# **Reversing Course**

*Insourcing provides unexpected revenue streams*

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Abstract

*Since 2007, the rise of outsourcing and offshoring has created an environment in which companies feel they are saving money. Yet, despite the cut in labor costs, the decreased regulation, and shift in employee overhead, companies are failing to see the big picture.*

*It is during this increased demand for pampering by customers, in which Information Technology allows them to choose the company that best suit, answers, or caters to their needs, that companies must pay careful attention. Customers are empowered to make decisions based upon personal whim, and no longer feel leashed to one company or service. The levels of frustration, particular with offshored technical service and support, has created a backlash and a demand for support services based in the United States, and for support agents who are not only fluent in English, or the caller’s preferred language, but who are a native speaker of it themselves.*

*Because of this, companies are reversing course, or taking the exact opposite tactic as before, and realigning their operations to meet these demands. Offshored positions are decreasing, and companies are coming to realize that insourcing, or using your own internal resources, is the means to create greater customer satisfaction, but also experience unexpected benefits through higher employee morale, customer goodwill, and through local or national government incentives. All of these factors contribute to the bottom line unexpected ways, and may not have an immediate financial impact, but will nonetheless benefit the company in the long term.*

In December of 2007, the world entered the Great Recession, marked by a decline of economic growth and a sudden downturn of resources experienced by all. Very few persons or businesses experienced little to no impact from the Recession, and though it eventually ended, many still feel the aftershocks. As the Global Economy declined, some business saw outsourcing and offshoring as an alternative that would allow them to reduce expenditures and protect profitability (Parker + Lynch).

Problems arose, however, when companies assumed that customer satisfaction standards and final products would remain in line with expectations. This was not always the case, and in many the costs to correct these issues was greater than the overall savings. While companies chose outsourcing as an opportunity to ease financial strain, in some cases, it created more, (Parker + Lynch).

The purpose of this research paper is to examine the costs, disadvantages, risks, and benefits of outsourcing, and conversely insourcing. **Reversing course, or insourcing key components of business operations, and then turning them outward as separate business offerings, will add value to the company, increase profits, and may create unexpected revenue streams.**

Before proceeding further, it is important to understand several key terms used throughout this paper: outsourcing, offshoring, and insourcing. Without this understanding, further examination of the subject is without value.

“Outsourcing is an allocation of specific business processes to a specialist external service provider,” (Flatworld Solutions). Whether manufacturing, human resources, payroll, administration, or customer service support, outsourcing is a means for a company focus on their product or service, without becoming distracted by the myriad of other responsibilities businesses must keep in mind.

Offshoring is a form of outsourcing, in which the business engages a contracting company located in a foreign nation. Also referred as Global Outsourcing, many view as the boogeyman of manufacturing and customer service standards, yet offers many advantages to companies looking to save labor costs and experience lower levels of regulation, (Cynthia Myers, Chron).

Insourcing is the exact reverse of outsourcing, and often represents “reversing course” by a business, or a sudden reversal of a business decision, similar to the naval term used to signify a dramatic shift of direction. With insourcing, a company relies on internal resources, infrastructure, and teams of specialized or dual role employees to complete tasks formerly assumed by an outsourced party.

While offshoring and outsourcing may have the opposite result companies are anticipating, when properly managed it is an effective cost savings measure, and often allows businesses to focus on other key tasks, such as product design. Offshoring, particularly in manufacturing, is not disappearing, nor will it. Companies worldwide rely on offshored, contracted factories in locations throughout the globe to provide the facilities and materials for their products. Therefore, while there is often a negative connotation associated with outsourcing, it does have a positive impact on the worldwide economy.

In its effort to reduce the development time and costs for the 787, Boeing embraced outsourcing; however, the result was an aircraft delivered three years late, and the eventual grounding of the entire fleet due to overheating batteries, (Steve Denning, Forbes).

One need only consider The Hyundai Corporation, founded in South Korea and its dramatic shift to American design and manufacturing to see the positive impact of insourcing. After constructing design, testing, engineering, manufacturing and headquarter facilities in three American states, Hyundai created over forty three thousand jobs in the states of Alabama, California, and Michigan.

How does one examine these two drastically different situations and determine the causes that led to the success of one venture, and the utter failure of another?

Though fundamentally both Hyundai and Boeing share many characteristics, there are several key differences which contributed to these drastically different results. Both are high tech companies, which design and produce complex machinery containing mechanical, computer, and electronic components that are vital to transportation infrastructure. Boeing outsourced much of its manufacturing process, however, with little or no oversight over the various contract agencies. This resulted in cost and quality issues caused from the use of counterfeit products or components, or from poor coordination of component suppliers and manufactures. The result was a complete redesign of the aircraft sub-assembly processes, as well as the implementation of innovative, yet untested technologies, (Steve Denning, Forbes).

