THE PERFORMANCE IMPLICATIONS OF OUTSOURCING CUSTOMER SUPPORT TO SERVICE PROVIDERS IN EMERGING VERSUS ESTABLISHED ECONOMIES

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Abstract

Recent discussions in the business press query the contribution of customer-support outsourcing to firm performance. Despite the controversy surrounding its performance implications, customer-support outsourcing is still on the rise, especially to emerging markets. Against this backdrop, we study under which conditions customer-support outsourcing to providers from emerging versus established economies is more versus less successful. Our performance measure is the stock-market reaction around the outsourcing announcement date. While the stock market reacts, on average, more favorably when customer-support is outsourced to providers located in emerging markets as opposed to established economies, approximately 50% of the outsourcing firms in our sample experience negative abnormal returns. We find that the shareholder-value implications of customer-support outsourcing to emerging versus established economies are contingent on the nature of the customer support that is being outsourced and on the nature of the outsourcing firm. Customer-support outsourcing to emerging markets is less beneficial for services that are characterized by personal customer contact and high knowledge embeddedness than for customer-support services that involve impersonal customer contact and are low on knowledge embeddedness. Firms higher in marketing resource intensity and larger firms benefit more from outsourcing customer-support services to emerging markets than firms lower in marketing resource intensity and smaller firms.

Key words: outsourcing, customer support, offshore, emerging markets, event study
1. Introduction

Increasingly, firms are outsourcing customer support. A research report by IDC (2011) reveals that the worldwide outsourced customer-care services market will grow at a compound annual growth rate of 5% to reach $66.2 billion in 2015. While the large majority of customer-support outsourcing is still done locally (Mudambi & Venzin, 2010), firms in established economies are increasingly considering emerging markets as attractive outsourcing locations (Javalgi, Dixit, & Scherer, 2009). Recent examples include Barclays, a global financial services provider that outsources call-center jobs to India, and T-Mobile UK that outsources part of its customer care to the Philippines.

Although customer-support outsourcing is all the rage, many outsourcing arrangements are not successful. Anecdotal accounts in the business press suggest that organizations can achieve cost savings of 25 to 30 percent through customer-support outsourcing (Gartner, 2005), especially when outsourcing to emerging markets with lower labor costs (Bharadwaj & Roggeveen, 2008). However, blinded by quick-fix cost savings, many firms forget that there can also be “hidden costs” in outsourcing services (Ren & Zhou, 2008, p. 370). Deloitte Consulting (2005, p. 21) states:

“50 percent of outsourcing in the near future will be successful, with the failures stemming from clients that don’t know what they are doing, don’t understand outsourcing, or don’t understand their own business.”

Against this backdrop, the goal of this research is to understand what distinguishes more versus less successful customer-support outsourcing practices.

We contribute to the extant literature in three ways. First, we study the financial performance implications of outsourcing customer support. Recent studies by Thelen and colleagues have focused on the negative consequences of customer-support outsourcing for consumers’ service
quality perceptions (Thelen, Honeycutt, & Murphy, 2010), sentiments (Thelen, Yoo, & Magnini, 2011), and subsequent (adverse) behaviors toward the outsourcing firm (Thelen & Shapiro, 2012). In contrast, when executives are asked about the financial impact of their outsourcing initiatives, they often respond that it cannot be readily quantified (Bryce & Useem, 1998; Jiang, Frazier, & Prater, 2006). To address this gap, our performance measure is the stock-market reaction around the outsourcing announcement dates.

Second, we study the financial performance implications of customer-support outsourcing to service providers from emerging versus established economies. Although a growing body of literature has examined customer-support outsourcing, most of this research has not distinguished between service providers from established versus emerging markets (e.g., Ren & Zhou, 2008; Thelen, Yoo, & Magnini, 2011). The recent spread in offshore outsourcing to emerging markets makes it paramount for marketing scholars to shift their attention. As such, we address the call for more research on marketing in emerging markets (Burgess & Steenkamp, 2013; Dekimpe, 2009).

Third, there has been limited research to date that examines how the performance implications of outsourcing customer support to emerging versus established economies may differ across firms. We examine whether these performance implications depend on (1) the nature of the customer support that is being outsourced and (2) the nature of the firm that is outsourcing the customer-support activities. Specifically, emerging markets present significant departures from established economies in terms of culture as well as regulation (Burgess & Steenkamp, 2006), which may lead to communication-style problems and enforcement problems, respectively. We argue that the extent to which outsourced services are prone to communication-style problems depends on the type of customer support that is being outsourced. Further, the extent to which firms are vulnerable to regulatory problems depends on the nature of the firm that
is outsourcing. By comparing the financial performance implications of customer-support outsourcing to providers from emerging versus established economies, and by identifying the factors that distinguish more versus less successful outsourcing practices, we hope to assist executives in avoiding future costly mistakes.

The remainder of this study is organized as follows. We first review the literature on the performance implications of customer-support outsourcing and outline our conceptual framework. Then, we introduce the hypotheses, describe the methodology, and present the results. In the final section, we discuss the study’s theoretical and managerial implications and we outline avenues for future research.

2. Theory

2.1. Literature review

Marketing strategy research has long emphasized the importance of studying the performance consequences of customer-support outsourcing. This has fueled a significant, multifaceted literature (see Table 1 for an overview). A first stream of literature has analyzed the performance implications of customer-support outsourcing for the outsourcing firm analytically. Hasija, Pinker, and Shumsky (2008) and Ren and Zhou (2008) examine how different contracts enable the outsourcing firm to increase its profits. Milner and Olsen (2008) study how alternate contracts affect service quality in the form of minimal customer delays. None of these studies consider how the performance consequences of customer-support outsourcing may differ across providers from emerging versus established economies.

[Insert Table 1 about here]

In addition to the game-theoretical literature, a number of studies have tested the performance
implications of customer-support outsourcing *empirically*. These studies can be described along two dimensions: (1) the nature of the performance measure used, and (2) the geographic scope of the study.

Most studies have examined the impact of customer-support outsourcing on consumer perceptions, sentiments, and behavioral intentions. Thelen, Honeycutt, and Murphy (2010) show that U.S. citizens’ perceptions of service quality vary considerably by the outsourcing provider’s country, with providers from established economies (e.g., Canada, Ireland) scoring much higher on perceived service quality than providers from emerging markets (e.g., China, India, Philippines). Roggeveen, Bharadwaj, and Hoyer’s (2007) experiments among U.S. MBA students indicate that locating a call center in India or the Philippines as opposed to England impacts anticipated satisfaction negatively, but only for outsourcing firms that are unknown (as opposed to reputable). In a similar vein, Bharadwaj and Roggeveen (2008) find that U.S. customers experience greater satisfaction with a call center representative’s communication skills and problem solving ability when a call center is located domestically rather than in India.

Other studies corroborate the finding that consumers harbor negative feelings toward services that are outsourced offshore (i.e. to a country other than the outsourcing firm’s domestic market). They find that U.S. consumers’ negative sentiments towards offshore outsourcing decrease their satisfaction with the service received (Sharma, 2012; Sharma, Mathur, & Dhawan, 2009) as well as their attitude and commitment towards the offshoring firm (Thelen, Yoo, & Magnini, 2011). Consumers’ negative sentiments towards offshoring further affect their behavioral intentions, ranging from decreased positive word-of-mouth intentions and increased intentions to boycott the outsourcing firm (Thelen, Yoo, & Magnini, 2011) to requests for domestic service providers and intentions to stop doing business with the firm (Thelen & Shapiro, 2012). These studies, however, do not compare providers from emerging economies with providers from established
economies. For example, Whitaker, Krishnan, and Fornell (2008) contrast domestic outsourcing to offshoring. They show that customer-support outsourcing decreases customer satisfaction in both cases, but they do not consider potential differences between providers from emerging markets and (nondomestic) providers from established economies.

We were able to locate only one study that addresses the financial performance consequences of customer-support outsourcing. Kalaignanam, Kushwaha, Steenkamp, and Tuli (2013) study the effect on shareholder value of outsourcing two types of Customer Relationship Management (CRM) processes – presales CRM (i.e. lead generation and order fulfillment) and postsales CRM (i.e. customer support). Although Kalaignanam et al. (2013) do not explicitly compare the performance consequences of outsourcing to providers from emerging versus established markets, they do study the role of cultural distance between the outsourcing firm and the outsourcing provider. They find that outsourcing customer support (i.e. postsales CRM) to culturally distant outsourcing providers has no adverse effect on shareholder value.²

In sum, while firms increasingly outsource to service providers located in emerging markets, research that explicitly compares outsourcing to providers from emerging versus established markets remains scarce (Mudambi & Venzin, 2010). In addition, even though firms primarily pursue cost savings when outsourcing customer support to emerging markets (a supply-side advantage), the scant empirical academic research has almost exclusively focused on the negative consumer appraisals that may result from customer-support outsourcing (a demand-side disadvantage). While it is of interest to quantify the impact on various performance indicators

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² Kalaignanam et al.’s (2013) study differs from our study in two important ways. First, whereas cultural distance is indeed an important dimension along which emerging markets and established economies differ, it is not the only one. As we will argue below, emerging markets are also markedly different from established economies in terms of institutional systems, which may create regulatory problems (Burgees & Steenkamp, 2006). Second, whereas Kalaignanam et al. (2013) analyze the performance consequences of outsourcing postsales CRM to culturally distant countries, we argue for a contingency perspective and hypothesize that the performance consequences of outsourcing customer support to emerging markets (rather than established economies) are contingent on the nature of the outsourced customer-support service and the nature of the outsourcing firm.
separately, it is first and foremost important to understand the overall net performance impact of outsourcing to emerging versus established economies. Apart from quantifying this net effect, the current study develops a contingency framework for identifying the boundary conditions of the relationship between customer-support outsourcing to emerging versus established economies and the outsourcing firm’s performance.

