Chapter 5
Exploring Processes and Capabilities in Offshoring Intermediation

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Abstract The growing offshoring phenomenon has radically transformed the configuration of many industries: fewer rivals, more powerful retailers, transformation of previous manufacturers into marketing companies and emergence of new players. The main driver of offshoring in commodity markets is still today the possibility to benefit from low labour cost. However, cost savings are not enough: the performance of offshoring strategies is determined by outstanding capabilities in product selection, control of suppliers and logistics. This chapter highlights why and how offshoring intermediaries emerged as new players. Using evidence from a case study in small household appliances industry, we describe how intermediating offshoring roles fit with the global reconfiguration of the value chain.

5.1 Reconfiguration of Global Value Chains and Emergence of Offshoring Intermediaries

The diffusion of offshoring strategies in the majority of industries led to the profound revision of firms' strategies and organizational roles. The relocation of manufacturing facilities to the low-cost locations or to the new emerging markets considerably changed the rules of the game for all industry players.

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The logics of the international allocation of firms' value chains received a significant consideration by international business (IB) scholars (Stopford and Wells 1972; Johanson and Wiedersheim-Paul 1975; Johanson and Vahlne 1977; Buckley and Casson 1993; Diaz-Alejadro 1977; O'Brien 1980; Levitt 1983; Kogut 1985a; Nigh et al. 1986; Bartlett and Ghoshal 1988; Dunning 1995; Africano and Magalhaes 2005). The scholars studied various aspects of the offshore relocation of value chain activities: the definition of which activities are to be relocated, the evolution of the competitive advantage of firms that decided for partial outsourcing and offshoring of their activities, the selection of offshore locations, the organizational aspects regarding the control and monitoring of the offshored activities and many others.

While significant research dealt with firm-level offshoring decisions, few studies were dedicated to the issue of *allocation of value chain activities among firms* in the international context. The classical assumption about the "black" or "white" allocation of value chain among different actors of the industry value system (Porter 1985), transaction costs logics still dominated the IB literature: the activity was located either within firm's boundaries, performed by the firm or outside of firm's boundaries, performed by suppliers or firm's direct clients or distribution channels (Coase 1937; Williamson 1981; Kogut 1985a; Grossman and Hart 1986; Hart and Moore 1990; Doz and Prahalad 1991; Dyer and Singh 1998; Tadelis 2002).

Porter's industry value system and "five forces" frameworks (1985) accounted only for the momentary overlaps in the value chains of different industry actors related to the downward integration of industry suppliers and upward integration of industry customers. In those cases, the overlaps in the actors' value chains lasted only for the industry reassessment phase. The overlap in the value chains of clients and suppliers was also partly acknowledged by scholars who studied concurrent sourcing occurring when "firms both make and buy some of their requirements for a particular component" (Parmigiani and Mitchell 2009).

In the international context with its strong information asymmetry (Johanson and Wiedersheim-Paul 1975; Johanson and Vahlne 1977; Nigh et al. 1986; Casson 1996; O'Grady and Lane 1996; Ricart et al. 2004; Ghemawat 2007), one may expect the existence of lasting, non-temporally overlaps in the value chain activities of firms located at different stages of the industry value system—we decided to call them "grey areas". The permanent "grey areas" of overlapping value chains appear when suppliers start performing their customers' activities or when customers enter their suppliers' businesses. The relocation of production or other value chain activities to low-cost or emerging countries creates favourable conditions for the emergence of lasting in time value chain overlaps among "onshore" firms and their "offshore" suppliers, in particularly when the relocated activity is strongly related to the product or service sold, such as manufacturing or research and design activity. Our paper considers one of the many industry examples, the European small household appliances industry, illustrating how offshoring strategies implemented by European small household appliances producers reshaped the entire industry value system and led to the creation of "grey

