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## Performance of professional service firms from emerging markets: Role of innovative services and firm capabilities

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### ABSTRACT

Professional service firms (PSF) from emerging markets face a financial dilemma: PSFs tend to utilize high-wage labor, yet their emerging market status makes foreign clients cautious regarding quality and less willing to pay high prices. To allay these concerns, PSFs may be able to develop attractive, highly innovative services, but as the resource-based view (RBV) notes, this requires emerging market firms to possess critical capabilities to support such a competitive advantage. Relying on services theory, we propose that entrepreneurial orientation (EO) of management and expert human capital (HC) are critical capabilities, enabling a PSF to develop and market innovative services profitably. In testing our model on 201 Indian PSFs, we find a mediating role for innovativeness whereby EO and HC drive service innovation which, in turn, accounts for financial performance. Further, we find EO positively moderates the innovative service–performance relationship as proactive, risk-tolerant managers improve foreign marketing. Insights for theory and practice are provided that enable PSFs to overcome the constraints and challenges of their emerging market origin.

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### 1. Introduction

In the last few decades, the global business environment has changed dramatically through the rise of emerging economies, liberalization of markets, and advancements in information and communication technologies. As a result, global services, especially professional services, have become one of the faster growing sectors of the world economy (Dotzel, Shankar, & Berry, 2013; Brock & Alon, 2009; Javalgi, Gross, Joseph, & Granot, 2011). Particularly important is the rapid growth of services in emerging markets such as India, where service contributions to GDP as well as service exports far outpace the global average (UNCTAD, 2015).

Often perceived as low-cost providers of basic services, many emerging market service firms are attempting to increase financial performance by climbing the value chain and are increasingly offering high-value, professional services (Milberg & Winkler, 2013). Professional service firms (PSFs) are specialized providers of knowledge-intensive, high-skill services that utilize a well-educated, professional workforce (Reihlin & Apel, 2007), and are traditional in fields such as law, accounting, management consulting, and engineering (von Nordenflycht, 2010). Reflecting the economic development of emerging markets, many emerging market firms are offering traditional professional services as they shift to higher-value offerings, attracted by the promise of higher profits and greater revenue associated with professional services (Gupta, Seshasai, & Ganguly, 2008).

Yet many of these professional service firms struggle to be profitable, as they confront economic problems associated with their emerging market origins (Javalgi & White, 2002). Emerging market firms face a financial dilemma as they move up the services value chain: PSFs encounter a rising cost structure because they intensively utilize higher-wage labor, yet their emerging market status weakens their pricing power to foreign clients who often are

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unfamiliar with and resist procuring professional services from emerging markets (Oshri, Kotlarsky, & Willcocks, 2011). Rising wage levels at home and price resistance from foreign clients who continue to associate India and other emerging markets with low-cost outsourcing threaten PSF profitability (Fairell, Noshir, & Sascha, 2005; Milberg & Winkler, 2013). To meet these challenges, some successful PSFs have developed capabilities to offer highly innovative services that provide unique, high-quality offerings that are differentiated from the traditional professional services of competitors. Importantly, the services literature (Lee, Ginn, & Naylor, 2009) recognizes that innovativeness of a service is crucial, since innovation tends to enhance financial performance by differentiating offerings, better satisfying user requirements through novel, high-value service solutions (Lowendahl, 2000).

Relying on the resource-based view (RBV), we propose emerging-market PSFs are able to innovate profitably to the extent they possess key firm-level capabilities, specifically management and labor inputs that both develop and deliver competitive professional services in a way that overcomes foreign client resistance (Javalgi et al., 2011). A PSF's ability to innovate successfully depends on its operant capabilities, the key resources that act on other resources to create value (Vargo & Lusch, 2004). Operant capabilities involve management and front-line labor resources that enable PSFs to develop innovative services and aggressively seek out foreign clients. Traditionally, orientations of business managers in emerging markets such as India have been conservative, tradition-bound, and focused on conventional business practices and processes (Virmani, 2007). In contrast to traditional management, entrepreneurial management is thought to be a more productive operant resource since entrepreneurial managers are better able to exploit business opportunities in emerging and developed markets (Oviatt & Mcdougall, 2005; Naman & Slevin, 1993). As for labor capabilities, the traditional comparative advantage of emerging market service providers was competent, low-cost human capital (Milberg & Winkler, 2013). To implement an innovative professional service strategy, many emerging market PSFs have upgraded their human capital, increasingly hiring high-skilled, high-wage employees and investing in state-of-the-art training (Oshri et al., 2011).

We ask the question: "How do operant capabilities of managerial and labor resources enable emerging market PSFs to compete profitably in global markets for professional services?" Specifically, we examine the entrepreneurial orientation of management and the expertise of human capital as necessary for emerging market PSFs to derive financial benefits from developing and delivering innovative professional services. However, this investigation is not straightforward since prior empirical evidence yields mixed results for the relationship between these two firm-level capabilities and financial performance. While some researchers (Hult, Hurley, & Knight, 2004; Zahra & Garvis, 2000) find a positive relationship between entrepreneurial orientation and profitability, other studies report weak or no effect of entrepreneurial orientation on performance (e.g., Atuahene-Gima & Ko, 2001; Slater & Narver, 2000; Jantunen, Puumalainen, Saarenketo, & Kyläheiko, 2005). As for human capital, some researchers (Sels et al., 2006; Ling & Jaw, 2006) find that human resource intensity enhances profitability. Others (Fung, Xu, & Zhang, 2007) find that proxies of human capital are either not linked to a firm's return on assets or negatively linked to financial performance. Overall prior findings are mixed, suggesting the relationship between operant capabilities and performance is complex, leaving unresolved the specific way entrepreneurial orientation and human capital create value for emerging market PSFs.

The current research makes three important contributions to the international business literature on services in the context of knowledge-based, professional service enterprises in emerging

markets. First, we not only recognize the central role of service innovativeness, but also develop a conceptual model that draws from the resource-based view (RBV) of the firm and links PSF capabilities, innovativeness of service offerings, and financial performance. We explain how the unique context of emerging markets constrains a PSF's ability to engage successfully in an innovative service strategy, challenging the firm's capabilities to develop and execute the strategy profitably. Second, we explain how key PSF resources (i.e., management and labor capabilities) are operant resources, meaning they influence financial performance indirectly by enabling a PSF to develop and market innovative service offerings. Our contribution lies in empirically demonstrating that the PSF capabilities–financial performance relationship is mediated by the innovativeness of a firm's service offerings. Third, we propose that financial payoffs from innovative service offerings are also contingent on PSF capabilities, demonstrating the need to efficiently implement an innovative service strategy to achieve profitability. We contribute by offering new theoretical insights into how and why operant capabilities may not directly drive financial outcomes for emerging market firms, but rather act as a moderator, enabling appropriately endowed PSFs to better develop and exploit their innovative service offerings.

