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# Fagbokforlaget

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*- An Offshoring Case Study*

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Master thesis in Business Analysis and Performance Management

This thesis was written as a part of the Master of Science in Economics and Business Administration at NHH. Neither the institution, the advisor, nor the sensors are - through the approval of this thesis - responsible for neither the theories and methods used, nor results and conclusions drawn in this work.



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## Executive Summary

This thesis is written as part of Master's degree of Science in Economics and Business Administration at the Norwegian School of Economics. Inspiration for this thesis came when attending a course in Outsourcing and Franchising (BUS438) in the spring of 2010.

The paper looks at a successful offshoring project in Poland by the Norwegian publishing company Fagbokforlaget. The success was a result of several factors, some are acknowledged by Fagbokforlaget such as organizational culture and some that FBF are seemingly oblivious about, such as the importance of cultural differences and hence cultural knowledge. This year however they are trying to achieve success abroad again, but this time in India. However success factors are not easily transferred and redeployed in different locations and FBF now faces challenges in India that they were unprepared for and they will have to put down a lot of work to make this second sourcing project a success as well.



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## 1. Introduction

In 2000 the Norwegian publishing company; Fagbokforlaget (FBF) offshored parts of their production, and later also IT services, to Poland when they established the subsidiary company VB Polska. Again this year they outsourced some of their IT functions to India, employing 3 people in New Delhi.

Outsourcing and to some extent offshoring is the result of what Adam Smith described in his famous book *The Wealth of Nations* as early as in 1776, the division of labor. Two centuries ago, however, the division of labor was limited to the extent of the market, but with today's globalization and significant improvements in the means of communication and transportation division of labor is becoming ever more widespread. Growth rates from OECD countries show a higher growth rate for trade in intermediate services as opposed to final services (Miroudot, Lanz, & Ragoussis, 2009), which could imply exactly what Adam Smith described, specialization and division of labor. Trade in services include Information systems and software solutions, and companies today are sourcing increasingly complex parts of their software development process to their own subsidiaries in low-cost countries (offshoring) or to 3<sup>rd</sup> party vendors (outsourcing) (Stack & Downing, 2005).

In addition to the increased complexity in the outsourced activities total sourcing has increased tremendously over the past 40 years. However studies show that almost half of all sourcing companies say that their outsourcing or offshoring programs fall short of expectations (BCG, 2005), only 10 % are highly satisfied with the cost's they are saving, and a mere 6 % are satisfied with the sourcing overall (Gottfredson, Puryear, & Phillips, 2005). This suggests that in spite of being a popular strategic move, outsourcing does not provide easy access to cost savings and other strategic goals.

Fagbokforlaget is actually part of the 50 % of companies that are happy and pleased with their offshoring decision, perhaps even in the 6 % of companies that are happy with the overall results. In fact they were so happy with their decision that they again this year have set out on yet another

offshoring pursuit, this time to India. How is it that Fagbokforlaget managed to accomplish what only a fraction of companies are able to accomplish? This is the basis for the problem statement.

### **1.1. Problem statement**

*How successful have VB Polska been for Fagbokforlaget seen from the owners' viewpoint, and can the experience from Poland be used towards achieving success in India?*

The remainder of the paper is, like the problem statement, divided into two main parts. In the first main part, which comprises sections 3-5 the case of the subsidiary in Poland will be presented and I will then look at the correctness of the offshoring decision as well as trying to identify any factors of success. In the second main part which is section 6 the case of India is presented. This part will also look at the correctness of the offshoring decision before it focuses on the challenges that FBF face in India. Also as a part of section 6 I will look at if and how experience from VB Polska can be used towards achieving success in India. Finally there will be a summing up in the conclusion.

## 2. Key words and definitions

*Business Process Outsourcing (BPO)*: outsourcing that involves the contracting of the operations and responsibilities of specific business functions (or processes) to a third-party service provider. Functions can be accounting, finance, IT, human resources and contact centers.

*Content Management System (CMS)*: It is FBF's own digital learning portal named Portfolio. It is where digital teaching aid is available for consumers and customers. (See *digital teaching aids* below)

*Digital teaching aids*: Digital teaching objects that exists either on its own or as a supplement to a book. Teaching aids like these are created to create interactivity which is believed to help the learning process.

*Microsoft/.Net*: Computer programming language

*Page Makeup*: Formatting a printed page, this includes the layout of headers, footers, columns, page numbers, graphics, rules and borders etc.

*Perl*: Computer programming language

*SW Testing*: Software testing is used to detect errors in the software and to provide information about the quality of the product or service under test.



### **3. Outsourcing and offshoring in the literature**

The terms offshoring and outsourcing are related to the company boundaries and used interchangeably in large amounts of literature. In this paper the two terms are used to describe two different situations. Offshoring is used when production is performed inside the company's organizational boundaries, but in a foreign country. Outsourcing is used when production is outside the company, performed by a 3<sup>rd</sup> party, however it is not geographically limited, and may be in the company's home country or abroad.

#### **3.1. Make or buy**

The decision of whether to make or buy is a strategic decision facing managers every day and it is without an universal correct answer. The make-or-buy decision is most often a choice between vertical integration (VI) and outsourcing. Make and buy are however two extremes in a continuum of possibilities. The continuum also shows how the costs, benefits and responsibilities of doing the work are split between two organizations. Figure 1 shows the continuum.

As the figure shows companies that chose to make carries the costs of all channel flows. There are personnel cost, warehouse cost, etc. They also carry all the risk. These costs and risk can only be justified by substantial benefits that offset the added cost and risk. One argument for vertical integration is often control. Control in itself, however, does not have an economical value. It is only when control is used to improve the overall economic performance that is it valuable (Coughlan, Anderson, Stern, & El-Ansary, 2006).

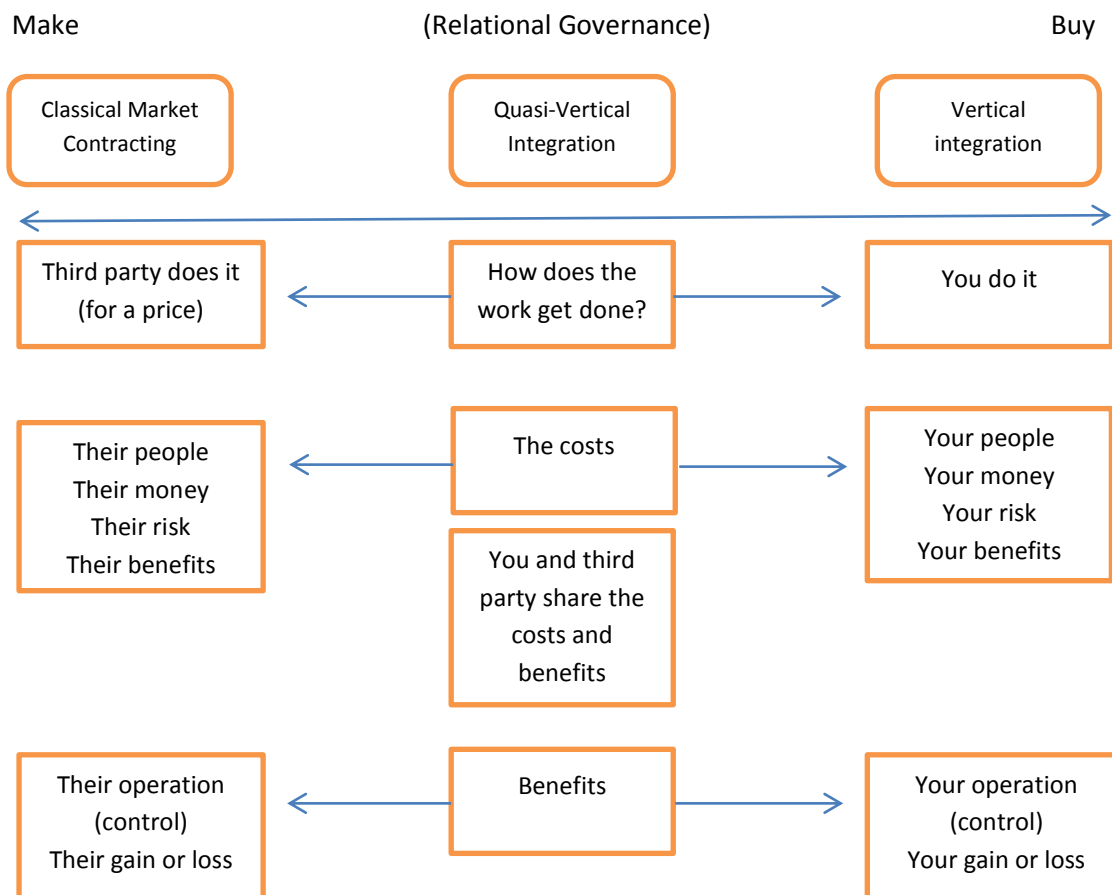


Figure 1 Continuum of degrees of vertical integration

Source: (Coughlan, Anderson, Stern, & El-Ansary, 2006)

When buying in the market the company avoids certain costs, such as for personnel and warehouses, and instead they face the cost (price) of the product or service they chose to buy in the market. In addition the supplier bears all the risk. However, the control is also in the hands of the supplier and the company loses the chance to earn profits from improving the economic performance.

However most arrangements with third parties involve some degree of relationalism, meaning that the company that buys has a greater share of cost and benefits than is the case under the classical market contracting. This compromising between the make and buy extremes is called relational governance and is shown as Quasi-Vertical Integration in figure 1. Relational governance is a good option when the arguments for integration are strong but not persuasive (ibid).

## **3.2. Outsourcing theories**

There are two main theories in the outsourcing field; core competence theory and resource based theory. Although different approaches they both seek to determine areas of competitive advantage for the firm.

