

The Impact of Firm Learning on Financial Value in Strategic Outsourcing Relationships

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We investigate whether managers in outsourcing firms, through their prior experience in managing similar strategic alliances and prior association with the provider, learn to create value in their outsourcing relationships. Value creation is estimated in terms of long-term abnormal stock returns to the outsourcing firm relative to an industry, size and book-to-market matched sample of control firms following the implementation of the outsourcing contract, announcement period returns, and allied wealth effects. We find that prior experience and prior association have a significant impact on long-term abnormal stock returns, suggesting that financial markets are slow to price learning effects in outsourcing. Further, while relational learning alone influences value creation in simpler fixed price contracts, both procedural learning through prior experience and relational learning through prior association with the provider have an impact on value creation in variable price contracts. This is because of greater ambiguity in cooperation and coordination between firms that characterizes variable price contracts. The results have implications for management of outsourcing engagements and their performance and valuation.

*To read the Full paper, please contact Arun_Kumar@isb.edu