

Should I stay (abroad) or should I go (home)?
Backshoring and dynamic capabilities

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Introduction

In the last few years, economic press and consulting firms reports have devoted increasing attention to cases of multinational companies which decided to move back home their operations from foreign countries (PwC 2013; BCG 2011; The Economist 2013). The phenomenon has been also fostered by political interventions: in the US, President Obama has made the return of manufacturing operations a part of the national agenda. Backshoring is defined as “*the decision to relocate in the firm’s home country production or supply previously off-shored*” (Fratocchi et al. 2014: p. 56). Backshoring is driven by trends (in wages, labour productivity, energy costs and exchange rates) that are redrawing the map of global manufacturing cost competitiveness, reducing the appeal of traditionally low-cost countries (e.g. China, Brazil, Russia) while increasing the relative competitiveness of leading exporting economies (e.g. US, Germany) (BCG, 2014).

The knowledge of backshoring is still mainly anecdotal. Few academic studies approached the topic (e.g. Fratocchi et al. 2013; Kinkel 2014), focusing almost exclusively on its (cost) drivers while leaving unaccounted the organizational processes that companies face when moving back home their operations. The present paper is exploratory. The aim of the paper is to contribute to the extent literature, identifying whether a typology of backshoring processes exists, and investigating how and to what extent organizational capabilities are involved when managing such processes.

We conducted an empirical research on a sample of Italian firms that have backshored their operations in the last decade. After clustering their backshoring processes, we conducted a multiple case study analysis in order to get detailed information on how they have reorganized their resource base when relocating their plants back home.

Backshoring: just a simple location problem?

Backshoring has been recently studied within the framework of the global supply chain literature (Gray et al. 2013), which appointed backshoring as “*essentially a manufacturing location decision*” (Ellram 2013: p. 3). Studies adopting such perspective are mainly focused on identifying drivers of the location decision and their evolution in the global economy. These drivers are factors related with product (e.g. raw materials location, weight), labour costs, skills availability, logistic infrastructures, strategic access to customers and suppliers, country risk, and government trade policies (Ellram, Tate and Petersen 2013). Similar drivers have been identified concerning the backshoring decision (see for instance, Fratocchi et al. 2013, Sarder and Nakka 2014, PwC 2013), even if the analysis aimed at defining such factors

are mainly based on few case studies and on secondary data. An exception is represented by Kinkel's study (2014), which offers empirical evidence of German backshoring activities over the past 15 years. According to his analysis, quality issues and high transport costs are the most important reasons for backshoring decisions, followed by availability of qualified personnel and labour costs.

Partially moving from the literature which represents backshoring as a typical location decision, Gray and colleagues (2013) suggest to interpret backshoring as the "reverse" of a previous offshoring decision. Following this perspective, backshoring is not an isolated decision, rather it is the final part of a complex process which starts from the offshoring decision (why, when, where and to whom the operation was originally offshored) and leads eventually to backshoring. In other words, Gray and colleagues (2013) implicitly suggest that the following backshoring decision is strictly linked with the preceding offshoring decision and the way the firm has managed the associated resources and competences during the offshored period.

Adopting a process perspective, Kinkel and Malonca (2009) suggest to consider backshoring as a correction of prior misjudgements in offshoring decisions rather than long-term adjustments to changing conditions at the foreign location. According to the authors, the main reason for such failure is related to problems in transferring knowledge on how to run reliable production processes.

Whether backshoring is considered as a planned location choice or the correction to a mistaken offshoring strategy, the extant literature is mainly focused on identifying its causes while leaving unanswered the question about "how" this process is managed (Fratocchi et al. 2014). As suggested by Gray and colleagues (2013: p. 29), studying the process of backshoring is "*a potentially fertile ground to gain new insights not only about managerial location decisions but also more generally about organizational learning*". During the offshoring period, companies learn what are the difficulties and the hidden costs of an offshoring experience: such knowledge represents a resource that may be useful in future location experiences. Furthermore, the process of relocation back home requires the company to find organizational procedures in order to preserve and transfer the tangible and intangible resources developed during the offshoring experience.

Dynamic capabilities for backshoring

In this paper we adopt the dynamic capabilities framework to investigate *how* firms manage the backshoring process.

The concept of dynamic capabilities has been originally proposed to provide further theoretical explanations on “how and why certain firms build competitive advantage in regimes of rapid change” (Teece et al. 1997: p. 509). Works on dynamic capabilities move from the assumption that firms must adapt to and exploit changes in their business environment to survive and prosper under conditions of change. This is contingent to the capabilities of firms of creating, extending and modifying their resource base (Eisenhardt and Martin 2000; Barreto 2000).

