Offshore outsourcing: a dynamic, operation mode perspective

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- Based on a study of an IT company, SimCorp, and its operations in Ukraine, we analyse offshore outsourcing in a broader foreign operation mode context.

- The case study approach allows us to explore the dynamic processes in depth.

- The case study shows how involvement in the foreign market generates learning that provides a foundation for eventual mode development or change.

- The study also shows how outsourcing can be used proactively as a springboard to deeper and changed operation mode activities in a foreign market.

Offshore outsourcing: A dynamic, operation mode perspective

Abstract

Based on a case study of the Danish company SimCorp and the development of its operations in Kiev, Ukraine, we analyse offshore outsourcing in a broader, longitudinal foreign operation mode context, and how it may contribute to mode change in the host country over a certain span of time. SimCorp had outsourced part of its software development work to two Ukrainian companies. The case study approach allowed us to explore the dynamic processes in depth. The study shows that involvement in the foreign market generates learning in various forms that provide a foundation for eventual mode development or change – beyond outsourcing specific learning. At the same time, restrictions on 3rd parties', that is, independent vendors' access to confidential client data, as well as protection of specific investments in human assets, may eventually become a driver for mode change, as in the SimCorp case, to ensure more effective control of the foreign operation. Finally, the case study shows how outsourcing can be used proactively as a springboard to deeper and changed operation mode activities in a foreign market.

Keywords: Outsourcing, offshoring, foreign operation mode dynamics, case study.

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1.   Introduction

Offshore outsourcing – the delegation of specified value chain activities to one or more foreign provider(s) – has, for good reasons, received considerable attention from international business and management researchers over the last decade. This has been reflected in recent special issues on offshore outsourcing (as well as captive offshoring) in *International Business Review* (2011), *Journal of International Business Studies* (2009), *Journal of International Management* (2007) and *Journal of Management Studies* (2005). Outsourcing was the focus of a recent special issue of *Industrial Marketing Management* in which its impact on business-to-business marketing was examined. In the introduction to the special issue Ahearne and Kothandaraman (2009, 376) maintain: 'Increasing globalization has made companies focus more on their outsourcing decisions. Moving beyond the tactical companies have begun to incorporate outsourcing as a strategic weapon in their armory'. Recently, attention has been drawn to the growing importance of offshore outsourcing in the services sector (Bunyaratavej, Hahn & Doh, 2008; Griffith et al., 2009). Given the size of the services sector in advanced economies, this latter trend is of particular significance (UNCTAD, 2004). The ability to utilize offshore outsourcing has been facilitated by the development of large multinational companies providing outsourced production and other services on a global scale (Welch, Benito & Petersen, 2007). Intermediaries like the Hong Kong-based company Li & Fung have emerged as specialists in handling the various steps in offshore outsourcing for their client firms – allowing companies effectively to outsource the outsourcing problem (Economist 2001; Einhorn 2009; Welch et al., 2007). In this article we focus on services and take the treatment of outsourcing, in offshore form, down a different strategic path by asking the questions: what follows, and what should follow, *after* offshore outsourcing?

Most of the research on offshore outsourcing examines the phenomenon at a certain point in time (see e.g. Bunyaratavej et al., 2007), whereas fewer studies apply a dynamic perspective (for an exception, see Lewin, Massini & Peeters, 2009). As examples of

dynamic issues, Dossani & Kenney (2004) and Manning, Massini & Lewin (2008) point to evidence of a change in outsourcing motives from basically being cost-focused towards a broader palette of strategic drivers. From substantial survey work, involving a full size range of European and US companies, Manning et al. (2008: 35) argue, that "reducing labor costs is no longer the only strategic driver behind offshoring decisions" (see also Harmancioglu, 2009; Fang, Gunterberg & Larsson, 2010; Kinkel, 2012; Lewin & Volberda, 2011). Other drivers include speed to market, manpower shortages in areas such as technological development, proximity to key customers, new service needs and, environmental issues. Further, Maskell et al. (2007) find evidence of offshore outsourcing as a gradually expanding process in which companies initially outsource limited tasks, but – as outsourcing experience is accumulated – broaden the range of business functions being outsourced to foreign providers. Outsourcing of manufacturing and IT tasks seems to lead to the addition of other value added activities to be outsourced, such as human resource management, finance and accounting, and research and development. Put together, these dynamic perspectives suggest that offshore outsourcing is a phenomenon that fits with conventional internationalization process theory in which firms' foreign engagements evolve as an incremental learning process (Johanson & Wiedersheim-Paul, 1975; Johanson & Vahlne, 1977/2006; Welch & Luostarinen, 1988); though with the important caveat that firms' offshore outsourcing location decisions may be less susceptible to a psychic distance logic (Hatönen & Eriksson, 2009) to the extent that the outsourcing location is affected countries' factor endowments and their cost implications. Nevertheless, physical and cultural distance cannot be dismissed as location decision factors when outsourcing operations imply learning and close interaction between the contractee and the outsourcing firm and/or its clients (Liu, Feils & Scholnick, 2011). Stringfellow et al. (2008) stress that interaction intensity and interaction distance (including language distance) have an impact on the extent of invisible costs in offshoring service work, and therefore its viability.

Although both static and dynamic studies have informed research about the offshore outsourcing phenomenon of the 1990s and 2000s, there is relatively little known about how this foreign operation mode intertwines with a firm's other modes of operation in the

host country, and whether and how it might be used to develop foreign operation modes in the host market, or other markets including the home market, as part of firm internationalization. The extant literature on offshore outsourcing at the firm level basically deals with this operation mode *in isolation*, addressing questions like: what are the motives for offshore outsourcing and what are its managerial and operational challenges?

Various definitions and terms have been applied to outsourcing activity in the research literature on the topic (Welch et al., 2007; Hatönen & Eriksson, 2009). Indeed, outsourcing as a term has only come into vogue in recent times, even though the phenomenon itself is much older (Hatönen & Eriksson, 2009). However, terminology and definitional consistency seems to be emerging around what has been proposed by UNCTAD (2004). In simple terms, offshoring refers to the relocation of one or more processes or functions to a foreign location (Deloitte Consulting, 2008). This relocation can be carried out either in-house, as a tied or captive form of operations via the firm's own subsidiary; or through the use of an independent external supplier in the foreign market (what we refer to as outsourcing). Thus, in this article, we concentrate on the latter category: international or offshore outsourcing (Kedia & Lahiri, 2007). Effectively, through offshore outsourcing, a company is able to tap into another company's production facilities and/or service provision capacities in a foreign location (Ahearne & Kothandaraman, 2009).

In this article we analyze offshore outsourcing in a broader and longitudinal foreign operation mode context (Benito, Petersen & Welch, 2009). To our knowledge this is the first attempt to do so. Our unit of analysis is not just the offshore outsourcing operation, but includes the type of changes associated with its use that lead to operation mode alteration in the host country over a certain span of time, including within mode change. Given the lack of previous research on these issues, our study is exploratory, both conceptually and empirically, although we draw on the extensive literature on foreign operation modes (reviewed in Welch et al., 2007). The focus on a single case, the Danish company SimCorp's development of operations in Kiev, allowed us to explore the

dynamic processes in depth.

