

# Insights of the Strategic Approach of Global Sourcing and the Modes of International Sourcing Strategies

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## Abstract

The modes of international sourcing entry strategies still an unusual research topic in International Business. The different entry modes still not well investigate in the literature. The increase in the research related with Global Sourcing reveal the importance to deeply investigate this subject. Recent research investigated the International Purchasing Offices as part of Global Sourcing. Other modes of international sourcing entry modes still not analyzed with the Global Sourcing and International Sourcing approaches. This article aims to investigate how the conceptual models of Global Sourcing and the modes of international sourcing entry strategies can be integrated. A literature review was made in order to develop this analysis. As a result, we present a set of entry modes that can be related with international sourcing and another list related with Global Sourcing. Though this article is limited by its theoretical approach, the model proposed here could be used to an empirical research.

**Keywords:** internationalization, sourcing operations management, global strategy, global sourcing

## 1. Introduction

The identification of the possibility to gain competitive advantages while adopting Global Sourcing has lead companies to re-structure their activities of sourcing internationalization. Changes in the global business environment and competitiveness, the introduction of new technologies, as well as the experiences of the companies, starting from the 1980s, have influenced these processes of re-structuration (Shet & Sharma, 1997). The incorporation of a more comprehensive and integrated vision for the area emerged in this new competitive process. It is leading the companies to search not only for lower sourcing costs, but access to new technologies, flexibility, reduction of the dependency on suppliers, anticipation of materials for developing new products, and even the establishing of the presence of the purchasing company in global markets (Monczka & Trent, 1991; Bozarth, Handfield & Das, 1998; Cho & Kang, 2001; Christopher, 2002; Jin, 2004; Agndal, 2006; Harris, 2006; Knudsen & Servais, 2007; Dutton, 2008). Trent and Monczka (2003a) realized that adopting Global Sourcing, simply while making international purchases, allows the development of better relationships with suppliers and the increase of communication flows between the companies.

The definition of Global Sourcing as a strategic orientation for searching and monitoring global suppliers, as well as an efficient management through integration and coordination of the activities related with functional areas and local units of business (Nunes, Vieira & Antunes Júnior, 2013) show that this practice is related to a strategic approach, and not a simple search for international suppliers. Trent and Monczka (2003) developed a scale through which we can identify that the internationalization of the supply area represents a process of widening the involvement of the company with the international market and the relevance given by the company to this area, starting from the national purchases until the implementation of Global Sourcing.

The relationship with the sourcing companies has been one of the challenges identified in the management of the activities of Global Sourcing. These relationships are gradually built, based on the development of trust relationships overtime (Salmi, 2006), as well as on the tightening of personal ties (Ghuri, Tarnovskayaand & Elg, 2008). The formalization of relationships between the companies must be established (Bozarth, Handfield & Das, 1998), which leads to the need for a further approximation with the global suppliers. Consequently, the presence of the purchasing company in the sourcing market started to be considered as part of the sourcing strategy. Benefits related to the direct interface with local suppliers, governments, and local communities have been identified (Goh & Lau, 1998; Carbone, 2002; Pedersen, 2004, 2004b; Bendorf, 1998).

Harris (2006) states that the presence of the purchasing company abroad can take place in various ways, which

gradually represent the increase of the local involvement. According to the author, the companies started this process with the use of intermediaries, and only after this, an *International Procurement Office* (IPO) was installed. According to Mulani (2008), IPOs represent the preferred alternative by the companies to incorporate new suppliers in global sourcing chains. Harris (2006) highlights the relevance of these units for searching opportunities related with technology and production. As it was noticed by Akesson, Jonsson, and Edanius-Hallas (2007), the direct purchase from international suppliers allows for greater flexibility and productive control and, especially in geographically further markets, the local presence through an IPO contributes to achieve these benefits.

