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Emilia-Romagna

By

Massimiliano Mazzanti, Sandro Montresor and Paolo Pini

**Danish Research Unit for Industrial Dynamics**

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# **Outsourcing, Delocalization and Firm Organization: Transaction Costs vs. Industrial Relations in a Local Production System of Emilia- Romagna**

**Massimiliano Mazzanti**

Department of Economics, Institutions and Territory  
University of Ferrara, Italy

**Sandro Montresor**

Department of Economics  
University of Bologna  
40125 Bologna, Italy  
Tel: +39.051.20.92651  
Fax: +39.051.20.92670

**Paolo Pini**

Department of Economics, Institutions and Territory  
University of Ferrara, Italy

## **Abstract:**

The paper aims at investigating how far transaction costs economics (TCE) concurs in the explanation of outsourcing decisions in firms characterized by “thick” industrial relations, that is where unions and employees are involved in, and are sometimes able to affect, the relative managerial decisions through participatory formal and informal mechanisms. What is more, the paper aims at investigating whether the concurrence of TCE and industrial relationships has different outsourcing implications for firms which are also involved in delocalization strategies. An empirical model, translating a set of theoretical correlations between an original outsourcing extent variable, on the one hand, and a number of proxies related to TCE, industrial relations and delocalization, on the other hand, is applied to a representative sample of manufacturing firms for the local production system of Reggio Emilia (RE) (in Northern Italy).

Overall, the empirical application shows that the role of TCE in accounting for outsourcing in the LPS of RE is quite blurred, if not even contradicted, while the role of industrial relations emerges instead quite straightforwardly. Finally, RE firms generally use outsourcing and international delocalization in a complementary way, but the correlation between outsourcing and delocalization turns out to be dependent on the kind of activity and of the nature of the delocalization channel.



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# 1 Introduction

Empirical evidence shows that *outsourcing*, meant in general as “the use of goods and services produced outside the enterprise” (OECD, 2007, p.15) has risen dramatically in the last decay, both in volume and in value. This has spurred a substantial increase of interest in economic literature for the phenomenon, in particular for those situations in which outsourcing occurs abroad, that is for what is usually called *offshoring*: either in the form of some kind of international sub-contracting to non-affiliated enterprises, or of some extent of production transfer abroad within the same group of enterprises or to newly created affiliates.

The standard approach in interpreting the outsourcing phenomenon focuses on transaction costs (e.g. Grossman and Helpman, 2002), ownership allocation (Grossman and Hart, 1986), formal vs. real authority (e.g. Aghion and Tirole, 1997) and, in general, on the entailed incentive conflicts which emerge between the “outsourcer” and the “outsourcee” (Foss, 2000). In particular, transaction cost economics (TCE) has emerged as an interesting explanation of the “make-or-buy” choices of the firm which conveniently matches the nature of the firm organization with that of the relevant transactions (e.g. Gonzalez-Diaz, Arruñada, and Fernandez, 2000).

In spite of its notable strengths, the TCE account of outsourcing relies on a set of non fully satisfactory hypotheses (Mahnke, 2001). First of all, and in general, it does not address the ‘real time’ (Langlois, 1992) in which outsourcing (as well as vertical integration) decisions are taken, and thus disregards phenomenon such as path-dependency, inertia and “governance inseparability” (Argyres and Liebeskind, 1999). Second, and in particular with respect to its international manifestation, TCE and the other contractual accounts of outsourcing (and of vertical integration) leave production as such “out of the door” (Langlois, 1992; Montresor, 2004), and ends up with treating the delocalization decisions of the firms as a pure variant of the broad outsourcing paradigm.

While possibly unproblematic in some other contexts, the two previous assumptions can be argued to limit the interpretative power of TCE with respect to the outsourcing decisions of firms which are “embedded” (Granovetter, 1985) in local production systems (LPS), of

which “industrial districts” represent the most notable example. On the one hand, in these contexts the presence of a consolidated ‘social capital’ usually mitigates the opportunism of the agents embodied by TCE, while the “thick” industrial relations of the local firms’ organization makes governance inseparability quite sensitive for the outsourcing decision. On the other hand, rather than a pure specification of outsourcing, in the same contexts delocalization decisions intertwine with it in a way – complementary or substitutive – which is also affected by the firms’ governance and by their industrial relations.

As a sort of illustrative test of this argument, the paper refers to a specific LPS of Emilia-Romagna (i.e. Reggio Emilia) in order to address two related research questions: (i) how far TCE matters in the outsourcing decisions of firms characterized by ‘thick’ industrial relations and embedded in a “typical’ local production system; (ii) whether and how the delocalization choice of these firms correlates with their outsourcing decisions.

In addressing these research questions the paper conveys at least three elements of originality. First, from a conceptual point of view, the outsourcing and delocalization decisions of firms are embedded in a setting where transaction costs are affected by idiosyncratic local elements, mainly the nature and quality of workers involvement in firm innovation decisions and industrial relations. Second, from a methodological point of view, both outsourcing and delocalization are captured going beyond standard, pure dichotomic variables (of the “yes” or “not” kind) and rather referring to their actual extent and to their specific patterns. Third, from an applied point of view, the empirical investigation is carried out by exploiting two consequential surveys administered to the same firms (in 2002 and 2005) in order to reduce the potential endogeneity stemming from the simultaneity between outsourcing and its potential drivers.

The structure of the paper is the following. Section 2 sketches the theoretical background of the paper by addressing the interpretations outsourcing and delocalization find in a LPS environment. Section

3 illustrates the extent of outsourcing and delocalization in the LPS of Reggio Emilia. Sections

4 and 5 present the model and the dataset through which the two phenomena are empirically investigated. Section 6 comments the main results and Section

7 concludes.

## **2 Outsourcing and delocalization: TCE and industrial relations in local production systems**

Although clearly related, *outsourcing* and *delocalization* are far from being coincident notions. Broadly defined as the use of goods and services produced externally, *outsourcing* can occur also in the absence of a *delocalization*, that is of a “a geographical movement or transfer of productive activities ...” ( UNIDO, 2003, p.17): such as when it occurs through subcontracting. Vice-versa, the decision of delocalizing some production activities out of the firm’s local and/or national system does not necessarily entail that their outcome is then re-used by the firm itself *in loco*, that is outsourced.

Rather than coincident, therefore, the two phenomena can be somehow related. In other words, firms can play with the two strategies as either complementary or substitutive, and their respective rationale and their relationship can find different specifications depending on the theoretical approach and on the relevant context of analysis.

Following the standard view, as we said, outsourcing should be generally explained in the light of TCE. In brief, by simply considering the firm’s attempt of overcoming the risk of post-contractual opportunism (“hold-up”) by externalizing non specific assets in the presence of low market uncertainty (Williamson, 1975). In this vein, among the others, the intangibility of the firm’s activity, on the one hand, the extent of its product differentiation and geographical diversification, on the other hand, can be seen as, respectively, hindering and favoring the resort to outsourcing (Gonzalez-Diaz, Arruñada, and Fernandez, 2000).