A key contribution of our analysis is to show the ways in which the process of offshore outsourcing may support a company's ongoing foreign operation mode development path(s), firmly placing the issue in an internationalization context, including the consideration of its use early or later in the development of international operations. We uncover some of the mechanisms underlying foreign operation mode changes, and show how outsourcing can lead to various forms of organizational learning and relational outcomes which may facilitate the extension of outsourcing activities or lead to new foreign organizational arrangements that perversely might involve the demise of outsourcing. In doing so, we change the focus away from cost reduction. Empirically, we contribute by providing an in-depth case investigation of outsourcing in the services area: bringing an insight into the process (from initial outsourcing idea to eventual subsidiary establishment) and the co-evolutionary factors that over time underpinned eventual mode change, considered from the perspectives of both contractees (in Kiev), the contractor (HQ and project management staff in Kiev), and the external consultant. In doing so, we follow Lewin and Volberda's (2011: 241) "plea for a more encompassing, co-evolutionary perspective of global sourcing stressing the interactions between managerial intentionality, path-dependent experience and knowledge accumulation, as well as the institutional and selection forces". Specifically, we unpick the type of learning and its links arising from outsourcing that support eventual mode change. While the internationalization process model stresses the importance of learning as a driver of international progression (via eg mode change), with an emphasis on experiential learning, the elements of relevant learning have not been well established, even less so with regard to the place of outsourcing in this overall picture.

Our article is organized as follows: we begin with a brief discussion of the broadening of strategic roles for outsourcing in companies' international operations. We then set offshore outsourcing within the context of firm internationalization – both as an initial foreign market activity, and as a subsequent step. SimCorp's evolving operations in Kiev are described and analyzed. We conclude with case findings and analysis, including the

development of a conceptual framework, and outline managerial and research implications.

2. Changing focus in offshore outsourcing: from cost to competence

Much of the extant literature on offshore outsourcing traces its development and explains its rise (Trent & Monczka, 2003, 2005), although recently going beyond explanations that concentrate on relevant cost differences between countries (Bunyaratavej et al., 2007; Kinkel, 2012). ORN (Offshoring Research Network) survey results – which trace developments over time through annual surveys (see e.g. Lewin et al., 2009) – indicate that companies are thinking about outsourcing at a more general strategic level: 'more and more companies are formulating and disseminating corporate-wide strategies for guiding outsourcing and offshoring decisions …and are integrating offshoring decisions into the overall corporate strategy' (Manning et al., 2008, 49). While governments in general have exhibited concern about, even attempting to restrain, the extent of outsourcing because of concerns about domestic job losses, at the same time there has been recognition of the need to use outsourcing as a means of accessing the global pool of skilled talent in areas of domestic shortage – even by governments (Lewin et al., 2009). Carson (2007: 49) comments that 'firms increasingly outsource new product development activities to external organizations…the popularity of outsourcing is due in part to firms' ability to reduce development costs, shorten time to market, improve flexibility, and gain access to the specialized resources of external suppliers'. This seems to be applicable in many fields, including software and IT services (Lewin et al., 2009).

From a company perspective, the appeal of outsourcing's potential to reduce costs is understandable – as is the interest in outsourcing's capacity to relieve shortages of high level manpower (Manning et al., 2008). The popularity of outsourcing solutions to such concerns (Kshetri, 2007), has nevertheless led other researchers to raise questions about the possible impact on a company's basic competitive core competence (Liu et al., 2011). However, the role of outsourcing as a legitimate means of entering and servicing different markets in the longer term, as an alternative or complement to foreign direct investment,

alliance arrangements, licensing and the like, and its role in operation mode development, has received far less attention (Welch et al., 2007; see also Johanson & Vahlne, 2009).

3. Outsourcing and internationalization

We focus on the way companies can use outsourcing to service foreign markets, on entry and beyond, and, through this, its impact on companies' internationalization. While going beyond the argument about cost reduction, we recognize that cost reduction may have some important flow-on implications for international expansion capacity and strategic options – for example through its impact on a company's international competitiveness (see e.g. Di Gregorio, Musteen & Thomas, 2009). Further, for many companies using outsourcing there is no interest in going beyond basic contractual arrangements. For example, large US retailers such as Toys 'R' Us and Liz Claiborne, are not using outsourcing as a path to other forms of international operations (Einhorn 2009). There are many cases of foreign outsourcing of manufacturing or servicing where the outsourcer merely plugs the product or service back into one minor part of its overall domestic value chain and will never have the scope or interest to develop the operation as an end in itself – it has an insignificant place in overall operations. In such circumstances, it would be highly unlikely for offshore outsourcing to be used or even considered as a springboard to expanded international operations.

In much of the literature, offshore outsourcing tends to be treated as an act, rather than as part of an ongoing, evolving process. An exception is Manning et al. (2008: 49), who stress the way in which offshoring, including outsourcing, is evolving in response to the development of relevant outsourcing capabilities within companies; being exposed to various related challenges; and finding 'new opportunities, such as the rise of new locations in the offshoring space and the emergence of new specialized external service providers' (see also Kotabe, Mol & Ketkar, 2008). Similarly we emphasize the dynamics of offshore outsourcing: co-evolving with a company's internationalization strategy, both influencing and being influenced by this strategy; and as part of a company's set of evolving operation modes in different foreign markets. It should be noted that offshore outsourcing may not be operating as a sole mode, and as a separate activity, in a given

foreign market, but may be in joint operation with other activities and modes – that is, as part of an integrated mode package (Benito et al., 2009). For example, outsourcing could be tied to a licensing arrangement with the foreign contractee.

3.1 Offshore outsourcing as the first international step

Despite its role as a common starting point in international operations provider (Welch & Luostarinen, 1993; Holmlund, Kock & Vanyushyn, 2007), there has been surprisingly little research on offshore outsourcing as a mode of international entry, and of the longer-term international consequences of this establishment role. As a triggering factor in a company's international start, offshore outsourcing may have implications for later internationalization that go well beyond the act itself. The emerging research on inward-outward connections in internationalization is suggestive of the different ways in which offshore outsourcing might contribute to expanded forms of foreign operations (Karlsen et al. 2003). It might involve contributions such as: basic international exposure to potential clients, on both inward and outward sides; network development in the foreign market; learning about, and developing skills in, various aspects of international operations that are transferable to other forms of international operations; and cross-cultural exposure. It is conceivable that a company starts with offshore outsourcing as an inward-oriented activity, but adds outward-oriented operations from its international outsourced base in the foreign market – servicing the contractee's market or third markets. However, research on inward-outward connections indicates that the connections may not be straightforward, often involving varied, indirect and opaque links over time (Welch & Luostarinen, 1993).

3.2 Offshore outsourcing as a later step

Contractual arrangements in various forms are often used as stepping stones to alternative mode arrangements in companies' international expansion processes (Welch et al., 2007). Contractual arrangements can even include clauses which facilitate later takeover (Petersen, Welch & Welch, 2000). In some cases, offshore outsourcing may perform its most important role as a foundation for penetration of a given foreign market, rather than as a source of any short term cost advantages. For companies that are engaged in varied

mode use in different parts of the value chain in a given foreign market, it may be relatively straightforward to move into, or out of, outsourcing with regard to one part of the value chain, especially if outsourcing experience and knowledge have already been acquired in other markets (Mudambi, 2008; Welch et al., 2007). Grote and Täube (2007), focusing on financial research activities, concluded that the ability to do so depended on the strength of ties to other parts and processes within a company.

Offshore outsourcing may be introduced into international operations at any stage in a company's foreign expansion beyond its starting point: the longer, deeper and more expansive a company's international involvement the more substantial the international experience base which a company can work from in establishing the outsourcing activity. There might be some cases where there is little value from past experience (as our case company SimCorp found**;** see also Karlsen et al. 2003), but others where the base is so long standing and substantial as to make for a relatively easy path into the new operation mode. The outsourcing could be fitted closely with preceding operations in a given foreign market, as part of a comprehensive mode package (Benito et al., 2009) or the connections may range to the point of almost full independence or disconnection, thereby ensuring limited support from the pre-existing operation. For example, divisions of the Norwegian multinational Norsk Hydro developed operations in India independently of each other – with limited utilisation of the others' experiences (Tomassen, Welch & Benito, 1998). The idea that the experiential learning generated by outsourcing on many fronts over time might contribute to operation mode development is in line with the so-called Uppsala process model of firm internationalization which has experiential learning as one of its key process drivers (Johanson & Vahlne, 1977, 2006, 2009). We now turn to the study of the Danish company SimCorp and its use of foreign outsourcing as a means of supporting its core software development activities.

