an overall service-oriented vision. Furthermore, he questions whether or not an end-product manufacturer is capable of adopting service logic and changing his existing business logic, e.g. due to the lack of supporting structures.

The meaning of adopting service logic has now been defined, however broadly. Previous literature on the problems and challenges associated with this adoption has also been reviewed. In the following section, the focus turns to the main subject of interest in this thesis, i.e. the externalisation of product services into inter-organisational alliances.

2.4 Externalising services

One important issue for industrial firms interested in leveraging the opportunities related to delivering various sorts of product services deals with the structuring of the distribution channels for the product services, and whether the internal organisation is to be used for the delivery of services or if external resources should be used, e.g. whether alliances should be implemented. As was mentioned above (for instance, on page 24) , it is often argued that the needs of the customers and the delivery of integrated solutions or full services, for instance, can only be satisfied by means of collaboration between industrial and service firms and by externalising less critical activities such as basic services.

The term externalising services means that an alliance is implemented and that some service processes are externalised to suppliers, including the burdens and benefits of managing them. Industrial firms tend to use external resources for their service processes when they do not have sufficient capabilities to perform the service efficiently and cost-effectively, or when they lack the capacity to perform the service at all (Axelsson et al., 2002).

In the delivery of product services, this is common practice in many industries, and the externalisation of product services is actually increasing in, for example, the UK (Management Services, 1998). According to Donald Blumberg, an independent consultant focusing on the product service business, today's service industry is changing dramatically and the externalisation of product services is increasing (2003b). The primary reasons for this are that the internal service organizations are unable to handle new technology and many outsourcing organizations are emerging. These new service organisations, including Electronic-Manufacturing Services (EMS) firms, consulting firms, and systems integrators, are striving to exploit the opportunities for economies of scale made possible by the commoditisation of many products. Some of them are also trying to achieve economies of scope by taking over not only manufacturing and basic services, such as repair, but also design and more advanced services, such as installation and consulting. Consequently, some of them have comprehensive service offerings, including product-oriented, transaction-based, relationship-based, and process-oriented services, covering a large part of the matrix in Figure 1 (Page 23).

The main focus of this thesis is problems arising during the externalisation of basic product services into alliances. Even if most previous research into alliances is not about product services, it is likely that much of what has been said in more general research into alliances is also applicable to product service alliances. Thus, some literature of a more general nature connected with the problems associated with alliances will be reviewed, as will literature on service alliances and literature focusing on the process leading to alliances. First, however, there will be a review of the literature emphasising a dilemma associated with externalisation.

2.4.1 A dilemma leading to externalisation problems?

In the preceding discussion, a dilemma can be observed which is related to the adoption of service logic at industrial firms. In order to adopt service logic and take full responsibility for meeting the needs and problems of the customers, the assistance of other firms is often necessary. Collaboration is often necessary, thus the achievement of full responsibility must be divided between several actors. In other words, the delivery of advanced services often has to be accomplished in concert.

The dilemma lies between the contradictory forces tending towards a greater level of responsibility vis-à-vis the customer and towards a smaller operational responsibility because of outsourcing and partnering. These contradictory forces are likely to make the externalisation of services troublesome since they pull in different directions, at least at a first glance. In general, each supplier firm is responsible for the development of a diminishing share of the total system offered to the customers, due to the increasing reliance on sourced technology. At the same time, there is an increasing demand for someone to take full responsibility for all

the products and services being purchased by industrial customers. One might ask what challenges are implied by the transformation of an industrial firm into a full-service provider with alliances.

Lovelock has expressed one challenge related to this dilemma (1992) thus:

“Fast, good quality response is sometimes more easily and cheaply obtained through subcontracting certain customer-service functions to outside firms”

“The negative side of such an approach is that the primary service supplier loses control over the quality of customer service, may fail to capture the valuable marketing information inherent in customer-service calls, and may even find the subcontractor actively promoting the competition”

These quotations call attention to the risks of losing control over aspects of the relationship with the customer when using external resources to deliver services. Ford, for example, also discusses the changing roles of suppliers in vertical alliances (1998):

“As retailers grow larger they may try to alter their relationships with end-users by building the reputation of their own-brands as a rival to those of the manufacturer”

“Some wholesalers may evolve towards more integrated, higher-service relationships at correspondingly higher prices”

Similarly, Karlsson (2003) describes the risk associated with new actors making an entrance in between the customers and the industrial firms, and also suggests how this risk can be handled:

“These actors are agents or navigators coming in between the OEM and their customers. They may appear to offer improved ways of reaching consumers but may cause deterioration in the competence in the value chain. This because their action takes away margin from the OEMs that then will have less possibilities of financing resources for purchasing, development, and production. A possible strategic response for the OEMs is to move in the direction of offering more and more complete functions. Otherwise there is a risk that they will be overrun in the marketplace by agents who offer more complete functions and more choices but who may not care about maintaining an industry with strong development capabilities”

These quotations illustrate the risk that suppliers “climb up the value chain” towards more attractive services closer to the end-customers, thus becoming competitors of the buying firm. In relation to this risk, Mathe and Shapiro (1993) describe two apparently opposing tendencies in the structure of service organisations: (1) the forces tending towards the integration of service units within the manufacturing firm, and (2) the forces tending towards greater differentiation, subsidiary creation, or subcontracting of services.

All quotations above, as well as the tendencies observed by Mathe and Shapiro, indicate the issue addressed by this thesis; i.e. the challenges related to the simultaneous externalisation of services and the transformation of an industrial firm into a provider of full-services and solutions. These challenges involve the possibility of losing the relationship with the customer to any of the suppliers or

partners. This risk (the lost customer relationship) is relevant to many forms of alliances, especially looser forms such as partnerships or non-equity alliances. Equity based alliances such as joint ventures are often used to reduce risks in alliances, but have other drawbacks such as a lower level of flexibility.

Thus, from the review of the literature, it can be concluded that, according to many authors, there are several *reasons* why the industrial firm should externalise its delivery of services into different sorts of alliances. In contrast, some researchers (e.g., Mathe et al., 1993) claim that, for firms that compete via their services and often change their services, an integrated service function is more suitable. Moreover, others suggest that that services providing long-term strategic competitive advantage should be conducted in-house. Less important services should be externalised whenever possible (Meyer & Blümehuber, 2000). This thesis focuses on a firm which externalises some of its service processes which it perceives to be less important to retain internally, i.e. basic services.

Because of the dilemma described above, the externalisation process can be expected to be problematic. A specific challenge that needs to be considered during the change process concerns how to maintain the relationship with the customer in spite of externalisation. There is a risk that customers will switch their first-tier supplier or partner, and that the supplier or partner will actively work towards this change. This risk may also become a critical strategic challenge for the industrial firm during its externalisation project.¹⁶ Employees may be reluctant to externalise services because of their perceptions of the involved risks, and the prospective partners or suppliers may act opportunistically during and after externalisation projects.

In the following section, literature dealing with problems associated with externalisation is reviewed.

2.4.2 Problems associated with externalisation

According to previous studies on problems associated with implementing alliances, the problems encountered are often about people/relationship issues (Kelly et al., 2002), i.e. related to collaboration between people. Examples of people/relationship problems reported in the literature include;

- Insufficient and ineffective communication between alliance firms (Kelly et al., 2002, Sahakian, 1998)
- Conflicts between alliance firms (Lorange & Roos, 1991, Mentzer et al., 2000, Mohr & Spekman, 1994, Moore, 1998)
- A lack of trust between alliance firms (Elmuti & Kathawala, 2001, Gulati, 1995, Parkhe, 1998)

¹⁶ This was confirmed during Study I and further investigated in Studies II-V

- Cultural differences between the alliance firms, e.g. in terms of different national or corporate cultures, possibly leading to misunderstandings, irritation, and miscommunication (Elmuti et al., 2001, Kelly et al., 2000, Lorange et al., 1991, Vyas et al., 1995)
- Organisational politics between alliance firms, hampering the implementation of the alliance (Lorange & Roos, 1992)

A second group of problems relates to operational issues, e.g. insufficient specifications or quality problems creating unpleasant and unwelcome surprises (Elmuti et al., 2001, Kelly et al., 2002). A third group of problems concerns more strategic issues, for example the risk of losing core competencies to a partner (Elmuti et al., 2001, Lorange et al., 1992). Finally, the performance or results of the collaboration, in relation to what was anticipated in advance, are sometimes referred to as a problematic area (Elmuti et al., 2001, Kelly et al., 2002).

Based on research into the early stages of alliances between manufacturing, service, and R&D-based firms, Kelly and colleagues (2002) found that the majority of the problems (55%) were related to soft issues, or people/relationship issues. Operational problems accounted for 29%, strategic problems for 11%, and performance-related problems for 5%.

When it comes to the literature focusing explicitly on *outsourcing*, on the other hand, internal resistance by employees is frequently mentioned as a problem, not least in practitioner-oriented journals. For example, “overt and covert resistance from your managers and employees who don’t understand and buy into the outsourcing strategy” (Harper, 2001) is often emphasised. Internal resistance in the buyer’s organization has also been acknowledged as the biggest obstacle to implementing an offshore strategy, and is something which, according to Bendor-Samuel, can only be moderated by a serious change management program (2004). For service outsourcing, Allen and Chandrashekar (2000), whose work was defined as one of the most pivotal publications in the area, mention several potential problems, e.g. managing a split workforce, articulating requirements regarding “a courteous attitude”, for instance, a dip in morale among the employees, and the leakage of confidential information.

Among the strategic risks associated with outsourcing, Quinn and Hilmer (1994) mention three. *First*, there is the risk of losing critical skills or developing the wrong ones. It can be difficult to assess *ex ante* exactly which skills are critical; outsourcing may entail skills being outsourced which were more important than the firm doing the outsourcing initially thought. *Second*, there is the risk of losing cross-functional skills as outsourcing reduces internal interaction between employees. It should, however, be possible to mitigate this risk by increasing interaction with the suppliers. *Third*, there is a risk of losing control over a supplier, and that suppliers, after having amassed their expertise with the buyers’ support, will attempt to bypass the buyer directly in the marketplace, or resell their

know-how to the competitors of the buyer. According to Lonsdale and Cox, the reasons for such behaviour are poor contracting, outsourcing into a limited supply market, asset specificity, and uncertainty. Poor contracting, in turn, is often the result of the inappropriate allocation of human resources, or the failure to use knowledge of the critical aspects of the products or services being outsourced (Lonsdale & Cox, 1998).

Barthélemy (2003) has provided a rare example of an empirical study focusing on reasons for *failed* outsourcing initiatives, based on interviews with senior managers and a questionnaire focusing on such initiatives. According to this study, there are seven principal reasons, denominated “deadly sins”: (1) outsourcing activities that should not be outsourced¹⁷, (2) selecting the wrong vendor, (3) writing a poor contract, (4) overlooking personnel issues, (5) losing control over the outsourced activity, (6) overlooking the hidden costs of outsourcing, and (7) failing to plan an exit strategy. Moreover, Useem and Harder (2000) focus on the “leadership capabilities” needed by firms that outsource different activities, based on interviews and a questionnaire: strategic thinking, deal making, partnership governing, and managing change (due to employee resistance).

It should also be noted that *business* markets for services, which are of interest in this thesis, have certain characteristics that are potentially important when implementing alliances. A review of some of the peculiarities of business markets may contain clues to problems relevant to the externalisation projects in focus in this thesis. For example, business services often need to be customized and are based on a greater level of complexity regarding organizational needs. Therefore, the supply of business services must be handled differently to the supply of consumer services (Fitzsimmons et al., 1998). Furthermore, the purchasing process in business markets is typically more complex than it is in consumer markets, involving numerous employees from both sides of the relationship, from different hierarchical levels, and from different functions within the organizations (Ford, 2002). Business purchasers are trained professionals, which sometimes makes the purchasing procedure more formalised (Johnston, 1981).

The complexity of many business services often makes the time-span of the purchasing process longer (Webster, 1991). Another important difference is that in industrial markets customer relationships are often close and long-lived. In business services, the actual service encounter accounts for a relatively small part of the relationship between buyer and seller, and the importance of the service encounter is thus often less critical than it is in consumer relationships. In business markets, service encounters are only an element of an ongoing sequence of

¹⁷ According to Barthélemy, however, it is difficult to implement a core vs non-core dichotomy on the firm level. This should instead be implemented on the activity level since most activities have parts that can be regarded as core and others that cannot.

episodes between the customer and the service firm which jointly constitute the relationship (Grönroos, 1994, Gummesson, 2002, Holmlund, 1997).

More generally, providing services in alliances entails different risks and challenges, compared with alliances focusing on developing and producing goods, due to the characteristics of services (Fitzsimmons et al., 2000). For example, the intangible nature of services makes the evaluation of the vendor more difficult and the specification of the desired service less precise. Many services have to be delivered close to the customer and cannot be centralised, and this makes the delivery structures of service alliances more complex. Judging whether or not the delivered services meet expectations is more difficult, because services are not subject to close scrutiny (Fitzsimmons et al., 1998). The relational nature of many services (Grönroos, 2000), meaning that “there are always relationships between a service organisation and its customers”, implies that the customer must be taken into account to a greater extent when implementing service alliances (O’Farrell et al., 1999). Service supply chains are often bi-directional, with production flowing from suppliers to customers as well as from customers to suppliers. Thus, there is a “customer-supplier duality” whereby the customers are also suppliers (Sampson, 2000). Many businesses’ service quality depends not only upon the performance of the supplier, but also on the customer’s performance when interacting with the supplier (O’Farrell & Moffat, 1991).

From the brief review above, it can be concluded that the relationship with the customer is pivotal in services, in particular in business markets and when the firm is seriously trying to become more service-oriented. Sustaining the customer relationship seems to be a potential challenge during the process of externalising services at industrial firms, assuming there is no clear and sequential process of implementing service alliances, where strategy formulation is followed by strategy implementation. Although this is not unique to business services, it is probably more important than in, for instance, manufacturing alliances because of the nature of services.

2.4.3 Processes of collaboration within alliances

There are a limited (but growing) number of studies focusing on the process of collaboration and the unfolding of the collaboration process. Examples of such studies include those conducted by Ring and Van de Ven (1994), Doz (1996) and Marshall (2004). The basic assumption here is that the outcome of the collaboration is based not only on the initial conditions and characteristics of the involved firms, but also on the collaboration process *per se*.

A shared feature of the models of collaboration developed by these scholars is the fact that the collaboration process is seen as a cyclic process whereby the initial conditions are revised and reviewed. For example, the model by Ring and Van de Ven is composed of the three cyclic (but overlapping) stages of negotiations,

commitments, and executions. During the negotiation stage, joint expectations are developed via the formal bargaining process. During the commitments stage, the parties' wills meet through reaching agreement and the terms and governance structure are established. During the executions stage, the commitments are executed. The alliance is also regularly assessed on the basis of its efficiency and equity. The model suggested by Doz is a sequence of learning, re-evaluation, and revised conditions.

Outsourcing is often described as a linear, or sequential, process, whereby planning is emphasised and implementation follows strategy formulation (see, for instance, Zhu et al., 2001). In contrast, Wasner (1999) concludes that outsourcing is inherently processual and that a rational approach is often unfeasible:

“Defining outsourcing as a processual phenomenon entails a notion of outsourcing as partly managed at the strategic level, in other words aligning planned action with strategy, yet to a large extent driven by actions at the operational level. Strategic management establishes a vision and sets frame restrictions, whereas operational developments lead to actions that determine the pace and partly the scope of the outsourcing commitment. This amounts to a gradual shift from strategic to operational focus as the process evolves.”

The reasons why Wasner claims that the rational approach is not feasible include the difficulty of predicting environmental changes and foreseeing events that will impact on the outsourcing process. Thus, there is a need to be flexible during the outsourcing process. This perspective seems particularly feasible in turbulent environments at firms which are also transforming their business more generally; e.g. firms that are also adopting service logic.

2.5 Summary

There will now be a summary, in a condensed and somewhat simplified format, of what the reviewed literature has to say about the meaning of adopting service logic that includes advanced services and about the externalisation of services. By comparing the different research areas, clues to challenges associated with the externalising of basic services, simultaneous to service logic being adopted, may also be found.

First, however, the present study's position in relation to the research field (externalising services and adopting service logic) is roughly illustrated in Figure 2. In the figure, the literature with a focus on the *change* (i.e. how?) and the adoption of service logic or the externalisation of services is separated from the literature with a focus on the *strategy* (i.e. what? and why?) and the adoption of service logic or the externalisation of services. Although this distinction is not always crystal clear or easy to make, the figure is an attempt to provide an overview of the literature and to highlight areas with relatively little literature.

In particular, it would appear that there is a lack of literature focusing on the simultaneous adoption of service logic and externalisation of services from a change perspective, which is also the focus of this thesis. The present thesis intends to contribute to this neglected area and will primarily be positioned in relation to the literature in the lower two quadrants and, in particular, the literature in the quadrant to the right. As mentioned earlier (see Section 1.4), the present study will primarily be compared with O’Farrell and Wood and Allen and Chandrashekar, and secondarily with the literature on change and the adoption of service logic.

The literature with a more strategic focus (the two upper quadrants) is also highly relevant to this thesis because it can, for instance, contribute to our understanding of alternative service and sourcing strategies and justify why these are feasible. In doing this, they can also help to explain why problems occur during the externalisation of services.

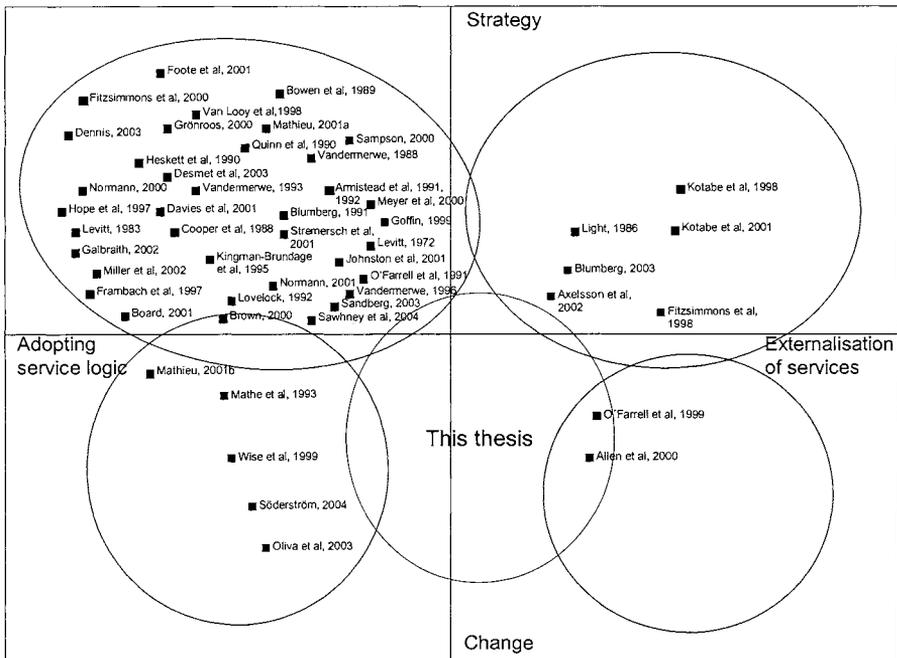


Figure 2. Overview of the reviewed literature and the focus of this thesis

According to the literature in the upper left quadrant of Figure 2, *the adoption of service logic* at industrial firms is basically associated with approaching the customer via the delivery of more comprehensive services and solutions that are adapted to the customers’ full needs, and aims to create longer-lasting relationships with customers from which both the supplier and the customer will benefit. These

new types of services emphasise the need to treat the customer as an important asset, with the repeat business of satisfied customer being pivotal to a sustainable business. An increasing level of technological complexity increases the demand for more comprehensive services that can simplify customers' business operations; satisfying this demand may be a way of differentiating oneself from the competition. Employees (not least service employees) are to be cultivated as a corporate resource. It is acknowledged that they possess knowledge and experience that can be used to improve the business.

The literature in the lower left quadrant supports the view that adopting service logic can be a difficult managerial task requiring skills for managing internal resistance and changing the internal culture. Adoption should focus on creating skills and infrastructure for the more customer-oriented services and creating a sustainable relationship with customers. Whenever feasible, service alliances should be established to help to make the firm even more customer-oriented. Moreover, the structure of the service channel has only been described by a few authors, whereby certain processes should be kept internal while others are externalised.

According to the literature in the upper right quadrant, *the externalisation of services at industrial firms (in particular the basic ones) into operational alliances* is, on the other hand, basically associated with the exploitation of external resources, most often for cost-related reasons but also for competence-related reasons.¹⁸ Furthermore, it is about releasing the industrial firm from managing certain activities so that it can focus on activities that are perceived to be more central to its core competency. This literature emphasises why externalisation is feasible and which areas should be externalised. To some extent, it describes the specificity of services and how this may influence externalisation. It also describes ongoing trends, addresses performance implications and the risks associated with externalisation, and describes aspects (e.g. contextual factors) to consider when externalising services. These are aspects that may potentially influence externalisation if not addressed appropriately during the strategy process.

The literature in the lower right quadrant suggests that externalising services can be a complicated task, and one that should involve communicating with the supplier or partner, in order to manage conflicts and politics, build trust, and manage specifications and strategic risks. The need to have senior management support and clear goals is often mentioned.¹⁹ An aspect that is not so frequently emphasised is the need to involve the customer in the change process. Internal resistance is often mentioned as a potential problem needing to be managed,

¹⁸ The description given here assumes that industrial logic dominates within the firm.

¹⁹ For explorative alliances, or alliances for innovation, the alliance process is more strongly emphasised than the need to have clear goals. See, for instance, Ring and Van de Ven (1994) and Marshall (2004).

whereas the role of the customer is most often neglected, with O'Farrell (1999) being a notable exception here.

In addition to the literature included in the figure, change management literature is also relevant as it provides a language and a framework useful for studying the shift of interest in this thesis.

Of the reviewed literature, the articles by O'Farrell and Wood and Allen and Chandrashekar were seen as most pivotal (for a review, see Section 1.4). As externalisation is seldom a goal in itself and rather a means toward another end such as, in this case, adopting service logic, literature on this topic focusing on change may also be useful for the present study. For example, this provides results regarding potential problems arising during adoption. This knowledge may be important to understand if externalisation is taking place in such an environment. This literature also describes the transitions to undertake in order to adopt service logic.

In the next section, the frame of reference is described and the research question is formulated.

CHAPTER THREE

Frame of Reference and Research Question

In this chapter, three challenges associated with the externalising of services are presented, with the purpose of clarifying the research issue of interest and converting the purposes of the thesis into both a frame of reference for the research and a more specific research question.

3.1 Introduction

Three vital challenges will now be described, all drawn from the literature reviewed and summarised in, for instance, the previous chapter, as well as from insights gained gradually during the empirical studies.

The challenges arise when basic services are externalised while service logic is being adopted. They result from the conflicting logics of the two trends, i.e. from the exploitation of external resources for service delivery and from attempts to take advantage of opportunities associated with developing and offering services that may create a sustainable relationship with customers. These challenges have different meanings as they address different subsystems of the organisations. They call for adjustments within the internal organisation, of the strategy formation process, and with regard to how customers become involved in externalisation. Here, they are called; (1) the internal challenge, (2) the strategy formation challenge, and (3) the customer relationship challenge.

Depending on how externalisation is carried out, the challenges may turn into overt problems that can hamper both the externalisation and the adoption of service logic. Consequently, the manner in which some of the literature suggests that the challenges and problems should be managed is also presented, prior to the frame of reference being summarised in a model and the research question being presented.

These challenges can be seen as the “spectacles” that supplement the theory mentioned in the previous chapter and they will be used when interpreting the gathered data. They are vague enough to allow me to keep an open mind but precise enough to focus my attention somewhat.

3.2 Three externalisation challenges

3.2.1 The internal challenge

This challenge concerns the internal change process associated with externalising basic services, and how this change process is managed during externalisation. It is basically about involving internal employees during the externalisation process, in order not to hamper the adoption of service logic and the externalisation process.

The employees of the organisation may see the externalising of services and the adopting of service logic as counter productive. Adopting service logic entails creating new skills and cultivating internal employees in order to approach the customers further, and to offer more advanced services that can simplify the customers’ business dealings. On the other hand, externalising services essentially means transferring part of the customer interface to an external firm and making the organisation more efficient. In other words, the two logics can be seen as conflicting, so resistance and confusion within the organisation can be expected.

Internal resistance to externalisation may arise on the basis of a reluctance on the part of the internal employees to externalise service activities that are perceived to be central to the way the firm is to compete and the branding of the firm (Ernst, 1996). Overt and covert resistance by managers and employees can be a serious obstacle to the change process, and can sabotage both the externalising process (Harper, 2001) and the adoption of service logic, consisting of the delivery of more customer-oriented services such as solutions (Mathieu, 2001b). According to Bendor-Samuel (2004), the internal resistance of the buyer’s organization is the biggest obstacle to the offshore outsourcing process, and change management can manage that resistance.

Although this resistance cannot, and probably should not, be avoided altogether, as it may also bring positive effects and, for example, stimulate more reflective decision-making (cf. Rahim, 1992, p. 5), there is often a need for conscious change management in order to reduce the negative effects of internal resistance to a more constructive level (cf. Bendor-Samuel, 2004) and thus avoid a dip in morale for example (see, for instance, Allen et al., 2000). In other cases, especially at prosperous firm and during boom periods, externalisation may be taken too lightly by employees and managers who are searching for new and interesting areas, with the basics of the firm being neglected (cf. Bettis et al., 1992).

Even though the ideal change process leading to a new alliance is often described as a linear one that should be well planned, have clear goals, etc. (see, for instance, Ellram & Eddis, 1996, Zhu et al., 2001), in reality this rational approach may not be feasible, which is something that has also been acknowledged by, for instance, Wasner (1999). According to Wasner, and based on in-depth studies of two in-depth cases of outsourcing development and production at Saab and Ericsson, outsourcing is *inherently processual*. As stated by Wasner, it is not only a matter of perspective but rather a consequence of a typical outsourcing's long duration and the difficulty in predicting environmental changes, making flexibility, iteration, and learning important features of the outsourcing process.

Furthermore, many industries operate in a state of volatility that makes it almost impossible to forecast, with any degree of accuracy, how the market will look more than a few months ahead. Under such conditions, responsiveness to changes in the market and technology can be more important than formal planning procedures (Bettis et al., 1992), and strategic technology planning is replaced by technological surprises (Bettis & Hitt, 1995, p. 11). Externalising basic services while service logic is being adopted constitutes a dynamic situation whereby not only the firm that is delivering the specific service is changing, but also the industry more generally, including the roles of the involved firms. This can be expected to make planning more difficult and responsiveness more important.

3.2.2 The strategy formation challenge

This challenge concerns the long-term strategic implications of externalising basic services, and how this challenge is managed during the externalisation project. It is basically about managing suppliers and partners during the externalisation process, and selecting an appropriate alliance strategy, in order not to hamper the adoption of service logic and externalisation.

To compensate for the externalisation of basic services to specialised service firms, and for the frequently-associated downsizing, firms are often recommended to introduce more customer-oriented and comprehensive services, so called advanced services (Oliva et al., 2003), and to increase the value for the customer. There are at least two approaches to this, similar to the transitions described on page 2. Miller, for instance, suggests integrating forwards in the value chain and taking over customers' operations or offering more integrated solutions composed of products and services (2002). These new sorts of more complete services release customers from dealing with some of their complexity, so they can focus on their core business, typically marketing and sales. According to many authors, introducing such services brings benefits to the supplier, e.g. expanded margins, stabilised revenues, differentiation from competitors, and cross-selling opportunities (e.g., Miller et al., 2002).

Another benefit to be reaped by supplier firms introducing such advanced services is that organisations located downstream, or close to their customers, such as solution providers and suppliers managing customers' operations, can typically obtain a better understanding of the customers and their needs (Storer et al., 2002). Through their role of intermediary between other firms and the customers associated with being a supplier of such services, the advanced services are also attractive to introduce. They can retain, or increase, the power of a firm that is externalising its basic services and its possibilities of influencing the design of the delivery system (cf. Light, 1986).

The challenge concerns protecting these new services (i.e. advanced services) from competition, as it can also be expected that some of the suppliers of more basic services may be interested in differentiating and offering more advanced services. Although not all firms are adopting service logic, some authors (e.g., Vargo et al., 2004) claim that, during recent decades, service logic has achieved dominance over, for instance, the goods-oriented logic. In other words suppliers of basic services may also intend to differentiate themselves from the competition by offering a higher level of services than their competitors (cf. Desmet et al., 2003). The externalisation of basic services may even facilitate this move on the part of the suppliers.

If each externalisation initiative is analysed in isolation from the overall strategy of the firm, and if the internal development of knowledge, and the risk of losing critical knowledge to the supplier, are not taken into account sufficiently, this may lead to a vicious circle for the firm that is outsourcing (Bettis et al., 1992, Quinn & Hilmer, 1994), ultimately leading to the decline of that firm. There is always a risk of opportunistic behaviour in business relationships (Das & Teng, 1999), which can entail, for example, the supplier integrating forwards in the value chain and becoming a competitor (McCutcheon & Stuart, 2000, Quinn et al., 1990) in the newer service areas where the industrial firm intends to compete.

Furthermore, the firm that is externalising a service should ensure that it does not become unnecessarily dominated by its partners and suppliers, which is why some authors suggest that non-competing enterprises should preferably be selected (Quinn et al., 1990) or that only areas remote from the core should be outsourced (Bettis et al., 1992).

3.2.3 The customer-relationship challenge

This challenge concerns the effect on the adoption of service logic caused by the externalising of basic services, and, in particular, the effect on the externalisation of the relationship with the customer and how this relationship is managed during the externalisation process. It is basically about managing the relationship with the customer during the externalisation, in order not to hamper the adoption of service logic and the externalisation process.

When a service process is externalised, it is important to communicate the planned changes to the customer, or even to have the customer sanction them, since he may be affected by the change and his perception of the firm may also be affected (O'Farrell et al., 1999). This is particularly important if the intention is to adopt service logic.

Often, it is suggested that services providing long-term strategic competitive advantage and differentiation from competition should be conducted in-house. Less important services should be externalised whenever possible (Meyer and Blümehuber, 2000), e.g. basic services such as installation and repair. However, when the production of a service is externalised, marketing remains important, and if the association between the service and the company, and the integration of the service within a broader company-based system is not clear to the customer, there is a risk that the customer will not be satisfied (Meyer et al., 2000).

Furthermore, the quality of many services not only depends upon the performance of the supplier, but also on how well the customer interacts with the supplier (O'Farrell and Moffat, 1991), which is why the customer should always be involved in a service-externalisation decision. Just how important this is will depend on the type of service being externalised, where, for instance, high-contact services, such as installation and training, are more directly visible to the customer than low-contact services, such as repair.

According to Payne and Frow (2000), the importance of building and maintaining long-term relationships with customers is currently being enhanced by trends such as the deregulation and internationalisation of markets, which are increasing the level of competition within the services sector. Furthermore, as early as in 1983 Berry was contending that marketing, in order to protect the customer base, was becoming increasingly important in services, owing to the increased supply of similar services resulting from deregulation (1983).

3.3 Research model

It was predicted earlier on in this thesis that externalisation may be problematic when conducted while service logic is being adopted, due to the challenges resulting from the conflicting logics of the two trends. The potential externalisation problems to be expected as a result of these challenges include resistance by employees, conflicts, the risk of losing competencies to suppliers and partners, organisational politics, and communication problems. In the previous sections, three challenges possibly leading to problems during externalisation were described. Some suggestions were also provided from the literature regarding how the challenges, and the potential problems resulting from them, should be managed.

Problems during externalisation constitute the core empirical base for the papers and this thesis. Another area of interest is how these problems can be moderated.

To recapitulate; in Chapter 1, the purposes of this thesis were stated:

- P1: to explore problems, as well as their sources, associated with the externalising of basic services at an industrial firm while service logic is simultaneously being adopted.
- P2: to suggest how externalisation should be carried out in order that externalisation problems may be moderated.

There are at least two alternative ways of moderating externalisation problems.

Firstly, by adjusting the sourcing and service strategies and finding the best possible balance between what is to be externalised and which skills are to be developed internally. Using the terminology of Pettigrew (1985, 1987, 1990) and Pettigrew and Whipp (1991), the *content of the change*²⁰, i.e. the objectives, purposes, and goals of the change, may be adjusted to reduce the challenges and make implementation easier. Well thought out strategies which are adjusted to relevant contextual factors, and which are also perceived to be correct by the employees, are likely to be easier to implement. If, for instance, a firm decides not to focus on service logic, externalisation problems resulting from the customer relationship challenge will probably be fewer, although the internal resistance may in that case be greater if the employees see adopting service logic as a logical move. The sourcing and service strategies, as well as the change approach, need to take the internal and external context of the externalisation project into account, including, for instance, technology, culture, capabilities, resources and organisational politics, and the broader external context.²¹

Secondly, and more pivotally in this thesis, moderate problems by adjusting the way in which the externalisation process is carried out, i.e. the change approach (or using Pettigrew's terminology, the *process of change*²²). This thesis assumes the perspective that the change approach needs to be adjusted to the specific situation or context for each change initiative and organisation (cf. Balogun et al., 2004, Hope Hailey et al., 2002).

Moreover, the challenges described above, and the contextual features, are closely related to each other. Contextual features are seen here as the underlying sources of the challenges, and a better understanding of them can thus deepen the understanding of the challenges, as well as the externalisation problems and appropriate change approaches. By using existing theoretical frameworks taken

²⁰ "the particular areas of transformation under examination" (Pettigrew, 1987)

²¹ The influence on *strategy*, or service channel, of the product, market, and firm contextual factors, is to some extent covered in Paper IV. More specifically, paper IV focuses on the influence on the appropriate service channel structure contextually. The effects of deviating from the appropriate structure are also investigated. From a change point of view, implementing a strategy that has not been adjusted to relevant contextual factors may be problematic.

²² "the actions, reactions, and interactions from the various interested parties as they seek to move the firm from its present to its future state" (Pettigrew, 1987)

from the change management literature regarding how appropriate approaches to change are moulded by context, a deeper understanding of the sources of externalisation problems may be achieved and more trustworthy advice about how the externalisation process should be carried out can, hopefully, be provided.

3.3.1 Influences of the change approach on externalisation problems

It is assumed here that these externalisation problems can be moderated by an appropriate externalisation process, i.e. by the way in which the externalisation is carried out.

For example (repeated from Section 3.2 above), the first challenge concerns the problem of internal resistance by employees who perceive the externalisation to be a threat to the adoption of service logic. As mentioned above in the description of the challenges, careful change management can deal with this, by involving employees and communicating extensively, for instance. Otherwise, employees who are not cooperating may hamper the externalisation project. The choice and management of suppliers to which the services are to be externalised is the second challenge. Suppliers' possible opportunistic behaviour is a potential problem associated with this which needs to be managed. Furthermore, the third challenge concerns the pivotal role played by the customers during the externalisation of services. This means that customers should be involved in decisions to externalise services because they will be influenced by it and may have opinions about it, which may also hamper the externalisation.

It is assumed here that the way in which the externalisation is carried out influences the extent to which the challenges turn into overt problems that may hamper the externalisation. The way in which the externalisation is carried out is called here the *change approach*, and is defined as:

The characteristics of the process of externalising services, i.e. the way in which the externalisation project is carried out.

According to Balogun and Hope Hailey, at least the following aspects of the change approach exist, which should all be adjusted to the change context:²⁴

- Change path; i.e. the end result of the change (transformation or realignment) and the nature of change (incremental or big bang), or if it is rational or emergent, cf. Ghoshal and Bartlett (2000) and Weick (2000).
- Change starting point; e.g. top-down or bottom-up
- Change style; e.g. the degree of communication and participation. The alternatives range from coercion to education and delegation.
- Change target; e.g. values, behaviours, or outputs.

²⁴ See also the literature review focusing on change management in Chapter 2.2.

- The change levers and interventions to use; e.g. technical and political interventions such as structures and systems, cultural interventions such as symbols and routines, and interpersonal interventions connected with communication education and training.
- Change roles; e.g. the combination of leadership, change action teams, and the use of external consultants.

The present thesis does not intend to take all of these into account, primarily focusing on the first three dimensions.

3.3.2 Adjusting the change approach to context

The importance of context to change management has been acknowledged by several authors, e.g. Pettigrew and Whipp (1991) and Nadler and Tushman (1989); also, previously highlighted contextual features capable of guiding the choice of change approach have been summarised by Hope Hailey and Balogun (2004, 2002) (see Section 2.2.1 on page 2 of this thesis). Although contextual features may also change over time, they are typically not easily changed by an externalisation project and should be adjusted to rather than be adjusted.

In this thesis, contextual features inherently associated with externalisation and the adopting of service logic will primarily be considered, i.e. features that may be expected in any large industrial firm simultaneously externalising its basic services and adopting service logic. In accordance with this delimitation, *change context* is defined as:²⁵

The internal and external contextual features inherently related to the adopting of service logic and the externalising of basic services.

Of the contextual features mentioned by Hope Hailey and Balogun (2004, 2002), *scope, preservation, diversity, and power* seem to be features of particular relevance to this study. This does not mean that the others (time, capability, capacity, and readiness for change) are deemed irrelevant. But, given the focus of this thesis, i.e. exploring the externalisation problems associated with the simultaneous adoption of service logic, as opposed to exploring problems more generally associated with, for instance, management, limited resources, and so forth, firm-specific features such as readiness for change, capacity, and capability are disregarded here, as are situational features such as the speed with which the change needs to be achieved. Such factors may suggest that another change approach than the one to be suggested in this thesis is being used, and should be taken into account in any real change situation faced by a firm. These are not, however, necessarily generalisable outside the studied firm.

²⁵ In Paper IV, another set of contextual factors are included (firm, market, and product contextual factors). These may be called “structural” to distinguish them from the change context.

Thus, the change approach suggested here and the contextual features discussed in this thesis are more closely related to externalising basic services and adopting service logic at the same time. Thus, they are the main contextual features that will be used to guide the interpretation of the data, being defined as follows:

- *Scope* concerns the degree of change required, e.g. realignment or transformation and whether the change affects the whole organisation or only parts thereof.
- *Preservation* concerns the assets, characteristics, and practices that need to be maintained and protected during the change.
- *Diversity* concerns whether the different staff/professional groups and divisions within the organisation are homogenous or diverse in terms of values, norms, and attitudes.
- *Power* concerns where power is vested within an organisation and who are the major stakeholders within and outside of the organisation who hold the power in the organisation. Whose support must be secured?²⁶

Moreover, the change context is moulded by the content of the change; in this case, the externalisation of basic services and the adoption of service logic. For instance, the depth and extent of the change (i.e. the scope) is inherently related to the effectuation of these specific intentions at the same time. Consequently, the content of the change influences the change context and thus also the type of change required, e.g. transformation or realignment.

For example, the extent to which it is essential to maintain continuity in certain practices, or preserve (or destroy) specific assets, has an influence on which type of change is feasible. Revolution may be unfeasible if important assets are to be preserved, e.g. in this case, presumably, the relationship with the customer since the intention is to adopt service logic. Regarding diversity, the local staff of industrial organisations such as SysCo, for instance, may identify more with their local organisation, and responsibility should be devolved there (cf. Balogun et al., 2004, p. 57). Powerful coalitions may sometimes block change, and in such instances, a directive management style may be feasible. However, when organisational support is needed, a participative approach may be more appropriate (Balogun et al., 2004, p. 91).

3.3.3 Research model and question

The frame of reference of this research is illustrated graphically in Figure 3 below, and a research question is formulated after that. The model should not be seen as a causal model with dependent and independent variables, rather as an attempt to

²⁶ Power can be defined as the “ability to act or produce an effect” (Merriam Webster Online Dictionary, www.m-w.com), or “the possession of controlling influence” (RhymeZone, www.rhymezone.com)

grasp the complexity of externalisation, with multiple and circular dependencies (cf. Pettigrew, 1990).

In summary, simultaneously externalising basic services and adopting service logic is inherently associated with a number of contextual features and leads to a number of vital challenges. These challenges may lead to problems during the externalisation process. They may be moderated by an appropriate change approach, i.e. one that is adjusted to the context. Solved and unsolved externalisation problems may serve as the starting point for readjustment of the initial intentions.

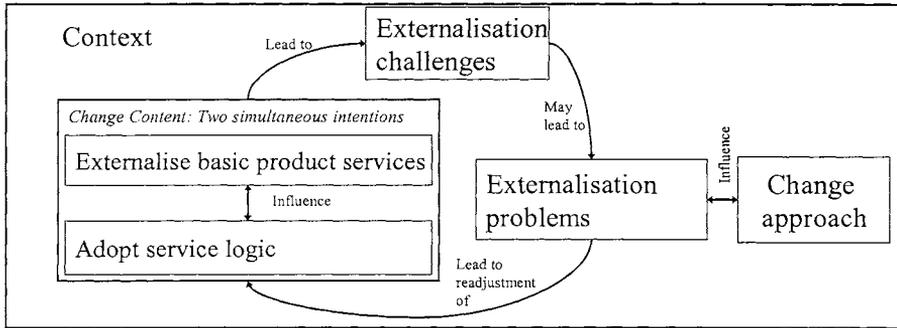


Figure 3. A model for studying externalisation problems and the factors that influence them

To be able to fulfil its purposes, this thesis explores externalisation problems encountered during several externalisation projects conducted by one industrial firm. To supplement this, it also explores problems encountered during the adoption of service logic associated with the externalisation of basic services.

In line with the purposes and the frame of reference illustrated in the model above, the research question in this thesis is:

RQ: How and why is the externalisation of basic services influenced by simultaneous intentions to adopt service logic and externalise basic services at industrial firms?

More specifically, this thesis intends to answer *how* (in terms of externalisation problems and change approaches) the externalisation process is influenced by these two intentions as well as *why* (in terms of change contexts and change approaches) problems emerge during externalisation in such a situation.

The externalisation problems identified in this study are summarised in Chapter 5 and further discussed in Chapter 6. Pivotal contextual features that can be expected include the increasing level of technological complexity and the commoditisation of technology, which are among the fundamental reasons why services are being externalised and service logic adopted in many industries. Contextual factors are discussed in Section 6.2 and change approaches in Section 6.3.

CHAPTER FOUR

Methodology

In this chapter, the process is described by which the five papers included in the thesis were crafted, and in particular how the thesis was crafted.

4.1 A patchwork case study

This thesis integrates several cross-sectional, retrospective, and longitudinal case studies which have been conducted at different points in time within the same organisation, i.e. SysCo, see Figure 4 below.²⁷

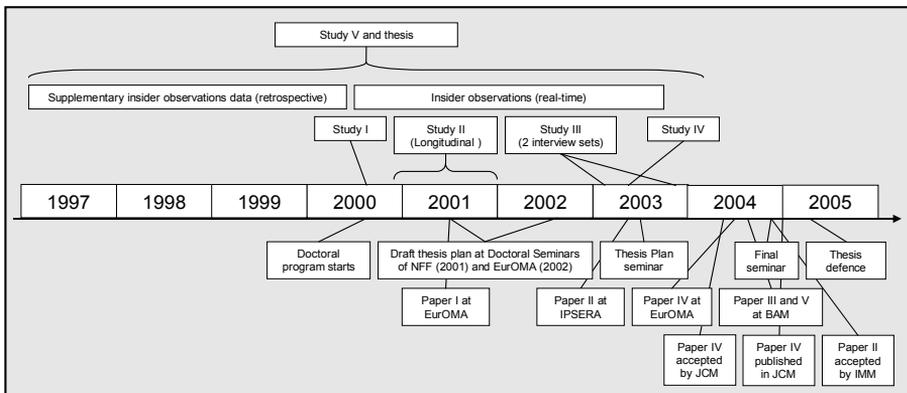


Figure 4. Overview of the research conducted

SysCo is the fictional name of a multinational company selling high-technology products to business customers. Although still primarily product-oriented, it is increasingly focusing on services as a way of competing. Most of the research data was collected from the service organization at SysCo's head office in Europe, where the overall responsibility for product management and strategies, for instance, resides.