2.2. Conceptual framework

Albeit prior studies have used slightly different approaches to distinguish emerging markets from established economies, they have in common that the country’s welfare per capita is the key distinguishing characteristic. We follow Burgess and Steenkamp (2006, p. 339) in adopting the World Bank’s definition of emerging markets as “countries in which PPP-adjusted GDP per capita, converted to U.S. dollar and smoothed for three-year currency fluctuations, is equal to or less than the highest ranked country classified as ‘middle income’ by the World Bank.”

Customer-support outsourcing to emerging markets can have both positive and negative effects on the performance of the outsourcing firm. On the positive side, firms may benefit from cost savings by taking advantage of lower labor costs offered by the outsourcing provider. On the negative side, the markedly different cultural and institutional systems of emerging markets (Burgess & Steenkamp, 2006) may create communication-style problems and regulatory problems, respectively. Communication-style problems may occur not only between the outsourcing provider and the outsourcing firm’s customers (e.g., Stringfellow, Teagarden, & Nie, 2008; Thelen, Honeycutt, & Murphy, 2010) but also between the outsourcing provider and the outsourcing firm’s employees. These communication difficulties make it more challenging for the outsourcing firm to coordinate activities with outsourcing providers from emerging markets (cf. Simonin, 1999), thereby increasing the outsourcing firm’s costs and/or concerns about its
customer service standards and quality.

In addition, regulatory problems may occur because emerging markets are characterized by less effective regulatory systems and contract-enforcement mechanisms, while established economies are marked by more formal and transparent rules and restrictions (Khanna, Palepu, & Sinha, 2005). When firms outsource to countries with a strong regulative system, they can expect their outsourcing providers to act upon the normative influence of regulation (Edelman & Suchman, 1997) to avoid penalties for noncompliance (Hoffman, 1999). This is a dangerous assumption to make when outsourcing to emerging markets. Due to emerging economies’ poor regulative system, outsourcing firms are less confident that their outsourcing providers will adhere to local laws and contractual agreements (Khanna, Palepu, & Sinha, 2005). This may further increase the outsourcing firm’s costs and/or may negatively affect service quality.

The communication-style and regulatory challenges of customer-support outsourcing are characteristic for outsourcing to emerging markets but less so for outsourcing to established economies. Hence, we expect that the performance implications of outsourcing customer support to emerging versus established economies depend on (1) the extent to which the outsourced service is prone to communication difficulties, and (2) the extent to which the outsourcing firm is vulnerable to regulatory threats. If the outsourced services are less prone to communication-style problems and the firm’s vulnerability to regulatory problems is lower, the performance implications of outsourcing customer support to emerging economies, compared to outsourcing to established economies, will be more favorable. We argue that the extent to which outsourced services are prone to communication-style problems is a function of the nature of the outsourced customer-support service, while the extent to which firms are vulnerable to regulatory challenges depends on the nature of the outsourcing firm. Figure 1 summarizes our conceptual framework.

[Insert Figure 1 about here]
2.3. The nature of the outsourced customer-support service

We argue that the proneness of customer-support services to communication-style problems varies along two key dimensions (Youngdahl & Ramaswamy, 2008): (1) the nature of the contact between the service employee and the outsourcing firm’s customers (impersonal versus personal), and (2) the level of knowledge embeddedness of the outsourced customer-support activity (simple services versus complex solutions). Whereas the former dimension captures potential communication-style problems between the outsourcing provider and the outsourcing firm’s customers, the latter dimension reflects possible communication-style problems between the outsourcing provider and the outsourcing firm’s employees.

2.3.1. Personal customer contact

Customer contact pertains to employee-customer interaction during the delivery of customer support (Hartline & Ferrell, 1996), and can be personal or impersonal. Customer contact is personal when the production and consumption of the service occur simultaneously through a channel that accommodates direct, real-time interaction between the service employee and the customer. For example, call centers involve personal contact between service employees and customers. In contrast, e-mail support services do not involve direct, real-time interaction and are therefore impersonal.

Communication is contextually bound (Newburry & Yakova, 2006). The low cultural proximity between firms from established economies and firms from emerging markets may create a barrier to interaction, a “friction-related invisible cost of communicating” (Stringfellow, Teagarden, & Nie, 2008, p. 170). For example, directness in speech is prized in the U.S. but may be perceived as rudeness in China. In a similar vein, “yes” in India actually means “I’ve heard you” whereas U.S. customers associate “yes” with making a commitment, which can cause
problems of overpromising (Metters, 2008). Hence, when firms from established economies outsource their customer support to providers from culturally dissimilar emerging markets, effective customer support delivery is more at risk than when they outsource to providers from culturally more proximate established economies.

Whereas communication skills are important in delivering any type of customer support, they are vital when the service requires personal customer contact (Thelen, Yoo, & Magnini, 2011). We argue that outsourcing to emerging markets is relatively more prone to communication-style problems when customer contact is personal rather than impersonal in nature. The differences between the customers’ and the provider’s communication styles may be more difficult to get around when the service involves personal (direct, real-time) interaction than when it involves impersonal (indirect) interaction, because personal interaction leaves less room for inspection or revision (Patterson, Cowley, & Prasongsukarn, 2006). In contrast, asynchronous, non-face-to-face communication that relies on written messages is easier to code in a communication style that fits customers from established economies. We therefore hypothesize:

H1 The effect on shareholder value of outsourcing customer support to emerging markets (rather than established economies) is lower for customer-support activities that are personal in nature than for customer-support activities that are impersonal in nature.

2.3.2. Knowledge embeddedness

Outsourced customer-support services also have different levels of knowledge embeddedness. Knowledge embeddedness is defined as the extent to which service providers need specialized skills and expert knowledge to deliver the customer support according to specifications (Youngdahl & Ramaswamy, 2008). Low knowledge embeddedness characterizes simple services (e.g., reservations), whereas high knowledge embeddedness characterizes complex solutions.
(e.g., technical customer support). The skills and knowledge required for customer-support services characterized by low knowledge embeddedness are relatively easy for the outsourcing firm to transfer to its provider without substantial misunderstandings (Liu, Feils, & Scholnick, 2011; Madhavan & Grover, 1998). On the other hand, the specialized skills and expert knowledge associated with complex solutions are notoriously difficult to transfer and require close interaction (Madhavan & Grover, 1998). Aron and Singh (2005) point out that when outsourcing providers require a great deal of domain experience and deep product knowledge to execute task processes, “they are unlikely to get those processes right for a long time” (p. 138).

We argue that transferring embedded knowledge is even more difficult when outsourcing customer support to emerging markets as compared to established economies. The communication-style problems that we discussed earlier in the context of employee-customer interactions may also arise between the outsourcing firm’s employees and the outsourcing provider’s employees (Stringfellow, Teagarden, & Nie, 2008, p. 173), rendering any knowledge transfer attempt to a provider from an emerging market less effective than to a provider from an established economy. These knowledge-transfer problems are further exacerbated when the provider’s trainees in turn train local employees underneath them. This is common practice when outsourcing to emerging markets, as Web.com, a medium-sized U.S.-based web hosting and Internet services provider, discovered when outsourcing customer service to Bangalore, India:

“Another negative side effect that we experienced was what we’ve now coined a ‘replicate fade,’ meaning our service and best practices became a copy of a copy of a copy. The highly qualified and skilled people we trained for three months at our corporate headquarters were training people underneath them who were then training others, and so on. Because the effectiveness of our training program was being diluted, our customers were not receiving the stellar customer support that is the cornerstone of our business” (TMCnet.com, 2004).

We therefore hypothesize:

H2 The effect on shareholder value of outsourcing customer support to emerging markets
(rather than established economies) is lower for customer-support activities with high knowledge embeddedness than for customer-support activities with low knowledge embeddedness.

2.4. The nature of the firm

The performance implications of outsourcing customer support to emerging versus established economies not only depend on the nature of the outsourced customer-support service, but also on the nature of the outsourcing firm. Some firms are better able than others to cope with regulatory problems that are prevalent in emerging markets. Below, we argue that an outsourcing firm’s vulnerability to regulatory problems in emerging markets is contingent on the outsourcing firm’s marketing resource intensity and on its size.