This way of looking at outsourcing strictly relates to the standard approach to delocalization, based on the idea of “international fragmentation of production” (e.g. Jones and Kierzkowski, 2001). In brief, integrated production activities would get segmented across international networks providing extra *coordination costs* (e.g. transportation and communication costs) are offset by lower production costs (e.g. less production factors and factor price differentials) (Grossman and Helpman, 2005). Also by following this simple basic idea, however, the correlation between outsourcing and delocalization can be twofold. Indeed, outsourcing and delocalization might be thought to correlate positively, by retaining that the search for production cost advantages via delocalization spurs the conversion of fixed costs into variable ones through outsourcing. Conversely, the correlation can be

thought as negative, if high international co-ordination costs are retained to spur firms not to disintegrate in order to avoid further contractual costs.

Although a theoretically consistent explanation of the phenomenon, TCE arguments might however not be the whole story. First of all, a “combined” approach, which integrates TCE with a resource-competence-based view of the firm, would suggest that for outsourcing to occur specialization advantages are required and should outweigh the transaction costs of trading (e.g. Jacobides and Winter, 2005; Nooteboom, 2004). Following this perspective, the organizational placement of the outsourced activities in the firm, typically in a correspondent division, should be considered as a means for codifying interfaces-knowledge among the firm’s activities themselves, and thus as an outsourcing enabler<sup>1</sup> (Mahnke, 2001). And the same holds true for the hierarchical degree of the firm’s organization, which thus contrasts the pure TCE view of it as a spanner for multiple decision-control mechanisms, which might make outsourcing more conflictive (Mazzanti, Montresor, and Pini, 2006a).

Going beyond standard TCE one should also, and above all, recognize that, in “real time”, the outsourcing firm is affected by both the history of its contracts (Argyres and Liebeskind, 1999; Langlois, 1992) and by its resources’ complementarities (Mahnke, 2001). This argument makes of the firm’s age a crucial variable in accounting for outsourcing. What is more, it sets the presence and the role of unions, along with the nature of the firm’s industrial relations, at the centre of the stage. Indeed, the direct participation of the workers, and of their delegates, to the firm’s decisions, augments the degree of the firm’s “governance inseparability” and might interact, if not even contrast, standard TCE predictions (Mazzanti, Montresor, and Pini, 2006a).

Last, but not least, in dealing with outsourcing one should also try to overcome the “atomistic” view of the TCE firm (Montresor, 2004) and retain that the outsourcing firm is embedded in specific socio-economic contexts (Granovetter, 1985). This embeddedness is particularly relevant with respect to local production systems (LPS) such as, for example, industrial districts (e.g. Brusco, 1982; Becattini, 1990). Within this socio-economic context outsourcing takes on special features, quite different from large, relatively more isolated

companies. In many Italian industrial districts, for example (e.g. Bramanti, 1992; Goodman, Bamford, and Saynor, 1989; Russo, 1986), outsourcing has been found to follow a 'cooperative', rather than a 'competitive' mode, "relying on tacit performance agreements, trust, and reciprocal adjustment" (Suarez-Villa, 1998, p.7). And this has been proved to prevent the emergence of those disparities among firms - for example, on the access to physical and human capital, knowledge and competences - which could make the relative transaction end up impoverishing the innovative capabilities of the smaller, or weaker partner (e.g. Suarez-Villa and Rama, 1996). More in general, the territorial proximity between purchaser and provider of the outsourced activity may potentially generate a number of "outsourcing economies" (e.g. Taymaz and Kilicaslan, 2005).

Going beyond TCE, and focusing on LPS firms, also the relationship between outsourcing and delocalization finds a more articulated explanation. From this point of view outsourcing has been investigated as one of the channels through which local systems are becoming sub-systems of broader, global production networks (e.g. Carabelli, Hirsch, and Rabellotti, 2007; Camuffo, 2003) with crucial implications for their employment levels, labour intensity, skill-upgrading (e.g. Federico, 2005; Murat and Paba, 2005). Once more, looking at delocalization as a competitive strategy for LPS, and adopting a more comprehensive view of the firm, the relationships between the two phenomena appears twofold. On the one hand, the search for upgrading in high-level global value chains (e.g. Humphrey and Schmitz, 2002) can spur the firm's reliance on actual external providers, so that outsourcing and delocalization would correlate positively. On the other hand, however, the entrance in a wider network of external relationships (via delocalisation) might spur the firm not to outsource given the pressure of industrial relations for a substitutive choice: accordingly, outsourcing and delocalization would correlate negatively.

In conclusion, the picture one gets by approaching outsourcing and delocalization with respect to a LPS environment appears quite complex. A number of potential explanations and relationships emerge and find different specifications depending on the relevant context of analysis. In order to get a more specific picture, in the following we refer to the LPS of Reggio Emilia which, although idiosyncratic in some respects, share some of the features of

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<sup>1</sup>Firms' activities and capabilities are in fact the easier to separate from each other, for example through outsourcing, the more this 'interface knowledge' is explicit, that is represented by norms and rules if not even by formal organizational relationships.



the typical LPS of Emilia-Romagna, and could thus help us in obtaining results with a certain degree of replicability.

### **3 Outsourcing and delocalization in the local production system of Reggio-Emilia**

Reggio Emilia (RE, Figure 1) is a province which hosts a particular local production system (LPS), characterized by a predominant presence of small and medium enterprises (SME) and strongly specialized in chemical, machineries, food, textile, and non metallic minerals sectors (Pini, 2004; Seravalli, 2001). The prevalence of SME is partially justified by the existence of two districts within the RE industrial system borders: the first, regarding non-electrical machinery and equipments - machinery for mechanical energy and agriculture in particular; the second, concerning non metallic mineral products - ceramic tiles in particular. Given the sectoral distribution of the firms, it can be easily infer that most of them operate in a district-like environment (Brusco, Cainelli, Forni, Franchi, Malusardi, and Righetti, 1997), usually constituted by networks of SME.

Insert Figure 1 around here

The LPS of RE is also characterized by the presence of public organizations, providing funds for services, infrastructures, social security and so on, which contribute to create a particularly efficient institutional set-up (Seravalli, 2001). In this context, a fundamental role is played by strong, well rooted and proactive unions, which in fact shape the RE industrial system.<sup>2</sup> In a strategic framework to which the conflict and the inner adversarial nature of the industrial relations are not unknown, the relations at firm level between management and union representatives are also driven by participative and cooperative behaviors in the recognition of mutual aims and gains (Antonioli and Pini, 2004).

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<sup>2</sup>This is especially true for the role of CGIL, the traditional confederation with socialist and communist origins. For an overview of the union history and the linkages with political party, see Baglioni (1998).

The overall characteristics of the industrial context outlined above set the RE industrial system within what have been called “the local production systems” of the Northern Italy (Seravalli, 2001), and make of it a paradigmatic version of the so called “Emilian model” (Brusco, 1982; Brusco and Solinas, 1997; Amin, 1999), marked by the presence of a district-like industrial system, a well marked entrepreneurship spirit and an equally strong, deep-rooted unionism. On the other hand, however, RE distinguishes for the importance hold by the industrial relations system, as well as for that of the innovation activities and of their relationship with the former. In particular, the typical “dense” industrial relations of the area and the participation of workers’ delegates to managerial decisions in work organization suggest to carefully consider, along the argument developed in Section 2, the potential role of industrial relations themselves and of TCE in accounting for outsourcing and delocalization decisions.