²⁷ One study featuring data from other firms was also conducted, see Paper IV, but this will not be described in detail here.

The reason why this research design was chosen is to be found in the nature of the research question as well as in the nature of my role as an industrial researcher employed by SysCo and active in the research programmes of Fenix²⁸ and at the Centre for Innovation and Operations Management. Both these research programmes have an interdisciplinary and applied managerial orientation. Much of the research is carried out in close collaboration with industrial and other organisations, over long periods of time when researchers actively take part in the change processes.

Given the desire to explore problems associated with the process of externalising basic services, and to achieve an *understanding* of this process, qualitative case research was natural. Case studies are often recommended when the aim of the research is to achieve a holistic understanding of the studied phenomenon (Voss et al., 2002). It is also suitable for building or modifying theory (McCutcheon & Meredith, 1993). The benefits of case research include facilitating the identification of new variables and relationships that were not included in the previous theory (McCutcheon et al., 1993), and the fact that it is better than alternative methods when exploring “holistic explanations within and between cases” (Pettigrew, 1997, p. 341). This matched the relatively broad interest I had in exploring problems during the externalisation process, together with their sources. It is unlikely that survey research, for instance, would provide data rich enough to be appropriate when investigating such a complex and multifaceted phenomena as the externalisation of services.

Gaining access to empirical data from SysCo, and being employed there as a process manager in the Partnering and Sourcing Department of its service organisation, further motivated my choice of conducting case study research at SysCo and was, perhaps, the most important reason for choosing the empirical base. Moreover, it has been a key ambition of mine, when researching, to contribute to practice, and this was emphasised by my practitioner role at SysCo during the study. This led my interest towards investigating in-depth a phenomenon happening in my immediate area at SysCo, i.e. the externalisation of services. Furthermore, given the exploratory character of the research-question, aimed at studying the complex relationship between contextual features, the change approach, and problems during externalisation, *inductive* case research (cf. Eisenhardt, 1989) was selected as the basic methodology. This meant that the research was based on an empirical issue and that the conclusions were primarily built on the empirical data. In this thesis, understanding of the studied phenomena was developed gradually by the process of externalising services, in general, and by the problems and challenges related to it, in particular, grounded in the empirical data collected.

²⁸ For a description of what it means to be an industrial researcher on the Fenix research programme, see Hart and colleagues (2003).

Knowledge was accumulated from several longitudinal and cross-sectional studies conducted at different points in time, each investigating the process from slightly different angles and at different points in time. These studies resulted in Papers I-IV; together they also functioned as input for the more general Paper V and culminated in this thesis. Since the different studies were conducted at different points in time, Paper V and the thesis have become *longitudinal*, just like study II is in itself. Jensen and Rodgers (2001) denominate such studies “patchwork case studies” and are of the opinion that such studies have the advantage of creating a relatively “complete and holistic picture of the dynamics associated with the entity”, but they are limited since they only focus on one entity. Furthermore, according to Voss and colleagues, longitudinal studies can facilitate analysis of the causes and effects, which is more difficult to do in retrospective cases (Voss et al., 2002), and this suited the purpose of exploring problems during the externalisation process, and the sources of the problems. Longitudinal case research conducted in real-time also facilitates the study of sensitive issues and problems, such as politics and conflicts, which respondents tend not to mention openly (Rhenman et al., 1970).

Moreover, the purpose was to explore a contemporary phenomenon and to build theory rather than to test it. Given such purpose, research focusing on a limited sample can be more fruitful than, for instance, conducting research on large scale samples, using quantitative surveys (Voss et al., 2002), because it enables a deeper analysis.

4.1.1 Unit and level of analysis

The *unit of analysis* used in the research is the externalisation projects where service alliances have been implemented. The focus was on the part of the externalisation projects belonging to one of the actors (SysCo), and in particular with regard to the role of SysCo Services. In Paper III, the unit of analysis is instead the service logic adoption process, and how externalisation influences this adoption process, but with the goal of contributing to the purposes of the thesis.

Externalisation projects are analysed on two *levels*; firstly on the level of the individual project(s) (Papers I-IV), and secondly on the level above the individual projects; the organisational level or the level of the portfolio of externalisation projects (Paper V and the thesis). The reason for using these two levels emerged during the research in step with the interrelationship between different externalisation projects becoming evident.

4.1.2 A note on the insider role at SysCo

Since I was an employee of the studied firm during the research and wanted to collect data as well as support ongoing change processes at this firm, e.g. the externalisation process into service alliances, the research approach bore some of

the characteristics of clinical research (Miller & Crabtree, 1994, Schein, 1987, Stymne, 1970). For example, SysCo decided the general focus of the research programme and my participation in it. The research focused on change that was happening in real-time, while the research methods followed on from the setting and the research question. Furthermore, I continuously discussed the research with different managers at SysCo in order to gain their commitment and support. However, in contrast to clinical research, I mostly decided about my specific research focus myself and I was more of an ethnographer who studied alliance projects than a real member of the alliance projects.

My formal role at SysCo was not directly connected to the externalisation projects I was studying, although closely associated with it. I myself was the project leader of one alliance project during 2003. Thus, I contributed to the organisation (SysCo) as an employee but the tasks I had were not directly related to the research projects. They provided some input for the research and were also to some extent able to gain from the knowledge achieved through my being a researcher, e.g. knowledge regarding potential problems associated with externalising services. I did take notes regularly during this project and inserted them into my database in NVivo, but the majority of the data for this thesis came from other projects.

Furthermore, several of my closest colleagues were project managers of externalisation projects. This proximity to the studied phenomena offered excellent opportunities for informal discussions during lunches and coffee breaks, in particular with regard to different alliance matters. This also facilitated my sensemaking process, as well as my understanding of the context.

Overall, my assessment is that my research benefited from the insider role since this enabled the gathering of several sorts of data. I also believe that being a member of the studied organisation enabled an understanding of the problems and challenges associated with externalisation, from the perspective of the employees at SysCo. Both the approach and the insider role enabled the studying of change processes in real-time, something that entails several advantages as regards reconstructing the same thing after the event. Asking people after the event has happened is an approach that risks biased views of what actually happened.

There are also some potential drawbacks to being an insider working in the studied organisation. For example, there may be a risk of “naïve subjectivity” as an insider working in the studied firm (Reason, 1993). Ethnographers mention the risk of being too close to the studied organisation, or “going too native” and not being able to reflect critically on one’s observations. Such risks may lead to biased conclusions if they are not taken into account. Consequently, I tried to stand back a bit and reflect critically on the data and conclusions as much as possible, without standing *too* far back and becoming completely disconnected (cf. Irwin, 1987). I believe that it was beneficial to the study that I did not have a more formal role in the studied projects, as this may have made it more difficult to reflect critically on

the data. The role which I had enabled proximity to the studied object without becoming too close and risking, for instance, glorifying or romanticising the studied organisation or people (Irwin, 1987). Moreover, during the last year of my research, I became an outsider with no formal connection with SysCo, thus a slightly more critical outsider perspective was made possible.²⁹

4.1.3 The process of empirical inquiry and the evolution of the study

The research process can be described as an iterative and creative cycle of induction and deduction. The initial question was gradually elaborated and answered through a combination of retrospective and longitudinal cases followed over time. I iterated between periods when I gathered and analysed empirical cross-sectional or longitudinal data associated with externalising services in order to find patterns and periods where I primarily reviewed previous literature and tried to apply it to the data that I had already gathered. Through the research process, I gradually built up both my empirical database, my understanding of patterns in the empirical data, and changes in the empirical data, regarding how SysCo managed its externalisation process, for instance. To enhance my understanding of the empirical data, I also analysed how the data related to previous theories and empirical research studies. This approach may be called abduction (see, for instance, Alvesson & Sköldbberg, 1994) and is similar to Pettigrew's (1997) description of the typical nature of process research, as well as, for instance, Hoepfl's (1997) more general description of qualitative research, Daft's (1983) "craft of organizational research", and Orton's (1997) "iterative grounded theory". Such an approach can be beneficial when the research is holistic and focuses on relatively uncharted waters. At the same time, it takes advantage of previously developed theory and insights grounded directly in the empirical data. To illustrate the nature of my research, it is described in a sequential manner below, wherein the iterative nature is implicit.

I started my research with a relatively broad focus on the externalising of services and the problems associated with this. Such a broad focus permits a relatively unbiased view and the gathering of rich data during the earlier stages of the research (Eisenhardt, 1989), although it is, admittedly, also a bit shallow. Hypotheses and theories were developed and included as the research proceeded. Furthermore, I consciously triangulated between several data collection methods, e.g. interviews and observations, in order to achieve a more holistic view of the studied phenomena (Jick, 1979, Patton, 1987). Table II provides an overview of the studies, the papers, and the thesis. For more details of data collection and sources, see Section 4.1.4 on page 2.

²⁹ See also the section on the quality of the research, viz. Section 4.4 on page 2.

Table II. Overview of studies, papers, and thesis

Number of study	Mainly reported in	Unit of analysis	Level of analysis	Case(s)
I	Paper I	Externalisation project	Project	11 externalisation projects
II	Paper II	Externalisation project	Project	1 externalisation project (longitudinal)
III	Paper III and V	Adoption of service logic	Project	One case of adopting service logic, several externalisation projects
IV	Paper IV	Alliance structure and context	Project	5 firms (SysCo and 4 other industrial firms)
V	Paper V and Thesis	Externalisation project	Organisation	Patchwork study

During the initial study (**Study I**), several instances of externalising product services, or trying to, were investigated retrospectively (Paper I). One purpose of this initial study was to generate hypotheses and tentative conclusions and theories for further examination in subsequent studies.

After this study, my understanding of the problems of externalising services was better than before, and a paper had been written (Paper I). However, I was not completely convinced that we had found the answers, or that we had avoided the post-rationalisation problem. Thus, I decided to search for an ongoing alliance project that I could follow more closely and longitudinally, and I soon found a suitable case in a pilot alliance project for training services (Paper II) where problems associated with externalising services could be explored in more depth (**Study II**). Relatively soon, I realised that this project was full of internal conflicts related to the externalisation, and I decided to focus on conflicts in this study, as a method of understanding the important elements of the externalisation process. In other words, conflicts in the alliance were seen as manifest illustrations of important organisational problems. This study resulted in Paper II.

A common problem area in these first two studies was the theme related to the customer relationship, and the fear of losing this to the supplier. Gradually, I came to realise that the customer relationship problem and the externalisation project were closely related to the adoption of service logic, and that the externalisation of services was a potential enabler of the adoption as well as a potential obstacle to it. However, there was no consensus regarding the interrelationship between the two changes, the adoption of service logic and the externalisation of services, neither for the employees of SysCo nor for me as a researcher. Neither was a satisfactory answer to be found in the literature.

Consequently, in the next study (**Study III**), the unit of analysis was changed from the externalisation project to the process of adopting service logic, as well as how externalisation influenced this adoption process. The purpose of this was to increase the understanding of how the externalisation of product services was interrelated with the adoption of service logic, with the overall aim of gaining knowledge of externalisation problems. This study was based on interviews conducted on two occasions, ten months apart. The reason for this approach was that it facilitated the identification of problems during the adoption process, as well as the countermeasures taken, which was the main focus of the study. This study primarily resulted in Paper III, but it also contributed to Paper V.

At the same time, I was having discussions with some of the managers at SysCo about a comparative cross-firm study, since they were convinced that SysCo could learn from other firms and other industries, and that the research-networks of other firms should be exploited. Consequently, **Study IV** was conducted with the dual aims of meeting the expectations of those managers and gathering data which would be of use in an article related to the subject of the thesis. The idea was to generate data on externalisation problems and change approaches that could increase the external validity of the findings from the single firm SysCo. It was, however, difficult to obtain reliable data on the externalisation processes; instead, I obtained data on the structure of the service distribution channel and on problems related to this structure.³⁰ This was useful since it enabled me to write a paper on the frequently discussed issue of whether or not to externalise the customer interface. (Paper IV).

Finally, in order to deepen my analysis of the sources of the problems, in order to fulfil the second purpose of the thesis and satisfy the need for actionable knowledge for managers, the perspective was raised from the level of the individual externalisation project to the one above that, and all the previous studies were analysed together. In doing this, I was trying to learn some lessons regarding how the challenges of externalising services could be managed. This final phase of the thesis work (**Study V and the thesis**) has focused upon summarising and interpreting the research results from the perspective of the research model, searching for cross-case patterns, making sense of all the gathered data, and compiling it into this thesis. The results of this study are reported both in Paper V and in this thesis.

In Figure 5, the main contributions of the papers constituting the thesis are illustrated and positioned in the research model.

³⁰ One employee at Beta laughed when I asked if I could see their implementation process, and denied me access because it was, as he put, “intellectual property” to them.

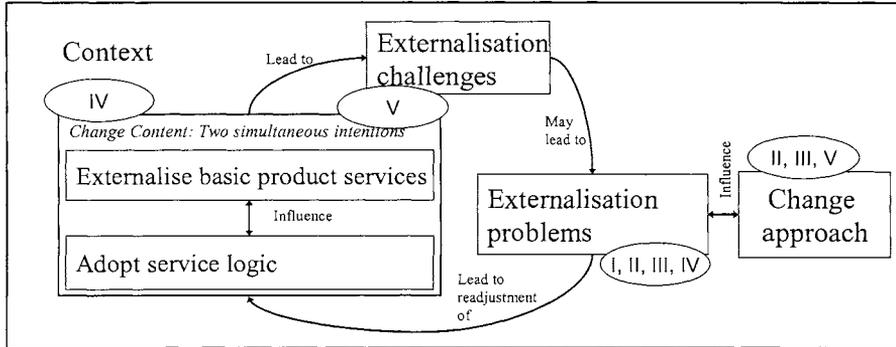


Figure 5. The main areas of contribution to this thesis made by the papers

4.1.4 Data gathering and sources

The vast majority of the data was collected via interviews, of which the majority were semi-structured and tape-recorded. For most of the interviews, formal interview guides³¹ were used, typically containing general questions, as well as questions adjusted to the focus of the specific study. During the more open-ended and unstructured interviews, a less structured interview guide was typically used, or just a few guiding themes around which the interview centred. In total, 92 interviews were conducted with 63 informants, of which the majority were semi-structured, with some being either structured or unstructured³². Eisenhardt (1989), for example, recommends keeping the research relatively broad and open during the early stages of case research in order to avoid bias and to permit the gathering of rich data which can subsequently be analysed. Especially during the initial studies, as well as during the initial interviews of each study, I worked in accordance with this advice. Gradually, however, the focus became narrower and the interviews more focused. Figure 6 below provides an overview of when the interviews were conducted, while more details can be found in the appended list of interviews.

On average, the semi-structured and structured interviews lasted for about one hour, ranging from about twenty minutes to two hours. A few of the more informal, and unstructured interviews were shorter, down to just ten minutes.

The choice of informant was based on his or her current and previous positions, as well as how I deemed the person capable of providing the relevant and supplementary perspectives that would yield richer empirical data suitable for answering the research question, e.g. relating to the strategic intentions, the change approach, the extent to which the intended changes were realised, and the problems associated with realising them. All informants were, or had been,

³¹ For an example, see Appendix 1.

³² The complete list of interviews can be found in Appendix 2.

involved in projects wherein services were being externalised. Employees from different levels and functions were deliberately selected; e.g. senior and middle managers, project managers, non-managerial staff, employees from staff functions, engineers, and human resource managers; in order to obtain a more holistic perspective.³³ Although this had the potential to complicate the research and give me a more complex set of answers, my ambitions to understand in-depth the externalisation process and its complexity justified this choice. The informants were typically asked about their suggestions for further informants. Moreover, almost none refused to be interviewed.

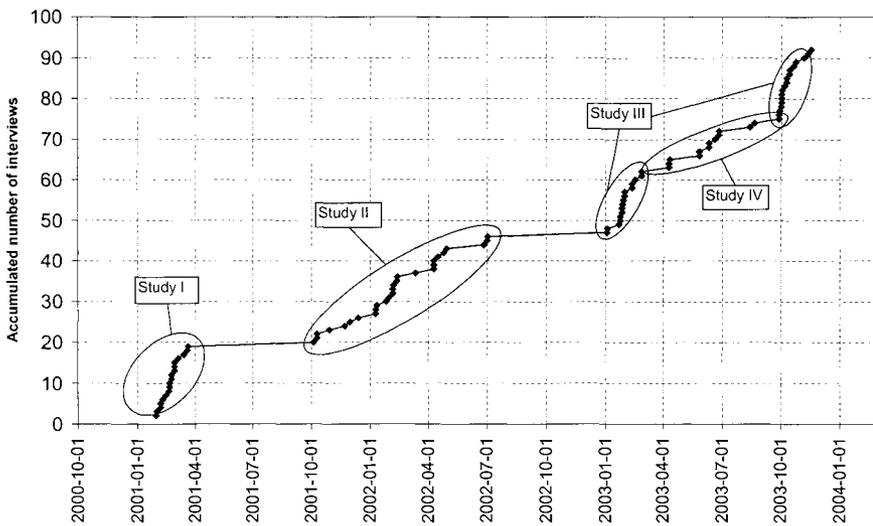


Figure 6. Overview of when the interviews were conducted

The data gathered during the interviews can be classified as “presentational data”, which, according to Woodside and Wilson (2003), is often;

“ideological, normative, and abstract, dealing far more with a manufactured image of idealized doing than with the routinized practical activities actually engaged in by members of the studied organization”

I tried hard to avoid obtaining only idealised descriptions from the informants, e.g. by being provocative, confronting the informants with real examples, and asking for stories from personal experience. Nevertheless, I recognised the need to supplement the interviews with secondary sources, e.g. ethnographical observations from meetings as well as discussions and documents. The documents read include business plans, strategies, process descriptions, company magazines, operational plans, intranet information, and the minutes of meetings. Such evidence was used primarily for my own sensemaking process and as a supplement

³³ Although many of the respondents had a job title containing the word “manager”, they were often the managers of *tasks* rather than the managers of *people*.

to the interview data, but it was also, to some extent, used more directly during the analysis (e.g. in Paper II). The insider role also provided access to extensive documentation.

A questionnaire³³ was used as part of the evidence for Paper II, administered to eight employees of SysCo Services and two of Teach IT (the training partner of SysCo during the studied alliance project) in order to quantitatively indicate the degree of conflict and to also conduct a qualitative assessment of the state of the project.

4.2 Data analysis

As I have already mentioned, my research can primarily be described as inductive and iterative, meaning that I went back and forth between data and theories, starting with the individual studies and papers and a focus on externalisation problems, ultimately reaching the final conclusions based on the results of the individual papers and a focus on problem sources and change approaches. To increase the credibility of this research, I will describe here how I conducted the analysis, but on an aggregate level. More details can be found in the appended papers.

Interviews constituted the core of my empirical data, with almost all of them being taped and transcribed in detail and linked to NVivo, a computer-based text analysis program. The ethnographical observations, as well as the preliminary conclusions, reflections, and ideas, were also linked to NVivo, and arranged in chronological order. In NVivo, I differentiated clearly between different categories of data, such as my own reflections and what people literally said. Such carefulness when taking and ordering field notes can increase the reliability of the research (Kirk & Miller, 1986). One advantage of using NVivo during explorative studies is that it enables the flexible and unprejudiced creation of nodes, and the gradual creation of an understanding of the studied phenomena (Nittmar, 2000). The flexibility of the tool, as well as the different search possibilities built into it, enable creativity when doing research.

In general terms, I iterated between within-case analysis, where individual alliance projects were analysed, to cross-case analysis, where several projects were analysed, during my research, as I steadily gathered data from more and more cases.

To give a concrete example of how the analysis was carried out, I had the summaries of the papers (see Chapter 5 on page 65) and all the complete papers available in printed format on a desk and based on these documents, I summarised the problems in a table (Table VI on page 76). I also analysed all the interviews in

³³ The questionnaire is inspired by Van de Ven and Ferry (1980), Jehn (1995, 1997) and Jehn and Mannix (Jehn & Mannix, 2001), and is available in Appendix 3.

one single NVivo data file and analysed them one more time using previously developed codes as guidelines. The goal of this analysis was to find problems and challenges that were common to the different papers and the different studies, independently of, for instance, the type of alliance studied.

Furthermore, I created a rough timeline containing different excerpts from interviews, as well as more anecdotal data gathered by me as an ethnographer and an employee of SysCo (see Table V on page 2). The purpose of this was to analyse changes and search for patterns in service and sourcing strategy, as well as the approach to externalising services.

Reports, documents, and other qualitative materials, together with a quantitative survey of the conflicts and other aspects of externalisation processes (Paper II), supplemented the interviews and the ethnographical observations, but were not linked to NVivo and thus not coded. This type of data primarily aided my sensemaking process, being used to crosscheck the data from the interviews. It enhanced my understanding of, for instance, the context, strategies, and externalisation problems.

4.3 Description of the empirical base

In this chapter, the studied externalisation projects are presented, together with an overview of the firm at which they were carried out. Apart from studying externalisation projects, and the adoption of service logic at SysCo, interviews were also made at four firms in other industries. These firms are described in Paper IV, and will not be described here. In Paper IV, SysCo was called “Gamma”.

4.3.1 Overview of SysCo

This study was conducted as case research at SysCo, a multinational systems provider with its head office in Europe. SysCo has been active in its field for over 50 years. It is listed on the stock exchange and currently has over 10,000 employees.

SysCo can be classified as an “infrastructure business”, i.e. an industrial firm involved in developing, manufacturing, and delivering infrastructure. SysCo may also be grouped under “complex manufacturing industry”, consisting of industries where products are typically composed of several specialised technologies manufactured by several different firms, and assembled and integrated by the firm (Nittmar, 2000). The goods that SysCo sells to its industrial customers all over the world, generally using its own sales force, are relatively complex and typically worth more than \$100,000. Increasingly, systems solutions rather than stand-alone products are being sold, composed of relatively complex bundles of several different types of products and services. Most goods can be classified as specialties, although the share of commodities is increasing.

Product services account for a significant proportion of the firm's revenues, and the proportion is increasing due to the maturing market for its goods. In 2004, SysCo Services was one of the largest service providers in the industry, with around 30% of its workforce being service employees spread across the entire globe. A wide range of product services is offered, but this thesis primarily focuses on services such as repair, product support, product-oriented training, installation, systems integration, business solutions, full maintenance contracts, and managing customers' operations. The last three services are relatively new to SysCo and are seen as strategically important. Using the typologies suggested by Canton (1988), SysCo is mainly expanding its service business in its present-day market, using both current and new services, although discussions are also taking place regarding entry into new markets. External technology is increasingly becoming integrated into the systems used in SysCo's products. SysCo is collaborating with external firms concerning the delivery of several types of product services.

4.3.2 Market and organisational changes at SysCo

During the period when this empirical research was being conducted, i.e. between 1997 and 2003, the industry to which SysCo belongs underwent a number of changes, suffering a severe financial crisis. There are several reasons for this crisis. One reason given was that the whole industry was making false predictions about sales growth, partly based on statistics in a report published by America's Department of Commerce in April 1998. This report, although largely incorrect apart from a brief period during 1995-96, led to a rush to invest and tremendous, but false, expectations. After a few years, in 2000, the bubble burst, and the prices of products bought from firms such as SysCo suddenly started to fall sharply, in an attempt to increase sales. Nevertheless, nothing could stop a dramatic drop in sales, prices, and share prices. Some firms went out of business. After the crash, the industry that SysCo belongs to has concentrated on activities such as restructuring debts, cutting costs, downsizing, and installing new management. The structure of SysCo has become flatter and decisions have been centralised.

Another reason for the problems experienced by many traditional firms in the industry that SysCo belongs to is that barriers to entry have been diminished in several areas, e.g. R&D and services, because an increasing share of the products integrated into the systems offered by SysCo have become commodities and are thus available off-the-shelf. Some Electronic Manufacturing Service (EMS) firms have started to design products as well as build them, and have thus become competitors to SysCo in some areas. Furthermore, a flourishing ecosystem of specialised service providers has emerged, specialising in various areas related to development as well as service delivery, and facilitating the externalisation of such activities.

However, even during this financial crisis in SysCo's industry, services flourished both in relative and absolute terms, and the focus of firms like SysCo changed due to the sudden attention being paid to services. While sales of products stagnated during the period, sales of services such as product support continued relatively unchanged (even increasing in some cases) as customers strove to keep their current product portfolios up and running, instead of updating them with newer products.

Many firms in the industry, including SysCo, were intensively trying to introduce more advanced services, such as solutions and full maintenance contracts, which would expand margins, stabilise revenues, and differentiate firms from their competitors. For the clients, this was expected to lead to simpler operations and cost savings, for instance. This meant that services like solutions were suddenly becoming very hot, as well as integrating forwards in the value chain and managing customers' operations. At the same time, efforts to reduce costs were also touching the services sections of firms like SysCo, as well as manufacturing and R&D, with alternative organisations for delivering services being introduced. Different sorts of alliances were emerging at an increasing pace between firms like SysCo and various service suppliers, and the externalisation of services was suddenly hotter than probably ever before. Within SysCo Services, these various externalisation initiatives were also being debated as some employees perceived them as a threat to their jobs. Some even saw them as a threat to the entire business operation of SysCo.

4.3.3 The studied externalisation projects

Data from several externalisation projects was included in the research. Some respondents talked solely about one specific externalisation project; for example, the respondents in Study II were all talking about the ongoing training alliance project between SysCo and TeachIT. Other interviews were revolving around the externalisation of services in more general terms, including the difficulties associated with it, based on the sum of their experiences of externalisation. For example, some respondents talked about several specific externalisation projects, a few others talked more generally about their experiences, without mentioning any specific externalisation projects, in spite of our attempts to get respondents to be specific and give examples of their practical experiences at SysCo. As there was no clear one-to-one relationship between the interviews and the different externalisation projects, however, it is difficult to list the studied projects exactly.

The majority of the studied projects concerned the delivery of basic services, i.e. services correlated with service space A, although interviews were also conducted with regard to alliances associated with services in the other service spaces, see Figure 7 below.

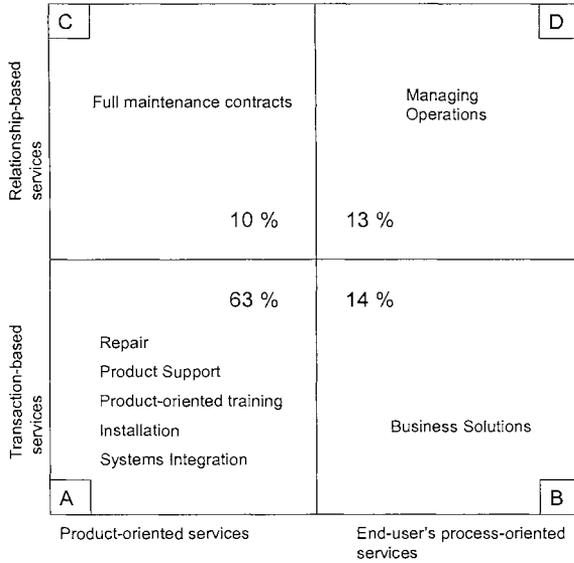


Figure 7. The services for which externalisation was studied (N=percentage of the interviews focusing on each service space)

Most of the alliances resulting from the studied externalisation projects were of a relatively operational nature and were governed by contracts. Moreover, a few of the alliance initiatives that were discussed during the interviews never reached the stage where a contract was signed. Furthermore, the externalisation projects generally took several months to carry out, sometimes years.

Another important aspect worth mentioning of the studied externalisation projects is that SysCo wanted to structure its alliances as “simple supply chains” meaning that SysCo strove to adopt a structure in its service distribution chain whereby SysCo itself retained the relationship with its customers and had the suppliers of service processes located behind it in the chain. In other words, SysCo primarily used, though not always, what is sometimes called “direct” service channel structures, as opposed to “indirect” ones.³⁵

In total, 63% of the respondents in the interviews (see Appendix 2) talked primarily about alliance projects and other aspects of service space A, 14% about service space B, 10% about service space C, and 13% about service space D.³⁶ Thus, the vast majority of the empirical data gathered via interviews concerned service space A, and the externalisation projects pertaining to those services.

³⁵ A more in-depth discussion of how to structure service supply chains can be found in Paper IV.
³⁶ In spite of the descriptions of the respondents in the appendix, which often contain the term “manager”, many of these were staff responsible for certain tasks and not line managers.

While the services for which alliance projects were studied can all be classified as product services, they are also different and can, for instance, be grouped under all the different service categories suggested by Silvestro and colleagues (1992), i.e. professional services (e.g. training), service shop (e.g. installation), and mass-services (e.g. repair). One advantage of this relative breadth of the empirical base of the study is that interaction effects can more easily be studied; for instance the effects of training alliances caused by installation alliances. Depth, on the other hand, had to be sacrificed somewhat. This probably also provides a more realistic picture of the challenges and problems on the corporate level. As this thesis will reveal, this breadth proved to be important.

4.4 Quality assessment

There are two fundamental criteria for assessing the quality of research: reliability and validity. Reliability is the extent to which the study's operations are correctly made and can be repeated with the same results (Yin, 1994, p. 33), however and whenever this is carried out.

The validity of the results of qualitative research lies in whether the instruments used actually measure what they are supposed to measure (Emory & Cooper, 1991) or in the extent to which they give the correct answer (Kirk et al., 1986, p. 19). The issue of validity in qualitative research is "a question of whether the researcher sees what he or she thinks he or she sees" (Kirk et al., 1986). To increase the validity, multiple sources of evidence are typically used (Yin, 1994, p. 33).

According to Morse and colleagues, "collecting and analyzing data concurrently forms a mutual interaction between what is known and what one needs to know. This pacing and the iterative interaction between data and analysis is the essence of attaining reliability and validity" (2002). My research approach was similar to this. For example, I conducted the interviews and made the observations over a longer time period, analysing the data and enfolding more theories during the whole course of the research.

I will now describe, in rather more detail, how I tried to increase the reliability and validity of my research.

4.4.1 Increasing the reliability

Although the longitudinal approach and the changes during the study in, for instance, contextual factors and strategies at one single firm may make it difficult to repeat the study with similar result at SysCo or at other firms, efforts were made to increase the level of reliability. All the papers were sent to the respondents for their comments to ensure that I had not misunderstood anything vital and to seek their views on my interpretations and conclusions. Most respondents, however, did

not provide any feedback. However, workshops were also held with the key informants to discuss some of the papers, and I generally received support for my conclusions. The final results of the thesis, including the identified problems and their sources, were also discussed with some of SysCo's employees. In general, they supported my interpretations and conclusions. The final interpretation was always mine, however.

During the interviews, probing (Van Maanen, 1979) was used, by asking the respondents for explanations and interpretations of the observations and of my tentative interpretations and conclusions. Several types of triangulation were also used; data triangulation, where different sources of information were used (e.g. by supplementing the interview data with printed material such as business plans), methodological triangulation (e.g. by supplementing the qualitative methods with quantitative surveys), and investigator triangulation (my tutors conducted several interviews and also contributed during the analysis).

In spite of these measures, there might still be a risk that I have not been able to reflect and question things sufficiently (cf. Coghlan & Brannick, 2001), and that I have tended to want to satisfy the urgent needs of the organisation rather than long-term issues. Managing organisational politics is also a critical issue for an inside researcher (Coghlan et al., 2001); by employing an insider/outsider (I/O) team research approach (Bartunek & Louis, 1996), and by involving external researchers in my studies, e.g. my tutor(s), the main weaknesses of the role could be dealt with, at least to some extent. One role of the outsider was to reflect critically on the data and the conclusions drawn by me as an insider.

As I was not formally involved in the studied externalisation projects, I could relatively freely make my own (critical) interpretations, independently of the organisation's needs, still taking advantage of my relative proximity in terms of access to data and a potentially better pre-understanding. Moreover, almost all the interviews were recorded and directed by interview guides, like the one in the appendix and, sometimes, less detailed ones. Most interviews were transcribed in detail. According to Voss and colleagues (2002), observer bias can be dealt with, at least to some extent, by recording almost all of the interviews and by using a structured research protocol

An audit and a transparency approach to field notes and interview transcripts can also increase reliability (Mason, 1996). Although I have not asked an independent judge to review the tapes and notes, as Hycner suggests (1985), all the research material is available if anyone would like to scrutinize it. Furthermore, the level of reliability, or dependability, can be increased by means of rigour during the research process, i.e. the way the observations are made and how the researcher keeps track of the gathered data (Kirk et al., 1986). I tried to be rigorous by using NVivo during my research as a tool for keeping track of all the data, including interview transcriptions and observation notes.

4.4.2 Increasing the construct and internal validity

According to Guba, credibility, which is an alternative term to validity, can be increased by letting peers corroborate tentative findings, by having frequent and thorough interaction with informants as information develops, and by participant evaluation (Guba, 1978). Since I was an insider at the studied organisation, frequent interaction with informants was unavoidable, possibly increasing the corroboration and hopefully also the credibility/validity of the research.

Triangulation between data sources is a way of increasing the construct validity. Accordingly, interviews were conducted with respondents from several different units and levels within the organisation. However, interviewees sometimes adjust their answers so that these convey what the interviewee wants to communicate, rather than what has actually happened, for instance. The answers given may also be misleading because of the time that has elapsed between the actual event and the interview, making it difficult for the interviewee to remember. Supplementing interviews with real-time observations, written documents, and a quantitative survey (Paper II), enabled an increase in the construct validity of the research, and the avoidance of some of the negative aspects of conducting interviews, such as the simplified and biased answers that the interviewees might give. Furthermore, given my interest in the problems arising during externalisation, as well as the sources of these, the observations were conducted over time, which increased the internal validity as it facilitated the tracking of cause and effect, e.g. in terms of the change approach and the effects of this.

4.4.3 Increasing the external validity

Although this study is based on data gleaned from several externalisation projects, and many different respondents, it is almost exclusively limited to one single firm in one specific industry. Thus, it is difficult to make generalisations reaching beyond this firm and its associated industry. However, it is likely that the results are also valid for, primarily, similar firms in the same and similar industries, i.e. relatively large and mature multinational firms involved in the development and delivery of complex products, supplemented by product services, to industrial customers, and which are about to go further downstream.

Furthermore, the study was conducted during a severe downturn in the economy, which may have affected the results. However, it can be expected that similar dynamic conditions and insecurities will also exist beyond this specific downturn. It is thus not entirely unlikely that the results are fairly generalisable, in spite of this.

There is another limitation in that, for SysCo, the externalising of services was a relatively new phenomenon, which made projects more exploratory in nature. Furthermore, the industry that SysCo belongs to was in the midst of a dramatic

change during the study and the position and role of the involved firms was very uncertain.

Bearing these aspects in mind, generalisation to more stable environments should be done with care. However, if we are to believe Bettis and Hitt (1995), for instance, it can be expected that situations such as the one experienced by SysCo will be commonplace in the future. According to these two authors, the “new competitive landscape” of the twenty-first century will be characterised by increasing risk and uncertainty and decreasing forecastability, due to increased dynamism, an increasing rate of technological change, the increasing use of computer and telecommunications technology, and an increasing level of knowledge intensity.

Nevertheless, through analytical generalisation (Yin, 1994, p. 30), or by comparing these findings with observations from other studies and associated theories, external generalisation may be increased slightly. Such comparisons are made, both with regard to the externalisation problems and their sources, in the final chapters of the thesis.

Perhaps more importantly, by describing the studied cases in as much detail as possible, given, for instance, space and confidentiality constraints, including the actual externalisation processes and the firm at which the externalisations were carried out, generalisation to similar settings becomes somewhat simplified. It is, however, primarily up to the reader to judge whether generalisation is possible or not (cf. Åhlström, 1997, p. 58). Similarly, Kennedy argues that the range of generalisation simply cannot be known to the researcher studying single cases, even though such a range would exist. Moreover, she claims that, for single case studies, judgements about the range of generalisation should be left to the receivers of the information. The researcher should produce and share the information enabling this judgement (Kennedy, 1979). Consequently, I have tried to present as much information as possible about the empirical data collected and the firm studied, as well as about the logic behind my conclusions. The decision to make the firm anonymous, however, has restricted the amount of detail that I was able to present vis-à-vis the firm.

CHAPTER FIVE

Summary of the Papers Integrated into the Thesis

In this section, the papers included in the thesis are presented, summarising their content, results, and conclusions. Each paper's contribution towards the purposes of this thesis is also commented on. Finally,, the challenges and their associated externalisation problems are summarised.

5.1 Introduction

The intention of this chapter is to stay relatively close to the empirical results of the studies. Problems encountered during externalisation projects and during the adoption of service logic are summarised, as are the results associated with the way in which the externalisation project was carried out, and should be carried out. This chapter serves as a starting point for the discussion in chapter 6, where the research question is answered on a more integrated level.³⁷

5.2 Paper I: Implementing service supply relationships

Given the relatively scarce amount of empirical research into the problems and challenges associated with externalising product services, this initial exploratory study was conducted to explore problem areas associated with externalising services. The research, which was based on 17 interviews held at SysCo Services, analysing eleven instances of implementing (or trying to implement) a relationship with an outside firm in order to provide service to the customer, resulted in four problem areas.

³⁷ Worth mentioning here is the fact that the terminology used in this chapter differs somewhat from the terminology used in some of the appended papers. The terminology used in the papers is adapted to fit their theoretical perspectives and the journal, whereas the terminology used here is sometimes aligned with that of the thesis.

The problems identified include, *firstly* and most centrally, the problem of maintaining, or the risk of losing, the relationship with the customer when service processes are being externalised. The other problem areas identified are also associated with this strategic problem, but on a more concrete level.

Secondly, it was problematic to write agreements with suppliers. Basically, this problem concerned how the agreements could be written in such a way that the benefits of the service business and the customer relationship were not jeopardised.

Thirdly, the problem of specifying service processes also concerned the customer relationship. One reason for this concern was that it was difficult to decide which processes the supplier should handle and which should be handled internally. Basically, this issue had to do with the strategic choice of service distribution structure and its effect on the relationship with the customer and the control of the service business. It was also a matter of change management. More specifically, there was resistance to the externalising of services among the employees of SysCo Services, in particular among the employees working operationally with the delivery of services. According to the interviewees, there was also ignorance, in particular among managers, as regards managing the internal implementation process and developing the service strategy and defining its associated processes.

The *fourth* problem area, handing over the actual point of service delivery to a supplier, was associated with doubts; in particular among employees who had been working operationally with the delivery of services themselves, regarding the suppliers' ability to actually manage the service processes. In some cases, for instance the repair of hardware, this was seen as a handicraft and something that had been learnt through years of experience. This issue is also associated with the problem concerning the relationship with the customer. Employees of SysCo Services were not happy to let their relationship with the customer go, and some of them also doubted that the customer would benefit from externalising the services to suppliers, which they in turn believed might hamper SysCo's credibility and relationship with its customers.

Comment: This paper primarily contributes to answering the "how" part of the research question. More specifically, the contribution of this paper to the thesis is the list of problem areas during the implementation of service alliances. Firstly, writing legal agreements for service exchanges. Secondly, clearly specifying processes to enable transferring them to suppliers. Thirdly, handing over the actual point of service delivery to a supplier. Fourthly, and finally, losing control over the relationship with the customer. Basically, the four problem areas provide a foundation for hypotheses for further research. Thus, this paper primarily functions as input for the subsequent studies making up the research.

5.3 Paper II: Identifying intraorganisational and interorganisational alliance conflicts

The extant literature on alliances tends to neglect the effects of intraorganisational relationships within each alliance partner on the implementation of the alliance. To address this gap in the literature, this paper investigates both interorganisational and intraorganisational conflicts occurring during the externalisation of customer training to an external education firm (for an illustration, see Figure 1 in Paper II). It aims to develop categories of conflicts as well as analyse how these conflict categories affect externalisation. To do this, a training alliance between SysCo and TeachIT was studied longitudinally, primarily from the perspective of SysCo and with myself acting as a participant observer. In the paper, conflicts in the alliance are seen as manifest illustrations of important problems with the alliance. Understanding these conflicts, as well as the categories of conflicts that are developed contributes to understanding externalisation problems.

Three interrelated categories of conflicts (inter- and intraorganisational), which may potentially hamper externalisation, are developed through analysing the data: 1) the scope of the alliance, 2) the customer relationship, and 3) the implementation process.

The first category, “the scope of the alliance”, had to do with differences in opinion regarding the scope of the appropriate alliance, or areas suitable for alliances, e.g. in terms of services and products feasible for externalisation to partners. One underlying reason for this was the perception that the alliance was a threat to the employees of SysCo. However, there were also employees who considered IT training to be one of the future core areas of the firm and an opportunity for high revenues in the future. These employees considered the scope of the pilot alliance to be “madness”, or completely inappropriate. Another pivotal concern was hardware products and systems feasible for training alliances. Involving an external partner in the development of courses for products and systems under development was considered a challenge due to the secretiveness of development activities. Another concern was the choice of products that were generating high or low revenues. Keeping the profitable areas in-house would decrease the prospects of the partner, and thus of the alliance.

The second category related to relationships with customers and the strategy and position of SysCo. Basically, the conflicts centred on the impact on the relationship with the customer of using external resources for IT training. IT was increasingly being integrated into the products offered by SysCo and, as noted above, was being perceived by some to be a cornerstone of both future product and service business. Thus, some employees of SysCo Services saw the need to develop IT competence internally, rather than to externalise it. Some traditional customers wondered if SysCo did not have the competence in-house, which could entail a

risk of diminished credibility for SysCo. Some employees of SysCo Services thought the alliance implied a risk of losing IT competence and, as a result, the potential loss of business to the partner. On the other hand, others saw the alliance as an opportunity to strengthen the SysCo brand.

The third category involved how externalisation was conducted and by whom. Basically, this conflict was about the inadequate involvement of employees at SysCo, and about the role of the pivotal Alliance Function³⁸ at SysCo Services. Employees working in the Training Function of SysCo Services were both irritated and astonished by the leading role that had been given to the Alliance Function, in some cases doubting the competence of the Alliance Function since it was partly recruited from outside the Training Function. However, when they were invited to participate in the development of an alliance strategy, they were not able to provide an agreed opinion on which processes and products were feasible for alliances. Thus, this conflict area basically concerned the way the change process was managed, as well as the difficulty of deciding on an appropriate alliance strategy.

On a general level, one conclusion standing in contrast to the majority of research into conflicts within alliances is that the vast majority of these conflicts were internal to SysCo. In other words, the internal problems were more severe than those occurring at the interface between the two alliance firms.

Comment: One contribution made by this paper to the thesis is that it provides details about problem areas during the externalisation of services, including their underlying sources. The paper focuses on conflicts as manifest illustrations of important problems during the externalisation of training. Thus, it is the underlying sources of the conflicts that are of particular interest here.

In essence, the underlying sources concerned the difficulties of determining the appropriate scope of the alliance and the perceived risk that the externalising of training would have negative effects on the relationship with the customer.

Furthermore, the way SysCo Services managed the externalisation initially; linearly (strategy followed by implementation) and top-down; did not seem to work very well and a more collaborative approach seemed to be necessary. The paper also provides knowledge of how the problems affect the externalisation process. Basically, they hampered it, although there were also positive effects. It seems evident from the research that the adoption of service logic can make the externalisation of product services problematic, due to the perceived negative effects on it. If services had not been perceived as being so important, the internal resistance and the conflicts would probably not have been as extensive. A different change approach might possibly also have been able to moderate the internal problems.

³⁸ A function set up at SysCo services to develop alliance strategies and manage alliance projects.