2.4.1. Marketing resource intensity

Regulative institutions have an essential role in supporting the effective functioning of the market mechanism, such that firms and individuals can engage in transactions without incurring undue costs or risks (Meyer, Estrin, Bhaumik, & Peng, 2009). Whereas regulative institutions are strong in established economies, they tend to be weak in emerging markets (McMillan, 2008). Thus, when firms outsource their customer support to emerging markets, they are faced with less effective contract-enforcement mechanisms (Liu, Feils, & Scholnick, 2011). Therefore, they can be less confident that their outsourcing providers will adhere to contractual agreements (Khanna, Palepu, & Sinha, 2005).

Wathne and Heide (2000) have argued that superior partner selection may help firms address contract-enforcement problems. However, whereas strong institutions come with a transparent disclosure environment, thereby providing firms with easy access to information about potential
business partners and reducing information asymmetries, the weak institutional arrangements found in emerging markets typically amplify information asymmetries (Meyer et al., 2009). As a result, outsourcing firms need to spend more resources searching for partner-related information in emerging markets (Tong, Reuer, & Peng, 2008). Since there is no easy way of evaluating the quality of the partner beforehand, outsourcing firms may face an adverse selection problem.

Marketing resource intensity is the extent to which a firm invests in marketing activities (Mizik & Jacobson, 2007), such as advertising, branding, and customer service (Dinner, Mizik, & Lehmann, 2009). In the spirit of Day (1994), we argue that firms higher on marketing resource intensity, have a stronger external focus, which enables them to better scan the environment. Their scanning ability allows them to better validate potential outsourcing providers’ claims and select a good partner. As a consequence, their cost of coping with regulatory challenges is reduced. We hypothesize:

H3  Firms with higher marketing resource intensity create more shareholder value by outsourcing customer support to emerging markets (rather than established economies) than firms with lower marketing resource intensity.

2.4.2. Firm size

The size of a firm is indicative of its financial resources (Contractor, Kumar, & Kundu, 2007; Cui & Lui, 2005), with larger firms having more financial resources than smaller firms (Johnson & Tellis, 2008). Hitt et al. (2000) find that emerging-market firms attribute more importance to their alliance partners’ financial resources than firms in established economies. Given their attractiveness as exchange partners in emerging markets, larger outsourcing firms can therefore more credibly threaten to switch providers in case their current provider attempts to exploit the weak regulatory environment. As such, we expect that outsourcing providers will more likely
adhere to contractual agreements if they are dealing with larger outsourcing firms. This will positively impact service quality, thereby increasing the outsourcing firm’s performance.

Moreover, larger outsourcing firms have more contact and clout in emerging markets than smaller firms (Acs, Morck, Shaver, & Yeung, 1997) and often receive preferential treatment from the local government (Cui & Lui, 2005; Schiffer & Weder, 2001), because they offer social benefits such as employment creation (Child & Tsai, 2005). Their stronger ties with local governments in emerging markets provide outsourcing firms with better insight into local market conditions (Radjou & Prabhu, 2012), which may increase their ability to select a good exchange partner. In sum, larger firms can credibly threaten to switch providers and may be able to select better partners through their stronger ties with local governments, both of which increase their ability to deal with the regulative challenges inherent to outsourcing to emerging markets. We therefore hypothesize:

H4 Larger firms create more shareholder value by outsourcing customer support to emerging markets (rather than established economies) than smaller firms.

3. Methodology

3.1. Evaluating the performance implications of customer-support outsourcing

Evaluating the performance implications of customer-support outsourcing is not straightforward. Commonly used performance measures such as return on assets, sales, or customer satisfaction may be less appropriate indicators to capture the performance of customer-support outsourcing, for the following reasons.

First, performance is a multifaceted construct and examining any single performance facet in isolation – such as sales or customer satisfaction – is not likely to produce an adequate overall
assessment (Kumar, Stern, & Achrol, 1992). This is particularly important in an outsourcing context, since the performance effects of outsourcing decisions can be wide-ranging and call for consideration of both demand-side and supply-side effects (Kalaignanam & Varadarajan, 2012). On the demand side, customer-support outsourcing may affect, amongst others, customer satisfaction (Bharadwaj & Roggeveen, 2008), customer referrals (Thelen, Yoo, & Magnini, 2011), and thereby customer sales. Supply-side effects refer to the impact of customer-support outsourcing on a firm’s cost structure (Kalaignanam & Varadarajan, 2012). Customer-support outsourcing may not only lead to cost advantages through economies of scale and lower labor costs (Stringfellow, Teagarden, & Nie, 2008), but also to more “hidden costs,” such as the costs of qualifying a good outsourcing provider, the costs of training the provider, and the costs of managing the provider to ensure that he lives up to his agreements (Business Week, 2003).

Second, traditional financial accounting measures such as return on assets have a historical orientation as opposed to a forward-looking focus. Yet, the financial outcomes of customer-support outsourcing decisions can be substantially delayed. Indeed, “companies that value short-term profit at the expense of meaningful customer service risk sacrificing long-term profits and the company’s own reputation” (Business Week, 2007). Because accounting measures only evaluate historical performance indicators, they are not well suited to capture such anticipated future cash flows (Srinivasan & Hanssens, 2009).

Third, the temporal aggregation level of financial accounting measures makes the link to specific events or decisions difficult (Geyskens, Gielens, & Dekimpe, 2002). End-of-the-year accounting numbers may be influenced by many marketing and strategic decisions that took place during the year, of which the customer-support outsourcing decision is just one.

To deal with these three issues, we use an event study to examine the effect of outsourcing customer support on shareholder value. First, shareholder value integrates multiple facets of
performance into a single “net-effect” measure (Gielens & Geyskens, 2012). Second, shareholder value hinges largely on growth prospects and sustainability of profits (i.e. how the firm is expected to perform in the future), in contrast to most accounting measures that are retrospective in examining historical performance (Srinivasan & Hanssens, 2009). Third, an event study allows for measuring the impact of a specific, discrete event on daily (i.e. temporally disaggregated) stock returns, and thus can be thought of as a controlled experiment (Mizik & Jacobson, 2003).³

3.2. Event-study methodology

The event-study approach relies on the assumption that financial markets are efficient. According to the semi-strong version of the efficient-market hypothesis, a firm’s stock price accurately reflects all publicly available information about the firm. When an event occurs (in our case, when information concerning a firm’s outsourcing of customer support is made public), investors update their expectations about the firm’s future performance and react by buying or selling shares of that firm. As a result, the firm’s stock price immediately changes to reflect the expected changes in future revenue streams associated with new information (Gielens, van de Gucht, Steenkamp, & Dekimpe, 2008). The percentage change in the stock price is the stock return.

We compare the observed stock return \( R_{it} \) on the event day (i.e. the day firm \( i \)’s outsourcing arrangement was announced) with \( E(R_{it}) \), the firm’s return that would be expected if the event had not taken place. The difference between the observed return for firm \( i \) on the event day and its expected return is the abnormal return, \( AR_{it} \), or the firm’s unexpected change in stock price, which is attributed to the event. The abnormal return \( AR_{it} \) provides an unbiased estimate of the future earnings generated by the event.

³ Despite the advantages of using shareholder value as a performance metric, it is not perfect. Stock prices, just like accounting measures, can be manipulated.
To obtain estimates of a firm’s expected returns, we use the world-market model developed by Park (2004). According to this model:

\[
E(R_{it}) = \hat{\alpha}_i + \hat{\beta}_i R_{mit} + \hat{\gamma}_i R_{wmt} + \hat{\delta}_i X_{it}
\]

(1)

where \(R_{mit}\) is the market-index return in the home country of outsourcing firm \(i\) on trading day \(t\), \(R_{wmt}\) is the world-market-index return on trading day \(t\), and \(X_{it}\) is the change in the foreign currency exchange rates in the home country of firm \(i\) on day \(t\). \(\hat{\alpha}_i, \hat{\beta}_i, \hat{\gamma}_i,\) and \(\hat{\delta}_i\) are firm-specific OLS estimates from regressing \(R_{it}\) on \(R_{mit}, R_{wmt},\) and \(X_{it}\) over an estimation period from 250 to 30 trading days prior to the event.