### **3.2.1. Core competence theory**

Core competence theory suggests that activities should be performed either in-house or by suppliers depending on whether an activity is classified as a core or non-core activity. Core activities are defined as all activities which are necessarily connected with a company's existence (Arnold, 2000), but it is also defined as activities that your company does better and cheaper than its rivals (Gottfredson, Puryear, & Phillips, 2005), and hence give a competitive advantage. One company can't do everything and at the same time be the best-in-class at all of these functions. Core theory then suggests that companies should keep their core functions in-house while functions that another company can do more effectively is a candidate for outsourcing. These are also known as non-core activities. They do not give a competitive advantage and should be considered for outsourcing (Gottschalk & Solli-Saether, 2005) (Gottfredson, Puryear, & Phillips, 2005). There is much literature on this area claiming that by focusing only on the company's core activities and outsource "the rest", the company will increase its competitiveness (Quinn & Hilmer, 1994) (Arnold, 2000). However, deciding what a company's core activities are is not trivial, and the fact that it could change over time makes it even more difficult.

### **3.2.2. Resource based theory**

According to the resource-based theory of the firm, outsourcing is a strategic decision, which can be used to fill gaps in the firm's resources and capabilities (Grover, Teng, & Cheon, 1998). Firm resources can be divided into four categories: financial capital, physical capital, human capital and organizational capital (Barney, 2007). There is an assumption that some of the resources are either very costly to copy, or inelastic in supply. Firms then possess different bundles of resources and the resource based theory suggest that differences in companies' profits can be attributed to differences

in access to resources and the ability to exploit these. In terms of outsourcing a company should outsource functions requiring resources and capabilities the company does not possess (Grover, Teng, & Cheon, 1998).

To decide on what are a firm's resources and capabilities there is a framework that is generally applicable for this purpose, it is called the VRIO framework. Using the VRIO framework companies can analyze their activities and determine whether it is a strength or a weakness for the firm. VRIO is an acronym that stands for the question of Value: *Do a firm's resources and capabilities enable the firm to respond to environmental threats and opportunities?*, the question of Rarity: *Is a resource currently controlled by only a small number of competing firms?*, the question of Imitability: *Do firms without a resource face a cost disadvantage in obtaining or developing it?* and the question of Organization: *Are a firm's other policies and procedures organized to support the exploitation of its valuable, rare, and costly-to-imitate resources?* (Barney, 2007).

### **3.3. Reasons to outsource**

There is much literature on reasons to outsource. Coughlan. et.al.(2006) lists six different reasons to outsource which also sums up the majority of the literature.

The first reason is motivation. The outsourced activity is performed by an independent company, which must perform in order to keep the contract. They take on risk in return for the prospect of rewards, which is a high-powered incentive. They know that they will be replaced if they do not perform well (Coughlan, Anderson, Stern, & El-Ansary, 2006).

The second reason is specialization, and as many companies that receive outsourcing contracts often specialize in one or a few activities this creates and deepens their competence. One company cannot perform every activity in a value chain and best at every one of them. Outsourcing on the other hand allows companies to specialize and excel in a few activities which then give advantages for all members of the value chain.



In a market where there are low entry and exit barriers only the economically fittest will survive, and this is the third argument for outsourcing. Companies that do not perform better than its competitors will not survive in the industry because of the low barriers that allows new companies to enter at low cost. Less performing firms will then be forced to exit unless they are able to subsidize the activity using funds from other performance areas (ibid). The specialized company that only performs one activity does not have this option and must perform at all times, which is advantageous for companies looking for suitable third party vendors.

The fourth reason comes from the practice of outside parties pooling their demand of a single activity allowing one company to do a lot of one thing. This way the company enjoys economies of scale, which benefits the companies pooling their demand as it would have been uneconomical to perform the task in-house. By producing large quantities the fixed costs is divided on a larger output, reducing the average cost of production (Besanko, Dranove, & Shanley, 1996) (Coughlan, Anderson, Stern, & El-Ansary, 2006).

Heavier market coverage is the fifth reason to outsource. When outsourcing for instance the marketing activity to an outside vendor your product is one of several that they will market. By covering more products the marketing company will cover larger market groups and they can also reap benefits from complementary sales. The coverage by third party vendors is much higher than what the company can reach on its own (Coughlan, Anderson, Stern, & El-Ansary, 2006).

Finally, there is the argument of achieving independence from a single manufacturer. From a customer point of view the vertically integrated actor is biased and not equally trustworthy as an independent salesman. A seller that only sells a single brand or product will of course recommend his product, while as a seller selling several brands will be more neutral in his recommendations, and hence more trustworthy from the customers view. However this can be a drawback for the manufacturer as it might not get the seller to present the product in a way that it desires or would have done had it sold the product itself.

### **3.4. Transactions Cost Economics (TCE)**

Using the two main outsourcing theories to decide what to outsource or not can be difficult. In the literature we find several theories on how to choose the optimal sourcing strategy, and transactions cost economics is one of them.

A transaction is communicative action or activity involving two parties, often containing the exchange of items of value, such as information, goods, services, and money (Merriam-Webster, 2011). Companies face transactions with third parties on a daily basis and there are many different ways to organize these transactions.

TCE theory suggests that the optimal organization of a transaction is found on the continuum of vertical integration. The placement on the continuum is dependent mainly on two factors: the asset specificity and performance ambiguity (Coughlan, Anderson, Stern, & El-Ansary, 2006), but there are some additional factors that also affects the placement.

The initial thought is that all transactions could be performed in the market using contracts. However, the classical market contract rests on some strong assumptions about people. The first is perfect rationality, that all actors have clear, consistent goals that maximize utility, that they have perfect information about their alternatives and their consequences and that all actors have the ability to analyze all relevant information and to choose the best alternative in any situation. In addition it assumes that people act according to self-interest but within legal or moral constraints, this way contract obligation is honored.

Transaction cost theory is on the other hand based on some quite different assumptions. The first is that people have bounded rationality, which refers to the individual's limited ability to process large amounts of information. Research shows that the short term memory has a limited ability to process information (Moray, 1967). This means that the more specific and complex a transaction is the more problematic it is using market contracting because it is difficult, if not impossible to create contracts that cover all contingencies. Contracts that do not cover all possible future outcomes are incomplete

and may lead to opportunism. Opportunism is the second assumption of transaction cost theory. It says that people are self-interest seeking and will steal, cheat or lie to get their way. Although not all people act this way, you never know who will. Parties can be holding back information when forming a contract or they might refuse to honor the obligations stated in the contract.

#### **3.4.1. Asset Specificity**

Asset specificity refers to the level of specificity in investments, which in practical terms means the value of the assets outside the specific investment. High asset specificity means that the investment has a low outside value, while low asset specificity means that the investment has a high alternative use value.

Asset specificity can be divided into four categories where the first is human asset specificity. If a company is looking to outsource an activity that requires the employees of the third party company to obtain skills that are specific for one single transaction or activity they might be unwilling to take on the task. Because when the skills are not usable in any other activity but the one contracted to them they will incur losses if the contract is terminated. The company then loses the money and time spent on the specific training that is no longer necessary. Human asset specificity could also mean that it is difficult for the outsourcing company to locate other qualified bidder companies. They are then dependent on the existing relationship and therefore cannot credibly threaten to business elsewhere if dissatisfied. This opens up for opportunistic behavior from the 3<sup>rd</sup> party vendor because they know that the outsourcing company has no other viable option. The outsourcing company could then replace the market mechanism with VI to avoid opportunism from the partner company.

Second is physical asset specificity. Like human asset specificity it can be that activities require the acquiring of certain machines or buildings that are not suitable for any other activity than the one contracted to them from the outsourcing company. Again they might refuse, or be reluctant, to take on this investment due to the risk of termination of the contract in which case the incurred costs no longer have the opportunity of being outweighed by future income. The physical asset is difficult to

redeploy for multiple users, and therefore it creates contracting hazards. With vertical integration the problem is solved.

Third is site specificity which is when a company locates, for instance a warehouse, near another company, or in a certain location due to a contract with another company. If the location of the warehouse is far from other companies that it can possibly serve then the value of the location is low or close to nothing should the contract be terminated. As with physical assets this creates contract hazards.

Finally there are dedicated assets or dedicated capacity. That is capacity created to serve a single company and which, by itself, represents overcapacity. Companies are unwilling to incur these obligations as the costs of removing or reduce this capacity can be high in case of contract termination. Common for all four categories of asset specificity is that their firm-specific production has little or no value in any outside use. The difficulties a company has in convincing a possible high-quality channel partner in taking on these investments often lead the company to vertical integration (Coughlan, Anderson, Stern, & El-Ansary, 2006).

Common for all specific investments is that they create a lock-in effect. A lock-in effect occurs because of the lack of alternative uses of the assets and it enables the receiver to opportunistically exploit or expropriate the investments' value (Rokkan, Heide, & Wathne, Specific Investments in Marketing Relationships: Expropriation and Bonding Effects, 2003). Companies will stick with the contract even though they are being exposed to opportunistic behavior because the alternative is worse.

#### **3.4.2. Performance ambiguity**

The problem of performance ambiguity arises when aspects of one's performances are not personally observable or when the level of accomplishment is socially judged by ill-defined criteria so that one has to rely on others to find how one is doing (Bandura, 1986). Performance Ambiguity generates large problems for market contracting, as one cannot easily observe the level of

performance it is getting from the third party. For instance in times of poor results it would be difficult to determine whether it is due to bad performance from the vendor, or if it is due to an economic recession or other performance inhibiting factors not by fault of the vendor. In general market contracting yields indicators of current results, and where current results are not good indicators of performance there is performance ambiguity (Coughlan, Anderson, Stern, & El-Ansary, 2006). In cases of performance ambiguity VI is used as a tool to gain information and the ability to direct behavior.

### **3.4.3. Other factors**

Uncertainty is another factor that adds to the effect of specific investments. An uncertain environment is one that is difficult to forecast. This may be due to a changing, dynamic, environment or it may be because it is complex. Uncertainty then poses special challenges that a company must solve. In an uncertain environment one strives for flexibility so that when the environment changes so can the company. There are two opposing views as to what is the best solution in an uncertain environment, where one is to outsource and be committed to no-one, that way when things change, one can simply change the third party to a more suitable one for the situation. The other view is to keep the activity in-house and use the control to learn more about the environment and carry out a fitting strategy to deal with it. The evidence supporting these views is mixed, and on a general basis there is no single best solution. However when there are specific investments involved the flexibility from the outsourcing view is lost, and loses its advantage. In uncertain environments with specific investments vertical integration is preferred (Coughlan, Anderson, Stern, & El-Ansary, 2006).