Studies as Sartor (2006) and Nassimbeni and Sartor (2006) have investigated how the companies are conducting the process of opening IPOs. However, the alignment of this unit with the global strategy of the company is not considered. Studies relating other forms of sourcing entry strategies were not found. In the last two levels of the Trent and Monczka's model (2003), when the companies actually adopt a strategic posture for the area of international sourcing, they started to integrate the activities of purchasing in global units interconnected with all the other units. However, the presence in the sourcing country is not considered in this model. In the model proposed by Arnold (1999), orientations for this aspect are not made.

Under the perspective of the international business area, the relationship between Global Sourcing and the sourcing modes strategies need more investigation. When observing Trent and Moczka's model (2003), the opening of an IPO seems to be related with the levels IV and V of internationalization of the supply area, while the use of an intermediate may be related with the levels II e III, where the adoption of Global Sourcing is not considered yet.

In parallel, it is possible to observe that the studies on internationalization of companies traditionally investigate the perspective of the local presence focusing on offering (sales). Studies of entry modes traditionally approach strategies as export, licensing, *joint venture*, and direct external investments (Osland, Taylor & Zou, 2001). Although studies as Harris's (2006) inform that there are different forms of presence in sourcing markets, these forms have not been investigated inside an approach of companies' internationalization. Actually, Sartor et al. (2014) state that the appropriate selection of the entry mode in sourcing markets is an essential aspect for the management of the complexity of the activities of international sourcing. This situation occurs due to the cultural heterogeneity, the presence of multiple actors, relationships with different and distant interlocutors, and unfamiliar business rules and behaviors to the companies. In this context, the presence of the purchasing company in the country of the supplier can be a solution to minimize these difficulties.

More recent research on the presence of the purchasing company in the sourcing market (Sartor et al., 2014; Jia et al., 2014; Jia et al., 2014a) reflects an effort of a collaborative research developed by Chinese and European academics, aiming the study of the installation of IPOs by Western companies in China. The first part of this study, represented through Jia et al. (2014) consists a literature review about the topics Global Sourcing and IPOs in the last 20 years. One of the indications of future perspective of research refers to the need for widening the study of different entry modes in the country of the supplier (*sourcing entry modes*). The installation of an IPO may represent one of the stages of internationalization of the supply area and. As Jia et al. (2014a) observed, this unit can present different functions, what enables its classification with different names. Besides, Jia et al. (2014) recommend that studies considering the presence of the company in the sourcing market and models of internationalization of the sourcing activity to be developed as dynamic functions, or as an evolutionary process. The concept of Global Sourcing presents studies that reveal this perspective, as the one proposed by Trent and Moczka (2003). This perspective was employed by Jia et al. (2014a) to analyze the IPOs, but the more comprehensive vision of the presence in the sourcing market through other forms, as well as through strategic partners, was not used in the study. Trent and Monczka (2003) highlighted that the selection of the appropriate sourcing entry modes is essential to manage the complexity of the international sourcing activities due to the participation of several actors, increasing the quantity of relationships, business models, and different cultural patterns.

These gaps identified in the literature represent opportunities of research. Thus, this study questions: How is it possible to integrate the conceptual models of Global Sourcing with the modes of International Sourcing Strategies?

It is important to highlight that most of the literature regarding modes of international sourcing entry strategies and especially IPOs can be considered as "grey literature", especially practitioner-oriented articles. Sartor et al. (2014) presented a literature review that revealed this situation. As the authors suggest, more research is required on an academic basis. While their complementary works (Jia et al., 2014; Jia et al., 2014a) only investigate the IPOs, we

argue to consider the International Sourcing Entry Strategies as a broader perspective to establish the presence at the sourcing market and try to integrate it to the theory related with the strategic approach of GS.

This article presents a theoretical investigation on Global Sourcing and the presence of the purchasing company in the sourcing market. This constitutes the basis for the development of an integrating theoretical model, which can be used later to conduct empirical researches on the topic.