4. The SimCorp case: Methodology

4.1. Research design and data collection

Given the paucity of prior research, we considered an exploratory study as the appropriate initial step in investigating the phenomenon of offshore outsourcing in a

dynamic mode development perspective. Eisenhardt (1989, 548: 9) has argued that case study research is especially 'appropriate in the early stages of research on a topic…or research areas for which existing theory seems inadequate' (see also Patton, 1990). However, we regard the study as not being merely exploratory as we were seeking to explain the process of outsourcing adoption through to the establishment of a subsidiary in Ukraine. Case studies are particularly suited to explanatory approaches – including "causal" explanations (Piekkari, Welch & Paavilainen, 2009: 571; Welch et al., 2011).

Case study approaches are also useful when trying to follow longitudinal patterns and processes of some complexity (Patton, 1990; Pratt, 2009; Blazejewski, 2011; Soulsby & Clark, 2011), as in this study, in which we retrospectively studied the outsourcing development over a number of years from its inception in SimCorp HQ in Copenhagen (2002) to ultimate subsidiary establishment in Kiev (2007) and beyond. Case study research has long been regarded as a suitable research approach when the focus of research is on "how" and "why" questions (Yin, 2003; Ghauri, 2004), and these were critical questions for our study as we sought to understand how SimCorp came to be involved in and went about outsourcing, the driving forces behind this move, and the process that led it to eventually replace its independent suppliers with its own subsidiary. While there is some controversy surrounding the term longitudinal study, we follow Blazejewski's (2011: 256) classification, using an "*ex post*" temporal perspective in that the investigation took place after the events in question, with the interviews, fact checking, and documentation and information searches being undertaken subsequently over about a two year period (2009-2011). Burgelman (2011: 594) comments that "historical methods…are inherently concerned with longitudinal development , and involve reconstructing the unfolding of individual and collective action patterns leading up to relatively unique events" (see Siggelkow's (2001: 839) "longitudinal study" of US clothing company Liz Claiborne).

An important reason for the choice of the case company SimCorp was the in-depth access to those involved in the outsourcing decision-making and its implementation, and to a number of employees at the Ukrainian contractees – that is, purposeful sampling was

undertaken. Patton (1990: 169) has argued that "the logic and power of purposeful sampling lies in selecting *information-rich* cases for study in depth" (see also Eisenhardt, 1989 & Yin, 2003). This also supported the longitudinal approach to the study. Further, the triangulation of informants was an important way of validating the case study data (Piekkari, Plakoyiannaki & Welch, 2010; Yin 2003). Access to the informants at the Ukrainian contractees was particularly helpful in contextualization. Piekkari et al. (2009: 572) stress that single cases may provide benefits such as "rich, contextual insights into the dynamics of phenomena", in contrast to the "thin description" that might apply in multiple case approaches. Further, data triangulation was assisted through access to documentary and secondary data made available by SimCorp – including administrative records, internal memos, reports and contractual agreements entered into.

In methodological terms the company and the situation surrounding the use of outsourcing and the eventual move to subsidiary establishment can be seen as representing a "critical" case dealing with the phenomenon under investigation – the role of outsourcing in foreign operation development (Eisenhardt, 1989; Patton, 1990). The benefit of such a single case investigation was the opportunity to delve more deeply into processual aspects of SimCorp's Ukrainian venture. Single cases trade the comparative insights of a multiple case study for such an in-depth approach (Dyer & Wilkins, 1991). Piekkari et al. (2010) argue that for processual investigations, in-depth case studies are particularly useful in exposing dynamic influences (see also Piekkari et al, 2009). Single cases are also useful for in-depth, exploratory investigations with the aim of theoretical extension (Ghauri, 2004).

We used an abductive approach in case analysis (Alvesson & Kärreman, 2007; Dubois & Gadde, 2002; Van Maanen, Sørensen & Mitchell, 2007). Dubois and Gadde (2002: 554) use the term "systematic combining", wherein "research issues and the analytical framework are successively reoriented when they are confronted with the empirical world", as an example of so-called "abductive" logic in research. For example, the empirical investigation, which revealed various forms of adaptation by SimCorp as the Ukrainian operation got underway, led back to a stronger focus on the nature of the

learning processes in explaining the evolution of outsourcing activities and mode change, bearing in mind that, for the company under investigation, this was a step into the unknown at two levels: the type of market (former Communist state) and the mode (offshore outsourcing). These aspects inevitably pointed to the type of processual explanations stressed in internationalization theory (Johanson & Vahlne, 2009). As Alvesson & Kärreman (2007: 1266) argue, the empirical material became a "dialogue partner" with the developing explanations of the evolution of SimCorp's outsourcing operation. This process was assisted by a final meeting with one of the key informants at some time removed from the initial interviews.

The primary interviews with key informants were conducted over a three month period in 2009 by one of the authors. Each interview lasted about an hour, and was recorded and transcribed. Interviews were conducted in the local language (Danish and Ukrainian), then translated into English by the interviewer. Prior to the interviews each informant was sent a list of guideline questions and themes to be covered in the interview. It is traditional to conduct exploratory studies by using open and unstructured interviews. However, for the purpose of our research it was decided to use *semi-structured* interviews - discussions, meaning that each respondent prior to an interview would receive a set of pre-defined guiding questions in order to lay a direction of a discussion. However, the pre-defined questions were not followed strictly in order to allow interview discussions to emerge and progress in a natural way thus giving the respondents a possibility to easily recollect their memories and the events that took place in the past. Questions varied depending on the group and status of the respondents, but all respondents were asked to reflect on the general nature of their engagement in the SimCorp offshore outsourcing venture and then by answering guiding questions created an individual account of the offshore outsourcing process in the chronological order starting from the internal decision making process (asked where relevant) through the entire process development and finally ending by the establishment of the own subsidiary in Ukraine. Thus, the key chronological periods - Outsourcing project (2005 – 2007), Establishment of own subsidiary (2007 – 2008) and Post-integration phase (2008 – ongoing) - were later on identified as a main coding element and used for processing and analyzing the interview

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findings. Langley (1999: 703) refers to this approach as a "temporal bracketing strategy". Nevertheless, themes that began to emerge, such as learning and HRM responses, became a stronger focus of questioning.

The same coding and analysis processes were followed across all three stages, ensuring that key milestones of the single phases (such as the decision to outsource, the pilot project, contractual negotiations and the JV option, the staff transfer agreement etc.) were correctly identified from each interview account and analyzed respecting both the chronological order of occurrences as well as the roles of the respondents. Two of the research team members were involved in the coding process, thus providing analytical triangulation (Patton, 1990). Further, the factual information regarding dates, positions, contractual agreements and terms was later on verified and triangulated by the means of secondary data.