Before moving to this latter point (in Section

4), it is worthwhile referring to a recent survey on the province of RE (Antonioli, Delsoldato, Mazzanti, and Pini, 2007) in order to appreciate the actual extent to which outsourcing and delocalization are diffused in it, and their particular characteristic features.

As far as outsourcing is concerned, this survey distinguishes as many as 19 activities, which can be grouped into three classes according to a functional criterion: (i) “ancillary activities” (*ANC*), so to say accessory to the production process as such, meant as the transformation of production inputs into output (e.g. janitorial services); (ii) “production supporting activities” (*PRODSUP*), not primarily productive, but contributing to the production process more directly than the former (e.g. engineering); (iii) “production activities” (*PROD*) as such.

Insert Table 1 around here

A glance at Table 1 reveals that outsourcing is a quite pervasive phenomenon in the LPS of RE, although with important differences in the number and the nature of the activities which are externalized. As in other contexts, the outsourcing patterns of the RE firms are strategic, as they show a propensity to outsource material, routine-based activities with a

low-value added, and to retain internally intangible activities with a higher value-added. What is more, outsourcing appears closely related to the intrinsic characteristics of the same LPS. In particular, unions and industrial relations, with a long tradition in the area, have an important role in the management's implementation of outsourcing strategies (Mazzanti, Montresor, and Pini, 2006a; Antonioli and Tortia, 2004).

As far as delocalization is concerned, the same survey allows to distinguish different export channels and forms of delocalization of production activities (Table 2). Given the large extent of export of RE firms – more than 50% of the whole production is for foreign markets, and 70% is the share of firms with export activities<sup>3</sup> – it is quite remarkable that only 15% of firms have own establishment for production abroad, while many firms make use of other channels for export, such as commercial networks and partnership with foreigner firms. The share of firms with establishment for production abroad does not change a lot if we consider activities not related to export (17%).<sup>4</sup>

Insert Table 2 around here

Keeping in mind this recognition of outsourcing and delocalization in RE, let us now move to the role that TCE and industrial relations play for them. This is done by applying an empirical model to a combined dataset which are both described in the following.

## 4 The empirical model

The empirical model used in the present paper is an “augmented” form of that we developed in a previous work to investigate the general profile of the RE outsourcing firm (Mazzanti, Montresor, and Pini, 2006a). The major innovative element with respect to that benchmark is the introduction of a temporal lag between outsourcing, on the one hand, and the other explicative variables on the other. The reduced form we estimate is then the following:

$$y_{OUT_{i,t}} = \beta_0 + \beta_1 x_{TCE_{i,t-1}} + \beta_2 x_{IR_{i,t-1}} + \beta_3 x_{DELOC_{i,t-1}} + \beta_4 x_{STR_{i,t-1}} + e_i \quad (1)$$

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<sup>3</sup>Although this is the case for firms with at least 49 employees, the percentages do not change much if we consider also firms with 20-49 employees.

In Equation (1)  $y_{OUT_{it}}$  represents the outsourcing ‘output’ of firm  $i$  at time  $t$ . Rather than considering a simple dichotomic variable (of the “yes” or “not” kind), as in the majority of the other studies, we here refer to two different variables of outsourcing extent. The first one tries to capture the “general outsourcing extent” of firm  $i$  ( $OUT_i$ ) by measuring the average extent to which firm  $i$  externalises the  $n$  activities considered:

$$OUT_i = \frac{\sum_j OUT_{ij}}{n} \quad (2)$$

where  $OUT_{ij}$  is the extent to which firm  $i$  externalises the activity  $j$  out of  $n$ , with the following positions: 0 (no externalized), 1 (partially externalized), 2 (mainly externalized), 3 (totally externalized).

The second outsourcing variable instead refers to the “specific outsourcing extent” of firm  $i$  ( $OUT_{ik}$ ) as the average extent to which it externalises the activities of a certain kind  $k$ , where  $k = ANC, PRODSUP, PROD$ .

As far as the independent variables are concerned,  $x_{TCE_{it-1}}$  collects a set of variables related to TCE at time  $t-1$ . More precisely, following Mazzanti, Montresor, and Pini (2006a), and along the arguments of Section 2, we refer to both standard TCE variables and to variables which try to augment it by retaining the firm’s organization and its governance inseparability (Tab. 3).

Insert Table 3 around here.

As has been discussed in Section 2, TCE arguments are in the present paper considered along with outsourcing explanations based on industrial relations, by retaining a number of variables,  $x_{IR_{it-1}}$ , built up by Antonioli, Mazzanti, Pini, and Tortia (2004) and described in Table 4.

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<sup>4</sup>Both the shares increase to almost 20% if we consider only the samples of firms with at least 49 employees.

Insert Table 4 around here.

Another innovative element of the model with respect to the benchmark is the fact that outsourcing is here related to a number of variables,  $x_{DELOC_{it-1}}$ , described in Table 5, aimed at capturing the extent and the characteristics of the delocalization strategies of the RE firms.

Insert Table 5 around here.

Finally,  $x_{STR_{it-1}}$  refers to a number of controls, among which, following the results obtained in previous studies (Mazzanti, Montresor, and Pini, 2006a, 2007), we have also retained innovation and flexibility related variables (Tab. 6).

Insert Table 6 around here.

It should be stressed once more that, with respect to the benchmark, the empirical model (1) is structured on a hybrid cross section environment, which includes most covariates in lagged terms, with an important benefit in terms of reduction of potential endogeneity stemming from simultaneity between outsourcing and its potential drivers. Still, we are linked to a concept of weak causality (Michie and Sheehan, 2005). Indeed, the causal relationship between outsourcing and the independent variables considered – those related with innovation in particular – might be bi-directional, so that the regression analysis is simply used to detect significant correlations. We nevertheless recall that even when focusing on “correlations”, rather than causal links – or on “weak causality links”– this regression based framework has the major strength that each specific relationship between  $Y$  (dependent variable) and  $X_i$  (independent variables) is controlled for other  $X_j$ . This helps to mitigate spurious correlations and to add robustness with respect to simple bilateral

correlations, or other statistical methods that do not control simultaneously for the various effects, possibly over emphasizing some relationships.

## 5 The dataset

Model [1] is estimated with reference to the manufacturing firms with at least 50 employees located in RE, using a new dataset obtained by merging other two ones – Dataset I and Dataset 2 – already applied in previous works of ours.

Dataset I, used for a first set of outsourcing analyses in RE (Mazzanti, Montresor, and Pini, 2006a, 2006b, 2007), is based on a direct survey to firm managers carried out in 2002 for the period 1998-2001, and incorporating balance sheets data starting from 1998 till 2002. The relative sample refers to 166 firms drawn from a universe of 257 manufacturing companies with at least 50 employees, listed in both national (Intermediate Census 1996 of the National Institute of Statistics) and local (Camera di Commercio in Reggio Emilia 2001) databases.<sup>5</sup> The sample covers 64.59% of the entire population and is overall representative.<sup>6</sup>

Dataset II, used for an analysis on the relationships between innovation, industrial relations and economic performance in RE (Antonioli, Mazzanti, and Pini, 2007b, 2007a), is based on a second direct survey to union representatives carried out in 2005 for the period 2004, and incorporating balance sheets data starting from 1998 till 2002. This sample refers to 192 firms drawn from a universe of 634 manufacturing companies with at least 20 employees, listed - as the previous ones - in both national (Intermediate Census 1996 of the National Institute of Statistics) and local (Camera di Commercio in Reggio Emilia 2001) databases.<sup>7</sup> The absolute number of respondents constitutes the 51% of the 376 firms

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<sup>5</sup>The survey is made up of a questionnaire addressed to the management, through face-to-face interviews, on four main topics: (a) firm's characteristics and employment structure; (b) organizational innovations and human resources management practices; (c) industrial relations; (d) employee evaluation and payment systems.