Frequency is another factor that can affect the optimal position on the VI-continuum. Frequency can affect the placement in two different directions. On one side a transaction needs to have a certain regularity and volume in order for e.g. hybrid or internal solutions to pay off relative to market contracts, due to set-up costs and scale considerations (Rokkan, Transaction Cost Economics & Agency Theory, 2011). On the other hand, although a weaker argument, transactions that are frequently repeated also have a larger chance of functioning in a market contracting situation

because over time the contract following the transaction can be adjusted and improved creating a more and more complete contract.

Coordination costs are a fourth factor affecting the optimal decision. With activities performed outside the company there is costs associated with coordination. Coordination can be to make sure that parts arrive on time and that tasks are performed in the right time etc. Without coordination, bottleneck may arise. The failure of one company to deliver parts may delay or in worst case shut down a factory (Besanko, Dranove, & Shanley, 1996). When outsourcing a whole department companies often retain a few employees on hand to overlook and coordinate activities with the new supplier, their wage is then considered coordination cost.

### **3.5. How strong are your capabilities**

The two main outsourcing theories, core competence theory and resource based theory, provide the larger outsourcing picture. There are then other theories that seek to determine the specific activities to outsource. These theories are for instance TCE theory presented above by Coughlan et.al (2006), but there is also a 6-step framework by Besanko et.al.(1996) and Gottfredson et.al (2005) have come up with a 3-step framework. The first two steps in Gottfredson et.al's framework are comparable with TCE but their final step differs from the other literature. Gottfredsson et.al's 3<sup>rd</sup> step suggest that after determining which capabilities or functions that offer the highest potential value from outsourcing, it can be beneficial for further decision making to evaluate how good and efficiently the company currently performs each one of them (Gottfredson, Puryear, & Phillips, 2005). This is done by determining the company's ability to perform the process or function and cost per transaction measured against the industry median. Gottfredson et.al then created a map, figure 1, which then shows the optimal sourcing decision in every situation and the rationale behind it.

Company's ability to perform function	Better than it needs to be	Source to reduce cost; sacrifice capability if necessary	Consider creating a new business (if adjacent to core business)	
	Sufficient	Source to reduce cost	Consider creating a new business (if adjacent to core business)	
	Not good enough	Source to increase capability at lower cost	Source to increase capability even at higher cost if necessary	
		Above industry median	At industry median	Below industry median
		Cost per transaction		

Figure 2 Strength of capabilities and recommended actions Source: Gottfredson, Puryear and Phillips (2005)

From the map we can see that functions with a cost above industry median are candidates for outsourcing, but for different reasons depending on the company's ability to perform the task. If ability is low, then outsourcing should be chosen to reduce cost but also increase capability. If capability is better than it needs to be, then outsourcing is recommended to reduce cost while some capability can be sacrificed. Activities that are performed at a cost below median industry could also be candidates for outsourcing if the capability is not good enough. Outsourcing is then suggested to increase capability. If the company performs any function at below industry median with a high capability the company should, according to Gottfredson et.al (2005), consider creating a new business, as long as this is in line with their core business. This function could then be a new area of competitive advantage for the company.

### 3.6. Other aspects to consider in an outsourcing decision

It is not only the financial aspects that should be considered in an outsourcing decision or for that matter an offshoring decision. One factor that is often ignored or forgotten is the employees in the outsourcing company. The employees hold much power that can be used to delay or overthrow a

strategic decision like outsourcing. Employees often resist change because they fear the uncertain outcome. There is a clear link between sourcing projects and workers continued employment, compensation and benefits, and they know it. It should be clearly communicated what the company wishes to obtain by outsourcing, and what is off limits, this way the stress felt by workers will be reduced (Greaver, 1999). The costs related to employees working against management decisions can be tremendous, it might be that workers lower their effectiveness or it might be that they sabotage production with the ramifications that might entail, and so on.

Another potential problem with outsourcing that must be taken into consideration is the leakage of private information. A firm's private information is information that no one else knows, and it often gives the firm a competitive advantage (Besanko, Dranove, & Shanley, 1996). This may be production know-how, customer information or product design features. It may be the secret recipe of Coca-Cola which have been a well-kept secret for 125 years (Adams, 2011). Using the market to produce intermediates or distribute goods firms risk losing control over private information. Private information that is no longer private, no longer gives a firm a competitive advantage.

### **3.7. Offshoring options**

The offshoring decision is one that is often considered after outsourcing has been ruled out. It can be core activities that are not viable for outsourcing, it could be lack of suitable 3<sup>rd</sup> party vendors in the market or it might be that the risk of outsourcing is too large.

As figure 1 indicated there is more than one offshoring option. As much as 70-80 % of all companies that offshore choose to set up a fully owned subsidiary abroad (BCG, 2005) but options include joint ventures and collaborative partnering.

#### **3.7.1. Fully owned subsidiary (Captive Center)**

A fully owned subsidiary, also known as a captive center, it is the most costly option and the major challenge is knowing the local culture, laws and bureaucracy relating to business and employment in the offshore location. To overcome these challenges the manager in the subsidiary should be a



person with extended local knowledge. Also there are considerable costs attached to the acquiring of property, hiring or transferring of employees, etc. In return for these costs a fully owned subsidiary offers the company full control of the offshore location (Eastwood, 2005).

### **3.7.2. Joint Venture**

A Joint venture is a less costly option, as the set up cost of a new subsidiary is avoided. The hiring costs are smaller as the local company already has people employed. Although additional employees might have to be hired, this cost is believed to be less than for hiring all new people. The joint venture is a more strategic option as goals may go beyond opportunistic outsourcing. Goals may include selling some of its own products or services in the geography (ibid).

However the joint venture does not give the same amount of control as a fully owned subsidiary. The plans and visions of the home company are not the only ones to be considered.

### **3.7.3. Collaborative Partnering**

Collaborative partnering is also known as Build and Transfer (BOT). It starts out as an outsourcing decision but where the outsourcing company agrees to acquire the offshore center at a pre-determined point of time. This way the company will get comfortable with the location, and it also provides adequate time to prepare for a remote location (ibid).



## **4. Fagbokforlaget (FBF)**

FBF is an independent Norwegian publishing company that was founded in 1991. Their headquarters is located in Bergen, Norway, but they also have offices in Oslo, Norway and Sopot, Poland. FBF is the largest imprint in the Forlagshuset Vigmostad & Bjørke group (V&B), which also comprises Forlaget Vigmostad & Bjørke, Eide forlag, John Grieg Forlag and Cantando. Forlagshuset also owns a significant share of Haugen Bok, Pirat Forlaget Norway and CampusBok. Initially FBF specialized in publishing books for educational purposes but today they publish any kind of literature. FBF does not print any of their own books; they outsource all printing and use 3<sup>rd</sup> party vendors across the globe, and FBF were therefore familiar with operations in the international market when they in 2000 opened a subsidiary in Poland named VB Polska. It started out with only 2 employees and today, 11 years later, VB Polska employs 35 workers, mostly within the production department, but also some in the IT department.

FBF has its own IT department which, in addition to serving FBF, also serves the entire V&B group. The IT department has a total of 11 employees. It is headquartered in Bergen, but also has employees in Oslo, Poland and now recently; India. The IT department is divided in two functional groups; operations and development. Both functionalities exist in all locations except for India, where it is only a development group.

### **4.1. VB Polska**

VB Polska is a fully owned subsidiary, a captive center, located in Sopot, Poland. It was started in 2000 with only 2 employees but has now by 2011 grown into a large production unit with 35 workers. The work being performed in Poland is mainly production with 33 employees and IT with 2 employees. The production unit in Sopot transforms written texts into books. This includes everything from fitting text to book pages, design, layout and proof reading; altogether it is called page makeup and is a part of the pre-print production. The required skills to perform these tasks are varied, fitting the text to book pages is low skill work which only would need some practice, design

and layout requires somewhat training or experience, while proofreading requires excellent knowledge of language and grammar.

The IT personnel in Sopot are employed both within the development and operation groups. The development group spends most its time working with the development of digital teaching aids on FBF's own content management system (CMS).

In their 2006 Global Outsourcing Guide, CIO Magazine defines Poland as a low-cost country where IT-personnel with two years training averages \$10,000-\$15,000 a year (Overby, 2006). Although there are countries with even lower wage levels, compared to Norway with IT worker salaries averaging around \$75,000 (SSB, 2006), Poland will be considered a low-cost country.

#### **4.2. New Delhi, India**

The IT workers in New Delhi, India are for all practical means offshored, but legally outsourced. They are employed by an Indian printing company, Replika Press Pvt Ltd. (RP), to whom FBF is a large European customer. The workers have their offices at a 3rd party location, for which FBF pays rent through RP. The recruitment process was in whole performed by FBF; where the CIO of FBF went to India in February 2011 to interview and hire 3 programmers. Also, the workers are paid by RP, who then charges FBF for the amount of the wages. The employment contracts are between the programmers and FBF. On this basis I will handle this sourcing as an offshoring situation.

Different from the IT workers in Poland, the three programmers in India are only with the development department. As part of the development group they write codes used in the digital teaching aid development. The manager for the three programmers in India is located in Poland, at VB Polska, and although he regularly travels to New Delhi to oversee the work being done (3 times from January 2011-October 2011) the day to day communication is performed using a web-based project oriented platform.

India is considered a low-cost country with a wage level that is even lower than in Poland. In 2006 IT workers with 2 years training had a wage within \$5,000-\$10,000 a year (Overby, 2006).

### **4.3. Measuring the offshoring decision**

Measuring success in the international outsourcing/offshoring relationship is extremely difficult.

Success is a multidimensional construct that is only meaningful when discussed from the point of view of a given stakeholder (Seddon, 1997). A company has many stakeholders and in the offshoring situation there are a number of stakeholders that will have their individual measure of success.