**2. Global Sourcing**

The activity of Global Sourcing (GS) started to be investigated in the late 1980s. One of the first researchers to characterize this activity as a strategic perspective of the supply area in the international context was Arnold (1989, 1999). According to this author, GS should be characterized by the making of sourcing operations in the external market and by the managerial orientation for the development of opportunities in heterogeneous environments, with the identification and overcoming of the difficulties inherent to these opportunities. The model proposed by Arnold (1989, 1999), even though it represents the different choices that the company can make related to their international sourcing strategy, is restricted to the analysis of two dimensions. It does not reflect the entire magnitude of the variables that a company needs to consider to internationalize their sourcing activities. It does not even consider the strategic level that must be applied to this decision.

Although the simplicity of the concept, it was used as reference in the initial studies of GS, such as Smith (1999), Li, Murray, and Scott (2000), Trent and Monczka (2003, 2003a), Overby and Servais (2005), Gelderman and Semeijn (2006), Quintens, Pauwels, and Matthyssens (2006), Knudsen and Servais (2007), Hartmann, Trautmann, and Jahns (2008), Steinle and Schiele (2008), and Trautamann, Bals, and Hartmann (2009).

According to Monczka and Trent (1991), there was a lack of studies showing how companies could adopt GS. Although the concept of Arnold (1989) had identified a strategic nuance to the activity of GS, more research was required to identify the differences between a non-strategic international purchase and GS strategy. The original model proposed by Monczka and Trent (1991) had four phases. Phase 1 represents the companies that perform only domestic purchases. In Phase 2, there are those companies who buy abroad only by necessity. In these two phases, the companies frame a reactive posture in relation to GS; while in the next phases, a proactive stance will be seen. Phase 3 is characterized by companies that had incorporated international purchasing in their sourcing strategy. Phase 4 represents the companies that made the integration of the overall sourcing.

GS strategies must involve, according to Kotabe and Murray (2004), the identification of units, inside a corporation, that will perform each activity, as well as the establishment of interfaces between the areas of Research and Development, Operations and Marketing in a global scale. These aspects are incorporated in the improved model of Trent and Monzka (2003). This second version can be considered an evolutionary model, according to Jia et al. (2014a).

The first proposed model, even though it fulfilled a number of limitations of the previous studies, still did not address in detail all the complexities of international sourcing. Monczka and Trent (2003) reformulated this structure with a survey of 162 respondents and the study of 10 cases, proposing as a result a new five-level model, presented at Figure 1.



Figure 1. The process of sourcing internationalization (Trent and Monczka, 2003)

By becoming part of the corporate strategy, international sourcing activities can change the relationship of the purchasing company and its suppliers. As identified by Schmitz and Knorrinda (2001), in some situations, there may be a change in the structure of the supply chain. The definitions for the product to be sourced can be so specific that the supplier only produces “tailored” to a global customer.

The Levels 4 and 5 comprise what the authors call as “global sourcing.” It differs from the previous levels by the increased complexity, as they include the proactive integration and coordination, similarity of materials, processes, design, engineering, and site operations. At these levels, the companies no longer need to be just trading partners to become active members that operate in a supply chain. Even if the company adopts the Level V, with the coordination of their purchases being made by a unit of the group, it is noteworthy that the benefits from this strategy may not be achieved if the company does not have an appropriate structure to assist the release and receipt of materials in different countries.

In none of the studies of the strategic perspective of global sourcing, an investigation of the perspective of the modes of international sourcing entries was identified and, more specifically, with the presence of the purchasing company in the sourcing market. The modes of international sourcing entry strategies are investigated in the sequence.