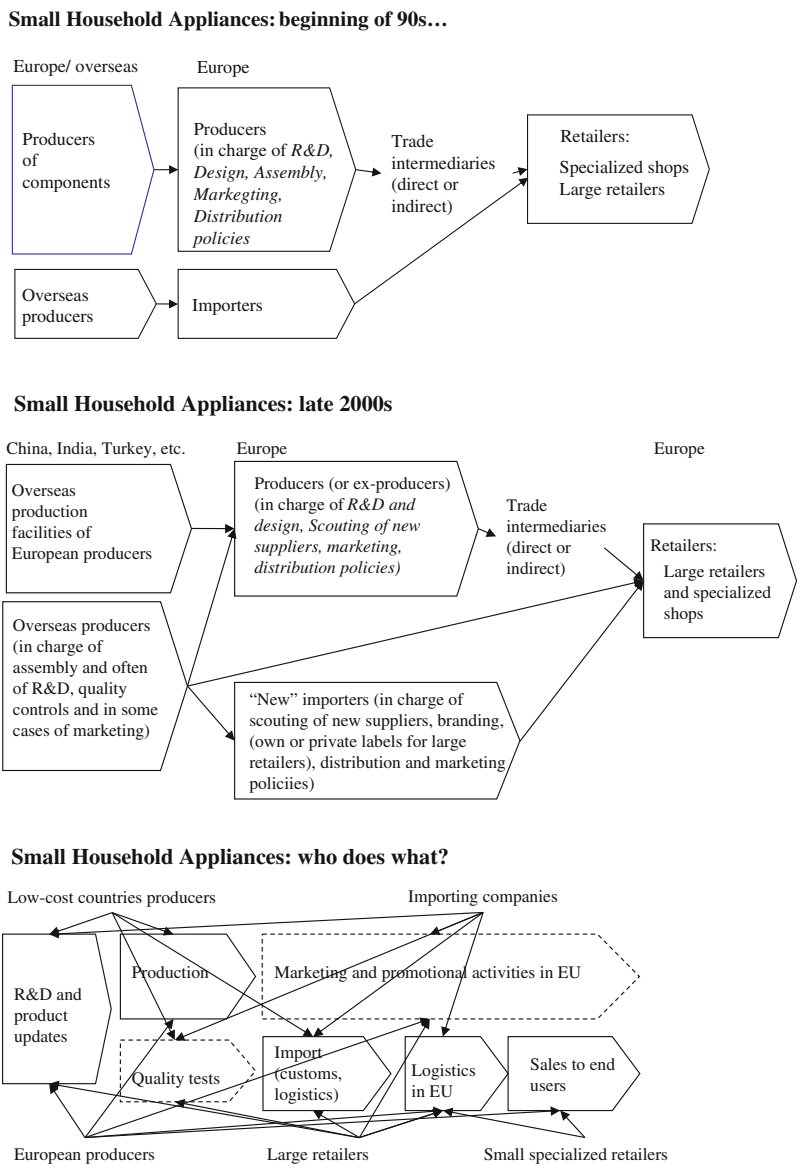

Fig. 5.1 Structural changes in the European small household appliances industry

areas". Figure 5.1 describes the structural changes occurred in the industry in question, comparing industry value systems in early 1990s and in mid-2000s.

Offshoring strategies on the one hand create momentary advantages to the firms in terms of the profit optimization, but on the other hand, in the long run, may call for the revision of the firms' competitive positioning. The evolved industry

structures with overlapping value chains of previously only vertically related industry actors require the new evolved approaches to the business models. The analysis of the sustainability of the firm's business models that traditionally relied upon the assumption that the firm's performance can mainly be challenged by industry trends or potential new entrants or by direct competitors (Porter 1985) with the primary focus on the later, should be completed by the analysis of the potential threat arriving from the vertical integration of value chains of international suppliers or buyers or distribution channels. Firms that happen to operate in the "grey area" of industry value system should evaluate the key factors that create most effective entry barriers and protect the sustainability of their competitive advantage, if there is any. Our exploratory research aims at understanding of the nature of the "grey area" in the international context, but the implications of the research could also be applied to a one-country situation characterized by a vertical integration mobility within an industry.

> Research question 1: In the international context, are there lasting overlaps ("grey areas") in the value chains of previously vertically related firms belonging to the same industry value system?

Our aim is to understand whether the existence of the "grey area" (the assumption was initially confirmed by an exploratory focus group with several industry opinion leaders) is a temporary phenomenon by longitudinal mapping of the value chain activities of offshore intermediaries (OIs) and its main clients and main suppliers.

5.2 The Resource-Based Sustainability of Competitive Advantage in Global Value Chains

The IB research largely employs the resource-based view of the firm for the explanation of the superior performance of internationalized firms. The ownership of superior management, entrepreneurship and technological skills is key for firms' international success (Dunning 1981; Hymer 1960). The accumulation of resources with the effects of scale, scope and learning economies and development of superior resources due to the favourable national context may also be hold responsible for the superior performance of firms on the international markets (Hitt et al. 1997; Kogut 1985b; Porter 1990).