Owners will measure success in terms of company value, profits and dividends. Workers in the home country might define it a success if they keep their jobs. Suppliers might call it a success if they don't lose any contracts. It is difficult if not impossible to take all stakeholders into account when measuring the success of a sourcing or offshoring decision. This does not mean that we should avoid measuring the success of an outsourcing. Instead we should focus on a single or a few stakeholders.

Measuring is essential for offshoring and outsourcing, and what a firm doesn't measure, it can't offshore well (Aron & Singh, 2005). The problem statement states that it is the view of the owners that is important for this analysis. For the remainder of this paper the success will therefore be measured with the owners as the key stakeholder. However, the two largest owners of FBF are the two founders Arnstein Bjørke and Arno Vigmostad that owns FBF 100 % through Vigmostad and Bjørke, which again is owned by Arnstein Bjørkes company Bjørkehagen AS, and Arno Vigmostads company Borgåsen AS. This means that the view of the owners coincide with the view of the CEO as Arnstein Bjørke is the functioning CEO of FBF. As shareholders Bjørke and Vigmostad will probably measure success in terms of generated profits, but as CEO Bjørke will likely, in addition to the financial aspect, also measure success in having skilled, talented and motivated employees that fit with the company's organizational culture.



## 5. Analysis

While creating a strategy plan in the late 1990's FBF considered every activity they performed and evaluated them to determine which were crucial to perform in-house and which were not crucial to perform in-house. This is similar to determining which activities are core and which are non-core. The result at the time was that page makeup fell below the line and it was offshored to Poland. This was the classical typography work, like fitting text to pages, proof reading and design. Accepting FBF's evaluation of the activities I will use the TCE theory to determine the correctness of the offshoring decision.

### 5.1. TCE Analysis

TCE theory mainly looks at the asset specificity and performance ambiguity when deciding on where to place the activity on the vertical integration continuum.

#### 5.1.1. Asset specificity

When looking in the market for an appropriate vendor FBF had to find a 3<sup>rd</sup> party that could do the job with the same or even better quality at an equal or lower price. Page make-up is easily available in the Norwegian market as it is a standardized task. The contracts used between a publisher and a page makeup company are also very standardized. For every book that is published there is a contract between the publisher and the company performing the page makeup. There are many companies and also many freelancers offering everything from graphical work to proof reading and page fitting for a well-known market price and there is therefore no human asset specificity attached to the task. No physical assets are required to do the job other than a computer and possibly some software, assets that are easily redeployed in the market if necessary, meaning that there is no physical asset specificity either. The page makeup job does not require the service provider to be at any particular location and hence there is no site specificity. Dedicated asset specificity is the only kind of specificity that might be present in this case. If FBF were to outsource all page makeup activity at once, in 2000 this was around 100 titles a year<sup>1</sup>, it is likely that a vendor accepting this

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<sup>1</sup> 120 new titles in 2003 (Aam, 2011). This number has grown steadily every year up until 2010 when they published 213 new titles. Around 100 titles therefore seem like a reasonable estimate for the year 2000-2002

contract would have to increase its capacity. If this capacity is increased by hiring staff on contracts with no expiration date there could be capacity specificity. However if the vendor increases its capacity by hiring freelancers on short term contracts, which is common in the publisher industry, the specificity is lower, in fact it might be nothing.

The page makeup activity can as mentioned be divided in two parts; graphical work and typography work. While both parts of the activity were available in the Norwegian market only the graphical work was available in the European market. Many printing companies offer these services on the side. The complete page makeup service was difficult to obtain in Europe as it requires proficient knowledge of the Norwegian language. One option could then be to outsource the graphical work, and keeping the proof reading in-house.

Finding a vendor offering the same quality to equal price was therefore possible; maybe even a somewhat lower price could be obtained if the company offering the service had large enough quantities to enjoy economies of scale. Although there were no actor in the Norwegian market that could offer the service at a cost giving FBF substantial financial benefits, the standardized task and low asset specificity made suitable vendors easy to find.

#### **5.1.2. Performance ambiguity**

There is hardly any degree of performance ambiguity in page makeup activities as the performance can easily be detected by the outsourcing company by reading the finished work.

#### **5.1.3. Other factors of TCE**

The future of paper books, which is an essential part of publishing, is very uncertain. Electronic books are on the rise and in May 2011 Amazon announced that they for the first time are selling more electronic books (e-books) than printed books (Miller & Bosman, 2011). However even e-books requires a publisher, and even though the future of paper books is uncertain, the future for publishers are more certain.



The level of frequency in the page makeup business depends on the number of titles that is released by FBF every year. As mentioned FBF published around 100 new titles a year around the time when VB Polska was initiated. In addition there are re-publishing of old titles that also could require some page makeup service. The 3<sup>rd</sup> party vendor would not handle all of these, but there would probably be several books a month. It is therefore plausible that the frequency is high enough to allow for a hybrid or vertical integration solution, as the set-up costs are spread on a sufficiently high number of transactions between FBF and the 3<sup>rd</sup> party vendor. However, when VB Polska first started there were only two employees, and it took several years before VB Polska reached the current amount of texts processed. Had FBF planned for the department to remain small it is unlikely that the frequency would be high enough to cover set-up costs in appropriate measure of time. It shall be noted that the set-up cost varies depending on whether it is a Greenfield investment or a Brownfield investment. With Greenfield investment a new facility is constructed and the company bears construction costs, while Brownfield investments involve the purchase or leasing of existing facilities. Existing facilities are often cheaper to acquire, but might bear larger maintenance costs. When constructing a new facility the company gets to form it to their specific needs, like size of rooms, storage space etc., however it does take longer time before the facility is ready for move in than if one had simply bought an existing facility, ready for use. With the purchase or renting of an existing facility the company loses the opportunity to shape the facility to their specific needs, but they can be lucky and find facilities that allow them to move in the next day. In the case of VB Polska, it is Brownfield investment, as FBF purchased the facilities they use.

Coordination cost is a factor that varies with complexity of the task that is being outsourced. For FBF who already had employees in several locations, Bergen and Oslo, adding a third location in Poland, might not be a large adjustment. Had the alternative to Sopot been having all the workers under the same roof, there would easily have been a marked rise in coordination costs. However, this was never an option for FBF, and coordination costs therefore were not a large issue,

#### 5.1.4. Summing up TCE

The page makeup task that is considered for outsourcing is a standard task that often is performed by freelancers and 3<sup>rd</sup> party vendors. The asset specificity is low, for all 4 types of asset specificity. There is no uncertainty to speak of and the frequency argument is a little ambiguous. Summing up it looks as the activity should be placed near the buy end of the VI-continuum. FBF however decided to offshore to Poland and in the next segment I will take a look at whether this was a good decision after all.

#### 5.2. Offshoring to Poland

FBF has experienced strong growth in the last decade and has grown to become a company categorized as a large size company, but in the 1990's they were a small publishing company by Norwegian standards<sup>2</sup>. When they were signing contracts for printing in Norway as a small company they had little bargaining power, and had to "wait in line" behind larger companies like Aschehaug, Gyldendal, Schibsted, Cappelen and Damm (Bjørke, 2011). When FBF in 1998 decided to outsource the much of the printing to a Polish company they did so to overcome the problem of low bargaining power in the Norwegian printing market. However they now faced a different problem, FBF were located far from their main printing site. In the 1990's when a book was ready to be printed a blueprint was made which then had to be approved by the publisher before the printing process began. The publisher would either travel to the printing site, or the blueprint itself was sent to the publisher for review and approval. Today this is all done electronically, but at the time it was a considerable cost for FBF to get hold of the blueprint, and also a question of time use, due to the long distance between FBF headquarters in Norway and the printing site in Poland.

In 2000 FBF then started the subsidiary VB Polska in Sopot, Poland and according to one of the two founders, Arnstein Bjørke, FBF had two main reasons for locating this department abroad. First and foremost it was a question of proximity to a printing company which is related to the distance and

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<sup>2</sup> In Norway companies are categorized as small when they have less than 20 workers, medium sized with 20-100 workers and large when they have more than 100 workers.  
<http://www.regjeringen.no/nb/dep/fin/dok/nouer/1995/nou-1995-16/5/2/1.html?id=336716>

time use described in the previous section; second it was cost reductions as Poland has a considerable lower wage level than Norway (World Bank, 2010). FBF could not locate any vendors near the printing company in Gdansk that could offer the services they requested. This is mainly because the worker that approves the blueprint will have to be proficient in the language of the book, which for FBF is mainly Norwegian. Polish workers fluent in Norwegian and with design skills were not available, and it seems unlikely that a Polish company would invest in Norwegian courses for their employees as this is a very specific investment.

If FBF they had requested the services and a company actually was willing to provide it, including the required level of Norwegian proficiency this would have added substantial human asset specificity to the project. Polish companies with knowledge of the Norwegian language are not common, and any vendor offering to deliver this service would have to have his workers trained in the language. This would have been a very specific investment for the vendor, with little outside value as Polish workers with skills in the Norwegian language are not easily redeployed in the Polish market. The vendor would then be open for the risk of opportunism from FBF, making the specific investment in the Norwegian language too expensive and risky. On the other hand the added human asset specificity also is also risky for FBF. They would have trouble locating one vendor able to perform the task, and would certainly have trouble locating additional viable vendors if they were unhappy with the performance from their first Polish partner. Not being able to credibly threaten to terminate the contract they would be exposed to opportunistic behavior from the Polish company. The option of outsourcing and market contracting was therefore lost if they were to keep proximity to printing company as the top priority due to the increased human asset specificity. Options then were limited to the three offshoring options; captive center, joint venture and build and transfer.

FBF decided to go for the first option, which is by far the most common offshoring preference. It was difficult finding companies in Poland that had the expertise needed for a Norwegian publishing company, and starting a separate company therefore became the preferred solution. By establishing

the captive center in Sopot, only a few miles from Gdansk, the expenses related to getting hold of and approving the blueprint could be considerably reduced. It took however some time for FBF to realize these savings.

