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SOCIAL CAPITAL IN KNOWLEDGE BASED BUSINESS PROCESS OUTSOURCING

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Abstract

Organizations are pursuing the outsourcing of business processes (BPO) to offshore locations. However, current research has shown that a knowledge-sharing gap between the client and vendor organizations leads to less than expected benefits. This research applies social capital theory to study the antecedents necessary for the creation of social and intellectual capital in the BPO relationship and their downstream impact on knowledge sharing behaviors. The benefits of the creation of social and intellectual capital translate to improved knowledge sharing and a better BPO outcome as measured using vulnerability, coordination and production costs from coordination theory. A case study of a knowledge management system (KMS) in BPO is used to support the propositions. Preliminary results indicate that investments toward client-vendor relationships in BPO can be worthwhile. They create social and intellectual capital, which improves knowledge sharing behaviors that lead to better utilization of knowledge management systems, lower coordination costs and an improved BPO outcome.

Keywords: Business process outsourcing, knowledge transfer, social capital theory, coordination theory

Introduction

The concept of transferring the operational ownership and execution of one or more business processes is referred to as BPO. Due to the rapid globalization of information technology and improvements in telecommunications networks, firms are pursuing offshore outsourcing to remote countries like India and China (Lieberman, 2004). Offshore outsourcing allows the domestic firms to tap into large pools of educated workers at significantly lower labor costs. Additionally, client firms benefit by getting access to large markets for products and services in the foreign countries and take advantage of time zone difference to staff round the clock operations without paying overtime wages. The offshore BPO market is the fastest growing segment of the overall outsourcing market and is growing 60% yearly (Trapper, 2003). However, risks in offshore outsourcing are different from onshore outsourcing and can lead to less than expected benefits.

Reports from actual outsourcing case studies indicate that many organizational goals remain unfulfilled. Lacity and Willcocks (1998) found that the risks of an outsourcing effort can be significant. Their study reported that only 54% of the outsourcing agreements that they surveyed realized cost savings. While the risks and challenges are significant in an offshore outsourcing relationship, management practices can play a major role to improve the effectiveness of these arrangements (Willcocks, et al., 1999). Using case studies, Rottman and Lacity (2004) identified 20 offshore sourcing best practices that included knowledge management (KM) initiatives such as balanced scorecard metrics, real time dashboards and identifying subject matter experts. A study of KM in IT outsourcing by Willcocks, et al. (2004) indicated the importance of intellectual capital and social capital in outsourcing relationships. Indeed outsourcing success is significantly linked to factors that fall beyond the written contract between the client and vendor (Koh, Ang and Straub, 2004). These include transfer of tacit knowledge and the development of relationship capital in the form of human obligations within the outsourcing teams.
The research on inter-organizational knowledge management shows that knowledge sharing, specifically the sharing of tacit knowledge, is particularly difficult between organizations (Burgess, 2005). Various IT solutions can facilitate the sharing of knowledge between firms (Hislop, 2002). Factors that impact knowledge sharing are the characteristics of the organizations, their relationship, the type of knowledge, and the transfer process (Argote, 1999; Ko, Kirsch, and King, 2005; Inkpen and Tsang, 2005). Social capital theory (SCT) is centrally concerned with the significance of relationships, or social capital and intellectual capital on the effectiveness of organizations (Nahapiet and Ghoshal, 1998). This theory argues that effective knowledge combination, exchange and transfer occur when sufficient enablers for social capital are present in the inter-organizational relationship. Several IS researchers have utilized SCT to study inter-organizational knowledge management systems (Kankanhal, Tan, and Wie, 2005; Wasko and Faraj, 2005). These studies found significant relationships between social capital and knowledge sharing processes. A study applying SCT to BPO relationships has not been attempted although it holds promise for explaining the ambivalent BPO outcomes witnessed thus far.