## 2. Theoretical background

The resource-based view of the firm (RBV) builds on firm heterogeneity, attributing the development and maintenance of competitive advantage through innovation to firm-specific resources and capabilities (Ahuja & Katila, 2004; Leonard-Barton, 1992). The basic premise is that resources and capabilities increase the efficiency and effectiveness of firms in general (Barney, 1991), and the development of new products and services in particular (Rindova & Kotha, 2001; Smith, Collins, & Clark, 2005). A firm's ability to develop and capitalize on an innovative service strategy depends upon its operant capabilities which function as a firm's "core competence, the fundamental knowledge and skills of an economic entity that represent potential competitive advantage" (Vargo & Lusch, 2004: 5).

Theorists (Barney, 1991; Vargo & Lusch, 2008) suggest operant resources enable the innovative services offered by PSFs to be developed and implemented profitably, allowing firms from emerging markets to compete in global markets through effective service development and delivery. Two components of a firm's intangible capabilities that have been identified as most relevant to facilitating financial outcomes are human capital of front-line employees (Bollen, Vergauwen, & Schnieders, 2005; Subramaniam & Youndt, 2005) and the entrepreneurial orientation of management (Hult et al., 2004; Naman & Slevin, 1993). Based on prior research, we suggest entrepreneurial management and expert human capital are key firm-level capabilities, the operant resources crucial to a PSF's ability to engage in an innovative, professional service strategy.

According to the RBV, human capital, including tacit knowledge and specialized skill of employees, is usually acquired through personal experience and direct involvement (Pralhad & Hamel, 1990), and is specific to the context and profession (Ployhart & Moliterno, 2011; Szulanski, 1996; Szulanski & Jensen, 2006). Once acquired, human capital can build a sustainable competitive advantage because, as an operant resource, it can leverage a firm's ability to create value (Pralhad & Hamel, 1990; Teece, 1998), and the creation process is usually difficult to imitate or substitute (Barney, 1991). For PSFs, front-line employees endowed with the appropriate operational skills, tacit knowledge, and personal capabilities are fundamental to successfully executing a service strategy (von Nordenflycht, 2010).

Different from human capital which highlights the knowledge repertoires of front-line employees, entrepreneurial orientation stresses the processes and practices of the firm's management in being proactive and willing to take risks in securing future performance (Cavusgil & Knight, 2009). In the fast-changing global environment, the operant resource of entrepreneurial management enables firms to implement plans creatively by diligently scanning the environment and responding to market challenges and new opportunities in novel ways (Jantunen et al., 2005). However, in many emerging markets, traditional approaches to management tend to be conservative and highly conventional, not particularly predisposed to risky, unorthodox actions (Virmani, 2007).

### 3. Hypotheses development

#### 3.1. PSF capabilities and innovative service offerings

Consistent with the economic development of emerging markets, many PSFs from India and elsewhere increasingly emphasize higher-value services, differentiating their offerings through innovative service solutions (Javalgi et al., 2011). Dotzel et al. (2013, p. 259) define service innovation as “a new or enhanced intangible offering that involves the firm's performance of a task/activity intended to benefit customers.” This is consistent with Hitt, Hoskisson, and Ireland's (1994) definition of service innovativeness as the tendency to introduce novel and creative processes, approaches, or ideas that provide economic benefits by improving productivity, client satisfaction, and other outcomes. Service innovation is considered crucial for performance enhancement, enabling service firms to offer customers new and upgraded benefits (Lee et al., 2009). Consequently, developing innovative services to meet the growing demands of global customers has become strategically important for firms to differentiate themselves from their international competitors.

Emerging market PSFs often focus their limited resources on the most promising service segments, employing a differentiation strategy to stimulate customer loyalty by effectively meeting the needs of the service marketplace (Cavusgil & Knight, 2009). Innovation supports a differentiation strategy, enabling firms to offer higher-value benefits to clients, potentially at premium prices and at attractive margins (Lowendahl, 2000). Innovative offerings involve improved service content and delivery, attracting new clients and fueling revenue growth (Maister, 1997). Revenue and margin benefits from innovative, professional services have the potential to be sustainable since service clients may face higher switching costs, resulting in an innovation-based barrier to entry that protects profits (de Brentani, 2007).

Theorists (Vargo & Lusch, 2008) imply that PSFs utilize their operant resources to develop and deliver innovative services to the global market. To create successful innovative services, PSFs are thought to engage their core competencies by utilizing human capital and entrepreneurial management to design unique, high-value service offerings.

#### 3.2. Entrepreneurial orientation

Entrepreneurial orientation (EO) is defined as “the processes, practices, and decision-making activities” of management that support new initiatives (Lumpkin & Dess, 1996: 136). Firms exhibiting an entrepreneurial orientation are more proactive, risk-taking, and inventive; and therefore, better able to perceive and act upon new opportunities. As pointed out in the literature, international entrepreneurship, “the discovery, enactment, evaluation, and exploitation of opportunities, across national borders, to create future goods and services” (Oviatt & McDougall, 2005: 540),

extends this operant resource to a global scale. In the context of PSFs, entrepreneurship is a managerial orientation which initiates change in the development and delivery of services, while creatively responding to the market and competitors regardless of expectations or traditional practice (Naman & Slevin, 1993; Lowendahl, 2000). Importantly, entrepreneurial orientation stresses the processes and practices of the firm's management in being proactive and willing to take risks for future performance (Cavusgil & Knight, 2009).

Innovative service offerings have become a critical factor for PSFs in emerging markets as these offerings create competitive advantage for the firm. Service innovativeness refers to the propensity to introduce service innovations to satisfy customers and improve firm value (Dotzel et al., 2013). Yet developing an innovative service involves uncertainty regarding customer acceptance and competitor reactions, requiring the firm to respond decisively to changing foreign market dynamics. In this way, EO is a key operant resource because entrepreneurial firms are proactive and actively seek major opportunities to gain competitive advantage. In the management and entrepreneurship literature, studies conclude that innovativeness is fundamentally driven by pro-activeness and risk-taking (Perez-Luno, Wiklund, & Cabrera, 2011). Thus, high levels of EO are expected to enable PSFs to develop innovative service offerings because entrepreneurial managers are predisposed to proactive, inventive activities.

**Hypothesis 1.** Entrepreneurial orientation (EO) is positively associated with innovativeness of service offerings (ISO) of emerging market PSFs.

#### 3.3. Human capital

Human capital expertise (HC), as a knowledge repository, is the intelligence, skill, knowledge, and expertise of human labor in the organization (Bollen et al., 2005; Griffith, Yalcinkaya, & Calantone, 2010; Ployhart, Iddekinge, & Mackenzie, 2011). As a knowledge-based organization, PSFs rely upon an intellectually skilled workforce, reflecting the key role played by human capital (von Nordenflycht, 2010). The expertise of service personnel is crucial to developing an innovative service strategy because customer variability requires that front-line employees be proficient at diagnosing problems, thinking creatively, and developing novel solutions (Lusch, Vargo, & O'Brien, 2007; Ployhart et al., 2011; Skaggs & Youndt, 2003). Firms that employ differentiation or customization require employees to possess prior training, experience, and education (Skaggs & Youndt, 2003). It is the prior experience and acquisition of new knowledge by employees that determine a firm's operant capability to successfully develop a service innovation (de Pablos, 2004). Human capital gives the PSF access to diverse knowledge domains and key skills which enable front-line employees to question prevailing norms and procedures, thereby enhancing the firm's innovativeness (Subramaniam & Youndt, 2005).