FBF decided to hire two people to perform the page makeup activity at VB Polska. One was fluent in Norwegian and the other had a background from design. This meant that FBF had to hire two people to do what was usually considered a one man job. This extra cost though was outweighed by the second reason why FBF located in Poland; lower wages, and as Arnstein Bjørke, told it: "As a rule of thumb the wage level in Poland is 30-45 % of the Norwegian level, and even when we hired two workers in Poland, it was cheaper than it would have been hiring one Norwegian worker" (Bjørke, 2011).

When FBF decided to keep the entire pre-printing production in their own value chain they also took on more risk than if they had outsourced it or had chosen another offshoring option. This substantial benefits that Coughlan et.al. claims must be present to outweigh the cost of risk is present for FBF through lower wage expenses and, also with the closeness to the printing company, the reduced cost of blueprint approval. The closeness to the printing company also implies that there could be some site specificity involved. However the location of VB Polska in Sopot is not in immediate closeness to the Polish printing company in Gdansk. Sopot is together with Gdansk and Gdynia called Tri-city, and is considered one destination as they are located really close to each other (Kreft, 2009). If doing business in Gdansk it does not matter if the company is located in Gdansk, Sopot or Gdynia as they are all interconnected. Site specificity is not relevant as any location in the three cities is deemed a central location in a flourishing business area and any general facility here should not be difficult to sell or use for other purposes.

On the other hand dedicated asset specificity could be important. If the workers that acquire the Norwegian skills are not used in other production than for FBF, they represent capacity that is available only for FBF and which would be overcapacity if the contract were to be terminated.

However, if the workers at the Polish company are Polish they would most certainly also be fluent in Polish, and able to perform the page makeup activity for Polish books as well, possibly reducing the level of dedicated capacity.

### **5.3. VRIO**

The activities performed in Poland are varied. The main idea was to have workers performing page makeup, and have them approving the blueprints from the printing company. Today this is still the main activity but there are also IT workers and some administration located at VB Polska. An activity that was initially considered uncritical to perform in-house has now developed into becoming an important activity for FBF and it is also now considered a core activity. By using a VRIO analysis on the page makeup activity at VB Polska I will evaluate this development, and consider if it actually is a core activity for FBF.

The university in Gdansk offers a master degree in Scandinavian studies, where students can specialize in Norwegian, Swedish or Danish alongside English or German. FBF have for several years targeted the students that specialize in Norwegian and offered them jobs at VB Polska in the production departments. FBF then have polish workers, with polish salary expectations, which are fluent in Norwegian.

#### **5.3.1. Value**

*Do a firm's resources and capabilities enable the firm to respond to environmental threats and opportunities?*

The workers at VB Polska are polish workers fluent in Norwegian, Polish and English, which are available to FBF at a lower cost than Norwegian workers. The publishing business is facing an uncertain future as many people expect the printed book to be substituted for cheaper electronic books in the future. In May 2011 Amazon announced that they for the first time are selling more electronic books (e-books) than printed books (Miller & Bosman, 2011). Even though e-books are

expected at a lower price, they still require proofreading and design. Already being able to perform this at an estimated lower cost than other Norwegian publishers, VB Polska is creates resource value.

In addition Polish workers are not protected by as strong labor unions as Norwegian workers. In an eventual recession in the publishing industry it is probable that FBF possess more flexibility with VB Polska, than what companies with production units in Norway face. The resource contains value.

### **5.3.2. Rarity**

*Is a resource currently controlled by only a small number of competing firms?*

Proof readers fluent in Norwegian are not a rarity, but proof readers fluent in Norwegian at low cost are. According to TgM, a Norwegian labor union magazine, page makeup for Norwegian publishers is almost exclusively done in Norway (Putten, Busk, & Joplassen, 2011). Despite that fact that it is very common for English, and American publishing companies to outsource pre-printing production to low cost countries like India (Menon, 2010) I have, besides FBF, not found any other Norwegian publishing companies that outsource the page makeup to a foreign, low cost country. This gives FBF an excellent opportunity for being a cost-leader in the area and the resource is rare.

### **5.3.3. Imitability**

*Do firms without a resource face a cost disadvantage in obtaining or developing it?*

Poland is not the only country offering Scandinavian or Norwegian studies. In Europe alone 94 universities and colleges offers studies in the Scandinavian languages. However, to imitate FBF resources, the workers employed must be in a lower-cost country than Norway, and comparable to Poland or even lower-cost than Poland. Using World Bank data I have eliminated all universities in countries with wage levels that are more than 50 % above Poland. I use GNI per capita data, and even though GNI data has serious limitations, this is only a rough estimate, and there is no need for exact numbers in this particular analysis.

In addition to the World Bank income level data I have used the World Bank data on Ease of Doing Business (EDB). The numbers below are ranking numbers, and have no absolute value; it only gives us

an indication of the relative ease of doing business in a country. It is also tempting to believe that the ease of starting up a business is related to the costs related to the set-up. I will not speculate more around this, and the rankings below are only used as an illustration of the imitability of FBF's set-up in Poland. By eliminating universities in countries with a GNI per capita level of more than 1.5 x Poland's level, only 34 universities remain. 20 of these are in countries with a high ranking, above 100, on the World Bank ease of starting a business ranking. This is countries like Russia and Ukraine which are also ranked as highly corrupt countries by Transparency International (Transparency International, 2010). It is reasonable to believe that setting up a department in these countries will be a costly option for companies willing to replicate VB Polska. This leaves 14 universities in countries like Bulgaria, Croatia, Romania, Latvia, Georgia, Hungary, Estonia, Serbia and Slovakia, where especially Georgia looks promising with a very low GNI level compared both to Poland and Norway, and they are also ranked high on the EDB list, at number 7 for starting a business and 16 overall. We should note however, that the ranking is constructed by using data on the EDB for national companies, and does not take into account the EDB for foreign companies in that country. It is however likely that the two are somewhat related. If it is difficult for a Polish person to start a company in Poland, it is not likely that it will be any easier for a Norwegian worker or company to set up a business. On the other hand, it might be hard for a foreign company to start a business in country, for example Georgia, even though it is relatively easy for a national. Some countries are more nationalistic and protected than others and require foreign companies that wish to start up to form alliances with local companies in order to get an operating license.

	<b>Number of Universities</b>	<b>Income level (GNI per capita) Current US\$</b>	<b>Ease of doing business ranking</b>	<b>Starting a business ranking</b>	<b>Potential for Imitation</b>
<b>Norway</b>		85340	6	41	-
<b>Belgium</b>	2	45360	28	36	-
<b>Bulgaria</b>	3	6250	59	49	+
<b>Croatia</b>	1	13780	80	67	+
<b>Czech Rep.</b>	2	17890	64	138	+/-
<b>Denmark</b>	4	59210	5	31	-
<b>Estonia</b>	1	14370	24	44	+

<b>Finland</b>	5	47160	11	39	-
<b>France</b>	6	42390	29	25	-
<b>Georgia</b>	1	2690	16	7	+
<b>Germany</b>	16	43290	19	98	-
<b>Greece</b>	1	27260	100	135	-
<b>Hungary</b>	1	12980	51	39	+
<b>Iceland</b>	1	33990	9	37	-
<b>Italy</b>	5	35150	87	77	-
<b>Latvia</b>	3	11620	21	52	+
<b>Lithuania</b>	2	11390	27	101	+/-
<b>Holland</b>	2	49750	31	79	-
<b>Poland</b>	5	12410	62	126	+/-
<b>Romania</b>	2	7840	72	63	+
<b>Russia</b>	8	9910	120	111	+/-
<b>Serbia</b>	1	5810	92	92	+
<b>Slovakia</b>	1	16210	48	76	+
<b>Slovenia</b>	1	24000	37	28	-
<b>Spain</b>	2	31750	44	133	-
<b>Switzerland</b>	2	70030	26	85	-
<b>Sweden</b>	3	50000	14	46	-
<b>Ukraine</b>	3	3010	152	112	+/-
<b>U. Kingdom</b>	9	38560	7	19	-

**Table 1 Potential for imitation. European countries offering studies in Norwegian and income levels in the different countries.**  
**Source: (Study In Norway, 2007) (World Bank, 2010).**

It is not impossible to imitate FBF's resources in VB Polska. We shall notice that Poland is ranked as number 126 in ease of starting up a business and FBF has succeeded there and claims to have made profits since year 3. However FBF has had first-hand knowledge of Poland, they had a positive relationship with a polish printing company, and the co-founder spoke polish. It is reasonable to believe this made the starting-up process easier than if they went into the process with no connection to Poland. This local knowledge makes it more difficult for other companies to imitate the resource.

#### **5.3.4. Organization**

*Are a firm's other policies and procedures organized to support the exploitation of its valuable, rare, and costly-to-imitate resources?*

Interviewing workers at FBF I got the impression of it being a dynamic company. The two founders are always open to new ideas, and it seems to be a policy at FBF that one is allowed to try out just about everything that seems interesting, and this has become The Fagbokforlaget Way. One consequence from this ideology is that FBF are able to react quickly to changes in the environment as



they don't spend too much time considering options, and rather just put things into life, but it also means that projects are not always thoroughly investigated before they are implemented. "It is not always a good thing and it has happened several times that I get half-planned projects on my table" (Aam, 2011).

Co-founder Arnstein Bjørke proudly explained how he feels, that FBF has accomplished the difficult task of being one organization despite the many locations; "Our workers are united across borders" (Bjørke, 2011). Workers from different locations work together every day aided by phone and internet. In addition to their Intranet FBF uses internet based communication tools such as: Office Communication Server which gives them opportunities for 1-on-1 video- and audio communication, and Meetcon which is a web-based video conference solution allowing 1-on-many interaction and also allows for sharing of documents (Aam, 2011). Creating a feeling of being a single organization despite the geographical distance is related to trust. Trust is a product of several factors, where one is knowledge. Without knowledge about other people or organizations you can't trust them. Gaining knowledge however is difficult and only emerges from long-time interaction (Rousseau, Sitkin, Burt, & Camerer, 1998). Over ten years workers in Sopot, Bergen and Oslo have worked closely together creating one organization and also trust. This combined with a culture that allows for innovative and creative workers makes the organization capable of pulling together in the same direction in a timely manner, necessary to exploit the valuable, rare and costly to imitate resources.