### 3. Modes of International Sourcing Entry Strategies

According to Rajagopal and Bernard (1993), there are four stages in the internationalization of strategic procurement. The first is the domestic purchasing, when firms purchase in the domestic market although this may involve purchasing foreign produced goods through local sources. The second is the experimental involvement, when firms “recognize that benefits can arise from external sourcing, but where (as yet) they do not perceive the advantages to be sufficiently great to warrant systematic search and involvement” (Rajagopal & Bernard, 1993: 48). The active involvement is the third type and includes the firms taking a proactive stance in searching for sources and materials on an international basis, including the establishment of purchasing groups, overseas purchasing offices or the subsidiaries to establish purchasing contracts. The fourth stage is the committed involvement when firms develop global information networks on a self-motivating basis, rather in response to specific request, while displaying a willingness to be flexible in the implementation of procurement strategies.

Based on these stages and through the adaptation of Rugan et al.'s (1988) work, Rajagopal and Bernard (1993) presented a continuum based on the depth of the involvement in foreign sourcing market and time, to present five modes of international sourcing entry strategies. The “Local Sourcing” is the first mode and represents the domestic purchasing company that may source goods produced abroad, but purchases them through local representatives. The second is the “Import via agents or distributors,” which is, like a simple offshore purchasing, similar to an arms-length relationship between independent purchasers and sellers. In this stage, supply can be procured through domestically located intermediaries (import via agents or distributors within the domestic market) – indirect import; or it can be procured through the intermediaries in the foreign market – direct importing. The “Import through subsidiaries and/or own representatives” represents the third stage, when firms tend to use subsidiaries or other corporate units for international sourcing assistance, especially when there is an increased need for information and expanded levels of international procurement activities. The fourth is the “Establish IPO” focused on function and region that purchase parts, components and manufacturing, and product development services for their plants worldwide. The last stage is the “Integrated and coordinated global sourcing through Direct Investment” that involves the worldwide integration and coordination of a firm’s procurement requirements with the main objective to maximize the purchasing advantage of the firm on a global basis.

The use of intermediaries has been identified in several studies, as the one by Akesson, Jonsson, and Edanius-Haltas (2007). The authors identified that making direct purchases from suppliers in the global market is the most used option by the manufacturing companies, given that this is how it is possible to obtain more flexibility and control, with the best approximation with the production operations. Although this is the most used form, the study identified also the use of intermediaries and agents, especially in geographically more distant markets.

The use of intermediaries, as *trading companies*, is one of the forms of presence of the purchasing company in the sourcing market that can occur through intermediaries. Harris (2006) highlights that, in this case, the intermediary usually assumes the attributions of negotiation between the parts, besides conducting the operational procedures. This author affirms that this is often an initial form of internationalization of the supply area, which precedes the use of a representatives of the purchasing company in the sourcing market. This representative can include the establishment of an IPO or not. Nassimbeni and Sartor (2006) identified that it usually starts with an employee of the company sent to be the purchase representative, who, besides doing this work, also becomes the responsible for structuring the IPO. A third way, identified by Harris (2006), is attributing the responsibility of Global Sourcing to

the purchase area of one of the units of the company, located in the sourcing country of interest by the company. This unit starts to support the other purchase units in the activities with that market, by giving the company conditions to take advantage of the best opportunities available in a specific market regarding technology and production.

Goh and Lau (1998) define IPO as a purchasing office abroad established to purchase components, parts, pieces, and other industrial inputs to be used by productive plants globally located. Nassimbeni and Sartor (2006) show that, following this concept, an IPO can be an isolated unit, only made for this end, or an office inside a subsidiary established abroad with their own resources or in partnership (*joint venture*). Considering the knowledge already developed about Global Sourcing, we must add to the concept of IPO that this unit should not be restricted only to components and other items feeding a production line, since final products are also the focus of activities of Global Sourcing nowadays (Nunes, Vieira & Antunes Júnior, 2013).

Studies related with IPOs are recent, as noticed by Sartor et al. (2014). Although the initial efforts have emerged in the 1990s (Goh & Lau, 1998), they were intensified throughout the 2000s (Pedersen 2004, 2004a, 2004b, 2004c; Bendorf, 1998; Avery 2002, 2002a). Aiming at aspects such as attribution of an IPO, its location, costs, benefits, problems, management of people and organizational structure, there is still a gap about the relation between the strategic involvement of the supply area, through the adoption of Global Sourcing, and the presence of the purchasing company abroad, whether through an intermediary or having their own structure. Although this relation is not clear yet, it is possible to identify that the entry of the company in the purchasing market can contribute to the success of the Global Sourcing.