Human capital resources include the “training, experience, judgment, intelligence, relationships, and insights of individual managers and workers in a firm” (Barney, 1991: 101). In the entrepreneurship literature, human capital is known to enhance the discovery and exploitation of business opportunities, leading to innovative services that meet changing customer needs (Shane & Venkataraman, 2000). Professional service firms rely heavily upon human capital resources to sustain competitive advantage by offering services that are new and inventive (Javalgi & Todd, 2011). Consequently, human capital is expected to be a key operant resource enabling a firm to develop innovative service offerings (Becker, 1993).



**Hypothesis 2.** Human Capital (HC) is positively associated with innovativeness of service offerings (ISO) of emerging market PSFs.

### 3.4. Mediating role of innovativeness of service offerings

In the literature, a positive relationship between innovativeness of service offerings and financial performance has been supported by studies in developed markets. Specific developed market examples include the U.S. (Cavusgil, Calantone, & Zhao, 2003), the Netherlands (Nijssen, Hillebrand, Vermeulen, & Kemp, 2006), Hong Kong (Luk, Yau, Sin, Chow, & Lee, 2008), and Italy (Cainelli, Evangelista, & Savona, 2006). Other studies have also documented the positive relationship between a firm's innovativeness and financial performance (Atuahene-Gima, 1995; Atuahene-Gima & Ko, 2001; Qian & Li, 2003; Zahra, Ireland, & Hitt, 2000). Hence, we expect the observed innovativeness of PSFs from emerging markets to be positively linked to financial performance, consistent with extant research.

However, prior research has not considered the role of operant resources such as human capital and entrepreneurial orientation in developing the innovative services that, in turn, yield financial performance. Theorists (Vargo & Lusch, 2008) recognize that profitable services marketed to customers are developed by the application of operant resources, the firm's core competencies and key to obtaining competitive advantage. Importantly, services offered to customers are the means by which operant resources are transmitted to the marketplace since the firm's human capital, entrepreneurial orientation and other competencies are embedded in the innovative services offered (Vargo & Lusch, 2004). In this sense, an offered service is a mediator, acting as a transmission mechanism connecting the firm's operant resources to customers. Because a PSF's management and labor capabilities are incorporated in service offerings, innovative services mediate the impact operant resources have on financial performance. That is, the causal logic of service theorists (Vargo & Lusch, 2008) supports the notion that human capital and entrepreneurial orientation enable the innovative service offerings responsible for a PSF's financial performance. Innovative service offerings are the means by which operant resources are translated into performance outcomes, meaning innovative services mediate the effect operant resources have on performance outcomes.

**Hypothesis 3.** Innovativeness of service offerings mediates the impact operant capabilities have on financial performance.

### 3.5. Moderating effects of entrepreneurial orientation and human capital expertise

While operant resources facilitate service development, they also may enable PSFs to implement and deploy an innovative service strategy efficiently, helping to market services to foreign customers and generate financial performance in the marketplace. Extant research focuses primarily on main effects of innovativeness on financial outcomes (Aas & Pedersen, 2011), largely ignoring the way operant resources moderate the service innovation–performance relationship.

However, PSFs from emerging markets face unique challenges to their profitability, creating variability in financial performance that reflects the varying operant capabilities of firms to market innovative professional services to foreign customers (Dess, Lumpkin, & Covin, 1997). We suggest the performance impact of an innovative service strategy for any given PSF is highly contingent upon the way strategy is implemented (*i.e.*, marketed to foreign customers) as influenced by the firm's managerial and labor resources. Given the unique, traditional characteristics of

firms in the emerging market context, this research further examines the moderating role played by key operant resources: entrepreneurial orientation of management and the human capital expertise of labor.

### 3.6. Entrepreneurial orientation

As noted, entrepreneurial orientation is associated with a proactive competitive posture and risk-taking activity (Slater & Narver, 1995). Unlike a tradition-bound manager from an emerging market such as India, an entrepreneurial manager will continue searching for opportunities and initiate improvement projects (Hult et al., 2004). Augier and Teece (2007) also conclude that bringing an innovation to market involves the entrepreneurial activity of scanning markets, technologies, and business models, and interpreting them differently to create new value. When managers are more proactive, they have higher tendencies to implement innovative ideas that increase their firm's ability to compete efficiently in foreign markets. An entrepreneurial orientation may enable PSFs to better exploit their innovative service offerings not only by proactively marketing services abroad, but also by assuaging risks that buyers perceive when purchasing high-value, professional services from emerging market providers.

Consistent with RBV, we suggest EO may play an indirect operant role, enabling a firm to entrepreneurially exploit other resources that may have the potential for financial payoffs. Our thesis is that entrepreneurial capabilities directly leverage the innovativeness of PSF's services by proactively executing the differentiated service strategy, aggressively initiating business activities and marketing processes necessary to penetrate foreign markets and gain acceptance by foreign buyers for highly innovative services. Entrepreneurial management of the PSF can exploit the foreign market potential for innovative professional services by aggressively seeking-out foreign clients and persuasively marketing services, thereby strengthening the innovative service–performance relationship.

Prior research results for a direct EO–performance relationship are equivocal, suggesting that entrepreneurial risk-taking, *per se*, may not consistently deliver superior financial outcomes. Yet research findings imply that firms with an entrepreneurial orientation have a higher capacity to exploit the benefits of innovativeness. For example, entrepreneurial orientation is reported to be a key enabler of market success for firm innovativeness (Hult et al., 2004; O'Cass & Weerawardena, 2009), both for technology and market-based innovations (Zhou, Yim, & Tse, 2005). Similarly, multiple studies undertaken to examine the effects of firm culture and strategy confirm the operant effects of an entrepreneurial orientation on leveraging or exploiting innovativeness for positive results (Cavusgil & Knight, 2009; Hult et al., 2004). Although EO, in and of itself, may not directly drive financial outcomes, prior findings support a positive moderating role for entrepreneurial orientation to improve the effectiveness of the way innovative services are brought to market, aggressively driving foreign sales. Based on the above discussion, we propose the following moderation hypothesis.

**Hypothesis 4.** Entrepreneurial orientation (EO) strengthens the positive relationship between innovativeness of service offerings and financial performance of emerging market PSFs.

### 3.7. Human capital expertise

In the unique context of emerging markets, PSFs that invest in the highest-quality human capital face a rising cost structure due to a growing demand for “best in class” professional workers as well as the general rise in wage levels in developing countries

(Contractor & Mudambi, 2008). In India, for example, not only are wages rising quickly, but there is also high turnover among professionals, increasing constraints on the supply of talent (Fairell et al., 2005). Emerging market PSFs that support a differentiated service by hiring high-skilled experts are engaging in a high cost implementation of their service strategy. Further, as noted, such emerging market firms are often unable to charge premium prices since foreign clients may resist high prices due to the continuing association of emerging markets with low-cost outsourcing (Oshri et al., 2011). Thus, the high cost of expert professional labor can squeeze the financial payoffs for emerging market PSFs, particularly given the price concerns of foreign clients that limit revenues.