While social theories can be used to explain inter-organizational knowledge transfer, transaction cost-based measures are needed to get better quantifiable measurements of impacts on the outsourced processes. Institutional theory (Teo, Wei, and Benbasat, 2003), process theory (Carmel and Agarwal, 2002) and economic theories (Ang and Straub, 1998) have been used to study outsourcing results. Coordination theory, which is based on the coordination, production and information costs associated with the interactions of organizational subunits (Malone and Crowston, 1999), has been used to study the impact of information technology on organizational structure (Malone, et. al., 1999). A model based on coordination theory can shed light on the effective flow of information and knowledge and the allocation of resources, both of which are critical components of BPO (Malone and Crowston, 1994).

The impact of the organizational enablers from SCT – combination opportunity, value expectancy, motivation, and combination capability – on the actual creation of social and intellectual capital in BPO and their downstream impacts on knowledge sharing behaviors has not been studied in IS. Such a study may explain the large variations seen in BPO outcomes. Additionally, the authors of SCT have called on research into the diffusion and exploitation of social capital in downstream knowledge processes in the organization, as well as measuring the impact of the social capital on the BPO outcome using transaction and coordination costs (Nahapiet and Ghoshal, 1998).

**Research goals**

This research on offshore BPO relationships draws on linkages between three research streams – SCT, knowledge transfer and coordination theory. BPO relationships are unique from other supply chain or industry spanning inter-organizational partnerships in several ways. Usually, BPO entails offshore relationships that involve different cultures, asymmetric infrastructures, complex contractual arrangements as well as different customer interface models (Aron, Clemons, and Reddi, 2005). While IT can facilitate knowledge processes, the premise of this paper is that enabling client-vendor interactions is critical for developing social and intellectual capital. These lead to enhanced knowledge sharing and improved BPO outcomes. The research goals are to:

1. Study organizational enablers in a BPO that can facilitate the creation of social and intellectual capital.
2. Understand the impact of the social and intellectual capital created on knowledge sharing processes at the worker level in a BPO.
3. Use interviews to perform a case study of BPO of core R&D processes supporting network design, product introductions, field trials and network installations in the high technology industry.

**Theoretical Background**

Social Capital Theory (SCT) is reviewed and applied to build a research model to study the impact of providing social capital enablers on the development of social and intellectual capital and knowledge sharing in the BPO relationship. The research framework is illustrated in Figure 1.

**Social Capital Theory**

The artifacts of SCT, social capital and intellectual capital refer to the resources embedded within the network of human relationships (Nahapiet and Ghoshal, 1998). Such resources only exist within a relationship and cannot be
separated from the network. They are created through exchanges that happen when the parties in the relationship facilitate opportunities for interaction.

Nahapiet and Ghoshal (1998) define three dimensions for social capital – structural (referrals, timing, context, network ties), cognitive (shared codes, language and narratives) and relational (trust, norms, obligations and identification). Researchers applying SCT have utilized these dimensions in incorporating social capital in studies (Adler and Kwon, 2002, Kankanhalli, Tan and Wie, 2005). In the inter-organizational context, emphasis is placed on network configurations, shared cognitive norms and trust (Inkpen and Tsang, 2005). BPO closely resembles strategic alliances, where firms enter into voluntary arrangements that involve inter-member social ties as a foundation for exchange and sharing of knowledge (Gulati, Nohria and Zaheer, 2000). The social capital generated in such associations has a higher rate of instability of relationships that demand cultural compromise; and produce conflict, with significant risk of opportunism and incompatible goals. The indicators of the social capital construct are: (1) Trust, referrals and self worth, (2) norms and obligations that can be sustained, (3) group identification, common language and practices and (4) story boarding to build shared narratives (Nahapiet and Ghoshal, 1998).

![Figure 1: Research Framework](image)

The organizational enabling conditions stated for supporting social capital creation are four fold: (1) creating opportunities for exchange, (2) creating an expectation that such combinations and exchanges will have value, (3) creating motivation for both sides to participate and (4) creating structural norms and symmetries to support combination capability (Nahapiet and Ghoshal, 1998). DeLone, et. al. (2005) has differentiated the components of the organizational enablers construct as: (1) Bridging, where individuals are brought together purposely for collective work, (2) Bonding, where cognitive norms and implicit understanding is developed by personnel on both sides, and (3) Linking, where structural connections are established for jointly owning ongoing activities. Wenger (1998) found these factors and their inter-relatedness to significantly impact social capital formation and knowledge transfer in communities of practice. Similar results can be expected in BPO:

**Proposition 1- The creation of Social Capital is positively related to the organizational enablers in BPO relationships.**
Studies in virtual communities or remote networks of practice have found that the social capital enablers in the relationship significantly impacted the quality of knowledge contributions, or intellectual capital (Brown and Duguid, 2001). Social capital builds trust and commitment and is a facilitator for collective action when multiple parties are engaged. Such collective action encourages the development of the components of intellectual capital as shared context is built up. Wasko and Faraj (2005) have used SCT to evaluate participation and quality of knowledge contributions to an electronic network of practice. Their study found that motivational factors and organizational factors could impact the establishment of structural norms or intellectual capital in the relationship. These structural norms (or intellectual capital) are defined by four facets: (1) shared language, (2) context, (3) work narratives and work stories of resolved problems and (4) a sense of shared practice (Brown and Duguid, 1991). In the BPO domain:

**Proposition 2 - The creation of Intellectual Capital is positively related to the organizational enablers in BPO relationships.**

**Knowledge Sharing**

Drawing on the research stream in knowledge transfer, we define knowledge sharing as the combination of one or both parties seeking knowledge and/or providing knowledge in response to the request, such that one or both parties are affected by the experience (Huang and DeSanctis, 2005, Szulanski, 1996). The facets of knowledge sharing in a BPO are: (1) one or both parties seeking knowledge to apply, (2) one or both parties transferring tacit knowledge or pointing to the location of already explicit knowledge in response to the request and (3) the seeking party using the new knowledge. The knowledge can be related to the outsourced process and/or product knowledge.

Social capital allows strategic networks to be built that facilitate knowledge sharing (Gulati, Nohria and Zaheer, 2000). Inkpen and Tsang (2005) also found that behavioral factors play a significant role in knowledge transfer in social networks. Knowledge sharing is more likely when social relationships are strong (Szulanski, 1996). Ko, Kirsch and King (2005) report a direct link between the quality of a relationship and the amount of knowledge sharing that happens. The more arduous the relationship, the less knowledge transferred, while greater the shared understanding, credibility and motivation, greater the knowledge transferred.

**Proposition 3 - Knowledge Sharing is positively related to Social Capital in BPO relationships.**

In their study of knowledge transfer from consultants to clients, Ko, Kirsch and King (2005) found the impact of several intellectual capital components on the effective sharing of knowledge in inter firm relationships. They identified factors such as communication encoding and decoding capacity that builds a shared understanding that impacts knowledge transfer. Szulanski (2000) identifies the importance of “bridging the communication gap, the coding schemes and cultural conventions” as critical to overcoming knowledge sharing stickiness. This study also claims that knowledge transfer occurs as opportunities for interaction are provided and common experience is built up and documented. These results can be extended into the BPO domain:

**Proposition 4 - Knowledge Sharing is positively related to Intellectual Capital in BPO relationships.**

**Evaluating BPO Outcome using Coordination Theory**

Coordination theory offers a vehicle to study organizations through business processes – referred to in the theory as coordination structures (Malone, 1987). There are three kinds of costs associated with each coordination structure. The combination of the three costs derived from coordination theory, termed as BPO outcome can provide an evaluation of the end result of social and intellectual capital on the worker level operations of client firm’s offshored process (Ghosh and Scott, 2005, Ghosh and Scott, 2006). The three costs and the impacts of knowledge sharing on them are listed below:

- **Production costs** include the “transaction” costs of running the outsourced processes and measures any efficiencies or deficiencies introduced. Social and intellectual capital can reduce production costs by economizing on information and coordination effort (Nahapiet and Ghoshal, 1998). Productions costs related to the operation of the process that is outsourced are lowered with the increase in knowledge transfer since improved performance is to be expected from the vendor as they become more knowledgeable. These benefits arise as the vendor can access knowledge and reuse it more rapidly (Watson and Hewett, 2006).
Coordinating costs are the “management” costs to manage the communication between the client and the vendor firms, prioritization of activities and the allocation of resources. Creating opportunities for knowledge sharing results in more informal exchanges of information among personnel in the two firms. This effectively improves coordination capabilities (Ghoshal, et al., 1994). The research stream in project management also identifies the flow of knowledge as a critical resource in coordination activities (Snider and Nissen, 2003). The greater the scope and frequency of knowledge sharing, the smoother the project coordination tasks such as resource allocation and task prioritization.