Hyundai differs in that it maintains strict control of its entire design, manufacturing, and assembly process. Rather than merely offshore and outsource its design and manufacturing process, it created a new subsidiary which handles all processes on behalf of the parent corporation.

The risks and disadvantages of outsourcing vary, but many are well known. No social media blog, or post is free from some nightmare story of horrible customer service, and the very notion of outsourced customer service has become so cliché as to enter popular culture in the form of memes, comics, and comedy shows.

One distinct disadvantage to outsourcing, particularly offshoring, is the false notion that it saves labor costs. While initially, offshoring provided a means of paying lower labor wages in foreign countries, these wages were often still greater than the standard wages workers in these areas receive in standard pay. In those cases that the wages did not exceed standard levels, the offshoring still created a greater supply of jobs in economically disadvantaged areas, which resulted in economic growth for the workers. Simple economics have proven that a prosperous workforce creates a higher salary cap, and as a result, labor costs in countries throughout the globe have risen. A 2004 study by the University of South Florida found that the cost of skilled laborers in India rose an approximate 15% yearly, (Cynthia Myers, Chron). When factoring these rising labor costs, present throughout the globe, with other costs such as freight shipping and political instability, the attractiveness of offshoring declines greatly, (Lewis Humphries, Investopedia).

Labor and shipping costs or global political instability notwithstanding, there are other factors that may create negative impact on any company engaging in outsourcing. As evidenced by Boeing’s poor planning for the 787, companies outsourcing key components of their industry experience a lack of control over those components, whether it be manufacturing, supply or customer support.

“A company's control over its operations differs if it uses outsourcing or insourcing. Companies that outsource a manufacturing process or a service often have little to no managerial control over the way in which the outside company operates. For instance, a company known for its friendly customer service cannot typically enforce its way of doing business on an outside customer support center. Companies that insource a manufacturing process or a service have complete control over its operations and employees,” (Aaron Marquis, Chron). No company has a guarantee of standards, nor will experience the same “buy-in” from an outsourced or contracted employee as they experience from a fully vested permanent employee. Simply put, there is no reason for the temporary, contract, or outsourced employee to care as much for the business as the employee who has worked for the company any number of years. This lack of company buy-in creates a situation in which the outsourced worker does not see the possibility of reward or consequence for their actions.

Because of this lack of control, another risk outsourcing companies face is data security. Lower regulation standards with outsource providers, particularly offshore means that business data is at risk of compromise. A lack of proper controls and inspection by the contracting company, enforcing standards as part of the contractual agreement, will result in data loss, breach or other targeted attacks directly affecting the business. “Service providers have often been the weakest link in a company’s security and will need to find better ways to address that concern,” stated Roy Parker to CIO Online (Stephanie Overby). In fact, contractors have been the center stage of several high profile security incidents affecting both the U.S. Federal Government, and large retail chains such as Target. This has resulted in the net loss of millions of dollars of revenue, or in the case of the government, risk of clandestine operations and methodologies through exposure to potential enemy nations.

Possible conflicts of interest is another concern of outsourcing, whether foreign or domestically. The biblical quote “No one can serve two masters,” (Matthew 6:24), applies equally to outsourcing. Companies may run into conflict of interest issues if the outsource provider contracts with competing agencies, or if the outsource provider is part of a larger conglomerate. Examples of conflicts of interest abound, such as the case of accounting firm Deloitte. Deloitte agreed to pay a fine of over one million dollars because of a business relationship its consulting affiliate maintained with parties serving on boards or committees it audits. While not necessarily a case of malfeasance, it clearly illustrates a lack of coordination, accountability, and control. These are root causes in several high profile events in recent corporate history, which helped to contribute to the Great Recession.

All of these preceding factors result in a tarnished company image. Whether the result of legal entanglements, failed product delivery schedules, higher costs associated with poor management, or a loss of confidential data, the company image suffers as a result. Customers will become dissatisfied, investors will become less trusting, and businesses will lose money as a result. Nowhere is this more evident than the recent trend of “cutting the cord,” where record numbers of traditional cable customers opt for Internet only plans and streaming video content such as that provided by Netflix. Not a large number at first, but increasing numbers of cord cutters may explain efforts by cable companies to provide bundles, limit the amount of Internet data a person may use per month, or throttle speeds of certain applications.

As companies face the challenges of outsourcing, and learn from the consequences of poor oversight and implementation, insourcing becomes an attractive alternative.

Several key influencers contribute to the adoption of insourcing, or reversing course on outsourcing and returning formerly outsourced tasks to company stewardship. While increased data security, and the several high profile data security incidents are a contributing factor, it is not alone.