However, compared to selling basic services, expert human capital may be appropriate for marketing highly innovative professional services. Marketing an innovative service benefits from highly skilled, creative employees because they can offset the hesitation of foreign buyers to purchase innovative services from emerging market service providers. While such buyers readily accept low-cost basic services from emerging market providers, they may be skeptical of procuring highly innovative professional services from emerging markets due to doubts regarding reliability, quality, and other desired service attributes (Ueltschy, Laroche, Eggert, & Bindl, 2007). The skill and capabilities of expert employees from emerging markets allay concerns regarding service quality since employee expertise signals high quality services (Quader, 2007). Skilled, creative employees also tend to introduce cost efficiencies into the marketing and service delivery process, increasing the financial payoff when bringing innovative services to foreign markets (Xu & van der Heijden, 2005).

Consequently, human capital expertise is expected to enhance the financial outcomes from marketing innovative professional services by improving revenues and cost efficiencies, thereby positively moderating the innovative service–performance relationship. Human capital expertise enhances performance outcomes from marketing innovative services abroad because expert employees increase foreign buyer’s confidence in emerging market services while skilled and creative employees better manage the cost of the service delivery process (Georgiadia & Pitelis, 2012; Verma & Jayasimha, 2014; Xu & van der Heijden, 2005). Hence, human capital expertise is expected to be a positive moderator, strengthening the relationship between innovative services and performance.

**Hypothesis 5.** Human capital (HC) strengthens the positive relationship between innovativeness of service offerings and financial performance of emerging market PSFs.

Fig. 1 provides a schematic representation of the conceptual model and the related hypotheses and also shows the significance of the hypotheses tests later performed.

**4. Method**

**4.1. Data collection and sample**

Although researchers face significant challenges to conducting empirical research in India (Varma & Budhwar, 2012), the emerging market of India was chosen as the setting for this study with a sampling from knowledge-intensive professional service sectors for two reasons. First, the tremendous growth in India’s economy in the last 50 years (1964 to 2014) is attributable to services, which grew from 37.4% of GDP in 1964 to 53.0% of GDP in 2014 (The World Bank, 2015). India is now ranked 6th in the world in commercial services exports (The World Bank, 2015) and, according to World Bank projections, is estimated to become the 4th largest world economy by 2020 (Varma & Budhwar, 2012). Second, India’s commercial service exports have tripled in the past 10 years, from \$52 billion in 2005 to \$156 billion in 2014, representing an average annual growth rate of 14%, which is much higher than the world average of 8% for the same time period (The World Bank, 2015; WTO, 2014).

Data collection was accomplished with a cross-sectional industry random sample of professional service enterprises located in India. The sample is comprised of knowledge-intensive, privately-owned firms from the following service sectors: computer/information technology, management consulting, architecture, engineering, health, financial, accounting/payroll, real estate/leasing, tourism, and legal services. Survey respondents were pre-qualified by e-mail and telephone to verify: (1) service classification, (2) international business involvement, and (3) that respondents were an owner, CEO, or a key international management executive.

From an initial sample of 730 firms, 201 responses (28% response rate) were received from the following service sectors: 54% computer/information technology, 24% management consulting services, 5% architecture/engineering, 5% health services,

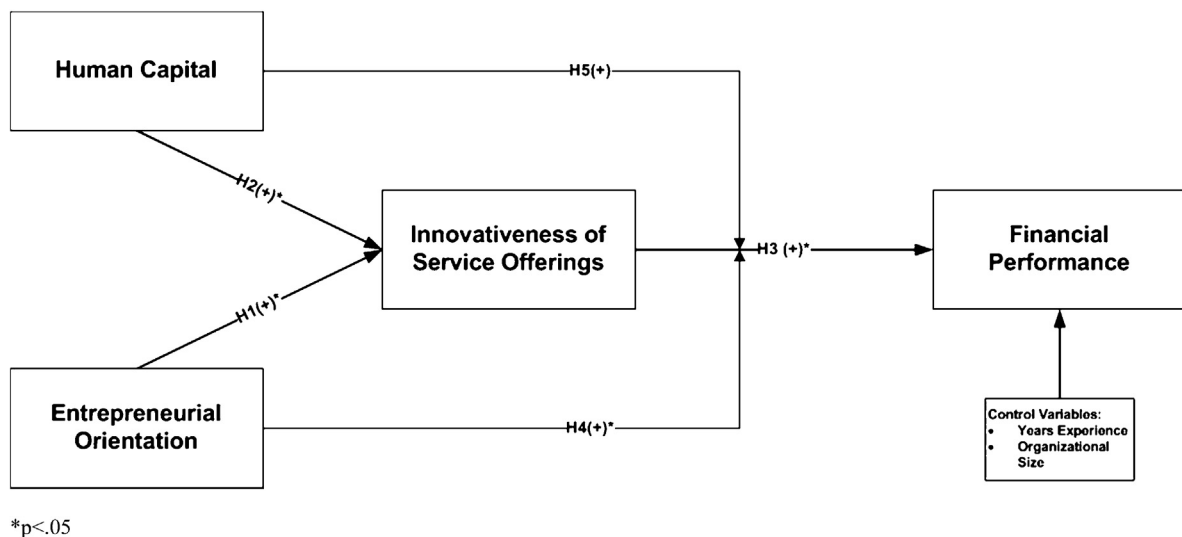


Fig. 1. Performance of professional service firms from emerging markets model.

4% financial services, 2% real estate/leasing services, 2% accounting/payroll services, 2% legal, and 2% tourism services. Specific sectors are more heavily represented due to government privatization and liberalization of the Indian economy beginning in the late 1980s with more prevalent growth having been targeted by the government in these industry sectors. The majority of firms sampled had anywhere between 25 and 49 employees. A comparison of early and late respondents revealed no differences, thus a non-response bias is not indicated (Armstrong & Overton, 1977).

Of the PSFs sampled, reported annual sales revenue indicated that 77.1% of the firms earned less than \$1 million, 20.4% of the firms earned between \$1 million and \$9.9 million, 2.0% of the firms earned between \$10 million and \$99.9 million and .5% earned over \$100 million. International expansion of PSFs in India was aggressive and accelerated with nearly 33% of firms earning over 50% of total sales revenue from foreign sales, and the majority of firms earning between 25% and 49% of sales from foreign markets.

## 4.2. Measures

All measures were adapted from previously used scales. Items were measured on a seven-point scale with “1” as strongly disagree or much worse and “7” as strongly agree or much better, respectively. Table 1 reports scale items, standardized loadings, composite reliabilities and average variance extracted for each measure.

### 4.2.1. Financial performance

PSFs in this study are privately held enterprises. In order to overcome hesitancy of owners in disclosing private financial performance, subjective performance measures were selected. Moreover, subjective self-report measures are deemed reliable (Pearce, Robbins, & Robinson, 1987) and both direct and indirect measures of performance are strongly correlated (Venkatraman & Ramanujam, 1986). Consistent with prior research, three items were used to measure financial performance which asked owners or key executives to assess the profitability of their firm relative to their principal competitor over the past three years on return on investment, return on assets, and foreign sales revenue growth (Contractor, Kumar, & Kundu, 2007; Lu & Beamish, 2001; Mcdougall & Oviatt, 1996).