#### **5.3.5. Summing up VRIO analysis**

The VRIO analysis shows that as a resource VB Polska's production unit is valuable, rare, somewhat difficult to imitate, and FBF has an organization capable of exploiting its resources. The page makeup activity has then gone from being deemed less important to becoming a strength for FBF and an area of competitive advantage and hence qualifying it for being a core activity. This was an important development for the activity as the investment in VB Polska was a very specific investment for FBF, because the alternative use of VB Polska is rather low for FBF. This in turn increased the risk of the

investment. To make up for this increased risk FBF needed substantial benefits, which is partly given by the page makeup activity transforming into an activity of competitive advantage.

**5.4. Strength of page makeup activity**

Positioning the page makeup activity in Gottferdson, Puryear and Philips capability strength map shows just how transformed the activity is.

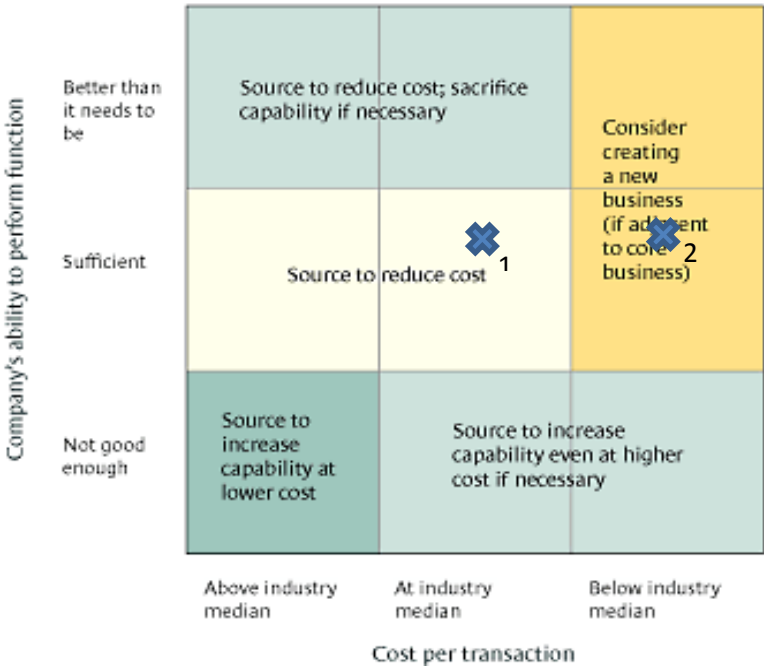


Figure 3 Placement of page makeup activity when performed in Norway (1) and at VB Polska (2)

When the page makeup was performed in Norway it was at a cost near industry median (point 1 in figure 3). FBF had employees at average Norwegian salary and there is no reason to expect them to be any more efficient than others in the industry. If anything they would be less efficient, if there are companies enjoying economies of scale, which it is likely that FBF did not enjoy as they were a reasonably new and small company in the 1990's. However good the capability was the map still recommends outsourcing to reduce cost and, depending on the capability, adjustment of the

capability. Now, the activity is performed at a cost below industry median (point 2) as the average Polish wage is approximately 30-40% of the Norwegian wage level<sup>3</sup>.

When VB Polska first started they employed two people doing one person's job as they could not find people that had design skills in addition to being fluent in Norwegian. As the scale of operations grew in VB Polska it is reasonable to believe that the amount of proof reading and design work became so high that a separation of design and proofreading would be a practical option, and hence the cost savings could increase further, which also makes up for the increased risk that followed the specific investment.

### **5.5. Success of VB Polska**

In addition to deciding whose viewpoint should be taken into account when measuring the success of an investment or other decisions one must also decide on a certain amount of variables which are to be measured. These variables should be related to the goals that FBF wishes to realize with their investment. However FBF did not have many specified goals when offshoring to Poland. As previously mentioned they opted for closeness to the printing company, which were expected to give a reduction in blueprint approval time, and hence costs. The cost reduction was not a goal in itself, and has hence not been given the amount of attention that one might expect when offshoring to a lower-cost country. Bjørke claims that VB Polska turned a profit for FBF as early as 2003 (Bjørke, 2011), but as no exact numbers were given me I was not able to verify this. It is therefore difficult to measure the financial success or lack of success in VB Polska. But what is a fact is that the page makeup activity that was initially deemed unnecessary to keep in-house has over the past 11 years become a source of competitive advantage for FBF. FBF has then turned a non-core activity into a possible core activity. The competitive advantage that FBF has created with VB Polska is likely to help generate financial profits for FBF.

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<sup>3</sup> According to numbers from Statistics Norway and Central Statistical office in Poland the average polish wage is actually only 1/5 of the average Norwegian wage level. However, FBF's experience is that the wage level of employees at VB Polska is about 30-40% of the wage level of similar workers in Norway.

<http://statbank.ssb.no/statistikkbanken/>  
[http://www.stat.gov.pl/gus/5840\\_1630\\_ENG\\_HTML.htm](http://www.stat.gov.pl/gus/5840_1630_ENG_HTML.htm)

Currently VB Polska is only performing page makeup for internal use. However as suggested by Gottfredson et.al's map, FBF could consider selling page makeup services in the market. This could also add to the economic performance of VB Polska, which would add to the benefits of making instead of buying. On the other hand this must be considered against the possibility of losing the competitive advantage they now enjoy over other Norwegian publishing companies that are currently purchasing or producing page makeup services in Norway at a higher cost.

Another reason why FBF enjoys success in Poland is related to the strong growth they have enjoyed over the last 5-10 years. FBF are constantly looking to invest and acquire other publishing companies in Norway. Over the last 6 years they have wholly or partly acquired companies like Eide Forlag (2005), Grieg Multimedia (2009), Cantando (2009), Migranorsk (2009), Haugen Bok (2011) and Piratforlaget (2011). The growth in the Vigmostad and Bjørke group eliminated the need for what otherwise would have been a required reduction in staff in Norway when work was moved to Poland. And this was proudly presented by Bjørke: *"We have never fired anyone in this process"* (Bjørke, 2011). The avoidance of lay-offs is most certainly a success factor for FBF in this process as uncertain and unhappy workers that fear for their jobs would be likely to resist the offshoring and use their powers to delay the decision. Delays and resistance can kill an outsourcing or offshoring project. FBF has managed to prevent this becoming the end of VB Polska by starting out small. The changes then came gradually, and it was in fact the workers themselves that eventually requested the opportunity to work with VB Polska. Initially it was only a few people that worked with the employees at VB Polska, and when other employees in Norway saw how well it worked, they wished and asked for the opportunity to do the same. This way FBF made the workers themselves make the larger changes, and this way the resistance was avoided. Aided by the fact that no Norwegian jobs were at risk this was a successful tactic for FBF.

According to Arnstein Bjørke VB Polska turned a profit already in 2003. However, larger cost savings are only realized when a company is able to hold on to workers for a longer period of time as there

are substantial costs related to initial training. In the beginning stages of VB Polska the workers did not have the same efficiency as the experienced free-lance workers we have in Norway but after a few years training this improved and their efficiency is now in line with the rest of our workers (Bjørke, 2011). It is then crucial to be able to hold on to your workers over longer periods of time. In FBF this is done mainly by creating a feeling of belonging in the company and incorporating the Fagbokforlaget Way in every aspect and location. Even though workers are geographically far apart FBF strives to make them feel part of the same company. It would seem as FBF has done some good work in this area as, for instance, the first worker employed at VB Polska back in 2000 is still employed there today.



## 6. India

### 6.1. Why India

FBF originally did not have the intention of hiring people in India. When they identified the need for more developers in their IT department they initially advertised for people in Poland that were to be located at VB Polska. Ads were posted for different developer positions. FBF needed developers with skills in 4 different areas; Perl, Microsoft/.Net, FrontEnd and SW testing. The Perl developer was the most difficult to find. Perl is a rare skill, and in Norway they are costly at a monthly salary of more than 45000 NOK (Aam, 2011) (SSB, 2006). Although Perl developers are less costly in Poland, FBF was not able to find any qualified people for the position. However they did receive applications from people in India for the Perl position. One of FBF employees at the IT department at VB Polska is Indian and then the idea of employing people in India developed. With the local knowledge of their Indian employee and the let's try it spirit that lives in FBF the hiring process in India was initiated.

### 6.2. Was offshoring to India the right decision?

The decision to hire an additional 3 workers in the IT-department came from the increased focus and demand for digital teaching aids. FBF is still publishing many works intended for educational purposes, and an increasing amount of educational books now come with additional digital teaching aids intended for use in classrooms and homework situations (Aam, 2011). This has increased the need for FBF to create these digital aids, which require substantial programming work.

This programming work is what FBF mainly offshored to India. It is standard IT-work that is contracted out by companies all over the world. Speaking to the CIO of FBF I got no impression that it would have been a problem to outsource the activity rather than offshoring it which indicates a low asset specificity. Low asset specificity and low performance ambiguity is as previously mentioned factors that determine the placement of the activity on the VI-continuum. When it comes to performance ambiguity this is not a large problem for software programming. *"We generally don't monitor the codes that are written, the fact that the software works is proof of good work"*, the CIO

of FBF tells me. This suggests that FBF don't see any problems with performance ambiguity in programming. This would mean that in this case outsourcing would be a viable option.

The FBF strategy however is to keep every function that is often used in-house, like IT. The CIO of FBF admits that the option of buying in the market was considered only for Norway and found to be too expensive. If hiring the three employees in Norway the wages alone would be close to 1.5 million NOK a year. The wages for the three employees in India are less than 1/5 of the Norwegian level. *"I would never have gotten the funds to hire the employees in Norway"*, Aam claims. However the option of outsourcing to a low-cost country was never considered. By outsourcing to an Indian company FBF would probably be able to get a price not too far off the wages they now pay for the three employees, and in addition be free of the risk associated with VI as modeled by Coughlan et.al. FBF on the other hand sees the risk as small, but they compare the risk with employment in Norway, and not outsourcing to an Indian company. The decision to offshore to India therefore does not seem to have been the best option for FBF, as theory suggest it should have been market contracted.