The analysis of sustainability of the business model of offshore intermediaries (OIs), an organizational form connecting domestic manufacturers and foreign buyers, represents a relatively fresh field of study which recently received an increased attention (Peng and Ilinitch 1998; Trabold 2002). The studies of international intermediaries also readily acknowledge the resource-based "view" of the firm. Some of the first scholars studying OIs embraced the manufacturers' perspective and justified the existence of export agents and middlemen as a result of manufacturers' lack of capital and expertise necessary to export their products

directly (Bello and Williamson 1985). Therefore, specialized export companies are there to take on the risks associated with this activity. The "middlemen" (Manke et al. 2008) and "export intermediary" appellations are often intended for export trading companies (ETCs), that is, firms that share the country of origin with the manufacturers they serve (De Noble and Moliver 1989). Global intermediaries are not confined to export agents, but include also local import agents, as well as multinationals that have established distribution facilities in the targeted geographical market (Terpstra and Yu 1990). An examination of the German and British clothing industries pays attention to the existence of mediators between foreign suppliers and domestic retailers, referred to as "co-ordinating firms" and to their coordination capability for their homonymous role in the market's value chain (Lane and Probert 2004). Retailers and merchandisers, in particular, are said to possess "brand name capital" or privileged access to customers that enables them to externalize production to independent suppliers while leveraging their control to obtain lower costs and higher profits (Strange 2006). Peng and York (2001) in their study of the determinants of the performance of OIs expand this approach by integrating transaction costs theory, agency theory and resource-based view of the firm. Their study shifts the focus of the research from the principal to the agent, or OIs, firms that facilitate indirect exporting by foreign manufacturers and importing by domestic distribution (Perry 1990). According to the empirical study conducted on US-based trading companies, (1) the knowledge of foreign markets by OIs, (2) the willingness of OIs to take title to goods and (3) the involvement of OIS in trade of undifferentiated, simple, commodity products with low technological content that do not require complex selling skills—are positively impacting the performance of OIS. In the analysis of the resources on which an OI may relay on, Peng and York (2001) considered mainly the international experience of an OI personnel along with the negotiation abilities of its managers.

A multinational enterprise, including international intermediary, should therefore aim at control of resources that are difficult to acquire, to imitate or substitute in the international context. The competing firms are able, however, in most of cases to acquire resources (skilled and unskilled labour, access to distribution channels, even firm's reputation and brands, client's trust) on the resource markets (Barney 1991). In the international context, the new emerging multinationals are increasingly filling the gaps in their resources mix through mergers, acquisitions, alliances and partnerships (Mathews 2006).

Assuming that a firm's critical resources are not available or are overpriced on the marketplace, the sustainability of its competitive advantage will depend on the degree of imitability of resources and capabilities (or strategic assets) possessed by the firm, namely on the time compression diseconomies, assets mass efficiencies, interconnectedness of asset stocks, asset erosion and casual ambiguity or substitution of asset stocks (Dierickx and Cool 1989). Time compression diseconomies emerge when firm's "crash" interventions on stock creation reveal themselves less efficient (Amit and Shoemaker 1993). If the "internal" organizational learning in some cases can be accelerated, the reaction of other market players (clients, suppliers, competitors and other related firms and individuals) to firm's action (or

"external" learning) is hardly achieved through leapfrog tactics. Some attention was given to the internal organizational learning in the international context (Johanson and Wiedersheim-Paul 1975; Johanson and Vahlne 1977), but few studies were conducted about the importance of "external learning" as one of factors that cause time diseconomies. Brands, clients' and suppliers' trust access to supply and distribution channels and firm's reputation are not only the result of firm's activities, but also the result of third parties' reaction to firm's activities: "it takes two to dance". The asymmetry of information due to cultural, administrative, economic and other distances makes this concept far more important on the international markets than in the one-country context (Casson 1996; Ricart et al. 2004; Ghemawat 2007; Nigh et al. 1986). The internal organizational learning process may allow for acceleration strategies, due to the external acquisition of resources and capabilities. However, such approach limits itself to the assumption that the market's reaction is perfectly rational and can be guided by "intelligent" firms with a "right" set of resources and capabilities. In the real-life situations, managers and entrepreneurs often prefer to deal with domestic or foreign counterparts whom they trust and used to work with, rather than the fellow more efficient competitor of the later. The guided acceleration of the external learning is therefore more difficult and discontinuous, even if still may largely depend on the firm's ability to create favourable perception of its brands, reputation and credibility. We would like therefore to go beyond the country-wise contextualization of the value of firm's resources and capabilities (Miller and Shamsie 1996; Priem and Butler 2001; Wan 2005) and verify the existence of the external *learning* phenomena in the international context which we intuitively assume to be one of the main factors responsible for the survival of OIs working in the "grey" area of global value systems. Other barriers to imitability include assets mass efficiencies and interconnectedness of asset stocks related to the accumulation of a stock of resources and of a "right" mix of resources that facilitate the future resources creation. The value of firm's stock of such resources may also be enhanced through the resources' complementarity (Amit and Shoemaker 1993). Perceived decay rates of assets (assets erosion) may discourage potential imitators. The casual ambiguity in the resources creation exists as is often difficult to determine which kinds of resources will be most relevant for the firm's future. Most of the above-mentioned factors allow us to derive the importance of the time factor, strongly relevant for all above-mentioned imitation deterrents. The time factor becomes most relevant in the fast-evolving international context: in fact, the new emerging "dragon" multinationals is in fact pursuing the accelerated internationalization via external resource-building strategies (Mathews 2006).