Vulnerability costs are the “strategic” costs associated with a delayed response to a changed market situation. Outsourcing arrangements are usually set up to have a loose relationship between the firms, which can hamper the partnership culture and information flow and cause the BPO client to be vulnerable to market changes (Lacity and Willcocks, 1998). In a typical BPO the client often relinquishes some of the customer interactions that are now managed by the vendor. Mechanisms need to be put in place to facilitate the sharing of customer knowledge that is collected by the vendor in their customer interactions back to the client. With an increase in knowledge sharing, it is anticipated that vulnerability costs will be lowered.

**Proposition 5 - BPO Outcome Costs as measured using vulnerability, production and coordination costs are inversely related to the amount of Knowledge Sharing in BPO relationships.**

**Methodology**

A two-stage methodology is adopted. The first stage involved interviewing key personnel in the client organization at their US location. These interview responses are analyzed as part of this report. A questionnaire is being developed to perform a survey of the onshore client personnel and the offshore personnel at the vendor location. Data from the onshore and offshore locations will be statistically compared but not pair-wise matched. Multiple structural models will be compared using the data (strong inference approach) to find the most parsimonious model with theoretical support and the best fit by testing for direct and moderating relationships (Aguinis and Adams, 1998).

**Study Variables**

The independent variable for this study is the Organizational Enablers for Social Capital. The dependent variable is the BPO outcome as measured by the three costs – production, coordination and vulnerability. Social capital, intellectual capital and knowledge sharing are the additional variables.

**Control Variables**

The strategy and operations of the client as well as the nature of the candidate process will have an impact on the outcome of the BPO (Ghosh and Scott, 2006). Two important dimensions of processes are (1) innovation/mechanistic and (2) efficiency/centralized (Mintzberg, 1991). Centralized processes can fare better when outsourced. A centralized, mechanistic process is more cost efficient in production costs, but is slow in responding to market changes compared to a decentralized, innovative process (Malone, 1987). Therefore, control variables included in the study will measure the organizational profile and strategic profile of the client and vendor firms and the profile of the candidate process (Ghosh and Scott, 2006).

**Organization Interviewed (Client Side)**

The client chosen is a multinational technical support organization. This organization is involved in the support of multi-vendor networking equipment, with network management and service capabilities. Network service offers include design, installation, monitoring and break-fix support. The product introductions, field trials, network design and installation services were outsourced to an offshore vendor to increase available headcount for these processes, reduce operating costs through labor arbitrage and provide in-region internationally located technical personnel.

The chosen organization was found to have several KM systems and practices to provide bi-directional transfer of knowledge from the client to the vendor and vice versa (Table 1). Usage data was collected over an 8-month period.
Table 1: Information Technology Usage for Knowledge Sharing

<table>
<thead>
<tr>
<th>Knowledge Management System</th>
<th>Objectives and Usage Goals</th>
<th>Average Monthly Usage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Listservers, Discussion Boards</td>
<td>Capturing threads of discussions on topics raised by team members and their subsequent contributions.</td>
<td>29 unique issues or threads of discussion created per month</td>
</tr>
<tr>
<td>Checklists</td>
<td>To guide technical support work from past experience and ensure that adequate data collection and situational analysis is being done. These checklists support building best practices on directed tasks such as configuring phones as well open-ended tasks such as collecting customer information for network designs.</td>
<td>3 New Checklists per month were developed</td>
</tr>
<tr>
<td>Lessons Learnt Lists, FAQ</td>
<td>To ensure that new “rules of thumb” and experience is captured and shared for future use</td>
<td>54 lessons learnt bullet points were documented per month</td>
</tr>
<tr>
<td>Training Presentations</td>
<td>Training materials are developed by scouring the listservers, discussion boards and FAQ. Presentations include all the listerv threads and their resolutions, the list of lessons learnt and pointers to any checklists or process/product document that is considered a “must read”.</td>
<td>Monthly training presentations created by the client personnel are imparted to all vendor personnel.</td>
</tr>
</tbody>
</table>

**Organizational Enablers for Building Social and Intellectual Capital**

In this BPO relationship, the client personnel are more experienced in the work domain than the vendor personnel. The client organization realized that to make the BPO effective vendor personnel needed to be mentored and trained in the domain. A mentoring process was put in place to increase vendor capabilities and encourage interactions between client and vendor staff on suitable learning projects (Figure 2). These practices enabled the creation of social and intellectual capital.