Those interviewed were:

- the head of the software development unit at SimCorp headquarters (until 2008);

- the outsourcing project manager (2005-2007) who re-located to Kiev after initially managing the project from Copenhagen;

- the managing directors of the two Ukrainian contractees Infopulse and ProFIX;

- four employees of SimCorp Ukraine who worked at the contractees on SimCorp projects and later shifted to SimCorp's subsidiary operation;

- the representative of the consulting firm who was involved in the original decision-making process that led to the selection of Ukraine and the contractees. This person eventually became an employee of SimCorp in February, 2008 (subsidiary manager), and then a vice-president of the company. He was a particularly important source because of having both outsider and insider perspectives on the outsourcing venture from the early stages, although not on the initial decision to pursue outsourcing. He made himself available for checking facts and adding information when this was sought after the initial interview. Three of the authors had a follow-up meeting with him at SimCorp headquarters in Copenhagen in 2011 (7 April) at which our initial findings were presented and some minor factual details clarified. He left SimCorp in March, 2012.

4.2 The company

SimCorp is a Danish company, specializing in financial services software. Its revenue in 2010 was EUR 185.4 million. In 2010 it had nineteen foreign subsidiaries and branches, including the one in Ukraine. In 2001, when the company first began to exploring outsourcing as an option it already had established subsidiaries in nine countries. Revenue is derived from three main forms: sales of software licenses, maintenance income and fees from professional services. SimCorp's main product – SimCorp Dimension – is a comprehensive system solution for professional investment managers that support all the elements of the investment management process. It accounted for approximately 95% of the Group's business. Table 1 summarizes the evolution in SimCorp's operations in the Ukraine: from offshore outsourcing to the establishment of its own subsidiary, although the initial idea occurred far earlier.

***** Table 1 about here *****

5. The outsourcing decision and implementation

5.1 Initial considerations

During winter 2001/2002, SimCorp's management for the first time considered the idea of outsourcing part of its software development work. It was initiated in the software development department (IMS Development) primarily because the market for good IT software developers and engineers had become tighter in Denmark. Consequently, it seemed reasonable to consider moving the future growth of development capacity to a place with lower costs. In a study of 31 Indian companies in the business process outsourcing sector, Lahiri and Kedia (2011) similarly found that skills shortages and escalating costs were contributing factors to client firms engaging in outsourcing. Another study was able to differentiate motives by size of offshoring firms finding that cost factors were more important for large and small companies, but "resource drivers" were stronger factors for medium- and large-sized companies (Roza, Van den Bosch & Volberda, 2011, 314). The cost factor was quite important as, at that time, SimCorp was struggling to match revenues and rapidly growing expenses. SimCorp's senior management team decided to investigate the general prospects of offshore outsourcing,

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and to establish a profile of an appropriate offshore outsourcing partner in the near geographical area. It was decided that a potential partner should be located within 2-3 hours flight distance from Copenhagen in order to be able to maintain close contact without being constrained by the long travelling hours.

In 2002 Russia was investigated. The move to outsource part of their software development, while investigated internally, was *facilitated* by a government program called 'Mind Match' which actively promoted outsourcing possibilities for Danish firms. The company was invited to take part in Danish government organized seminars and to meet with potential partners in Saint Petersburg in 2002 as part of its investigation of outsourcing options. However, suitable candidates were not found in terms of data security, available infrastructure, educational level, managerial competencies, price level, and communication capacity (eg English skills). Furthermore, the company's management realized that SimCorp was not ready to deal with all the challenges of an offshore outsourcing venture. As a result, SimCorp turned its attention back to the domestic market, looking for possible qualified partners among Danish firms in order to try out outsourcing possibilities without the perceived major challenges and risks stemming from offshore outsourcing. This did not work out either, as SimCorp was again unable to find suitable partners. Thus, after some consideration, SimCorp's senior management team (SMT) decided to postpone the decision about any form of outsourcing. An internal evaluation at that point in time showed the company was not fully ready to carry out an outsourcing project. However, during the period up to autumn 2004 it became even harder to find qualified IT programmers in Denmark, which brought the outsourcing discussion back on the table. SimCorp's management decided to start a new investigation of offshore outsourcing opportunities. For this purpose, it hired a consultancy firm, Developmate, which specialized in IT offshore outsourcing, to conduct a thorough examination of outsourcing possibilities in cooperation with SimCorp management. After initial screening and a thorough country investigation by Developmate, SimCorp's management decided to proceed with Ukraine, which resulted in further screening of the market for potential suitable contractees (or partners as they were called). Following the partner screening process, the representatives from

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SimCorp's senior management group and IMS Development department paid a number of visits to three Ukrainian companies of interest in February 2005. In the decision process, SimCorp always wanted to have more than one cooperation partner in the same area. This was considered crucial in order to be able to balance and compare service providers against each other in terms of price and quality of work, as well as stimulate a continuous positive rivalry among the partners. Another aspect equally important for SimCorp in this regard was to diversify the risk of becoming too dependent on one particular partner.

5.2 The pilot project

The selection process led to the choice of two companies, Infopulse and ProFIX. SimCorp started carrying through pilot projects with them on a probationary basis. The parties signed a Memorandum of Understanding (MoU), which outlined the terms and conditions of the projects and probation period. The MoU outlined also the initial framework for future potential cooperation between SimCorp and the Ukrainian service providers. This included three phases: 1) the pilot project phase; if successful this would lead to 2) a long-term cooperation phase; potentially followed by 3) the exercise of a joint venture option with the service provider. The pilot project set-up had the following conditions: A duration period of approximately three months; involvement of 4-5 full-time software engineers who would receive extensive training at SimCorp premises in Copenhagen. Upon completion of the pilot project, results would be evaluated by SimCorp's senior management and benchmarked against the standards of newly employed Danish candidates as well as against other external consultants used by SimCorp. SimCorp additionally secured the intellectual property rights on all material conceived, discovered or produced in connection with the pilot project. If the arrangement did not work out, each party was to cover their own part of the costs and cease cooperation.

5.3 Long-term cooperation

After both pilot projects produced satisfactory results, during the autumn of 2005 SimCorp and both service providers had a number of negotiations over entering the next

phase of long-term cooperation - in essence continuing the outsourcing cooperation between SimCorp and Infopulse and ProFIX. The partner firms were to provide the services of searching, selecting and recruiting new, qualified candidates for the SimCorp development teams, and to provide the physical environment, technical support and infrastructure. As successful completion of the pilot project was a precondition for further cooperation, a number of terms and conditions were not finalised in the initial MoU, which required further negotiations after completion of the pilot project phase. The legal contract signed between the parties was an extended version of the original MoU. The Cooperation Agreement outlined the important conditions for long-term outsourcing cooperation and the rights and responsibilities of each party. Accordingly, the service providers were obliged to commit named and specified resources to the SimCorp development team based on SimCorp's specifications. In its turn, SimCorp was responsible for providing the necessary training and education of the vendors' personnel.

In November 2005 SimCorp expatriated its outsourcing project manager to Kiev in order to better coordinate and control the offshore development. It had become more and more difficult to manage the operation from Copenhagen. A person was needed in Kiev who could ensure SimCorp control, help Ukrainian project staff understand "the SimCorp way" of doing things, and ensure good communication flow between Kiev and Copenhagen. Two more employees from SimCorp Denmark were expatriated to Kiev during 2006. SimCorp had attempted to head off potential control problems through the terms of its partner (contractee) contracts. For example, the service providers were obliged to commit named and specified resources to the SimCorp development team based on SimCorp's specifications. However, SimCorp was not able to anticipate the full gamut of issues that emerged, particularly in relation to its ability to manage the Ukrainian software developers, their work and employment conditions: these were not directly controllable because it was dealing with independent entities. Establishment of its training facility (SimCorp Academy) in Kiev in 2006 allowed the company to achieve a measure of control over the training and development of local staff.