Another important factor that protects the industry from the new entrants can be their unwillingness to enter the market. This aspect of sustainability of the business model of OIs was partially addressed by Anderson and Gatignon (1986) in their research that studied the impact of different factors on the efficiency of entry modes.

Research question 2: How OIs, presumably operating in the "grey" area of the industry international value system, manage to maintain their competitive advantage?

Our aim, therefore, will be to investigate on the sources that protect the sustainability of the business model of OIs presumably operating in the "grey area" of the industry value system.

5.3 Research Method

The research questions requiring careful mapping of industry value system activities among key players and understanding of the in-depth reasons of the long-term longevity of OIs, called for a within-case analysis as the basis for building a more focused investigation and for confirming the significance of our research questions (Eisenhardt 1989). When implementing a range of basic choices, the industry players employ certain operative methods that, under our hypothesis, can render their business model more sustainable in the future. To do such an evaluation, we focused on a longitudinal single-case study (Eisenhardt 1991).

First of all, we did a focus group with opinion leaders and market experts to identify the industry major changes. As the main body of the research, we provided a longitudinal quantitative and qualitative assessment of the selected firm and its competitive environment based on various data sources (Yin 1984): (1) over 30 one- to two-hour long interviews with 6 managers responsible for the key activities (purchasing, new product launch, marketing, finance, sales and administration, retailing), three area sales managers, the current CEO and the company founder, the head of the branch office in Hong Kong; (2) mapping of key processes of the selected company; (3) silent observations of three day-long meetings organized by company between its sales representatives and its clients (circa 40 participants); (4) longitudinal firm's statistics analysis; (5) interviews with executives and entrepreneurs in five manufacturing and commercial firms; (6) 8 in-depth face-to-face interviews with large distributors; (7) in-depth financial data analysis for the selected company and its competitors.

5.3.1 Industry Selection

We started our empirical study with the analysis of the international evolution of value system of Italian consumer electronics and small household appliances. According to the exploratory focus group held with 11 industry experts and opinion leaders (coming from distributing companies and industry magazines), the two industries represented common evolution dynamics from the point of view of the product maturity, price-based competition and consecutive production concentration and delocalization of production activities and, in some cases, of such

value-adding activities as design and technology development to low-cost countries. The consumer electronics and small household appliances underwent the "commoditization" process as few service, brand, performance- or quality-improving innovations remain possible. The price competition had an immediate negative effect on the firms' profitability whose possibilities and propensity to invest in technology development and customer service had been constantly diminishing.

Since the end of 1990s, the availability of low-cost suppliers and the incapability or unwillingness of the Italian distribution to source directly in the Far East stimulated the entrance of importing companies, sometimes through an improvised acquisition of containers with a vast range of products at best price in the Far East and consecutive distribution in Italy. Those actors became also the channel through which international producers started obtaining access to more evolved and sophisticated markets which stimulated them to improve their product quality and product range.

Our choice of industry is also justified by heterogeneity of firm strategies in dealing with globalization and increasing price pressures, remained as described by Baden-Fuller and Stopford in (1991).

5.3.2 Company Selection

CAT S.p.A was selected as the most appropriate for the analysis of our research constructs as: (1) its origin dates back to 1983 offering the opportunity to have a sufficiently long time frame for the analysis of strategic factors accumulation (Eisenhardt and Graebner 2007); (2) the firm showed the best performance in 2008 (17 mill. Euro, +25 % respect to 2007; +48 % in 2007/2006), it grew more than the industry on average (+3 % in 2008/2007); (3) the financial holding (i.e. Dmail Group) is listed on Milan Stock Exchange allowing transparent and clear information. The longitudinal case study analysis allowed us to obtain insights on the international allocation of industry value system and to understand the underlying determinants of the inimitability and sustainability of some OIs' competitive advantage.