<sup>6</sup>The sample firms' distribution by sector and size is characterized by a limited bias, as the textile sector and small-size firms (50 to 99 employees) are slightly under-represented. However, no significant distortion emerges in all other sectors and dimensional employees' classes, with the number of interviewed firms approaching or reaching 100% of the total in many of them. The sample representitiveness is also confirmed by the application of a Marbach Test (Cochran, 1977) which yielded tolerable results in a previous application (Mazzanti, Montresor, and Pini, 2006a).

<sup>7</sup>The survey is made up of a questionnaire addressed to the union representatives, through face-to-face interviews, on five main topics: (a) firm's structural characteristics; (b) employment structure and labour

having union representatives (RSU), out of the 634 of the entire population (30% of the entire population). Firms with at least 50 employees represents the 43% of the entire population and the 69% of the surveyed firms, a fact that is mostly due to the lower union presence in small firms. A part from this under-representation of small firms, only some other minor biases emerge so that the sample is overall representative.<sup>8</sup>

From the merge of the two previous datasets, a new one is obtained. It refers to 97 manufacturing firms, with at least 50 employees, with information based on interviews in 2002 and in 2005, and with balance sheets available from 1998 to 2002. As Table 7 shows, the sample reveals a limited bias in the firms' distribution by sector (textile sector is slightly under-represented) and in that by size (relatively small firms - 50-99 employees - are under-represented given the lower RSU presence affecting the Dataset II). However, applying the usual Marbach Test (Cochran, 1977) we get tolerable results (Table 8) so that the representativeness of the sample is satisfactory.

Insert Tables 7 and 8 around here

Although the merge generates a limited numbers of observations with respect to the original Dataset I, several advantages should be stressed. First of all, we have now a useful hybrid cross section framework, given the lag between the main outsourcing variables, captured for 2004 through the second survey (Dataset II), and the potential explanatory variables dated 2001 and 1998-2001, based on the first survey (Dataset I). In this way, cross-section endogeneity flaws are mitigated. Secondly, with the merge we can now focus on some relevant international issues: indeed, unlike Dataset I, in Dataset II some

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contracts; (c) innovation policies in technologies, firm organizations, training, adoption of information and communication technologies; (d) flexibility in labour utilization; (e) industrial relations. The interviews were conducted on a representative sample of 250 firms random selected among the 376 firms with union representatives, with a very high reply ratio (77%). With respect to Dataset I, this survey goes deeply for acquisition of more accurate information on the outsourcing strategies of the firm. In addition, it contains information on some international perspective of the firm organizational strategies, such as delocalisation of plants and production activities.

<sup>8</sup>The machinery sector is the only one to be slightly under-represented, but the Marbach Test (Cochran, 1977) still shows results in line with the usually accepted margin of error (Antonioli, Mazzanti, and Pini, 2007b).

delocalization aspects are elicited and allow us to estimate Equation [1] by including  $x_{DELOC}$

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## 6 Main results of the empirical application

The empirical application of model [1] to the merged dataset of RE is carried out in two different steps: we first analyze the extent to which the general outsourcing index is correlated with the set of regressors, and secondly we focus on the specific sub realms – ancillary activities, production activities, production supporting activities – in order to disentangle eventual diverse relationships.

Before illustrating the two sets of results, the main issues of econometric relevance for interpreting them should be addressed first. Endogeneity has already been tackled above, and should not represent a major problem, if any, in the analysis. Due to the richness of factors, a careful analysis of the correlation matrix has been preliminary attempted, showing that high correlations are here not a major flaw (the matrix is available upon request). When excessive correlations have been found, nevertheless, variables have been included separately in the estimated regressions. This is aimed at reducing collinearity problems, selecting a limited set of not highly correlated covariates for testing each specific hypothesis.

Heteroskedasticity, a major flaw in cross-sections, is here addressed by using white corrected estimators and the potential omission of relevant variables – one of the main causes of endogeneity (correlation between explanatory variables and errors) often due to data unavailability – is mitigated by the very rich source of explanatory variables we may exploit.

Concerning the regression analysis, a “from general to particular” backward stepwise method is here applied, which may result more consistent with this framework since over fitting specifications, starting from a conceptual model, is less severe than excluding relevant factors, and can be resolved by eventually deleting non-significant variables step by step.

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<sup>9</sup>To be sure, because of this data availability, unlike in model [1], delocalization variables refer to time  $t$  rather than to time  $t-1$ .



Finally, we should stress that regressions are robust on many respects (Wooldridge, 2000).  $F$  tests denote good overall significance, mainly as expected for the general outsourcing index,  $R^2$ s are averagely fine<sup>10</sup>, and finally many coefficients linked to relevant variables are significant.

## 6.1 General outsourcing extent

Coming to the main results, the analysis of the *general outsourcing extent* index,  $OUT_{ij}$ , shows a good statistical performance (Table 9), since both  $F$  tests and  $R^2$  are (very) high (3.08 and 0.22, respectively) if we consider the relatively limited number of units. This means that, in addition to, and as a consequence of, sample representativeness, the number of observed firms provides a robust basis for sound empirical investigations.

Insert Table 9 around here.

At the outset, such an investigation confirms our expectations about the limited explicative role of TCE variables (Tab. 3) in the LPS of RE. Indeed, TCE-related outsourcing “predictions” are quite blurred. While asset specificity (*ASPEC*) actually discourages outsourcing, unexpectedly for TCE, the same holds true (though much less significantly) also for the proxy capturing the administration costs linked to organizational complexity (*ORGHIER*). What is more, uncertainty (*MKTUNC*) spurs, rather than inhibiting as in TCE, outsourcing, suggesting that the risk of facing problems of governance inseparability when uncertainty unfolds might matter more than the risk of post-contractual opportunism (Mahnke, 2001).

Our expectations are also confirmed as far as the role of industrial relations and of the workers’ involvement in strategic management are concerned (that is for the  $x_{IR}$  variables in Table 4). Both factors actually affect outsourcing decisions significantly, by hampering

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<sup>10</sup>The  $R^2$  is intrinsically lower in cross-sections environments, with “good” values being even at 20% or less

it. First of all, when participating to the operational and problem-solving decisions of the management (*INV-INIT*), workers seem able to put their fear of employment losses at work by contrasting outsourcing. Second, an alternative specification of the model (not reported here for scope constraints<sup>11</sup>) shows that, when workers' involvement occurs through the unions' participation to specific outsourcing decisions, it acts in blocking the externalization of specific assets (*ASPECGOV* in Tab. 3)<sup>12</sup>, even when the latter (that is *ASPEC*) is not significantly perceived by the firm as problematic to contract out.