### 4.2.2. Entrepreneurial orientation

A PSF's entrepreneurial orientation is measured using a scale based upon the work of Naman and Slevin (1993). The scale has been empirically tested in the literature (e.g. Hult et al., 2004). The scale uses three items to measure an entrepreneurial orientation at a firm level. Respondents indicated the degree to which they “believe that wide-ranging acts are necessary to achieve our objectives,” “initiate actions to which other organizations respond,” and “have a strong proclivity or tendency for high-risk projects.”

### 4.2.3. Human capital expertise

A four-item measure of the skill, knowledge, and the ability of employees of the firm was used to measure the construct of human capital expertise (Subramaniam & Youndt, 2005). The scale was developed from human capital and strategic human resource management literature and has been tested in a variety of industries including services. Respondents indicated the degree to which their employees “are experts in their particular job and functions,” “are widely considered the best in our industry,” “are highly skilled,” and “are creative and bright.”

### 4.2.4. Innovativeness of service offerings

Innovativeness of service offerings was measured using a four-item scale based upon the work of Atuahene-Gima (1995). Respondents were asked to describe their firm's services by responding to a list of statements that inquired about the innovativeness of the firm's service strategy compared to competitors. Respondents indicated the degree to which their service(s) “offer unique benefits to the customers, not offered by competitors,” “are radically different from competitor services,” “are highly innovative, replacing a vastly inferior alternative,” and “provide higher quality than competitors.”

### 4.2.5. Control variables

Control variables used in this study are firm size and international business experience. Firm size is commonly measured by the number of full-time employees (FTE; Kundu & Katz, 2003) and has been shown to impact performance (Durand & Coeurderoy, 2001; Pan, Li, & Tse, 1999). International business experience, measured as the number of years a company has been involved in international business (YRIBE), was also used as a

**Table 1**  
Measures, standardized loadings, composite reliabilities and average variance extracted.

Construct	Item	SL <sup>*</sup>	CR	AVE
Financial performance (PERF)	Compare your firm over the past 3 years relative to your two most important competitors on return on investment	0.86	0.86	0.67
	Compare your firm over the past 3 years relative to your two most important competitors on return on assets	0.85		
	Compare your firm's foreign sales revenue growth of services since the start of the international activities to competitors	0.73		
Entrepreneurial orientation (EO)	We believe that wide-ranging acts are necessary to achieve our objectives	0.72	0.75	0.52
	We initiate actions to which other organizations respond	0.94		
	We have a strong proclivity or tendency for high-risk projects	0.41		
Human capital expertise (HC)	Our employees are experts in their particular job and functions	0.93	0.95	0.83
	Our employees are widely considered the best in our industry	0.87		
	Our employees are highly skilled	0.93		
	Our employees are creative and bright	0.92		
Innovativeness of service offerings (ISO)	Our service(s) offer unique benefits to the customers, not offered by competitors	0.88	0.88	0.66
	Our service(s) are radically different from competitor services	0.91		
	Our service(s) are highly innovative, replacing a vastly inferior alternative	0.74		
	Our service(s) provide higher quality than competitors	0.69		

SL = standardized loadings; CR = composite reliability; AVE = average variance extracted.

Measurement model fit  $\chi^2(91) = 206.87$ ,  $p < 0.01$ ; RMSEA = 0.08; CFI = 0.94; TLI = 0.92; SRMR = 0.06.

\* All standardized loadings are significant at  $p < .001$  level.

**Table 2**  
 Item means, standard deviations, and correlations.

Variable	Mean	S.D.	EO1	EO2	EO3	HC1	HC2	HC3	HC4	ISO1	ISO2	ISO3	ISO4	PERF1	PERF2	PERF3	FTE	YRIBE
EO1	4.91	1.3	–															
EO2	4.66	1.33	0.68	–														
EO3	4.83	1.25	0.21	0.39	–													
HC1	5.86	1.13	0.18	0.23	0.11	–												
HC2	5.33	1.32	0.16	0.23	0.17	0.80	–											
HC3	5.68	1.3	0.17	0.26	0.15	0.85	0.78	–										
HC4	5.87	1.1	0.19	0.22	0.15	0.86	0.81	0.86	–									
ISO1	5.49	1.14	0.39	0.45	0.25	0.26	0.20	0.28	0.28	–								
ISO2	5.28	1.24	0.37	0.45	0.34	0.24	0.18	0.27	0.20	0.81	–							
ISO3	5.99	0.97	0.30	0.31	0.09	0.27	0.13	0.28	0.26	0.61	0.58	–						
ISO4	5.59	1.2	0.21	0.34	0.17	0.27	0.16	0.32	0.26	0.59	0.68	0.66	–					
PERF1	5.49	1.09	0.23	0.25	0.22	0.24	0.29	0.24	0.24	0.33	0.38	0.34	0.37	–				
PERF2	5.4	1.13	0.23	0.21	0.20	0.13	0.14	0.12	0.14	0.43	0.46	0.37	0.40	0.75	–			
PERF3	5.48	1.28	0.33	0.39	0.32	0.40	0.39	0.32	0.40	0.47	0.33	0.41	0.63	0.60	–			
FTE	3.17	1.86	0.06	0.00	0.07	0.02	–0.04	–0.03	–0.02	0.04	0.06	0.08	0.03	0.22	0.25	0.17	–	
YRIBE	2.85	1.26	0.07	0.05	0.00	0.02	0.01	0.01	–0.02	0.04	0.05	0.09	0.04	0.09	0.05	0.10	0.06	–

For all correlations:  $p < 0.05$ .

control since international experience may influence firm performance (Yeoh, 2004; Zahra et al., 2000).

4.3. Measurement validation

To assess the construct validity of the measurement model, construct items were analyzed in a confirmatory factor analysis (CFA) using MPlus 7.0 (Muthén & Muthén, 2012). The measurement model included 14 items for the four latent factors and two items for the control variables. The CFA indicated a reasonable fit of the data ( $\chi^2_{(91)} = 206.87, p < 0.01$ ; RMSEA = 0.08; CFI = 0.94; TLI = 0.92; SRMR = 0.06). Convergent validity was assessed through the examination of factor loadings, composite reliabilities and average variance extracted, as shown in Table 1. All standardized loadings were positive and significant (Anderson & Gerbing, 1988). Composite reliabilities were well above the 0.70 cut-off value and ranged from 0.75 to 0.95 (Bagozzi & Yi, 1988). Average variance extracted ranged from 0.52 to 0.83 and was above the 0.50 cut-off for all factors (Fornell & Larcker, 1981). Discriminant validity was assessed by comparing the average variance extracted for each construct to the squared correlations of the other factors. The squared correlations ranged from 0.00 to 0.30 and in all cases the average variance extracted was larger than the squared correlations, supporting discriminant validity of the factors (Anderson & Gerbing, 1988; Fornell & Larcker, 1981). Additionally, discriminant validity was tested by comparing the measurement model to a model where the correlations between factors are constrained to unity (Bagozzi & Yi, 1988). A chi-squared difference test between the two models ( $\Delta\chi^2_{(12)} = 62.01, p = 0.00$ ) indicates that the correlations are significantly different from 1, establishing discriminant validity. The assessment of convergent and discriminant validities supports the validity of study constructs.