5.4 Paper III: Managing the process of adopting service logic in collaboration with suppliers

The literature on service logic has mostly focused on strategies, business models, and the benefits of delivering services, and has tended to ignore the problem of actually introducing it at industrial firms. To this end, the purpose of this paper is to identify issues encountered when adopting service logic at an industrial firm. A second purpose is to investigate how the externalisation of services affects the process of adopting service logic, i.e. how it leads to adoption problems, which is an area where very little empirical research has been done. Case research has been conducted at a multinational systems provider (SysCo) in the midst of the change process, introducing relationship-based and process-oriented services with the support of several suppliers and partners.

Several problems have been identified, divided into internal issues, downstream issues, and upstream issues, see Table III below. These groups of issues correspond to the challenges suggested in this thesis (the internal challenge, the customer relationship challenge, and the strategy formation challenge).

Table III. A summary of the issues identified during the adoption of service logic

Internal issues	Downstream issues	Upstream issues
<u>General issues</u> <ul style="list-style-type: none"> • Service and solutions strategy and offering • Service and solutions competence • Change management • Management system • Service operations <u>Externalisation issues</u> <ul style="list-style-type: none"> • Managing partners and suppliers • Contracting • Supporting externally-sourced products • Partnering strategy 	<u>General issues</u> <ul style="list-style-type: none"> • Customer perception • Customer demand difficult to predict • Marketing and sales process and customer interaction <u>Externalisation issues</u> <ul style="list-style-type: none"> • Losing customer relationship to suppliers/partners • Prime contractor role • Degree of outsourcing (full/partial) to retain power over the customer relationship 	<u>General issues</u> (also externalisation issues) <ul style="list-style-type: none"> • Collaboration with and between technology suppliers for the delivery of product support • Competition from suppliers and partners

Three main conclusions are drawn. *Firstly*, that the issues previously identified by Oliva and Kallenberg (2003) (see Table I in Paper III) may be generalised to include firms that have gone further in their adoption processes. *Secondly*, the externalising of services can be an important issue when adopting service logic and may impede the overall adoption of service logic. *Thirdly*, the strategy itself (the service strategy or the sourcing strategy) is an important issue; difficult to formulate and difficult to implement if formulated. In other words, it seems to be

difficult to formulate a strategy centrally and implement it in a sequential manner. A final conclusion is that a double-loop composed of a participative loop and an authoritarian loop seems to be a fruitful approach to managing the adoption process.

Comment: This paper contributes to answering the research question of this thesis, but from the perspective of the adoption of service logic. This paper contributes two things to the thesis: (1) knowledge of issues associated with adopting service logic at a firm that is also externalising services, and (2) suggestions regarding how to manage the adoption process so that the issues are dealt with. More specifically, the paper illustrates that the externalisation of basic services has entailed consequences for SysCo's adoption of service logic; including how and why it did this.

For example, some suppliers of basic services, e.g. installation and repair, were also aiming for the more advanced services corresponding to service spaces B-D (see Figure 1 on page 2), and were thus perceived as threats to adoption. Customers did not thus far perceive SysCo to be a competent solutions provider, since it had not had time to develop a history in providing solutions. There were other competing supplier firms that were considered more competent in providing advanced and consultative services, typically consulting firms and systems integrators. SysCo's response was to avoid these particular suppliers altogether.

In contrast to the conventional wisdom of externalising supplementary services or activities, where the firm does not have unique capabilities, to specialised service firms, this study has indicated the need for a more cautious sourcing strategy in order not to impede the overall adoption of service logic. A model is suggested for managing the adoption process (the "double-loop process"), which can be described as a repetitive process of a participative loop wherein information about the internal and external context was gathered and the commitment of the employees was gained, and a more authoritarian loop wherein more informed strategies were implemented. Such a model seems to be a fruitful approach to managing the adoption process, contributing to both the managerial implications part of the thesis and to the part concerning the change approach and its effect on externalisation problems.

5.5 Paper IV: Searching for the optimum product service distribution channel

One purpose of this paper is to develop a series of propositions regarding how product, market, and firm contextual factors influence the appropriate channel structure of product services. Another purpose is to identify organisational actions resulting from maladjusted channel structures. This paper is based on case research conducted at five firms in different industries (all firms are involved in the delivery

of goods to their customers, and to this end, they are also involved, to varying degrees, in delivering different product services).³⁹

In this paper, three central service processes are suggested in the channel for product services: (1) contracting: the purchase of the service by the customer and, perhaps, the signing of the service contract, (2) ordering: the ordering of the service by the customer, in line with previously arranged contracts, and (3) expediting: delivering the service to the customer. Each of these processes can either be direct (using the internal organisation to deliver the services) or indirect (using agents, retailers and third party service providers, etc.). Building on previous research, six propositions (P1-P6) are presented with regard to how the choice of direct/indirect process is influenced by structural contextual factors related to the market, the goods, and the firm itself, see Table IV below. The results of the case studies indicate that firms strive towards adjusting to the appropriate channel structure suggested by the propositions, or compensate for the maladjustment (deviations from the structure suggested by the propositions) by taking other measures.

Table IV. Effects of contextual factors on the service distribution channel

Propositions leading to direct processes	Propositions leading to indirect processes
P1a: For complex products, industrial firms will choose direct contracting and ordering processes for services	P1b: For simple products, industrial firms will choose indirect contracting and ordering processes for services
P2a: For specialty products, industrial firms will choose direct expediting processes for services	P2b: For commodity products, industrial firms will choose indirect expediting processes for services
P3a: For products with a low service intensity, industrial firms will choose direct expediting processes for services.	P3b: For products with a high service intensity, industrial firms will choose indirect expediting processes for services.
P4a: Industrial firms operating in business markets will choose direct contracting and ordering processes for services	P4b: Industrial firms operating in consumer markets will choose indirect contracting and ordering processes for services
P5a: Industrial firms using direct contracting and ordering processes for their goods will choose direct contracting and ordering processes for services.	P5b: Industrial firms using indirect contracting and ordering processes for their goods will choose indirect contracting and ordering processes for services.
P6a: Industrial firms for which services (potentially) contribute significantly to profits will choose direct contracting and ordering processes.	P6b: Industrial firms for which services (potentially) contribute only slightly to profits will choose indirect contracting and ordering processes.

The propositions could function as a managerial tool for identifying inappropriate channel structures, and thus also for identifying the need for change. The propositions in the paper are more *specific* than the propositions presented in previous research, and they differentiate explicitly between the three central

³⁹ In this paper, SysCo was called “Gamma”.

service processes. Furthermore, these six propositions jointly provide a more *comprehensive* picture than most of the previous literature does since they summarise several of the previously suggested contextual factors.

Another conclusion of the paper is that it is obvious that no optimum distribution model for product services exists, because this is contingent upon several contextual factors and, if the contextual factors are taken into account, there will seldom be a crystal-clear optimum. Nevertheless, looking at the contextual factors can at least provide *indications* of an optimum for each firm, and facilitate a sound choice of distribution model.

Comment: This paper addresses the problem concerning the relationship with the customer, previously identified in Papers I-III. It also serves as input to the managerial implications as it provides advice regarding the relationship between contextual factors and the structure of the service distribution channel. The propositions explain how different contextual factors affect the structure of the service distribution channel, and the papers show that deviations from the structure suggested by the propositions may lead to problems and the need to change. For example, Proposition 6a suggests that firms where profits accruing from services are potentially high will choose direct contracting and ordering processes. Using such a structure, the industrial firm retains its relationship with the customer and its influence over the profitable service business. The research shows that neglecting to follow this advice may lead to problems, i.e. it may be difficult to implement an indirect contracting and ordering structure because of resistance on the part of employees or investors, for instance.

This paper sheds light on the complexity of the strategic make-or-buy issue for product services, which apparently had been causing lots of trouble at SysCo. As such, it provides advice associated with how the strategy formation challenge (see Section 3.2.2) influences the process of externalising services. Furthermore, the case studies also illustrate (for instance, in the case of Delta) the risk that suppliers making an entrance between the industrial firm and the customer may choose to offer more complete services and become solutions providers. The case of Epsilon illustrates how an increasing effort concerning the relationships with the customers, e.g. by holding regular events with them, can moderate the negative effects of using intermediaries in the service distribution channel.

5.6 Paper V: Managing the challenges of outsourcing services

The purpose of this article is to describe externalisation challenges and provide lessons regarding how they can be managed, based on data gathered between 1997 and 2003.

Table V below summarises how SysCo gradually learned from its experiences between 1997 and 2003 and how it re-shaped its partnering and sourcing strategy,

divided in accordance with the three challenges described in Chapter 3. The table includes data that will be used as input for answering *why* externalisation is influenced by the simultaneous intentions to adopt service logic and externalise services.

The table is included as an illustration of, *firstly*, how difficult it can be to set a detailed sourcing strategy and implement it in a linear fashion. The story of SysCo should not be seen as a success story for firms to copy, and neither should their sourcing strategy during 2003 be seen as “best practice”. As a matter of fact, among many SysCo employees, in late 2003, there was still some uncertainty regarding the viability of the partnering and sourcing strategy for services. There were also concerns about how the change processes were being managed and how SysCo were learning from experience.

Secondly, the table contributes some information that can help to draw conclusions regarding the effect of adopting service logic on the externalisation of services, as well as suggesting implications for managers. For example, with regard to the strategy formation challenge, as indicated in the table, SysCo changed from a relatively straightforward approach, whereby basic services would be outsourced to world-class suppliers, to a more cautious approach. For example, during the later stages of the study, it was decided that critical areas of the service business should be kept internal, instead of being externalised altogether.

Thirdly, as can be seen in the customer-relationship row in the table, the importance of some of the basic services to SysCo was acknowledged during the later stages of my research.

Regarding the customer-relationship challenge, SysCo acknowledged its importance right from the start. Gradually, however, SysCo realised the need for a more flexible approach wherein the relationship with the customer sometimes had to be externalised. Also, the approach to change was altered somewhat during the study, and managers became rather more conscious of the need to involve the employees in the implementation process, and the need to be flexible.

In this paper, a more normative posture is taken in an attempt to provide knowledge that is useful to practitioners. Three main lessons learned during the research are described, regarding the externalisation of services. *Firstly*, the change process should be interactive and reflective. *Secondly*, all externalisation projects should be coordinated. *Thirdly*, the customer relationship should be constantly nurtured during the outsourcing process. The three lessons described are associated with managing the process of outsourcing services. The lessons are drawn from data originating from the training alliance described in Paper II, as well as from externalisation projects concerning repair, installation, and full-services.

Table V. The evolution of SysCo’s view of outsourcing and partnering

	1997	1998	1999	2000	2001	2002	2003
Strategy Formation Challenge	“Outsource basic services to global world-class suppliers”		→ “Outsource basic services to non-competing suppliers of low cost and sufficient quality”			→ “We depend on basic services and must not outsource them too quickly”	
		“Installation is not our core business and will be outsourced completely”			→ “Operational parts of installation will be outsourced, but project management will remain internal”		
Customer-Relationship Challenge	“We must always face the customer”		→ “Sometimes we face the customer, sometimes not”		→ “For Product X and Service Y, we must face the customer, but not for Product X and Service Z..., because...”		
						→ “One of our most aggressive suppliers was awarded the full-service contract by our customer in India, and I can’t say the customer made the wrong decision”	
Internal Change Challenge		“Implementation is not an issue for us, we just need to define our strategy correctly and the implementation will follow”			→ “How can we learn from our experiences?”		
					→ “Under what conditions do internal conflicts prove fruitful?”		
						→ “We have never been able to identify changes. And my conclusion from this is that we need to guard against unforeseeable events and to be flexible, rather than to plan”	

Comment: This paper addresses the second purpose of the thesis, since it provides advice on how the externalisation should be carried out (see the three lessons above). It also provides descriptions of the problems encountered during the externalisation projects as a supplement to what has already been described in the other papers. One problem described concerns how local employees and local customers of SysCo refused to accept alliances suggested by head office, due to, for example, cultural and cost reasons. It also describes how some suppliers contracted by SysCo were not satisfied with merely conducting installation services on behalf of SysCo, and were increasingly offering supplementary services directly to the customers of SysCo, including different solutions and even the management of customers’ operations. In other words, they tried to climb up the value chain into more customer-oriented advanced services just like SysCo did.

5.7 Summary of the externalisation problems covered in the papers

The following table summarises some of the problems hampering externalisation, identified during the studies and reported on in the papers. Consequently, the table illustrates how the papers contribute towards answering the “how” part of the research question⁴⁰. Just how they contribute to the second purpose of the thesis, together with the implications for managers, is covered in the next chapter.

An observation that can be made here is that the problems identified in the studies and summarised in the table below are somewhat disparate. Furthermore, the problems often fit into more than one challenge; perhaps the challenges are better suited to conceptual understanding than to the exclusive categorisation of problems.

Thus, there is a need for further analysis and grouping the problems into more fundamental reasons and effects. This will be the topic of the next chapter, which is divided into a section concerning the influence of the change context on externalisation problems and a section concerning the influence of the change approach on externalisation problems.

⁴⁰ The papers *contribute towards* answering how externalisation is affected, although they do not fully and clearly answer this. A more concise answer to the research questions will be provided in Chapter 6.

Table VI. The challenges and their associated externalisation problems

Challenge	Externalisation problems (Number of Paper)
Internal challenge	<ul style="list-style-type: none"> • Resistance to externalising service processes (I) • Ignorance and lack of skills among managers as regards managing the change process and making decisions about sourcing strategy (I) • Doubts that the customer would benefit from the externalisation of services (I) • Alliances perceived as a threat to the employees of SysCo (II), to the adoption of service logic (III), and to the profitability of SysCo, leading to scepticism • Different opinions about the appropriate alliance scope, leading to internal conflicts (II) • Doubt about suppliers' ability to manage service processes, because this was perceived as a craft learnt through long periods of experience (I)
Strategy formation challenge	<ul style="list-style-type: none"> • Writing agreements, specifying processes, and selecting distribution structure so that the customer relationship is not jeopardised (I) • Uncertainty regarding the appropriate scope of the alliances, e.g. services and products suitable for alliances (II) • Threshold between 1) the risk of losing competence and business to partners and 2) the opportunities provided by it for strengthening own brands (II) • Difficult choice between developing own resources and skills and using external resources (II) • Suppliers climbing the value chain into more advanced and complete services, becoming a threat to the adoption of service logic (III, V), in particular suppliers that were intermediaries between the industrial firm and its customers (IV). • Absent, wrong, unclear, or incomplete partnering and service strategies (III, V)
Customer relationship challenge	<ul style="list-style-type: none"> • The externalisation of service processes can deteriorate customer relationships (I, II) • Uncertainty over whether suppliers would be able to satisfy the needs of their customers, which could hamper SysCo's credibility and relationship with its customers (I) • Uncertain effects of using external resources on relationships with customers (II) • Customer concerns regarding whether the competence for new technologies exists at the industrial firm, leading to diminished credibility (II) • Customers perceive suppliers to be more competent in providing solutions and advanced services (III)

CHAPTER SIX

Synthesis, Discussion, and Conclusions

Several problems arose during the externalisation of services at SysCo Services, and this was summarised in the previous chapter. In this chapter, the problems are first synthesised and the effect on the problems caused by the change context and the change approach will then be discussed, in line with the research model. Finally, some comprehensive conclusions are drawn.

6.1 Introduction

The previous chapter remained close to the empirical results presented in the appended papers and primarily contributed towards answering *how* the externalisation of basic services is influenced by the simultaneous intentions to adopt service logic and externalise basic services, primarily by describing the problems encountered during externalisation. This chapter goes one step further and aims to provide a more developed answer to the same question, as well as answer *why* it is influenced.

Moreover, lessons learned from the research, in terms of change approaches that seem to moderate the externalisation problems, are provided at the end of each subsection of Section 6.3. Finally, in Section 6.4, the results are summarised and conclusions are provided on a general level.

6.2 Externalisation problems and the change context

In this section, I seek to extend the discussion on the problems encountered when externalising services, based directly on the collected empirical data and previously described in this thesis. The purpose of this is to gain a deeper understanding of the challenges, problems, and *contextual features* that influence them.

Some of the encountered problems are first recapitulated and synthesised and then the influence of the contextual features and the change approach is discussed. At the end of each subsection below, there is a summary of the contextual features that seem to have affected the externalisation problems.

6.2.1 Problems generated by the internal challenge

Managing the internal part of the change associated with externalising basic services can be a significant problem for industrial firms that are simultaneously adopting service logic. According to the paper dealing with conflict in alliances (Paper II), this has the potential to be the most important problem associated with managing the change. In the study of the process of adopting service logic in collaboration with suppliers (Paper III), the internal problems were also extensive. The research showed that gaining the support of the employees, as well as firmly establishing strategies, can be a significant problem, and this was manifested in, for example, the many internal conflicts that hampered the externalisation process.

At SysCo Services, there was general resistance to externalising services among many of the employees, this was connected not only with fear for their jobs, but also with concerns about the implications of adopting service logic and the sustainability of their business. Some employees were certain that service alliances, such as the training alliance described in Paper II, would hamper the adoption of service logic, and this caused resistance which in turn hampered the externalisation process. They saw great business potential in certain service areas which they wanted to be exploited by their internal service organisation, not shared with external firms. They also saw a risk of deteriorating credibility if certain services, relating to certain products, were not delivered by their own organisation, such as training in IT-related products.

While some managers seemed to be uncertain about how they should manage the change process, most of them seemed not to be bothered so much about this change process. They were generally more concerned with the issue of deciding which areas would be feasible for externalisation and how to divide up the service portfolio and the hardware and software as regards internal versus external service delivery. For example, should the newer products and the products generating high revenues be kept internal, or should they be externalised? Should product-related training be externalised at all? Deciding upon and describing exactly the processes to be externalised, and for which products, was difficult and caused many internal conflicts, hampering externalisation projects. One underlying reason for these problems seemed to be the ambition to adopt service logic. This made it more important to evaluate the consequences of externalisation; but this appeared to be difficult.

There were several opportunities to externalise several service processes for several technologies, since much of the technology was becoming commoditised

and competence and willingness existed among the suppliers. The internal problems and debates were more frequently being associated with concerns regarding the effect of the externalisation on the adoption of service logic and on the relationship with the customer. Would suppliers contracted to deliver basic services, such as installation and repair, stick to those services or would they also, sooner or later, opt for the advanced services, such as solutions and managing customers operations? Should the customers receive as good a level of service from the suppliers as they did from their own firm, based on tacit knowledge amassed over several years (Paper I)?

Moreover, although it was generally accepted that the customer relationship was important and that the customer interface should be kept internal, just exactly how this should be done for each service, and for each hardware or software product, was the object of internal debate. The ambition to adopt service logic emphasised the importance of this, and the ensuing debate hampered several of the externalisation projects. More generally, there were considerable internal problems regarding how to work with partnering and sourcing for the services and management systems associated with this.

Finally, the relationship between head office and the market units of SysCo Services was troublesome, and some market unit managers were working fairly independently and selecting suppliers and partners themselves, without regard for directives from head office. One reason for this was that local SysCo employees deemed this more expensive than locally-sourced alternatives, preferring to collaborate with firms that they had already established bonds with (Paper V). This behaviour caused trouble with regard to the implementation of some of the larger alliances that had global coverage, these being dependent on buy-in from most markets. Although this may not only have to do with the adoption of service logic, it can be expected that similar issues are of particular importance when relationships with customers are being emphasised. The perspectives and opinions of local employees working in the market units may be essential as they can be assumed to have a particularly good insight into the needs of the local customers, as well as the abilities of local suppliers to satisfy those needs.

Previous research has acknowledged that soft factors can constitute one of the most significant problems when alliances are being implemented (Kelly et al., 2002), for example conflicts between alliance firms (Lorange et al., 1991, Mentzer et al., 2000, Mohr et al., 1994, Moore, 1998). The results of the present study agree broadly with this, but they also stand somewhat in contrast to conclusions made by previous researchers because the problems identified in this thesis are overwhelmingly internal to the firm that is externalising a service and implementing an alliance. Although this result may have looked slightly different if, for instance, customers had been interviewed (no customers were interviewed in the present study), there are some other plausible explanations for this. One

possible explanation might be that the externalisation projects studied here were aiming to implement alliances of a more operational character than those studied by the mentioned researchers, which may have meant that they were easier to specify than the more “open-ended” alliances studied by the other researchers. On the other hand, services are often characterised as more difficult to specify than, for instance, the manufacture of physical products, which should have led to trouble at the interface between the two alliance firms.

However, when the results are compared with previous literature on outsourcing, the result is less surprising, because, in the outsourcing literature, internal problems are frequently acknowledged as problematic, not least because of the fear among employees of losing their jobs. For instance, Allen and Chandrashekar (2000) are of the opinion that it is almost impossible to avoid a dip in morale when a firm makes an outsourcing announcement, emphasising the need for active management to minimise discomfort within the firm. In particular, it can be expected that a firm with a strategy that involves the adoption of service logic will encounter a high degree of internal resistance from its employees because these may perceive it to be counterproductive to externalise services.

Another potential explanation for the relatively high degree of the internal problems identified is that these internal problems were connected with the strategic uncertainty concerning, for instance, the long-term consequences of alternative decisions. For example, it was not completely clear what the long-term consequences of externalising installation would be regarding the adoption of service logic, for instance. Technology was maturing and the availability of competent suppliers was increasing, and this decreased the profit margins associated with delivering basic services. The suppliers were also starting to seek differentiation opportunities. In particular, some of them were aiming at more complete services and solutions, and becoming the intermediary between the customer and other suppliers.

Furthermore, managers and others at industrial firms, including board members, may have a mindset of industrial logic, in particular during the early stages of the adoption process and downturn periods, which is typically the time when an industrial firm tries to adopt service logic. This means that the focus is on increasing efficiency, e.g. through the externalisation of services, rather than improving the relationship with the customer by developing and offering more customer-oriented, advanced services. A senior manager at SysCo Services had this to say:

“I have a Board above me in the organisation and they are constantly telling me that I have too many employees. This is their basic attitude. When I enter the room, they tell me this and they continue until I have done my presentation. This is their mindset; to be careful with the number of employees. But I cannot see how I can deliver services without people. Then they tell me that I should have partners. Well, that’s the issue, and

that's why I appreciate that you are conducting research in this area. How can we make our service business profitable?"

Decisions concerning the externalisation of services at industrial organisations, as well as decisions related to service strategy, may be based primarily on a logic emphasising efficiency and neglecting the service or customer logic. This is particularly likely when the change is taking place during a downturn period. This may lead to internal conflicts and, in the worst case, hamper the adoption of service logic.

6.2.1.1 The influence of contextual features

To begin with, the *scope* of change associated with externalising services may be classified as realignment. However, in this study, externalisation is embedded in a larger transformation that affects a large part of the organisation (the adoption of service logic), i.e. a change that cannot be handled within the existing paradigm and organisational routines (Balogun et al., 2004, p. 19). This makes it a relatively complex change process that needs to take the greater context into account as well. At SysCo, this was apparently a problematic process, full of uncertainty, thus it was difficult to agree on the strategy, for instance.

Moreover, *preserving* the relationship with the customer is particularly important for industrial firms adopting service logic. This contextual feature seems to have led to internal problems during externalisation, since several of the internal problems were about the (perceived) risk of losing this relationship, as a consequence of externalisation, and how this risk could be moderated.

Furthermore, externalising services and adopting service logic may be seen as changes that are counterproductive, as discussed previously in this thesis. Different units within the organisation may have different opinions regarding, for instance, whether efficiency is more important than the relationship with the customer, and so forth. This may be conceptualised as *diversity* within the same organisation, or as a conflict between different business logics within the organisation. At SysCo, this caused internal conflicts between the different units of the organisation and this hampered the change process.

Finally, the uncertainty regarding the current and future actions of suppliers, e.g. whether they would also attempt to take over the more customer-oriented and advanced services, caused hesitation in the organisation regarding the externalisation of basic services, in turn affecting the externalisation process. This may be associated with the commoditisation of technology and the increased availability of suppliers able to handle the services. This technological change is increasing the suppliers' opportunities, but it is also forcing them to seek other business opportunities as the profit margins on servicing commodities are typically decreasing, e.g. integrating forwards into more customer-oriented services. This technological change, which is one of the reasons for adopting service logic, is

affecting the *power* balance and dynamics of the industry, and causing confusion at SysCo, thus hampering the externalisation process. Commoditisation may not only be responsible for *industrial* firms moving into services. As commoditisation often also increases the level of competition, it also leads specialised *service* firms to search for alternative business opportunities, e.g. delivering more advanced and complete services.

6.2.2 Problems generated by the strategy formation challenge

The determination and formulation of the strategy to be implemented, both the sourcing and service strategies, can be a significant challenge that may be problematic for industrial firms externalising services and adopting service logic. This challenge is associated with difficulties in assessing the effects of the sourcing strategy on the firm's adoption of service logic. At SysCo Services, there was actually no clear sourcing strategy for a long time, and, when one was presented by the partnering and strategy manager, the employees saw it as either unclear or incomplete, with the same being said about the service strategy (Paper V). One reason for this may be the adoption of service logic and the ongoing changes associated with it at suppliers and customers.

For SysCo, the service and sourcing strategies were evolving based on a growing experience and interaction with suppliers, employees, and customers rather than being formulated by top management and implemented in a linear fashion. For example, the initial strategy of always facing the customers, and not allowing any supplier to come between SysCo and its customers, was proving to be unrealistic and was gradually changed. This change in strategy was partly caused by the previous intention to externalise installation to one global supplier, which was never really implemented for several reasons. Installation was initially externalised completely, but the project management part was later brought back to SysCo because it was seen as an important element for retaining control of current and future business. Installation was a significant source of revenue, as well as a service which was interrelated with other services and which could potentially facilitate the supplier in developing competence centring on other services, creating a closer relationship with the customers. Furthermore, local customers and local units of SysCo did not accept changing to the new supplier which had been contracted.

Moreover, the project through which repair was to be externalised had to be halted suddenly when it was realised that the supplier that had been selected, and with which a contract was to be signed, had become too powerful. The supplier had also been awarded a contract for the installation of SysCo's products, and it was suddenly realised that this firm had strong ambitions not only to be a supplier to SysCo and similar firms, but also to become a full-service supplier, thus becoming a competitor in an area where SysCo saw one of its future business opportunities.

An excerpt from an interview with a manager at SysCo Services illustrates one reason for this issue:

“I have been working for several years with strategy exercises at SysCo. I have recorded every strategic plan made by the firm. The conclusion is that we have never been able to identify changes. And the conclusion drawn from this is that we need to guard against unforeseeable events and be flexible, rather than plan”

This excerpt illustrates the difficulties of implementing formulated strategies, and the need to adopt or adjust to events in one's environment rather than implement strategic changes such as adopting service logic or externalising services in a sequential manner. The simultaneous adoption of service logic means that externalisation is carried out in a changing environment, and this complicates the strategy process.

When suppliers and partners are involved, it can be very difficult to determine the details of the service and alliance strategies *ex ante*. It can be particularly difficult when both the buying firm and the suppliers and partners adopt service logic, as it can mean that the firms are collaborating and competing simultaneously (cf. Bengtsson & Kock, 2000). In such situations, a linear approach to strategy can be difficult, and the roles of the involved firms become less clear, for instance in terms of their positions in the service distribution channel. Moreover, as discussed in Chapter 2, the adoption of service logic and the externalisation of services are associated with maturing technology and commoditisation. When technology matures and the products become commodities, the competitive advantage of the industrial firm associated with the knowledge of technology diminishes. This paves the way for competition in a wider area of services than is the case when most goods are specialties, and it is likely that this makes it even more difficult to determine a strategy and implement it in a linear fashion.

It has previously been acknowledged that strategies often emerge during the course of time, rather than being planned in advance (Mintzberg, 1978), and that they are the outcome of a negotiation and learning process. Furthermore, strategy, by definition, deals with the unknowable (Quinn, 1999). Nevertheless, the lack of service and partnering strategies has caused a lot of internal frustration at SysCo Services, being perceived by some employees as preventing SysCo from positioning itself in the marketplace.

On a more general level, the problems mentioned are associated with the issue of keeping the customer relationship internal (see Section 6.2.3), and what this means for the processes and strategies associated with services and sourcing. At SysCo, there did not seem to be any consensus as regards how to handle this issue, although the basic idea was to keep the interface and relationship with the customer internal as much as possible, and to have suppliers doing the operational back-office work behind the customers' line of visibility.

6.2.2.1 *The influence of contextual features*

Initially, the change *scope* was typically seen as limited to the individual externalisation projects being conducted at SysCo, e.g. by project and line managers at SysCo Services. However, during some externalisation projects, it turned out that this should probably also have been coordinated with a wider scope, including other externalisation projects and the development of a service strategy. This limitation of the assumed scope of the externalisation projects sometimes led to a temporary halt in some of the externalisation projects, when the more feasible wider scope was being considered, and the selection of an alternative supplier.

The problem caused by the scope of change is connected to another of the pivotal issues of the strategy process, i.e. how it should be designed and formulated in order to *preserve* the relationship with the customer and avoid losing the business of providing advanced services to suppliers. At SysCo, the strategy changed somewhat during the study, e.g. from completely externalising services such as installation to always keeping the customer interface internal to something between .

Furthermore, there were many conflicting internal ideas and goals as regards areas feasible for externalisation, for instance, while the two *diverse* logics of externalisation (or the industrial logic) and service logic inherent in the organisation made it difficult to make strategic decisions. Balancing the degree of externalisation and the adoption of service logic seemed to be a difficult issue.

Moreover, the strategy, e.g. as regards areas feasible for externalisation, was initially very rigid but was subsequently adjusted to take differences in *power* between the different suppliers and SysCo into account, where, for instance, the strategies of powerful and competent suppliers could not be neglected. The relative independence of the different organisational units of SysCo was also considered, e.g. the relatively high level of power wielded by internal stakeholders, with the change approach being adjusted accordingly. For example, local organisations were given a more central role in externalisations.

6.2.3 **Problems generated by the customer relationship challenge**

As revenues from sales of products are falling, and products are becoming more like commodities, it can be expected that firms which best can meet the needs of their customers will win their appreciation, e.g. those which can help improve the customers' business. Service contracts will go to firms which can provide convenience and improvements, e.g. in terms of solutions and other advanced services. Doing this requires knowledge of the customers' business and a presence at the customers' premises, typically achievable through the delivery of different sorts of services.

A fundamental problem is that the externalisation of services may decrease the chances of creating and maintaining good relationships with the customers, which is vital to firms adopting service logic. A consequence of externalisation is that aspects of the interaction and relationship between the customer and the supplier are externalised to a supplier. These aspects may be more or less visible to the customer, e.g. training being highly visible, but repair much less so, nevertheless externalising service processes impacts on the relationship with the customer.

The effect of externalising services on the customer relationship may be more direct, as in training alliances and other people-oriented front-office services, or indirect, as in equipment-oriented back-office services such as repair. Repair, for instance, may have an effect on the relationship because; (1) it makes up one important (however invisible) part of the product service offering, (2) it contributes to the suppliers' learning, and (3) suppliers responsible for many operational services, such as repair and installation, may be perceived to be a more credible supplier for more advanced services, too.⁴¹ Customers may have concerns about the competence of an industrial firm that uses external suppliers to deliver services and this may have negative effects on the brand-image of the industrial firm.

When SysCo externalised training in IT products, some customers wondered whether or not SysCo had the competence associated with IT services in-house (Paper II). This may also have had more general effects on the brand and image of SysCo, not just for training services.

Another potential externalisation problem is that customers may have opinions about the use of other particular firms for the delivery of services. In the case of SysCo, there were examples where customers refused to let one of the global suppliers contracted by SysCo install the products, because they had opinions about this supplier related to cultural and other aspects (Paper V).

The importance of involving the customer in the externalisation process has previously been emphasised by O'Farrell and Wood (1999), although their advice was not based on any empirical advice accounted for.

⁴¹ It is worth noting that some customers may not see the value-added in having an intermediary between themselves and the suppliers of basic services, although others may see having just one single supplier as a significant value. Particularly during downturn periods, it can be expected that customers may value a low price more than the convenience of having one only supplier that can provide full-services. Many companies today succeed just because they are not offering any supplementary services, but focusing on high-quality products and low prices, e.g. Southwest Airlines (Meyer et al., 2000). In other words, every firm has several different alternatives and a low-cost strategy may be just as viable as a total solutions strategy; the preferences of different customers can be expected to differ. This thesis, however, focuses on a firm that is primarily trying to add value by offering advanced services as well.

6.2.3.1 *The influence of contextual features*

The problems described above are largely about the **preservation** of the relationship with the customer, and the potential negative consequences for that caused by externalising services. This problem was clearly illustrated during several of the studied externalisation projects, e.g. the training alliances where customers doubted SysCo's competence when externalising IT training and installation, which in some cases led to lost full-service contracts.

Another important feature is the **power** of the customer, which may also lead to problems during externalisation. The customer may have opinions regarding the choice of supplier, and with regard to installation, for instance, the customers had firm opinions about the suppliers contracted by SysCo. This hampered the project and ultimately led to an altered sourcing strategy.

6.2.4 **Summarising the contextual features and their influence**

One of the most fundamental reasons for the externalisation problems, underlying many of the problems described above, seems to be the risk, or at least the perceived risk, of losing the customer relationship as a consequence of externalisation. **Preserving**, or improving, a close and sustainable relationship with the customer is one of the goals of adopting service logic, and this seems to be something that needs to be taken into account seriously during the externalisation process.

The issue of **power** is more complex and deserves an extended discussion. The adoption of service logic is often justified by *decreasing revenues from product sales*. This in turn is associated with factors such as product *commoditisation* in many industries and increasing competition and the availability of competencies on the market, both with regard to product development and service delivery. For commodity type products, there is a potential for economies of scale to be exploited, in particular by firms who can provide services for multiple technologies and for multiple customers. By exploiting economies of scale, service firms can reduce costs, particularly if services are delivered for several product vendors. As the installed base is increasing in many industries (e.g. for cars, but not for VCRs) the incentives for going downstream are increasing (Wise et al., 1999), and this is the same for all firms, for industrial firms as well as for independent service firms.

Basic services are easy to copy (Vandermerwe, 2000), and thus do not often provide any sustainable competitive advantage in themselves. Thus, it can be expected that firms which are exploiting the economies of scale resulting from, for instance, the commoditisation of products, will also strive for differentiation from their competitors by delivering supplementary non-standard services that are typically more advanced, customized, and specialised. This is also what some of

SysCo's suppliers did. For example, one installation and repair supplier was particularly interested in broadening its offering from basic services to more advanced and complete services, aiming to become the intermediary between the customer and other suppliers of services, and thus a threat to SysCo (Paper V).

On the other hand, products are increasingly being composed of parts delivered by different firms, with few industrial firms developing and manufacturing entire systems. Thus, while the separate products are being commoditised and exposed to competition from independent service factories in the service channel, the whole system is becoming *increasingly complex*. This increases the need for highly-skilled service professionals who can release customers from dealing with the complexity, and who have knowledge of systems integration and a consultative manner, for instance. Depending on how the products in the system are connected to each other, managing the services for entire systems requires competence not only as regards the commodities built into it, but also as regards how the system works as a whole.⁴² Thus, only systems integrators or firms involved in the development, delivery, and integration of the entire system are able to differentiate themselves through their ability to handle the services relating to complex products, which may or may not be composed of commodities.

This discussion can be compared with the literature on manufacturing wherein, for instance, Karlsson (2003) differentiates between vertical technologies involving specialized areas, e.g. brakes and engine management for cars, and horizontal technologies related to the functions of the products, e.g. safety and comfort. According to Karlsson, vertical technologies can be sourced externally while horizontal ones should be handled in-house, or through partnering, because they are so closely associated with the characteristics of the product. Shifting to horizontal technologies creates a need for engineers with wider perspectives and the involvement of many more functions and employees in managing the technology.

There may, however, be a risk that the suppliers of basic services for simple commodity products learn about more complex services and may gradually (but perhaps suddenly in the case of the industrial firm) be able to take responsibility for full-services, especially if they are awarded the contract for many of the service processes, e.g. repair, systems integration, and installation. These suppliers may also learn how to manage services for complex products. According to Bettis (1992), the outsourcing of manufacturing has led to a spiral of decline that has ultimately left firms without the skills and competencies they need to compete. This has, however, been moderated by new innovations and growth in the service sector. Politicians, as well as some academics (e.g., Bardhan & Kroll, 2003), now fear that the new wave of off-shoring services, e.g. call-centres and applications

⁴² This need will be moderated if the commodities are truly modular and can be flexibly combined with other commodities.

support, to low-cost countries may result in similar negative effects, or even worse than those of the outsourcing of manufacturing, while many others emphasise that outsourcing to low-wage countries is necessary for productivity reasons and that the loss of jobs will be compensated for by the emergence of new jobs of a higher intellectual level (see, for instance, Economist, 2003, 2004).

Basically, the technological changes (in particular the commoditisation of products) underlying both the adoption of service logic and externalisation, have weakened some of the base for sustainable competitive advantage and the *power* of industrial firms, based on their previously unique skills for handling the services. Commoditisation decreases the uniqueness of their skills and paves the way for specialised service providers to exploit economies of scale (efficiencies associated with the scale of production), and economies of scope (efficiencies associated with the scope of marketing and distribution based on the increased number of products produced).

On the other hand, the increasing technological complexity resulting from specialisation and increased external sourcing have provided a new opportunity for offering advanced services and managing this complexity for others. Insecurity regarding how the services in the different service spaces (Figure 1, page 2) are interrelated, in terms of the competencies needed, for instance, may lead, however, to internal insecurity and conflicts between the different opinions as regards the most appropriate strategy. Particularly when external firms are also trying to adopt the same sort of service logic, it may be difficult to predict the effects of externalising certain service processes.

A close customer relationship is one of the aims of adopting service logic, and can counteract the decreased differentiation of industrial firms resulting from the commoditisation of products. Such relationships can thus be pivotal for firms simultaneously adopting service logic and externalising services. Although the risk associated with externalising services (and the appropriate channel structure) is contingent on factors associated with, for instance, the product, the firm, and the market (Paper IV), the more general and vague *perception* that externalising services has a negative impact on the adoption of service logic and the relationship with the customer, or the *uncertainty* around what effects this might have, can impact upon the change process and cause resistance, reluctance, and paralysis in the service organisation of the industrial firm.⁴³ In other words, the *scope* of the change influences the externalisation; in this case, an externalisation that is embedded in an adoption of service logic.

⁴³ The impact on the customer relationship of externalising services differs from service to service and from service process to service process. From an implementation standpoint, however, the problems will be just as severe no matter how serious the risk actually is and need to be taken into account. For example, Herbert Simon points out that most people are only partly rational, and are in fact often emotional and irrational (1957); so called bounded rationality.

In particular, employees working in the service organisation of the industrial firm may have an *identity* that opposes the focus on traditional efficiency measures, e.g. head-count reduction, whereas the majority of the employees of an industrial firm may have an identity that is more in line with an industrial logic. In other words, *diversity* exists in the organisation and should be taken into account during the change process. An excerpt from an interview with a senior manager of SysCo Services illustrates the conflicts between the different logics:

"Why don't you ask our Systems Development Manager why they are so afraid of the head-count. You will then see things from a different angle and hear his view on this issue. I wonder what lies behind the focus on head-count reduction. We are very much influenced by this focus, and I just don't get it"

Internal conflicts like the one illustrated by the excerpt, as well as many others (see, for instance, Paper II), were not unusual at SysCo and differences in the way the different employees and the different organisational units, e.g. service and product units, saw the mission of the organisation seem to have contributed to these problems. To overcome such a clash between service and product logic and succeed in becoming more customer-oriented, Sandberg (2003) recommends infusing service logic throughout the entire organisation, and that the dual identities be managed and explained through conscious rhetoric.

The problems and the underlying contextual features discussed above are synthesised in Table VII.

Table VII. Contextual features and their effects on externalisation

Contextual features	Externalisation problems
<p><u>Scope</u></p> <ul style="list-style-type: none"> • Complex change process composed of a realignment (externalisation) embedded in a larger transformation (adopting service logic) 	<ul style="list-style-type: none"> • Internal resistance, conflicts, doubts, and fear. • Difficulties in selecting and agreeing upon an appropriate strategy, make or buy decision, selection of processes, products feasible for external service delivery due to the new situation requiring more detailed decisions, not just per service, but per service process and per product • Difficult to write agreements. • Customer refusing to use suppliers selected by headquarters. • Externalisation of services perceived as a threat, new competitive landscape where some suppliers are also adopting service logic. • Doubts about suppliers' abilities, and concerns about the effects on the credibility and the relationship with the customer, and the brand.
<p><u>Preservation</u></p> <ul style="list-style-type: none"> • Customer relationship needs to be preserved in spite of externalisation. 	
<p><u>Diversity</u></p> <ul style="list-style-type: none"> • Conflicting business logics make the change process difficult 	
<p><u>Power</u></p> <ul style="list-style-type: none"> • Commoditisation of technology deteriorating the power of industrial firms and increasing the power of suppliers. On the other hand, there is increasing technological complexity on the systems level. • Power of the customer 	

6.3 Externalisation problems and the change approach

This section contains discussion on how and why the *change approach* influences the problems encountered during the externalisation of basic services. Just as in Section 6.2, the discussion commences with a description of some of the problems experienced by SysCo during its externalisation projects. This is followed by a discussion on how this was influenced by the change context and, in particular, by the change approach (which should be adjusted to the change context). Thus, given the ambition of also basing this part of the discussion on the problems observed at SysCo, some of the same problems will be repeated here. Conclusions are drawn regarding the influence of the change approach on externalisation problems.

At the end of each section, lessons for managers gleaned from the research are presented. The lessons should not, however, be taken as *prescriptions* to follow without making judgements. Each externalisation project has its own contextual features, and the features that have not been considered in detail during this thesis include time constraints, and capability and capacity aspects (Balogun et al., 2004). Nevertheless, these lessons should prove useful with regard to *informing judgements* made during individual externalisation projects.

6.3.1 Problems generated by the internal challenge

Many employees at SysCo felt neglected and steamrolled by management when it came to externalisation matters, often reacting negatively to these initiatives. Many of these employees felt that the strategies and plans for partnering and sourcing had not been sufficiently communicated to and established with SysCo's employees. Furthermore, a significant proportion of them felt that the strategies, as they had heard about them or perceived them, were wrong.

Although it is not possible, based on the study, to clearly assess whether the actual strategies were right or wrong, neither is this the purpose of the thesis, it can be concluded that the externalisation showed itself to be difficult, due to resistance on the part of SysCo's employees, as well as its suppliers and customers. As described in Paper V, there are at least two basic and interrelated reasons for this difficulty.

Firstly, the initial partnering and sourcing strategy was not very flexible but rather rigid. The change process was seen as a linear implementation process rather than an adaptive process of strategy formation. For example, the definite strategy of always facing the customer, ("we must always face the customer", see Paper V), set by top-management, proved to be unrealistic and was subsequently changed. Understanding of this gradually developed through interacting with suppliers, customers, and internal employees by means of negotiations and confrontation with the initial strategy. The strategy of externalising installation altogether, for example, also proved to be non-functional, following attempts to implement it and

then failure, and was replaced by a strategy whereby only the operational parts were outsourced and project management was retained at SysCo.

Secondly, the strategy had not been established with the employees, customers, and suppliers, thus implementing it was difficult. However, because of the turbulent market conditions, it would probably have been impossible to set a detailed strategy at the outset which would have remained unchanged later on.

A lesson regarding the externalisation of basic services that can be learned from the present research is that the change approach needs to be iterative in character and involve interaction between the employees, customers, and suppliers, as well as the development of an overall strategy by top management. Formal planning and managing the change from the top are often unfeasible due to the need to take in local knowledge (e.g. regarding customers) and local strategies; neither is a fully-fledged bottom-up approach to change because of the need to coordinate several externalisation efforts at the same time. In particular, when externalisation is being carried out while service logic is being adopted, the uncertainty may be greater. The positions of suppliers and customers change, as do the opinions of internal employees, based on the increasing focus on advanced services. This emphasises the need to reflect frequently over the strategies and expectations of the customers and the suppliers.