5.4 Subsidiary establishment

SimCorp established a wholly-owned subsidiary in Ukraine in 2007. The company had been building towards this step through the range of internalization steps (noted above) already made in seeking to achieve greater control over its Ukrainian operations undertaken through its partner firms. Without such actions, it is arguable whether SimCorp would have preferred subsidiary establishment to a joint venture arrangement. After deciding to do so, it negotiated an agreement that would allow the company to "acquire" the service providers' personnel and transfer them to the newly established entity. As SimCorp did not have a clause in the Cooperation Agreement that would specify the terms for establishment of a wholly-owned subsidiary and transfer of resources, an addendum to the original cooperation contract was negotiated and put in place. Further a clause was inserted in the addendum to cover future HR cooperation – specifically concerning help in finding suitable staff.

6. Case analysis and findings

A number of key interactive dynamic factors emerged from the case data as influential in the change in mode stance by SimCorp, and ultimate change in operation method. They were dynamic in the sense that they evolved over time as a result of SimCorp's experience with using outsourcing in Ukraine. We now examine these factors and changes in them that impacted on operation mode decision-making.

6.1 Learning

A key factor in mode change for SimCorp was learning (Johanson & Vahlne, 1977, 2006; Kenney, Massini & Murtha, 2009. Because SimCorp lacked previous experience with outsourcing, of Ukrainian operations, and with the partners (contractees) chosen, it was engaged in mode, contextual and partner learning. Although the main focus in this article is on the mode learning which underpinned eventual mode change, we acknowledge the interactive effects of partner and contextual learning. For example, partner learning was important in demonstrating the extent to which SimCorp had to become directly involved in Ukrainian operations in various ways beyond simple outsourcing in order to assure the quality of the software being developed. SimCorp quickly learned that despite engaging in outsourcing, the operation needed to be relation-intensive. Contextual learning was

also important in assisting SimCorp to adapt the way it treated Ukrainian software developers. The unfolding learning process was critical to its assessment of future mode development possibilities. The pilot project formed an important base: it was viewed by SimCorp management as a way of allowing experimentation without long-term commitment. It provided a low-risk platform for learning about the practicalities and demands of outsourcing, as well as the potential for a more substantial, long-term commitment. One key aspect was for SimCorp to be assured that it could effectively teach Ukrainian staff to work with SimCorp's software development platform. The project manager commented: "*It is a quite special system and a programming language [APL] that is not so well-known, which needed to be learnt first*". There were unintended learning benefits from the first project (with Infopulse) to the second (with ProFix) because of a delay in starting the latter. Feedback from running the first project ensured that SimCorp was more prepared to start the second project, as well as equipping the company with a concrete assessment tool that had already been proven to work. A high level of interaction between the parties, and movement between Copenhagen and Kiev, as cooperation developed over time, facilitated the learning process on both sides, and in both locations.

***** Figure 1 about here *****

The different aspects of mode learning experienced by SimCorp, and supporting mode change, are depicted in Figure 1. The learning components noted on the left-hand side of the figure are case derived. Some of the learning was fortuitous, some deliberate. SimCorp was very conscious of the need to find ways to build effective communication between its software development unit in Copenhagen and its Ukrainian contractees to ensure acceptable quality of the end-product. The inclusion of a joint venture option in its cooperation agreement was indicative of a preparedness to vary its approach on the basis of feedback from the outsourcing operations. But much of the learning was not deliberate. For example, various aspects of contextual learning and ways of managing people issues evolved with experience, as did the realisation that a SimCorp project manager needed to be stationed in Kiev along with a formal training facility. SimCorp

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fed its early experience with its first contractee into the arrangement with its second contractee. March (1991: 71) points out that exploratory learning includes elements such as 'variation, risk taking, experimentation, flexibility and innovation' which were all present in SimCorp's approach to using outsourcing. However, 'organizational learning is a dynamic and integrative concept' (Dodgson, 1993: 376) and it is a linked concept: it does not occur in a vacuum – it is dynamic in the context of other related changes. Thus, in Figure 1 we show a link to other co-evolving mode influences that contributed to and were affected by mode specific learning. For example, emerging control concerns led to the search for ways of exercising greater control of the outsourcing operation in Kiev, and implementation of additional control measures. As SimCorp sought to bring about greater control over its Ukrainian operations, it was effectively establishing a case for a wholly-owned subsidiary rather than a joint venture. In the end, control was a decisive factor in dropping the joint venture option. Moreover, it had been building the type of management skills (e.g. human resource management) that it could use in an owned subsidiary operation.

6.2 Control

Control has featured as an important factor in foreign operation mode decision studies, but its co-evolution and interaction over time with other influences such as those in this study have received more limited attention (Hill, Hwang & Kim, 1990; Benito et al., 2009). Interaction with other dynamic influences can infuse control concerns with greater substance and meaning. For example, feedback and learning from experience may heighten control concerns, as indicated in Figure 2, which in turn may lead to a re-consideration of how a company operates in a foreign location. According to Harmancioglu (2009: 395) "Control mechanisms are broadly divided into formal versus informal…formal controls rely on written mechanisms informal control mechanisms (such as social norms, peer pressure, shared beliefs and experiences) utilize social strategies to reduce goal differences between the principal (buyer) and agent (supplier)". In Figure 2 we distinguish between control measures and relational actions, which broadly correspond to the formal versus informal categorization. The control and relational components noted on the left-hand side of the figure are case derived.

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***** Figure 2 about here *****

Our case analysis suggests that HRM considerations came to be seen as more important over time, exposing the limitations of SimCorp's control over management of the outsourcing operation – and leading to rising concern about how to get on top of the 'problem'. It appears that SimCorp had sought to internalize and control the activities of its contractees in various ways – including what might be called 'soft' informal control measures, such as in the emphasis on implanting its 'performance culture'.

In addition to changing control concerns it took time for SimCorp to uncover what the relevant control levers were, or should be. As pointed out by Carson (2007: 61): "Incomplete contracting theory indicates that parties subject to bounded rationality will not be able to anticipate future conditions adequately and formalize a plan to work in complex environments, such as product development". Our case certainly supports Carson's broad idea – particularly in conditions of genuine uncertainty. A feasible outcome is mode change to get rid of the original contract once the realities of the type of control considered necessary are exposed through experience. Buvik and John (2000: 53) also stress incomplete contracting theory and the impact of uncertainty: "unforeseen contingencies cannot be addressed by writing more complex, contingent (complete) contracts". Buvik and John suggest that trying to come up with complete contracts prevents firms from responding flexibly and profitably to emergent circumstances. This points to the benefit of having incomplete contracts, but they add: "incomplete contracts can work only within supportive governance structures" (Buvik & John, 2000: 53). In our case the supportive structure to the contract was an evolving informal (soft – e.g. relational) one, but also included more formal ones such as expatriate appointments and setting up the training institute. In the end though, despite the various control measures brought into use as the operation evolved, dispensing with the contractual arrangement and setting up a subsidiary was deemed to be the most appropriate governance structure for ensuring control.