To FBF defense they are expecting to expand the IT-department further, and if they are able to get the department in New Delhi to function well that is where the expansion mainly will take place (Aam, 2011). This fact is the only aspect that might justify the decision to offshore rather than outsource to India. In that case the offshoring to India becomes a strategic move, were future plans trumps the current optimal position on the VI-continuum.

### **6.3. Doing business in India**

Independent of whether the decision to offshore to India was a wrongful decision or a rightful strategic move any company that is doing business or planning to do business in India should be aware of some of the challenges and advantages of doing business there. India is becoming an increasingly popular destination country for outsourcing and offshoring. Cheap labor coupled with good English language skills has made India a preferred option. While the United States of America has been the number one provider of IT workers for many years, India is now running up as one of



the world's leading exporters of services related to information technology and software giants such as TCS and Wipro are based there (EconomyWatch, 2010). Doing business in India is however not without risk. Every year the World Bank Group ranks 182 countries according to the ease of doing business in that country. The overall ranking is based on rankings on several topics. India is in 2012 ranked as 132 out of 183. Singapore is ranked as number 1, and Chad as number 183. Although being ranked as 132 is not a good performance, it is an improvement from 2011, when India was ranked 139. It should be noted however, that it is a ranking and not an absolute number.

The specific topic ranking can be seen in table 1. From the table we see that India have varied scores in the different topics, and it is especially 4 topics that influences the low overall rank for India. That is *Starting a Business, Dealing with Construction Permits, Paying Taxes and Enforcing Contracts*. This suggests that India has possibly large, but definitely slow working bureaucracy, which is challenging for companies wishing to start up in India.

<b>Topic Rankings</b>	<b>DB 2012 Rank</b>	<b>DB 2011 Rank</b>	<b>Change in Rank</b>
<b>Starting a Business</b>	166	166	No change
<b>Dealing with Construction Permits</b>	181	181	No change
<b>Getting Electricity</b>	98	109	11
<b>Registering Property</b>	97	96	-1
<b>Getting Credit</b>	40	37	-3
<b>Protecting Investors</b>	46	44	-2
<b>Paying Taxes</b>	147	165	18
<b>Trading Across Borders</b>	109	107	-2
<b>Enforcing Contracts</b>	182	182	No change
<b>Resolving Insolvency</b>	128	140	12

Table 2 Doing Business - Topic Rankings 2012 India

Source: (The World Bank, 2011)

Companies that offshore to India rather than outsource will feel the problems, which are the basis of the ranking, more heavily than companies that outsource. As FBF is legally outsourced, they avoid

some of the direct problems of starting a business and they won't have to deal with construction permits or tax payments as this will be the responsibility of Replika Press. They will however be exposed to the risk of problems with enforcement of contracts.

**6.4. Lewis model of culture**

Cultural differences are regarded as a major factor that determines success or failure in international business relations. Many relationships have gone sour because parties are not able to work together efficiently across cultural borders (Johnson, Lenartowicz, & Apud, 2006).

One model that tries to capture the essence of different cultures is the Lewis Model of culture (Lewis, 1998).

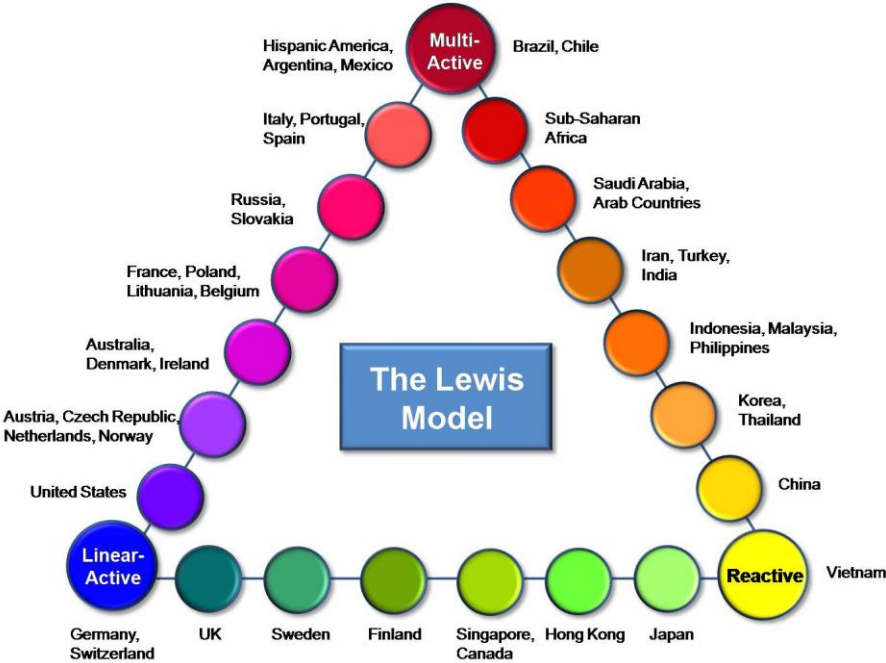


Figure 4 Lewis-model of Cross-cultural Communication

Source: (Lewis, 1998)

It classifies cultures into three categories; Multi-Active, Linear-Active and Reactive. Each category has its own set of values and believes that identifies the social behavior and business behavior of the people in cultures near that category. Countries are then placed in the triangle according to their main characteristics.

The model shows how people in different cultures vary in their concepts of time and space, how their communication styles are reflected in the language patterns they use, how they view the truth: as absolute or negotiable and what their values, attitudes and world views are.

People in cultures that are linear-active are polite but direct, they place facts before sentiment, logic before emotion; demonstrate task orientation; have limited body language and respects officialdom.

People in multi-active emotional and displays feelings, they are people oriented, put feelings before facts, have unlimited body language, they are impatient and seeks out key persons to establish connection to get what they want.

Reactive people are polite and indirect, they conceal their feelings and must not lose face, and they are very people oriented, patient and use their connections to get what they want (ibid).

#### **6.4.1. High and low context communication**

One example of cultural differences that may affect business relations is high and low context culture and communication. A high context communication or message is one in which most of the information is already in the person, while very little is in the coded, explicit, transmitted part of the message. A low context communication is just the opposite; i.e., the mass of the information is vested in the explicit code (Hall, 1976). Different cultures differ in the level of context. Norway and Scandinavia is considered a low-context culture, while India together with most Asian cultures is a high-context culture. Communication between people from high- and low-context cultures is difficult. People from low context cultures rely on messages to be given explicitly, and will miss out on much of the message given from someone from a high-context culture. On the other hand, people from a low-context culture are often considered rude by people from high-context culture due to the directness of their communication. In his 2005 study on outsourcing relationships Imsland discovered problems when people from different context cultures communicated. A low-context party expected a high-context party to be straightforward when reporting on project status, while the high-context party expected the low-context party to “read between the lines”. A similar problem is reported by

the Norwegian CIO of FBF which claims that the Indian people always say yes: “When I ask them for anything, they always say yes” (Aam, 2011). When asked to perform certain tasks the Indian reply is always “yes”, and while the CIO accepts this as a positive, the workers probably expects him to “read between the lines” and hence understand when it is a positive and when it is a false positive.

#### **6.4.2. Language**

Another important part of culture is language and communication. Communicating with people from other cultures can be challenging. In addition to high and low context there is the problem of language. Language and culture is closely intertwined, but whether it is language that shape culture or the other way around is still debated (Boroditsky, 2010). One can't completely understand a foreign culture without knowing the local language. For instance: the Norwegian language includes words that are not easily translatable to other languages; such as *Dugnad*. To fully understand the Norwegian culture one must understand the concept of *Dugnad*.

### **6.5. Challenges for FBF in India**

#### **6.5.1. Turnover rates**

*“We never know if they will turn up for work tomorrow” – CIO Fagbokforlaget*

During an interview the CIO of FBF expressed concern about the job turnover rate in India, and his worries seem to be justified. Job turnover is difficult to measure, as companies are not obliged to report this, but many researchers (Eastwood, 2005) (Cawthorne, 1995) (Dayasindhu, 2002) (Budhwar & Harsh K. Luthar, 2006) have expressed their worries about increasing turnover rates in India. The increasing turnover ratio not only forces companies to spend more on hiring new people, but it also increases the wage level necessary to retain people from switching to other jobs. The BPO sector in India was estimated to be short 262.000 employees in 2008 (Budhwar & Harsh K. Luthar, 2006). The lack of skilled personnel adds additional pressure on wages. This increase in employee compensation level has been contributing to increasing the cost of Indian software services, driving many customers to explore cheaper options in other countries (Dayasindhu, 2002).

The three workers employed by FBF in New Delhi have not contributed to high turnover rates for FBF so far. FBF did however get to feel the possible ramifications of these high rates during the hiring process in India: A total of 400 applications were received for an original 4 job advertisements. Of the 400 applications 26 were judged interesting for 3 of the positions. FBF then decided only to hire 3 people and as 1 job advertisement, SW-testing, received few applications and at the same time was deemed the least important, it was eliminated. 26 people were then contacted for a phone interview, but only 13 replied. FBF was surprised by the poor response and decided to contact an additional 3 applicants. 16 candidates were then asked to perform a test specific for the position they applied to.. The test would take about 8 hours to complete. Even though this is common practice in the IT-industry only 4 completed the test. Again surprised and annoyed by the low turnout, FBF still decided to invite 12 people to an interview. Out of the 12, only 6 people came to the appointed interview time. After interviews they offered employment to 2 people. In addition they hired one worker who was currently situated in Malaysia that had been interviewed on video conference.

Although FBF now are happy with the people they decided to hire, they were not prepared for the low turnout. Although there is little empirical evidence of why this happens, it is sensible to believe that it is a result of the many available positions in the IT-industry. This gives skilled workers the opportunity to constantly shop for new jobs looking for higher wages. It is worth noting that the wage expectations of the 400 applications ranged from 1,500 NOK per month to more than 20,000 NOK per month (Aam, 2011). Wages in the 20,000 NOK range is extremely high in India, even for programmers, which give the impression that applicants are not necessarily looking for a new job, in that case they would have put up a realistic wage requirement, but they are looking for the high wage it would be worth changing jobs for. They are job-shopping.