Another aspect is that the local employees of the industrial firm, for instance, may have a different view of the externalisation. Since their support during externalisation is normally required, the services and the relationship with the service suppliers are typically handled, at least to some extent, by them, a participative approach may be more feasible than a directive one. Such an approach spreads the ownership of the change and may increase commitment (cf. Balogun et al., 2004, p. 34). This may be particularly important if local units are working fairly independently. If service logic is also being adopted, it may be particularly important to involve both the employees and the other important stakeholders in the externalisation. In such situations, when there is an overall ambition to move into services, but not all details have been decided upon or communicated, there may be several different and conflicting views regarding the strategies and how to effectuate them. Thus, there is a need for a more interactive, or participative, change approach.

There also seems to be a need to explain why a simple top-down approach is not feasible. Just waiting for things to emerge from the lower, and less central, levels of the organisation may cause irritation among the employees expecting to be led by their managers. Managers must also be honest with their employees and explain that they cannot deliver clearly-formulated and definite strategies as they do not have all the information and knowledge needed.

Dunphy (2000) recommends a similar approach, however, to change more generally, where top-management sets strategic intent in collaboration with other employees of the organisations. His recommendation for managing change is that strategy and vision should be created based on service employees' insights, for instance, as well as senior managers' overview. Furthermore, according to Niederkofler, flexibility is necessary when alliances are implemented because they seldom succeed as planned (1991).

Furthermore, the experiences from SysCo support a view wherein a dynamic and reflective approach to externalising services is needed, where rigid definitions of core/non-core service areas should be avoided (Leonard-Barton, 1992). Instead, the sourcing strategy should be constantly called into question and assessed against the overall service strategy of the firm and suppliers. In a situation where service logic is being adopted while services are being externalised, it also seems important to change the sourcing strategy in incremental steps, and to be prepared to return to the old strategy if necessary. Drastic changes in the direction of completely new and fancy service areas and the externalisation of more basic services may be tempting for innovative firms, but it may be safer to keep these old services in-house, at least for a while, because they may be more important than first thought. Revolutionary forms of change may be infeasible if important assets are to be preserved (Balogun et al., 2004), e.g. the relationship with the customers, and it may be necessary at the outset to stick to the more basic services for longer than expected.

To sum up, the linear and top-down approach to the externalisation process initially employed at SysCo Services was not capable of securing the necessary support of the employees of the organisation. Neither did it make use of the knowledge residing in it. Because of the complexity of the change process (the *scope*), the *diversity* of the organisation and the *power* of local service organisations, a more participative and reflective approach would probably have been more feasible.

6.3.1.1 Lessons for managers

A linear and top-down change model seems to be inappropriate and should be avoided. If a linear top-down approach is used, it seems that internal resistance to the alliance will be greater, as will the risk of choosing the wrong alliance strategy. The adoption of service logic seems to increase the need for an approach to change that can be described as participative and reflective in nature, involving interaction between employees, customers, and suppliers, as well as the development of an overall strategy by senior management.

This lesson agrees particularly well with the overall ideas in research pertaining to relationship marketing, e.g. Grönroos (2000) and Gummeson (2002). Regarding research that is more closely related to this thesis, O'Farrell and Wood (1999) and

O'Farrell and Moffat (1991) have previously made similar suggestions. However, their advice was not grounded in empirical research, thus this thesis verifies their research and constitutes an empirical contribution.

6.3.2 Problems generated by the strategy formation challenge

Neglecting, or being unable, to consider more than one externalisation project at a time during externalisation may result in a situation where the supplier becomes more powerful than is desired. Failing to take the overall situation into account, e.g. the suppliers' overall ambitions and the total scope of the suppliers' collaborations with their own firm, can thus be dangerous. At SysCo Services, such neglect was typically discovered when the externalisation project had come relatively far (e.g. the repair externalisation project in Paper V), and the project thus had to be terminated or take another direction. Sometimes, this meant another supplier being selected, while in other cases, it meant the scope of the alliance being changed, i.e. the choice of processes to be outsourced was changed.

One underlying reason for this problem is connected with the *scope* of the change process, i.e. the degree of change required. In the present study, externalisation is embedded in the broader adoption of service logic. This complicates the change process and may make emergent or bottom-up change less appropriate and a gradual process combining the bottom-up and top-down approaches more feasible. The deeper and broader the change, the more difficult to manage and time-consuming it will be (Balogun et al., 2004). Because of the relatively complex change studied here, with the externalisation embedded in the larger transformation of the firm, a combination of top-down and bottom-up approaches would seem necessary.

Another potential imperfection, related to the one just mentioned, is the neglect of externalisation project managers to take changes in their own firm's service strategy into account. If these changes are not considered, the members of the externalisation project may fail to acknowledge certain risks related to the adoption of service logic. In the case of SysCo, there seemed to be a risk that the externalisation of basic services, e.g. installation and repair, would hamper their move into the advanced service business, e.g. managing customers' operations. Had the alliance project considered this at the outset, then this risk might have been better managed. More examples of coordination problems can be found in Paper V where there is a discussion on how the externalisation of basic services, e.g. repair and installation, might hamper the introduction of advanced services.

Each separate externalisation decision may be sound on its own merits, but together, several of them may lead, in the worst case scenario, to the long-term decline of the industrial firm, because this may lead to lost service business. If the externalisation process is not managed carefully, taking other alliance efforts into account, the economies of scale may gradually move towards the supplier, and

overheads will have to be allocated to a diminishing operational business (Bettis et al., 1992). Therefore, it seems that each new alliance, resulting from the externalisation of basic services such as installation or support, should be analysed from the perspective of its effect on the advanced services and the relationship with the customer. Accordingly, the extent to which an externalisation initiative may result in increased competition in the new core service areas, e.g. solutions and managing customers' operations, should be analysed.

Furthermore, firms externalising basic services should ensure that they do not become too dominated by their partners and suppliers, which is why some authors suggest that non-competing enterprises should preferably be selected (e.g., Quinn et al., 1990). If each externalisation initiative is analysed in isolation from the overall strategy of the firm, and if the development of knowledge internally, and the risk of losing critical knowledge to the supplier, are not sufficiently taken into account, this may lead to a vicious circle for the firm that is outsourcing (cf. Bettis et al., 1992, Quinn et al., 1994). There is always a risk of opportunistic behaviour in business relationships (Das et al., 1999), which can entail, for example, the supplier integrating forwards in the value chain and becoming a competitor (cf. McCutcheon et al., 2000, Quinn et al., 1990) in the newer service areas where the firm that is externalising intends to compete.

Thus, a lesson that can be learnt is that there seems to be a need to coordinate different externalisation projects and to assess them against the current service strategy. Doing this should facilitate the formulation of both service and sourcing strategies, and, not least, identification of the competencies needing to be developed to stay ahead of the competition. It is not just service externalisation projects that should be coordinated. Externalisation in other areas than the services delivered to customers should also be carefully considered, e.g. the externalisation of R&D and manufacturing. The reason for this is that such changes may assist supplier firms in conducting services that require knowledge of the technology and the products, thus decreasing the competitive advantage of the firm that is externalising.

Another lesson that can be learnt is based on the following observation; "We shall always face the customer" was repeated like a mantra at SysCo Services, although on closer inspection, this was not 100% true and, as would be demonstrated later, neither was it feasible. However, at the beginning of the study, reflected in, for instance, Paper I, nobody was able to say when the customers were to be managed internally or not, and what doing this would entail. This uncertainty meant that SysCo Services was hesitant vis-à-vis its alliance efforts, and that it was refusing to enter into alliances where it was unable to hold on to the customer interface itself. In practical terms, this meant that some negotiations never came to a close.

Gradually, however, a more insightful and detailed strategy emerged, as described in Paper V. The mantra changed and became less rigid, viz. "sometimes we face

the customer and sometimes not”, see Table V on page 2. Associated with this change, Paper IV includes advice on how different service processes (contracting, ordering, and expediting) can be adjusted to different contextual factors⁴⁴. The advice is formulated as a number of propositions regarding how contextual factors influence the appropriate channel structure of product services and can be interpreted as a contingency factor that should be taken into account during the alliance process, or as a challenge/potential problem. The advice stresses the need to adapt the product service channel to the product, market, and firm contextual factors and that contextual analysis must be built into the alliance process. Otherwise, if for example, a less appropriate (deviating from propositions P1-P6) structure is implemented, the externalisation project may encounter resistance from employees or investors, for instance. This was confirmed by the results of Study IV.

To sum up, neither a top-driven directive change approach nor a fully-fledged bottom-up approach based on delegation and involvement seem to be able to handle the complexity of an externalisation that is embedded in the adoption of service logic (i.e. the complex *scope* of the change). The need to put individual externalisation projects into the perspective of the larger context underscores the need to combine top-down and bottom-up approaches.

6.3.2.1 *Lessons for managers*

The adoption of service logic seems to increase the need for coordinating service alliances, because the different externalisation projects, and ongoing alliances, may hamper the adoption of service logic, not only individually but also collectively. Consequently, externalisation projects should not be conducted in an authoritarian manner, by senior management, because it may then fail to notice the effects associated with the combination of different alliances. Neither does a bottom-up approach seem to be enough in itself, for instance because the overall intentions of the firm may then be overlooked. Thus, a combination would seem necessary.

This lesson agrees broadly with the advice given by, for example, Dyer and colleagues (2001) who suggest central alliance functions for coordinating different alliances at large firms. Also, Allen and Chandrashekar (2000) make a similar recommendation, i.e. having a centralised contractor management council to discuss and formulate corporate policies on outsourcing. In contrast to the others, I say that different externalisation projects and ongoing alliances must be assessed against each other, and together, from a strategic point of view or from a service logic point of view. Service strategy, individual externalisation projects, and the whole portfolio of service alliances (as well as other alliances) should be assessed against each other so that they do not interfere with each other. Thus, this thesis

⁴⁴ The contextual factors discussed in Paper IV are not be confused with the contextual features of the *change context* described in Section 3.3.2.

constitutes an extension, or a refinement, of the previous recommendations since it more explicitly emphasises that externalisation projects should not be conducted by senior management in an authoritarian manner. Thus, the lesson presented in this thesis is more oriented towards the externalisation process than towards alliance management in a steady-state phase.

Furthermore, the adoption of service logic seems to increase the need for contextual awareness and awareness of the details of the service processes. The fundamental reason for this is that adopting service logic increases the strategic importance of the service alliances, and thus the importance of “doing the right things” as well as “doing things right” when it comes to service alliances. Taking contextual factors into account is by no means new advice *per se* (cf. Lawrence & Lorsch, 1967), even though the literature on, for instance, change management often neglects contextual factors (Collins, 1998). The value of my advice lies instead in the specificity of the propositions (see Paper IV) and lessons.

6.3.3 Problems generated by the customer relationship challenge

Unless the intention of the firm which is externalising its basic services is to turn its back on services altogether, and focus on other areas, such as the development and mass-production of simple goods, it will be important to nurture the relationship with the customer, independently of the structure of the delivery chain, e.g. if a simple supply chain, management through intermediaries, or a supply partnership (Johnston et al., 2001) is used. Customer relationship management is becoming increasingly important as markets are maturing and becoming oversupplied (Grönroos, 2000, Payne et al., 2000). Even in 1983, Berry was contending that the importance of marketing to protect the customer base is increasing in services, due to an increased supply of essentially similar services (Berry, 1983).

In the case of SysCo, with its lengthy history as a product supplier in the first instance, the relationship with the customers was not very well managed initially, e.g. during the training alliance described in Papers III and V. At SysCo, the relationship was primarily based on technical expertise and superior products. For example, SysCo did not sufficiently communicate the intended changes to its customers or ask for their opinions before embarking upon the pilot project with the training partner. In this case, the customers were unaware that the alliance existed nor of the purpose of it. As a result, they were very confused by this. According to O’Farrell (1999), the relational nature of services means that customers should always be involved in decisions regarding service alliances. To some extent, neglecting to do this put the relationship with the customers at risk when SysCo failed to involve its customers in the pilot project via which training services were to be externalised. As described in Paper V, SysCo was gradually starting to acknowledge the importance of this and to change its behaviour.

Offering and delivering more customer-oriented services, such as business solutions and managing customers' operations, is, in itself, closely related to nurturing the relationship with the customer, although a relationship requires much more than this. For instance, it is also about attitude and keeping promises. It is widely recognised that the purchase of a service is influenced by more than just the service product itself, also being influenced by, for instance, the service delivery system, the quality of the interaction with point-of-contact personnel, and the reputation of the firm (Storey & Easingwood, 1998). This is sometimes termed the augmented service offering (Grönroos, 2000, Chapter. 7, Storey et al., 1998).

To sum up, the lesson seems to be that the constant nurturing of good customer relationships seems to be of the utmost importance to service-oriented industrial firms externalising their services (i.e. *preserving* or improving the relationship with the customer). According to O'Farrell and Wood; "there is a need to incorporate service experience into any theory of SA formation" (1999) and "the role of alliance clients in the development and success of SAs, an issue neglected in previous SA literature", and "business service SAs require client sanction...". In today's competitive environment, this can be the key to retaining customer confidence, and to a sustainable business. For firms really interested in becoming more service and customer-oriented, the establishment of an ongoing customer relationship and a reputation as a service provider are critical, and one of the biggest challenges (Oliva et al., 2003).

6.3.3.1 Lessons for managers

Externalising services without involving the customer during the change process seems to be risky, because it may lead to weakened credibility and the risk that customers ally themselves with the suppliers. This thwarts the ambitions of adopting service logic. The adoption of service logic seems to increase the need for constantly nurturing the customer relationships during the externalisation project. This has to do with the importance of the relationship with the customer, especially for firms trying to adopt service logic.

This lesson agrees broadly with the recommendation made by O'Farrell and Wood (1999) and O'Farrell and Moffat (1991), i.e. to involve the customer in service alliance projects. It also agrees, albeit more broadly, with the more general alliance process models suggested by, for example, Ring and van de Ven, (1994), Doz (1996), Ariño and de la Torre (1998), as well as the model for innovation partnering suggested by Marshall (2004). All these authors emphasise the iterative character of alliance formation.

The lesson presented here can be interpreted as a specification, or as a special case, of the more general models suggested by these authors in that their advice explicitly emphasises the need to involve the customer during the *service* externalisation process. On the other hand, it contrasts with the more linear models

suggested by, for example, Ellram and Eddis (1996), as well as the more generic and top-down models for change management suggested by Conger (2000), for instance. One reason for this difference is probably the fact that this study takes the context of adopting service logic into account more explicitly. Reasons for the difference may also be found in the “new competitive landscape” of the twenty-first century described by Bettis and Hitt (1995), including, for example, increasing risk and uncertainty, increased dynamism, an increasing rate of technological change, etc. This is something that Ellram and Eddis and Conger do not take explicitly into account in their articles. Another reason lies in the characteristics of services, e.g. the inseparability, as well as the desire to be close to the customer if the strategy is adopting service logic. More generally, there is a need to consider the specific context of the externalisation before a change approach can be selected, and to be critical before any advice given is used in a specific situation.

6.3.4 Summary

In Table VIII, the analytical logic behind the lessons is illustrated, by providing examples of imperfect change processes used by SysCo, their consequences, and conclusions with regard to better ways of managing the externalisation. Reference is also made to the papers where more details of the mentioned problems can be found.

Table VIII. Imperfect change approach, problems, lessons and paper

Challenge	Change approach leading to externalisation problems		Externalisation problems that were observed		Lessons	Paper
Internal Change	Linear and top-down change approach.	→	Failing to take suppliers' and employees' knowledge and opinions about suppliers, strategies, and projects into account, leading to alliance initiatives that are inappropriate and/or difficult to conclude, because of internal resistance.	→	Externalisation projects should be interactive and reflective.	III, V
Strategy Formation	Neglecting to consider the interrelationship between several externalisations. Neglecting to consider the interrelationship between externalisation and service development initiatives. Neglecting to take contextual factors into account	→	Suppliers learn very much from different tasks they are awarded and may suddenly become powerful competitors, which can stop the externalisation. For example, suppliers of basic services developing solutions and becoming competitors in intended core areas of the industrial firm. Difficulties in taking alliance initiatives to conclusion	→	Externalisation initiatives should be coordinated. A combination of top-down and bottom-up change approach seems needed. Contextual factors should guide the structure of the channel for product services, in line with P1-P6 in Table IV	IV, V
Customer Relationship	Neglecting to involve customers during the externalisation process, e.g. regarding the motivation for decisions and changes associated with alliances.	→	Deteriorated credibility and risk that customers ally themselves with the suppliers. This may cause resistance to the alliance internally and externally.	→	Good customer relationships should be nurtured during externalisation projects.	I, II, V

6.4 Externalisation problems and the influences of the change context and change approach

It has now been empirically illustrated in this thesis that externalising basic services while service logic is being adopted may be problematic, in line with the predictions made earlier on in the thesis. In spite of the limited sample, some tentative conclusions of a general nature will now be drawn in relation to the research question (how and why externalisation is affected by the simultaneous intentions to adopt service logic and to externalise).

Firstly, going from industrial logic to service logic, i.e. adopting service logic, changes the structure and nature of the business environment of the firm. For example, this change may mean the emergence of new players and new borders between different firms and industries. Such turbulence in the overall competitive environment makes it difficult to plan and set definite strategies (cf. Bettis et al., 1992, Bettis et al., 1995) and this difficulty may in turn surface during the externalisation process. The externalisation process becomes more complex as it is embedded in the more general transformation associated with the adoption of service logic.

In the present study, several externalisation problems were identified and described (see, for instance, Table VI on page 2). Many of these were associated with the risk of losing the relationship with the customer. This is partly a consequence of the externalisation *per se*, but also of the more general transformation towards service logic implemented at SysCo and other firms (cf. Desmet et al., 2003, Kingman-Brundage et al., 1995, Normann, 2001, Vandermerwe et al., 1988, Vargo et al., 2004). This (perceived) risk caused resistance among both managers and employees, as well as conflicts between different employees and organisational units, making the choice and formulation of the service and sourcing strategy difficult. On the whole, the problems arising during externalisation made it proceed somewhat more slowly. Their identification also led to readjustment of the details of the change content (i.e. the simultaneous intentions). For instance, SysCo decided to in-source project management for installation. It also induced changes in the way in which the externalisation was carried out, with the new, more participative approach seeming to moderate the problems.

Secondly, because of the complex change context of the externalisation, caused by the simultaneous intentions to externalise services and adopt service logic, a rational and linear approach to the externalisation; e.g. trying to work in accordance with clearly and centrally-defined step-by-step programmes, may not be useful. In *transformational* business conditions such as during the early stages of the adoption of service logic; i.e. where the fundamental logic of the industry and the positions of the customers and suppliers are changing and where it is difficult to anticipate the borders of the system and its components, adaptation,

learning and flexibility become pivotal, as opposed to planning and rationality (cf. Normann, 1975, Prastacos et al., 2002). Under such conditions, which are similar to those of, for instance, innovation alliances (see, for instance, Marshall, 2004) where there is often significant uncertainty regarding the future, it can be expected that the process, or “the collection of tasks and activities during the externalisation” (Garvin, 1998), of externalisation will be seen by the organisation as more essential and formal planning less so.

While externalisation corresponds to a fairly small change, i.e. realignment, the adoption of service logic can be seen as a transformation. Externalisation must take the transformation into account. Otherwise, the different externalisation projects may, in the worst case scenario, lead to a decline in the industrial firm’s service business. The reasons for such a potential negative outcome may include the overall effects of the different externalisations on the adoption of service logic possibly being underestimated or neglected, or that it will be difficult to effectuate the intentions, even if these are sensible, unless the process of the change and the change approach are taken seriously.

In other words, we may draw the conclusion that externalisation will (and should) become a more iterative process which cycles between; (1) initial intentions and vision and (2) incremental steps in the externalisation process (cf. Wasner, 1999, p. 32). In the present study, such a change in the approach to externalisation could also be observed to some extent, i.e. a change from a rational and top-down approach to a more participative and iterative one where, for instance, learning from failures, local employees and customers took on a more central role (cf. Table V on page 2 and Table VIII on page 2).

More specifically, the preceding discussion can be described in terms of some *contextual features* that are inherently related to the simultaneous adoption of service logic and the externalisation of basic services. These contextual features influence the externalisation, possibly leading to problems and emphasising the importance of the process, or the way in which the externalisation is carried out:

- The complexity of the scope of the change, with the externalisation embedded in the greater transformation of adopting service logic
- The need to preserve the relationship with the customer, if service logic is to be adopted
- The conflicting business logics of industrial firms adopting service logic
- The changed balance of power caused by the commoditisation of technology and increasing complexity on the systems level

Generally speaking, neglecting to carefully consider and manage the process of externalisation may reinforce externalisation problems. In any case, it does not moderate them.

More specifically, the reasons for externalisation problems associated with the *change approach* at firms such as SysCo include:

- The usage of a linear and top-down change approach.⁴⁵
- Neglecting to consider the interrelationships between several externalisation projects
- Neglecting to consider the interrelationships between externalisation projects and service development projects
- Neglecting to take structural contextual factors (cf. Table IV) into account
- Neglecting to involve customers during the externalisation process

In essence, one conclusion drawn from the research is that, unless the change approach and the problems encountered during externalisation are taken seriously, the externalisation project may be difficult to effectuate. A fundamental reason for this is that the simultaneous and complex adoption of service logic influences the externalisation, making it more difficult to plan and carry out in a linear and top-down manner.

The results can be illustrated in a flowchart (see figure below) in which the challenges and externalisation problems, as well as the sources of the latter (change context and change approach), are included, as well as the structural context (regarding the structural context, see Paper IV for more details). In the next chapter, the contribution made by the present study to existing knowledge in the literature is summarised.

⁴⁵ It may also be described as an approach that was linear and top-down, but also, to some extent, bottom up and emergent. However, the two did not meet and were not sufficiently coordinated.

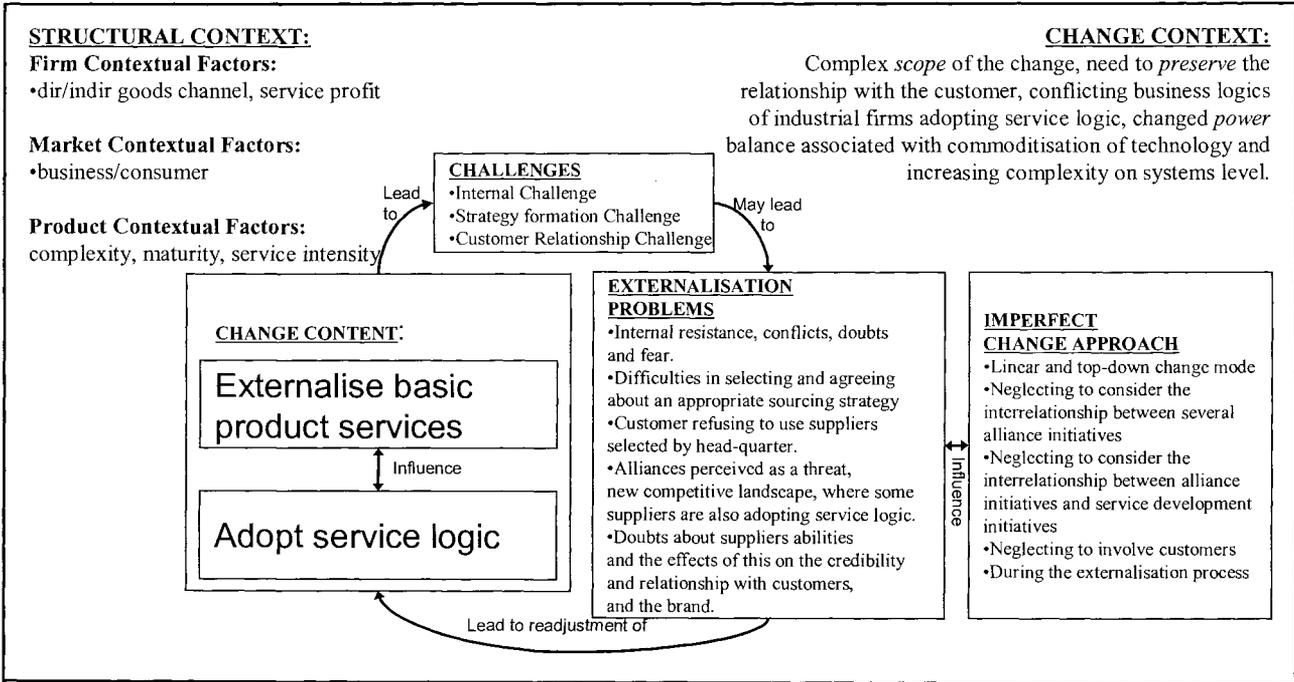


Figure 8. How and why the externalisation of basic services is influenced by the simultaneous intentions to adopt service logic and externalise basic services at industrial firms

CHAPTER SEVEN

Contributions and Implications

In this chapter, the theoretical contributions made by the research are discussed, in relation to the literature. The implications of the study for managers and policymakers are also presented. This is followed by the implications for further research and an epilogue.

7.1 Introduction

The purposes of this thesis have been; 1) to explore the problems arising, as well as their sources, associated with externalising basic services at an industrial firm simultaneous to service logic being adopted, and 2) to suggest how externalisation should be carried out so that externalisation problems are moderated. The approach to finding the answers and complying with these purposes was to study one firm in depth over several years and to combine several cross-sectional, retrospective, and longitudinal studies into an integrated whole. To my knowledge, no previous studies have been published on this topic using such an approach, thus I would suggest that I have made an empirical contribution.

Moreover, surprisingly little research explicitly addresses the externalisation of services at industrial firms which are also adopting service logic. Thus, it was also difficult to find studies addressing *problems* during such externalisation, as well as their sources. However, as mentioned in the introductory chapter, there are some publications that are relatively closely-related to the issue in focus in this thesis, i.e. O'Farrell and Wood (1999) and Allen and Chandrashekar (2000). Summarising how the results and conclusions of my study compare with their publications, as well as with a few others, provides clues as to the contributions made by this thesis to knowledge in the literature.

Before doing this, it must be noted that the present thesis is built on data from an exploratory study held at one firm. Consequently, it will be difficult to make any certain generalisations reaching beyond the studied firm and its industry. It is, however, likely that the results will be valid primarily also for similar firms in the

same and similar industries, i.e. relatively large and mature multinational firms involved in the development and delivery of complex products supplemented by product services to industrial customers and about to go further downstream. Such generalisation remains to be tested, however. Moreover, the present study focuses on a selection of all possible contextual features, rather than all of them. Other contextual features may suggest a different change approach than the one suggested in this thesis, and should be taken into account in any real change situation a firm might face.

In spite of these limitations, some suggestions for the present study's contribution to knowledge will now be discussed. These are followed by a discussion on the implications for managers, some suggestions for further research, and an epilogue. In brief, the contributions are: (1) knowledge of externalisation problems and (2) their sources, (3) issues during the adoption of service logic, and (4) the influence of (structural) contextual factors on service distribution channels.

7.2 Contribution to the literature on externalising services

Some authors (e.g., Goffin, 1999, Mathe et al., 1993) claim that more research is needed into manufacturing firms externalising services into alliances. This is an area where this thesis contributes new knowledge.

More specifically, one pivotal contribution made by the present study concerns knowledge of **externalisation problems at a firm that is also adopting service logic**. This is not explicitly addressed by any of the other studies. In the present study, exploration of the problems arising during the externalisation of services has constituted the main focus of data gathering and has been a means of answering how externalisation is influenced by the simultaneous adoption of service logic and the externalisation of basic services.

Allen and Chandrashekar (2000) highlight a number of the potential problems of outsourcing services, e.g. the risk of causing negative feelings among the employees of a firm externalising its services, the risk of a decreased level of service quality, and the loss of organisational memory, thereby reducing the possibilities of bringing the externalised activities in-house again. The present thesis provides a more detailed and comprehensive picture than theirs, and is more explicitly grounded in an empirical study. The problems identified also differ somewhat. For example, the loss of organisational memory was not explicitly addressed by the present study. Moreover, the focus of their article seems to be inclined towards the stable stage following the exploratory and developing stages, and thus differs from the present study (which focuses primarily on the exploratory and developing stages). Thus, the results of the present thesis *supplement* Allen and Chandrashekar, providing *more substantial empirical evidence* than their study.

O'Farrell and Wood (1999) primarily draw attention to one important, but hitherto largely neglected, aspect of alliance formation and development; the role of the customer in the development and success of alliances. They argue, for instance, that service alliances typically need to be sanctioned by the customer. Moreover, they emphasise that the quality of many business services is dependent on how well the customer performs in interaction with the supplier (O'Farrell et al., 1991). The present study agrees with this and *empirically* illustrates some of the potential implications, in terms of externalisation problems, i.e. that neglecting to include the customer in the externalisation may lead to problems. Thus, it *verifies* that the argumentation of O'Farrell and Wood may be generalised to industrial firms which are externalising basic services.

Furthermore, and more explicitly than either O'Farrell and Wood (1999) and Allen and Chandrashekar (2000), the present study examines the effects of implementing a *portfolio* of service alliances and not just one service or one alliance, e.g. externalising repair or installation. Moreover, several externalisation projects were studied *over time*. Thus, it was possible to see the effects on the corporate level associated with the externalising of services, e.g. the effects of one externalisation on another. From the perspective of the individual externalisation projects, the risk of creating a competitor vis-à-vis the delivery of advanced services was not as evident as when the different externalisations were studied together. Based on these findings, it was suggested that different alliance projects should be coordinated in order to assess the effects on the entire portfolio of alliances. This suggestion is more oriented towards the externalisation process than alliance management in a steady-state phase. Thus, it *supplements* the advice given by Allen and Chandrashekar (2000), i.e. to have a centralised contractor management council to discuss and co-ordinate outsourcing policies.

The results of this thesis also indicate that the risk that the externalisation of basic services may negatively influence the adoption of service logic should be taken seriously, both from the change management and strategic standpoints. The reasons for this include the risk of diluting knowledge and skills when such services are being externalised. Although the implication of this risk is not necessarily *to avoid* externalising services, the conclusion may be interpreted as a *contrast* to the conventional wisdom of externalising supplementary services to specialised service firms (see, for instance, Kotabe et al., 2001). On the other hand, Kotabe and Murray, for instance, also emphasise the need to retain the relationship with the customer when supplementary services are externalised.

Another important contribution made by this thesis concerns knowledge of the **influences of the change context and change approach on externalisation** (cf. Figure 8 on page 2). More explicitly than the other studies, the present thesis sheds light on some of the underlying sources of externalisation problems. None of the other studies addresses this explicitly, although touching upon aspects of it. In

particular, Allen and Chandrashekar (2000) and O'Farrell and Wood (1999) both emphasise the importance of involving the customer when services are externalised and alliances implemented. Since the present study focuses more explicitly on this issue, it can also provide a more elaborated picture of the factors that may influence externalisation. Although the model suggested in this thesis is not exhaustive⁴⁶, its contribution is a comparatively holistic and comprehensive depiction of the problem of externalising services while service logic is being adopted, as well as the sources of such problems. It may be classified as a *refinement* of previous knowledge.

7.3 Contribution to the literature on adopting service logic

It has been recognised by several researchers (e.g., Oliva et al., 2003) that empirically-based literature on adopting service logic at industrial firms is sparse. Furthermore, there have been calls for further research into the costs associated with implementing the service manoeuvre, especially the political costs (Mathieu, 2001b). The present thesis can be interpreted as a contribution to these areas.

It was acknowledged in Section 2.3 that some published literature exists on the topic of adopting service logic at industrial firms. Some of this has provided empirical results associated with discussion about problems arising from adoption (see, for instance, Oliva et al., 2003). One contribution made by this thesis to this literature is knowledge of **issues arising during the adoption of service logic**. It verifies that most of the issues previously identified by Oliva and Kallenberg, for instance, seem to be prevalent also at firms that have gone further in the adoption process. Moreover, in contrast to the other literature, Paper III focuses on adopting service logic when several service processes are being *externalised*, as well as the effects of this externalisation. Thus, the paper is a *verification and extension* of the previous literature.

I would also like to draw the reader's attention to another contribution to knowledge residing in the **propositions made in Paper IV** (see Table V on page 2), regarding the interrelationship between contextual factors and service distribution channels. These propositions build on previous research by Armistead and Clark (1991, 1992), Goffin (1999), Hull and Cox (1994), and Loomba (1996). Although the role of context is by no means new, see Lawrence and Lorsch (1967) for instance, the contribution made by Paper IV lies in its propositions being *more specific* than previously presented propositions, explicitly differentiating between three key service processes; i.e. contracting, ordering, and expediting. In addition, the effects of maladjustments, i.e. divergence from the appropriate service channel structure suggested by the contextual factors, are examined in Paper IV. This can be seen as a *refinement and extension* of previous theory.

⁴⁶ For instance, firm specific and situational features are excluded; see Section 3.3.2 on page 2.

7.4 Implications for managers

In this thesis, it has been empirically illustrated that it is not an exaggeration to claim that the externalisation of services at industrial firms is a significant managerial challenge. Furthermore, just *how* this change process is carried out seems to be important for the progress of the externalisation project.

Although this thesis is based on a small sample and contains results that require further elaboration, it has provided some lessons regarding ways of managing the externalisation process. These lessons are based on the empirical research leading to this thesis and would seem to be useful for managers involved in the externalisation of services. They deal with the inherent challenges associated with externalising services while service logic is being adopted, and would seem to improve the chances of externalisation coming to fruition. To sum up, the lessons about how to manage the externalisation of basic services were:

- The management of externalisation projects should be participative and reflective.
- Externalisation projects should be coordinated.
- A combination of top-down and bottom-up change approaches seems necessary.
- Contextual factors should guide the structure of the channel for product services; in line with P1-P6 in Table IV (page 2).
- Customer relationships should be nurtured during externalisation projects.

The lessons may be further synthesised into a more general conclusion; i.e. that externalising basic services while adopting service logic should be seen as a *constructive* change process (cf. Van de Ven & Poole, 1995). While a *prescribed* mode of change progresses in a predetermined direction and in a predictable way, a constructive change is more unpredictable and discontinuous. Externalisation should be carried out in close participation with suppliers, employees, and customers, with a central externalisation office coordinating the different projects and developing and readjusting strategies based on experiences and feedback. Using such an approach, externalisation may be more turbulent and less predictable, but the more participative approach may also lead to less resistance to the change. It can also be expected to lead to better outcomes as it makes better use of knowledge that is both internal and external to the organisation. Such an approach may be useful since, through a recurring sequence of gradually readjusted visions, intentions and feedback cycles, it more easily breaks with past assumptions and better exploits and creates knowledge within the organisation (Van de Ven et al., 1995, p. 523).

Of course, there are also *structural* solutions which may be used in conjunction with the *processual* solutions (i.e. the change approach) suggested in this thesis.

Potential structural solutions include choosing between different sorts of alliances such as mergers and acquisitions and joint ventures, or more collaborative alliances based on a high level of trust. Other potential solutions include working with lock-in effects, government regulations, and, perhaps, creating a separate service organisation. These solutions, however, are outside the focus of this thesis and I will now suggest a few potential areas for further research.

7.5 Implications for future research

There are several potential areas for future research; of these, a few will be mentioned here.

Firstly, as the present study is not based on any data directly gleaned from customers, a similar study from the perspective of the customer would also enhance our understanding of externalisation. A similar study from the perspective of the service suppliers of firms such as SysCo would probably also be fruitful.

Secondly, seeking to generalise the findings of this study to other relatively large multinational firms involved in the delivery of complex products and product services, and perhaps also to other industries. This would typically require broader samples. Of equal interest would be conducting a similar study but in another (better) business situation, with regard to other services and with regard to firms with more experience of similar situations.

Thirdly, one possible area would be to study the externalisation of services in even greater depth, as a suggestion longitudinally, to obtain an even better understanding of the process, as well as the underlying reasons for problems associated with it. One limitation of the present study is that it primarily focused on the externalisation problems encountered but only secondarily on the way the externalisation was carried out. Thus, even greater depth is needed.

Fourthly, focusing on a narrower set of services and alliances would enable greater depth than was possible in this study. Even though the present study focused primarily on basic services (very probably affecting the results), even these are multifaceted.

Finally, investigating the long-term implications of externalising the delivery of product services for the business of an industrial firm would also be of interest to study; as a suggestion, longitudinally. The present study touched upon this issue slightly, even though it was by no means in focus. Although a few externalisation problems were identified, no conclusions were drawn as regards the long-term effects of externalisation. Two important questions that emerge here are: How can the positive aspects of the externalising of services be exploited and the potentially negative long-term effects counteracted? What kinds of alliances can we expect

between industrial and service firms in the future? These questions and others beg answers.

7.6 Epilogue

In the introduction to this thesis, there is an excerpt from an interview with a senior manager at SysCo Services, expressing his concerns regarding the decision to externalise services as well as how to make other managers take the step of externalising their services. It is difficult to provide a simple solution to his concerns, but based on the research, the response lies in convincing his managers that it is a matter of both structure and process. Rather than trying to convince those managers about the rationale for externalising certain services, he should be making them realise that there is no omnipotent, best delivery strategy for services and asking them to take contextual factors into account. He should also ask them to care about the way the externalisation is carried out.

Externalising services is a complex change process, particularly if service logic is also being adopted. It is not just a question of allocating time to strategic analysis and finding the right arguments. There is also a need for flexibility during the change process. Another excerpt may illustrate this, also from a senior manager at SysCo services:

“We have never been able to identify changes. And my conclusion from this is that we need to guard against unforeseeable events and be flexible, rather than plan”

Externalisation may be likened to *walking a tightrope* between the industrial and service logics; a difficult balancing act between efficiency of operations (e.g. minimising cost through externalising basic services) and effectiveness of marketing (e.g. providing customers with convenience by adopting service logic). This is all about exploiting opportunities for cost efficiency without losing sight of the customers. It is about being close to the customer and keeping operations efficient. It is about being adaptive to changes internally, at the supplier's, and at the customer's during externalisation. It is a balancing act that requires concentration, flexibility, skills, and direction. The propositions put forth in this thesis⁴⁷, as well as the contextual features described⁴⁸, may be a starting point for such a balancing act, indicating the direction of the externalisation. The lessons for managers⁴⁹ provide guidance as regards *how* to move in that direction while on the tightrope.

⁴⁷ Table IV on page 2.

⁴⁸ Section 6.4.

⁴⁹ Section 6.3 (summarised in Section 7.4).

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APPENDIX 1

Interview Guide for Study 1

INTRODUCTION

- *Us* - name and background
- *Study* - background, objectives, why here (firm/person)
- Confidentiality and next step in data analysis

GENERAL COMPANY INFORMATION

- The interviewee - background and current position
- Business - products, competitors, sales
- Organisation - size, structure, chart, person

WHAT RELATIONSHIPS DO YOU HAVE WITH EXTERNAL COMPANIES?

- Types of relationships with external companies (partnerships/alliances)
- Number of suppliers per service
- Amount of detail in contracts
- Length of contracts
- What is outsourced
- Co-operation with competitors?
- Alliance-ready (core competence and competitiveness thinking)
- Introduction phase of these relationships
- Customers/Suppliers

WHAT ARE THE MOTIVES FOR HAVING THESE RELATIONSHIPS

- *Motives* for collaboration with external companies
- *Driving forces* behind this trend
- *Reasons* for outsourcing
- What is the core competence(s)
- *Definition* of core competence
- *Strategy* for external relationships

HOW DOES THE IMPLEMENTATION OF THE RELATIONSHIPS WORK?

- Implementation
- Selection of suppliers
- Training of suppliers
- Communication with suppliers
- Joint meetings with suppliers

HOW DO YOU ORGANISE THE MANAGEMENT OF THE RELATIONSHIPS

- Organisation to handle the relationships
- Management of relationships
- Information provided to and from suppliers
- Career paths for managing external relationships

WHAT ISSUES AND SUCCESS FACTORS ARE RELATED TO THESE EXTERNAL RELATIONS?

- Problem areas in supplier relationships
- Challenges to implementing co-operative relationships
- Does the company culture foster co-operation
- Communication
- Power
- Knowledge Management/Transfer

WHAT RESULTS CAN YOU SEE FROM THESE RELATIONSHIPS?

- Results of partnerships
- Internal consequences of the results
- Consequences of outsourcing on corporate culture

FINAL QUESTIONS

- Personal experience of co-operative relationships
- Sources of knowledge of co-operative relationships
- Difference between outsourcing manufacturing and services?
- Interesting cases
- Suggestions for further research within this area
- Possible to return for supplementary questions?
- Proposal for other interviewees?

APPENDIX 2

List of Interviews

Study				Description	Date
I	II	III	IV		
I				Manager, Hardware Services	2001-01-23
I				Process Manager, Hardware Services	2001-01-30
I				Manager, Sourcing and Master Planning	2001-01-31
I				Manager, System Support	2001-02-06
I				Supply Chain Developer	2001-02-06
I				Manager, Field Services	2001-02-09
I				Regional Manager, Customer Support	2001-02-14
I				Vice President, Global Services	2001-02-19
I				Manager, Regional Support Office EMEA	2001-02-20
I				Manager, Human Resources	2001-02-20
I				Internal Sourcing Process Consultant	2001-02-23
I				Vice President, Corporate Strategic Alliances	2001-02-23
I				Program Manager, Partnering and Sourcing	2001-02-28
I				Senior Contract Manager, Customer Support	2001-02-28
I				Senior Contract Manager, Customer Support	2001-02-28
I				Manager, Customer Support	2001-03-06
I				Marketing Manager, Professional Services	2001-03-15
I				Serviceability Engineer, ex Repair Centre Manager	2001-03-20
I				Project Manager, Installation Services	2001-03-21
	II			Manager, Training Alliances	2001-10-04
	II			Partner Manager, Training Services	2001-10-10
	II			Process Manager, Service Alliances	2001-10-10
	II			Manager, Training Alliances	2001-10-29
	II			Process Manager, Service Alliances	2001-11-22
	II			Partner Manager, Training Services	2001-11-30
	II			Process Manager, Service Alliances	2001-12-13
	II			Manager, Training Alliances	2002-01-09
	II			Process Manager, Service Alliances	2002-01-09
	II			Partner Manager, Training Services	2002-01-11
	II			Strategic Product Manager, Training	2002-01-25
	II			Delivery Manager, Training Services	2002-01-30
	II			Partner Manager, Training Services	2002-02-05
	II			Process Manager, Service Alliances	2002-02-05
	II			Product Manager, Training Services	2002-02-06

Appendix 2: List of interviews (continued)

II	Delivery Manager, Training Services	2002-02-11
II	Marketing Manager, Training	2002-02-12
II	Partner Manager, TeachIT	2002-03-12
II	Manager, Training Alliances	2002-04-09
II	Partner Manager, Training Services	2002-04-09
II	Process Manager, Service Alliances	2002-04-09
II	Partner Manager, Training Services	2002-04-15
II	Partner Manager, Training Services	2002-04-24
II	Manager, Training Alliances	2002-04-29
II	Partner Manager, Training Services	2002-06-26
II	Sales Coordinator, EMEA	2002-07-01
II	Manager, Training Services EMEA	2002-07-02
III	Outsourcing Engagement Director	2003-01-03
III	Manager, Product Management and Marketing	2003-01-04
III	Vice President, Foresight	2003-01-22
III	Marketing Manager, Global Services	2003-01-24
III	Regional Manager, Customer Support	2003-01-24
III	Manager, Product Management, Business Solutions	2003-01-27
III	Product Manager, Business Solutions	2003-01-27
III	Product Manager, Business Solutions	2003-01-28
III	Partner Manager, Training Services	2003-01-29
III IV	Manager, Customer Support at Epsilon	2003-01-31
III	Senior Contract Manager, Customer Support	2003-01-31
III IV	Manager, Partnering and Sourcing, Customer Support	2003-02-12
III	Vice President, Global Services	2003-02-12
III	Manager, Partnering & Sourcing, Installation Services	2003-02-17
II	Manager, Training Services EMEA	2003-02-27
II	Partner Manager, Training Services	2003-02-27
	IV Business Development at Alpha	2003-04-10
	IV Business Intelligence at Alpha	2003-04-10
	IV Technical Co-ordinator at Alpha	2003-04-11
	IV Business Development at Alpha	2003-05-26
	IV Service Product Manager at Alpha	2003-05-26
	IV Procurement at Beta	2003-06-10
	IV Procurement at Beta	2003-06-10
	IV Manager Technical Support Marketing at Beta	2003-06-19
	IV Sourcing Manager at Delta	2003-06-25

Appendix 2: List of interviews (continued)

	IV	Sourcing Manager at Alpha	2003-06-26
	IV	Sales Manager, Product Support Services at Beta	2003-08-13
	IV	Spare Parts Engineer at Alpha	2003-08-20
III		Partner Manager, Training Services	2003-09-28
III	IV	Senior Contracts Manager, Customer Support	2003-09-28
III		Regional Manager, Customer Support	2003-09-29
III		Marketing Manager, Global Services	2003-10-01
III		Partner Program Manager	2003-10-02
III		Product Manager, Business Solutions	2003-10-02
III		Product Manager, Business Solutions	2003-10-02
III		Manager, Product Management and Marketing	2003-10-03
III		Product Manager Consulting Services	2003-10-07
III		Project Manager, Product Platform Development	2003-10-10
III		Vice President, Partnering and Strategy	2003-10-10
III		Vice President, Global Services	2003-10-14
III		Manager, Solutions	2003-10-15
III	IV	Manager, Customer Support at Epsilon	2003-10-21
	IV	After Sales Project Manager at Delta	2003-10-24
III		Manager, Partnering and Sourcing, Customer Support	2003-11-06
III		Contracts Manager, Installation Services	2003-11-12
	IV	Sales Manager, Product Support Services at Beta	2003-11-17

APPENDIX 3

Questionnaire For Study 2

QUESTIONNAIRE ABOUT ALLIANCE BETWEEN SYSCO AND TEACHIT

This questionnaire is part of a research programme being conducted with regard to alliances and partnerships. Its purpose is to learn more about how different units work together in an alliance context. The results of the survey will be used to identify organisational issues and to suggest whether or not and where improvements can be made in order to improve organisational effectiveness and productivity.