When moving to *delocalization* (that is to the  $x_{DELOC_i}$  variables of Tab. 5), the results suggest that, according to Section 2, delocalizing might actually correlate positively with outsourcing, but only at certain conditions. Indeed, in general, benefiting from lower production costs (*DELOC*) seem to require the firm turning fixed into variable costs through outsourcing. On the contrary, however, establishing foreign production units (*FOREPROD*) and collaborating with foreign partners (*AGREEM*) to gain foreign market shares are strategies that firms carry out only “at the price” of lower outsourcing. And this substitutive, rather than complementary, relationship is possibly explained by the industrial relations arguments we have discussed in the conceptual part (Section 2).<sup>13</sup> In brief, our evidence does show that outsourcing and delocalization dynamics are, as expected, quite correlated, but that the sign of this relationship is not to be taken for granted, given the high contingent nature of the links and the various theoretical underpinnings of complementary and substitution effects.

Finally, the “technological profile” of the RE LPS – which is not core in the paper, but nevertheless relevant for interpreting the results and easing the control of omitted firm-specific heterogeneity – seems to matter in accounting for the firms' outsourcing decisions. Indeed, confirming the results we previously obtained in a pure cross-section frame without lags (Mazzanti, Montresor, and Pini, 2006a, 2006b, 2007), and those of a larger set of works, externalizing ancillary activities to refocus on high value added ones, or even tapping into the providers' competences, correlate with the RE firms' product

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(Greene, 2000).

<sup>11</sup>All results are nevertheless available upon request, as well as the questionnaire questions.

<sup>12</sup>On this point see also Mazzanti, Montresor, and Pini (2006a).

<sup>13</sup>Let us observe that, once interacted with *INVOL3* (i.e. workers' participation through negotiation), *DELOC* keeps a positive sign, but loses significance. Furthermore, both *AGREE* and *FOREPROD*, once interacted with *INVOL3*, keep a negative sign and increase their significance.

innovativeness. What is more, outsourcing seems a necessary organizational innovation to supplement technological ones, even in sectors mainly characterized by a Schumpeter Mark II technological regime (as shown by the significance of *HERFINNO*).

In concluding, let us observe that the structural variables (Tab. 6) provide some further elements for better qualifying the results. Quite interestingly, the sectoral dummies seem to suggest that the most industrial-district-like sectoral partition of the LPS outsources relatively less.<sup>14</sup> However, this seems valid just for the larger firms, as also the *SIZE* dummy is significant and negative. All in all, we infer that outsourcing may threaten the cohesion of the districts, but only if it concerns their “champions”.

## 6.2 Specific outsourcing extent

Moving to the analysis of the *specific outsourcing extent* index, that is  $OUT_{ik}$ , let us observe that, in general, the outsourcing of ancillary activities ( $OUT_{ANC}$ ) fits the model relatively better than general outsourcing, and the reverse holds true for that of supporting-production ( $OUT_{PRODSUP}$ ) and production activities ( $OUT_{PROD}$ ) as such (Tab. 10)

Insert Table 10 around here.

More in detail, as far as TCE predictions are concerned, retaining the different nature of the firm’s activities (Tab. 1) helps us in better qualifying the first slot of general results obtained in Section

6.1. First of all, the unions’ role in making the outsourcing of specific assets sensible and significant (*ASPECGOV* in Tab. 3) (even when specific assets alone are not) appears to be driven by the risk of post-contractual opportunism with respect to ancillary activities (*ANC*) only. A result that, although apparently a signal of the weakness of the trade unions’ strategy, concerned with low value added activities, has, as we will see in the following, a

certain rationale. As expected, the typical TCE interaction between market uncertainty and asset specificity (i.e. *MKTASPEC* in Tab. 3) becomes significant only for “truly” production outsourcing (*PROD*), while with respect to ancillary ones (*ANC*) it is idiosyncratic (rather than sectoral) firm uncertainty (*FIRMUNC* in Tab. 3) which calls for vertical integration. Reminding that, in general, that is with respect to  $OUT_{ij}$ , uncertainty spurs, rather than inhibiting outsourcing, the mixed role that TCE finds in accounting for it in the LPS of RE gets confirmed.

Moving to the role of industrial relations, it is interesting to observe that the presence of negotiation actions between unions and management (i.e. *INVOLV3* in Table 4) confirms to play a braking role *only* with respect to the outsourcing of ancillary activities (*ANC*). Once interpreted as the attempt of trading outsourcing for other internal kind of changes, this result may be perceived as a weakness of the trade unions’ strategy, being ancillary activities linked to a lower value in terms of economic relevance, employee skills and other factors. One may wonder why unions do not focus their effort on more relevant activities. Nevertheless, it could be that unions are worried about the outsourcing of ancillary activities since they lead to a substitution of unionized workforce, typically Italian, with non unionised workforce employed by subcontractors (mainly migrant workers highly concentrated in low value added markets). This could lead, in the end, to a net loss for unions in terms of unionization of the territory following the outsourcing implementation, even if the providers of these externalized, ancillary activities remain local, and not out of sight and control.<sup>15</sup> Some weakness may be present in unions bargaining on innovation and outsourcing choices by firms, though we claim that the situation may more complex. Quantitative and qualitative empirical evidence is needed to interpret the results.

Quite interestingly, the outsourcing of production activities (*PROD*) as such “needs” a different mechanism to be hampered, as this occurs only when managers and employees interact in the relative decision (*MAN-EMPL-OUT* in Table 4). In other words, with respect to higher value added activities, employees function as substitutes for a role potentially played by the industrial relation dynamics.

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<sup>14</sup>The sectoral dummies for machinery (*MACH*) and, even more, ceramic tiles (*CER*) are significant and related to *OUT* with a negative sign.

<sup>15</sup>Recent anecdotal evidence, available from the authors, suggests that this hypothesis may actually be a possible explanation of the present result.

As far as production supporting activities (*PRODSUP*) are concerned, investing in high performance work practices and in workers' competences through their involvement (*INVINIT*) seem to reduce the opportunities of outsourcing strategic activities like, for example, R&D. As innovative opportunity and sunk costs are increased by these investments, it is sensible to think that firms faces endogenously-driven disincentives to outsource such a kind of activities.

All in all, the analysis on specific activities tells a coherent story, mainly for the influence of employee's involvement and industrial relations on different aspects of the outsourcing decisions.

Coming to the role of delocalization, let us observe that, unlike in the general case, delocalizing production supporting activities (*PRODSUP*) through a commercial/business unit (*COM-UNIT*) does not seem to require a 'compensation' in terms of less outsourcing. Quite interestingly, on production activities as such, delocalization strategies and outsourcing seem instead to be run independently. Apart from these results, the level of ancillary activities basically confirms the positive and negative signs we observed for *DELOC* and the exported oriented strategic decisions for the general outsourcing extent indicator (Section

6.1). Substitutions and complementary effects that were commented on there thus probably derive from the level of ancillary activities which remains, we underline, the most widespread in merely quantitative terms.

Finally, we note that regarding pure controls and innovation variables (Tab. 6), evidence is largely confirmed at all three levels. *HERFINNO* shows a very noticeable good significance, as well as *INOOTECH* and *INNOPROD*, confirming the positive link between outsourcing and innovation, and specifying its higher expected significance for  $OUT_{PROD}$  and  $OUT_{SUPPROD}$ <sup>16</sup>.