5.4 International Allocation of Industry Value Chain

The main players of the medium–low segment of analysed industries were low-cost foreign manufacturers, large integrated small domestic (Italian) retailers and large domestic (Italian) retail chains, domestic (Italian) producers that import a part of their product offer, domestic (Italian) wholesalers, OIs (as defined above). The international goods flow was also served by other firms, such as logistics and transportation firms or product quality testing firms.

In 2007, the low-cost manufacturers' value chain included the following activities: logistics, assembly and packaging of final products, sales to OIs and "direct" sales to foreign clients (in our case Italian retailers). Marketing and product promotion activities were limited to product catalogues and participation to trade fairs. Customer service was almost inexistent, mainly due to the low value of the final product. Other activities included product development (often based on imitation of well-known models and brands) and frequent adaptation of product characteristics to the requirements of key foreign clients in terms of quality, product performance and design, procurement, HR and other firm infrastructure activities. The emphasis of the value chain was shifting towards product development activities compared to the standardization and price focus back in the 1980s and 1990s.

CAT S.p.A., as an OI, performed the following activities: definition of the product portfolio in terms of product lines and product categories, scouting of foreign suppliers, product co-development with foreign suppliers, design of product packaging, on-site and pre-shipment product testing, logistics, vertical marketing channel selection and other marketing activities including proprietary brand management.

The domestic (Italian) producers' value chain activities underwent a drastic transformation in the past decade and in 2007 included the same activities performed by OIs and production of some "historical" products (such as grills and barbeques of G3 Ferrari); some of them also maintained or even delocalized in low-cost countries the product development and design functions (e.g. Bimar, Ariete, Imetec).

The small Italian retailers' value chain included the definition of the product range, procurement of products via wholesalers or via "direct" manufacturers' sales representatives and basic store management.

The large Italian retailers' value chain included the definition of the product range, procurement of products via OIs, wholesalers or via "direct" domestic or foreign manufacturers' sales representatives, marketing activating including advertising, promotional campaigns, advanced visual merchandizing, pre-sale and after-sale customer services and, in some cases, online promotions and sales.

The "grey" area of the industry value system contained therefore the following activities: (1) product development performed by OIs and foreign low-cost manufacturers; (2) quality testing performed by OIs and foreign low-cost manufacturers; (3) sell-in activities (transition of products from low-cost foreign producers towards retailers) performed by foreign low-cost manufacturers by direct contacts with domestic retailers, by domestic retailers by scouting and selecting of foreign low-cost manufacturers and also by OIs who act as middlemen between foreign low-cost manufacturers and domestic retailers; (4) brand creation: brands were attributed by some foreign or domestic producers, large retailers (so-called private labels, for example, Kennex by Coop or Watson by Metro) and by OIs.

According to the interviews and to the mapping of value chain activities of CAT S.p.A.'s and of its clients, suppliers and competitors, the overlaps in the

value chain activities of the above-mentioned players existed for at least a decade (starting from early 1990s).

The hypothesis of the persisting existence of the grey area can therefore be confirmed, even if the "grey" area had been continuously evolving: for example, the development of OIs capabilities encouraged large distribution to reduce their involvement in direct purchases from foreign low-cost producers.

5.5 Identification of Key Resources and Capabilities of OIs: CAT

In order to assess CAT's ability to maintain its competitive advantage (RQ2), we identified its main capabilities, identified indicators that allowed us to compare them with CAT's direct competitors and, as suggested by Dierickx and Cool (1989); we then analysed their imitability in terms of time diseconomies, asset interconnectedness and asset stocks, asset erosion and casual ambiguity.

Definition of the product portfolio and product co-development: firm's product selection and development capability relied on the firm's ability to predict market needs on the basis of strong interfunctional links between sales, procurement and product development departments. The three functions jointly analysed market trends (industry trends, firm's own and its potential clients' sales statistics, product offer of large producers and of their direct competitors), defined the tentative product portfolio and then visited most of important trade shows in the Far East and some major low-cost producers compiling the firm's product portfolio. In some cases, CAT directly intervened on product design and performance by suggesting product alterations to producers. The firm's advanced capability to product development was measured by a large number of product categories, significant product renewal (new product categories and articles introduced each year), short product development lead time, share of product modified upon CAT's request in terms of colour, design and technical characteristics).

Procurement: firm's ability to select reliable suppliers (measured with longevity of suppliers) was based on frequent company visits by firm's management, pre-visit analysis of supplier's financial position (where possible). The local personnel of the branch office in Hong Kong was also largely involved in supplier's scouting activities.

Product testing: capability to guarantee the product quality in many cases exceeding clients' expectations was supported by four product quality testing procedures (sample testing along with the technical description of the product technical characteristics, in-line inspection, pre-shipment sample inspection and final inspection in Italy before the delivery to the retailer) which were not compulsory. The product testing activities were performed internally (technical office) and by external international entities employed by CAT.