This questionnaire mainly focuses on collaboration *within* SysCo Services and *between* SysCo Services and TeachIT. Each of the questions will probe some aspect of the relationships existing within your unit and between different units.

Your answers will be especially helpful as regards understanding how units perceive the contents and process of the alliance. Moreover, I hope that answering the questions will help you to step back and reflect upon how the alliance is working.

Your answers are strictly confidential. They will be grouped together with the answers given by other people, and no individual person will ever be identified in any report.

I have developed this survey as a researcher on the FENIX programme (www.fenix.chalmers.se) at the Stockholm School of Economics, and as an employee of SysCo. I am also conducting it. The individual details included in the results are my property and will not be available to anyone in your organisation. I am personally responsible for suggesting improvements resulting from the survey.

Thank you very much for your co-operation.

Fredrik Nordin

Instruction

Choose the number that most accurately reflects your answer to each question and circle it. If you do not understand a question, PLEASE BE SURE TO ASK ME FOR HELP. I realise that not all of the questions are straightforward.

Introductory questions

1. Name of your organisation: _____
2. Your name (Optional) _____

Main questions

Q1. Consider the equality of the give-and-take relationship in the alliance. How fair do you feel the “payoffs” from TeachIT to SysCo are?

We get much less than we ought to	We get slightly less than we ought to	Balanced	We get slightly more than we ought to	We get much more than we ought to
1	2	3	4	5

Q2. To what extent has TeachIT fulfilled its responsibilities and commitments vis-à-vis SysCo over the past year?

No extent	Little extent	Some extent	Considerable extent	Great extent
1	2	3	4	5

Q3. To what extent has SysCo fulfilled its responsibilities and commitments vis-à-vis TeachIT over the past year?

No extent	Little extent	Some extent	Considerable extent	Great extent
1	2	3	4	5

Q4. To what extent do you feel the relationship between SysCo and TeachIT is productive?

No extent	Little extent	Some extent	Considerable extent	Great extent
1	2	3	4	5

- Q5. To what extent is the time and effort spent on developing and maintaining the relationship with TeachIT worthwhile?

No extent	Little extent	Some extent	Considerable extent	Great extent
1	2	3	4	5

- Q6. Overall, to what extent were you satisfied with the relationship between SysCo and TeachIT over the past year?

No extent	Little extent	Some extent	Considerable extent	Great extent
1	2	3	4	5

- Q7. For TeachIT to meet its goals and responsibilities, how much does it need the services, resources, or support of SysCo?

Not at all	Very little	Slightly	Quite a bit	Very much
1	2	3	4	5

- Q8. For SysCo to meet its goals and responsibilities, how much does it need the services, resources or support of TeachIT?

Not at all	Very little	Slightly	Quite a bit	Very much
1	2	3	4	5

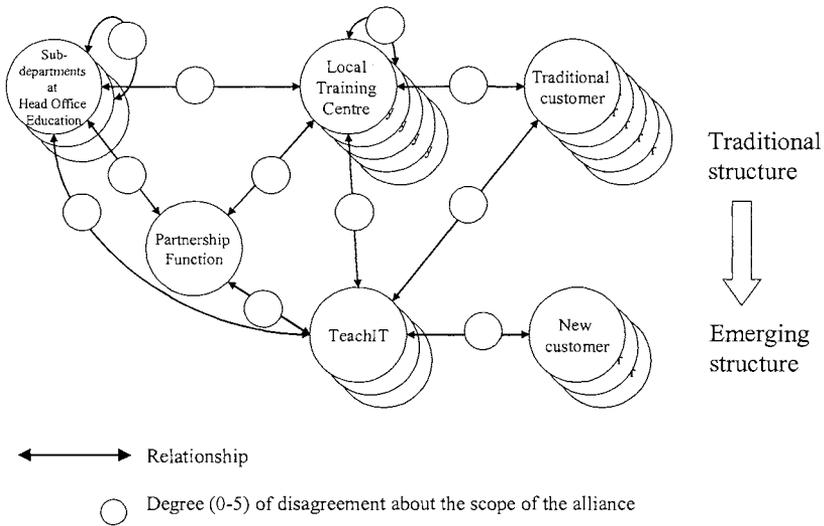
- Q9. How important was TeachIT as regards attaining the goals of SysCo over the past year?

Not very important	Slightly important	Quite important	Very important	Absolutely crucial
1	2	3	4	5

Q10. Over the past year, how much have these units disagreed about an appropriate scope for the alliance? (E.g. products, markets, processes, etc)

Use the following scale and mark your answer in the small grey circles in the sociogram below:

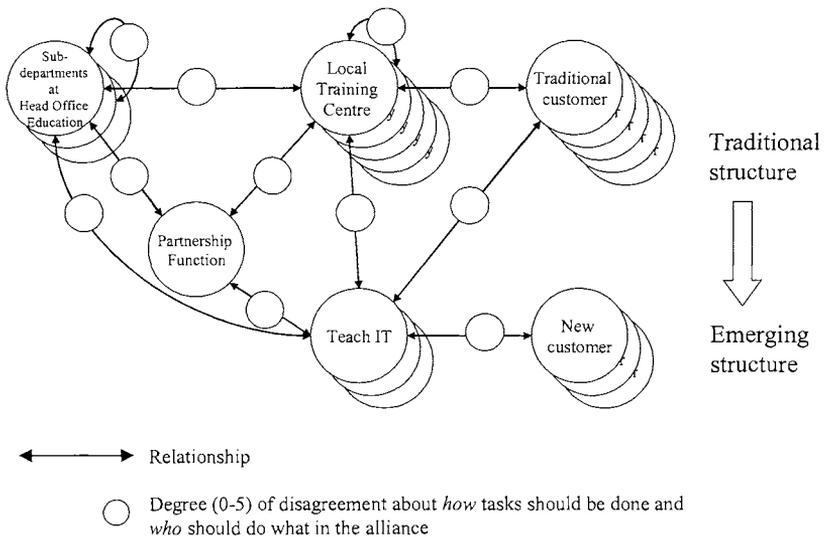
Don't know	No disagreement	Disagree a little	Disagree to some extent	Disagree quite a bit	Disagree very much
0	1	2	3	4	5



Q11. Over the past year, how much have these units disagreed about *how* tasks should be done and *who* should do *what* in the alliance?

Use the following scale and mark your answer in the small grey circles in the sociogram below:

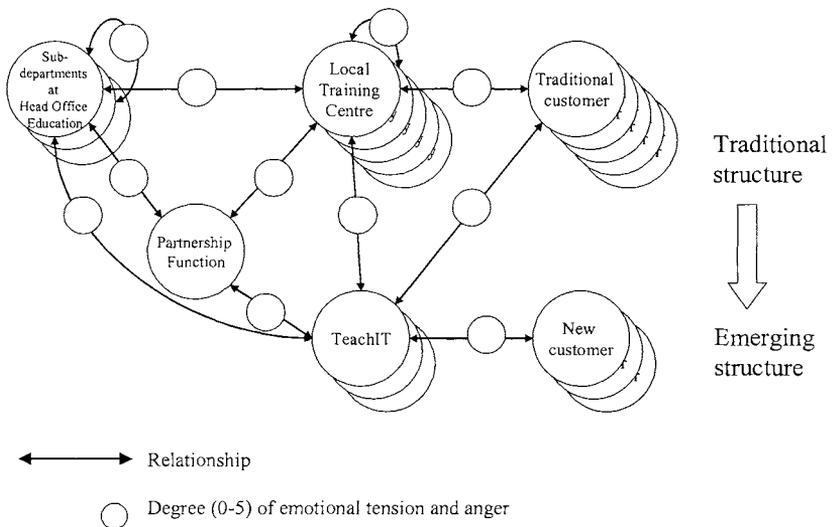
Don't know	No disagreement	Disagree a little	Disagree to some extent	Disagree quite a bit	Disagree very much
0	1	2	3	4	5



Q12. How much emotional tension and anger between the individuals of the two units has there been over the past year?

Use the following scale and mark your answer in the small grey circles in the sociogram below:

Don't know	No tension	Little tension	Some tension	Much tension	Very much tension
0	1	2	3	4	5



In the following two questions, mark your answer with a cross in the tables below.

	Not once	About 1-3 times a month	About 1-3 times a week	About 1-3 times a day	About every hour
Q13. During the past year, how often did you receive or send written reports or e-mails related to your work from each of the following units?					
1. Any other unit within the education practice					
2. Partnership support function					
3. Any SysCo training centre					
4. Any traditional customer					
5. Any new customer					
6. TeachIT					

	Not once	About 1-3 times a month	About 1-3 times a week	About 1-3 times a day	About every hour
Q14. During the past year, how often did you have work-related discussions (face-to-face or by telephone) with each of the following units?					
1. Any other unit within the education practice					
2. Partnership support function					
3. Any SysCo training centre					
4. Any traditional customer					
5. Any new customer					
6. TeachIT					

Q15. When disagreements or disputes relating to the alliance occurred over the past year, how often were they handled in the following four ways?

a. *By avoiding or ignoring the issue?*

Almost never	Seldom	About half the time	Often	Almost always
1	2	3	4	5

b. *By smoothing over the issue?*

Almost never	Seldom	About half the time	Often	Almost always
1	2	3	4	5

c. *By bringing the issue out into the open and working it out jointly?*

Almost never	Seldom	About half the time	Often	Almost always
1	2	3	4	5

d. *By getting a high-level manager or other authority to resolve the issue?*

Almost never	Seldom	About half the time	Often	Almost always
1	2	3	4	5

Now, do a self-assessment of the most problematic relationships you feel that your unit maintains with other units.

Hopefully, the questions you have answered so far have stimulated you into making a self-assessment like this.

Describe the major problems you have encountered in your relationship with each of the other units over the past year	Suggest some specific ways of overcoming these problems with each of the other units
Other Unit 1 Name _____	
Other Unit 2 Name _____	
Other Unit 3 Name _____	
Other Unit 4 Name _____	

Finally, do you have any other suggestions or comments regarding what has been good and/or bad about the alliance with TeachIT?

Write these suggestions or comments here

APPENDIX 4

Papers

PAPER I:

IMPLEMENTING SERVICE SUPPLY RELATIONSHIPS

IMPLEMENTING SERVICE SUPPLY RELATIONSHIPS

Pär Åhlström and Fredrik Nordin

To be revised and submitted for second review in *Journal of Purchasing and Supply Management*

Abstract

Literature on supply chain management has mostly focused the exchange of goods and has tended to ignore the issue of implementation. To this end, the aim of this paper is to identify problem areas encountered when implementing service supply relationships. Case research has been carried out within the service division of a global company, analyzing eleven instances of implementing (or trying to implement) a relationship with an outside company in order to provide service to the customer. Four problem areas are identified through inductive analysis. First, writing legal agreements for service exchanges. Second, clearly specifying processes to enable leaving them to suppliers. Third, handing over the actual point of delivering the service to a supplier. Fourth, and finally, losing control over the relationship with the customer.

Introduction

Companies increasingly focus on their core competencies (Prahalad & Hamel, 1990), which often mean that complementary competencies have to be obtained from other firms (Collis and Montgomery, 1995, Leonard-Barton, 1992, Doz and Hamel, 1998, Nooteboom, 1998, McIvor, 2000). Regardless of terminology used for describing how companies obtain these complementary competencies – partnerships (Lambert et al., 1996, Bensaou, 1999); alliances (Gomes-Casseres, 1996, Nooteboom, 1998, Doz and Hamel, 1998); outsourcing (McIvor, 2000, Kotabe and Murray, 2001, Allen and Chandrashekar, 2000, Marwaha and Tommerdahl, 1995); or supply chain management (Handfield, 1999, Lambert et al., 1998, Croom et al., 2000, Giannakis, 2001, Skjoett-Larsen, 1999) – it results in a need to implement supply relationships.

Despite the trend towards closer collaboration with external companies in supply relationships, there is evidence that many efforts have failed to meet the expectations (Barringer and Harrison, 2000, McIvor, 2000, Stuart and McCutcheon, 2000). Still, the problems of implementing supply relationships is not that well researched (Boddy et al., 2000, Elmuti and Kathawala, 2001, Stuart and McCutcheon, 1996, Spekman et al., 1998).

Furthermore, most literature on supply chain management has so far focused on the exchange of goods, and the usefulness for services of the models developed for manufacturing has not been sufficiently examined (Giannakis, 2001). Due to the

characteristics of services, the exchange of services in the supply chain poses different risks and challenges to the purchasing company (Fitzsimmons and Fitzsimmons, 2000).

Both areas mentioned above serve as background to this paper: 1) the lack of studies on the implementation of supply relationships and 2) the lack of studies investigating supply chains where services, not physical goods, are being exchanged between companies. The purpose of the paper is to identify problem areas encountered when implementing service supply relationships.

Problem background and research motivation

Implementing supply relationships

The literature on supply chain management can, from the perspective of interest in the present paper, be seen as part of the literature on partnerships and alliances. When discussing the problems of implementing service supply relationships, we can draw on the broader literature on alliances, partnerships and other types of inter-firm collaboration.

Most research on inter-firm collaboration has so far has been about the benefits of the collaboration. Recently, however, literature focusing on challenges and problems during the implementation of collaboration between companies is appearing. According to many of these studies, the problems encountered are very often about soft issues, related to collaboration among people. Examples include:

- Insufficient communication (Sahakian, 1998, Kelly et al., 2002)
- Conflicts (Lorange and Roos, 1991, Mohr and Spekman, 1994, Moore, 1998, Mentzer et al., 2000)
- Lack of trust (Elmuti and Kathawala, 2001, Gulati, 1995, Parkhe, 1998)
- Culture (Elmuti and Kathawala, 2001, Kelly et al., 2000, Lorange and Roos, 1991, Vyas et al., 1995)
- Organisational politics (Lorange and Roos, 1992)

A second group of problems are operational, for example insufficient specifications or quality problems (Kelly et al., 2002, Elmuti and Kathawala, 2001). A third group is the strategic problems, for example the risk of losing core competencies to the partner (Elmuti and Kathawala, 2001, Lorange and Roos, 1992). Finally, the performance or the results of the collaboration are sometimes referred to as problematic (Kelly et al., 2002, Elmuti and Kathawala, 2001). Based on research on the early stages in alliances among manufacturing, service and R&D-based companies, (Kelly et al., 2002) found that the majority of the problems (55%) were related to soft issues. Operational problems accounted for

29%, strategic problems for 11%, and performance-related problems accounted for 5%.

Although these studies have significantly advanced the knowledge of alliance implementation issues, they generally don't take the differences between different types alliances into account. First of all, existing studies don't consider differences in the scope of the studied alliances. Alliances can take a number of forms, perhaps most importantly regarding the degree of co-operation. The degree of co-operation can vary from a short-term focus, involving only one division or functional area within each organisation, to the organisations sharing a significant level of integration, where each party views the other as an extension of their own firm (Lambert et al., 1996).

A second shortcoming of existing literature is that it does not consider the differences in problems that arise when companies from different industries and markets implement alliances. Although existing studies provide very useful information on generic problems, they give little details on more specific problems. Of particular interest here, existing studies do not focus on the implementation of supply relationships to provide services to customers, in industrial markets. In fact, there is a general lack of empirical research into the difficulties of procuring services (Smeltzer and Ogden, 2002). The lack of studies into services is also apparent concerning the provision of services in collaboration with suppliers, which is the focus in the present paper.

Providing services in collaboration with suppliers entails different risks and challenges compared with alliances focusing on developing and producing goods, due to the characteristics of services (Fitzsimmons and Fitzsimmons, 2000). The intangible nature of services makes the evaluation of the vendor more difficult and the specification of the service desired less precise. Many services have to be delivered close to the customer and cannot be centralised, and this makes the delivery structures for service alliances more complex. Judging whether the delivered services meet expectations is more difficult, because services are not subject to close scrutiny (Fitzsimmons et al., 1998). The relational nature of services (Grönroos, 2000) implies that the customer to a larger extent must be taken into account when implementing service alliances (O'Farrell, 1999). Service supply chains are often bi-directional and production flows both from suppliers to customers and from customers to suppliers. Thus, there is a "customer-supplier duality" where the customers are also suppliers (Sampson, 2000). Many businesses service quality depends not only upon the performance of the supplier but also on the customer's performance in the interaction with the supplier (O'Farrell and Moffat, 1991). The implication of services' characteristics for the implementation of service supply relationships is the main focus of our research.

Supply relationships in providing business-to-business services

Within the area of services, we focus on business-to-business services, not business-to-consumer services, which make up the majority of studies on service management (Andersson and Norrman, 2002, Fitzsimmons et al., 1998). The rationale for our interest in business-to-business services is that these markets have certain characteristics that are potentially important when implementing supply relationships: heterogeneity, co-evolution, and interdependence (Ford et al., 1998). Business services often need to be customized and are based on a greater complexity of organizational needs. Therefore, the supply of business services must be handled differently from the supply of consumer services (Fitzsimmons et al., 1998).

Industrial business relationships are distinctive in several ways compared with consumer relationships. The purchasing process is more complex and involves multiple employees from both sides of the relationship, from different hierarchical levels and different functions in the organizations (Ford, 2002). The business purchasers are trained professionals, sometimes making the purchasing procedure more formalized (Johnston, 1981). The complexity of many business services often makes the time-span longer for the purchasing process (Webster, 1991).

A further important difference is that in industrial markets the customer relationships are often close and long lasting. In business-to-business services, the actual service encounter accounts for a relatively small part of the relationship between buyer and seller. The interaction process between buyer and seller is by some divided into “episodes” or in the relationship, e.g. the service encounters, and the longer-term “relationships” which are interrelated to the episodes (Håkansson, 1982). The “episodes” or “transactions” between different actors are framed by relationships (Normann, 2001). The importance of the service encounter is thus often less critical than in consumer relationships. In business-to-business markets the service encounters are only an element of an ongoing sequence of episodes between the customer and the service firm (Grönroos, 1994, Gummesson, 2002). All these differences lead to our interest in studying the implementation of service supply relationships in industrial markets.

Definition of research questions

So far we have elaborated on the background to and motivation for our research. We now go on to provide a clearer definition of our research questions. Our interest is in the implementation of service supply relationships. Three things need to be kept in mind here:

First, we focus on identifying problem areas during implementation. These are areas where problems arise as a result of implementing or attempting to implement supply relationships to provide services in business-to-business markets.

Second, we focus on problem areas that appear due to the characteristics of services. We thus exclude from our analysis the problems that are general to implementation of supply relationships, which have been described in previous literature.

Third, we focus on problem areas that are related to the relationship being implemented. We are not interested in problems that are internal to the company. These types of problems have been thoroughly documented in previous literature.

With these definitions and delimitations, we can now formulate the main research question guiding the research in the paper:

Q1. In what areas are problems encountered during implementation of service supply relationships?

This main research question is extended in two directions. We need to examine the effects on problem areas of (a) the type of supply relationship and (b) the stage in the relationship.

Problem areas and type of supply relationship

As argued above, in the review of literature on problems in implementing alliances, existing literature largely ignores the effect of the type of alliance on problem areas. Concerning services, there are strong reasons to expect that the type of supply relationship being implemented has an impact on the problems encountered. The major reason for this is that the closeness between the supplier and the customer will vary depending on the service supply relationships. The structure of the service delivery process and each company's position and role in the process is important in services. Services are inherently relational, because the customer always has to interact with the service provider in some way (Grönroos, 2000), and thus the position a company in relation to its customers is important.

Furthermore, our interest in the structure is based upon the increasing importance of downstream activities such as distribution and after-sales services, which is pushed by a stagnating product demand and an expanding installed base in many industries (Wise and Baumgartner, 1999). The most powerful participant in a supply relationship in terms of their influence on the design of the delivery system is normally the service firm or the intermediary providing the services (Light, 1986). This power has been increasing lately due to for example better management information systems (Stern and Weitz, 1997) and many industrial customers' move from adversarial relationships with suppliers to more co-operative (Swift, 1995). Thus, we formulate the following research question:

Q2. Are there any differences in problem areas encountered depending on the type of supply relationship?

Implementing a service supply relationship does not necessarily mean that the relationship to the customer is externalized. The central variable here is how close

to the supplier/partner that the customer will become. A useful way to distinguish between different types of supply relationships has been suggested by Johnston and Clark (2001):

- *Simple supply chain.* In this type of relationship the provider needs to ensure that its own key suppliers meet targets to enable the provider to deliver services to its customers. The supplier is thus not in a direct relationship with the end-customer.
- *Management through intermediaries.* Here the service provider uses some kind of middleman to deliver services to its customers. The provider thus has (at least) one layer between itself and the customer. This is a common form of relationship in for instance after-sales services (Ford et al., 1998).
- *Supply partnership.* This type of relationship relates to the formation of a partnership or alliance to provide a jointly managed service delivery mechanism.

Although this classification by no means is exhaustive, and there are other classifications of the type of relationship, it does provide a starting point for investigating the effects of the type of supply relationship on problem areas. Figure 1 illustrates the difference between these three, concerning the flow of goods, services and information.

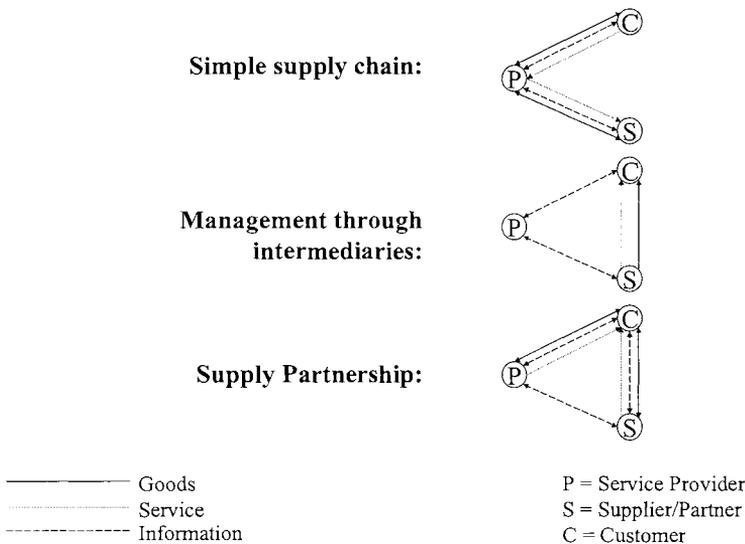


Figure 1. Types of supply relationships

Problem areas and stage in the relationship

Our investigation into the problem areas encountered during implementation of service supply relationships also needs to take into consideration the stage in the relationship (Ford, 1980). There are reasons to expect that the problems encountered when implementing supply relationships are different depending upon how far the relationship has developed (Ford et al., 1998). Ford et al. (1998) argue that in general terms, prior to going into the relationship, sources of inertia are lack of resources for evaluating suppliers and the cost of and reluctance to change. During the ensuing serious discussions and negotiations, uncertain future benefits and a lack of trust are the main inhibitors. When the contract has been negotiated and business is growing, the main inertia is that of learning and adapting.

A key reason to expect the problem areas to be different has to do with the relational characteristics of services (Grönroos, 2000). The customer will only enter into the service supply relationship in the later stages of the relationship, hence the problems in later stages can be expected to be different from the problems in the early stages of the supply relationship. This leads to our third research question:

Q3. Are there any differences in problem areas encountered depending on the stage in the relationship?

Different authors have suggested alternative definitions of stages in the development of supply relationships. A number of authors use three stages. Noteboom (Nooteboom, 1998) uses the stages contact, contract, and control. Scanzoni (1979) uses the stages exploration, expansion, and commitment. Ring and Van de Ven (1994) suggest the stages negotiation, commitment, and execution. Other authors use four stages, for example Hallen and Wiedersheim-Paul (1984) who use the stages pre-contact, initial interaction, development, and mature relationship.

Finally, there are those who use five stages. One example here is Ellram and Eddis (1996), who differentiate between: preliminary phase, identify potential partners, screen and select, establish relationship and evaluate relationship. Another division into the five stages is: awareness, exploration, expansion, commitment, and dissolution (Dwyer et al., 1987, Levitt, 1983). Wilson (1995) use the stages partner selection, defining purpose, setting relationship value, and relationship maintenance.

The main difference between the definitions above is one of how much detail is used to describe the various stages and the attendant number of stages. As a middle ground to the above-mentioned definitions, we chose a definition encompassing four stages (Ford et al., 1998).

- Before negotiations - *Pre-relationship Stage*

- During serious discussions and negotiations - *Exploratory Stage*
- Growing or changing business – *Developing Stage*
- When stability or routine has been reached - *Stable Stage*

The main motivation for this choice is that the exact division into stages is not as important as actually taking the stage of the relationship into consideration. In reality, the four stages normally overlap and a relationship does not normally evolve in such a predetermined way – it is not a linear process of moving the relationship in one direction. We still believe that it is useful to separate these stages for analytical purposes, and that each phase has its own characteristics, including its own implementation problems.

Method

Research design

The paper is based on case research. Research into implementation issues in service supply chains is scarce, which makes case studies an appropriate choice, since they suit questions which are not thoroughly researched (McCutcheon and Meredith, 1993, Leonard-Barton, 1990). Case studies are also appropriate when one is interested in questions concerning “how” and “why”(Yin, 1989).

The research is carried out within one global company selling high technology products to business customers. Adding services to the products is becoming increasingly important for the way the company competes. About one fifth of the company's employees work within the service division. The company is currently undergoing transformation, from having performed most activities associated with developing, manufacturing and servicing the products internally towards relying on external partners for non-core activities. The case thus provides us with a chance to investigate our research problem in a variety of different service settings.

Although we have conducted our research within one company, we have several cases, since our research focuses several services provided by the company. Thus, we define a case as one instance of implementing (or trying to implement) a relationship with an outside company in order to provide service to the customer. In total, the research covers eleven different cases. More details on the cases can be found in the data section.

Data collection

Data were collected through 17 semi-structured interviews with several types of respondents. We taped all interviews and transcribed them immediately after each interview. We chose semi-structured interviews to remain flexible during data collection. The focus of our interviews was problems that had been experienced

upon implementing supply relationships. Our research framework was used to direct our attention, since collecting data requires knowing what to look for (Eisenhardt, 1989). To allow for inductive inquiry (Mintzberg, 1979), our research framework was the starting point but we retained flexibility to incorporate observations outside the framework, if they related to the implementation of supply relationships.

Considering the exploratory nature of our research, our aim was to interview a broad spectrum of people to maximize our chances of discovering problems related to implementing supply relationships. Our respondents held different positions, at different hierarchical levels of the company. They included executives at a divisional level, managers responsible for setting up and running supply relationships, as well as employees working in these relationships.

We also chose respondents with experience from a broad range of services within the company. The respondents belong to three different types of service organizations, as divided by the company:

- Consulting Services - provide design, consulting, integration and operation of the company's hardware to customers.
- Customer Services - offer Hardware and Software Services to meet all customers support requirements.
- Implementation Services - deliver and install products to the customers.

Data analysis

Our analysis focused on generating lists of possible obstacles to implementing supply relationships within service supply chains. We did this by searching our material for themes, clustering them and developing theoretical constructs around them. Thus, we use an inductive method, which is common in explorative case research (Yin, 1989).

The first step of the analysis was to read the interviews and write notes in the margin, with the main purpose to identify problems in implementing supply relationships. This was made by two researchers to improve the reliability of the analysis. Where differences in interpretation existed between the two researchers, a procedure of joint discussion and coding took place until agreement was achieved.

The second step was to create nodes in N-vivo, a computer-based text analysis program, with our notes as guidance. The text was now classified in terms of the respondents' organizational belonging. Each section of the text was also classified according to the research framework. Third, problem codes were inserted. Text searches were also made, looking for key words and controlling that everything was coded satisfactorily.

The purpose of our research was to explore problems encountered when implementing service supply relationships. We were thus interested in service specific problems; i.e. problems that are particularly apparent when implementing supply relationships where there is a high degree of service content in the exchange. Hence, an important analytical challenge was to separate between those problems that were service specific and those that were not. This is not a trivial task; business exchanges normally involve a bundle of goods and services, with a varying division among services and goods (Slack et al., 1995).

To distinguish service-specific problems we first excluded generic problems. These are problems that could be found in any relationship context and not only a service context. To make this distinction we used existing literature alliances and change management literature. Examples of problems that were excluded are trust, communication and internal resistance to change. In making this distinction, we also used the commonly recognized characteristics of services as a starting point, such as intangibility, heterogeneity, inseparability, and perishability. Satisfying the characteristics of services was a necessary but not sufficient condition for being classified as a service specific problem. The context of the problem had to be analyzed in order to see if the issue really had to do with services.

Secondly, we excluded problems first and foremost related to the studied organization. Examples here are incentive systems and company culture. Although these types of problems are important, they are not necessarily generalisable outside the studied company. However, it needs to be pointed out that making the distinctions between generic vs. service-specific and general vs. company-specific was not a trivial task. Therefore, as displayed in Figure 2, although our focus was on more general problems in implementing service supply relationships, it was hard to confine ourselves completely.

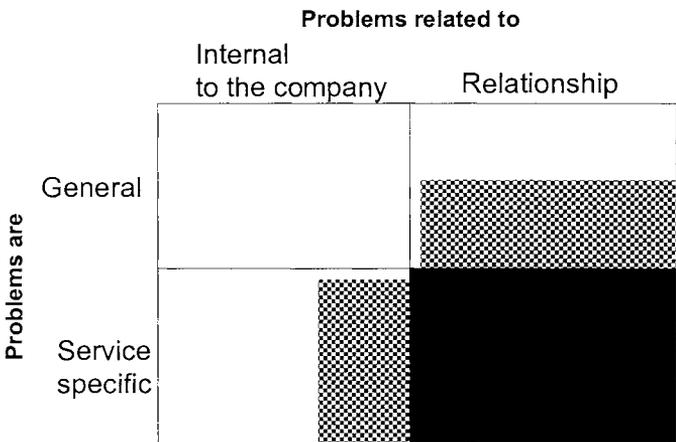


Figure 2. Focus of the study

We then grouped our list of service specific problems into four main areas of associated problems. The basis for grouping was that of commonality. Problems that referred to similar sources were grouped together. As a quantitative measure we counted how many times each problem was mentioned during the interviews. We could then compare the frequencies and get an idea of the relative importance of each problem area. Counting enables researchers to remove nagging doubts about the accuracy of their impressions about the data (Silverman, 1993).

Data

This section contains a presentation of the cases included in our research. In total, there are eleven cases. Table I contains a brief description of each case and its characteristics. We have also included the number of interviews where the respondents referred to the case.

Table I. Description of cases included in our research

Name	Description	Type of supply chain	Type of service	Number of interviews
Field Maintenance	Collaboration to maintain customers' systems on-site	Intermediaries	High judgment High customer contact	1
Systems integration	Integration of different systems from different vendors into one solution, and operation of that solution	Simple supply chain	High judgment Low customer contact	1
Service Logistics	Outsourcing and centralisation of logistics management: warehousing, order handling and inventory management, from several points worldwide to a central point.	Simple supply chain	Low judgment Low customer contact	3
Software Support	Attempts to establish a Joint Venture with the purpose to deliver software support on next generation product applications	Supply partnership	Low judgment High customer contact	1
Recycling	Collaboration for recycling old hardware products	Simple supply chain	Low judgment Low customer contact	1
Spare Parts Management	Management of a tailor-made spare parts management service, with spare parts positioned close to the customer	Intermediaries	Low judgment High customer contact	1
Centralisation of Repair	Outsourcing and centralisation of the repair operations from one large repair centre in a number of smaller repair centres worldwide to a central point in Europe.	Simple supply chain	Low judgment Low customer contact	3
Product Support	Collaboration with companies providing complementary products and services on these products	Simple supply chain	Low judgment Low customer contact	3
Repair	Collaboration with hardware repair providers.	Simple supply chain	Low judgment Low customer contact	1
Civil Works	Global strategic alliance with a large construction company, to establish premises for location of products that the company delivers worldwide.	Supply partnership	High judgment High customer contact	1
Installation	Collaboration for installation and test of the company's systems worldwide.	Intermediaries	Low judgment High customer contact	1

Problem areas in implementing supply relationships

When presenting our results, it is important to keep in mind that our focus is on problems related to the implementation of service supply relationships. We exclude problems that refer to supply relationships in general and problems internal to the company.

In the following, we have grouped our findings into four problem areas. The problem areas were arrived at through our analysis and are illustrated using excerpts from our interviews. The main purpose of the excerpts is to introduce to the reader how we reached our conclusions, to facilitate the reader's learning process (Normann, 1980). We have also made reference to literature, to help explain and develop our findings.

Figure 3 summarizes the four problem areas. The figure reflects the frequency groups of issues were mentioned during the interviews.

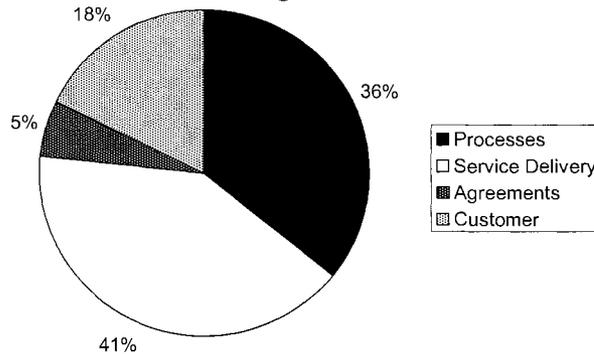


Figure 3. Frequency problem areas were mentioned in interviews.

Writing agreements for service exchanges

A particular area where problems arose was contractual agreements. According to the respondents, contractual agreements were difficult for several reasons, since they concerned services. The lawyers used by the company did not understand what it meant to write alliance agreements for services, but tried to use the same templates and models as they used for non-service alliances. For example, the services concerned could not be centralized and this made the contractual arrangements more complex. One respondent said:

"We have lots of experience of outsourcing manufacturing, from negotiating level through to lawyers. Since services are produced as they are delivered, they are always local, which puts different demands on the contract. We have had problems in drafting contracts, since our starting point was our old manufacturing-based contracts."

Pricing was also difficult due to the intangible nature of services. Finally, the problems concerned the importance of people and their competence for service businesses, a competence that is difficult to specify in a contract.

The characteristics of services make agreements and pricing more complex than for goods. Expectations of services are often difficult to specify, standardize and predict. The contract must therefore be flexible enough to cover unexpected events (Allen and Chandrashekar, 2000). This proved to be a challenge to the company.

Having clearly defined processes

A recurring theme, expressed by several respondents, was the importance of having clearly defined processes before going into service supply relationships. In the broadest sense “process” refers to how things are done rather than what is done (Schein, 1987). Here the term is taken to illustrate the transformation of inputs into services (Christensen and Donoval, 1999).

One of the important characteristics of services is the overlap between process and the product, that is the service (Slack et al., 1995). The process is part of the customer’s experience, which is together with the outcome make up the product (Johnston and Clark, 2001). Processes are therefore important in service supply chains. Division of work in a service alliance is often done in terms of processes, while in a product alliance it is done in terms of functions (Slack et al., 1995).

One source of problems for the studied company was the tendency to require the supplier to use the company’s way of doing things, their processes. This practice caused problems, particularly when the processes were not properly developed. If roles and responsibilities were not clearly defined at the company end, then leaving the tasks to suppliers was quite difficult.

”We have failed in supporting the supplier at the hand over and during the implementation, and the roles and responsibilities have not been clear”

The general opinion was that the processes that the supplier shall operate by should not be describe too much in detail, but rather described on a higher level, in order to maximize the exchange from the supplier.

”I have a concrete opinion regarding how we use our partners: we say we are going to outsource one of our processes. Then we say that the processes shall be done in our way. We want to have a lot of control over the processes. There are many interdependencies among sub-processes. We don’t handle the interfaces very well. We can’t give them the total responsibility with a logical scope and few dependencies. The intensive dependencies make heavy demands on the interaction and how they shall do things for us. We should make a careful map of our processes, find the logical scope for an outsourcing with few dependencies so that they can do their tasks their own way and make their own processes which they do better than we do.”

This is in line with Andersson et al. (2002) who mean that the definition of the service is critical but difficult, especially for companies that are not used to buying

services. Their advice is to describe the service as a function, activity, performance, or a competence, but without over specifying the service.

The idea expressed in the quotation above was that there was a need for clearly defined processes to successfully outsource services. However, modeling a service process is no guarantee that a service will be successful (Congram and Epelman, 1995). Processes are particularly difficult to transfer to outside companies, since they are often entwined in the social fabric of a company (Doz and Hamel, 1998).

It needs also to be pointed out that not all respondents classified processes as problems:

“I see the problems with processes as details in this context. It might be a problem during the implementation, but processes are not the reason why alliances don't work.”

This respondent had been project manager for an attempt at establishing a large alliance, which did not reach an agreement. The tendency during our interviews was that more senior managers did not see processes as a problem, whereas managers involved in the operational details of implementation saw processes as a problem.

Service Delivery

The actual point of delivering the service was considered complicated to hand over to a supplier. Take for instance repair services, where many different product versions needed to be handled at the same time. This made it difficult to specify a business in detail for a supplier. A large part of the knowledge required for delivering the service was embedded in peoples' minds and the experience was hard to document. Delivering some services was almost like handicraft, something that had been learnt through years of practice.

“Those who have worked here a long time have a lot of knowledge of old products, which exists only in their heads. These individuals are crucial to our success and are very difficult to replace with suppliers.”

This kind of tacit knowledge is of course also present in other businesses, but is perhaps even more evident in many service businesses. The knowledge and attitudes of the service firm's employees have a greater impact on the quality, values and cost compared with the manufacturing company (Heskett et al., 1990). Managing an outsourced delivery requires a new kind of competence, which our respondents did not think currently existed in the company.

The complexity of outsourcing the actual point of service delivery was compounded by the fact that many services must be delivered physically close to the customer. Quite often, the customers were themselves suppliers, providing input to the service to act on, e.g. a broken piece of equipment. This “customer-supplier duality” (Sampson, 2000) makes services more heterogeneous and difficult to predict. The complexity increases in a multinational or global business,

which our case represents. This difficulty reduced the willingness to let an external supplier handle the service delivery.

Controlling the relationship with the customer

A recurring theme during our interviews was the importance of keeping the control over the relationship with the customer. Although not being the most frequently mentioned problem, it was considered the most important and complicated. The contention was that going into a supply relationship must not imply that the control over the relationship with the customer is lost. Neither could a supply relationship mean that another company enters between the customer and the company. In talking of the importance of keeping control over the relationship with the customer, respondents referred both to the negotiation with the customer and the service encounter, the actual service delivery. Having control over the service encounter, they said, gives an understanding of the customers' needs, which can lead to new business and increased sales.

"We must not lose the control of the customer and we want to sit at the negotiation table with the customer, we don't want to become a sub-supplier of someone else. If we lose the control of the customer we will not hear that the customer wants to reinvest before we receive the invitation to tender."

Several authors have described the advantages of close collaboration with customers, e.g. from a product innovation perspective (Prahalad and Ramaswamy, 2000, von Hippel, 1988, Gupta and Wilemon, 1990). According to them, collaboration with customers can lead to new product ideas and business opportunities. The frequent customer interactions in many service businesses imply especially many opportunities for product ideas.

Having control over the service encounter was also considered important for quality control purposes. Keeping internal employees in the service encounter facilitates quality control, was the argument used. In a service business frontline employees are critical both for the seller and the buyer. The service encounters must be carefully governed since they can have a high impact on the customer satisfaction (Lewis and Entwistle, 1990, Chandon et al., 1996). However, it is still difficult to supervise a large number of frontline employees often located in hundreds of service facilities close to the customers (Heskett et al., 1990).

A third reason for retaining control over the relationship with the customer was of a more competitive nature. Externalizing a service business mean that core competencies and core businesses must to be protected from competitors (Quinn and Hilmer, 1994). The service encounter can be such a critical area. If the value for the customer is supplied during the service encounter, this must be carefully controlled was the argument used:

“We cannot let go of too much. There is limit somewhere, after which the customer will start turning to our supplier instead, which is not acceptable. We must own the customer.”

A fourth reason for keeping the interface with the customer in-house was that internal employees were believed to have a better network within the company, something that was considered important for being able to solve the customer’s problems. A final reason for keeping control over the relationship with the customer was the perceived importance of displaying the company’s employees to the customer, for branding purposes.

However, many respondents were at times somewhat vague regarding the nature of what activities that could be handled by an external company. Less intellectual activities were generally considered possible to outsource.

“It also depends. For simple services, like exchanging hardware, one could imagine putting a supplier next to the customer.”

”In some places the help desks can be low competence, and then you could outsource it. In terms of actually outsourcing a high level of competence from help desks I can’t see that we will outsource it”

Effects of type of and stage in the relationship

In the following, we develop our analysis of the four different problem areas in accordance with research questions two and three. The aim is to further our understanding of the problems of implementing service supply relationships.

Problem areas and type of supply relationship

The second research question concerned the effects of the type of relationship on problems encountered during implementation. To this end, we classified our cases into either simple supply chain, management through intermediaries or supply partnerships.

We found that agreements was a relatively larger issue for the partnership cases than for the other types of relationships we studied, possibly because of the large and complicated relationships these partnerships were, financially and strategically. In the software support partnership, the partners were also potential competitors, complicating the situation even more. Losing the relationship to the customer to the partner was seen as a serious risk when the partner was a competitor, making the agreement being seen as a critical control function. The complexity and dynamic nature of these relationships made it difficult to describe and agree on all the details in the agreement, which was perceived as a problem.

For the other supply relationships the division of roles and responsibilities was clearer than it was in the partnerships, and there were no seriously perceived competition between the parties in the relationship. The scope of the relationship

was clearer, more predictable, and easier to describe in a contract. Thus, the focus was on collaboration issues on a lower level such as processes. Processes were probably as large an issue in the partnership cases in absolute terms, but relatively it was not as large in the partnership cases.

