



# Logistics service innovation by third party logistics providers in China: Aligning *guanxi* and organizational structure<sup>☆</sup>



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## ABSTRACT

In response to intensifying competition and escalating customer expectations, third-party logistics (3PL) providers need to become more innovative. In logistics service innovation, external relationships are important sources of resources and knowledge. Drawing on social capital theory and the strategy-structure-performance paradigm, this study proposes that *guanxi* (Chinese system of social networks and relationships that facilitates business and other dealings), expedites logistics service innovation by 3PL providers in China. This study also proposes that the effect of *guanxi* on logistics service innovation is contingent on the alignment between the type of *guanxi* and the provider's organizational structure. We tested our proposed model using survey data from 165 3PL providers in China. Our findings suggest that both political and business *guanxi* have a positive effect on logistics service innovation; however, those types of *guanxi* should be used in consideration of the firm's organizational structure. The results suggest that with respect to logistics service innovation, political *guanxi* is more effective for 3PL providers whose organizational structure is highly centralized or has low formalization. The converse applies to business *guanxi*.

## 1. Introduction

Given intensifying competition and escalating customer expectations, third-party logistics (3PL) providers need to become more innovative (Flint et al., 2005). That is particularly true in China. There, most 3PL providers lack sufficient value-added service provisions (Cui et al., 2012), while facing mounting requirements for modern, comprehensive logistics services from customers, especially from multinational companies (Cui et al., 2012). Innovation is essential for 3PL providers in responding to demands for advanced logistics services (Pedrosa et al., 2015). Through innovation, 3PL providers can increase customer satisfaction (Bellingkrodt and Wallenburg, 2015), expand market share, outperform competitors, and enjoy a first-mover advantage (Pedrosa et al., 2015; Wagner, 2008). Again, that is particularly true in China.

With such significant benefits, recent logistics studies have called for research into service innovation for 3PL providers (Busse and Wallenburg, 2011; Flint et al., 2005; Grawe, 2009). Busse (2010) highlighted significant differences in service innovation by 3PL providers from that by manufacturers and other service providers. A few studies have investigated 3PL industry-specific service

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innovation and identified several drivers of such innovation; the drivers include customer requirements, absorptive capability, environmental issues, and geographic coverage (Cui et al., 2012; Panayides and So, 2005). Nevertheless, research on service innovation by 3PL providers remains in its infancy (Busse and Wallenburg, 2011; Grawe, 2009), and “research on logistics innovation in China is almost nonexistent” (Cui et al., 2012 p. 100). Considering the uniqueness of China’s logistics context (e.g., distinctive culture, recent deregulation, and booming logistics markets), there is an urgent need to understand service innovation by 3PL providers in China. Thus, the present study examines whether *guanxi* (a characteristic of Chinese culture) facilitates logistics service innovation by 3PL providers; it examines how the alignment between *guanxi* and the organizational structure affects logistics service innovation.

*Guanxi* has profound implications for doing businesses in China (Park and Luo, 2001). It refers to particular connections that bond partners through exchanges of favors and mutual obligations (Lovett et al., 1999). In Western relationship building, cooperative behavior is stressed at the organizational level, such as through trust and commitment to the system (Grawe et al., 2015; Wang, 2007). By contrast, *guanxi* emphasizes the use of individual connections and social interactions at the personal level, such as the exchange of personal care, favors, and *ganqing* (affection) (Chen et al., 2013; Shaalan et al., 2013). As a result of these differences, it is important for Western managers operating businesses in China or conducting businesses with Chinese partners to understand the essence of *guanxi*. Such understanding is particularly important for managers of international 3PL providers, who may lack experience with China or familiarity with Chinese ways of doing business (Rahman et al., in press) as the Chinese logistics industry was not deregulated until the end of 2005. However, research on *guanxi* in the context of 3PL is scarce (Chen et al., 2010). Moreover, the bridging role of the 3PL provider as an orchestrator of the supply chain and extensive interactions among multiple supply chain members (Zacharia et al., 2011) make *guanxi* critical for 3PL providers. It is possible that *guanxi* for such providers is different from *guanxi* among manufacturers. Accordingly, an understanding of *guanxi* needs to be extended to the 3PL context.

