MANAGING TRANSACTION DEPENDENCE: AN EMPIRICAL EXAMINATION OF THE MODERATING ROLE OF RELATIONSHIP CLOSENESS ON THE USE OF VERTICAL CONTROL

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ABSTRACT

This study addresses a limitation of the Transaction Cost Analysis framework, namely its narrow focus on the dependence that arises from specific asset investments as a rationale for the installation of governance mechanisms in exchange relationships. We identify several additional components that contribute to the replaceability and rewards dimensions of dependence and consider how they arise from the underlying procurement need and decisions made by buyers and suppliers when arranging a new transaction. A conceptual model that proposes that the effect of these components of dependency on the use of vertical control is contingent on the nature of the pre-existing relationship between the buyer and supplier.

CONCEPTUAL BACKGROUND AND OVERVIEW OF MODEL

The notion that firms seek to exert control over their exchange partners has long fascinated researchers from a variety of disciplines, including marketing, organizational analysis, and institutional economics. Market-mediated exchanges are recognized to be heterogeneous phenomena, ranging from one-time (spot market) transactions to quasi-integration, or ongoing, relational exchanges (Heide 1994). Correspondingly, the means of governing these exchanges, i.e., exerting control to ensure partner performance, varies considerably (Heide and John 1992).

One governance mechanism that buyers may employ is to establish vertical control (Heide and John 1992), by which the seller cedes some of its decision autonomy to the buyer. However, the literature suggests that vertical control is not granted freely by suppliers; nor is it sought by buyers, per se, because of the costs associated with obtaining such control. Scholars have also noted that the use of this governance mechanism is subject to efficiency considerations, thus it may only be warranted under certain circumstances (Williamson 1985).

The transaction cost analysis (TCA) is one framework that elaborates on these circumstances and provides a general rationale for the use of particular governance mechanisms within exchange relationships. The predominant factor identified by this framework is the presence of transaction specific assets (i.e., investments that cannot be transferred for use with another exchange partner), which gives rise to a dependency situation (Williamson 1985) and the threat of opportunism by the exchange partner. While both parties may make these dedicated investments, the relative symmetry of specific asset investments is expected to be a key determinant of whether additional control mechanisms are crafted into the exchange relationship.

However, TCA fails to recognize is that dependency can also arise from other factors in the task environment, which may be unrelated to whether specific assets are present to support the particular transaction. Drawing on the industrial marketing, organization, and sociology literatures, we find that dependency (and its obverse, power) is also a function of whether a customized product is being procured, the number of alternatives available (size of the supplier set), the degree of purchasing and sales concentration, and the risk involved (in terms of dollar amount and/or importance of the resource towards fulfilling organizational goals) (Bunn 1993; Heide and John 1988; Pfeffer and Salancik 1978).

In this paper, we also take into consideration recent arguments that the relational context also plays a significant role in governance decisions (e.g., Granovetter 1985). We propose an extension to TCA theory by positing that the effects of transaction specific assets and other sources of dependency are contingent on the nature of the preexisting relationship between the buyer and supplier. (as depicted in the Figure).

The research setting chosen for this research is SIC major group 28, manufacturers of chemicals and allied products. A national mail survey was administered. Measurement validation followed the procedures recommended by Gerbing and Anderson (1988). Tests of our substantive hypotheses were performed using ordinary least squares (OLS) regression analysis.

Our results reveal that relationship closeness moderates the effect of two components of dependency related to replaceability, investment asymmetry and product customization, as well as the reward component of sales concentration. No moderating effect was found relative to the other rewards components of purchasing concentration, size of the supplier set, overall dollar amount, and item importance.

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Figure 1
Conceptual Model