Problem areas and stage in the relationship

Figure 4 contains a graphical representation of the relationship between problem areas and stage in the relationship. The figure shows the frequency with which the problem areas were judged to occur in each stage.

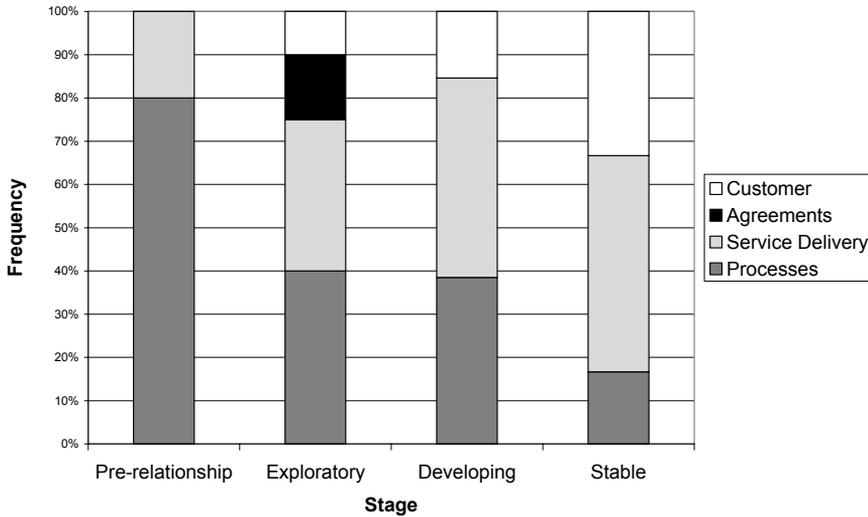


Figure 4. Relationship between problem areas and stage in the relationship

During *the pre-relationship stage*, the importance of having clearly defined processes seems to be critical. The reason for this could be that this is the stage during which the scope of the relationship is set. When considering going into an alliance, issues that become important are for example strategies, division of responsibilities, processes, and interfaces between different organizations and organizational units. During this stage, before going into the exploratory phase and starting the negotiations, it is important to understand the business and the operation. Understanding processes is a way of achieving this aim.

During *the exploratory stage*, the negotiations start and the agreements and pricing come into focus. Processes and service delivery are still important issues, since they will to some extent be part of the agreement. Without sound understanding of the processes and the actual service delivery, it will be difficult to negotiate a good agreement.

During *the developing stage*, the focus shifts to service delivery and controlling the relationship with the customer, although having clearly defined processes remains an important issue. Finally, in the *stable stage*, service delivery was the most frequently mentioned problem area followed by controlling the relationship with the customer. This seems reasonable since during this stable stage processes and agreements are probably established and requiring little attention, whereas issues related to the service delivery and the relation to the customer have become more obvious and perhaps even critical.

Conclusions

Our study indicates that implementing service supply relationships is far from easy. In particular, we identified four problem areas. Considering the exploratory nature of our study, there is a need to validate the findings in future research. In particular, two aspects of our research design needs to be taken into consideration since they may have had an impact on our results - the nature of the industry and the company's characteristics.

The industry the company belongs to may have affected our results. The products provided could be characterized as complex product systems (Gann and Salter, 2000), where customers buy a complex mix of hardware and software. The industry is also characterized by rapid technological progress, but where old technology still coexists together with new technology. There is a need to investigate implementation issues in the service supply chain in other types of industries, to control for the effect of the industry's characteristics.

The fact we have carried out our research within only one company may also have affected our results. Although we have several cases, they are all from the same company. First, there is the issue of generalization. Here it is important to bear in mind that generalization from case studies takes place towards theory, not towards samples and universes (Yin, 1989). Nevertheless, there is the issue of the effect of the company's characteristics on our results. The company has traditionally manufactured most of its products and recently started to focus more on core competencies, leading to outsourcing of both products and services. Some of the problems encountered in implementing service supply relationships may be due to the company's experience and competence in managing suppliers, rather than being general to service supply relationships.

With these remarks in mind, we develop our conclusions in the following. Our conclusions are summarized in Figure 5. The figure is intended to summarize all of our results, attempting to in picture summarize all three research questions.

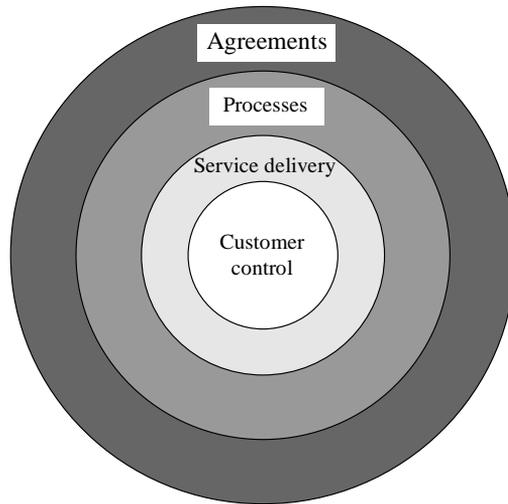


Figure 5. Problem areas in implementing service supply relationships

The figure contains our four problem areas, arranged in order of increasing difficulty and their strategic importance. Starting from the outside in Figure 5, the first layer, or problem area, is that of agreements. Writing legal agreements for service exchanges is relatively difficult, compared with exchanges involving only physical products. It is especially difficult in complex and dynamic relationships such as partnerships. However, agreements are a concern mostly in the early stages of a relationship. Once these agreements have been written, they don't affect the implementation negatively.

Having written the agreements, the second layer or problem area concerns processes, how things are done. When outsourcing services, there is a need to clearly specify processes to enable leaving them to suppliers. Like agreements, processes are of the nature that once specified, they become less problematic. Therefore, they are most likely to be a problem in the early stages of a relationship. They are particularly critical in the very early stages of a supply relationship.

The third problem area in implementing service supply relationships concerns the difficulty of handing over the actual point of delivering the service to a supplier. The nature of many services, being intangible and people-based, makes managing outsourced service delivery a difficult set of skills to develop.

Fourth, and finally, the risk of losing control over the relationship with the customer is at the core of the model. The issue of whether or not there is a need to control the relationship with the customer is a much more strategic issue than agreements and processes. It is also a complicated and multifaceted issue. Using suppliers that enter between a company and its customers may result in a loss of control over the relationship with the customer. Although this may not be a

problem and may also be something that can be managed, there is a need to consider the impact of not having direct contact with customers.

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PAPER II:

**IDENTIFYING INTRAORGANISATIONAL AND
INTERORGANISATIONAL ALLIANCE CONFLICTS
- A LONGITUDINAL STUDY OF AN ALLIANCE PILOT
PROJECT IN THE HIGH TECHNOLOGY INDUSTRY**

IDENTIFYING INTRAORGANISATIONAL AND INTERORGANISATIONAL ALLIANCE CONFLICTS - A LONGITUDINAL STUDY OF AN ALLIANCE PILOT PROJECT IN THE HIGH TECHNOLOGY INDUSTRY

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Abstract

The extant literature on alliances tends to neglect the effects of intraorganisational relationships within each alliance partner on the implementation of the alliance. To address this gap, this paper investigates both interorganisational and intraorganisational conflicts occurring during the implementation of a service alliance and aims at developing categories of conflicts as well as analysing how these conflict categories affect the implementation of the alliance. Thus, the overall purpose is to contribute to our understanding of implementation issues in alliances for the delivery of services. In order to do so, one *case* of a high-technology alliance has been studied longitudinally, with the researcher acting as a participant observer. Three interrelated categories of conflicts are developed through an analysis of the data: 1) the scope of the alliance, 2) the customer relationship, and 3) the implementation process. One important conclusion of this study is that the perspectives of several of the stakeholders, including the customers indirectly involved in the alliance should be included when implementing service alliances.

Introduction

Companies are increasingly focusing on activities for which they are supposed to have a core competence (Prahalad & Hamel, 1990). As a result, many firms are finding that they need to obtain complementary competencies from other firms for the activities that were previously conducted in-house. However, there is evidence that the efforts of firms to implement such alliances have failed to meet expectations (Barringer & Harrison, 2000, McIvor, 2000, Stuart & McCutcheon, 2000) and that the problem of implementing alliances is not that well researched although it is improving (Boddy, Macbeth, & Wagner, 2000, Elmuti & Kathawala, 2001, Spekman, Forbes, Isabella, & Macavoy, 1998, Stuart & McCutcheon, 1996).

The perspective taken in most of the extant literature on implementing alliances is from the level of analysis of the firm and it deals primarily with the relationship between the two partner firms. As a result, the firms themselves are generally viewed as black boxes (Kothandaraman & Wilson, 2000, Spina & Zotteri, 2000). However, business relationships in industrial markets are often complex, involving

people from different hierarchical levels and different functions in the organisations on both sides of the alliance relationship (Ford, 2002, Webster, 1991). In particular, relational exchanges such as partnerships normally imply broad interactions between the involved firms (Kothandaraman et al., 2000). For example, during the implementation of an alliance, firms experience changes in their operations and as a result, the differences in needs, interests, values, and preferences across individuals and groups within the organisations often lead to conflicts (Buchanan & Badham, 1999) both within and between the involved firms. Consequently, in order to better understand the problems involved in implementing alliances, it is necessary to investigate more deeply the relationships inside alliances by studying the relationships between the different functions in the involved partner firms.

This paper focuses on an industrial firm's attempt to improve its marketing effectiveness through the implementation of an alliance with an education company. In contrast to much of the previous research on implementing alliances, this paper includes an analysis of the relationships between several functions in both the studied partner firms. In other words, this paper not only looks at interorganisational relationships, but it also looks at the intraorganisational relationships related to the implementation of the alliance. Thus, the overall purpose of this paper is to contribute to our understanding of implementation issues in service alliances. To fulfil this purpose, this paper focuses on the narrower concept of conflicts occurring during the implementation of alliances for the delivery of services. Researchers have suggested that conflicts in alliances are one of the most prevalent reasons for alliance failure (Kelly, Schaan, & Joncas, 2002, Lorange & Roos, 1991, Mentzer, Min, & Zacharia, 2000, Mohr & Spekman, 1994, Moore, 1998) and that managing the soft issues such as conflicts is a key managerial issue (Kanter, 1994, Maloni & Benton, 1997, Wildeman, 1998). In this paper, identifying and analysing conflicts is seen as a method for understanding important elements of the alliance implementation process. In other words, conflicts in the alliance are seen as manifest illustrations of important problems in the alliance. The specific purpose of the paper is to identify and analyse conflicts between different actors involved in the implementation of a service alliance and to suggest categories of conflicts in service alliances. Since the aim is not to contribute to theories on conflict but to the understanding on alliance implementation issues, implications for how to implement service alliances in marketing channels are also discussed as well as some implications for the development of new industrial marketing strategies.

This article presents a case in which the conflicts within the firm implementing the alliance were stronger than those between the partners. This result indicates that managerial attention should be focused more on internal relationships than what the majority of the alliance literature suggests. The article also presents details on the implementation process and the conflicts that occurred. The results of this

paper are based on a longitudinal study of an alliance pilot project between SysCo, an industrial company, and TeachIT, an education company¹. The paper is organised as follows. First a theoretical background is presented, including a review of literature on alliance implementation problems and conflicts in alliances. Second, the methodology and analysis of the case are presented. Third, the results and conclusions are presented.

Theoretical background

Alliance implementation problems

To date, a significant portion of the research on alliances has focused on the benefits of alliances. Recently however, a number of articles focusing on the challenges and problems during the implementation of alliances have been published. According to many of these studies, the problems encountered during alliance implementation are very often about the soft issues related to collaboration among people involved in the alliance. Examples of such soft issues are insufficient communication (Kelly, Schaan, & Joncas, 2002; Sahakian, 1998), conflicts (Lorange et al., 1991, Mentzer et al., 2000, Mohr et al., 1994, Moore, 1998), a lack of trust (Elmuti et al., 2001, Gulati, 1995, Parkhe, 1998), culture (Elmuti et al., 2001, Kelly, Schaan, & Joncas, 2000, Lorange et al., 1991, Vyas, Shelburn, & Rogers, 1995), and organisational politics (Lorange & Roos, 1992). Another group of problems is operational, for example insufficient specifications or quality problems (Elmuti et al., 2001, Kelly et al., 2002). A third group involves strategic problems, for example the risk of losing core competencies to the partner (Elmuti et al., 2001, Lorange et al., 1992). Last, the performance or the results of the alliances are sometimes referred to as problematic (Elmuti et al., 2001, Kelly et al., 2002). According to a paper by Kelly and colleagues (2002), based on research on the early stages of alliances among manufacturing, service and R&D-based companies, the majority of the problems are soft, followed by a relatively large number of operational problems. In their study, strategic and performance problems composed only a small part of the problems. In this study, they found that people/relationship problems accounted for 55% of the total while operations accounted for 29%, with strategic and results accounting for only 11%, and results 5%, respectively. This result supports previous work by both Kanter and Wildeman, who argue that managers often lack the ability or interest to handle soft issues (Kanter, 1994, Wildeman, 1998).

Additionally, due to specific characteristics of services, implementing alliances for the delivery of services poses different risks and challenges to the involved

¹ Pseudonyms have been used in this paper to protect the anonymity of the companies and the involved participants.

companies (Fitzsimmons & Fitzsimmons, 2000). For example, strategic issues in service alliances that potentially lead to tensions involve the management of the customer interface and the brand of each partner firm (Ernst, 1996). In other words, it can be expected that implementing alliances for the delivery of services will involve certain specific conflicts that need to be managed.

Conflicts in alliances

The literature on alliance conflicts is practically endless and there are many different definitions. For example, Rhenman and colleagues (1970) define conflict as “a breakdown in or a threat to co-operation”. Conflict has also been defined as “perceived incompatibilities or perceptions by the parties involved” (Boulding, 1963), or “the amount of disharmony and strife between organisations in a system” (Alter, 1990). Conflicts have previously mainly been viewed as something detrimental to organisations and something that should be avoided or resolved. Avoiding or minimising conflict in alliances is often mentioned as a success factor (e.g., Gomes-Casseres, 1998; Mentzer et al., 2000).

Today most scholars argue that conflict has both good and bad sides and that some conflicts should be eliminated while others should not be (Rahim, 2000). While recent research by Duarte and Davies (2003) supports a negative relationship between conflict and performance, Jehn (1995) concluded that a medium level of task conflict can be positively related to the performance of groups conducting non-routine tasks. Furthermore, others argue that conflicts can stimulate creativity and development (Brown, 1983, Pascale, 1990, Pondy, 1967). For example, Doz and Hamel (1998) posit that conflict can enhance learning in alliances, and Assael (1969) argues that conflicts can lead to better communication, a more critical view on previous events, and a creation of a power balance.

The nature of an alliance is likely to influence the level of conflict, both positively and negatively. For example, the informal governance of many alliances (Barringer et al., 2000) and the dynamic and unstable nature of many alliances (Dussauge & Garette, 1999, Ring & Van de Ven, 1994) are among the factors that can potentially increase the degree of conflict in alliances. On the other hand, trust in alliances is argued to be a mediating factor for the level of opportunism and conflict (Gulati, 1995). While some authors claim that arm’s length relationships are more conflictual than closer relationships, such as partnerships or alliances, Gadde and Håkansson (2001) take a contrary view. They propose that a high level of conflict is only a problem in contexts with a low degree of collaboration and that the optimal situation is where a high level of conflict is combined with a high level of collaboration (1993).

Industrial business relationships are often complex with broad interactions between the involved parties (Webster, 1991) and consequently involve more

opportunities for conflict. In relationships with more standardised content there is not so much to argue about, and there will be fewer conflicts (Ford et al., 1998).

Several quantitative studies on alliance and channel conflicts have been conducted (Alter, 1990, Kemp, 1999, Laine, 2002), providing propositions and statistical correlation factors between variables such as conflict, trust, and performance. Most of the research focuses on the development and delivery of physical goods as opposed to services. In-depth qualitative data on alliance conflicts for the delivery of services is sparser but is sometimes used as background information in quantitative studies. An example of this is a study by Alter (1990) in which the primary conflict data are quantitative, and interviews are used to gather a better understanding of the context. However, similar to other studies on conflicts, this study provides little detail on the content of the conflicts. Nor does it address the organisational complexity of the organisations. In general, organisations are viewed as black boxes in the research literature on alliances (Kothandaraman et al., 2000, Spina et al., 2000), neglecting the impact of intraorganisational conflicts on the alliance.

Because of the lack of detail provided in extant literature on the conflicts that arise *within* organisations implementing alliances, a longitudinal case study on the conflicts in service alliances was carried out.

Methodology

Case description

This study was conducted within SysCo, a hardware-oriented industrial firm with over 10,000 employees with its head office located in Europe. SysCo sells relatively complex goods typically worth between \$100,000 and \$5,000,000 to industrial customers all over the world through its own sales force. Increasingly, systems solutions rather than stand-alone products are sold, composed of relatively complex bundles of several different types of products. Most goods can be classified as specialties although the share of commodities is increasing. Services correspond to a significant portion of the firm's revenues, and it is increasing due to the maturing market for its goods. Information technology is increasingly becoming integrated into the systems of the company's products and is developed both internally and externally.

The specific focus of this research is an alliance pilot project in which the training of the company's customers on general IT issues was handed over to an external partner ("TeachIT") during a pilot period. TeachIT is one of the largest multinational education companies in the world, with over 1000 employees. During the pilot project, the alliance included customers in one country only, but the intention was to create a global alliance. The motivation for the alliance was

that the general manager of SysCo's service business unit wanted to learn about partnering. Training was considered a potential arena for this learning.

This alliance could primarily be classified as a marketing alliance (Lynch, 1993) since the main purpose was to reach new markets, increase sales, and potentially also develop new services. The alliance pilot was run as a project by a recently formed Alliance Function. During the pilot, SysCo received royalties from TeachIT based on the sales of training. Thus, the alliance had a licensing agreement. After the pilot period, the alliance was to be evaluated and a decision made as to whether the co-operation should continue or not. The studied alliance could be considered relatively dynamic, and the agreement and the scope of the relationship were initially openly defined and formalised in a temporary agreement during the pilot alliance. The primary rationale for selecting this specific alliance for the study is that it explicitly aimed at developing a close alliance in an area that had previously been handled internally. It was considered a learning experiment by the involved authors and an interesting arena for studying both interorganisational and intraorganisational conflicts in alliances.

Research design

The research reported in this paper can be characterised as a single case study of an exploratory nature. This method allows gathering considerably detailed data (Yin, 1989) enabling a deep understanding of the sequences of events but sacrificing the ability to achieve statistical generalisability. Case studies are especially appropriate for exploring new areas (Leonard-Barton, 1990, McCutcheon & Meredith, 1993) and when the researcher is interested in questions concerning "how" and "why" (Yin, 1989). During more than 8 months between 2001 and 2002, the author of this paper was a participant observer, acting as an ethnographer involved in collecting and analysing data as well as an informal adviser to the project.

In line with suggestions by other scholars (Brown, 1983, Vaaland & Håkansson, 2003), the alliance companies were not treated as black boxes. Instead, the individual perspectives from several of the stakeholders within one of the alliance companies were collected. Accordingly, besides the alliance managers and project managers, employees from the Training Function at Head Office of SysCo, the Market Units and Local Training Centres of SysCo and from the Training Partner were included. The reason for this was that the implementation of the alliance involved stakeholders from several different units in both companies, who all contributed both positively and negatively to the implementation and success of the alliance. The organisational units that were studied are presented in table 1.

Table I. Key units involved in the alliance pilot

Unit	Description
Head Office of SysCo, Training Function	Responsible for customer training strategies and training product management. Divided into sub-units for product management, service delivery, and business development.
Head Office of SysCo, Alliance Function	Responsible for selection and contracting of partners for delivery of training.
Local Training Centres in the Market Unit of SysCo	Responsible for sales and delivery of services to traditional customers in a specific market. The Local Training Centres were formally governed by the central Head Office, but legally belonged to the Market Unit.
Training Partner	Responsible for sales and delivery of general IT training to traditional and new customers.
New customers of training (non-traditional)	Purchasing of IT training from TeachIT. These customers were not previously customers for SysCo.
Traditional customers	Responsible for purchasing of hardware, systems and services such as training from SysCo and IT training from TeachIT.

Data collection

Data were collected through three means: interviews, a questionnaire, and workshops. A series of twenty-four interviews were conducted with employees from different functions primarily within SysCo. The interviews ranged from being formal, semi-structured interviews to unstructured, informal meetings that occurred spontaneously, e.g., next to the coffee machine, with eight being of a more formal nature. The eight more formal, semi-structured interviews lasted between one and two hours and were tape-recorded and transcribed by the author in detail. These included five employees from Sysco's Training Function, one of Sysco's Local Training Centre managers, the alliance project manager from TeachIT, and the alliance project manager from SysCo's Alliance Function. The sixteen informal meetings included employees from the different organisational units within SysCo, of which the majority were from the Alliance Function and the Training Function. They generally lasted between five and fifteen minutes and recorded detailed notes from these meetings directly afterwards. Additionally, reflections from observations were recorded almost every day.

In the interviews, the focus was on five broad themes that were selected based on their relevance for the study of alliance conflicts and implementation: organisational relationships, strategies, conflicts, frictional events, and implementation. The conflict phenomenon is inherently difficult to study, requiring caution when interacting with the interviewees so that the relationship is not jeopardised. Håkansson and Vaaland (2003) suggest an indirect approach focusing

on “frictional events” that can potentially lead to conflicts rather than conflicts as such. In this study, specific conflicts were only asked for directly when the researcher had a close relationship with the informant. Otherwise an indirect approach was used, focusing on frictional events.

During the more structured interviews, an illustration in the form of a sociogram of the alliance’s central stakeholders was presented for the interviewees in order to uncover information about the conflicts between the different stakeholders (see figure 1). In line with Freeman's (1984) definition of a stakeholder, the stakeholders were selected based on a judgement of which organisations could affect or be affected by the alliance project. Thus, this illustration worked as a basis for a discussion of conflicts and facilitated a more specific discussion focusing on specific intra- and interorganisational conflicts.

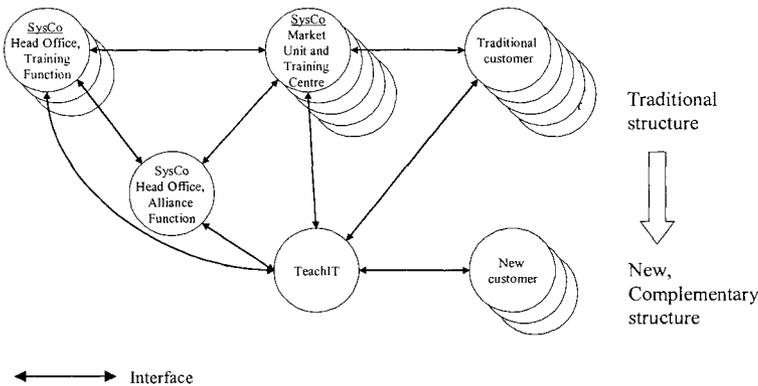


Figure 1. Traditional and complementary training structure at the organisational interfaces. The shaded circles correspond to the new, complementary structure resulting from the alliance.

The same illustration was also used in a questionnaire administered to eight employees from SysCo and two from TeachIT. This questionnaire was conducted in the middle of the pilot and provided quantitative information about the perceived levels of intra- and interorganisational conflicts. The questionnaire contained questions about task conflict (i.e., disagreement on alliance scope), process conflict (i.e., disagreement on how tasks are done) and relationship conflict (i.e., degree of emotional tension) that were inspired by Jehn (1995, 1997) and Jehn and Mannix (2001). In this paper, these have been aggregated to a more general level of conflict.

At the end of the alliance pilot project, a workshop was conducted with the three main project members from the Alliance Function within SysCo in which preliminary results were presented and comments were received. Additionally, a

second workshop was held with one of the main project members and one of Sysco's Training Centre managers. During this second workshop, the results of the study and managerial implications were presented and discussed.

Analysis

The analysis focused on generating lists of possible conflicts that had occurred during the implementation and clustering them into larger categories of associated sources for conflicts. This was done by searching for statements and observations of conflicts and frictional events that were related to more than one individual or organisation. The material was then grouped into sub-themes, pattern codes were generated, and theoretical constructs were developed around them.

As a first step, all interview transcripts and field observations were read and notes were written in the margin, primarily to identify conflicts in the alliance. Apart from the author of this paper, a senior researcher from the same research program also did this to improve the reliability of the analysis. Differences in interpretation were revealed in a few cases, and as a result a procedure of joint discussion and coding took place until agreement was achieved. The second step was to create nodes in N-vivo, a computer-based text analysis program, with the manual notes as guidance. Text searches were also made, looking for key words and checking that everything was coded satisfactorily.

The next step involved grouping the conflicts into three main areas of associated conflicts. The basis for grouping was that of commonality and conflicts that referred to similar topics were grouped together. After some iteration, this analysis finally resulted in three main groups of conflicts that were seen as sufficiently distinct from each other although they were also to some extent overlapping. The majority of the observed conflicts could be grouped into either of these conflict areas and each conflict area contained statements from several different respondents. The interview transcripts were also coded according to the location of each of the conflicts.

Intra- and interorganisational conflicts in the training alliance

In the following discussion, the location and degrees of conflict at the different organisational interfaces in the alliance that was studied are presented as well as the categories of conflicts that resulted from the analysis. Excerpts from the interviews will be used to illustrate the meaning of each category and to facilitate the reader's learning process (Normann, 1980). The three main categories of conflicts were (1) Alliance scope, (2) Customer relationship, and (3) Alliance implementation. Additionally, references to the appropriate literature are made to

help explain and develop the results. Finally, the consequences of the conflicts are reported.

Location and degree of conflict

All three identified categories of conflicts were both inter- and intraorganisational although the relationship between the Alliance Function and TeachIT was almost free from conflicts. The only conflict between the Alliance Function at SysCo and TeachIT occurred at the end of the pilot when TeachIT wanted to expand the scope of the relationship to involve all the courses previously provided by SysCo. TeachIT wanted to do this to improve the prospects of success for the alliance. However, SysCo was of another opinion why a minor conflict occurred.

Other observations that can be made are that the scope of the alliance primarily resulted in conflicts within SysCo, and not at the interface between SysCo and TeachIT, and that the interface between SysCo’s Training Function and Alliance Function (Interface b) consisted of all three categories of conflicts, indicating that this situation may be more difficult to solve. Looking at the degree of conflict, Figure 2 summarises the quantitative data about the perceived degree of conflict at each organisational interface from the questionnaire.

The figure shows that the level of conflict varies at the different interfaces. A conflict level of 1 corresponds to “no disagreement”, 3 to “disagree somewhat”, and 5 to “disagree very much”.

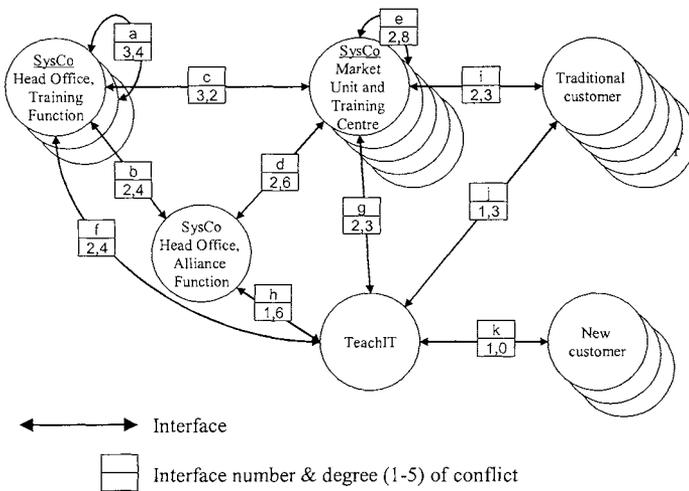


Figure 2. Location and degree of alliance conflict

The average degree of conflict in each individual interface is generally below 3. The total average, calculated for all the interfaces together, is around 2, corresponding to “disagree a little”. Thus, in general there was not a very high

level of conflict in this alliance. However, the study did reveal that that the highest average reported degrees of conflict were in the intraorganisational interfaces and not in the interorganizational interfaces. The lowest average degrees of conflict, close to 1, were reported at the interfaces between TeachIT and the customers and between TeachIT and the Alliance Function. The highest individually reported degree of conflict (5) was reported for the interface between the Local Training Centre and Alliance Function (Interface e). The qualitative data from the interviews also strongly supported the results. For example, one respondent from TeachIT said,

“If we go more deeply inside the organisations, especially on the SysCo side, there are frictions and probably communication problems.”

However, similar to the majority of existing literature on alliance conflicts, figure 2 does not reveal much about the contents of these conflicts. For this reason, the content of these conflicts is discussed in the following section. More specifically, three categories of conflicts derived from the data will be presented.

Categories of alliance conflicts

Alliance scope

One intention with the alliance pilot project was to evaluate the scope of the appropriate alliance, or areas suitable for alliances, e.g. in terms of services and products feasible for externalisation to partners, and to develop an alliance strategy. However, there was a lack of agreement within SysCo on the appropriate scope of the training alliance during the pilot. Some employees in SysCo considered the scope of the pilot alliance to be “madness”, or completely inappropriate. These employees considered IT training to be one of the future core areas of the company and an opportunity for high future revenues. One interviewee explained this in the following quotation:

“There were many protests initially, a hole in the head they called it. They saw IT education as core and did not want to outsource it, and they still do not want to do so.”

However, most of these employees were vague about the appropriate scope of training alliances and there was no agreement between the different individuals and departments on the appropriate scope. While they were primarily positive about the alliance, they did not want their specific training product to be handled by an external partner. One interviewee explained,

“All product managers are generally positive to the idea of partnerships but not for their specific product.”

In contrast, others believed that external partners could handle practically everything as this interviewee stated,

“I don’t know, but it is difficult to only go halfway in alliances. For me it is difficult to set the boundaries. If we are going to have partners or outsource training, the easiest

thing to do would be to sweep out everything to the partner, at least when it comes to the delivery of training.”

A central concern was about hardware products and systems feasible for training alliances. Involving an external partner in the development of courses for products and systems under development was considered a challenge due to the secretiveness of the development activities. Another concern was about the choice of products that were generating high or low revenues. Keeping the profitable areas in-house would decrease the prospects for the partner and thus for the alliance. One employee exhibited this feeling in the following quotation:

“The scope from training has been to get rid of non-profitable or dead products, but they have understood that this would not work. We could use TeachIT to generate business instead, but the product managers have not had that perspective.”

SysCo’s Market Units and Local Training Centres feared for their business and for their *raison d’être* when part of the training business was taken over by an external partner. This fear risked resulting in a deterioration of the relationship between the Local Training Centre and the Head Office since the local companies perceived that the Head Office was responsible for this strategic move which they perceived being a mistake. One interviewee made the following statement:

“There is a scepticism and a worry, especially within the Local Training Centres. They are afraid of losing their jobs.”

In summary, the alliance was perceived as a threat to the employees in SysCo. This could be expected since the character of SysCo probably also contributed to the resistance. SysCo could be characterised as a segmentalist organisation (Kanter, 1983), which means a large, functionally differentiated organisation with complex hierarchies, and departmental subcultures. Segmentalist organisations are often resistant to change due to institutionalised behaviour (Hannan & Freeman, 1984).

Customer relationship

The second alliance conflict area was related to the relationships with the customers and the strategy and position of SysCo. Basically the conflicts revolved around the impact of using external resources for IT training on the relationship with the customers. These conflicts occurred at both inter- and intraorganisational interfaces. Both the traditional customers and employees from SysCo were sceptic about the externalisation of IT training. IT was increasingly integrated with the products offered by SysCo to its customers and, as noted above, was perceived by some to be a cornerstone of both future product and service business. Thus, some employees in SysCo saw a need to develop IT competence internally rather than externalising it. Some traditional customers wondered if SysCo did not have the competence in-house, which could be a risk for diminished credibility of SysCo. Some employees from SysCo thought the alliance implied a risk for losing IT competence and as a result, they could lose business to the partner. One interviewee commented on this in the following manner:

The traditional customers had already shown scepticism about having an external partner providing IT training which they perceived to be a cornerstone for the future business of SysCo. They wondered if SysCo did not have the competence in-house, something that diminished the credibility of the company. There was a risk that the traditional customers would eventually decide to ally themselves with the new training partner, something that would probably not be applauded by the Market Units.”

Others saw the alliance as an opportunity to strengthen the brand of SysCo, since the reputation of SysCo in the IT training area was not good, as indicated in the following quotation:

“We have an undeserved bad reputation in the market that we can’t handle IT-training. TeachIT are world leaders there and could strengthen our position in this market.”

Another conflict was related to the royalties received by SysCo from the sales of training by TeachIT. For example, should they be given to the Market Units & Local Training Centres to increase their motivation for the alliance? The Market Units had the main responsibility for the traditional customers and was consequently an important player in the alliance, as one interviewee noted:

“SysCo’s Swedish sales organisation is doubtful about training alliances. They own the customer and want to sell themselves.”

The concerns of the employees within SysCo are related to the relational nature of services taking place directly between the service provider and the customer such as training (e.g., Grönroos, 2000). Since the transactions with the customer can be a foundation for a longer-term relationship with the customer (Normann, 2001), there is a risk that externalising the transactions such as the delivery of training deteriorates the relationship with the customer. These transactions can also potentially affect the brand and the customers’ image of the company. Consequently, the transactions such as the service encounters must be consciously managed to provide a positive brand image to the customer (Grönroos, 2000). In business relationships, all interfaces with the customer must be considered, not only the actual service delivery but also the invoicing and sales processes involving people from several functions in the involved organisations (Ford et al., 1998, Webster, 1991).

Alliance implementation process

The third conflict category involved how the implementation of the alliance was conducted and by whom. These conflicts occurred particularly within SysCo but also at the interfaces between SysCo and TeachIT and between SysCo and its customers. One aspect of these conflicts was that the leading role for the implementation of the alliance was taken by a special Alliance Function that was separate from the Training Function. The alliance was initiated not by the Training Function but by the general manager of the services business unit. The Alliance Function initially took a very broad responsibility, including a strategic responsibility for alliances (for example areas for alliances). As a result, employees

in the Training Function were both irritated and astonished, and in some cases they doubted the competence of the Alliance Function since it was recruited partly from outside the Training Function. Employees in the Training Function also felt neglected by the Alliance Function, as one employee noted:

“The pilot alliance with TeachIT implied that many employees felt run over. Rumours started to spread.”

Halfway through the pilot, employees in the Training Function were invited by the Alliance Function to write a requirement specification for appropriate areas for training alliances in the future. This specification was intended to guide the Alliance Function towards a more specific scope of the future alliance in line with the expectations from the Training Function. However, the Training Function never delivered this specification. The Alliance Function expected the Training Function to have clear expectations and requirements on the alliances, but the Training Function was struggling with discussions about core competencies. At the same time, many employees from the Training Function had firm but varied opinions on where alliances were inappropriate or had specific requirements on which processes and products were feasible for alliances. Thus, they hindered the Alliance Function in their explorative work with finding and establishing alliances.

Another central conflict was the inadequate involvement of other units within SysCo outside the Head Office. Many employees within the Market Units, which had the main responsibility for the traditional customers, were not aware of the alliance before it was already running. One Market Unit employee made the following statement:

“As a sales organisation we came in very late and heard that an alliance had already been initiated and was about to start within two months. Those who wrote the agreement were not collaborating sufficiently with other organisational units.”

One serious conflict occurred when TeachIT approached the customers to sell their courses. These customers were unaware that the alliance existed and of the purpose with it, and as a result, they were very confused by this. According to O’Farrell, the relational nature of services means that the customers should always be involved in the decision about service alliances (1999). The complexity of many business relationships and the involvement of a multitude of people from different functions and hierarchical levels (Ford et al., 1998, Webster, 1991) mean that implementing alliances affects many people and many organisational units. This must be considered carefully before and during the implementation of change such as alliances and a broad involvement of the organisation may be necessary for the implementation to be successful (Kothandaraman et al., 2000). Negotiating from an ivory tower or neglecting internal communication should be avoided (Sahakian, 1998).

Consequences of the conflicts

As mentioned above, conflicts can have both positive and negative effects on the success of an alliance. In this case, some of the conflicts hindered the alliance, but they did not lead to the dissolution of the alliance. Rather, the conflicts led to a passive resistance that hindered the development of the alliance and its implementation progress, thus deteriorating the working climate. One example of this resistance was the difficulty in using teachers from the Local Training Centres as resources together with teachers from TeachIT, in spite of their low occupancy rate for these teachers. One interviewee from TeachIT commented,

“We wanted to use SysCo’s teachers that were not fully occupied at the moment. It was very difficult to make them support us; they claimed they did not have the time. There was a passive resistance.”

Although not many directly hindering conflicts could be observed, the frustration and discontent with the alliance project sometimes made it difficult for a professional and productive debate between the Alliance Function and the Training Function. One of the employees at the Alliance Function made the following statement:

“I like my job and I have good arguments for what we are doing, but the working environment is disgusting.”

There were also indications that the conflict between the Local Training Centres stimulated an internal competition for the training business among the Local Training Centres, as indicated in the following quotation:

“There is a very high degree of competition between the Local Training Centres. This may increase or decrease when we introduce an alliance. They have one common enemy, Head Office. The three biggest Local Training Centres don’t like each other; they would rather compete than collaborate. It’s about survival as they see it.”

To some extent, the conflicts also stimulated discussions and the development of a sound alliance strategy. The conflicts made the pilot more turbulent, but also stimulated learning in all the involved organisations even though the learning process was rather ad hoc than conscious and structured.

Discussion and implications

One of the starting points for this research was the limitation of existing research in taking the complexity of many alliances into account and studying the relationships between different functions in the involved partner firms. The foregoing presentation revealed that intraorganisational conflicts were more severe than interorganisational conflicts in this studied alliance. This result suggests that the perspectives of several of the stakeholders within the partner companies should be included when implementing or studying service alliances. This finding supports the work by Kothandaraman and colleagues (2000) and Spina and colleagues (2000) who argue that intraorganisational conflicts may hinder the

implementation and development of an alliance and should thus be taken into account by management. This conclusion is also consistent with the suggestions by scholars of the IMP school, (e.g., Vaaland and Håkansson, 2003), scholars of the industrial marketing school (e.g., Webster, 1991), and some conflict scholars (e.g., Brown, 1983).

Another starting point was the limitation of existing research in providing details on conflicts occurring in alliances (Kothandaraman et al., 2000, Spina et al., 2000). In this paper, three interrelated categories of conflicts have been developed, the alliance scope, customer relationships, and alliance implementation. The results of this study suggest that the alliance scope should be determined such that the customer relationship is not put at risk. The alliance scope may affect the implementation process; therefore, the alliance scope and the implementation process should involve customers and other stakeholders. Customers may have opinions on the scope of the alliance and the implementation process, and employees within either of the organisations may perceive the alliance as a threat to their own position. All conflict areas should be taken into consideration together since this study indicates that neglecting any one of the areas is likely to lead to conflicts that will spread to the other areas, resulting in a vicious circle. The suggestion of the three categories of conflicts is a conclusion that builds on the more general knowledge of the importance of conflicts in alliances.

Furthermore, the overall purpose of this paper was to contribute to the understanding of implementation issues in service alliances. The paper fulfils this purpose by describing the effects of the conflicts on the implementation. The effects were primarily negative; that is the conflicts hindered the progress of the alliance implementation. This is in line with the research by Duarte and Davies (2003). To some extent, the conflicts also contributed to learning in the alliance, in line with the suggestions by several scholars, e.g., Doz and Hamel (1998), and to the development of a sound alliance strategy.

A final conclusion that can be drawn from the results of this study is that interorganisational conflicts should be considered especially in alliances where the alliance strategy is being formed during the implementation. In the studied case, the scope of the alliance pilot was defined in an agreement and consequently there was not that much room for further discussion about this between the two partner firms. However, this alliance pilot was run at the same time as an overall alliance strategy was being developed within SysCo, and there was still plenty of room for debate internally within SysCo. Conflicts emerged primarily at organisational interfaces for which there were no formal or informal agreements, typically at interfaces within SysCo.

Managerial implications

This study has several implications that are of interest to industrial marketing managers. To begin with, this study has implications for the development of industrial marketing strategies, and in particular for distribution strategies. The findings of this study have shown that it can be very difficult to determine the details of a changed strategy at the outset of an alliance, e.g., the choice of services and products to be marketed through alliances. Instead, the strategy should be formed during the implementation of the alliance. However, as the case of SysCo indicates, such an approach is also likely to be turbulent and involve considerable internal conflicts. Consequently, what appears to be important is to pay special attention to the process of implementation including aspects such as conflicts within the organisation, rather than trying to implement a strategy that is formulated by top-management in a linear fashion.

Moreover, there are some important implications for the process of implementing alliances in marketing channels. Managers attempting to implement alliances in their marketing channels should pay special attention not only to conflicts between the partner firms during the implementation, but also to conflicts within their own firm. Although it is probably impossible to avoid conflicts altogether, an interactive and reflective approach to alliance implementation, involving interaction between employees, customers, and suppliers, is likely to moderate the degree of conflicts and their negative effects. In particular, as the marketing strategy emerges during implementation, there is a need to involve the organisation in the change process and to explain why a simple top-down approach is not feasible. Managers should be open to the opinions of their employees and explain that they cannot deliver clearly formulated and definite marketing strategies because they do not have all the information and knowledge that they need.

More specifically, managers should anticipate conflicts associated with (1) the scope of the alliance, (2) the consequences of the relationship with the customer, and (3) the implementation process. If the three categories of conflicts are appropriately managed, it is likely that the positive effects of them (e.g., learning and improved decision making) can be enhanced in favour of the negative effects. In other words, the three categories of conflicts could be used as a framework for the management of the implementation. The alliance scope is perhaps the most important category of conflicts since it affects both the customer relationship and the implementation process and can lead to conflicts in both these areas. The tentative conclusion that can be drawn from this study is that the scope should be set with at least three things in mind. First, the effect of the scope on the competitiveness and brand image of the involved partner firms should be considered so that the chosen scope can be communicated and motivated. Second, the customer should preferably be involved in the decision. Third, the different internal functions should be involved in the decision since they may have

important knowledge that is of relevance for the alliance. If these things are neglected, conflicts that hinder the implementation of the alliance may emerge.

Limitations and directions for future research

Since this paper is based on only one case, it is important to consider contextual factors that may have affected the results and decreased the generalisability of it. The emphasis on internal conflicts in this study originates from several internal and contextual circumstances for the studied case. The results are developed based on an analysis of one single case, and as such it is difficult to generalise to other cases without having a clear understanding of the case and its context. However, it can be expected that the results are relevant for similar alliance implementation projects where strategy is formed over time. It is important to note that the emphasis on internal conflicts may also reflect that there was a severe downturn in the economy during the project causing massive layoffs within SysCo. Consequently, there was a relatively high level of fear among the individuals in the company, a fear that only increased due to the alliance project. This fear caused a resistance to the alliance since it was seen as a reason for further layoffs. However, there were also indications that this fear accelerated the development of competence internally within SysCo, and thus the fear had both positive and negative effects. Another contextual factor was that SysCo had clear ambitions to grow in the service business. This ambition probably counteracted the ambitions to implement the alliance. Although training was a very small share of the revenues for SysCo, it was perceived as an essential element in the service strategy.

Future research should investigate how the results of this study fit in other alliances to test the generalisation of his study. Alliances between firms with different organisational and national cultures could be studied with the purpose to see how this difference affects the conflicts. Second, contextual factors such as the economic situation in the business and of the involved alliance companies are likely to affect the patterns of conflicts. Thus, a systematic study of the effects of contextual factors on conflicts in alliances is another potential arena for the future research.