The mentoring resources on the client side were limited and needed to be managed effectively. To serve the two fold goals of providing training to the vendor personnel as well as supporting the bi-directional knowledge transfer, the client decided to institute practices to build social and intellectual capital. A mentoring program was instituted, whereby vendors could apply for client mentoring and assistance on an upcoming project. The client established a review board to screen each request for knowledge potential and optimal fit for the goals.

If a project is selected, then personnel from the vendor and client work collaboratively on the project over a span of 4-6 weeks. Advantages are seen in building intellectual capital – in terms of exchange of norms, work practices, common language and standards as well as tacit knowledge that is difficult to codify and contextualize. Social capital is built, as obligations are set and met, resulting in the development of trust, understanding of cultural diversity and establishment of joint ownership for work. The latter was critical, as the BPO goals were broader than cost savings. Project meetings are held frequently and the client personnel served as mentors in the relationship – thus there was an expectation of value to be obtained from the process on the part of the participating vendor staff.

Likewise, the client participant was able to build up site specific and international expertise. Both parties, client and vendor, are motivated to participate in the mentoring program to improve network installation quality and minimize downstream customer network issues. Hence, the program established the preconditions necessary for intellectual and social capital to form (Nahapiet and Ghoshal, 1998).
RESULTS

Interviews of Client Side Personnel

Interviews were conducted with members of the client organization, who were involved in supporting the BPO through participation in the mentoring program as well as supporting customers after the vendor had performed installations at those sites. A service operations manager and two technical engineers were interviewed. One of the engineers (A) had been regularly participating in the mentoring program and had mentored multiple vendor staff on multiple projects. It may be noted that the engineers had other responsibilities and participation in the mentoring program was only a secondary responsibility for them. The questions posed include:

1. Describe the problems that you face in the BPO?
2. What knowledge management processes are used?
3. Do they solve any of the problems in the BPO?
Table 2: Interview Responses

<table>
<thead>
<tr>
<th>Interviewee</th>
<th>Interview Response</th>
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<th>S</th>
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<tr>
<td><strong>Q1. Problems Faced in the BPO?</strong></td>
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<tr>
<td>Manager</td>
<td>“Root cause analysis indicated the troubles were due to incorrect installations and inadequate trouble shooting experience on the part of the vendor”</td>
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<td></td>
<td></td>
<td>X</td>
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<tr>
<td>Engineer A</td>
<td>“I am frustrated with the lack of lead time on these troubles, often I have to get site information on a call with an irate customer contact in the middle of the night”</td>
<td>X</td>
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<tr>
<td>Manager</td>
<td>“Our web site with all the technical documents and checklists and lessons learnt was not being consulted by the vendor, they just did not understand how they could apply it”</td>
<td>X</td>
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<td><strong>Q2. What knowledge management processes are used?</strong></td>
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<td>Engineer B</td>
<td>“We considered reducing the vendor’s responsibilities to tier 1 level field support, who perform remote functions solely on command from the client engineers. But that would not help our need for more support engineers, and probably increase our workload”</td>
<td>X</td>
<td>X</td>
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<tr>
<td>All</td>
<td>“The knowledge was all there on the support site - if only we could get the vendor to understand the practice and utilize it correctly”.</td>
<td></td>
<td></td>
<td>X</td>
<td>X</td>
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<tr>
<td>Engineer A</td>
<td>“We decided on using a mentoring program that could allow the vendor to learn the correct way to do the job in real situations by having one of us helping them out. We were motivated to reduce the midnight calls and they wanted to continue their BPO business. We did not want them to just transfer their work to us, so we instituted a selection process in the mentoring program”</td>
<td>X</td>
<td>X</td>
<td>X</td>
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<td>X</td>
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<tr>
<td>Manager</td>
<td>“We still get more requests than we can support”</td>
<td>X</td>
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<td><strong>Q3. Do they solve any of the problems in the BPO?</strong></td>
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<tr>
<td>Manager</td>
<td>The regular communications and scheduled bimonthly training sessions developed a strong relationship with the offshore people. We need them to do the work correctly. They learned our way of doing things and we gained offshore experience.”</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
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<tr>
<td>Engineer B</td>
<td>“They developed confidence and were able to engage us as peers. We saw an increase in the usage of our knowledge bases and tools.”</td>
<td>X</td>
<td>X</td>
<td>X</td>
<td>X</td>
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<tr>
<td>Engineer A</td>
<td>“The number of customer complaints have been reduced dramatically. Finding time to serve as Mentors is still tough.”</td>
<td>X</td>
<td></td>
<td></td>
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<td>X</td>
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</table>