Table 2 shows the item level means, standard deviations and correlations. The means for the items range from 2.85 to 5.69. Notably, the high means for the human capital expertise and financial performance measures substantiate the highly-skilled nature and strong performance of India’s PSFs. The correlations between the pairs of variables were all positive and significant.

4.4. Common method bias

As suggested in the analytic literature (Podsakoff & Organ, 1986), three methods were employed to examine the potential for common method bias. First, the wordings of the items were improved to ensure their clear meanings to the survey respondents. Second, the data were examined for common method bias using the Harman Single-Factor Test (Harman, 1967; Podsakoff, Mackenzie, Jeong-Yeon, & Podsakoff, 2003). All variables were loaded onto a single factor and then compared to the confirmatory factor analysis. The chi-squared difference test showed the confirmatory factor model has superior fit ( $\Delta\chi^2 = 1016.16, df = 11, p = 0.00$ ), indicating that common method bias may not be of serious concern. The third test for common method bias utilized the marker variable technique (Lindell & Whitney, 2001). As a proxy for common method bias, we utilized a variable that was theoretically unrelated to the scales in the analysis. We used a scale that measured the number of years between the inception of the firm and the firm’s entry into international sales. The correlations and statistical significance of the zero-order correlations were adjusted downward by the lowest positive correlation ( $r = 0.02$ ) between the marker variable and other variables (Lindell & Whitney, 2001; Sheng, Zhou, & Li, 2011). As seen in the off diagonal of Table 3, none of the significant correlations between the latent

**Table 3**  
 Construct means, standard deviations, and correlations.

Variable	Mean	S.D.	PERF	EO	HC	ISO	FTE	IBE
Financial performance (PERF)	5.46	1.02		0.33**	0.28**	0.55**	0.25**	0.08
Entrepreneurial orientation (EO)	4.80	1.02	0.35**		0.25**	0.51**	0.00	0.04
Human capital expertise (HC)	5.69	1.13	0.29**	0.27**		0.30**	–0.03	–0.01
Innovativeness of service offerings (ISO)	5.59	0.98	0.56**	0.53**	0.32**		0.05	0.04
Organizational size (FTE)	3.17	1.89	0.27**	0.01	–0.02	0.06		–0.07
International business experience (IBE)	2.85	1.26	0.09	0.06	0.01	0.06	–0.06	
MV marker (years to entry)	3.48	5.91	0.02	–0.11	–0.15*	–0.15*	0.10	0.17

Notes: N = 201. Zero-order correlations are below the diagonal; correlations adjusted for potential common methods variance are above the diagonal (Lindell & Whitney, 2001; Sheng et al., 2011).

\*  $p < 0.05$ .  
 \*\*  $p < 0.01$ .



variables became non-significant, indicating that common method bias is not a serious concern.

**5. Hypotheses testing and results**

To test the hypothesized relationships, structural equation modeling using MPlus 7.0 (Muthén & Muthén, 2012) was employed. We present the coefficients for three models, a main effects model, a direct effects model and the moderating effects model, in Table 4. Model 1 estimates the main effects of entrepreneurial orientation (EO), and human capital expertise (HC) on innovativeness of service offerings (ISO), and ISO on financial performance of professional service firms (PERF). The main effects structural model estimates provide good fit:  $\chi^2 = 213.39$  ( $df = 99$ ,  $p < 0.00$ ), TLI of 0.93, CFI of 0.94, SRMR of 0.07 and RMSEA of 0.08 (Hu & Bentler, 1999). Following Iacobucci, Saldanha, and Deng (2007), Model 2 estimates the coefficients for the direct paths from entrepreneurial orientation and human capital to performance and allows us to test for mediation. The direct effects structural model provides good fit:  $\chi^2 = 208.87$  ( $df = 97$ ,  $p < 0.00$ ), TLI of 0.93, CFI of 0.94, SRMR of 0.06 and RMSEA of 0.08. A chi-squared difference test ( $\Delta\chi^2_{(2)} = 4.52$ ,  $p = 0.10$ ) indicates that the main effects model is the better fitting model. As such, we use the main effects model for hypothesis testing for Hypotheses 1 and 2 and the direct effects model to test the mediation effects proposed in Hypothesis 3. Model 3 is used to test Hypotheses 4 and 5, and includes the moderation effects of both entrepreneurial orientation and human capital expertise on the relationship between innovativeness of service offerings and the financial performance of professional service firms.

Hypotheses 1 and 2 posit that entrepreneurial orientation and human capital are positively associated with innovativeness of service offerings. In Model 1, the coefficients are positive and significant ( $\beta_{EO} = 0.51$ ,  $p < 0.00$ ;  $\beta_{HC} = 0.18$ ,  $p < 0.01$ ;) providing support for both Hypotheses 1 and 2.

Hypothesis 3 proposes that innovativeness of service offerings mediates the PSF capabilities relationship with financial performance. Specifically, Hypothesis 3 posits that innovativeness of service offerings mediates the impact of human capital on the financial performance relationship. As suggested by Iacobucci et al. (2007), the significant paths between HC and ISO, and ISO to PERF, ( $\beta_{HC} = 0.18$ ,  $p < 0.05$ ;  $\beta_{ISO} = 0.45$ ,  $p < 0.00$ ), along with non-significant direct effects from HC to PERF ( $\beta_{HC} = 0.12$ ,  $p > 0.05$ ;) indicate a mediation effect (see Model 2). A comparative Sobel z-test demonstrates that the sizes of the mediated path is greater than the direct path for HC ( $z = 2.21$ ,  $p < 0.05$ ), providing support for complete mediation. As such, Hypothesis 3 is supported. Further, Hypothesis 3 suggests that innovativeness of service

offerings mediates the impact of entrepreneurial orientation on the financial performance relationship. The significant paths between EO and ISO, and ISO to PERF, ( $\beta_{EO} = 0.51$ ,  $p < 0.00$ ;  $\beta_{ISO} = 0.45$ ,  $p < 0.00$ ), along with non-significant direct effects from EO to PERF ( $\beta_{EO} = 0.06$ ,  $p > 0.05$ ), indicate a mediation effect. A comparative Sobel z-test demonstrates that the sizes of the mediated paths are greater than the direct path for EO ( $z = 3.81$ ,  $p < 0.01$ ), providing support for complete mediation. As such, Hypothesis 3 is further supported.

Hypotheses 4 and 5 propose that entrepreneurial orientation and human capital moderate the relationship between innovativeness of service offerings and performance. As predicted, entrepreneurial orientation is shown to have no direct effects on performance ( $\beta_{EO} = 0.11$ ,  $p > 0.05$ ), but the interaction term is positive and significant ( $\beta_{EO \times ISO} = 0.18$ ,  $p < 0.05$ ), indicating that entrepreneurial orientation strengthens the relationship between innovativeness of service offerings and performance (see Model 3). Hence, Hypothesis 4 is supported. No support was found for Hypothesis 5, where both the direct effects of human capital on performance and interaction terms were found to be non-significant ( $\beta_{HC} = 0.09$ ,  $p > 0.05$ ;  $\beta_{HC \times ISO} = -0.12$ ,  $p > 0.05$ ).