To account for information leakage before the event day (for \(t_1\) time periods before the event) and for the possibility that some information is disseminated after the event day (for \(t_2\) time periods after the event) (McWilliams & Siegel, 1997), we aggregate the abnormal returns for a firm over the event window \([-t_1, t_2]\) into a cumulative abnormal return \(CAR_i\) to draw overall inferences for the event of interest (where \(t = 0\) on the event day):

\[
CAR_i[-t_1, t_2] = \sum_{t=-t_1}^{t_2} AR_{it}
\]

(2)

Because we conduct the event study over \(N\) outsourcing events, this \(CAR\) can be averaged into a cumulative average abnormal return (\(CAAR\)):

\[
CAAR[-t_1, t_2] = \frac{\sum_{i=1}^{N} CAR_i[-t_1, t_2]}{N}
\]

(3)

To test the significance of the \(CAAR\), we use the Patell (1976) statistic, in which the abnormal returns are standardized by the standard deviations of the regression residuals that were obtained for the estimation window (cf. Jain, 1982). This reduces problems of heteroskedasticity that may

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4 The market model, compared to the world-market model, overestimates changes in firm value when applied to a multi-country event study.
arise when the estimated variances of the world-market model residuals vary across different firms. The length of the event window \([-t_1, t_2]\) is an empirical issue and is determined by selecting the most significant \(CAAR\) from several calculated \(CAARs\) for different event windows (see Geyskens, Gielens, & Dekimpe, 2002 and Gielens et al., 2008 for similar practice).

To test our hypotheses on the performance consequences of outsourcing customer support, we regress the outsourcing firms’ standardized cumulative abnormal returns on the covariates:

\[
CAR_i[-t_1, t_2] = \beta_0 + \beta_1 \text{Emerge}_i + \beta_2 \text{PersCont}_i + \beta_3 \text{KnowEmb}_i + \beta_4 (\text{PersCont}_i \times \text{Emerge}_i) \\
+ \beta_5 (\text{KnowEmb}_i \times \text{Emerge}_i) + \beta_6 \text{MktInt}_i + \beta_7 \text{Size}_i \\
+ \beta_8 (\text{MktInt}_i \times \text{Emerge}_i) + \beta_9 (\text{Size}_i \times \text{Emerge}_i) + \sum_{k=1}^{K} \gamma_k \text{Control}_{ki} + \mu_i
\]  

(4)

where \(\text{Emerge}_i\) refers to the selection of an emerging market rather than an established economy as outsourcing location, \(\text{PersCont}_i\) and \(\text{KnowEmb}_i\) capture whether the outsourced customer support requires personal customer contact and embedded knowledge, respectively. \(\text{MktInt}_i\) is the outsourcing firm’s marketing resource intensity, \(\text{Size}_i\) indicates the outsourcing firm’s size, and \(\text{Control}_{ki}\) is a set of \(K\) control variables. To account for potential inter-correlation among outsourcing firms located in the same continent, we use robust clustered error-term estimation (cf. Mizik & Jacobson, 2009).

Firms may have chosen an emerging market versus an established economy as an outsourcing location to optimize their performance, such that only maximizing choices are observed. To account for self-selection, we follow the Heckman two-step procedure (Heckman, 1979). In the first step, where we also take into account the clustered nature of the data, we specify a probit selection model to estimate the likelihood that a firm would engage in customer-support outsourcing to an emerging versus an established market \((\text{Emerge})\). As determinants, we include variables at the transaction, the firm, the industry, and the (home) country level which previous

\footnote{The continent clusters are Asia, Australia, Europe, and North America.}
At the transaction level, we account for the two customer-support characteristics (personal customer contact and knowledge embeddedness) that are included in Equation (4). Firms may be less inclined to outsource customer support that is personal in nature and that is characterized by high levels of embedded knowledge to a provider from an emerging market, for reasons outlined in the hypotheses section. At the firm level, we control for the two firm characteristics (marketing resource intensity and firm size) that are included in Equation (4), again for reasons outlined in the hypotheses section. We further include the firm’s past performance, as reflected in its profitability and leverage in the year prior to the outsourcing announcement. On the one hand, good past performance may motivate companies to experiment with outsourcing to providers from emerging markets. On the other hand, poor past performance signifies the ineffectiveness of existing operations and thus may provide strong and legitimate reasons for firms to outsource to providers from emerging markets in an attempt to obtain cost savings (Zhou, Tse, & Li, 2006). At the industry level, we include industry concentration. Highly competitive industries typically force firms to resort to frequent price cuts in order to wrest market share from competitors. Key to the long-term viability of price cuts is the ability of the firm to achieve cost savings through, e.g., outsourcing to providers from emerging markets (Kalaignanam & Varadarajan, 2012). This suggests that outsourcing to providers from emerging markets may be pursued to a greater extent in industries characterized by higher levels of competitive intensity. At the country level, we include a customer satisfaction index, which captures the corporate emphasis on customer satisfaction in the outsourcing firm’s home country. Selecting an emerging market as an outsourcing location is a less likely strategy in countries where firms emphasize customer satisfaction, since such a strategy may negatively affect consumer perceptions (Thelen,
Honeycutt, & Murphy, 2010). Finally, we include a yearly trend variable to capture the increasing popularity of customer-support outsourcing to providers from emerging markets.6

We then compute the inverse Mills ratio. In the second step, we add the inverse Mills ratio to the right hand side of Equation (4) to control for potential selection bias. An insignificant inverse Mills ratio indicates that selection bias is not likely to be a concern.

3.3. Sample

We gathered customer-support outsourcing announcements through extensive searches in the Lexis Nexis, Factiva, and SDC Platinum databases over the 1993-2007 period. This search resulted in an initial sample of 167 outsourcing announcements for firms from established economies that outsource customer-support activities to either established or emerging economies. Elimination of firms that were not publicly traded reduced the sample to 114 announcements. We further removed eleven announcements for firms for which stock price information was missing around the event day. To minimize the presence of confounding effects that might have extraneous influences on stock prices, we deleted 16 more announcements that included information about other important firm events (e.g., firm sales, earnings, CEO appointment) or if another announcement concerning the same firm appeared within a four-day

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6 We specify the selection model as follows: \( \text{Emerge} = \alpha_0 + \alpha_1 \text{PersCont} + \alpha_2 \text{KnowEmb} + \alpha_3 \text{MktInt} + \alpha_4 \text{Size} + \alpha_5 \text{Profit} + \alpha_6 \text{Leverage} + \alpha_7 \text{IndCon} + \alpha_8 \text{SatEmph} + \alpha_9 \text{Trend} + \epsilon \), where \( \text{Profit} \) is net income divided by sales in the year before the outsourcing announcement, \( \text{Leverage} \) is the ratio of long-term debt to total assets in the year before the outsourcing announcement, \( \text{IndCon} \) is a measure of industry concentration equal to the sum of the market shares of the four largest firms in the industry (low values indicate high competitiveness), \( \text{SatEmph} \) is a customer satisfaction index which measures the extent to which customer satisfaction is emphasized by companies in the outsourcing firm’s home country (taken from the World Competitiveness Yearbook), and \( \text{Trend} \) is a yearly trend variable. The results show that outsourcing to providers from emerging markets is more likely when the outsourcing firm’s past profitability is higher (\( \alpha_5 = .04, p < .01 \)), when its leverage is lower (\( \alpha_6 = -2.66, p < .01 \)), in industries characterized by higher levels of competitive intensity (\( \alpha_7 = -.92, p < .05 \)), and in countries where corporate emphasis on customer satisfaction is lower (\( \alpha_8 = -.18, p < .10 \)). We further find that a firm’s probability to outsource to a provider from an emerging market increases over time (\( \alpha_9 = .12, p < .01 \)), indicating the increasing popularity of this practice. The model shows acceptable fit with a pseudo R² of 17%. Interestingly, none of the focal variables in our study (\( \text{PersCont}, \text{KnowEmb}, \text{MktInt}, \text{Size} \)) were significantly related to a firm’s propensity to outsource to a provider from an emerging market (\( p > .10 \)).
window around the announcement.

The final sample of 87 announcements spans 21 industries. All outsourcing firms come from established economies, with the majority of outsourcing firms coming from the United States (40%), the United Kingdom (20%), and the Netherlands (7%). Most outsourcing firms are active in the communications (Standard Industrial Classification (SIC) code 48), business services (SIC code 73), and industrial machinery and equipment (SIC code 35) industries. The outsourcing providers come from a wide variety of countries, namely Australia, Belgium, Canada, Estonia, Germany, India, Indonesia, Ireland, Japan, Malaysia, Mexico, the Netherlands, Pakistan, the Philippines, Singapore, South Africa, Spain, Sweden, Taiwan, the U.K., and the U.S. One third of the outsourcing firms in our sample outsource to a service provider from an emerging market (with India being the most popular outsourcing location), whereas two third opt for an outsourcing provider from an established economy. Of the latter, 67% outsource to a service provider that is located in their home country (i.e. domestic outsourcing).

3.4. Operationalization

Financial measures. We obtained data on stock prices and market-wide indices from the Center for Research on Security Prices (CRSP) and from Datastream. To capture global market movements, we use the Financial Times Stock Exchange (FTSE) World Index. To account for foreign currency exchange rates, we use the exchange rate between the U.S. dollar and the local currencies (cf. Park, 2004).

Emerging market versus established economy. We use a dummy variable that equals one when the outsourcing firm selects an outsourcing provider in an emerging market, and that is zero when it selects a provider in an established economy. Following Burgess and Steenkamp (2006, p. 339), we define an emerging market as “a country in which PPP-adjusted GDP per capita,
converted to U.S. dollar and smoothed for three-year currency fluctuations, is equal to or less than the highest ranked country classified as ‘middle income’ by the World Bank.”