6.3 Partner relationships, trust and mutual adaptation

Communication between the parties intensified as the operation moved beyond the initial pilot project activities. To some extent this was a by-product of the type of activity being outsourced – software development – which ensured that there had to be a high level of personal interaction between HQ development teams and those in Kiev. In addition, HQ management was actively involved in managing activities and relationships in Kiev. Initially this was accomplished through travelling staff, then through expatriate appointments. SimCorp consciously sought to drive this process of interaction through different integrative steps, structural and social, with the aim of fostering communication. Development employees in Ukraine were divided into groups according to the organization structure in SimCorp and had direct communication with their respective teams in Copenhagen. Thus, despite being an outsourcing project, close day-to-day interaction and involvement between the offshore operation and SimCorp developed. The strength of relational development with its two Ukrainian partners was critical in enabling SimCorp to enact so many of its policies including some that were not covered under the terms of the Cooperation Agreement. However, the positive communication and staff interaction that took place did not occur in a vacuum: they evolved and depended on a supportive relational context between the parties. There was a process of mutual adaptation between the parties as relations developed. This was most evident in the key area of training and staff deployment – in Kiev and Copenhagen. Cooperation between the SimCorp development teams in Kiev and IMS Development in Denmark increased gradually as training of the people in Kiev progressed and they started to become more competent and specialised in working for SimCorp. Such adaptations increase commitment on both sides and can become part of a base for extended collaboration, as happened in this case (Madhok, 1995). Over time, this became characterised by trust, to the extent that it was a facilitator of the move to a wholly-owned subsidiary: it supported a continuation of cooperation between the parties in the area of staffing even after the subsidiary was established.

Kedia and Lahiri (2007) point to the contribution of trustworthiness to the development of long term cooperation in outsourcing relationships. As Gainey and Klaas (2003: 209)

stress, 'while an outsourcing arrangement may begin as an arm's-length relationship, disciplined only through market-based mechanisms, over time it may be transformed through a social exchange process'. In their study, they found a positive connection between trust and outsourcer satisfaction with outsourcing, while trust was positively related with relationship tenure and communication behaviour. In the case of SimCorp and its Ukrainian partners, although they began with a long term perspective, the development of trust was critical to subsequent commitments. Given SimCorp's action in not going ahead with the JV option, it might have expected a less cooperative response by its Ukrainian contractees were it not for the relational trust engendered by their positive dealings.

Language was a further aspect of adaptation. Ukrainian staff in general did not speak English fluently, but SimCorp required English proficiency for every member of the development teams. This was somewhat atypical for ProFIX, which used to work with projects where only a couple of people were required to speak the language and they served as a communication channel for the rest of the group. Nevertheless, because SimCorp was offering interesting and challenging work, people were motivated to invest time to improve their English proficiency. Infopulse management offered English courses at the company's expense for upgrading language skills if SimCorp found technically appropriate candidates among Infopulse staff who lacked English communication skills.

6.4 HRM issues and confidentiality requirements
Staff retention and confidentiality requirements were dynamic influences that emerged strongly from the case data. Given the service business that SimCorp was involved in, people were key, and they could leave at any time, so the need to control the HR levers was recognized very early. The move to a subsidiary operation was almost an inevitable end point once this was clearly recognized and commitment to the Ukrainian operation firmly established within the company. The SimCorp project manager stressed the challenge of retention: *"One of our biggest problems in cooperation with partners was the fact that we did not have control over the employee salary. The partners did. And it was sometimes difficult, as there were cases, where we would like to retain [people] also*

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on higher salary, but because partners did not want to give the salary increase, we would lose those people, and it was too bad". Similarly, the head of the SimCorp development unit related: *"the whole establishment of own subsidiary … would give us opportunities to make certain things (happen), which we could not do because we worked with partners i.e. differentiate people's salary, retain and motivate people"*.

Even more important for the decision to move to a subsidiary operation were the restrictions on using 3rd party development resources for client support. As a result of their surprisingly quick upgrading, the time arrived when it would be natural to let the teams of the two partner firms collaborate directly with SimCorp's clients around customizing their software. However, given the confidentiality of the information held by the clients only SimCorp's own developers were allowed access to the client systems. SimCorp's head of the software development unit expressed the pressing need for employing the Ukrainian system developers in the following way: "*We could not take Ukrainian people and send them to work on projects in Scandinavia, England or other places, as they were not directly employed by SimCorp. This is prohibited according to the contracts we have with our clients. So, we wanted to open up for this possibility [...] to be able to have a resource pool in Ukraine, whose people could be sent for 3-6 months projects to different places. This would be possible without any problems, if they would be employed by SimCorp.*"

6.5 Mode change
The various dynamic, interactive factors examined above are summarized in Fig 3. Their combined, evolving influence was important in moving the company to a stage where mode change was almost a natural next step. While stressing mode learning and control concerns, the other dynamic factors or mechanisms played important contributory and interactive roles. Because of the interactivity of the various influences on mode change, it is difficult to assign primacy to any particular influence. Positive relational development assisted mode learning, but control concerns also arose in connection with these, all helping to bring mode change into focus.

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From a theoretical perspective, co-evolution theory appears to be an appropriate framework for setting mode change in the wake of offshore outsourcing, given its focus on process, and interacting factors in development (see e.g. Cantwell, Dunning & Lundan, 2010; Lewin & Volberda, 1999; Shidu & Volberda, 2011). Pajunen and Maunula (2008: 249) argue that "for a co-evolutionary relation to occur it is necessary that two or more processes must have a noticeable influence on each other's evolution". They apply co-evolution theory to internationalization in general, but the ideas are equally applicable to mode development dynamics. Lewin et al., (2009: 921) have used a co-evolutionary framework, with managerial intentionality, in empirically examining the rise of offshoring in innovation projects. From their empirical data they found support for 'the idea of cumulative experience building' and an important role for managerial intentionality in explaining the development of offshoring. Substantial *within mode change* (Benito et al., 2009) acted as a lead into, and stimulus for, eventual mode change. This took various forms: through various HR activities, including personnel visits, both ways; expatriation of HQ staff members to Kiev; training; and language policies, all of which had the effect of gradually integrating the Ukrainian operations into SimCorp, even though the services were notionally provided by independent Ukrainian companies.

The evolution of trust between SimCorp and its Ukrainian partners provided an important foundation for mode change: the change process was simplified through partner support rather than hostility which might otherwise have been expected. There is evidence that even with shorter term single contract arrangements, outsourcers prefer to develop these deals with trusted suppliers, that is, within the context of longer term relationships (Kakabadse & Kakabadse, 2005). The process of establishing a contractual relationship and of enacting the relationship may open up different possibilities for further forms of cooperation that lead to mode change. These might include, for example, joint activities with the contractee's staff or training and technological exchanges as in the SimCorp case. Such collaborative activities allow for the evolution of knowledge and understanding between the two parties, of adaptations to each other, and the development of trust (Young and Wilkinson, 1989).

The development of trust between parties encourages disclosure and sharing of knowledge, particularly when it involves access to and use of personal networks, thus supporting the learning process (McEvily, Perrone, & Zaheer, 2003; Michailova & Husted, 2003; Welch & Welch, 2008). This contributes to the development of social capital. Thus, as a positive relationship between the outsourcer and foreign contractee develops, embedded within growing social capital, it provides a foundation that supports any consideration of extension of the core outsourcing operation into other arrangements, including more formal types of integration. Ultimately, from this process there might be a substantial foundation for a move to a stronger link. Relationships may develop to such an extent that quasi-integration takes place, facilitating formal internalization steps by the outsourcer (Morgan & Hunt, 1994; Petersen, Welch & Benito 2010). Shidu & Volberda (2011) point to the challenges associated with coordination between the parties and caution against being too optimistic about always achieving positive outcomes. The experience in our case was nevertheless that employees at the contractees and later at the subsidiary seemed happy to adopt SimCorp's culture and ways of doing things – the benefits of 'belonging' were seen as rewarding – eg language training and other work benefits. A Ukrainian employee at one of SimCorp's contractees commented that: *"All this together [bonuses, social events, trips to Copenhagen]… contradicted strongly with the thesis that being an outsourced part we were not a part of the company. This was not the case. We felt ourselves almost equal to SimCorp employees"*.