**INTERVIEW RESPONSE TABULATIONS**

| 7 | 3 | 6 | 4 | 4 |
The interview responses are tabulated in Table 2. The interview responses show the relationship between the creation of intellectual and social capital and the downstream success of knowledge sharing efforts in the BPO. Key word and key phrase analysis was done to find instances of support for each of the constructs in the research model.

Keywords and phrases such as items that induce expectations/motivation to participate, e.g., “lack of lead time”, “increasing workload”, “reducing vendor responsibilities”, provide opportunities for interaction – “regular meetings” are coded as social capital enablers.

Words such as “relationships” and “confidence” are coded as social capital, while “experience”, “understanding how”, “correct way”, “our way” imply the intellectual capital construct of building structure.

Keywords that infer knowledge sharing include “utilize knowledge”, “usage”, “learn” and “transfer”.

Phrases used to imply impact on the BPO outcome include: “reduced customer troubles”, “reduced midnight calls” and “complaints have been reduced”.

The mentoring program established a vehicle for the creation of social and intellectual capital through cooperative work opportunities. Both parties were able to build a strong relationship and common work practices. The coding of the interview responses indicates that 7 responses referred to the creation of organizational enablers for social and intellectual capital (OE).

Confidence was established in the relationship that allowed for the creation of social and intellectual capital. Three and six responses alluded to the development of properties of social (SC) and intellectual capital (IC), respectively. Additionally, four responses quoted the increase in knowledge sharing (KS). Each knowledge sharing response was also associated with a reference to social or intellectual capital formation.

The interviewees quoted the improved quality of installation work performed and the reduction of customer trouble reports. The impact of social and intellectual capital on the BPO outcome is evident from 4 of the 9 interview responses, which have mentioned some aspect of the reduction of BPO costs (BPO). Two of the responses had key words that referenced all five components of the model.

**DISCUSSION**

The results support the propositions listed, and justify the need to pursue a larger field study using a survey to collect data from both sides of the BPO – the client and vendor.

The client – vendor relationship in a BPO can be quite arduous, with jobs at stake and differences in capabilities of the two organizations. This study shows that if a mutually beneficial mentoring program is instituted that increases interactions and both parties have an expectation of benefits, then the overall relationship in the BPO can be improved. With an improved relationship and the development of shared work practices, social and intellectual capital is created resulting in greater knowledge sharing. As a result the BPO outcome is improved. Practitioners may note that the investment into building successful working level relationships in a BPO can be worthwhile.

**Implications for Research**

A research framework based on SCT to study knowledge sharing in BPO is developed and supported. Organizational enablers to build relationships across the client and vendor personnel can impact the establishment of social and intellectual capital. The results of this study support the notion that benefits of SCT can be seen in downstream knowledge sharing processes. The preliminary results indicate that the BPO outcome is improved. By linking SCT with the coordination costs from coordination theory, this study makes a valuable contribution to the body of IS research. Researchers have been looking for the manifestation of social and intellectual capital in downstream work processes. This research finds empirical evidence of such linkages using a case study of a BPO.
REFERENCES


