Chapter 2
Country Environments and the Adoption of IT Outsourcing

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ABSTRACT

Research on information technology (IT) outsourcing adoption has been confined to a single-country perspective. The understanding of how country-specific variables influence the adoption of IT outsourcing is limited. This study uses new institutional economics to build a framework that links country-level factors to the adoption of IT domestic outsourcing. The authors suggest that country-level factors, such as the maturity of the IT-related legal system, social trust, uncertainty avoidance, Internet penetration, and the maturity of the IT outsourcing market, affect the opportunism costs and coordination costs involved in domestic IT outsourcing and influence its adoption among firms. The results show that the maturity of the IT-related legal system, social trust, and the maturity of the IT outsourcing market are positively associated with IT outsourcing adoption. The authors conclude the paper with a discussion of the study's implications for practice and future research.

INTRODUCTION

Since the landmark decision by Eastman Kodak to hand over IT functions to IBM, Businessland, and DEC, the practice of outsourcing a firm's IT facilities and services to outside vendors has become increasingly popular (Dibbern et al., 2004). IT outsourcing refers to a significant contribution by external vendors in the physical and/or human resources associated with all or part of the IT infrastructure in the user organization (Loh &

Venkatraman, 1992). In general, IT outsourcing may involve IT functions such as data processing services, communication and network services, facilities management services, application development services, etc. (Cullen, Seddon, & Willcocks, 2005). A report by the Gartner Group indicated that worldwide spending on IT outsourcing would rise rapidly from $268 billion in 2009 to $325 billion in 2013 (Harris et al., 2009). Willcocks et al. (2006) predicted that spending on IT outsourcing will rise by at least 7% per annum over the next five years. While IT outsourcing has recently

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evolved to new forms such as offshore outsourcing (Hahn, Doh, & Bunyaratavej, 2009; Remus & Wiener, 2009; Schwaig, Gillam, & Leeds, 2006), our study focuses on domestic IT outsourcing.

The value of IT outsourcing has been long documented in the literature and it is suggested that IT outsourcing can provide firms with various economic benefits, technological benefits, as well as strategic benefits (Grover, Cheon, & Teng, 1996). For instance, it is suggested that IT outsourcing may reduce IT operation costs, improve technical competence, and increase business value (DiRomualdo & Gurbaxani, 1998; Levina & Ross, 2003). Since IT outsourcing was recognized as one of the most pervasive organizational practices, many studies have investigated factors that affect the adoption of IT outsourcing (Dibbern et al., 2004). Research found that, in general, two groups of factors are key antecedents of IT outsourcing adoption: the attributes of IS functions and the comparative advantages of IT outsourcing over in-house provision of IT services.

Though insightful, research on the adoption of IT outsourcing has been mainly conducted based on a single-country perspective. As a result, we still lack a clear understanding on how country-specific factors influence IT outsourcing adoption. For instance, after reviewing 84 papers on IT outsourcing from 1992 to 2000, Dibbern et al. (2004, p. 90) concluded: "research to date has mainly been confined to a single-country perspective and this neglects the insight to be gained from multinational or cross-cultural research." Similarly, Gonzalez et al. (2006) reviewed IT outsourcing research until 2005 and found that only 1.9% of the studies attempted either to account for national differences or analyze outsourcing in different country contexts.

A few studies have examined the differences in IT outsourcing practices between two or three countries. These studies suggest that the institutional environments (e.g., employee power, norms and common beliefs) and resource environments (e.g., IT supply and demand markets) of a country can affect firm adoption of IT outsourcing (e.g.,

Grimshaw & Miozzo, 2006; Slaughter & Ang, 1995). However, data from two or three countries cannot be used to test the effects of country-level factors on the adoption of IT outsourcing. In order to study these effects, data from more countries are needed. In addition, no research to date has identified important dimensions of country environments for understanding how country influences firm IT outsourcing decisions. In this study, we attempt to address these issues.

Our study contributes to research in several ways. Taking the lens of opportunism costs and coordination costs, our study suggests that country-level factors, such as the maturity of the IT-related legal system, social trust, uncertainty avoidance, Internet penetration, and the maturity of the IT outsourcing market influence firm decisions on IT outsourcing adoption. We expand existing literature by identifying a list of important dimensions of country environments that matter for IT outsourcing and by showing how they affect firm decisions on IT outsourcing adoption. In addition, our research model is tested based on data from 18 countries. Data based on a relatively larger number of countries enable us to study the effects of country environments on IT outsourcing adoption in a relatively robust way.

The rest of paper is structured as follows. We first review the empirical studies investigating the effects of country-level factors on the adoption of IT outsourcing. Based on new institutional economics, we then build a theoretical framework to understand how country-level variables affect firm decisions on IT outsourcing adoption. The framework is then tested using data from several sources. We conclude the paper with a discussion of the implications of the findings and potential future research.

LITERATURE REVIEW

A limited number of studies have investigated the effects of country-specific factors on the adoption of IT outsourcing (see Table 1 for details). Among

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