*Nature of the outsourced customer-support service.* We content-analyzed the outsourcing announcements to identify whether the outsourcing arrangement involved personal customer contact (e.g., telephone support) or impersonal customer contact (e.g., e-mail support). In a similar vein, we identified whether the outsourcing provider required highly embedded, complex knowledge for delivering customer support (e.g., technical customer support) or whether the outsourced customer-support processes were simple services characterized by low knowledge embeddedness (e.g., reservations). Two coders were introduced to the theoretical concepts “personal customer contact” and “high knowledge embeddedness,” and how they differ from “impersonal customer contact” and “low knowledge embeddedness.” Subsequently, the coders independently evaluated each outsourcing announcement on the basis of the construct definitions. Inter-coder agreement was over 90%. Differences between the coders were reconciled through in-depth discussion between the coders. We operationalize personal customer contact as a dummy variable that equals one when the outsourcing arrangement involves personal customer contact and zero otherwise. ⁷ Similarly, we use a dummy variable that equals one for customer support that is characterized by high knowledge embeddedness and zero otherwise.

*Marketing resource intensity.* We measure the outsourcing firm’s marketing resource intensity as its annual Selling, General and Administrative (SG&A) expenditures divided by total assets. Although the SG&A measure also contains items that are not strictly marketing expenses, it is the best publicly available measure of marketing spending (see, e.g., Dinner, Mizik, & Lehmann, 2009 and Luo, 2008 for similar practice).

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⁷ Nine announcements pertained to outsourcing arrangements that involved both personal and impersonal customer contact. We assessed the robustness of our findings by removing these nine cases from our sample. Results remained substantively the same.
Firm size. Following Gielens et al. (2008), we measure the outsourcing firm’s size as its total sales, one year prior to the outsourcing announcement. We log-transform this measure to reduce skewness and to account for potential diminishing returns to scale (see, e.g., Dekimpe et al., 1997).

Control variables. Labor-cost savings are the primary reason for most companies to outsource customer support to emerging markets. We therefore control for labor-cost differences between the countries of the outsourcing firm and the outsourcing provider. We divide labor costs in the country of the outsourcing firm by labor costs in the country of the outsourcing provider in the year prior to the announcement. Higher scores reflect that the outsourcing firm takes advantage of the lower labor costs in the country of the outsourcing provider.

Approximately 22% of the outsourcing firms in our sample opted for an outsourcing provider from an established economy that differed from their home country (as opposed to selecting a domestic provider). Prior research has shown that consumers believe that domestic workers are superior to foreign service providers in serving them (Theelen, Yoo, & Magnini, 2011, p. 272). Moreover, consumers associate outsourcing providers with a foreign accent with lower service quality, competence, and credibility (Stringfellow, Teagarden, & Nie, 2008; Theelen, Yoo, & Magnini, 2011). To account for such an effect, we include a domestic-outsourcing dummy that equals one when firms outsource to providers from their home country, and is zero otherwise.  

We further control for industry concentration, which is measured as the sum of the market shares of the largest four firms in the outsourcing firm’s industry (cf. Cleeren, van Heerde, &

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8 Consistent with this line of research, we thus assume that, e.g., an Indian provider will not outperform a French provider, even though English is an official language in India. Both Indian and French speakers have an English accent that is likely to negatively affect the ease of communication. Nevertheless, we further examined whether communication-style problems are less severe if the outsourcing firm and the provider share an official language. We added a dummy variable to Equation (4) that equals one when the outsourcing firm and the outsourcing provider share the same official language (e.g., U.S. firm – Indian provider or U.S. firm – U.K. provider), and is zero otherwise (e.g., U.S. firm – French provider). In line with our expectations, our results remained substantively the same.
Dekimpe, 2013), to account for the fact that outsourcing strategies may more closely fit with the environmental demands of less concentrated (i.e. more competitive) industries (Schilling & Steensma, 2001).

Following Luo (2007) and Raassens, Wuyts, and Geyskens (2012), we control for additional financial information of the outsourcing firm that may influence stock returns, namely its profitability (net income divided by sales in the year before the outsourcing announcement) and leverage (ratio of long-term debt to total assets in the year before the outsourcing announcement).

To control for unobserved heterogeneity across industries and years, we add dummy variables for each industry and year to Equation (4). Instead of retaining all industry and year dummies, which would lead to unstable results and multicollinearity, we estimate a trimmed model in which only the dummies that are significant at $p < .10$ are retained (cf. Anderson & Weitz, 1989).

A summary description of all measures, including the diverse data sources used, can be found in Table 2. Table 3 reports descriptive statistics (in original metrics) and correlations. Bivariate correlations exceeding .8 (Judge et al., 1988) and variance inflation factors exceeding 10 (Mason & Perreault, 1991) indicate potential multicollinearity problems. All correlations and variance inflation factors are well below these critical values. Hence, multicollinearity is not a concern.

[Insert Tables 2 and 3 about here]

4. Results

Of all windows surrounding the event day, the one from -1 to +2 shows the most significant CAAR: $CAAR[-1,+2] = -.15\%$ ($p < .05$). This implies that, on average, the customer-support outsourcing announcement led to a decrease of .15% of shareholder value. Although customer-support outsourcing is, on average, evaluated negatively by the financial markets, the
performance implications differ substantially across outsourcing firms. Whereas 49% of the outsourcing firms show a negative CAR, 51% were evaluated positively by investors. To explain this cross-sectional variation, we estimated Equation (4).

Table 4 presents the results. We find that the effect on shareholder value of outsourcing customer support is, on average, more favorable for outsourcing to providers located in emerging markets as opposed to established economies ($\beta_1 = 2.61, p < .05$).

As hypothesized (H1), we find a negative interaction effect between customer-support outsourcing to emerging (versus established) markets and personal customer contact (H1: $\beta_4 = -1.90, p < .05$). Thus, the performance advantage of outsourcing to emerging markets is lower when the outsourced customer support involves personal customer contact. Also H2 is supported. The performance advantage of outsourcing to emerging (versus established) markets is lower when the outsourced customer-support activity is characterized by high knowledge embeddedness ($\beta_5 = -2.49, p < .05$).

As hypothesized in H3, we find a positive significant interaction effect between customer-support outsourcing to emerging (versus established) economies and the outsourcing firm’s marketing resource intensity ($\beta_8 = 3.22, p < .05$). H4 proposes a positive interaction effect between customer-support outsourcing to emerging (versus established) economies and the outsourcing firm’s size. Also this hypothesis is supported ($\beta_9 = .41, p < .10$). The coefficient of the inverse Mills ratio was not significant ($\lambda = -1.52, p > .10$). Thus, endogeneity was not a major concern in our study.

[Insert Table 4 about here]

5. Robustness checks
To check the robustness of our findings, we perform three additional analyses.

**Alternative event window.** Our measure of performance is the cumulative abnormal return over the 4-day event window [-1,2]. We validate our results across the alternative window [-1,1]. We opt for this window because it is at the same time short enough to benefit from increased power of the test statistic (McWilliams & Siegel, 1997), and long enough to deal with the lack of synchronism in stock-market trading hours between countries (5-6 hours difference between American and European countries and between European and most Asian countries; 12 hours difference between American and Asian countries; Park, 2004). Our results are robust for this alternative event window. Specifically, we replicate the positive and significant main effect on shareholder value of outsourcing to providers in emerging (rather than established) economies ($p < .05$). Further, all interaction effects have the expected sign and are significant ($p < .10$).

**Long-run correction.** To test the efficient market assumption, we check whether the initial evaluation was not just a short-run over- or under-reaction that was corrected in the longer-run (Fama, 1998). We calculate 3-months, 6-months, 1-year, and 2-year long-term effects using the buy-and-hold abnormal returns (BHAR) and Ibbotson’s returns across time and securities (IRATS) models. We find no effect on long-term abnormal returns ($p > .10$), suggesting that the stock market is reasonably efficient. Thus, the abnormal returns to outsourcing customer support occur in the short-term window and there are no corrections in the long-run.⁹

**Validation of theoretical arguments.** The arguments underlying our hypotheses are based on the markedly different cultural and regulative systems of emerging markets and established economies. In particular, the theory underlying H1 and H2 pertains to the communication-style

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⁹ Our dependent variable is the short-term cumulative abnormal return accruing from the outsourcing announcement to the outsourcing firm. Although this measure materializes in the short term (consistent with the efficient market hypothesis that a firm’s stock price immediately reflects all new information), conceptually this measure reflects the stock markets’ best estimate of the change in the long-term value of the firm. Significant long-term abnormal returns, as computed by the BHAR or IRATS methodology, reflect that the stock market is not efficient, but rather over- or under-reacted to the announcement. They do not connote long-term firm performance.
problems that are inherent to the cultural system of emergent markets, while the theory behind H3 and H4 relates to emerging markets’ regulative system. To validate our line of reasoning, we re-estimate our model after replacing our focal variable $Emerge_i$ (which captures the selection of an emerging market rather than an established economy as outsourcing location) with two continuous measures: (i) a cultural-distance measure, to capture communication-style problems, and (ii) a rule-of-law measure, to capture the regulatory framework in the country of the outsourcing provider. To account for the potential endogeneity of cultural distance and rule-of-law, we use Garen’s (1984) selection-correction estimation technique. In the first step, we regress cultural distance and rule-of-law on the same variables we included in the first step of the Heckman procedure, while accounting for the clustered nature of the data. Then we obtain the residuals and compute the interaction term between the residuals and cultural distance and rule-of-law, respectively. In the second step, we add these terms as regressors to control for potential selection bias. Table 5 presents the results. We find that the interactions between personal customer contact and cultural distance ($\beta = -1.15, p < .05$) and between knowledge embeddedness and cultural distance ($\beta = -.52, p < .10$) are significant and in the expected direction. As expected, we also find significant negative interactions between marketing resource intensity and rule-of-law ($\beta = -1.78, p < .05$) and between firm size and rule-of-law ($\beta = -.34, p < .05$). Hence, this analysis corroborates the underlying developed arguments.