The boundary conditions for our main effects model were tested to determine whether development capabilities of management and labor are non-linear in relation to innovativeness of service offerings. We believe this is important because it not only extends study findings but it also reduces the likelihood of having spuriously significant interaction effects (Cortina, 1993). The quadratic results are reported as Model 4 in Table 4. The results of this post-hoc analysis suggest that the significant interactions are not spurious. Additionally, the analysis found one significant quadratic effect. The quadratic effect for entrepreneurial orientation is negative and significant ( $\beta_{EO \times EO} = -0.16$ ,  $p < 0.00$ ). This suggests that the relationship between entrepreneurial orientation and innovative service offerings is an inverted U-shape. That is, the relationship between entrepreneurial orientation and innovativeness of service offerings is the weakest at low and high levels of entrepreneurial orientation, suggesting EO initially increases ISO up to a point after which greater EO decreases ISO. This implies the efficacy of EO on ISO declines at higher levels of EO, where greater pro-activeness and higher risk-taking begin to interfere with developing unique, high-quality innovativeness of professional services. Additional analysis shows that the quadratic term for human capital was non-significant ( $\beta_{HC \times HC} = 0.01$ ,  $p < 0.88$ ).

All tests for main effects and moderation hypotheses were controlled for organizational size (number of employees, FTE) and number of years of international business experience (YRIBE). For all models, international business experience was non-significant and organizational size was significant (see Table 4).

**Table 4**  
 Structural model results with unstandardized estimates.

Paths	Model 1: main effects		Model 2: direct effects		Model 3: moderating effects		Model 4: moderating effects plus quadratic	
	Est.	p-Value	Est.	p-Value	Est.	p-Value	Est.	p-Value
EO → ISO (Hypothesis 1)	0.51	0.00	0.51	0.00	0.51	0.00	0.46	0.00
HC → ISO (Hypothesis 2)	0.18	0.01	0.18	0.01	0.17	0.01	0.18	0.03
ISO → PERF	0.51	0.00	0.45	0.00	0.50	0.00	0.51	0.00
FTE → PERF	0.12	0.00	0.12	0.00	0.13	0.00	0.13	0.00
YRIBE → PERF	0.06	0.24	0.06	0.22	0.04	0.45	0.04	0.45
EO → PERF	–	–	0.06	0.49	0.11	0.29	0.14	0.182
HC → PERF	–	–	0.12	0.06	0.09	0.16	0.08	0.24
EO × ISO → PERF (Hypothesis 4)	–	–	–	–	0.18	0.02	0.19	0.02
HC × ISO → PERF (Hypothesis 5)	–	–	–	–	–0.12	0.06	–0.12	0.06
EO × EO → ISO	–	–	–	–	–	–	–0.16	0.00
HC × HC → ISO	–	–	–	–	–	–	0.01	0.88

Model 1 fit:  $\chi^2 = 213.39$  ( $df = 99$ ,  $p < 0.00$ ), TLI of 0.93, CFI of 0.94 and RMSEA of 0.08. Model 2 fit:  $\chi^2 = 208.87$  ( $df = 97$ ,  $p < 0.00$ ), TLI of 0.93, CFI of 0.94 and RMSEA of 0.08.



## 6. Discussion

Drawing on the resource-based view (RBV), we develop and test a conceptual model of relationships between service innovation and performance of emerging market professional service firms. We suggest innovative, high-value services that offer foreign clients new and upgraded benefits have the potential to enhance profitability. Notably, developing and deploying valuable services in foreign markets are theorized to rely on key firm-level managerial and labor resources. According to the RBV, firms operate by leveraging and exploiting their operant resources, thereby attempting to gain a competitive advantage. The RBV provides insights into the potential benefits of acquiring and utilizing internal organizational resources that are appropriate to a PSF's contextual setting so as to achieve superior organizational performance (Day, 1994; Barney, 1991).

Importantly, our theoretical research question asks how managerial and labor operant resources enable emerging market PSFs to achieve desirable financial outcomes. As we note, extant research on managerial orientation and human capital is equivocal regarding a direct association with firm profitability, leaving unresolved the particular way these operant resources create value for emerging market PSFs. Our conceptualization of the drivers of financial performance for these firms recognizes that innovativeness of services mediates the impact operant capabilities have on revenue and profit outcomes. That is, we posit managerial orientation and human capital are key capabilities enabling PSFs to be highly innovative when developing professional services. Our empirical findings support the mediating role of service innovativeness, indicating expert front-line employees and proactive risk-tolerant management are necessary for PSFs to develop professional services that will be competitive in global markets. Our findings suggest these important labor and management attributes empower the creativity and inventiveness necessary for innovation in professional services.

Inventiveness is crucial for PSFs in emerging markets like India because they face daunting challenges such as escalating wages, low-cost reputations and many other constraints. Consequentially, our conceptualization acknowledges that emerging market PSFs confront serious challenges in the marketing and delivery of their service offerings within international markets. While foreign buyers are familiar with purchasing low-cost, basic services from emerging markets providers, they are unfamiliar with procuring innovative professional services, as they question service quality and resist higher prices. In exploring the moderating role of EO, we propose and find that PSFs with an entrepreneurially-oriented management are able to increase the financial returns from innovative services marketed in foreign countries. Entrepreneurial managers have a propensity to be proactive, take risks, and constantly push new ideas and approaches throughout the professional service organization (Hult et al., 2004; Melia, Perez, & Dobon, 2010). Our findings support the notion that entrepreneurial management strengthens the services–performance relationship by proactively marketing service innovations in foreign countries and mitigating the business risks associated with facing customers and international competitors (Javalgi & Todd, 2011).

Interestingly, our *post-hoc* analysis finds a significant quadratic effect for entrepreneurial orientation, suggesting a range limit for positive benefits from entrepreneurial managers. At low-to-moderate levels, proactive risk-taking facilitates service innovativeness but at high levels such aggressive management may interfere with organizational processes and routines, dampening innovativeness. We find that entrepreneurial management and service innovativeness have an inverted u-shape relationship suggesting that, at moderate levels, proactive risk-taking managers create a competitive advantage as they seek out and act upon new

opportunities. However, at high levels, intensely novel and risky managerial behaviors become dysfunctional, disrupting the firm's ability to develop commercially viable professional services. Nevertheless, our research documents that innovation is crucial, demonstrating that PSFs offering unique high-quality professional services differentiated from international competitors are best able to grow foreign revenues in a profitable manner.

However, our results indicate that while human capital expertise drives the innovativeness of service offerings, it does not moderate the services–performance relationship. Apparently, employee expertise for our sampled PSFs is most helpful in designing innovative services, but is not particularly influential in enhancing the payoff from marketing the services in foreign markets. While expert human capital positively influences inventiveness of PSFs at home, these labor-related resources do not enhance profitability in host countries where innovative services are marketed to foreign clients. Rather, it is entrepreneurial management that strengthens the services–performance relationship, suggesting that moderate proactive risk-taking by PSF management is the key operant resource for selling to foreign markets.