6.6 Sequential internationalization
In one sense SimCorp's foray into Ukraine via offshore outsourcing proceeded like a classic case of sequential internationalization, despite its preceding range of international experience (Johanson & Vahlne, 1977; Welch & Luostarinen, 1988). The company was unsure about what it should do, even whether the outsourcing step was appropriate or not, with considerable internal debate. Uncertainty was strongly felt by management. This was illustrated by the decision in 2002 to go back to the Danish market to seek local contractees rather than pursue the offshore path once difficulties were exposed. It only re-

launched its offshore search when it became evident that a Danish solution would not be forthcoming. Thus, the processes of adopting offshore outsourcing, the country of choice and the choice of eventual contractees were marked by a high level of caution and concern. Having decided on Ukraine, with external consulting help, it started with two pilot outsourcing arrangements – thereby limiting its commitment, taking an experimental approach to its initial involvement, enabling withdrawal with limited costs if the outcome was deemed unsatisfactory. It clearly viewed much of its international knowledge base as not being readily adaptable to its Ukrainian venture. Nevertheless, it had built up sufficient internal commitment to the new strategy such that it was prepared to declare a serious long term interest in the initial agreement with the Ukrainian contractees – including the possibility of a change to a JV. Such internal commitment development can be as important as the market commitment which is the primary focus of internationalization models. From the outset, there was a recognition that if relations and performance had evolved as hoped the initial outsourcing operation might develop into something more substantial: independent outsourcing was seen as not necessarily the finishing point. The head of SimCorp's software development unit referred to the company's strategy in Ukraine in terms of "*building up the development capacity offshore at low cost*".

Despite the flagging of future mode development via a JV, how the outsourcing operation unfolded was crucial to further commitment, and in the end the path chosen, was not as originally anticipated. Depending on the nature of a company's foreign market involvement through outsourcing, exploitable, new market opportunities beyond the confines of the initial contractual relationship may emerge, within the foreign market and/or beyond (Hatönen & Eriksson, 2009). In SimCorp's case, although heavily involved in the Ukrainian operation, this was relatively narrowly confined so that, for example, learning benefits centered around outsourcing and related activities, and less strongly related to the market in Ukraine.

7. Conclusion

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The SimCorp case demonstrates that offshore outsourcing may involve much more than the outsourcing act itself. This 'more' can be quite substantial, depending on how much the outsourcer becomes involved in the foreign market and with its foreign partner. This is perhaps even more the case with services outsourcing, where there is often considerable focus on training and interaction of staff on both sides to ensure the quality of what is ultimately supplied – with cost implications. Whether it is a starting intention or not, involvement in the foreign market inexorably generates learning in various forms which may build a foundation for eventual mode development or change. Such mode-related learning goes beyond the outsourcing-focused organizational learning noted in other studies (Manning et al., 2008). At the same time the inevitable concern about retention of key personnel at the outsourcing partners (representing significant, sunk investments in training and education), problems of contractual restrictions on the use of 3rd party development resources for client support, aligned with the outsourcer's internal learning processes, eventually became a driver for mode change at SimCorp to ensure more effective control of the foreign operation. However, while we have emphasized learning and control, this does not mean that other dynamic mechanisms are less influential or less interactive – it is the way in which they evolved and influenced responses in each other that in a combined form explain mode change. The factors that emerged in this study may be situation and company specific, but we suspect that they are suggestive of the types of mode change factors that might be found for in other studies of international outsourcing in an operation mode development context.

Our study reveals how outsourcing can be used as a springboard to changed foreign operation mode activity in the host foreign market. Although the shift to captive outsourcing via subsidiary establishment entailed a substantial change in commitment, it could be argued that it was a sequential change: in various ways SimCorp had sought to internalize and control the activities of its contractees – including what might be called 'soft' control measures, such as in the emphasis on implanting its 'performance culture'. These actions prepared SimCorp in such a way that the subsidiary step was not viewed as a major one for the company. SimCorp's Ukrainian experience exposed a number of change influences that emerged, and evolved, in an interactive way, driving its

developing responses through the independent outsourcing stage. A high level of interaction and communication between the parties facilitated evolving trust, lowering perceived risk and uncertainty, supporting the transition to a subsidiary, and continued cooperation. As the company's first step into outsourcing, it was perhaps inevitable that the type of learning would be a key factor in how it reacted and built the Ukrainian operation. Nevertheless, SimCorp began with a perspective that signaled and perhaps colored the nature of its perception of, and responses to, the Ukrainian experience - as indicated by its insertion of a foreshadowed JV option even at the pilot project stage. Thus, the outcome showed strong evidence of both co-evolution and managerial intentionality (Lewin et al., 2009).

The SimCorp experience shows clearly that offshore outsourcing can play an important developmental role in a company's penetration of foreign markets - an aspect of outsourcing that has received little attention in the literature. As a result, offshore outsourcing should be considered alongside other foreign operation modes not merely as a way of lowering costs but potentially as part of a strategic pathway or bridge to extended and deepened internationalization. Thus, outsourcing may perform a useful temporary role, but the more positive its contribution the more substantial the seeds of its own demise. While cost advantages were not stressed as the key factor in the outsourcing move, they were a continuing underlying consideration for SimCorp: the shortage of software development talent in Denmark pushed up remuneration rates, and made Ukraine more attractive. Countering this effect, though, SimCorp experienced a range of costs associated with establishing and running its Ukrainian venture. Some of these costs were associated with ensuring control, such as the expatriation of its project manager to Kiev.

8. Managerial implications and research issues
Offshore outsourcing is an important part of the international business operations picture that is here to stay, and likely to grow rather than diminish, so that it needs to be considered as an integral part of the internationalization strategies of companies. This means placing greater emphasis on both inward and outward sides of international

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activities and their connections. Wherever the drive for offshore outsourcing comes from, its future market development potential needs to be considered at the outset. If deeper future commitment is a possibility, a range of steps need to be taken – including the content of contractual arrangements, a more comprehensive assessment of potential contractees and market options, and possible links to the use of other modes as part of a more substantial mode packaging arrangement for the market in question. Our analysis has shown that companies can use offshore outsourcing in a proactive way in fostering internationalization. It might be feasible for the next step to be set up as an option in the initial contract with the foreign contractee, as SimCorp did, and many companies have done with joint ventures, licensing deals, and intermediary arrangements (Petersen et al., 2000). Importantly though, it requires a change in strategic thinking, to pursue its potential beyond cost reduction - capturing and applying the various learning outcomes from the outsourcing experience. Internalization via equity or other forms of foreign involvement can be facilitated by contractual arrangements that include internalization options. To include mode switching options up front, though, requires a deliberate, planned approach to foreign operation development whereas emergent approaches tend to be more typical. In a study of contracting within the personal computer industry, it was found that contracts evolved over time as relationships between the parties developed and that they exhibited the impact of incremental, experiential learning. In particular, they observed that 'rather than anticipating … problems and contingencies, the parties had to actually experience an adverse situation before addressing it in new contracts' (Mayer & Argyres, 2004, 395).

In this article we have focused on one company's experience, with all the limitations this approach entails, and it was its first foray into outsourcing, in a relatively unknown market area. There is obvious need for this account to be supplemented by others, including those where companies have used outsourcing in different places in their patterns of internationalization, to assess whether there are different types of learning, control and relational experiences leading to mode change. As well, there is a need for examples of companies that have gone on to other mode forms than wholly-owned

subsidiary establishment, such as to JVs or a broader mixed mode approach (Benito et al., 2009).