[Insert Table 5 about here]

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10 Cultural distance is operationalized as a composite index, using the cultural dimensions (power distance, uncertainty avoidance, individualism, and masculinity) developed by Hofstede (2001) and the operationalization by Kogut and Singh (1988). Rule-of-law is operationalized as the extent to which agents have confidence in and abide by the rules of society (i.e. the quality of contract enforcement, property rights, the police, and the courts, and the likelihood of crime and violence). The measure is taken from Kaufmann, Kraay, and Mastruzzi (2008). Both variables are highly correlated with $Emerge_i$ ($r = .70$ for cultural distance and $r = -.93$ for rule-of-law) and with each other ($r = -.65$).
6. Discussion

Customer-support outsourcing has received bad press, featuring alarming headlines such as “Outsourcing’s Impact on Customer Satisfaction: It’s Not Good,” “Beware: Your Customers Oppose Outsourcing,” and “Losing Money by Spending Less.”\[1\] Despite the bad press, customer-support outsourcing is still on the rise, especially to service providers from emerging markets. The primary reason for firms to embrace a customer-support outsourcing strategy is to obtain cost savings. However, approximately 50% of the outsourcing firms in our sample experience negative stock market reactions. Thus, whereas outsourcing customer support works for some firms, it is not a one-size-fits-all strategy. Our focus is on explaining what makes customer-support outsourcing to providers from emerging versus established markets more versus less successful. Below, we discuss the theoretical and the managerial contributions of our research.

6.1. Theoretical implications

The moderating role of customer-support characteristics. Extant research (e.g., Bharadwaj & Roggeveen, 2008; Roggeveen, Bharadwaj, & Hoyer, 2007) has repeatedly shown that the geographic location of the outsourcing provider influences consumer expectations and satisfaction, and that consumers prefer support services from their own country. Based on this work, one might be tempted to conclude that customer support should never be outsourced offshore – and certainly not to emerging markets. We show that the logic is more intricate. While, on average, outsourcing to providers from emerging markets enhances shareholder value more than outsourcing to established economies, there is substantial variation depending on the nature

\[1\] Headlines taken from business websites itbusinessedge.com, gmj.gallup.com, and tmcnet.com.
of the outsourced customer-support service and the nature of the outsourcing firm.

To fully understand the performance implications of customer-support outsourcing, one should acknowledge the differences between outsourced customer-support services rather than generalize across them, which has been the convention in extant research. We find that outsourcing customer support to emerging markets is less beneficial for support services that are characterized by (1) direct, real-time interaction between the customer and the service employee (as opposed to impersonal contact), and/or (2) highly embedded knowledge (as opposed to more superficial knowledge).

The triadic nature of customer-support outsourcing. Our findings contribute to recent endeavors, primarily in the area of supply chain management, to understand service triads (e.g., Gunawardane, 2012; van der Valk & van Iwaarden, 2011). This emerging stream of literature builds on earlier conceptualizations by both operations management and marketing scholars of the triadic nature of exchange (e.g., Choi & Wu, 2009; Wuyts, Stremersch, van den Bulte, & Franses, 2004). Service triads consist of three actors (the client firm, the service provider, and the end customer) and the ties that bind them (e.g., due to an outsourcing agreement). Outsourcing to providers from emerging markets increases communication difficulties in two ties: (1) the tie between the service provider’s employees and the customer, and (2) the tie between the outsourcing firm’s employees and the service provider’s employees. On the one hand, when service employees in emerging markets engage in direct, real-time interaction with customers in established economies, customers can become irritated and engage in negative behaviors toward the outsourcing firm. On the other hand, when the outsourced service entails highly embedded knowledge, communication-style differences between employees of the service provider and employees of the outsourcing firm can complicate effective knowledge transfer. Whereas the extant marketing literature on customer-support outsourcing has extensively studied the tie
between the service provider and the customer, the tie between the outsourcing firm and the service provider has received much less attention. Our results corroborate the need to acknowledge the triadic nature of outsourcing.

_The moderating role of firm characteristics._ The performance potential of outsourcing customer support to emerging markets as opposed to established economies also depends on the nature of the outsourcing firm. First, larger firms benefit more from outsourcing customer-support services to emerging markets than smaller firms, presumably because they can credibly threaten to switch to other providers and can select better partners through their preferential relationship with local governments. Second, outsourcing customer support to emerging markets leads to a higher performance potential for firms with a higher marketing resource intensity than for firms with a lower marketing resource intensity. This finding, along with the validation that a high marketing resource intensity can help firms hedge against a weak regulatory system, contributes to earlier efforts to understand the role of marketing (e.g., Kumar & Shah, 2009; Moorman & Rust, 1999; Verhoef & Leeflang, 2009). Drawing on Day’s (1994) seminal work, we bring back in marketing’s role in terms of environmental scanning and we argue that firms with a strong marketing focus are better able to identify appropriate exchange partners. As a consequence, these firms can better deal with the partner-related risk that is associated with weak regulatory environments. Conversely, our results suggest that a strong legal environment substitutes for some of the benefits offered by a strong marketing focus. This is in line with the results of Wu (2013), who shows that marketing capabilities have a weaker effect on firm performance in countries characterized by strong legal systems.

6.2. _Managerial guidelines_
To arrive at a better understanding of the impact of customer-support and firm characteristics on performance, we conduct a “what-if” analysis. We use the estimates from Table 4 to calculate the performance implications of outsourcing customer-support services characterized by personal (as opposed to impersonal) customer contact and requiring highly embedded (as opposed to more superficial) knowledge for small versus large-sized firms that are low versus high on marketing resource intensity. Table 6 presents the results.

[Insert Table 6 about here]

We first turn to the left upper quadrant, i.e. the case where the outsourced customer-support service is impersonal and knowledge embeddedness is low. Irrespective of a firm’s size and marketing resource intensity, outsourcing to a provider from an emerging market has more positive performance implications than outsourcing to a provider from an established economy. The difference in performance implications between emerging and established markets is least pronounced for small firms with a low marketing resource intensity, but even these firms experience shareholder value increases that are approximately 40% higher when outsourcing to providers from emerging (CAR = 2.61) rather than established (CAR = 1.86) economies.

The picture reverses when the outsourced customer-support service is personal and knowledge embeddedness is high (right lower quadrant). In three out of the four cells, the shareholder value implications of outsourcing such services are higher for providers from established rather than emerging economies. For small firms with a low marketing resource intensity, outsourcing personal and specialized customer support to providers from emerging markets even becomes value-destroying, as attested by the CAR of -69. Only for large firms with a high marketing resource intensity, providers from emerging markets should be preferred over providers from established economies, although the performance difference is relatively small in magnitude (CAR = 1.37 vs. 1.05).
The other two quadrants show more variation. *When outsourcing personal customer support services that are low on knowledge embeddedness* (right upper quadrant), firms are generally better off selecting an outsourcing provider from an emerging market. Only small firms with a low marketing resource intensity would do better to outsource to providers from established economies (CAR = 2.63) rather than emerging markets (CAR = 1.48). *When outsourcing impersonal customer-support services that are high in knowledge embeddedness* (left lower quadrant), the same conclusion can be drawn. Large firms are better off selecting an outsourcing provider from an emerging market (regardless of their marketing resource intensity). Small firms with a high marketing resource intensity are also better off selecting an outsourcing provider from an emerging market, but small firms with a low marketing resource intensity experience more favorable performance implications by selecting an outsourcing provider from an established economy.

In sum, when considering the different quadrants in Table 6 jointly, large firms always benefit more from outsourcing customer support to emerging markets rather than established economies, except when their marketing resource intensity is low and the service is both personal and high in knowledge embeddedness. For small firms, the picture is more intricate. In case of high knowledge embeddedness, they are better off selecting a provider from an established economy except when their marketing resource intensity is high and the service is impersonal in nature. In contrast, when small firms outsource services that are low on knowledge embeddedness, they are better off selecting a provider from an emerging market, except when their marketing resource intensity is low and the service is personal in nature.