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<sup>16</sup>Let us also observe that, for  $OUT_{PRODSUP}$  and also for  $OUT_{PROD}$ , the role of size (*SIZE*) becomes insignificant, while for  $OUT_{PROD}$  only time (i.e *AGE*) increases outsourcing experience rather than governance inseparability.

## 7 Conclusions

The paper has presented new conceptual and empirical insights on outsourcing decisions by firms embedded in a quite idiosyncratic socio-economic environment. In so doing, it aims at integrating TCE theoretical reasoning and arguments on firm outsourcing and delocalization strategies with such factors as employees' involvement and industrial relations. This is, for sure, the core point and main added value of the paper.

Another added value, in our opinion, is the treatment of outsourcing as a strategy that is differentiated by the intensity of its adoption and by the kind of activity it refers to. This allows a deeper investigation both of the forces moving behind it and of the different links occurring at, for example, the level of ancillary or production activities.

Last, but not least, at empirical level, the richness of explanatory factors and the lag structure of the model are a further keystones that add robustness and partially resolve the usual flaws encountered in cross section settings.

Overall, empirical evidence shows that the role of TCE in accounting for outsourcing, at least regarding the firms playing in (this) idiosyncratic LPS, is blurred. The TCE binomium "asset specificity-with-uncertainty" works only for production activities, while the significance of TCE-related arguments decreases, when it is not even contradicted, by considering other kinds of activities.

The role of industrial relations in accounting for the RE firms' outsourcing emerges instead quite straightforwardly, and with a great incremental value, also claiming for further research. First, whoever is involved in the decisional process, workers and/or workers delegates are able to counteract it, but probably with different objectives and effects. Unions seem to play a role in signalling the post-contractual problems of contracting out specific assets. The way they "contrast" outsourcing when negotiation is present is the more substantial, the more "pervasive", but the less "strategic" are the outsourced activities. This may signal a potential weakness in dealing with outsourcing, or the different roles played by pure industrial relations and firm internal involvement and participatory practices witnessing employees and managers to confront on such issues. Some brakes to outsourcing

may even derive from managerial decisions, as a consequence of investments in strategic assets and innovation.

We also note that, in general, firms use outsourcing and international delocalization in a complementary way. A “disintegrated” organizational structure appears more favourable to benefit from the cost and competitive advantages of delocalizing. However, when delocalization is used to penetrate foreign markets, outsourcing appears to be used substitutively, since extra-coordination costs might counteract the savings in production costs, and unions and worker delegates (consider what commented on above) might want to use the two instruments as substitutive bargaining tools. In brief, the correlation between outsourcing and delocalization is “activity-dependent”: delocalizing through a commercial/business unit, rather than a production unit as such, might not require “compensation” in terms of less outsourcing; whereas delocalization strategies and outsourcing seem to be run independently if regarding production activities.

The technological profile of RE firms also matters in accounting for their outsourcing decisions, as their technological innovativeness (mainly product innovations) correlates positively with outsourcing, even at the risk of a certain knowledge leakage. A result which confirms previous evidence on both this and other LPSs. Finally, and quite interestingly, the most industrial-district-like sectoral partition of the LPS seems to outsource relatively less, but with different insights in terms of firm size. Accordingly, outsourcing may be said to threaten the cohesion of the RE districts, providing it is made by the district largest firms (i.e. their ‘champions’).

The future research agenda may move along the following directions, in order to provide new and more robust outcomes. First, gathering information about the nationality of the outsourcer (national vs. international outsourcing)<sup>17</sup> would be essential and really valuable with respect to the literature, both to provide evidence on strategic choices of internationalization and to analyze more in depth the extent to which the regional/national/international content of outsourcing matters for industrial relations and bargaining outcomes between the parties. An hypothesis to test is related to the fact that unions and employees are more willing to bargain on outsourcing if this remains within the

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<sup>17</sup>Although the reference dataset contains some rough data on this point, the relevant analysis has been omitted from the paper and postponed in order to collect and elaborate more accurate information.

LPS, thus more easily monitored in its dynamics. In addition, it would be helpful also to refine the analysis of delocalization strategies by retaining the organizational structure of the firms (national vs. multinational corporations). Finally, extending the analysis to a broader sample of firms, possibly at regional level if not national, is certainly a way to provide more general results and limit the role played by idiosyncratic factors which, nevertheless, are interesting since they show the extent to which theoretical approaches and associated hypotheses must be adapted and interplayed when facing complex LPS.



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## **Tables and Figures**

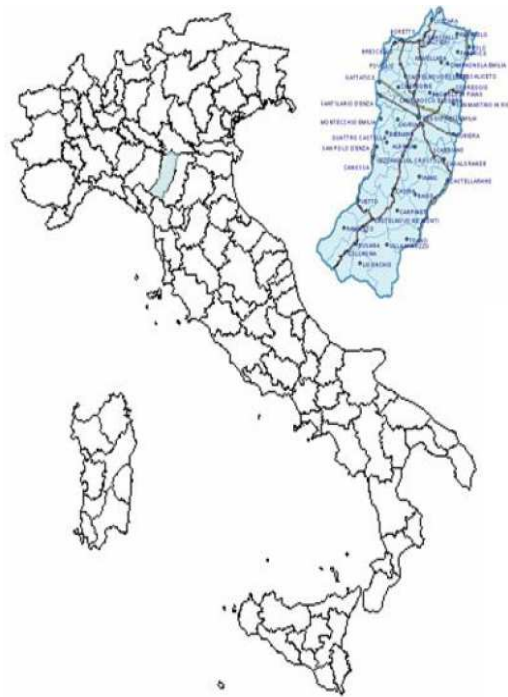


Figure 1: The province of Reggio-Emilia

Outsourced activities	Full sample 2004: 192 firms with more than 19 employees		Reduced 2004 sample: 134 firms with more than 49 employees		Restricted 2004 sample: 97 firms with more than 49 employees (used in the analysis)	
	(1) %	(2) Index 0-3	(1) %	(2) Index 0-3	(1) %	(2) Index 0-3
Ancillary activities	54.76	1.185	56.18	1.183	53.00	1.119
1. Inventories management	17.19	0.240	20.15	0.284	19.00	0.260
2. Distribution, logistics and transports	58.85	1.167	60.45	1.172	54.00	1.040
3. Machinery maintenance	55.73	0.958	58.21	0.993	57.00	0.950
4. Plants maintenance	70.31	1.745	72.39	1.791	72.00	1.810
5. Cleaning services	76.56	1.922	82.09	2.060	79.00	2.010
6. Payroll management	68.23	1.641	64.93	1.470	57.00	1.300
7. Electronic data processing (e.g. accounting, data, EDP)	36.46	0.625	35.07	0.515	33.00	0.460
<i>Production supporting activities</i>	20.77	0.320	20.71	0.313	18.57	0.277
8. Engineering	28.13	0.422	24.63	0.373	21.00	0.330
9. Research	22.92	0.349	22.39	0.328	18.00	0.250
10. Development and testing procedures	23.44	0.318	23.88	0.313	20.00	0.260
11. Human Resource Management (HRM)	9.90	0.135	10.45	0.134	10.00	0.120
12. Quality control	13.54	0.188	11.94	0.149	12.00	0.140
13. Sales	19.79	0.281	20.90	0.313	16.00	0.240
14. Marketing	31.77	0.578	34.33	0.634	33.00	0.600
15. Integrated information systems (ERP, SCM, CRM, ...)	16.67	0.292	17.16	0.261	17.00	0.220
<i>Production activities</i>	36.98	0.538	39.74	0.582	39.75	0.573
16. Supply of intermediate products	63.02	0.979	66.42	1.000	65.00	0.910
17. Specific production stages (e.g. assembling, packaging, ...)	37.50	0.458	37.31	0.455	37.00	0.440
18. Specific products to be sold	30.73	0.464	35.07	0.552	36.00	0.610
19. Specific trademarks	16.67	0.250	20.15	0.321	21.00	0.330
<i>Average on all activities</i>	36.71	0.685	37.78	0.690	35.63	0.646