Vertical marketing channel selection: CAT's capability to work on multiple channels creating important product and activity synergies was the result of careful monitoring of channels' needs and of the firm's related ability to create ad hoc product portfolios and brands in order to avoid conflicts among different channels (e.g. specialized retailing and large distribution).

Domestic logistics: CAT's capability to efficiently manage domestic (Italian) logistics (measured by competitive delivery time to clients) was based on firm's own automated warehouse, long-term contracts with three logistic service providers and firm's own truck for emergent deliveries. CAT's competitive delivery lead time was also the result of immediate order processing procedure (whereas most competitors employed 4–5 days) and of the key product items availability at the warehouse in Italy. Activity and knowledge sharing with the parent company of CAT (a leading direct marketing company in Italy) further enhanced CAT's logistics capabilities.

If some of the firm's resources (such as human resources, financial assets, firm's warehouse) could have been initially acquired on strategic asset markets, the internal process of accumulation and resource interconnectedness allowed for superior firm performance and could serve as a base for the sustainability of the firm's competitive advantage (Table 5.1).

5.6 "Internal" and "External" Time Compression Diseconomies

CAT S.p.A., initially a family-run company, started importing activities in 1983 with a stock of tradable resources (basic human and financial resources and firm's owned warehouse in Italy); at that time, the founder used to go only once a year to the Hong Kong Trade Fair, without a product plan and a list of purchasing criteria, where he would collect manufacturers' catalogues and, coming back to Italy, would order those products to be sold in large quantity, basing his decision mainly on price. The company always tried, however, to comply with its clients' quality expectations by performing random internal quality tests on samples and upon product delivery to CAT's warehouse in Italy, but without involving external quality certification entities and without insisting with suppliers on modifications of their standard products as the product development department was literally inexistent. CAT sold its products (small appliances were not sold until 1992) via a general catalogue (a sort of "bazaar") to the specialized retailers, competing directly with manufacturers at the low end of the market. All contacts between CAT and suppliers were managed by the purchasing office in Italy.

The firm's operations grew, but firm's predominantly intuitive approach to management remained unchanged until the acquisition by Dmail Group, one of the largest direct marketing firms in Italy, in 2000. CAT, therefore, obtained an access to the extensive experience of Dmail on the international supplying markets:

Table 5.1 CAT's capabilities and indicators (2007)

CAT's capability	Indicator	CAT's value	Average competitor's value (as perceived by CAT)
Product selection and development	Product categories (no.)	56	11
	New product categories and articles introduced each year (no.)	243	43
	Product development lead time (months)	3	~4
	Product co-designed with supplier (percentage on total no. of models)	76 %	13 %
Selection of reliable suppliers	Suppliers' rotation rate (percentage of suppliers with at least 10-year long contracts with the firm)	36 %	Close to 30 % for "old" players (who often manage less than 50 suppliers)
Product quality	Percentage of defects	<0.1 %	~3 %
	No. of products sequestered by state quality control entities	0	4
Capability to work on multiple channels	No. of channels served	4 (large retail chains, small retailers, wholesalers, direct sales)	
	Agents (no.)	26	15
	Clients concentration index (top 10 clients on 100 % of sales)	28 %	79 %
	Privately managed brands (no.)	4	1
Domestic logistics	Average delivery time to clients (months)	3	5

Source Company data and interviews

Dmail's sourced its products in low-cost countries through its advanced and well-organized structure and distributed them via Internet, directly owned shops and via mail orders. After the acquisition, CAT restructured its major activities by focusing on quality improvement, delivery time reduction and on the development of new distribution channels (e.g. large retail chains).

In 2006, Dmail appointed a new CEO (an engineer with an MBA title and a 10-year international experience) with the objective to turnaround CAT's operations while maintaining the company's basic values ("historical" attention to the product quality, partner relationships with suppliers) and competencies (e.g. in managing logistic companies). In 12 months, the new management completely restructured the product offer by careful segmentation and renewal of product catalogue and launching of a new brand for the large distribution. The firm restructuring included implementation of interfunctional product development and procurement processes, constitution (in 2006) of a branch office in Hong Kong for the daily supervision of international suppliers, organic growth of the quality testing department, creation of a commercial department with three sales area managers dedicated to each of distribution channels, automation of the firm's warehouse, reorganization of the back office that led to the reduction in order processing time. The evolution of CAT's personnel and external indicators is shown in Table 5.2.