An interesting observation stemming from our endogeneity analysis is that when outsourcing customer support to emerging markets versus established economies, firms did not yet take the performance implications into account. Hence, it appears that firms do not yet behave optimally
in terms of the performance that could be obtained. A possible explanation stems from the fact that outsourcing to emerging markets is a fairly recent phenomenon, while it takes time to develop optimal practices (Nelson & Winter, 1982). Firms have little or no own prior experiences to rely on, and are therefore still uncertain about the benefits and drawbacks of their outsourcing decisions. Hence, our study provides several valuable first insights for firms intending to outsource customer support in the near future.

6.3. Future research directions

We organize our agenda for future research along five trajectories: (1) using more fine-grained measures, (2) uncovering heterogeneity among emerging markets, (3) further characterizing outsourcing firms and outsourcing providers, (4) solving the paradox between outsourcing marketing activities while not eroding internal capabilities, and (5) examining the full outsourcing firm – service provider – customer triad.

First, our measure of marketing resources is coarse. Although SG&A is a frequently used measure of marketing spendings (see, e.g., Dutta, Narasimhan, & Rajiv, 1999; Mizik & Jacobson, 2007), it does not only capture the firm’s expenditures in sales force, advertising, and promotional activities, but also covers general overhead and legal costs. Future research would benefit from a more fine-grained measure that isolates the marketing spending items.

Second, our study focuses on systematic differences between emerging and established economies. Fostered by current developments in the outsourcing market, where the most popular outsourcing locations (e.g., India) are overheating and losing ground to locations such as South Africa, Morocco, and Brazil, future research could study differences among emerging markets.

Third, our coverage of firm-related characteristics is only partial. Thus, future investigations could enhance our research by examining additional firm characteristics. In addition, a question
that remains unanswered in this paper is to what extent the performance implications of outsourcing customer support depend on characteristics of the outsourcing provider. The outsourcing providers were often located in countries where firm-specific information is poorly documented. Hence, we were unable to test for characteristics of the outsourcing providers.

Fourth, our finding that firms higher in marketing resource intensity benefit less from outsourcing customer support to established economies raises a broader strategic question related to the boundaries of the firm. How should firms balance nurturing internal marketing capabilities with outsourcing customer support? For any given marketing function, does nurturing internal capabilities substitute for outsourcing, or do internalized capabilities and outsourcing serve as complements? Whether firms should retain a certain degree of activities in-house to reap the benefits from outsourcing remains an issue for future research.

Fifth, outsourcing service delivery leads to a triadic relationship between the outsourcing firm, the service provider, and the customer. When customers are dissatisfied with service delivery by the service provider, this may have ramifications for the outsourcing firm – customer relationship. Customers may call upon the outsourcing firm to correct the outsourcing provider. Metters (2008) gives the example of a customer who complained to Dell about the “horrible accent an Indian call center worker had” and who “threatened to forego future business with Dell” (p. 205). More research is needed to understand this governance mechanism, which is known as two-step leverage in the network governance literature (Gargiulo, 1993; Wuyts, 2010).
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### Table 2
Variables and data sources

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<th>Construct</th>
<th>Measure</th>
<th>Data Source</th>
</tr>
</thead>
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<td>Shareholder value</td>
<td>Changes in stock prices over a four-day event window using standardized cumulative abnormal returns</td>
<td>CRSP &amp; Datastream</td>
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<tr>
<td>Emerging market</td>
<td>Dummy variable: outsourcing firm outsources customer support to an outsourcing provider located in an emerging market (1) versus an established economy (0)</td>
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<td>Personal customer contact</td>
<td>Dummy variable that equals one when the outsourced customer-support service involves personal customer contact; zero otherwise</td>
<td>Lexis Nexis, Factiva, &amp; SDC Platinum</td>
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<tr>
<td>Knowledge embeddedness</td>
<td>Dummy variable that equals one when the outsourced customer-support service entails complex solutions that require highly embedded knowledge; zero otherwise</td>
<td>Lexis Nexis, Factiva, &amp; SDC Platinum</td>
</tr>
<tr>
<td>Marketing resource intensity</td>
<td>The outsourcing firm’s Selling, General, and Administrative (SG&amp;A) expenditures divided by total assets</td>
<td>Compustat &amp; Annual reports</td>
</tr>
<tr>
<td>Firm size</td>
<td>Total sales (log-transformed) of the outsourcing firm</td>
<td>Compustat &amp; Annual reports</td>
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<td>Labor-cost savings</td>
<td>Ratio of labor costs in the country of the outsourcing firm and labor costs in the country of the outsourcing provider</td>
<td>World Development Indicators</td>
</tr>
<tr>
<td>Domestic outsourcing</td>
<td>Dummy variable that equals one when the outsourcing firm outsources customer support domestically; zero otherwise</td>
<td>Lexis Nexis, Factiva, &amp; SDC Platinum</td>
</tr>
<tr>
<td>Profitability</td>
<td>Net income divided by sales in the year prior to the outsourcing announcement</td>
<td>Compustat &amp; Annual reports</td>
</tr>
<tr>
<td>Leverage</td>
<td>Ratio of long-term debt to total assets in the year prior to the outsourcing announcement</td>
<td>Compustat &amp; Annual reports</td>
</tr>
<tr>
<td>Industry concentration</td>
<td>Sum of market shares of the four largest firms in the outsourcing firm’s industry</td>
<td>Compustat</td>
</tr>
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</table>
Table 3
Descriptive statistics and correlation matrix

<table>
<thead>
<tr>
<th></th>
<th>Mean</th>
<th>s.d.</th>
<th>Min.</th>
<th>Max.</th>
<th>1.</th>
<th>2.</th>
<th>3.</th>
<th>4.</th>
<th>5.</th>
<th>6.</th>
<th>7.</th>
<th>8.</th>
<th>9.</th>
<th>10.</th>
<th>11.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Standardized CAR([-1,+2])</td>
<td>.18</td>
<td>2.01</td>
<td>-4.62</td>
<td>5.66</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Emerging market</td>
<td>.33</td>
<td>.47</td>
<td>.00</td>
<td>1.00</td>
<td>.09</td>
<td>1.00</td>
<td></td>
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<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Personal customer contact</td>
<td>.67</td>
<td>.47</td>
<td>.00</td>
<td>1.00</td>
<td>.05</td>
<td>.03</td>
<td>1.00</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Knowledge embeddedness</td>
<td>.34</td>
<td>.48</td>
<td>.00</td>
<td>1.00</td>
<td>-.15</td>
<td>-.10</td>
<td>-.10</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Marketing resource intensity</td>
<td>.26</td>
<td>.33</td>
<td>.00</td>
<td>1.87</td>
<td>-.07</td>
<td>-.03</td>
<td>-.00</td>
<td>.30</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Firm size (in millions $)</td>
<td>15,682</td>
<td>25,069</td>
<td>4.64</td>
<td>155,445</td>
<td>.07</td>
<td>.10</td>
<td>.18</td>
<td>-.14</td>
<td>-.40</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Labor-cost savings</td>
<td>7.28</td>
<td>11.64</td>
<td>.64</td>
<td>72.68</td>
<td>.01</td>
<td>.62</td>
<td>.06</td>
<td>-.07</td>
<td>-.01</td>
<td>.06</td>
<td>1.00</td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>8. Domestic outsourcing</td>
<td>.45</td>
<td>.50</td>
<td>.00</td>
<td>1.00</td>
<td>-.02</td>
<td>-.64</td>
<td>-.10</td>
<td>.18</td>
<td>-.30</td>
<td>-.49</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>9. Profitability</td>
<td>-.97</td>
<td>5.64</td>
<td>-46.30</td>
<td>.78</td>
<td>.04</td>
<td>.11</td>
<td>.09</td>
<td>-.20</td>
<td>-.18</td>
<td>.40</td>
<td>-.09</td>
<td>-.19</td>
<td>1.00</td>
<td></td>
<td></td>
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<tr>
<td>10. Leverage</td>
<td>.14</td>
<td>.16</td>
<td>.00</td>
<td>.63</td>
<td>-.03</td>
<td>-.24</td>
<td>-.15</td>
<td>-.15</td>
<td>-.28</td>
<td>.16</td>
<td>-.11</td>
<td>.09</td>
<td>.04</td>
<td>1.00</td>
<td></td>
</tr>
<tr>
<td>11. Industry concentration</td>
<td>.61</td>
<td>.25</td>
<td>.19</td>
<td>1.00</td>
<td>-.15</td>
<td>.07</td>
<td>.17</td>
<td>.16</td>
<td>.06</td>
<td>-.11</td>
<td>.03</td>
<td>-.01</td>
<td>-.13</td>
<td>1.00</td>
<td></td>
</tr>
</tbody>
</table>
Table 4
Drivers of the stock market reaction to outsourcing customer support