Table 1: Outsourced activities in RE (2004): (1) percentage of firms with outsourced activities on the total; (2) outsourcing average extent (0 = activity not outsourced; 1 = partially outsourced; 2 = mostly outsourced; 3 = totally outsourced)

	<b>Full sample 2004: 192 firms with more than 19 employess</b>		<b>Reduced 2004 sample: 134 firms with more than 49 employees</b>		<b>Restricted 2004 sample: 97 firms with more than 49 employess (used in the analysis)</b>	
	N.	%	N.	%	N.	%
<b>Delocalization:</b> Establishments for production abroad, not related to export activities	33	17.19	27	20.15	19	19.59
<b>Export channels</b>						
Establishments for production abroad	29	15.10	26	19.40	19	19.59
Commercial headquarters abroad	48	25.00	44	32.84	35	36.08
Partnerships in local foreign firms	26	13.54	24	17.91	18	18.56
Agreements with local commercial networks	109	56.77	82	61.19	61	62.89
Others (trade fair, etc.)	46	23.96	34	25.37	26	26.80

Table 2: Delocalization and export channels of production activities  
in RE (2004)



Label	TCE related variable	Definition	Positions
i	<i>ASPEC</i>	asset specificity	$\frac{1}{N_j} \cdot LOCREV_j \cdot REV_{ij}$ $N_j = n.$ of firms in branch $j$ $LOCREV_j =$ local share of branch $j$ 's revenues $REV_{ij} =$ firm $i$ 's share of branch $j$ 's revenues
ii	$UNION_i$	union density (governance inseparability)	$\frac{UMPI_i}{EMP_i}$ $EMP_i = n.$ of employees $UMPI_i = n.$ of unionized employees
iii	$FIRMAGE_i$	firm age (governance inseparability)	$\lg(2002 - SETYEAR_i)$ $SETYEAR_i =$ firm $i$ set-up year 2002: latest year of the survey
iv	$ASPEGOV_i$	asset specificity conditional on governance inseparability	$ASPEGOV_{1i} = ASPEC_i \cdot UNION_i$ $ASPEGOV_{2i} = ASPEC_i \cdot UNIOU_i$ $UNIOU_i = 1$ unions either informed or consulted $UNIOU_i = 0$ neither informed nor consulted
v	$INTASS_i$	intangible assets (intensity of)	$\frac{\sum_{t=1998}^{2001} INTINV_{it}}{\sum_{t=1998}^{2001} CAPINV_{it}}$ $INTINV_{it} =$ intangible investments in $t$ $CAPINV_{it} =$ invested capital in $t$
vi	$ORGPLA_i$	organizational placement (interface knowledge)	$\frac{NOUTDIV_i}{NOUT_i}$ $NOUTDIV_i = n.$ of out. activities with division $NOUT_i = n.$ of out. activities
vii	$ORCHIER_i$	organizational hierarchy (interface knowledge)	$\frac{NHIER_i}{NDIV_i}$ $NHIER_i = n.$ of hierar. levels among divisions $NDIV_i = n.$ of organizational divisions
viii	$PRODDIF_i$	product differentiation	$PRODDIF_i = 1$ if both large and small production $PRODDIF_i = 0$ if either one or the other
ix	$GEODIV_i$	geographical diversification	$\frac{\sum_g (REV_{ig} - MREV_{ig})^2}{4}$ $g =$ REG, NAT, EU, INT $MREV_{ig} =$ mean of the 4 $g$
x	$MKTUNC_j$	market uncertainty	$\sqrt{\frac{\sum_{t=1998}^{2001} (REV_{jt} - MREV_{jt})^2}{4}}$ $REV_{jt} =$ sector $j$ 's revenues in $t$ $MREV_{jt} =$ mean of $REV_{jt}$
xi	$MKTASPE_i$	mkt uncertainty conditional on asset specificity	$MKTUNC_j \cdot ASPEC_i$ see (i) and (x)
xii	$FIRMUNC_i$	firm uncertainty	$\sqrt{\frac{\sum_{t=1998}^{2001} (REV_{it} - MREV_{it})^2}{4}}$ $\sqrt{\frac{\sum_{t=1998}^{2001} (REV_{it} - MREV_{it})^2}{4}}$ see (x)

Table 3: TCE related variables

i	INVOLV	Degree of involvement between managers and unions (workers delegates) on techno-organisational changes	Average Index ranging from 0 to 1 capturing the intensity of involvement, from absence, to low involvement (information only), to medium involvement (consultation), to high (negotiation)
ii	INVOLV1	Involvement through information	Dummy variable capturing the presence of information actions related to adoption of innovations
iii	INVOLV2	Involvement through consultation	Dummy variable capturing the presence of consultation actions related to adoption of innovations
iv	INVOLV3	Involvement through negotiation	Dummy variable capturing the presence of negotiation actions related to adoption of innovations
v	INDREL	Degree of involvement between managers and unions (workers delegates) on 22 defined issues (employment, production, innovation, training, health, wages, etc..)	Average Index ranging from 0 to 1 capturing the increasing intensity of involvement: from absence, consultation, to negotiation
vi	MAN-EMPL	Degree of involvement between managers and employees (workers delegates) on 22 defined issues (employment, production, innovation, training, health, wages, etc..)	Average Index ranging from 0 to 1 capturing the increasing intensity of involvement: from absence, consultation, to negotiation
vii	MAN-EMPL-OUT	Degree of involvement between managers and employees on the outsourcing issue	Variable taking value 0,1,2 according to no involvement, consultation, negotiation
viii	INV-INIT	Manager initiatives to involve employees in production activities and/or problem solutions; Workers' participation to production decisions	Average Index ranging from 0 to 1 capturing the increasing intensity of participatory initiatives: from absence, to hierarchical ones, to teamworking, to joint committees, to more participatory pronounced actions
ix	BTC	Bilateral manager-workers technical committees	Dummy variable for the presence in the firm of bilateral technical committees for consultation and negotiation on selected issues
x	INNO-PART	Consultation and delegation activities in work organization	Additive index built by synthesizing the intensity of introduction and presence of participation practices in work organization (see table 12, Antonioli et al., 2004)
xi	INNO-ACTION	Tecno-organisational and work changes introduced through the action of unions, joint committees or workers involvement	Average Index ranging from 0 to 1 capturing 13 work and innovation changes introduced through the involvement of unions, joint committees or workers in 1998-2001
xii	INNO-ACTION1	Tecno-organisational and work changes introduced through the action of unions	Average Index ranging from 0 to 1 capturing 13 work and innovation changes introduced through the involvement of unions in 1998-2001
xiii	INNO-ACTION2	Tecno-organisational and work changes introduced through the action of joint committees	Average Index ranging from 0 to 1 capturing 13 work and innovation changes introduced through the involvement of joint committees in 1998-2001
xiv	INNO-ACTION3	Tecno-organisational and work changes introduced through the action of workers involvement	Average Index ranging from 0 to 1 capturing 13 work and innovation changes introduced through the involvement of workers in 1998-2001