The pre-shipment and on-site quality tests started being routinely managed by international competent bodies (with which, however, CAT had already had long-term relationships). The firm's employees (not only the CEO, as it happened in the past, but also the heads of product development and procurement departments) started to participate to other trade fairs in Asia, USA and Germany and to scout potential producers also outside of China while maintaining long-lasting historical

Table 5.2 CAT's development indicators

	1983	1993	2003	2007
Year of entry in CAT of personnel employed in 2007	3	12	22	27
Quality test department personnel (no. of persons)	0	1	1	3
Purchasing department personnel (no. of persons)	1	1	1	3
Product development department personnel (no. of persons)	0	0	1	2
Marketing and graphics personnel in sale department (no. of persons)	0	0	0	2
Agents (no.)	4	17	22	26
Warehouse (sq. metres)	1,300	3,000	7,000	8,800
Product lines (no.)	15	160	359	637
Suppliers (no.)	7	15	98	138
Clients (no.)	500	1,103	1,710	1,997
Large retail chains				
• No.	0	3	10	19
• Percentage on total revenues	0	10	30	50
Customer care centre personnel (no. of persons)	43	133	247	217

Source Company data and interviews

relationships with the firm's most reliable suppliers. With the time, the suppliers' and product portfolio selection criteria, initially a result of the CEO's intuition, started being developed via a complex mechanism of sales statistics analysis, competitive intelligence, in-store observations, brainstorming with sales area managers and key clients. The selection criteria evolved from price-quality evaluations to a set of variables that included suppliers' reliability, possibility of co-development, possibilities of product or regional exclusivity. The sales department's responsibilities evolved from mere sales activities to a complete product offer management that included definition of graphics, packaging and branding activities.

The firm's "internal" capabilities development received a significant spur after the acquisition by Dmail and the nomination of the new CEO, which, however, would not have been possible without firm's intangible assets being strongly related to the "external market learning" (established relationships and reputation gained with Italian retailers and with some key foreign suppliers) accumulated in 25 years of firm's operations on the market. The long-term relationships with suppliers (more than one-third of suppliers had been working with CAT since mid-1990s) would lead to a preferential track for CAT's orders in terms of suppliers' production planning and would give CAT an advantage of exclusive contracts for product distribution. The long-term relationships with retailers would, on the other hand, lead to an increasing share of CAT in clients' product portfolio who rarely entrusted significant contracts to distributors without having "tested" them for several years.

5.7 Asset Efficiencies: Sustainability of Scale and Scope Advantages

Asset efficiency effects, intended as lower marginal cost of production of further additions to asset stock (Dierickx and Cool 1989), in CAT's case resulted in the possibility for the firm to include large retail chains in its clients' network, initially composed by specialized retailers. The infallible organization of shipments to large retail chains derived from CAT's long-term connections with suppliers network and quality testing entities, logistic companies and CAT's accumulated know-how and financial strength.

The scope advantages of CAT consisted in sharing of CAT's activities and assets (e.g. personnel, customer care centres, warehouse facilities, transport for urgent delivery) among its 1,997 clients (as at 2007): a single, even large, retail chain would incur much higher expenses compared to CAT. In fact, CAT accumulated a significant bargaining power with its suppliers (including 138 producers and dozens of suppliers of services and necessary external consultants, such as logistics and quality testing) whom it also put in competition in order to obtain best possible prices.

CAT also benefited from synergies with its parent company, Dmail, in terms of the knowledge sharing of market trends and negotiation with manufacturers and logistic companies. Dmail's direct marketing activities also provided CAT with an early market feedback on new product categories.

5.8 Asset Erosion and Casual Ambiguity

CAT, in order to avoid the decay of its main capabilities (product selection and development, suppliers' management, product quality, multiple distribution channels management and domestic logistics), had constantly been investing in their maintenance (Table 5.2). CAT invested in the preventive product quality tests in order to fuel its image as a reliable partner, whereas its competitors often preferred ad hoc investments in product repairs. CAT also attempted to create entry barriers by offering post-sales customer service (information about CAT's private label products and eventual repairs) directly to the final consumer.

Ambiguous casual relation of CAT's critical capabilities and its performance laid in general erroneous perception of OIs business model as based mainly on competitive pricing, whereas, according to discussions with CAT management, agents and clients, the main determinants of CAT's success were in its customized approach in fitting various distribution channels' requirements with ad hoc product ranges and brands and assured quality standards along with competitive prices.