Drawing on the social capital theory, this study proposes that *guanxi* facilitates service innovation of 3PL providers in China. In fact, *guanxi* has been documented as a Chinese version of social capital; it allows firms to access external resources and information (Zhang and Li, 2010), and it thus facilitates innovation (Cui et al., 2013; Wu, 2011). This approach is particularly relevant in relation to service innovation by 3PL providers in China because most 3PL providers in China lack the resources for innovation (Cui et al., 2012). Therefore, *guanxi* tends to be regarded as more important and effective for Chinese 3PL providers that wish to access external resources and knowledge for logistics service innovation.

However, in the literature on manufacturer innovation, the findings regarding the effect of *guanxi* on innovation are inconclusive: some studies identified the positive impact of *guanxi* on innovation (Liu et al., 2012; Ng and Law, 2015); others suggested that *guanxi* may not always facilitate innovation (Cui et al., 2013; Wu, 2011). This may be because, besides its benefits (Chen et al., 2013; Luo et al., 2012), *guanxi* also has a “dark side” (i.e., potential damaging effects due to corruption, collective blindness, and domino effects when firms within the *guanxi* network fail) (Gu et al., 2008). This issue is important because it addresses the potential paradox in the relationship between social capital and innovation raised by Florida et al. (2002). Those scholars argued that a strong social network might result in conformity, which undermines innovation; weak social ties allow new ideas to be accepted quickly into the social network, thereby encouraging innovation.

To better understand this point, drawing on the strategy-structure-performance (SSP) paradigm (Chandler, 1962; Rumelt, 1974), this study further examines the contingent effect of organizational structure. According to SSP, the effectiveness of a strategy depends on alignment between the strategy and the organizational structure. Thus, we argue that the effect of *guanxi* on logistics service innovation is dependent on its alignment with the organizational structure (e.g., decentralization, formalization, and specialization).

The rest of this paper is structured as follows. In Section 2, we provide a literature review and develop our hypotheses. In Section 3, we describe our methodology. Our findings along with their implications are covered in Section 4, followed by conclusions in Section 5.

## 2. Literature review and hypothesis development

### 2.1. Logistics service innovation

Owing to globalization and deregulation, 3PL providers are facing mounting demands for value-added, comprehensive logistics services and increasingly severe competition (Pedrosa et al., 2015). To survive in a competitive market, providers have to innovate. Innovation among 3PL providers is fundamentally different from that in other service industries and manufacturing (Busse, 2010; Wagner, 2008): it often arises not as a result of a formal plan or process but as an ad hoc response to customer requests (Busse, 2010; Cui et al., 2012). Accordingly, industry-specific studies on innovation are important for 3PL providers.

However, service innovation by 3PL providers has been insufficiently studied (Busse and Wallenburg, 2011). There is even a lack of common understanding as to what logistics service innovation actually signifies (Cui et al., 2012). For example, following a broad definition of innovation, Panayides and So (2005) defined innovation by 3PL providers as “the adoption of an idea or behavior—whether pertaining to a device, system, process, policy, program, product or service—that is new to the adopting organization” (Panayides and So, 2005, p. 182). From a user’s perspective, Daugherty et al. (2011) defined logistics service innovation as “a new, helpful ideal, procedure, or practice in logistics operations that is different from a company’s current practice” (Daugherty et al., 2011, p. 26). In contrast, Flint et al. (2005) defined logistics service innovation as “any logistics related service from the basic to the complex [developed by 3PL providers] that is seen as new and helpful for a particular audience” (Flint et al., 2005, p. 114).

Such variation in the definitions reflects the diversity in the literature related to service innovation (Biemans et al., 2016; Witell et al., 2016); several conceptualizations of service innovation and related terms appear (Snyder et al., 2016; Witell et al., 2016). Some studies have conceptualized service innovation with different dimensions or categories, such as product versus process service

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