Regarding the IPOs, when reviewing the literature on the topic, Nassimbeni and Sartor (2006) identified that, once they are established, the IPOs have been performing functions of operational support, quality control of suppliers, selection, and development of suppliers, reduction of the cultural distance, and cooperation in the activities of development of new products. Among the benefits resulting from opening an IPO, companies have obtained price reduction, higher levels of quality control, cultural distance reduction, risks reduction, elimination of intermediaries, establishment of direct relationship with the suppliers, establishment of relationships with the local government and the business community, facility in the management of great volumes, faster problem solving, and better coordination of all the activities abroad (Nassimbeni & Sartor, 2006). Despite these benefits, problems with managing people, cost with managing the unit, cultural issues, need of high minimal, annual volumes of purchase, support from the superior management of the company, location, and even with suppliers distant from the IPO have been observed (Nassimbeni & Sartor, 2006).

Jia et al. (2014a) highlight that IPOs must be constituted inside the logic of dynamic and evolutionary models. The authors identified five types of IPOs based on the breadth and depth of the activities of IPOs and the strategic importance to the parent company. The first two are considered as “International Sourcing Office – ISO” and are responsible to collect sourcing market intelligence, search, audition, and selection of suppliers, and basic quality control. It can be an independent, intermediary trading company or an intermediary plants/sale office, called “Intermediary ISO,” or an in-house purchasing office, reporting to corporate purchasing department, called “In-house ISO.” Based on the increase of the purchases, the authors identified that more responsibilities may be given to the ISO, related with duties after suppliers are qualified, order fulfilment, logistics/shipping, and quality control/inspection, so that it can become an IPO. According to them, there are two types of IPOs: an IPO focusing on serving global plants through exports (E-IPO), and an IPO serving both global and local plants (E&L-IPO). The last type is the “Overseas Corporate Purchasing Organization – O-CPO” that covers all the supply functions of an HQ-based CPO, but it is located overseas. It takes overall responsibility for making global sourcing policy and coordinating the relationship between the supply base and other departments, leads R&D projects, and sometimes provides sales support and manages operations in the host country.

#### **4. Proposed Model**

Based on the previous literature, and using the types of involvement proposed by Rajagopal and Bernard (1993), we analyzed the types of sourcing proposed of Rajagopal and Bernard (1993), Harris (2006) and Jia et al. (2014a). To integrate the literature review, Figure 3 also includes the proposal of Arnold (1989) and, Trent and Monczka (2003) to understand the concept of GS and its strategic characteristic.