Table 4: Industrial relations variables

i	DELOC	International delocalization	Foreign direct investments in production activities (d)
ii	FOREPROD	Production delocalization for exports	Foreign production units for supporting exports (d)
iii	COM-UNIT	Commercial delocalization for exports	Foreign commercial/business unit for supporting exports (d)
iv	FOR-PART	Foreign participation for exports	Ownership participation to a foreign firm for supporting exports (d)
v	AGREEM	Foreign agreements for exports	Agreement with a foreign commercial/business network for supporting exports (d)

Table 5: Delocalization variables

<b>STRUCTURAL VARIABLES</b>			
i	SIZE	Size of the firm	Number of employees (2004)
ii	MACH	Machinery sector	Firm belonging to machinery sector (d)
iii	CER	Ceramic sector (non metal minerals)	Firm belonging to ceramic sector (d)
iv	INTREV	International market revenue (openness)	Share of revenue in international markets
v	PRIV	Private firm	Private ownership (d), vs cooperative ownership, group membership
vi	TRAIN	Training	Training Coverage
vii	SKILL	Skill workforce content	Ratio of skilled on unskilled workers
<b>INNOVATION VARIABLES</b>			
viii	INNOTECH	Technological innovativeness	Index of technological innovation averaging process, product and quality product innovations (1998-2001)
ix	INNOPROD	Product innovation	Product innovations (1998-2001)
x	INNOPROD	Process innovation	Process innovations (1998-2001)
xi	HERFREV	Market concentration	Herfindhal index of the sector's revenues
xii	HERFINNO	Innovation concentration	Herfindhal of innovations
xiii	SPEARINNO	Sectoral turbulence in innovation activities	Spearman correlation in innovation rankings
xiv	INNOORG	Organisational innovations	Index averaging the adoption of five organizational practices (TQM, QC, JIT, TW, TR)
<b>FLEXIBILITY VARIABLES</b>			
xv	FLEXREL	Flexibility in work organizations	labor service flexibility in work organizations
xvi	FLEXINNO	Firm flexibility	synthetic index of flexibility indicators

Table 6: Structural control variables

Sectors	Size (employees)					Total	
	50-99	100-249	250-499	500-999	>999	%	Abs. values
Food	0.00	3.09	2.06	2.06	0.00	7.22	7
Other Industries	0.00	0.00	0.00	0.00	0.00	0.00	0
Chemical	2.06	2.06	1.03	0.00	0.00	5.15	5
Wood and Paper	0.00	0.00	2.06	0.00	0.00	2.06	2
Machineries	23.71	19.59	9.28	4.12	3.09	59.79	58
Non-metallic mineral	6.19	8.25	3.09	4.12	1.03	22.68	22
Textile	2.06	1.03	0.00	0.00	0.00	3.09	3
<b>Total (%)</b>	34.02	34.02	17.53	10.31	4.12	100.00	
<b>Total (absolute values)</b>	33	33	17	10	4		97

Sectors	Size (employees)					Total	
	50-99	100-249	250-499	500-999	>999	%	Abs. values
Food	0.78	1.95	1.17	0.78	0.78	5.45	14
Other Industries	0.78	0.00	0.00	0.00	0.00	0.78	2
Chemical	3.11	2.72	0.78	0.00	0.39	7.00	18
Wood and Paper	1.56	0.78	1.17	0.00	0.00	3.50	9
Machineries	28.02	15.95	5.06	2.72	3.50	55.25	142
Non-metallic mineral	9.73	6.61	1.95	2.72	0.78	21.79	56
Textile	1.56	1.56	2.72	0.00	0.39	6.23	16
<b>Total (%)</b>	45.53	29.57	12.84	6.23	5.84	100.00	
<b>Total (absolute values)</b>	117	76	33	16	15		257

Table 7: Sample and population firms (distribution and absolute values)

Sectors	Margin of error $\theta$	Size (employees)	Margin of error $\theta$
Food	0,277	50-99	0,148
Other Industries	n.a.	100-249	0,132
Chemical	0,391	250-499	0,171
Wood and Paper	0,661	500-999	0,200
Machineries	0,101	> 999	0,443
Non-metallic mineral	0,168		
Textile	0,537		
<b>Total</b>	0,080	Total	0,080

Table 8: Marbach test

<b>Dependent variable: OUT</b>	
<b>Covariates</b>	
Constant	1.940
ASPEC	-2.208 **
ORGHIER	-1.449
MKTUNC	2.659 ***
INV-INIT	-2.055 **
DELOC	2.810 ***
AGREEM	-1.871 *
FOREPROD	-3.293 ***
INNOPROD	3.097 ***
HERFINNO	3.212 ***
FLEXREL	1.885 *
SIZE	-2.129 **
MACH	-1.753 *
CER	-2.731 ***
Adjusted R-squared 0.2194750	
F-test (prob) 3.08 (.0009)	

Table 9: General outsourcing extent

Dependent variable: OUT <sub>ANC</sub>		Dependent variable: OUT <sub>PRODSUP</sub>		Dependent variable: OUT <sub>PROD</sub>	
Covariates		Covariates		Covariates	
Constant	2.630	Constant	-1.394	Constant	2.128
ASPEGOV	-5.091 ***	ORGHIER	-3.008 ***	MKTASPE	- 2.575 **
MKTUNC	3.948 ***	MKTUNC	2.920	ORGHIER	-2.536 **
FIRMUNC	-2.510 **	FIRMUNC	-1.747 *	AGE	1.282
INVOLV3	-3.310 ***	INVINIT	-2.600 ***	MAN-EMPL-OUT	-2.018 **
DELOC	2.134 **	BTC	-1.657	INNOPROD	2.763 ***
AGREEM	-2.416 **	COM-UNIT	1.948 *	HERFINNO	2.426 **
FOREPROD	-2.506 **	INNOTECH	1.904 *	STRUCTORG	2.366 **
HERFINNO3	0.235 ***	HERFINNO	2.452 **	SIZE	-0.775
SKILL	1.572	FLEXREL	2.397 **	MACH	0.126
SIZE	-1.027	SUBFOR	1.435	CER	-0.991
MACH	-1.777 *	SIZE	-1.569		
CER	-3.901 ***	MACH	-2.147 **		
		CER	-1.543		
Adj. R <sup>2</sup> 0.3038220		Adj. R <sup>2</sup> 0.1633140		Adj. R <sup>2</sup> 0.1253886	
F-test(prob) 4.49 (.0000)		F-test(prob) 2.44 (.0075)		F-test(prob) 2.38 (.0155)	

Table 10: Specific outsourcing extent