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Table 1: *Key phases in the development of SimCorp's Ukrainian operation.*

| Phases / Duration	Context of the Relationship	Contracts and Provisions	Use of Options
Pilot project: **Offshore outsourcing** March - August 2005	***Probation period*** To test the parties' compatibility on a small scale project	***Memorandum of Understanding*** Pilot project terms and conditions. Draft version of the contract	***Inherent options*** Option to abandon the project if deemed un-successful (not exercised); Option to expand the project if deemed successful (exercised)
Full cooperation: **Offshore outsourcing** August 2005 – September 2007	***Outsourcing cooperation*** Service providers acting as subcontractors. Search for and selection of qualified personnel. Idiosyncratic investments by SimCorp in training and education. Increasing asset specificity	***Cooperation Agreement*** Legal framework for outsourcing cooperation. Terms and conditions of each party's responsibilities. Option for future cooperation – JV option.	***JV option in the contract*** SimCorp 51% of shares; appoint managing director and chairman of the board (the option was not exercised). ***Implicit options*** staff motivation, retention and integration into SimCorp (partly exercised)
Wholly owned subsidiary establishment; operations and staff transfer Autumn 2007 – May 2009 (including future HR cooperation)	***Integration of human resources*** Taking over the service providers' personnel on a legal basis after establishment of own subsidiary. Option of further transfers after reaching 18 month experience threshold.	***Addendum to Cooperation Agreement*** Extension of the contract to operationalise staff transfer. Option of future cooperation – future HR services.	***Future cooperation option*** Option to transfer, on a selective basis, project staff members to own subsidiary (exercised). Option to use the service providers' assistance in search for, and selection of, new staff candidates (partly exercised).

Figure 1. *Mode learning.*
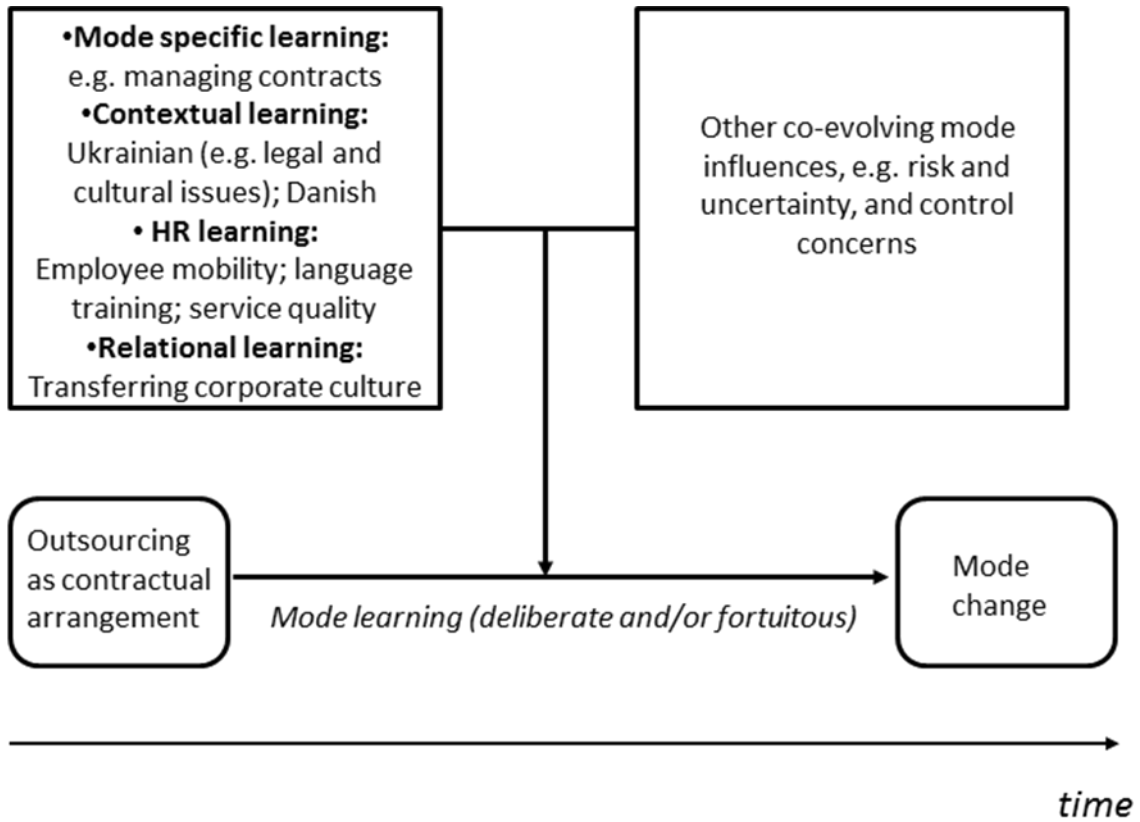
Figure 2. *Evolving control concerns*.
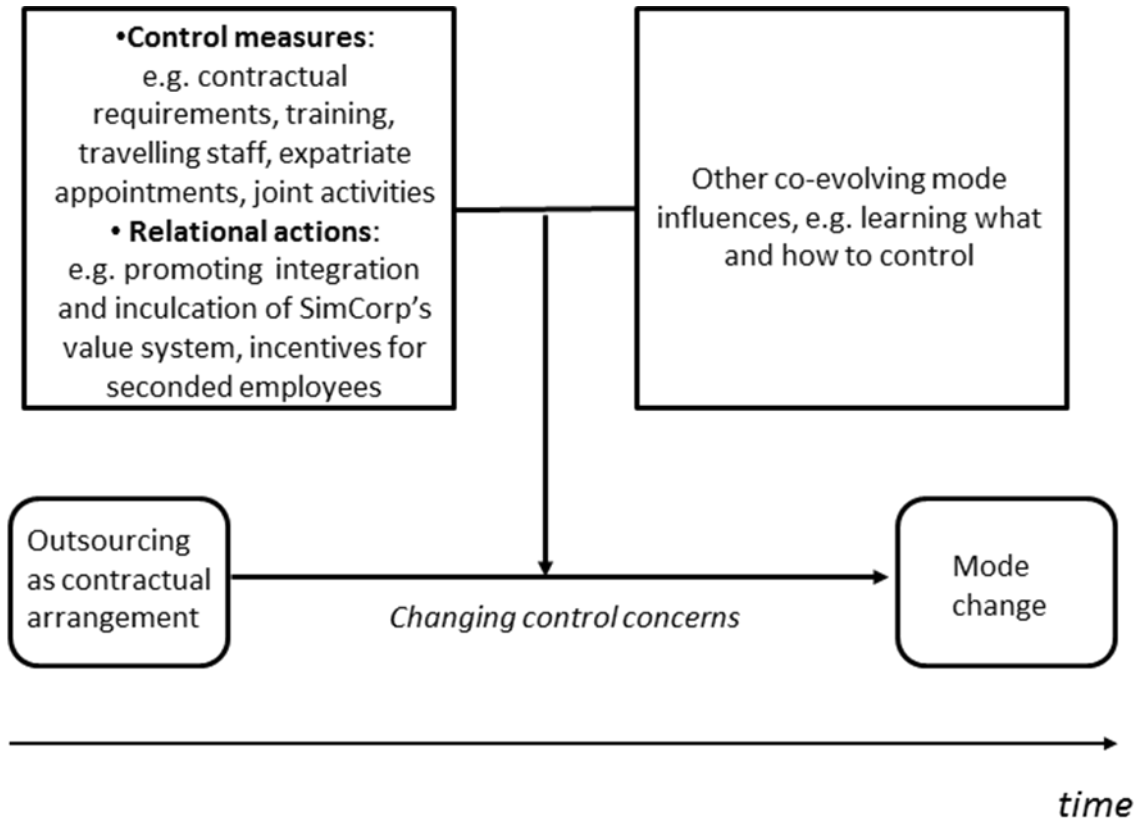
Figure 3. *Offshore outsourcing as a springboard.*