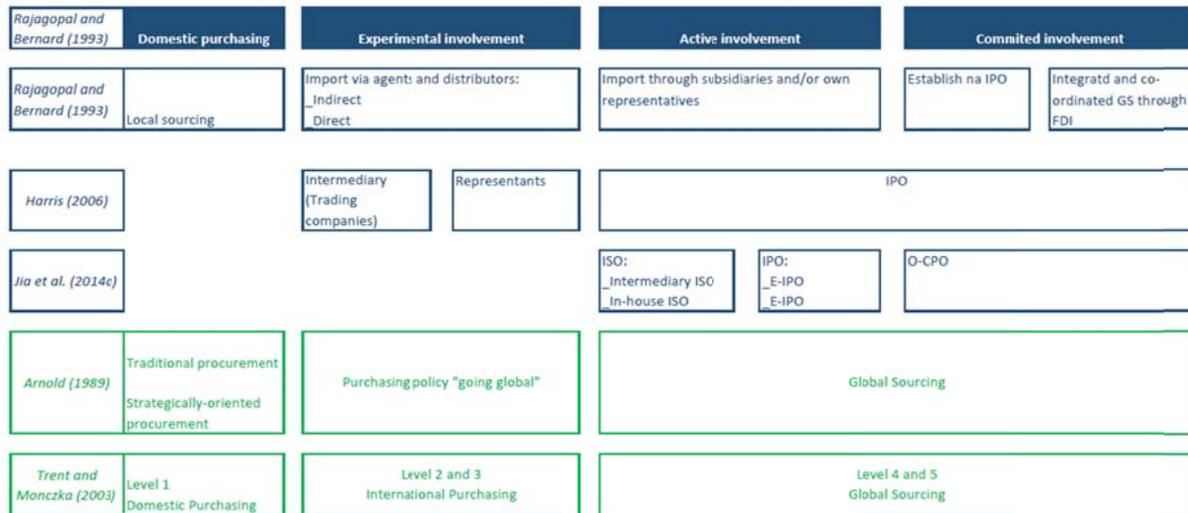


Figure 2. Theoretical review integration

Through the literature investigation, it was also possible to identify which entry modes can be related with International Sourcing and which ones are related with Global Sourcing (Figure 3).

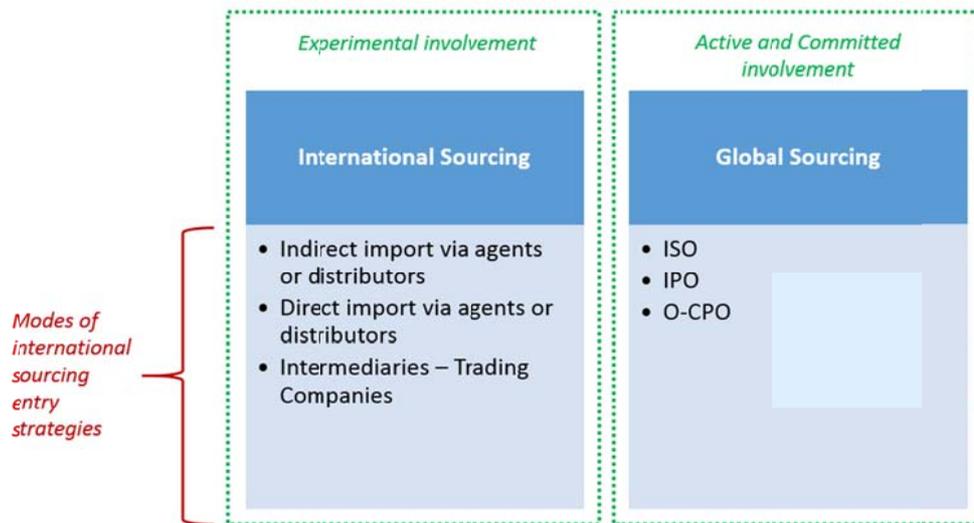


Figure 3. Modes of international sourcing entry strategies

Considering the previous studies, it is important to highlight that the “Import through subsidiaries and/or own representatives” was defined by Rajagopal and Bernard (1993) as an Active Involvement and, following the literature review, we re-classified it as an “Experimental Involvement” level.

**5. Final Considerations**

In order to investigate how it is possible to integrate the conceptual modes of GS and the modes of international sourcing entry strategies, a literature review was made. The list of entry modes related with International Sourcing includes the Indirect and Direct Import via agents or distributors, and the use of intermediaries – Trading Companies. The entry modes related with GS include ISO, IPO, and O-CPO.

Considering that the identification of the modes of international sourcing entry strategies was made based on the literature review, an empirical work must be developed to test this segmentation. Before that, an exploratory study to identify the existence of other entry strategies is suggested. As this is a new topic at the International Business literature, and some of the available literature sources can be considered “old,” it is possible to assume that the empirical environment may have developed different strategies that were not identified here.

This article represents the first effort of a research that aim to identify the entry modes that are being adopted by companies to develop their sourcing strategy.

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