Overall, the literature on dynamic capabilities is aimed at exploring how firms identify and develop new opportunities, how they exploit such opportunities through the coordination of assets and how, in doing so, they generate new business models and governance forms (Dunning and Lundan 2010; Helfat et al. 2007; Teece and Pisano 1994). Put differently, dynamic capabilities represent the (inimitable) capacity of a firm to shape, reshape, configure and reconfigure its resource base to cope with or to promote changes at the technological and/or market level.

We believe that the dynamic capabilities framework is appropriate to study backshoring for two reasons.

First, backshoring implies the variation of firms’ resource bases. We argued that (first offshoring and then) backshoring decisions are primarily location choices. Any location choice involves the variation of the resource base as firms have to replicate or create ex-novo their tangible resources, human capital and knowledge assets in a different location. The variation of the resource base is even more complex if the location choice is combined with a change in the firm’s value chain configuration. That is, when firms combine the choice of relocating activities with the choice of reducing the degree of vertical integration through outsourcing strategies or of increasing it through insourcing strategies (Gray et al. 2013).

Second, backshoring choices are associated with changes at the market level. Backshoring decisions are based on attempts to catch cost-related, risk-related or quality-related advantages and are explained by changes in the level of such factors across countries at different points in time. Moreover, several backshoring operations involve emerging countries that are going through deep economic and technological changes (BCG 2014). Again, it can be difficult to discern between temporarily or permanent changes, as well as to anticipate all their possible consequences.

Therefore, dynamic capabilities, in terms of sensing, seizing and transforming processes (Teece 2007), are fundamental to wisely manage location decisions.

Methodology and preliminary results

We conducted an empirical analysis on a sample of Italian firms which, over the last decade (2003-2013), decided to backshore their production. The first step of the analysis (conducted on a sample of 27 firms) is aimed at identifying a typology of backshoring processes. Hence we developed three case studies, representing the backshoring processes previously identified. We focused our analysis on Italian firms because Italy is the second country (just after the US) in terms of number of companies which backshored, as shown by Fratocchi and colleagues (2013) on a survey on 230 international cases of backshoring.

The list of companies to include in our analysis was compiled consulting 1) LexisNexis® Academic, one of the world's largest general news databases, searching for Italian newspaper and magazine articles which contain the word "backshoring"; 2) white papers by consulting companies; 3) internet research engines; 4) existing academic studies. Then, we enriched our information through the AIDA database, which contains comprehensive economic and financial information on over 1 million Italian companies. The final sample is composed by 32 backshoring cases, concerning 27 Italian companies (the discrepancy in numbers is explained by the fact that 5 companies implemented more than one backshoring activity). For each backshoring case, we collected information about: location of the headquarter, industry, year in which offshoring was implemented, year in which backshoring was implemented, country of backshoring, disclosed reasons for backshoring (evaluated on a scale from 1 = cost to 9 = quality); backshoring mode (new plant, increasing of the production capacity of an existing plant, outsourcing); cultural distance between the home and the host country (Kogut and Singh 1988).

We use this data for conducting a hierarchical cluster analysis, in order to identify a typology of backshoring processes. Our preliminary results show four main clusters:

- Cluster 1 (6 cases) includes firms that offshored their operations in the '90 in countries close to Italy (mainly East European countries), and recently (on average backshoring occurred in 2011) they decided to come back. Quality is the most important backshoring factor reported by firms.
- Cluster 2 (10 cases) includes firms that offshored their operations at the beginning of 2000s in countries culturally close to Italy (mainly East European countries). Backshoring mainly occurred in 2012. A variety of backshoring reasons, both internal (e.g. costs, supply chain management optimization) and external (e.g. competitive pressure, institutional opportunities) are indicated by companies.

- Cluster 3 (6 cases) includes firms that offshored their operations at the beginning of 2000s in countries that are both geographically and culturally distant (such as China and Bangladesh). Backshoring mainly occurred in the period 2012-2014. Backshoring is driven by increasing labor cost combined with the firm's product portfolio repositioning.
- Cluster 4 (10 cases) comprises firms that offshored since 1990 in a variety of both European and East Asian countries. They started backshoring since the first years of 2000s, representing a group of "first movers". Their offshoring experience was on average short, thus suggesting either wrong location choices or strategy aimed at exploiting short-term low-cost conditions.

Starting from this typology, we will select three case study from different clusters, in order to study the organizational processes that the firm manages to backshore. Our aim is to investigate which kind of capabilities are involved in backshoring processes and whether different backshoring processes imply different capabilities.

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