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## Outsourcing and supplier learning: insights from the Indian software industry

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**Abstract:** There is increasing agreement that Indian software firms are making the transition from competitive advantage based on low cost to competitive advantage based on innovation. However, there are few insights about how this transition process works. This paper seeks to bring together the outsourcing, global value chains and firm capability literatures. It draws on empirical material focused on learning and innovation 'events' in Indian software firms – their inputs and sources – and makes headway in opening the 'black box' of supplier learning in outsourcing relationships. This paper suggests that learning from customers was important but insufficient for making the transition. Capability formation depended significantly on other channels and mechanisms outside or independent of outsourcing relationships. This paper shows how firms actively mobilised and combined internal and external sources to address spaces for learning and innovation created by outsourcing.

**Keywords:** firm capability; global value chains; India; Bangalore; innovation; learning; outsourcing; software industry; globalisation; technology; knowledge intensive industries; supplier.

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**Biographical notes:** Rasmus Lema is an Assistant Professor at the Department of Business and Management, Aalborg University. He obtained his DPhil from the University of Sussex in 2010. The research for this paper was undertaken at the Institute of Development Studies (IDS) at the University of Sussex.

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### 1 Introduction

In recent decades, firms in China and India have become major producers of products and services for markets in OECD countries. Observers agree that outsourcing and offshoring from Northern America and Western Europe to these 'rising powers' of Asia has brought about major changes in the global distribution of *production capabilities*. Conversely, *innovation capabilities* have so far remained largely concentrated in the so-called 'West'. However, this is now starting to change. There is increasing evidence that China and India are progressing from production to innovation in a range of different industries (Altenburg et al., 2008). But despite the increasing agreement that offshore outsourcing has a major influence on the shift in innovation capabilities, the literature has only