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PAPER III:

**MANAGING THE PROCESS OF ADOPTING SERVICE
LOGIC IN COLLABORATION WITH SUPPLIERS**

MANAGING THE PROCESS OF ADOPTING SERVICE LOGIC IN COLLABORATION WITH SUPPLIERS

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Abstract

The purpose of this paper is to identify issues encountered when adopting service logic at an industrial firm in collaboration with suppliers. A second purpose is to investigate how the implementation of supply relationships affects the adoption process. Case research has been conducted at a multinational systems provider in the midst of the change process, introducing relationship-based and process-oriented services with the support of several suppliers and partners. Several issues are identified and three main conclusions are drawn. First, that issues previously identified by other researchers may be generalised to include firms that have gone further in their adoption processes. Second, implementing supply relationships can be an important issue for the adoption for service logic and may impede the overall adoption of service logic. Third, the strategy itself (service or sourcing) seems to be an important issue; difficult to formulate and difficult to implement if formulated. A final conclusion is that a double-loop composed of a participative loop and an authoritarian loop seems to be a fruitful approach to managing the adoption process.

Introduction

Delivering services can be a means of compensating for decreased profitability when selling goods and can increase profit margins. It can also lead to closer bonds with the customer, improved customer satisfaction and can increase the success rate of new products. However, since products and services are often easy for competitors to copy, merely complementing the product offering with basic services, e.g. installation and repair, is often not enough as a differentiator, and other ways of creating value for the customer, over time, should be sought. Some authors stress the need to offer more advanced and customer-oriented services such as consulting, solutions and training in order to stand out from those delivering the more standardised product services (Mathieu, 2001a). Others are of the opinion that industrial firms should focus on the customers' value-creating processes instead of the output from the production processes (Vandermerwe, 1996). Researchers have also empirically observed that some firms are starting to deliver a new kind of offering intended to make their customers' lives easier and better, either by integrating products and services in complete solutions or by integrating forward in the value chain and taking over the customer's operation (Miller et al., 2002). All these descriptions and empirical observations reflect a shift in focus

among product-oriented industrial firms which has been conceptualised by Oliva and Kallenberg (2003) as two transitions: (1) from product-oriented services to the end-user's process oriented services, and (2) from transaction-based services to relationship-based services. Managing these transitions constitutes a major managerial challenge, but the literature is surprisingly sparse as regards describing the strategic issues inherent in the transitions (Oliva and Kallenberg, 2003).

In this paper, strategic issues are seen obstacles to the adoption of service logic and organisational problems occurring as a consequence of the adoption process. The first purpose of this paper is to identify issues during the adoption process for a firm that has gone further in the transition process and to compare them with issues suggested by previous researchers. The second purpose of this paper is to investigate how the implementation of supply relationships, for the delivery of product services, affects the adoption process of a service logic involving relationship-based and process-oriented services, which is an area where very little empirical research has been done.

One case study was conducted at a multinational systems provider, here called "SysCo", which was attempting to adopt service logic with the support of several suppliers and partners. The paper is divided into three main parts. In the first part, a literature review is presented, focusing on transitions and issues in the adoption of service logic. In the second, the case of SysCo and the methodology are presented. The third part of the paper presents the results and the conclusions of the paper. Apart from identifying strategic issues during the adoption process, the results indicate that caution is needed when outsourcing basic services so that the adoption of service logic is not jeopardised.

Theoretical background

Although this paper focuses on the adoption process rather than strategy, some of the literature on strategy will first be summarised in order to define the transitions needed to undertake adoption of the service logic. The literature focusing on strategic issues during adoption will then be reviewed. Previously, this is an area which has only been addressed to a very limited extent (Oliva and Kallenberg, 2003).

Transitions during the process of adopting service logic

Industrial firms are increasingly adding services as a key component of their business strategy and are moving from manufacturing physical goods to delivering services. The advice given by many researchers is that industrial firms should assume a "service logic", meaning that the customers' needs and wants are seen as business opportunities, in contrast to, for instance, the "industrial logic" where cost minimisation is the focus (Kingman-Brundage, George and Bowen, 1995). The move to services basically means that service management is positioned as a

strategic opportunity. However, since copying services is often easy for competitors to do, merely offering standard services is often not enough and better ways of creating value for the customer must be sought, e.g. offering and delivering tailored, more complete offerings, sometimes designated “integrated solutions”, “customer solutions”, “turnkey solutions” or “full-services”. Some authors stress the need to offer more advanced and proactive services (e.g. consulting and training) in order to stand out from those delivering the more standardised product services (e.g. repair) (Mathieu, 2001a). All these different concepts and suggestions mean that the focus is on the customer’s economics rather than just on the product’s economics or on the customer’s value-creating processes instead of the output from the production processes (Vandermerwe, 1996). Offerings such as solutions and full-services are basically about making the customers’ lives easier and better, whereas products are about functionality (Miller et al., 2002).

In this paper, based mainly on Oliva and Kallenberg’s paper (2003), adopting service logic corresponds to a number of basic transitions that are made in the offering. The last two transitions are not necessarily sequential.

- T1. From industrial logic to service logic, or the entrance onto the service market of the delivered goods.
- T2. From product-oriented services to the end-user’s process-oriented services, or from a service supporting the customer’s product to a service supporting his actions (Mathieu, 2001a). Product-oriented services are, for instance, maintenance services. Process-oriented services are professional services and operational services such as managing operations.
- T3. From transaction-based services to relationship-based services. Transaction-based services include basic services such as documentation, repairs/spares, upgrades/updates. Relationship-based services include maintenance services such as preventive maintenance and spare-parts management.

Firms that have undergone transitions T2 and T3 can typically act as intermediaries between the customer and the suppliers of products and more basic services, meaning that they have increased their power and their possibilities of influencing the design of the delivery system (Stern and Weitz, 1997). Furthermore, a full-service or solutions strategy, which corresponds to these last transitions (T2 and T3), is typically interrelated with a number of strategic changes on the supply side of companies. For example, the outsourcing of non-critical activities and the establishment of close relationships with suppliers, reducing the number of suppliers, and implementing alliances with partners and suppliers in order to satisfy customers and provide the total customer experience. Thus, another transition can be formulated, which can be seen as both a precondition for, and a consequence of, the adoption of service logic.

T4. The introduction of new supply relationships at various points in the service distribution channel

The focus of this paper is to study issues perceived by a firm as a result of the ongoing attempts to undergo transitions T2-T4. Of more specific interest is to see how the introduction of supply relationships (T4) affects the adoption of service logic.

Strategic issues in the adoption of service logic

Very few examples were found of empirically grounded studies that focus on issues related to the transition process of industrial firms towards services. One exception is an empirical study by Oliva and Kallenberg (2003), which is based on interviews with senior managers and archival data from eleven equipment manufacturers relatively early during the adoption process. A few other studies have suggested challenges based on studies of archival data, interviews with top-management, or without referring to any empirical data. Although the empirical evidence is sparse, the challenges suggested in previous research will now be summarised (see Table I), grouped into internal issues (within the industrial firm), upstream issues (in the relationship with suppliers and partners) and downstream issues (in the relationship with the customer). Of the studies referred to, the one by Davies et al (2001) focused on a transformation corresponding to transitions T2-T4, while the others focused on transition T1.

Table I. A summary of previously identified issues in the process of adopting service logic.

Internal issues	Downstream issues	Upstream issues
<ul style="list-style-type: none"> •Infrastructure, i.e. building and managing systems and an infrastructure for services (Oliva and Kallenberg, 2003) •Service Skills, i.e. developing skills in, for instance, providing services (operational, relationship-based, and process-oriented), pricing, and risk management. (Davies et al., 2001, Mathe and Shapiro, 1993, Mathieu, 2001b, Oliva and Kallenberg, 2003) •Change Management, i.e. managing internal resistance and cultural change when moving from products to services (Davies et al., 2001, Mathieu, 2001b, Oliva and Kallenberg, 2003) 	<ul style="list-style-type: none"> •Establishing an ongoing customer relationship and a reputation as a service provider (Oliva and Kallenberg, 2003) 	<ul style="list-style-type: none"> •Establishing appropriate collaboration within the service distribution channel in order to become more efficient and customer-oriented (Davies et al., 2001, Oliva and Kallenberg, 2003)

Adopting service logic – a case study

This study was conducted as case research within SysCo, a multinational systems provider with over 25,000 employees and its head office in Europe, selling relatively complex specialty goods and systems solutions to industrial customers all over the world. Services correspond to a significant proportion of the firm's revenues, and this is increasing due to the maturing market for its goods. This paper focuses on repair, product support, product-oriented training, installation, systems integration, business solutions, full maintenance contracts, and managing customers' operations. The last three services are relatively new and are seen as strategically very important, and are also the goal of the current adoption of service logic, see Figure 1. SysCo is currently implementing several supply relationships for the delivery of several types of product services.

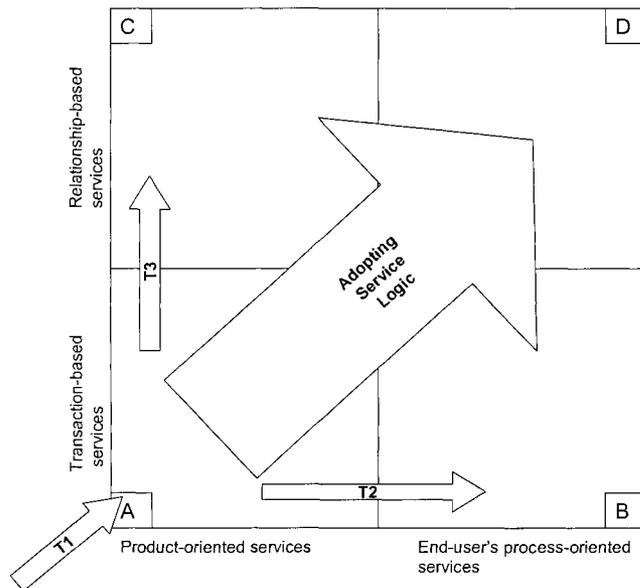


Figure 1. Strategic issues during the adoption process

Data was primarily collected through 30 semi-structured interviews with several types of respondents from several of the SysCo's organisational units. The respondents ranged from product and line managers to alliance and contract managers, primarily from the service side of the organisation, but also from the product side. The interviews were conducted on two occasions, with ten months between them. Supplementary to the interviews, the author read several internal documents and participated in several presentation meetings and conferences for

the employees of the studied firm. This was made possible by the author being a part-time employee of SysCo during the period under study.

The analysis focused on generating lists of strategic issues related to the adoption of service logic and on clustering them into large categories of associated sources of strategic issues. The location of the strategic issues was also coded in line with the theoretical background used in this paper (internal, upstream, downstream, or contextual). As a quantitative measure, the occurrence of each type of issue during the interviews was counted. The numbers were then compared in order to get an idea of the relative importance of each issue.

This section summarises the findings regarding strategic issues during the adoption process of service logic, and are illustrated using excerpts from the interviews. This section also summarises the countermeasures that were identified during the study. The issues are grouped into internal, downstream and upstream issues in line with the theoretical background described above.

Internal strategic issues

One recurring theme in the interviews was the lack of appropriate competence for adopting service logic at SysCo. According to the respondents, adoption required better competence in developing and offering solutions instead of developing and offering predefined platforms and stand-alone products and services. Other areas where competence was judged to be insufficient were partnering and sourcing, while competence was also lacking for externally sourced technologies. Since products were increasingly being sourced externally, the competence for product support was being weakened. One employee explained his view of sourcing competence:

”We sign agreements, and suddenly the third-party supplier says that the budget has been used up, and everything stops. We have to solve everything and the costs of the supplier keeps on accumulating, making the collaboration very expensive for us” (Project Manager, Hardware Platform Development)

Another issue mentioned was that the management system of SysCo was considered inappropriate both for a service business and for collaborating with suppliers and partners. One employee said:

”You can’t call your firm a service firm if you do not know what you have sold in terms of hardware and software to your customers. It’s quite fascinating that we don’t know that” (Service Sales Manager)

A third issue was that the actual service operation was not working satisfactorily at SysCo. The delivery of both basic services, such as product support, and of more advanced services, such as systems integration, was problematic. One suggested reason for these problems was the complexity of the systems and the increasing external sourcing of technology. Finally, some respondents named internal resistance and the inability to manage the internal change effectively and

efficiently as a major issue. For example, there was concern that alliances would reduce the profitability of some units at SysCo, causing scepticism towards partnering. The culture was also considered a problem since the product culture was still prevalent. One employee described the internal problems thus:

“Many of our former employees have been outsourced to our current suppliers and partners, and the Market Unit managers seem to have a predilection for these, giving them the contract no matter what we say” (Contracting Manager, Installation Services)

In contrast, others expressed that there was actually too much effort going into introducing more advanced services and solutions, and that the internal resources were not being used efficiently or effectively during the adoption.

As illustrated in the excerpts, there was evidence in the interview data for all the categories of internal issues summarised in the theory section of this paper. Apart from these issues, the service and partnering strategies were also considered to be strategic issues. Several respondents described the strategies as absent, unclear, wrong, or incomplete. SysCo was apparently struggling with its service and partnering strategies. One employee expressed his view thus:

“I can’t see any partnering strategy on a high-level that I can align myself with, so I have to create my own strategy for training services. Our managers talk a lot about partnering, but very little is done to make something happen regarding our partnering activities” (Partnering Manager, Training Services)

Countermeasures: Significant documentation and communication measures were conducted between the two sets of interviews. Strategies and plans were formulated more clearly and communicated internally. Some extraordinary actions were taken by individuals in the organisation in order to improve the efficiency and effectiveness of the services delivered, triggered by the currently low service levels and high costs. These individuals seemed to be driven by their own motive power, rather than any formal role or responsibility. Several internal management meetings were held, where strategies and plans were presented and discussed. The number of services included in the service portfolio was reduced and the internal rhetoric was changed. One employee explained,

“Instead of talking about specific services, we now talk about the sum of the capabilities represented by the portfolio. The communication has been lifted to our capabilities and the customers’ issues” (Service Marketing Manager)

Downstream strategic issues

Meeting the customers’ needs, marketing, offering, and selling services and solutions were all considered problematic for several reasons. First, the customers did not yet perceive SysCo as a competent solutions provider since it did not have much of a history in providing solutions. There were other competing supplier firms that were considered more competent in providing advanced and consultative services, typically consulting firms and system integrators. Second, the marketing

and sales processes used by SysCo were not considered proactive enough, and the focus was still on marketing and sales of goods. One employee had this to say:

”We are working traditionally, submitting quotations only when the customer requests it, instead of being proactive. We believe the customer wants it like that, but our dilemma is that we believe we understand the customer’s needs, and then we are surprised” (Product Manager, Business Solutions)

Countermeasures: Areas where SysCo should, or should not, front the customer, were decided upon and documented. A partnering and supplier strategy was also developed and communicated. Discussions about taking over customers’ operations were continued, although no new orders were taken. As a matter of fact, the demand for these services was somewhat lower than expected. These discussions were with the CEOs and CFOs of the customers. Furthermore, Business Advisors were assigned to work in the direct sales process, to analyse the situation of the customer and come up with proactive ideas. A “prime contractor role” was described and documented, and a function focusing on this role was set up to develop the concept. Project management of installation projects was brought back to SysCo in order to maintain the relationship with the customer and reduce the risk of competition from installation suppliers. In other words, SysCo went from turnkey to partial outsourcing (Van Weele, 2002) One employee described this challenge thus:

”Installation is a gigantic business and we want to be the intermediary between the customer and the installation suppliers. Then we want to carry out the more advanced tasks ourselves, such as integration, testing, and verification” (Service Marketing Manager)

Upstream strategic issues

These issues are related to supply relationships in the service distribution channel and how this affects the adoption of service logic. Competition from suppliers and partners in the service distribution channel was described as the most significant issue by several of the respondents. In particular, there were several (potential) suppliers and partners that also wanted to become a single point of contact for the customers, acting as the intermediary between the customer and other suppliers of products and services. Nevertheless, SysCo had to collaborate with some of these potential competitors in order to provide the comprehensive solutions that the customer wanted. Furthermore, the increasing external sourcing of goods made collaboration with technology suppliers for the delivery of product services necessary. SysCo’s strategy was to front the customer in most cases and use the technology suppliers as suppliers. However, the profitability when supporting external technology was low and it was difficult to manage all suppliers. During the adoption process, SysCo experienced that some suppliers of basic services, such as installation and repair, tended to develop more advanced services and offer a broader range of services directly to SysCo’s customers, thus entering into

competition with SysCo in providing more complete services to customers. The basic services functioned as a door-opener and a starting point for the offering of other services also being offered and delivered by SysCo. One employee described the competition from suppliers thus:

”Some suppliers admit that their strategy is to compete with SysCo. Their goal is to become full-service providers to our customers. These tendencies are emerging everywhere; it is not just a case of isolated incidents. We almost lost the project management for installation, and if you lose project management, there is a risk that you will lose the ability and capacity to deliver other services” (Contracting Manager, Installation Services)

Countermeasures: A more selective supplier strategy was introduced, using the new experiences from suppliers competing for the service business. Suppliers of basic services, such as repair, were evaluated from the firm level rather than just the business unit level to account for the risks of competition on the overall level. One employee described it like this:

”We do not want to collaborate with firms that have too many ambitions in the areas where we want to compete. Now there is a steering group for all our supplier and partner relationships, where senior managers from several functions at the firm make sure that we have a firm level perspective on these relationships” (Product Manager, Managing Operations)

Synthesis and discussion of the identified issues

The following table summarises the areas that were identified as issues at SysCo, including the countermeasures that were taken. A distinction is made between general issues and issues related to the implementation of supply relationships in the service distribution channel.

Table II. A summary of the identified issues in the process of adopting service logic.

Internal issues (75%)	Downstream issues (10%)	Upstream issues (15%)
<u>General issues</u> Service and solutions strategy and offering Service and solutions competence Change management Management system Service operations <u>Supply relationship issues</u> Managing partners and suppliers Contracting Supporting externally-sourced products Partnering strategy	<u>General issues</u> Customer perception Customer demand difficult to predict Marketing and sales process and customer interaction <u>Supply relationship issues</u> Losing customer relationship to suppliers/partners Prime contractor role Degree of outsourcing (full/partial) to retain power over the customer relationship	<u>General issues (also supply relationship issues)</u> Collaboration with and between technology suppliers for the delivery of product support Competition from suppliers and partners

The numbers in the table reflect the occurrence groups of issues and countermeasures were mentioned during the interviews. An initial observation is the overwhelming number of internal issues that were mentioned, which may reflect the fact that SysCo's adoption process is still at an early stage. Another explanation may be that the majority of respondents were from the head office of SysCo rather than Market Units, and thus had relatively less insight into the downstream and upstream issues occurring in the delivery channel.

Three main observations can be made from this study: The first one is that the general issues identified in this paper (see Table II) are similar to those suggested by previous researchers (see Table I), thus confirming previous research. For example, service skills, change management, and systems were found to be internal issues in the present study as well as in previous studies. Likewise, the interaction and relationship with the customer were found to be problematic in both this and previous studies. Finally, collaboration with suppliers in the service distribution channel was found to be an issue in both present and previous studies. This is interesting because the issues suggested by Oliva and Kallenberg are based on their study of firms relatively early on in the adoption process, while this study is based on a firm which is about to go further into the adoption process and which has been working intensively with the adoption of service logic for several years. Thus, the results of the study conducted by Oliva and Kallenberg seem to be generalisable further than their own data can substantiate, including firms about to adopt a service logic which includes more advanced and customer-oriented services. The second observation is that this case study illustrates the importance of supply relationships for the adoption of service logic more explicitly than do Oliva and Kallenberg (2003), for example. For SysCo, this was clearly one of the most challenging issues. Furthermore, by taking the analysis of the data from this study one step further, it can be concluded that the outsourcing of basic services entailed consequences for SysCo's adoption of service logic. For example, some suppliers of basic services, such as installation and repair, were also aiming for the more advanced services corresponding to service spaces B-D (see Figure 1), and were thus perceived as threats to adoption. SysCo's response was to avoid these particular suppliers altogether. In contrast to the conventional wisdom of outsourcing supplementary services or activities, where the firm does not have unique capabilities, to specialised service firms, this study has indicated the need for a more cautious sourcing strategy in order not to impede the overall adoption of service logic. This can be compared with McCutcheon and Stuart's advice to avoid supply chain partners that may integrate forwards and become competitors (2000) and Kotabe and Murray's general advice to strive to maintain the relationship with the customer when services are outsourced (2001). The third, and final, observation is that this study also identified the issue of strategy, which was not explicitly mentioned in any of the other papers cited. An excerpt from an interview

with the former manager of the service organisation of SysCo could illustrate one reason for this issue:

“I have been working for several years with strategy exercises at SysCo. I have recorded every strategic plan made by the firm. My conclusion is that we have never been able to identify changes. And my conclusion from this is that we need to guard against unforeseeable events and be flexible, rather than plan” (Senior Vice President, Global Services)

This excerpt illustrates the difficulties of implementing formulated strategies, and the need to adopt or adjust to events in one’s environment rather than implement strategic changes such as service logic. In particular, when the transformation is achieved by means of implementing supply relationships, it is very difficult to determine the details of the service strategy *ex ante*. The strategy emerges during the course of time, rather than being planned in advance (Mintzberg, 1978), and it is the outcome of a negotiation and learning process. By definition, strategy deals with the unknowable (Quinn, 1999). Nevertheless, the lack of service and partnering strategies caused a lot of frustration internally at SysCo and was perceived by some employees as preventing SysCo from positioning itself on the marketplace.

A new approach to the adoption process emerges

As a response to the issues encountered, summarised in the description above, the managers of SysCo, e.g. the partnering and sourcing manager, were starting to realise the need for a different approach to the adoption process. Instead of the linear and top-driven process previously employed, a more participative approach was emerging where input and involvement from the organisation in the process of adopting service logic and in the formation of a partnering and sourcing strategy was encouraged. The managers were starting to realise that they had to use, and leverage from, the knowledge residing in their organisation, about their own capabilities and about their customers and suppliers. They had also realised the need to involve the employees in the adoption process, to avoid resistance and gain their commitment, and as a consequence a number of meetings, communications, and information gathering acts were held in the organisation. Thus, an adoption process similar to the one described by Manz and colleagues (1991) was emerging, where the knowledge in the organisation was better utilised. In short, the emerging process, based on the experiences by SysCo, can be described as a repetitive process of a participative loop where information about the internal and external context was gathered and commitment from the employees gained, and a more authoritarian loop where more informed strategies were implemented. According to the interviews made, this approach seemed to work much better than the previous approach and many of the internal issues, composing 75% of the issues encountered, seemed to be eliminated. This double-loop utilised the knowledge in the organisation better, and also facilitated the implementation process.

Conclusions

Three main conclusions can be drawn from the study. First, that the issues identified by Oliva and Kallenberg (2003) may be generalised to firms that have gone further in the process of adopting service logic. Second, supply relationships can be an important issue for the adoption of service logic and may impede the overall adoption. Thus, there is a need for a more cautious sourcing strategy than is suggested by the conventional wisdom of outsourcing supplementary services or activities, where the firm does not have unique capabilities, to specialised service firms. Third, the strategy itself (service or sourcing) seems to be an important issue when adopting service logic; difficult to formulate and difficult to implement if formulated. On a more general level, this study lead to the conclusion that, to succeed with the adoption of service logic, the change process should be managed as a repetitive double-loop composed of a participative loop and an authoritarian loop. According to this study, such an approach facilitates knowledge transfer and increases commitment among the employees.

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PAPER IV:

**SEARCHING FOR THE OPTIMUM PRODUCT SERVICE
DISTRIBUTION CHANNEL: EXAMINING THE
ACTIONS OF FIVE INDUSTRIAL FIRMS**

SEARCHING FOR THE OPTIMUM PRODUCT SERVICE DISTRIBUTION CHANNEL: EXAMINING THE ACTIONS OF FIVE INDUSTRIAL FIRMS

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Abstract

One purpose of this paper is to develop a series of propositions regarding how product, market, and firm contextual factors influence the appropriate channel structure of product services. Another purpose is to identify organisational actions resulting from maladjusted channel structures. The results of five case studies indicate that firms strive to adjust to the appropriate channel structure suggested by the propositions, or compensate for the maladjustment by taking other measures. The propositions could function as a managerial tool for identifying inappropriate channel structures, and thus also for identifying the need for change.

Introduction

“Can you help us to select the best distribution model for our after-sales services? We need to know how successful firms are working. Why don't you get us some information from some of the other firms in your research network and then tell us what we have to do?”

This excerpt from a discussion with the managers of a leading industrial firm was the origin of the case research reported in this paper. The assignment we were given by these managers was to study some leading firms from other industries and find the optimum distribution model to be implemented. We asked ourselves whether it would be possible to learn anything relevant from the other firms, and whether we would be able to give any satisfactory answers to those managers. Is there such a thing as an optimum distribution model at all? Although we had our doubts, the discussion reflected an area of great practical importance for industrial firms and which contained relatively little published academic research, namely post sale product service (henceforth: product service). Consequently, our discussion resulted in the cross-industry case study of service distribution channels reported in this paper.

Product services can be defined as “the set of all potential additional services a supplier can supplement his product offering with” and include, for example, failure handling and regular maintenance inspections (Frambach et al., 1997). Industrial firms delivering goods to their customers generally need to ensure that product services related to the goods can be offered to the same customers to

secure the use and operation of the delivered goods. The importance of product services is increasing, propelled by a stagnating product demand and an expanding installed base in many industries (Wise and Baumgartner, 1999). Delivering product services can be a means of compensating for decreased profitability from selling goods and can increase profit margins (Quinn et al., 1990, Wise and Baumgartner, 1999) and lead to closer bonds with the customer (Berry, 1995). Product services have been associated with the following benefits to the manufacturing firm: (1) they can be a source of revenue for manufacturing firms, (2) they can improve customer satisfaction, (3) they can provide competitive advantage, and (4) they can increase the success rate of new products (Goffin, 1999).

One important issue for industrial firms interested in leveraging the opportunities related to delivering product services deals with the structuring of the distribution channels for the product services (henceforth: service channels). Services are inherently relational because the customer always has to interact with the service provider in some way (Grönroos, 2000), and thus the position of a company, in relation to its customers, is important. The most powerful participant in a service channel in terms of its influence on the design of the delivery system is normally the service firm or the intermediary providing the services (Light, 1986). This power has been increasing lately due to, for example, better management information systems (Stern and Weitz, 1997) and by the tendency of many industrial customers to move away from adversarial relationships with suppliers towards more cooperative ones (Swift, 1995). However, the choice of direct channels (using the internal organization for the delivery of services) or indirect channels (using agents, retailers and third party service providers, etc.) must be guided by the attributes of the products, the market, and the firm (Loomba, 1996).

Although product services is still an area with relatively little published academic research (Goffin, 1999), some articles have been published on service channels (Loomba, 1996, Goffin, 1999, Armistead and Clark, 1992, Hull and Cox, 1994, Armistead and Clark, 1991). Still there is a need for further empirical testing, refinement and extension of the research into how service channels should be arranged, and how they are actually arranged. Due to the importance of the service channel, it can be expected that firms failing to arrange their service channels appropriately will encounter pressure from investors and informed employees within their own organisation.

The first purpose of this paper is to summarise, extend and refine the previous research into product service channels by Armistead et al (1991, 1992), Goffin (1999), Hull and Cox (1994) and Loomba (1996) in propositions that relates product, market, and firm contextual factors to the appropriate service channel structure (direct or indirect) for three product service processes (contracting, ordering, and expediting). Testing whether these propositions reflect the state-of-the-art is not the purpose of this article, neither is it to test how average firms do.

Instead, *the second purpose* is to investigate the results of maladjustment, or divergence from the appropriate service channel structure suggested by the contextual factors, in the form of the behaviours, actions and activities of the firms. Here, a service channel is called *appropriate* if it agrees with propositions P1-P6, even though there may sometimes be sound reasons for employing other structures. Consequently, a service channel is called *maladjusted* if it does not agree with one or more of the propositions. It can be assumed that maladjusted service channels lead to problems, and put pressure on the firms to change the structure of the service channel or to take measures to compensate for the inefficiency of the applied service channel structure.

This paper is divided into three main parts. In the first part, a theoretical background is presented and propositions regarding how contextual factors influence the service channel structure are suggested. In the second, the methodology and cases are presented. Finally, the findings and conclusions are presented. The results of the five case studies conducted at American and European firms indicate that the propositions could function as a managerial tool for identifying maladjustments in the applied service channel structures, and that a maladjusted service channel structure stresses the need to implement a change of structure or to take measures to compensate for the maladjustment.

Theoretical background

Key processes of a product service channel

Before a product service channel can be structured, it is essential to select its various processes for which individual decisions can be made. Several authors have already described alternative channel arrangements, both in general (Cespedes and Corey, 1990, Hardy and Magrath, 1988, Stern et al., 1996) and specifically for services (Light, 1986, Maltz and Maltz, 1998, Loomba, 1996, Cohen et al., 2000). Common to these descriptions is the fact that they stay on a relatively high conceptual level, neglecting the different processes and functions included in a service relationship and neglecting to take more than one, or maybe two, contextual factors into account. One notable exception is the research of Goffin (1999), which provides the most comprehensive empirically-based description so far of the product service channels, distinguishing between the sales channel and the support channels. Another exception is the research of Armistead and Clark (1992, 1991) who attempt to formulate a framework for the choice of channel structure. This research has certainly extended our knowledge of service channels, but due to the peculiarity of product services, for example the customer-supplier duality (Sampson, 2000), there is reason to make an even more detailed differentiation between different service processes in interactions with customers, taking several of the contextual factors into account at the same time. For the purposes of this paper, using a purchasing process perspective has been seen as a

fruitful point of departure when defining the central service processes in the arrangement of the product service channel, since it clearly differentiates between different types of on-stage activities (Kingman-Brundage, 1992). According to Van Weele (2002, p. 15), the purchasing process includes the following three processes:

- The contracting process: purchase of service by customer and perhaps signing of service contract
- The ordering process: ordering of service by customer when the product needs support/maintenance, in line with previously arranged contracts
- The expediting process: delivery of service to customer (e.g. repair, field service, software updates, delivering spare parts, service logistics)

In this paper, these three processes are seen as the core of the interaction between the buyers and sellers of product services, and the key processes in a channel for product services for which individual make/buy decisions can be made. In other words, each process can either be conducted by the internal organization (direct) or by external intermediaries (indirect), and the decision can be made for each process separately. For example, when an industrial firm lets an external service supplier handle the repair of its sold products (expediting), this does not mean that the contracting process should be between the service supplier and the customer. The contract may still be signed between the industrial firm and the customer in order to retain some in-house control (Armistead and Clark, 1992) and the service orders may either be taken by the industrial firm or by the service supplier. Thus, although the choices are interrelated, separate choices can (and often should) be made for each of these processes. This is normally not explicitly addressed in the previous literature

Effects of contextual factors

An industrial firm interested in leveraging the opportunities related to delivering product services to its customers faces several choices when designing its channel for product services. As mentioned above, it is generally better to be close to the customers since this more central position entails greater possibilities of influencing the others involved in the service system. This would mean that the contracting, ordering, and expediting processes should all be conducted in-house. However, this is often unfeasible, for efficiency, effectiveness, and capacity reasons, which will be discussed in the following section. Industrial firms tend to outsource service processes when they do not have sufficient capabilities to perform the service effectively, the ability to perform the service cost efficiently, or the capacity to perform the service (Axelsson and Wynstra, 2002). Previous research into how contextual factors guide the choice of service channel structures has been broadly based on the same motivations as those suggested by Axelsson and Wynstra (2002), i.e. efficiency, effectiveness, and capacity motivations.

Here, the contextual factors guiding the choice of service channel structure are divided into product related factors, market related factors, and firm related factors. As there is often no distinction between the contracting, ordering and expediting processes in the previous literature, clarifications and distinctions between the different processes are suggested in this paper. Although many of the suggested contextual factors are interrelated, they are separated here to provide a more detailed picture. Contracting, ordering and expediting are different processes for which different decisions can be made. The propositions are to be seen as rules-of-thumb under which factors of effectiveness, efficiency, and capacity are implicit.

Product contextual factors

Complex products are typically engineering-intensive and composed of several tailored components and sub-systems. They always play a role in a larger system, in contrast to simple mass-produced stand-alone products (Hobday, 1998). Taking full responsibility for complex products requires complete understanding and control of the whole system, including interfaces and software. According to Armistead and Clark (1992), complex goods typically require more support and manufacturers of complex products often use direct service channels to retain control over the services delivered, in contrast to manufacturers of simple goods. Complex products may be composed of several simple products for which the expediting process can be handled by external firms. Thus, the following propositions are suggested:

P1a: For complex products, industrial firms will choose direct contracting and ordering processes for services

P1b: For simple products, industrial firms will choose indirect contracting and ordering processes for services

The expertise for supporting commodity products (mass-produced non-specialized products) is generally available on the market, and thus indirect service expediting is typically chosen. Typically, specialized service companies can achieve economies of scale that are not possible at industrial firms. For specialty products, on the other hand, the expediting of services is typically direct since there is less expertise available on the market (Loomba, 1996) and thus the industrial firm has a unique capability (Quinn et al., 1990) to support the products.

P2a: For specialty products, industrial firms will choose direct expediting processes for services

P2b: For commodity products, industrial firms will choose indirect expediting processes for services

A reliable product entails a lower service intensity, which is typically associated with direct product service channels. This is typically dependent on the stage of the lifecycle, with mature products having higher reliability (Armistead and Clark, 1992, p. 50-51), leading to direct expediting processes. The frequency of preventive maintenance required, the availability requirements, and the number of installed units also affect the service intensity. Indirect channels are most appropriate when the service intensity is relatively high, as for non-reliable products requiring frequent corrective or preventive maintenance. Only when the service intensity is high is it normally justified for independent firms to take on the responsibility of expediting the services and building the necessary capabilities. Otherwise the industrial firm typically expedites the services in its own regime, which is relatively easy because the expertise associated with the product is already available in the firm.

P3a: For products with a low service intensity, industrial firms will choose direct expediting processes for services.

P3b: For products with a high service intensity, industrial firms will choose indirect expediting processes for services.

Market contextual factors

Direct marketing channels, here interpreted as the channels for contracting and ordering, are appropriate for the more heterogeneous business markets, whereas indirect channels are appropriate for the more homogenous consumer markets (Cespedes and Corey, 1990, Anderson and Narus, 1998, Ford et al., 1998). Business markets typically involve fewer customers with individual needs. In contrast to consumers, companies are generally buying products and services in large quantities, have high expectations on the support, and prefer to have close working relationships with their suppliers. These factors provide economic incentives for industrial firms, which do not exist in consumer markets, to choose direct service processes (Anderson et al., 1998).

P4a: Industrial firms operating in business markets will choose direct contracting and ordering processes for services

P4b: Industrial firms operating in consumer markets will choose indirect contracting and ordering processes for services

The choice of product service channel (direct/indirect) is often similar to the choice of product distribution channel (Loomba, 1996), because the underlying logics are similar. Furthermore, there is often reason to have the same channel for product distribution and product service, because this provides convenience for the

customers. The choice of product service channel in turn depends on e.g. the type of market (Cespedes and Corey, 1990, Anderson and Narus, 1998).

P5a: Industrial firms using direct contracting and ordering processes for their goods will choose direct contracting and ordering processes for services.

P5b: Industrial firms using indirect contracting and ordering processes for their goods will choose indirect contracting and ordering processes for services.

Firm contextual factors

A high contribution to profits by the services typically leads to an integrated service function (Mathe and Shapiro, 1993), here interpreted as direct contracting and ordering processes. With such structure the industrial firm retains the relationship with the customer and the influence over the profitable service business. Among other things, this relative profit depends on the ratio of installed units to annual new-unit sales (Wise and Baumgartner, 1999), which is normally high for mature products.

P6a: Industrial firms for which services (potentially) contribute significantly to profits will choose direct contracting and ordering processes.

P6b: Industrial firms for which services (potentially) contribute little to profits will choose indirect contracting and ordering processes.

Research proposition: Effects of maladjusted product service channels

It would be naïve to assume that all firms adopt service channel structures that maximise efficiency and effectiveness. On the contrary, in order to leverage the opportunities of product services, some firms may go too far in implementing direct service processes, whereas others will miss the opportunities provided by services and let external firms handle everything connected with services. It is common that the applied channel structure is sometimes maladjusted and not well adapted to the contextual factors and propositions of this paper. It can be assumed that industrial firms with a maladjusted channel structure will tend to change channel structure or take measures compensating for the deficiency in order to better leverage the opportunities of services. The pressure to take action may come from inside the firm (e.g. from employees) or it may be external (e.g. pressure from investors). Similarly, it can be assumed that firms trying to implement the wrong, or maladjusted, channel structure will encounter resistance. The maladjustment may be the result of sound strategic, operational, or other reasons. In this case, the firm may stay with its chosen channel structure and compensate for the maladjustment by taking measures such as introducing stronger governance mechanisms, or increasing internal expertise. The maladjustment may also be the

result of bad management, and in this case the firm should preferably adapt to a more appropriate channel structure. In other cases, the different contextual factors support contradictory propositions for the same service process. For example, one contextual factor may propose direct expediting whereas another one may propose indirect expediting. This makes the choice of channel structure more complex and, irrespective of the choice made, one or more propositions will not be supported. Also, measures may be needed here to compensate for this maladjustment, or the channel structure can be changed. In this case, however, the maladjustment cannot be avoided altogether.

The following research propositions can be formulated:

P7: Firms with maladjusted service channel structures (deviating from the service channel structures described in propositions P1-P6) will strive to change the service channel structure or introduce measures to compensate for the deviation.

Using direct service processes when the contextual factors suggest indirect service processes can be expected to lead to either a changed channel structure or compensation in terms of increased internal resources and competencies. Using indirect processes, when the contextual factors suggest direct processes, can be expected to lead to either a changed channel structure or compensation in terms of reinforced governance mechanisms of the customer relationship and relationships in the service channel to retain control of the strategically important relationship with the customer (Kotabe and Murray, 2001).

Methodology

Research design

This paper is based on case research at five companies from different industries, Alpha, Beta, Gamma, Delta, and Epsilon (pseudonyms have been used in this paper to protect the anonymity of the companies and the involved participants). All firms are involved in the delivery of goods to their customers, and, to this end, they are also involved, to varying degrees, in delivering different product services.

The firms were intentionally selected because they represented a variety of contextual factors, thus covering the propositions in this paper. A wide range of industry sectors was included (from mechanical engineering to IT). The studied firms were also selected because of their varying degrees of service orientation, from being involved solely in basic product services, such as the supply of spare parts, to focusing on providing services and complete solutions. The reason for this variety was that it enabled the analysis of firms with maladjusted service channels, as well as firms with service channels which were well-adjusted to the contextual factors.

Data collection

Data was collected by means of formal semi-structured interviews with 15 respondents from the studied firms. Of the respondents, seven were employees at Alpha, five at Beta, two at Gamma, two at Delta, and two at Epsilon. On average, the interviews lasted for about one hour. The respondents were selected because they were recognized as being knowledgeable about the strategy and the post sale business models of their respective firms. They held different positions at their firms, ranging from service operations managers to contract managers and salespersons. The interviews were recorded and transcribed in detail. The interviews focused on (1) the strategy and business of the firm, (2) the structure of the service channel, and (3) problems associated with the applied channel structure. During the later interviews, the preliminary results of the analysis were also discussed with the respondents and gradually refined. Case descriptions were also reviewed by some of the respondents.

Besides these interviews, empirical observations were made by the author of this paper over several years, both as a researcher and an employee of Gamma, in addition to informal discussions and meetings with colleagues from Gamma. Three informal meetings were also held with employees from Beta and Delta to discuss the findings of the study. These employees, one from Beta and two from Delta, did not participate in the 15 semi-structured interviews described above and thus increased the sample of respondents. Several informal phone calls with employees of the studied firms, together with company documents such as annual reports, organizational charts, and process descriptions, were also used as sources of information.

Data analysis

The analysis focused on:

1. Classifying the contextual factors of the cases according to propositions P1-P6
2. Identifying maladjustments in the applied service channel, i.e. identifying where the applied service channels deviate from those suggested by the propositions.
3. Identifying issues described by the respondents from the case firms related to the structure of their service channels.
4. Testing proposition P7 by comparing identified maladjustments with the issues identified during the case studies. A correlation between the identified maladjustments and issues means that proposition P7 is supported, indicating that the propositions could be used for the identification of (potential) areas needing special attention by management.

5. Investigating what sorts of measures will be taken by the studied firms to eliminate or compensate for these maladjustments.

Propositions P1-P6 are based on the previous literature and are taken for granted in this paper. They have not been tested but are used as a means of classifying the cases and testing proposition P7, which is the central issue of this paper. For sake of simplicity, the analysis is done at the corporate level, although the diversity of the product lines of Beta, Gamma and Delta may suggest that the product market level had been more appropriate. Nevertheless, as it showed to be fairly easy to categorise the contextual factors and service distribution channels at the corporate level, without generalising too much, the level of analysis was judged as appropriate for the purpose of this paper.

Description of the cases

A summary of the contextual factors and problems which the respondents described with the applied business models will be described here for each case.

Alpha uses indirect contracting, ordering, and expediting of services and is a goods-oriented industrial firm with over 10,000 employees. Alpha has its head office in Europe. It develops and sells mass-produced complex stand-alone goods, mainly mechanical, typically worth about \$25,000, to consumers all over the world through independent dealers in which Alpha is not a stakeholder. The product lifecycle is typically about 10-20 years. Parts and components included in the goods are normally highly standardized and increasingly sourced by Alpha from external suppliers of complete systems, and then integrated and assembled by Alpha. Delivering spare parts to the same independent dealers for sales and delivery of the maintenance and repair of the goods has resulted in revenues and profit margins greater than those resulting from the sale of the goods. In spite of this, service is not considered to be very strategic by the management of the company. The overall service intensity can be classified as high due to the very large volumes sold and the corrective and preventive maintenance the goods regularly undergo.

Beta uses direct contracting, ordering, and expediting processes for its business customers and indirect processes for its consumer business. Beta is a leading service-oriented industrial firm with over 100,000 employees and has its head office in the US. Beta develops and sells a broad range of hardware-related simple and complex software-based goods worth between \$100 and \$1,000,000 to industrial customers and consumers all over the world. The goods are sold by an internal sales force in the case of the business products and by independent dealers in the case of the consumer products and smaller businesses. Systems solutions rather than stand-alone products are typically sold to industrial customers, consisting of relatively complex bundles of several different types of products. Both the industrial and consumer goods are increasingly becoming commodities,

although some of the industrial goods can be classified as specialties. Due to the very high volumes of both business and consumer goods sold, the service intensity can be classified as high. The specialty industrial goods are sold in lower volumes, but they have a greater complexity and are less mature. Thus, they also have a relatively high service intensity. The product lifecycle is typically between 3 and 20 years, with a mix of internally and externally developed parts typically making up the products. Apart from offering basic product services, such as maintenance and repair, Beta is increasingly offering functions instead of products, as well as other more advanced services such as multi-vendor services, solutions, and remote software-services. Services and solutions correspond to a significant portion of the firm's revenues. Beta handles the contracting and ordering processes using its own employees for all business services, as well as a large proportion of the expediting process. Consumer services, on the other hand, are handled indirectly. Technology suppliers are consulted regarding back-end service processes related to their products, and governed by very detailed contracts. An external logistics firm operates spare parts warehouses.