Overall, findings of this study demonstrate that innovative PSFs from India (and perhaps other) emerging markets should be guided by a service strategy that recognizes both the constraints and opportunities associated with achieving financial payoffs from professional services. Given the challenges of emerging markets, emerging market PSFs should develop and deploy innovative service strategies by aligning labor and management with the economic expectations of international clients. The strongest financial performers among the emerging market PSFs in this study possess crucial operant resources, suggesting that less endowed PSFs may need to make strategic investments in front-line labor and proactive managers, or partner with or acquire better endowed organizations.

Further, our research reveals the way labor and management capabilities drive financial performance for emerging market PSFs; operant resources enable firms to develop and deliver innovative professional services in a way that increases foreign sales and accounts for greater financial outcomes. By aligning with emerging market context and conditions in the global marketplace for professional services, appropriately endowed PSFs are able to capitalize on the capabilities of employees and management to profitably provide innovative professional services.

### 6.1. Managerial relevance

By highlighting the importance of innovativeness of service offerings in explaining financial performance, our study conveys to managers/owners of Indian and (potentially) other emerging market PSFs the need to appropriately leverage organizational operant resources. In particular, knowledge and skills of front-line employees (human capital expertise) and entrepreneurial orientation of management are crucial. For instance, Indian managers of professional service firms should utilize their front-line employees' skills and capabilities to develop innovative services such that the hesitation of foreign clients regarding service quality is mitigated. In a professional service context, the ability to deliver innovative services and solutions more effectively and efficiently than competitors is increasingly seen as a way to expand service offerings, retain existing clients, and acquire new foreign clients (Hogan, Soutar, McColl-Kennedy, & Sweeny, 2011). Yet the emerging market context sets limitations on the profitable deployment of expert labor when international market conditions constrain the pricing power for conventional professional services. This necessitates that emerging market PSFs engage in a highly differentiated, innovative approach to developing professional

services that are particularly attractive to foreign clients by providing greater value and convincing service solutions. Likewise, managers should recognize the need to be proactive in marketing their professional services abroad, engaging foreign clients to recognize and accept high-quality, professional services from emerging markets service providers.

Professional service firms in emerging markets are constantly challenged with respect to: (1) offering highly innovative, quality services to foreign clients, (2) sustaining competitive advantage by being innovative and entrepreneurial to achieve overall performance goals, and (3) developing and nurturing intangible resources, such as human capital expertise, so that employees continually develop new knowledge and stay current in the professional services sector in a highly-competitive global environment. Thus, our findings are consistent with researchers and managers seeking to understand the challenges and opportunities of managing emerging market, professional service firms (de Clercq, Sapienza, Yavuz, & Zhou, 2012).

As is evident, professional service firms face many challenges to acquiring, sharing, institutionalizing, and exploiting the appropriate mix of operant capabilities and service expertise. Both entrepreneurial management and professional service personnel serve as human links that integrate the firm's disparate internal functional knowledge areas. While focusing on cost efficiency, a means to enhance service effectiveness is through knowledge sharing, by creating a customer-oriented service culture within the emerging market PSF that focuses on collaborative goals and metrics among professionals, thereby aligning and strengthening the links of the firm's human capital expertise. From a management perspective, the firm's organizational structure and reward systems should be efficiently aligned to foster knowledge sharing, innovativeness of service solutions, and professional human capital expertise retention. For example, in the highly-skilled software industry, the lack of leadership training, learning, and growth opportunities for professionals was found to contribute to high attrition rates among Indian software firms (Agrawal, Khatri, & Srinivasan, 2012). Thus, selectively retaining appropriate service professionals is critical for sustained firm-specific advantages in today's global services marketplace.

### 6.2. Directions for future research

The current research highlights the ways emerging market PSFs can capitalize on the operant endowments of labor and management to achieve financial success. Perhaps, service sectors differ in the ability to leverage human capital expertise and entrepreneurial orientation, and consequently differ in the propensity for intangible capabilities to exploit service innovation to enhance performance. Examination of various service settings where operant resources can leverage innovativeness is important in understanding the most effective ways for emerging market PSF firms to grow and prosper in competitive global markets. Beyond the need to consider multiple service sectors, this research does not take into account changes over time in PSFs as the data were collected at a single point in time (Zikmund, 2003). A longitudinal study would allow firms to be studied over time and give a clearer picture of the causal effects of resources and capabilities on the financial success.

Additional research is also needed on the role of culture. A meta-analytic review of the relationship between innovation and performance among firms found that outcomes are dependent upon culture, and the type of innovation (Rosenbusch, Brinckmann, & Bausch, 2011). Cultural factors associated with the international service client, as well as the host and home markets, may influence the productivity and efficiency of human capital expertise to exploit innovative service solutions

and enhance performance outside of domestic markets. Furthermore, cultural differences are thought to directly affect entrepreneurial behaviors (Hitt, Bierman, Uhlenbruck, & Shimizu, 2006; Parasuraman, Zeithaml, & Malhotra, 2005). Evidence of cultural predispositions to entrepreneurship may create differential performance effects across countries, possibly predisposing firms from certain cultures to internationalize successfully or create competitive advantages.

The proposed model of PSF financial performance should also be tested in different institutional settings since the institutional environments of countries differ in the manner and extent to which they facilitate human capital expertise, entrepreneurship, innovation, and financial success. Institutional theory may offer insight into the environmental setting of emerging economies that help or hinder PSFs (Hoskisson, Eden, Lau, & Wright, 2000). Regulatory regimes, business practices, infrastructure issues, government policies, and subsidies are among the many country-specific conditions potentially impacting the potency of firm-level capabilities to affect performance. Although liberalization and privatization of many emerging market economies have increased competitive intensity, emerging markets such as India are leading contributors to global service trade.

### 6.3. Limitations

There are limitations to the conceptual scope of the research that may limit generalizability to other research domains and contexts. Our constructs are conceived as global variables, assessed as single, multi-item constructs and thereby ignore the potential implications of possible subcomponents or multiple dimensions. While adequate for examining our particular hypotheses, different conceptualizations and definitions may have revealed different relationships and outcomes. Likewise, we conceptualize services as largely basic or professional, and countries as being emerging or developed. These and other conceptual simplifications may limit the scope of our findings. In terms of our empirical analysis, our use of cross-sectional, self-report data and subjective performance measures may limit the conclusions that can be drawn relative to other research designs and methods. Similarly, our sample size, constrained by the size of our research budget, is modest but adequate to test our limited number of hypotheses. Overall, some caution should be exercised regarding our findings since the scope of research is bounded by various conceptual and empirical limitations.

In summary, this research contributes to understanding how PSFs from emerging markets translate operant resources of labor and management into strong financial performance. To compete internationally against larger firms from the developed world that possess stellar reputations and abundant resources, emerging market PSFs necessarily must rely upon intangible managerial and labor resources to develop and leverage service innovation. Profitable returns and foreign sales growth observed in this study highlight the importance of key capabilities for emerging market firms. Since operant capabilities of high-performance PSFs are not easily duplicated, service innovation and global expansion are likely to continue to pay-off financially for well-managed emerging market, professional service firms.

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