### **6.5.2. The caste system**

The caste system is an important part of the Indian culture and understanding the caste system helps the understanding of the Indian culture.

Even though the caste system was legally abolished with the writing of the constitution in 1949, it is still flourishing today. Caste defines the core of Indian tradition, and it is seen today as the major threat to Indian modernity (Dirks, 2001). There is no universal accepted theory about the origins of the Indian caste system, but it does show resemblance with the Iranian caste system. There are four main divisions in the caste system; Brahmin; Kshatriya; Vaishya and Shudra and each division have countless sub-castes. Brahmin, Kshatriya and Vaishya are known as upper castes, while people of Shudra together with Other Backward Classes (OBC), Scheduled Caste (SC) and Scheduled Tribe (ST) make up the lower caste.

The caste system lay down social rules for the Indian population and among these is the marriage-rule. Marriage within a specified birth-group is the residual essence of caste (Ghurye, 2005). This effectively creates different layers of society and people of lower caste in India face discrimination every day. Today people of different castes interact more as people from lower castes are given quotas in school enrollment, and public sector jobs, but the single fact that there is a need for quotas for lower-caste people shows how the caste system is very much alive today. As late as 2008 Human Rights Watch put focus on how the Dalits (known as Scheduled Caste) and indigenous peoples (known as Scheduled Tribes) continue to face discrimination, exclusion, and acts of communal violence in India (Human Rights Watch, 2008).

Although people from different castes interact in today's business world it is not without problems. FBF experienced this when their Indian manager, located in Sopot went to New Delhi to visit the three employees situated there. The owner of RP does seem to treat FBF's manager as lower caste, and as the CIO of FBF told it: "They don't refuse to do what he asks, but it is with little respect" (Aam, 2011). As a solution to the problem FBF tried to be clear about how the Indian manager was FBF's "chosen one", and they urged the owner of RP to honor this. It seems however implausible that a request from FBF will trump centuries of tradition and a rigid caste system. It will require substantial

work from FBF and their Indian manager to earn him the respect needed to keep him in the managerial position with the three employees in New Delhi.

### **6.5.3. Other cultural problems**

FBF also came across other problems in the hiring process in India that is related to cultural differences; the determination of wages and the issue of transport to and from work. FBF negotiated different wages with the three workers they hired. It went back and forth with demands and offers before they finally agreed on a sum. When the contract then was to be signed it turned out that the wage offered by FBF was the gross sum, while the amount expected by the employees was the after tax wage. This was a misunderstanding generated by the lack of understanding of local procedures. One can debate whether FBF should have known about this Indian way of wage negotiating, and adapted this procedure, or whether the workers should have realized that the contract and wage would be by Norwegian standards. To end this disagreement FBF added an allowance to the wages that made up for the difference between pre and post-tax wage, hence resulting in a direct extra cost for FBF due to lack of local knowledge.

The issue of transportation to and from work is another common Indian practice that FBF was oblivion about. If the company is located far from public transport it is common that the employer organizes, and pays for, transport to and from the nearest public transport area to the work place. This is a security measure, as workers are exposed to robbery when travelling to work, and they are especially vulnerable on payment day. This transport expense is then another added cost that FBF was not prepared for.

### **6.6. Can the success factors from VB Polska be transferred to India?**

It is debated whether experience from previous sourcing can help the success in another sourcing project. In an empirical study on German companies it was found that offshoring success in one location had a significant effect on the level of success in another location. However it was very small. Other factors that had larger impact were the level of mutual trust and knowledge transfer

(Westner & Strahringer, 2010). This is in line with Imsland's (2005) recommendations of building trust to achieve success in IT-sourcing situations.

A point worth noting is that while the decision to move to Poland was the result of several factors and among them local knowledge and business partners, the decision to hire people in India happened pretty much by chance. They were therefore less prepared, and the hiring process shows that even though they had an Indian man on board they came across unexpected problems that added costs to the project. The Fagbokforlaget way and spirit entails as mentioned that there is an openness and acceptance to try out new ideas. However FBF must also be aware of the potential and problems of groupthink. It is in fact possible that the move to India was a result of groupthink, and although FBF shall be outgoing and try new ideas, they must not mistake it with the belief that they will always succeed at it.

The main success factor of VB Polska as presented by CEO Arnstein Bjørke was the ability to function as one organization despite large geographic distance. Bjørke believed this was accomplished largely because workers in different locations worked together on a daily basis. By reducing the success factor to this I believe Bjørke has very much simplified the situation. To evaluate the transferability of the VB Polska experience to India, one must look at the underlying causes of success.

Firstly it is local knowledge, which is also related to knowledge of culture. From the Lewis model we see that Norway and Poland are placed rather close on the triangle, suggesting that the two cultures are very similar. But they are not equal because then they would have been placed together. This means that there are some cultural differences between the two countries, and cultural differences, however small they are, are possible troublemakers.

When studying a language one also automatically learns about the culture in the country or countries that speak that language. The workers employed at VB Polska that have studied Norwegian have also learned about the Norwegian culture. Although one might never fully understand a culture different from your own, they have more knowledge about Norwegian culture than the average Polish person.



Additionally, Arno Vigmostad, co-founder of FBF, is married to a Polish lady and he speaks Polish. This means that he has some knowledge of Polish culture. Although this is not recognized by FBF as a success factor, they undoubtedly had both local knowledge and knowledge of culture before they started in Poland, and at the same time the employees at VB Polska's cultural knowledge of Norway is high. This way they have overcome problems that might have developed due to cultural differences, and the feeling of being one organization may have formed easier than if the local and cultural knowledge was absent. From the Lewis model we can also see that the cultural distance between India and Norway is much larger than it is between Norway and Poland. The local knowledge and cultural knowledge then becomes even more important as the differences are bigger. The Indian workers have little cultural knowledge about Norway, but FBF have the advantage of having one Indian man employed in Poland, and they should therefore try to take advantage of his local knowledge about India, to make the cultural differences less distressing. Nevertheless, it does seem much more difficult to reach the same level of mutual cultural knowledge in this relation.

The cost aspect of the success, seem to be transferable. The wages FBF pays in India are somewhat lower than what they pay in Poland (Aam, 2011). But to fully enjoy this advantage FBF must keep workers from leaving too soon. Thus they must prevent a high turnover. This is the largest challenge they face in India, and needs attention from the management. Solutions could be progressive pay schemes that give workers incentives to stay for longer periods of time; it could be bonus plans or other schemes that encourage employees to stay. Simply just giving a higher wage than other companies in the area is not a good solution as this will simply add to the already large pressure on wages, and in the end FBF will lose the low cost advantage that India currently displays.

The practice of having people work together on a daily basis to reduce the effect of geographical distance is also not easily transferable to India, as the workers in India and Poland perform different activities. While the people at VB Polska mainly perform pre-printing production which requires coordination with project leaders in Norway, the employees in India are programmers and mainly

work alone. Although they all have access to Meetcon, the communication tool used by FBF, this does not mean that they actually communicate. Without this mandatory daily communication it seems difficult for FBF to use this tactic to include the workers in New Delhi in the one organization. However it might not be necessary to include the IT workers in India into the organization in the same manner as the production workers in Poland to achieve the same level of success. IT-workers often work alone, many work from their homes and hardly ever meet their colleagues, while production workers expect more interaction with colleagues and hence the need for a united organization is larger.

## 7. Conclusion

The high human asset specificity that occurred when FBF prioritized closeness to the Polish printing company made offshoring the only viable option for FBF. The decision was a good one as it resulted in costs savings created by the lower wage levels in Poland compared to Norway. In addition the page makeup activity that was initially considered unimportant to keep in-house was transformed into a source of competitive advantage and then also a core competence. This success was the result of the successful implementation of their organizational culture in Poland, the Fagbokforlaget Way, but as we also saw later the thorough knowledge FBF retained about Poland and how the majority of the Polish workers were familiar with Norwegian culture. From the owners' viewpoint then, VB Polska has contributed to improve FBF's competitiveness in the market through lower costs, creating a competitive advantage and a core competence.

The cultural aspects are difficult to transfer to India as the workers there do not have the same education in Norwegian culture. Although FBF has an Indian manager on board it is limited what he can accomplish as the knowledge in this relation only goes one way. The IT-workers in India are also more autonomous and less dependent of being part of the organizational culture to perform their job than the production workers in Poland.

FBF was less prepared when entering into India than they were in 2000 when they entered Poland. It could be that since so many years have passed since 2000 that the details around the start-up has been forgotten, or remembered in a simplified fashion, and that FBF this way underestimated the difficulties of a new start-up. It could also be that the outgoing and new thinking culture of FBF have created a groupthink problem where they falsely believe that they always achieve success in new projects. What is a fact is that the cultural differences were severely underestimated, which has created challenges for FBF both during the hiring process as well as in the working situation in New Delhi. I believe that FBF did not realize the importance of cultural knowledge when they established in Poland as they never witnessed how problems could occur had the knowledge not been present. It is also a fact that FBF now faces several challenges in India that are not equally present in Poland.

Cultural differences account for most of them and the most important lesson to learn for FBF is that cultural differences do matter and no culture is better than the other, just different. It is important to reconcile the differences and instead of handling problems as they arise try to identify possible future problems and solve them. Much can be done by learning about the Indian culture and it would be a natural starting point to use the knowledge and information possessed by FBF's Indian manager.

The most pressing problem in India is though the high turnover rates and it would be wise for FBF to use time and resources to look for salary programs or other solutions that keep workers from leaving FBF. This is especially important if they are to keep their plan of expanding in India in the future.

The success and experience from Poland are not easily transferred to India due to larger cultural differences and the fact that the workers are part of a different department than the majority of the workers at VB Polska. With much focus and attention on cultural knowledge and with appropriate actions in terms of reducing turnover it is possible for Fagbokforlaget to copy their success from VB Polska.

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