<table>
<thead>
<tr>
<th></th>
<th>Hypothesized sign</th>
<th>b&lt;sup&gt;a&lt;/sup&gt;</th>
<th>t-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>-.95</td>
<td>-.88</td>
<td></td>
</tr>
<tr>
<td>Emerging (1) vs. established market (0)</td>
<td>2.61**</td>
<td>4.93</td>
<td></td>
</tr>
<tr>
<td><strong>Customer-support characteristics</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Personal customer contact</td>
<td>.77</td>
<td>1.96</td>
<td></td>
</tr>
<tr>
<td>Knowledge embeddedness</td>
<td>.33</td>
<td>.44</td>
<td></td>
</tr>
<tr>
<td>Personal customer contact * Emerging</td>
<td>-1.90**</td>
<td>-3.53</td>
<td></td>
</tr>
<tr>
<td>Knowledge embeddedness * Emerging</td>
<td>-2.49**</td>
<td>-2.39</td>
<td></td>
</tr>
<tr>
<td><strong>Firm characteristics</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Marketing resource intensity</td>
<td>-1.33</td>
<td>-1.96</td>
<td></td>
</tr>
<tr>
<td>Firm size</td>
<td>-.22</td>
<td>-1.48</td>
<td></td>
</tr>
<tr>
<td>Marketing resource intensity * Emerging</td>
<td>+3.22**</td>
<td>3.38</td>
<td></td>
</tr>
<tr>
<td>Firm size * Emerging</td>
<td>+.41*</td>
<td>2.14</td>
<td></td>
</tr>
<tr>
<td><strong>Control variables</strong>&lt;sup&gt;b&lt;/sup&gt;</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Labor-cost savings</td>
<td>-.00</td>
<td>-.15</td>
<td></td>
</tr>
<tr>
<td>Domestic outsourcing (1 = yes, 0 = no)</td>
<td>.28</td>
<td>.32</td>
<td></td>
</tr>
<tr>
<td>Profitability</td>
<td>-.03</td>
<td>-.78</td>
<td></td>
</tr>
<tr>
<td>Leverage</td>
<td>2.82</td>
<td>1.02</td>
<td></td>
</tr>
<tr>
<td>Industry concentration</td>
<td>2.43**</td>
<td>3.35</td>
<td></td>
</tr>
<tr>
<td>λ (inverse Mills ratio)</td>
<td>-1.52</td>
<td>-1.10</td>
<td></td>
</tr>
</tbody>
</table>

* p < .10; ** p < .05; *** p < .01

<sup>a</sup> We use one-sided tests for hypothesized effects, two-sided tests for non-hypothesized effects.

<sup>b</sup> For simplicity of presentation, the results for the industry and year dummies are not reported in the table.
Table 5
Validation of theoretical arguments

<table>
<thead>
<tr>
<th></th>
<th>Hypothesized sign</th>
<th>b&lt;sup&gt;)&lt;/sup&gt;</th>
<th>t-value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td></td>
<td>-4.46*</td>
<td>-2.36</td>
</tr>
<tr>
<td>Cultural distance</td>
<td></td>
<td>4.61</td>
<td>2.23</td>
</tr>
<tr>
<td>Rule-of-law</td>
<td></td>
<td>-.56</td>
<td>-.59</td>
</tr>
<tr>
<td><strong>Customer-support characteristics</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Personal customer contact</td>
<td></td>
<td>1.97*</td>
<td>3.02</td>
</tr>
<tr>
<td>Knowledge embeddedness</td>
<td></td>
<td>-.46</td>
<td>-.50</td>
</tr>
<tr>
<td>Personal customer contact * Cultural distance</td>
<td>-</td>
<td>-1.15*</td>
<td>-2.51</td>
</tr>
<tr>
<td>Knowledge embeddedness * Cultural distance</td>
<td>-</td>
<td>-.52*</td>
<td>-2.07</td>
</tr>
<tr>
<td><strong>Firm characteristics</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Marketing resource intensity</td>
<td></td>
<td>.29</td>
<td>.67</td>
</tr>
<tr>
<td>Firm size</td>
<td></td>
<td>-.46*</td>
<td>-3.08</td>
</tr>
<tr>
<td>Marketing resource intensity * Rule-of-law</td>
<td>d)</td>
<td>-1.78**</td>
<td>-3.44</td>
</tr>
<tr>
<td>Firm size * Rule-of-law</td>
<td>d)</td>
<td>-.34**</td>
<td>-3.79</td>
</tr>
<tr>
<td><strong>Control variables&lt;sup&gt;b,c&lt;/sup&gt;</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Labor-cost savings</td>
<td></td>
<td>.00</td>
<td>.01</td>
</tr>
<tr>
<td>Domestic outsourcing (1 = yes, 0 = no)</td>
<td></td>
<td>-1.22</td>
<td>-1.35</td>
</tr>
<tr>
<td>Profitability</td>
<td></td>
<td>-.04</td>
<td>-1.44</td>
</tr>
<tr>
<td>Leverage</td>
<td></td>
<td>7.86</td>
<td>2.26</td>
</tr>
<tr>
<td>Industry concentration</td>
<td></td>
<td>3.56*</td>
<td>5.33</td>
</tr>
<tr>
<td>η&lt;sub&gt;cd&lt;/sub&gt;</td>
<td></td>
<td>-5.97</td>
<td>-2.30</td>
</tr>
<tr>
<td>η&lt;sub&gt;rol&lt;/sub&gt;</td>
<td></td>
<td>-1.40</td>
<td>-1.38</td>
</tr>
<tr>
<td>η&lt;sub&gt;cd&lt;/sub&gt; * Cultural distance</td>
<td></td>
<td>1.03***</td>
<td>5.87</td>
</tr>
<tr>
<td>η&lt;sub&gt;rol&lt;/sub&gt; * Rule-of-law</td>
<td></td>
<td>-.96</td>
<td>-1.76</td>
</tr>
</tbody>
</table>

<sup>)</sup> We use one-sided tests for hypothesized effects, two-sided tests for non-hypothesized effects.
<sup>b)</sup> For simplicity of presentation, the results for the industry and year dummies are not reported in the table.
<sup>c)</sup> η<sub>cd</sub> and η<sub>rol</sub> correct for selection bias of cultural distance and rule-of-law, respectively, while their interactions with cultural distance and rule-of-law account for unobserved heterogeneity over the range of the continuous selection variables.
<sup>d)</sup> We expect a negative interaction effect with rule-of-law (as opposed to a positive interaction effect with Emerging in Table 4) because lower values on the rule-of-law measure are reflective of weaker regulatory environments.
Table 6
Performance potential (predicted CAR) of outsourcing customer support to emerging versus established economies as a function of customer-support and firm characteristics\(^a\)

<table>
<thead>
<tr>
<th></th>
<th>Impersonal customer-support service that is low in knowledge embeddedness</th>
<th>Personal customer-support service that is low in knowledge embeddedness</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Small firm</td>
<td>Large firm</td>
</tr>
<tr>
<td>Low marketing resource intensity</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Emerging market</td>
<td>2.61</td>
<td>3.55</td>
</tr>
<tr>
<td>Established economy</td>
<td>1.86</td>
<td>.74</td>
</tr>
<tr>
<td>High marketing resource intensity</td>
<td></td>
<td></td>
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<tr>
<td>Emerging market</td>
<td>3.72</td>
<td>4.66</td>
</tr>
<tr>
<td>Established economy</td>
<td>1.07</td>
<td>-.05</td>
</tr>
<tr>
<td>Impersonal customer-support service that is high in knowledge embeddedness</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Small firm</td>
<td>Large firm</td>
<td>Small firm</td>
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<tr>
<td>Low marketing resource intensity</td>
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<td></td>
</tr>
<tr>
<td>Emerging market</td>
<td>.44</td>
<td>1.38</td>
</tr>
<tr>
<td>Established economy</td>
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<td>1.06</td>
</tr>
<tr>
<td>High marketing resource intensity</td>
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<td></td>
</tr>
<tr>
<td>Emerging market</td>
<td>1.56</td>
<td>2.50</td>
</tr>
<tr>
<td>Established economy</td>
<td>1.40</td>
<td>.28</td>
</tr>
</tbody>
</table>

\(^a\) To calculate predicted values, the indicator variables to measure the nature of the customer-support service are set to zero or one, while the continuous variables to measure the nature of the outsourcing firm are set to one standard deviation above or below their mean (except for low marketing resource intensity, where we use the minimum instead of one standard deviation below the mean to stay within the range of the data). The other variables are held fixed at their baseline level (i.e. zero for indicator control variables and the mean for continuous control variables).
Figure 1
Conceptual framework

**Customer-support characteristics**
- Personal customer contact (H1: -)
- Knowledge embeddedness (H2: -)

**Firm characteristics**
- Marketing resource intensity (H3: +)
- Firm size (H4: +)

Customer-support outsourcing to providers from emerging vs. established economies

Shareholder valuation