Gamma uses direct contracting, ordering, and expediting processes. Gamma is a hardware-oriented industrial firm with over 50,000 employees and has its head office in Europe. Gamma sells relatively complex goods typically worth between \$100,000 and \$5,000,000 to industrial customers all over the world using its own sales force. Increasingly, systems solutions rather than stand-alone products are being sold, consisting of relatively complex bundles of several different types of products. Most goods can be classified as specialties although the proportion of commodities is increasing. The specialties typically have less reliability than the commodities due to greater complexity and lower maturity. As the sold volumes are very high, the overall service intensity can still be classified as high. The product life span is typically between 5 and 20 years, and a mix of internally and externally developed parts typically makes up the products, increasingly software-based. Gamma is responsible for the integration of internal and external parts, although some products are stand-alone and for which Gamma is only a reseller. Apart from selling basic product services, such as maintenance and repair, more advanced services, such as systems integration and consulting, are increasingly being offered to its customers. Services correspond to a significant proportion of the firm's revenues, and this is increasing due to the maturing market for its goods. Gamma uses its own employees for the contracting and ordering processes, and for a large proportion of the expediting process. Technology suppliers are consulted for back-end service processes related to their products, governed by detailed contracts. Commodity goods suppliers in particular expedite the services for their goods. Repair and field service is outsourced, although spare parts warehouses are still operated by employees of Gamma.

Delta uses direct ordering and contracting processes and indirect or direct expediting. Delta is a service-oriented industrial firm with over 10,000 employees

and has its head office in Europe. Delta sells both simple and relatively complex goods typically worth between \$100 and \$1,000,000 to industrial customers and consumers, primarily in Europe, using its own sales force. Systems solutions developed by Delta, rather than stand-alone products, are typically sold. These solutions are composed of relatively complex bundles of several different types of products. The product life span is typically between 2 and 10 years. The goods are typically developed and manufactured by external suppliers, and then purchased by Delta from one main reseller with which they have a contract. The majority of the goods can be classified as specialties, generally with a relatively high level of reliability. The overall service intensity can be classified as relatively high, although certain products are exceptions. The reason for the high service intensity is the very high requirement regarding total systems availability, requiring that technicians be available close to the location of the products. The reseller is also responsible for delivering the goods, and the product services sold by Delta, to the customers.

Epsilon uses indirect contracting, ordering, and expediting processes. Epsilon is a service-oriented industrial firm with over 1,000 employees and has its head office in Europe. Epsilon develops complex software-based goods with many interfaces with other systems, worth about \$100,000 and \$1,000,000, aimed at small and large companies all over the world. The goods are produced in fairly high volumes, are normally customized for each customer, and can be classified as specialties. The product life span is typically between 2 and 10 years. Customers are offered a mix of products developed by Epsilon and other suppliers, through a network of sales partners with whom Epsilon has contracts. Epsilon is primarily involved in the development of software, while hardware design is subcontracted to external firms. The overall service intensity of the goods is not very high since these are reliable and relatively mature. Epsilon uses an indirect strategy for its product services whereby the services are defined by Epsilon but offered and delivered to the end-customers by service partners. Apart from basic product services, a range of more advanced services is offered, e.g. technical consulting and integration. Epsilon's revenues come from products sold to the sales partners where one share of the margin is specifically dedicated to cover Epsilon's back-office service units.

Classifying the contextual factors of the cases

The following table summarizes the contextual factors of the cases.

Table I. Summary of the contextual factors of the firms

			FIRM				
			Alpha	Beta	Gamma	Delta	Epsilon
CONTEXTUAL FACTORS	Product	Product technology	Complex	Simple and complex	Complex	Complex	Complex
		Product maturity	Commodity	Commodity and specialty	Specialty	Specialty	Specialty
		Service intensity	High	High	High	High	Low
	Market	Type of market	Consumer	Business and Consumer	Business	Business	Business
		Contracting and ordering of goods	Indirect	Direct	Direct	Direct	Indirect
	Firm	Services' contribution to profit	High	High	High	Low	Low

Results

Identifying maladjustments

One major focus of this paper is to see whether the cases provide support for proposition P7, and thus to see whether deviations from the appropriate channel structure suggested by propositions P1-P6 will lead to problems related to the service channel structure of the studied firms.

The applied and appropriate service channel structures are summarized in Table II.

Table II. Comparing the typical and applied service channel structure. The numbers indicate the number of propositions suggesting direct/indirect processes.

		FIRM				
		Alpha	Beta	Gamma	Delta	Epsilon
Appropriate business model according to the contextual factors	Contracting	Direct (2) or indirect (2)	Direct (indirect for consumers)	Direct	Direct (3) or indirect (1)	Direct (2) or indirect (2)
	Ordering	Direct (2) or indirect (2)	Direct (indirect for consumers)	Direct	Direct (3) or indirect (1)	Direct (2) or indirect (2)
	Expediting	Indirect	Direct (1) or indirect (1)	Direct (1) or indirect (1)	Direct (1) or indirect (1)	Direct
Applied business model	Contracting	Indirect	Direct (indirect for consumers)	Direct	Direct	Indirect
	Ordering	Indirect	Direct (indirect for consumers)	Direct	Direct	Indirect
	Expediting	Indirect	Direct (indirect for consumers)	Direct	Direct or indirect	Indirect

Some observations can be made. First, the appropriate service channel structure for the studied firms is generally ambiguous. The main reason for this is that the contextual factors are incompatible. Consequently, most maladjustments were caused by contextual factors providing contradictory suggestions. Secondly, of the studied cases, Alpha and Epsilon seem to have the most complex sets of contextual factors, leading to ambiguous advice from propositions P1-P6, while the contextual factors of Beta, Gamma, and Delta are more homogenous. Finally, according to the propositions, Epsilon should change expediting from indirect to direct.

Table III is another way of illustrating the same thing, and shows more clearly where the combination of contextual factors (from Table I) and applied service channel structure (from Table II) of each case either provides support (S) for each proposition P1-P7, or where there is a maladjustment in the applied service channel structure (M).

Table III. The applied service channel's fit with the service channel described by the propositions. "Mx" means that there is a mismatch between the context and the applied business model related to proposition x.

		Alpha	Beta	Gamma	Delta	Epsilon
Product	Complexity (P1)	M _{1a}	S	S	S	M _{1a}
	Maturity (P2)	S	S	S	M _{2a}	M _{2a}
	Service intensity (P3)	S	M _{3b}	M _{3b}	S	M _{3a}
Market	Business/ Consumer (P4)	S	S	S	S	M _{4a}
Firm	Dir./indir. goods channel (P5)	S	S	S	S	S
	Service profit (P6)	M _{6a}	S	S	M _{6b}	S

This analysis indicates that Alpha and Epsilon should either change their channel structure or take measures to compensate for the maladjustments. Beta and Gamma have service channels that are fairly well adjusted to their contextual factors and should only take measures to compensate for the use of direct expediting, in spite of the high service intensity. To test proposition P7, the maladjustments in the applied business model of each case will be compared with the problems and measures described by respondents from each case.

Testing proposition P7 for each case

Since propositions P1-P6 are taken for granted in this paper, maladjustments, or propositions that are not supported by the case (M in Table III), indicate that the firm has made an imperfect choice and needs to adapt to the more appropriate business model described by propositions P1-P6, or take other measures to compensate for this maladjustment. This is what proposition P7 is about, and comparing the issues and measures of each case with the maladjustments tests the correctness of P7. For this reason, the issues and measures described for each case will now be summarized and compared with the maladjustments.

Among the strategic issues described by the respondents from **Alpha** was the lack of understanding by company management of the opportunities of product services and how to leverage them. Another problem was that the large systems suppliers were climbing the value chain to leverage the opportunities rendered by delivering spare parts directly to the dealers, thus going into competition with Alpha. According to the respondents from Alpha, the reason for Alpha's inability to leverage the opportunities offered by services is primarily historical. The firm has

a long history of mass-producing goods and thus has a limited focus on the opportunities related to services. However, as the market for goods is maturing and the profitability from selling goods is decreasing, the need arises to reconsider the business model of the firm. At that moment, there was no consensus within the firm regarding how this should be done. The difficulty choosing a distribution model reflects the ambiguous contextual factors of Alpha and also corresponds broadly with M_{1a} and M_{6a} (indirect contracting and ordering in spite of complex products and high service revenues). The market contextual factors suggest indirect contracting and ordering processes, but the high level of profits from services implies that measures other than changing the business model are needed. Alpha has recognized these maladjustments and has recently set up a team to analyze the business model for services. Acquiring control of the dealers is not an option at the moment due to the problematic financial situation of the firm. The combination of maladjustments and issues at Alpha provides support for P7.

The respondents from **Beta** described few strategic issues related to the product service channel. The service strategy was very clear and there was also a very clear implementation process that had been developed over many years. On the other hand, some suppliers had difficulties accepting that Beta always insisted on managing the customer relationship, including the contracting and ordering processes, but for Beta, this was not a major issue. Beta uses a direct expediting process, in spite of the high service intensity, corresponding to M_{3b} . This choice is nevertheless reasonable since Beta has developed a very large internal service delivery organization comprising about half of its total workforce. In other words, Beta can expedite the services themselves because it has compensated for the maladjustment by developing a large and competent internal service delivery organization. Another reason for their choice is the specialty products, making indirect expediting difficult. Thus, Beta also provides support for P7.

Gamma did not describe any major question marks related to its applied product service channel. Gamma used direct expediting for some service processes (e.g. the operation of spare parts warehouses) in spite of the high service intensity. One explanation for this is that Gamma, just like Beta, also has a very large and competent internal service delivery organization enabling this. However, the long-term strategy is to outsource most of the expediting processes, except for specialty products and more advanced services. Because of the specialty products, Gamma employs direct expediting in spite of the high service intensity. Bearing this in mind, Gamma provides support for P7.

A major problem described by the respondents from **Delta** was that one of the major product suppliers, completely dominating its specialty product market, refused to have a reseller as an intermediary between itself and Delta. Thus, an exception from the business model has recently been made for this single supplier and Delta will now expedite the services for this specific product. In other words,

Delta changed from an indirect to a direct expediting process for specialty products, which is a change supported by P2b. In spite of the relatively low revenues from product services, direct contracting and ordering was used. This corresponds to M_{6b} . This was not perceived to be a problem at Delta and no particular measures were needed to handle the contracting and ordering process for the services since the processes for contracting and ordering goods were already being handled by Delta. Thus, Delta provides partial support for P7.

The sales and service partners of **Epsilon** were reluctant to offer and deliver more complex solutions to their customers since they were associated with a higher business risk. As a consequence, the simpler business deals also tended to be lost. This also hindered Epsilon's attempts to differentiate itself from the competition. To overcome this issue, Epsilon had improved the support given to its sales and service partners to facilitate the offering of more advanced solutions and services. This was necessary but also required extra efforts on the part of Epsilon. The sales and service partners were also dissatisfied with the low service intensity and the high reliability of the products. This made it difficult for them to sell service contracts to their customers. Furthermore, Epsilon is operating on a business market and should thus use a direct contracting and ordering process in accordance with P4a. Since an indirect model is chosen, different sorts of measures have been taken at Delta to compensate for this maladjustment. For example, Delta regularly arranges events with its customers, sales and service partners to close the gap between itself and its customers. It also has employees who are responsible for each of its major customers, who are often located at the respective customer's premises. The management team of Epsilon had recently begun to pave the way for alternative business models for both their product and service business. It is worth noting that the contextual factors of Epsilon are very ambiguous, which can justify the choice of compensation for the maladjustments, rather than changing the channel structure. Epsilon also provides support for proposition P7.

To sum up, the issues experienced and the measures taken by the studied firms, as described by the respondents of this study, tend to deal with the same areas as the maladjustments do. Thus, this study provides support for proposition P7. Furthermore, in line with the predictions made earlier on in this paper, the following two tendencies could be observed. First, firms using more direct service processes than suggested by the propositions of this paper (e.g. Beta and Gamma) were striving to compensate for this by strengthening their competencies and resources. Second, firms with more indirect service processes than suggested by the propositions (e.g. Epsilon) were striving to compensate for this using reinforced governance mechanisms.

Table IV contains a summary of the maladjustments and the corresponding problems of each case.

Table IV. Comparing the maladjustments in the applied service channel structure with problems described.

Firm	Issues and measures	Maladjustments	Support for P7?
Alpha	Lack of understanding of how to leverage the opportunities from services. Parts suppliers bypassing Alfa, delivering spare parts directly to dealers.	Indirect contracting and ordering (M_{1a}) for complex products. High service revenues but indirect contracting and ordering (M_{6a})	Yes
Beta	No serious issues were described. Large internal service organisation.	Direct expediting process in spite of commodity products (M_{2b}) and high service intensity (M_{3b}).	Yes
Gamma	No serious issues were described. Large internal service organisation.	Direct expediting process in spite of the high service intensity (M_{3b}).	Yes
Delta	One major product supplier refusing to have a reseller as an intermediary between itself and Delta. Reseller offering competing products and becoming solutions provider.	Low service profit but direct contracting and ordering (M_{6b}). Indirect expediting process for specialty products (M_{2a}).	Partial
Epsilon	Sales and service partners not able/neglecting to sell/expedite complex solutions and services. Improved support of service and sales partners. Regular events with customers.	Indirect contracting and ordering for complex products (M_{P1a}) and business markets (M_{4a}). Indirect expediting for specialty products (M_{2a}) and low service intensity (M_{3a}).	Yes

Is there an optimum distribution model for product services?

With reference to the questions illustrated by the excerpt in the introduction to this paper; Did we find an optimum distribution model? The answer is no, we did not find an optimum because it is contingent upon several contextual factors, and, even if you take the contextual factors into account, there will seldom be a crystal clear optimum. Nevertheless, looking at the contextual factors can at least provide *indications* of an optimum for each firm, and facilitate a sound choice of distribution model.

Conclusions and implications

In this paper, three central service processes are suggested in the channel for product services: contracting, ordering, and expediting. Each of these processes can either be direct or indirect. Building on previous research, six propositions (P1-P6) are presented regarding how the choice of direct/indirect process is influenced by contextual factors related to the market, the goods, and the firm itself. One contribution made by this paper is that these six propositions are somewhat more *specific* than the previously presented propositions, explicitly differentiating between the three key service processes. Furthermore, these six propositions jointly provide a more *comprehensive* picture than does most previous literature since they summarise several of the previously suggested contextual factors. Taking all six propositions into account makes the choice of business model more complex, but it also provides a more realistic picture of the real situation facing managers of industrial firms, thus facilitating a better choice. By identifying ambiguities between the propositions, it also becomes easier to take the appropriate measures.

A seventh proposition (P7) was suggested regarding how maladjusted service channels put pressure on the industrial firm to change the service channel, or to compensate for the maladjustment by taking other measures. The case studies have provided support for this proposition and illustrated alternatives for how the compensation may be carried out. Firms using more direct service channel structures than appropriate can compensate for this by strengthening their competencies and resources for product services. On the other hand, firms with a more indirect business model than appropriate can compensate for this, using reinforced governance mechanisms of customer relationships and relationships in the service channel to retain in-house control. Thus, this proposition, in combination with the first six propositions, seems to be a potential management tool for finding maladjustments. Neither has a similar proposition been explicitly proposed or tested by previous researchers.

Further research is needed into the mechanisms that can compensate for deviations from the appropriate service distribution channel. Further research is also needed as regards when the contracting and ordering processes can be separated, and into the contextual factors leading to such distribution models.

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PAPER V:

**MANAGING THE CHALLENGES OF OUTSOURCING
SERVICES: LESSONS GLEANED FROM A SYSTEMS
PROVIDER'S INTERORGANIZATIONAL
RELATIONSHIP INITIATIVES**

MANAGING THE CHALLENGES OF OUTSOURCING SERVICES: LESSONS GLEANED FROM A SYSTEMS PROVIDER'S INTERORGANIZATIONAL RELATIONSHIP INITIATIVES

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Abstract

The purpose of this article is to describe the challenges of outsourcing services and provide lessons regarding how they can be managed. The literature on the outsourcing of services has mostly focused on strategy and has tended to neglect the challenges associated with the outsourcing process. One in-depth longitudinal study of a leading European systems provider has been carried out and data from between 1997 and 2003 has been used. Three main lessons learned during the research are described. First, the change process should be interactive and reflective. Second, all outsourcing and partnering initiatives should be coordinated. Third, the customer-relationship should be nurtured constantly during the outsourcing process.

Introduction

Despite the great interest shown in service outsourcing recently there is a shortage of in-depth longitudinal studies of the actual process by which firms outsource their services. The literature is mostly concerned with the make-or-buy decision, the benefits of outsourcing, and to some extent the risks or challenges associated with outsourcing. The actual process of outsourcing and how the challenges can be managed are not addressed as much.

This article addresses this gap by reporting on a leading European systems provider's global service outsourcing initiatives, that is initiatives where service processes that were previously done inside a firm are handed over to another business. More specifically, the focus of this paper is on business services, i.e. "services delivered by companies and bought by other companies" (Axelsson & Wynstra, 2002). The services focused in this article may also be categorised as "product services", i.e. "the set of all potential additional services a supplier can supplement his product offering with, in order to differentiate his offering relative to the competitors' as perceived by (potential) customers and distributors" (Frambach, Wels-Lips, & Gündlach, 1997). For sake of brevity, they will mostly only be called "services" in the paper. In some cases the term "basic services" is used, to contrast services such as repair and installation with more customer-

oriented services such as solutions and managing customers' operations (Oliva & Kallenberg, 2003). As a supplement, one partnering initiative is also described, that is an attempt to broadening the service offering by aligning with partners. The challenges of outsourcing services are described and lessons are gleaned regarding how these challenges can be managed during the outsourcing process.

This article is divided into three main parts. In the first part, three managerial challenges associated with the outsourcing of services are presented, focusing on organizational process issues, based on a literature review conducted during the research process. In the second, the methodology and four illustrative cases are presented. Finally, three lessons about how to handle the three challenges are presented, gleaned from the research, as well as some conclusions.

Three challenges associated with the process of outsourcing services

The following sections briefly describe literature relevant for the process of outsourcing services, divided into three challenges: (1) the internal change challenge, (2) the strategy challenge, and (3) the customer-relationship challenge.

The internal change challenge

Unless the outsourcing process is carefully carried out, internal resistance may arise based on a reluctance by the internal employees to externalise service activities that are perceived to be central to the way the company is about to compete and the brand of the firm (Ernst, 1996). Overt and covert resistance by managers and employees can be a serious obstacle to the change process, and can sabotage both the outsourcing process (Harper, 2001) and the adoption of service logic, consisting of the delivery of more customer-oriented services such as solutions (Mathieu, 2001). Although this resistance cannot be avoided altogether, there is a need for conscious change management in order to reduce the negative effects of internal resistance to a more constructive level. In other cases, especially at prosperous firm and during boom periods, outsourcing is taken too lightly by employees and managers who are searching for new interesting areas, with the basics of the firm being neglected (Bettis, Bradley, & Hamel, 1992).

Even though the ideal outsourcing process is often described as a linear one that should be well planned, have clear goals, etc. (Ellram & Eddis, 1996), in reality this rational approach is often unfeasible. Many industries are so volatile that it is almost impossible to forecast, with any degree of accuracy, more than a few months into the future. Under such conditions, responsiveness to changes in the market and technology are more important than formal planning procedures (Bettis et al., 1992). This is even more important in many service businesses, where knowledge of the customers' needs and strategies is often decentralised to service

employees in the field. Management must involve its employees in the change process if it is to succeed, e.g. its service employees and purchasers must have knowledge of the supplier's strategies. Management may have a broad overview of the business, but in rapidly changing environments and complex organisations, it must gather information from those who are better informed about the market. Management must also ensure that the employees have an overview of the strategic intent of the firm so that interactions with customers and suppliers are consistent with the overall ambition of the firm (Dunphy, 2000).

The strategy challenge

To compensate for the outsourcing of basic services to specialised service firms, and the downsizing of the firm, firms should introduce more customer-oriented and comprehensive services, and increase the value for the customer. There are at least two approaches to this, e.g. integrating forwards in the value chain and taking over customers' operations or by offering more integrated solutions (Miller, Hope, Eisenstat, & Galbraith, 2002). These new sorts of more complete services release customers from handling some of the complexity, so they can focus on their core business. According to many authors, introducing such services brings benefits to the supplier, e.g. expanded margins, stabilised revenues, differentiation from competitors, cross-selling opportunities (Miller et al., 2002). Another benefit for the supplier firms lies in organisations located downstream, or close to customers, such as the solution providers and suppliers managing customers' operations, typically having a greater understanding of the customers and their needs (Storer, Holman, & Pedersen, 2002). The introduction of such customer-oriented services is also attractive since it can retain, or increase, the power of the outsourcing firm and its possibilities of influencing the design of the delivery system (Light, 1986, Stern & Weitz, 1997)

However, these new services must be protected from competition. Each new service supply relationship, resulting from the outsourcing of a non-core basic service such as installation or support, must be analysed from the perspective of its effect on the new core services and the relationship with the customer. Consequently, the extent to which an outsourcing initiative may result in increased competition in the new core service areas, e.g. solutions and managing customers' operations, must be analysed. Furthermore, the outsourcing firm should ensure that it does not become overly dominated by its partners and suppliers, which is why some authors suggest that non-competing enterprises should preferably be selected (Quinn, Doorley, & Paquette, 1990).

If each outsourcing initiative is analysed in isolation from the overall strategy of the firm, and if the development of knowledge internally, and the risk of losing critical knowledge to the supplier, are not sufficiently taken into account, this may lead to a vicious circle for the outsourcing firm (Bettis et al., 1992, Quinn &

Hilmer, 1994). There is always a risk of opportunistic behaviour in business relationships (Das & Teng, 1999), which can mean, for example, the supplier integrating forwards in the value chain and becoming a competitor (McCutcheon & Stuart, 2000, Quinn et al., 1990) in the newer service areas where the outsourcing firm intends to compete.

The customer-relationship challenge

A third challenge has to do with the effect on the customer of outsourcing services, and the effect on the outsourcing process on the relationship with the customer. When a service process is outsourced, it is important to communicate the planned changes to the customers, or even to have the customer sanction them, since he may be affected by the change and his perception of the firm may also be affected (O'Farrell & Wood, 1999). Furthermore, the quality of many services not only depends upon the performance of the supplier but also on how well the customer interacts with the supplier (O'Farrell & Moffat, 1991), which is why the customer should always be involved in a service-outsourcing decision. Just how important this is will depend on the type of service being outsourced, where e.g. high contact services, such as installation and training, are more directly visible for the customer than low contact services, such as repair.

According to Payne and Frow (2000), the importance of this challenge is currently enhanced by trends such as deregulation and internationalisation of markets, which increases the competition and makes good relationships imperative. Furthermore, already in 1983 Berry contended that marketing in order to protect the customers base was becoming increasingly important in services, owing to the increased supply of similar services resulting from deregulation (Berry, 1983).

Methodology

This study was conducted as a three-year inductive case research project (Eisenhardt, 1989) dealing with the process of implementing service alliances and outsourcing services. Research into this process is scarce. This makes case studies an appropriate choice, since they suit questions that are not thoroughly researched (Leonard-Barton, 1990, McCutcheon & Meredith, 1993). Furthermore, case research is an appropriate approach for exploration in the early stages of research projects (McCutcheon et al., 1993), to achieve a relatively full understanding of a studied phenomenon (Voss, Tsikriktsis, & Frohlich, 2002), and to build theory (Eisenhardt, 1989).

The study was conducted within SysCo, a multinational systems provider with over 25,000 employees and its head office in Europe. SysCo sells relatively complex goods, typically worth between \$100,000 and \$5,000,000, to industrial customers all over the world to through its own sales force. The firm is market leader in its systems business, and is generally perceived as the most service-

oriented in its business field. The main business of SysCo still lies in selling systems, but SysCo is currently conducting a strategic transformation (Blumenthal & Haspeslagh, 1994) where services is expected to play an increasingly important role in the future. It is thus not yet as service-oriented as, for instance, IBM, and is still struggling to become more service-oriented and to introduce more customer-oriented services, e.g. solutions and managing its customers' operations. It is also increasingly relying on external suppliers and partners, both for its non-core activities such as delivering basic services to its customers, and for the emerging core activities such as delivering full-services. This makes it a feasible object for studying the process of outsourcing basic services and how it has affected the introduction of more customer-oriented services. The purpose with studying SysCo was thus driven by theoretical motives, as opposed to statistical ones (Glaser & Strauss, 1967, Yin, 1994). This paper focuses on alliance initiatives involving services such as repair, product support, product-oriented training, installation, systems integration, business solutions, full maintenance contracts, and managing customers' operations. The last three services are relatively new and are seen as strategically very important, and are also the goal of the servitisation (Vandermerwe & Rada, 1988) of SysCo.

The research was conducted between September 2000 and October 2003 and consists of 92 interviews with executives on different levels and performing different functions. They included executives at a divisional level, managers responsible for sourcing and partnering strategies, outsourcing project managers, as well as employees working in the service alliances. Respondents with experience from a broad range of services within the company were chosen. Thus, both product services prior to the purchase (pre-sale product services), product services directly relevant to the purchase (sale product services), and product services following the purchase decision (post sale product services) (Frambach et al., 1997) were covered by the research, making it more general. The respondents belong to several different types of service organizations, and were working with product services such as repair, product support, product-oriented training, installation, systems integration, business solutions, full maintenance contracts, and managing customers' operations. In total, the respondents reported on more than 20 service alliance initiatives, with some respondents reporting on several initiatives and others only one.

The interviews ranged from being formal, semi-structured interviews to unstructured, informal meetings that occurred spontaneously, e.g., next to the coffee machine, with eight being of a more formal nature, with the overwhelming majority being of the more formal nature. The formal, semi-structured interviews lasted between twenty minutes and two hours and were tape-recorded and transcribed in detail. To increase the internal validity of the findings, the author read several internal documents and participated in several presentation meetings and conferences for the employees of the studied firm, supplementary to the

interviews. This was made possible by the author being a part-time employee of SysCo during the period under study. Reflections from observations were recorded almost every day.

To make sense of the extensive data, and to draw conclusions about how the challenges, drawn from the literature, were managed, short case stories were written for the studied cases. Visual maps were created, to analyse and illustrate the gradual changes of SysCo's strategy, and how actors within SysCo gradually learnt by their experiences. The analysis was done both for the individual cases, and across the different cases, in an iterative cycle back and forth between data on different levels and between data and theory, aiming at searching for patterns in the observed processes and gleaning lessons related to the outsourcing of service. The whole research process was aided by N-Vivo, a computer-based text analysis program.

Case stories

The following four case stories are selected, among the over 20 cases studied, as illustrations of how SysCo managed the three outsourcing challenges described above. The first three cases are about the contracting of an external supplier to deliver basic services which were previously conducted in-house. The fourth case is about broadening the service offering by aligning with partners as a means of becoming more customer-oriented. Together, these cases illustrate the findings of the research, and also represent the three different categories of product services; pre-sale product services, sale product services, and post sale product services.

Outsourcing product training

In a pilot project conducted between 2001 and 2002, SysCo had an external training firm, based in the US, sell and deliver IT-related courses directly to its customers. The general purpose of the project was to learn about alliances, and to develop an alliance strategy. The specific purpose was to reach new markets, increase sales, and potentially also develop new services. The alliance project created a lot of frustration and conflict at SysCo, which hampered the progress of the project. One reason for the conflict was the different views held at SysCo as to whether or not it was wise to use external firms for these courses. Many employees saw the alliance as "foolish" and were of the opinion that IT training was instead an area where SysCo should further develop its own competence, thus internal support for the alliance at SysCo was very low. The project also caused frustration among some of the customers, who had not been informed about the changes in advance (reference to be added here after review). Some customers wondered whether or not SysCo had the necessary competence in-house, and this meant a risk of reduced credibility for SysCo. Some employees of SysCo thought the

alliance implied a risk of losing IT competence and, as a result, they would lose business to their partner.

The collaboration was terminated after the initial pilot project. Although the official reason for this was the general downturn in the economy and the rather unlucky market conditions, the correctness of the alliances is still being debated. Some employees saw the alliance as an opportunity to access competence in the selling and supplying of IT training. Others saw it as the outsourcing of an area that was too close to SysCo's core business, and an area that should be further developed internally.

Outsourcing Product installation

Another example is the installation of SysCo's products. Around 2000, this was completely outsourced to a global construction firm with its head office in Europe (henceforth called Global Service Corp), including the project management part. However, this turned out to be a disaster for several reasons. First of all, Global Service Corp conducted very few installation projects because local SysCo employees deemed it more expensive than locally sourced alternatives, preferring to cooperate with firms which they already had established bonds with. Secondly, many local customers (e.g. in France) wanted to have installation firms from their own domestic market, with their own language and culture. Thus, neither the local customers nor the local employees of SysCo were committed to using Global Service Corp. Finally, some installation providers were not satisfied with merely conducting installation services on behalf of SysCo, and were increasingly offering supplementary services directly to the customers of SysCo, including different solutions and even the management of customers' operations. In other words, they tried to climb up the value chain into more customer-oriented services just like SysCo. Building on their experiences from doing installation and other operational services for SysCo, as well as for competing System Providers of SysCo, they were able to offer a complete bundle of services and solutions to their customers, with some customers actually contracting them to manage their systems, for instance. Based on the negative experiences from outsourcing installation work, SysCo's strategy changed. Instead of outsourcing installation altogether, installation resources would be sourced locally and project management kept within SysCo. Strong suppliers such as Global Service Corp would not be used at all. Another measure was replacing managers of local SysCo offices who were not adapting to the strategy decided by SysCo Headquarters.

Outsourcing hardware repair

Repair was gradually being outsourced to external service firms, from around 1997, with the purpose of decreasing costs and facilitating a focus on other areas. When a new repair re-structuring and outsourcing project, that had been initiated

in 2003, had found a preferred supplier, based in Asia, which it wanted to contract for repair work in one or more of its regions, management suddenly stopped the selection process, and the second-choice supplier had to be contracted. The project had made their decision, based on the rigorous formal evaluation of several suppliers, but the managers of SysCo had gradually realised over the years that this specific supplier had become too strong. They were suddenly afraid that it would benefit too much from being awarded the repair contract. This specific supplier happened to be one of the suppliers that had also been contracted for installation services, for instance. The emerging awareness of this firm's ambitions to compete with SysCo led to a temporary halt in the outsourcing project, and the selection of a less dangerous supplier.

Partnering for full-services

In around 2002, SysCo started to discuss partnering, or horizontal alliances, internally and with firms that it believed could help it expand its service offering and cover a broader range of its customers' products. This, and an expansion into even more customer-oriented services such as solutions and taking over the customers' operations, was seen as critical to SysCo's service business when many of the basic services had been outsourced to specialised service firms for efficiency reasons. In spite of the terminology used by SysCo, "partnering", e.g. the partnering manager of SysCo said that SysCo should always face the customer in these alliances. Otherwise, he said, there would not be a deal with the supplier. The customer relationship was deemed too important to leave to, or share with, another firm.

However, this strategy was gradually relaxed as SysCo realised that both the potential alliance partners and the customers were of different opinions, and that there were also technological reasons for not always fronting the customer. Thus, the initially very firm statement about always fronting the customer in horizontal alliances was replaced by a pragmatic view where the preferred structure was dependent on each specific case, e.g. the customers' wishes and the partners' competence. Gradually, a more detailed partnering strategy was developed where the structural question regarding who would be closest to the customer was formulated for each of SysCo's different service areas, e.g. Systems Integration, Installation, and After-Sales Services. For example, where the external partner firm had expertise in one of the customer's applications, e.g. Business Management Systems like SAP, they realised that it would not typically be viable to have SysCo fronting the customer. SysCo did not have core competence in this area, and neither did it have any history of delivering and supporting applications such as SAP for its customers.

Apart from the formulation of a partnering and sourcing strategy, or rather guidelines for the make-or-buy decision for the different service areas, the prime

contractor role was also developed. The Manager of SysCo’s service organisation explained:

”We are very clear in that we will always be the prime contractor and retain the responsibility for services for products, from transmission up to the service-layer. Over and above that, we can let other firms handle things”

A new organisational unit was also set up for coordinating partnering and sourcing issues at headquarters.

Lessons gleaned from the case study

Table I summarises how SysCo gradually learned from its experiences between 1997 and 2003 and how it re-shaped its partnering and sourcing strategy.

Table I. The evolution of SysCo’s view of outsourcing and partnering

	1997	1998	1999	2000	2001	2002	2003
Strategy Challenge	“Outsource basic services to global world-class suppliers”		→	“Outsource basic services to non-competing suppliers of low cost and sufficient quality”		→	“We depend on basic services and must not outsource them too quickly”
	“Installation is not our core business and will be outsourced completely”				→	“Operational parts of installation will be outsourced, but project management will remain internal”	
Customer-Relationship Challenge	“We must always face the customer”		→	“Sometimes we face the customer, sometimes not”		→	“For Product X and Service Y, we must face the customer, but not for Product X and Service Z..., because...”
							→
Internal Change Challenge	“Implementation is not an issue for us, we just need to define our strategy correctly and the implementation will follow”				→	“How can we learn from our experiences?”	
					→	“Under what conditions do internal conflicts prove fruitful?”	
					→	“We have never been able to identify changes. And my conclusion from this is that we need to guard against unforeseeable events and to be flexible, rather than to plan”	

The table is included here as an illustration of how difficult it can be to set a detailed sourcing strategy and implement it in a linear fashion. The story of SysCo should not be seen as a success story for firms to copy, and neither should their

sourcing strategy during 2003 be seen as “best practice”. As a matter of fact, among many SysCo employees, late in 2003, there was still some uncertainty regarding the viability of the partnering and sourcing strategy for services. There were also concerns about how the change processes were being managed and how they were learning from experience. However, a number of lessons about how to handle the three challenges associated with the outsourcing of services can be learned from this case study of SysCo’s outsourcing experiences. Three lessons of more general importance drawn from the case study will be presented. Data from the case study is used to illustrate the lessons, and reference is made to the literature in order to help explain and develop the findings.

Lesson one: The need for interactive and reflective change management

The experiences of SysCo, from the cases summarised above, for instance, illustrate the difficulty of planning and implementing sourcing strategies for services. The initial sourcing strategy showed itself to be difficult to implement, due to resistance by SysCo’s employees, and its suppliers and customers. There were two basic and interrelated reasons for this difficulty.

First, the strategy was not very flexible but rather rigid. For example, the strategy of always facing the customer showed itself to be unrealistic and was subsequently changed. Understanding of this was gradually developed via interaction with suppliers, customers, and internal employees through negotiations and confrontation with the initial strategy. The strategy of outsourcing installation altogether also showed itself to not work, following attempts to implement it and failure, and was replaced by a strategy where only the operational parts were outsourced and project management was kept at SysCo. Second, the strategy had not become established among the employees, customers and suppliers, and implementing it was thus difficult. However, because of the turbulent market conditions, it would probably have been impossible to set a definite strategy at the outset. Thus, the first lesson to be learned is that change management is important and should be iterative in character and involve interaction between the employees, customers, and suppliers, as well as the development of an overall strategy by top management. Formal planning from the top is often unfeasible because of the need to take in local knowledge and local strategies. Neither is a full-fledged bottom-up approach to change because of the need to coordinate several outsourcing and alliance efforts at the same time (compare, for instance, Dunphy (2000)). Instead, flexibility is necessary since cooperative relationships seldom succeed as planned (Niederkofler, 1991). In the case of SysCo, the approach to change was gradually changing from the top-down formal planning mode to an approach whereby the local knowledge of various organisations within its organisation was appreciated.

Thus, the lesson is that there is a need to involve the organisation in the change process, and also to explain why a simple top-down approach is not feasible. Just

waiting for things to emerge from the lower, and less central, levels of the organisation may cause irritation among employees expecting to be led by their managers.

Furthermore, the distinction between core/non-core areas is not as simple as the conventional literature sometimes suggests, and the experiences from SysCo clearly support a view where basic services that may look feasible for outsourcing at first glance, should be constantly assessed against the other services and the other outsourcing and alliance initiatives. In other words, a more dynamic and reflective approach to outsourcing services is needed, where rigid definitions of core/non-core service areas should be avoided (Leonard-Barton, 1992), and the sourcing strategy is constantly being questioned and assessed against the overall service strategy of the firm and the suppliers. It is also important to change the sourcing strategy in incremental steps, and to be prepared to return to the old strategy if necessary. Drastic changes towards completely new and fancy service areas and the outsourcing of old and more basic services may be tempting for innovative firms, but it may be safer to keep these old services in-house, at least for a while, because they may be more important than first thought. The manager of SysCo's service organisation explained:

“Only if our basic services are working will we be able to talk about anything else. You cannot go to the customer otherwise. This is what I try to teach my employees”

SysCo was so focused on newer services and solutions, that it did not see the value of its more basic services such as after-sales support. Suddenly, the whole organisation was talking about, and developing, new solutions, and the management of basic services was suffering.

Lesson two: Coordinating different alliance initiatives

The degree of centralisation or decentralisation of organisational change has long been debated and business practice seems to be constantly changing from one mode to the other. From this case study, it can be concluded that there is a need for central coordination of the different alliance and outsourcing efforts taking place at one firm. Otherwise, the different initiatives may impede each other. Specifically, the outsourcing of basic services may impede the introduction of more customer-oriented services, and the effects of outsourcing basic services on the more complete and customer-oriented services must be taken into account. Each separate outsourcing decision may be sound on its own merits, but together several of them may lead to the decline of the outsourcing firm. The economies of scale will successively move towards the supplier, and overheads must be allocated to a diminishing operational business (Bettis et al., 1992). Examples of this were found when a customer contracted SysCo's installation and repair supplier to manage its operations in some markets. This supplier was becoming very strong at providing various basic services, not only for SysCo but also for some of its competitors, and

was gradually being seen by some customers as the preferred choice for more advanced services, too, and for services such as managing its operations. One may ask whether SysCo could have foreseen this at the outset, and the answer would probably be no. However, if all alliance and outsourcing efforts had been better coordinated, the strength of this specific supplier (there were a few more of this kind) would not have come as such a surprise, and the outsourcing project would perhaps have taken another route and not been stopped once this particular supplier had been evaluated and selected as the preferred choice for repair work. Thus, the outsourcing firm should be careful about contracting suppliers of basic services that are too strong and ambitious, keep track of their strategies and be adaptive to changes in their strategy and behaviour. Although the main focus should be the development of the internal core competence, potential competitors should not be nurtured uncritically with small items of knowledge which together, in the long run, can create competitive advantage. An overview of all suppliers and all outsourcing and partnering initiatives would also facilitate sound sourcing decisions and the development of an appropriate service strategy. Thus, the lesson learned is that there is a need to coordinate different outsourcing and partnering initiatives and to map them against the current service and customer relationship strategy. Doing this facilitates the formulation of both service and sourcing strategies, and not least the identification of competencies to be developed in order to stay ahead of the competition. A dedicated alliance function not only facilitates internal coordination, but can also, for example, function as a focal point for learning from prior alliance initiatives and for sharing of know-how related to processes associated with alliances (Dyer, Kale, & Singh, 2001).

At the end of the study, SysCo was starting to coordinate its alliance initiatives. One Partner Manager explained:

“We have, for instance, a Strategic Partner Board where decisions are taken and a Partner Team where the operational issues are dealt with, and where processes are coordinated”

It is not only service outsourcing initiatives that should be coordinated. Outsourcing of other areas than the services delivered to customers should also be carefully considered, e.g. the outsourcing of R&D and manufacturing. The reason for this is that such outsourcing may assist supplier firms in conducting services that require knowledge of the technology and the products, thus decreasing the competitive advantage of the outsourcing firm.

Lesson three: Nurturing the customer relationship

Unless the intention of the outsourcing firm is to turn away from services altogether, and to focus on other areas, such as the development and mass-production of simple goods, it is very important to nurture the relationship with the customer, independent of the structure of the delivery chain in use, e.g. simple

supply chain, management through intermediaries, supply partnership (Johnston & Clark, 2001). Nurturing the relationships with the customers is becoming increasingly important as markets are maturing and becoming oversupplied (Grönroos, 2000). In the case of SysCo, this was not very well managed initially, which the following excerpt from the outsourcing of product training illustrates:

“The customers had already shown some scepticism as regards having an external partner provide IT training, which they perceived to be a cornerstone of the future business of SysCo. They wondered whether or not SysCo had the competence in-house, something that reduced the credibility of the company. There was a risk that the customers would eventually decide to ally themselves with the new training partner”

However, within the central marketing functions of SysCo, the importance of good customer relationships and conveying the correct message to the customer was becoming well-understood. In 2003, one service marketing manager explained how the rhetoric was changing:

“We have changed the rhetoric related to our service portfolio, and turned from focusing on each separate service to talking about the sum of our capabilities, represented by our service portfolio. Instead of saying, for instance “we can do systems design” and “we can do this and that” we now say “SysCo’s organisation has the capability to...”, “we are leading in...”, “we have done this several times before”, or “from experience, we have learnt that...”. We have started to focus communication on our customers’ issues and how our capabilities can help them to solve their problems”

To summarise, the lesson that can be learned is that constantly nurturing good customer relationships is of the utmost importance to service-oriented firms outsourcing services. In today’s competitive environment, this can be the key to retaining customer confidence, and a sustainable business. For firms really interested in becoming more service and customer-oriented, the establishment of an ongoing customer relationship and a reputation as a service provider are critical, and one of the biggest challenges (Oliva et al., 2003). One of the five key success factors of SysCo was labelled “Focus on customer business” and was targeting the same issue. The following excerpt from SysCo’s Business Plan explains:

“It’s essential for a services business to understand its customers’ business, including its customer’s customers, i.e. consumers and enterprises/governments, as well as its external environment (market development, competition, legal issues etc). Upon understanding this, we will be able to create, and explain, substantial business value using our portfolio for our customers in the areas of Product Evolution, Business Growth and Efficiency”

More customer-oriented services, such as business solutions and managing customers’ operations (Miller et al., 2002), are closely related to nurturing the relationship with the customer, although a relationship requires much more than just developing and offering new service concepts to one’s customers. For instance, it is also about attitude and keeping promises (further details of developing customer relationships in services can be found in, for instance, Grönroos (2000)).

Summary and conclusions

In this article, three challenges associated with outsourcing services are described on the basis of a literature review; the strategy challenge, the internal change challenge, and the customer relationship challenge. Thus, the article provides an overview of the different aspects of outsourcing services which can often be problematic, and which should all be considered when outsourcing services. Three lessons with regard to how these challenges can be managed are drawn from a longitudinal study of a leading systems provider, see Table II.

Table II. Summary of lessons relating to the process of outsourcing services

Lesson one	Change management should be interactive and reflective in character, involving interaction between the employees, customers, and suppliers, as well as the development of an overall strategy by top management.
Lesson two	There is a need to coordinate different outsourcing and partnering initiatives and to map them against the current service strategy.
Lesson three	Good customer relationships must be constantly nurtured during the outsourcing process and are of the utmost importance when service-oriented firms outsource services.

The first lesson entails that, instead of employing a pure top-down or bottom-up approach to change, firms that are outsourcing services should employ a more interactive and reflective process, involving customers, suppliers and employees in the change process. The second and third lessons are more specific, and entail that the relationship with the customer should be assessed continuously, or at least regularly, during the outsourcing process, as well as all the different alliance and outsourcing initiatives taking place within the firm. The three lessons agree with the more general suggestions for change management made by, for instance, Dunphy (2000), and with the process models for alliances suggested by, for instance, Ring and van De Ven (1994). The basic idea is that there is a need for iteration between the subsequent stages of the outsourcing process, rather than trying use a linear sequence for the outsourcing of services. In other words, the mode of change is rather constructive than prescriptive (Van de Ven & Poole, 1995). The iterative and reflective approach should be supplemented by a recurring assessment stage where the relationship with the customer is assessed and nurtured and the different alliances are assessed and coordinated.

This study is based on data taken from several alliance projects, and many different respondents. However, since all the data is taken from the same single firm, it is difficult to make any empirical generalisations beyond this specific firm. Although there are reasons to believe that the results of this exploratory single case study are also valid for other firms outsourcing services, and for that matter also for firms outsourcing other areas than basic services such as R&D and manufacturing, the results should be seen as the basis for further research. The

generalization of the results of this study should be tested by conducting multiple case studies. Generalizability may also be achieved by focusing on the outsourcing of other areas such as R&D.

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