5.9 Conclusions

The aim of our study was twofold. Firstly, we analysed one of the many industries that experienced important structural changes thanks to the exponential implementation of offshoring strategies by industry incumbents. Our study allowed to confirm, via a within-case analysis of the evolved international configuration of consumer electronics and small household appliances value system, the existence of the lasting overlaps ("grey areas") in the value chains of previously non-competing firms belonging to the same industry. Secondly, we investigated how firms, operating in the "grey area" emerged thanks to the proliferation of offshoring strategies within the industry's global value system, manage to maintain and defend their competitive advantage.

The case of CAT S.p.A (a firm operating in consumer electronics and small household appliances industry as an offshore intermediary between Italian retailers and Far Eastern low-cost manufacturers), analysed in 2007, confirmed the first hypothesis about the existence, since mid-1990s, of overlaps in product development, quality testing, branding and selling activities among low-cost manufacturers, OIs and Italian retailers. The morphological analysis of CAT's resources and capabilities revealed the importance of "external" time compression

diseconomies that regarded lasting in time acquisition of trust from the part of CAT's suppliers and clients. Asset mass efficiencies allowed CAT to overcome its initial limitations as a supplier of specialized retailers and to start working with large retail chains, which led to further asset accumulation. Asset accumulation in terms of number of suppliers and product lines, maintained by CAT by continuous investments, allowed it to partially transfer its cost, quality and timely delivery advantages to the growing, as a consequence, number of its clients. CAT's asset interconnectedness existed also in terms of the complete service offer to the retailers in terms of product portfolio selection, product testing, branding, logistic services and customer after-sale services. CAT's competitive advantage was also protected by existing casual ambiguity between the firm's performance and the underlying factors as CAT was perceived by its competitors mainly as asset accumulator and scale economies seeker. The capabilities developed by CAT served not only in its direct competition with other OIs, but also as a prevention of complete potential vertical integration of CAT's clients (dissuaded by excellent performance of CAT in terms of service level and pricing, but also by the completeness of CAT's offer) and of CAT's suppliers (discouraged by CAT's development of brands and its strong lock-in relationships with the most important distribution channels for their industry in Italy).

Our exploratory study limits itself to a singular industry case analysis; our findings and our attempts to find indicators characterizing firms' resources and capabilities would allow other researchers to further explore the allocation of industry value systems and to apply resource-based view of the firm in its analysis of 360° sustainability of firm's business model in other international contexts, industries or in a single-country environment.

Our study opens several theoretical implications for future research.

In the first place, the acknowledged via an in-depth longitudinal case study the new phenomenon—"grey areas"—as a consequence of the implemented offshoring strategies should be further explored by quantitative research in other industries that experienced the diffusion of offshoring strategies.

Secondly, our study focused on the sustainability of the competitive advantage for an international offshore intermediary, leaving unexplored the challenges created by the appearance of "grey areas" on the industry competitive landscapes to the industry "main" competing incumbents, former final products producers. The implementation of offshoring strategies certainly allowed those firms to access low-cost resources, to focus on their "core" competences, to slim their corporate structures. But would they be able to defend their competitive positions in case of the intensification of the competitions, with new competitors that enter their "core" businesses and easily develop or access their "core" competences.

Thirdly, the acknowledgment of the "grey areas" in the industries value systems that faced the growing importance of offshoring calls for a deeper analysis of the industry structure and for a new theoretical model able to better explain the evolved industry value systems. According to Porter (1985) and other "classical" approaches to the industry structures, the value chains of the vertically related within-industry firms rarely overlapped: the end of a supplier value chain related to the

beginning of its customer value chain, with rare cases of overlaps. Figure 5.1 described in our chapter showed a whole different picture for one industry that increasingly experience the offshoring of the production facilities to the low-cost locations. The future research should account for the new spatial allocation of the industry value systems and propose a new framework that would account for the "grey areas" in the industry value systems and their implication for the firms' competitive positioning.

Our study also has important implications for the practitioners that evaluate the offshoring opportunities and that attempt to build scenarios for industry evolution. Since the 1970s, the growing specialization in most of manufacturing and service industries brought significant consequences for the firms' competitive strategies. Firms increasingly focused on their "core" competences and "core" businesses, presuming that those competences and businesses were surrounded by everlasting walls able to protect firms from competitors attacks. The source of the competitive advantage was perceived to be in the activity or asset itself rather than in the links among various activities. The latter definitely disappear if a firm decided to implement offshoring strategies, making its competitive position extremely vulnerable to the downward or upward integration of former suppliers or former customers that often managed to relatively easily learn to perform firms' core activities and to acquire the necessary set of competences. Our paper also creates a warning to a practitioner who perceives parallels in the dynamics in its firm's industry evolution with what occurred in the European small household appliances industry and calls for an important consideration about the future of the firm and or its "core business".

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