Labor costs in particular become less of a concern in a global, information-based economy. Collaboration, oversight, and communication is easier now, thanks to the prevalence of mobile Internet devices, smartphones, Cloud Computing, and other technologies or devices that constitute the “Internet of Things.” Vendor management, material sourcing, supply chain management, and design are all within the grasp of even the smallest business, as the complex infrastructure needed to support them moved from the physical space, into The Cloud, or have shrunk in both power requirements and physical dimensions, so that they are less a burden.

Higher exports have also contributed to the rise of insourcing in recent years. The Global Economy demands goods from every corner of the Earth. Just as American suburban families are experiencing new foods and interacting with cultures other than their own, so too are American goods reaching new customers throughout the world. Though Hyundai is listed as the example earlier, it is not the only foreign automobile manufacturer in the United States. Toyota, Honda, BMW and Volkswagen all have manufacturing centers in the United States. All of these companies used a form of insourcing to increase their productivity. One cannot call their employees outsourced, or contractors. These employees work for the company and contributed to their productivity for many years. While one may not see a Ford Explorer on the streets of Berlin, one will see a BMW or Volkswagen. Where these vehicles assembled in the United States, or elsewhere? Were all of the components from the same factory? At some point, everything is exported.

There are risks associated with insourcing, however. Formerly outsourced tasks, or newly created insourced tasks, create employee overhead. Law in the United States regulates employee benefits such as insurance and overtime, while other benefits strive to create a competitive marketplace for employers. This will require considerable effort on the parts of payroll, human resources, and accounting to meet new requirements or new employee staffing numbers. In addition, the infrastructure required to support these efforts is a consideration. Companies now insourcing their customer service lines, as an example, must invest in appropriate equipment and facilities to accommodate increased call volume, while companies formerly outsourcing their human resources must ensure their newly formed HR department understands labor laws as they apply throughout their company, in every location. Everything from telephones, to printer paper, and the building the new employees work represents a potential additional cost.

Buy-in from all parties is essential, and may be a barrier to insourcing. Teams or individuals assuming new responsibilities, or assuming additional responsibilities, will require additional attention. Requiring additional effort from teams or individuals, with no consideration of a reward or this extra effort is a formula for failure. Additionally, parties, officers or other individuals within the company may have critical influence on the success or failure of any insourcing or outsourcing effort. Regardless of the direction, in or out, of the flow of work, one must take into consideration the opinions, input, and requirements of all concerned employees, or the effort will fail.

However, these risks if properly managed do not outweigh the potential benefits. For every disadvantaged listed in outsourcing, a properly managed insourcing effort experiences the exact opposite.

Vested employees feel empowered and know their actions affect the success of the company. Company success may create a better reward system for the employees, and thus they are happier. In every industry in the world, all know that those who enjoy their work or efforts are more productive than those who are unhappy. An unhappy employee does not care if their work production falls short, but a happy employee is motivated to excel and exceed.

Data security is less of a concern, though surely never one that goes away, in a company in which all of its customer and operations data consolidates under one organization. This consolidation results in the streamlining and cohesion of standards appropriate to the company’s standards of satisfaction and operations. Attackers pick the avenue of least resistance, so if the company adheres to industry best practices and standards, they are safer than the company who distributes their data among one or more outsourced companies, each with their own standards and practices.

The economic boon to the national and local economy is a strong motivator, as companies may experience benefits in the form of tax breaks or may exert some influence on the political scene (though it is noted that this is not without its own risks and potential disadvantages as well). “Bringing jobs back” is a strong positive statement, and may result a better positive public image as companies focus on local hiring initiatives or participate in programs such as Vocational Rehabilitation, which creates value for the companies hiring Veterans.

Yet one unrealized potential benefit of insourcing is turning that expertise and service outward, in which the insourced team now becomes a source of revenue for the company. In addition to adding value and contributing to a positive public image, these newly hired or vested employees create a potential source of income in the form of new customers, particularly if the company that employees them creates a good or service they demand. Still, business should consider that a properly trained, equipped and experienced support network, or other insourced business unit, might turn their expertise outward. In this case, the company itself becomes an outsource provider.

Redirecting an insourced business unit to provide outsource services is difficult, and not without risk. The first consideration all companies must consider is the type of service the business unit is able to provide, followed by the customer base. In some cases, outsourcing the business unit is simply impractical, such as those providing human resources services to their companies. Learning the policies and procedures of the contracting company, coupled with the laws, rules, and regulations of any state or nation the company operates within, is simply a task too complicated to tackle for all but the largest of companies. However, one possible alternative, which lends itself well to the outsource model, is customer support.

Customer support, IT support, and Logistics support represent the strongest contenders for any company seeking to provide outsource services to customers, and demand the greatest fees because of their specialized skillsets. Any company may realize unexpected revenue streams by outsourcing their support units to sister companies or affiliates owned by a parent organization, such as the Mazda brand, owned by Ford Motor Company. In this case, some products are identical, and just have a different marking on the vehicle. Other potential customers include the company’s supply chain, who undoubtedly has other customers, and distributors or level one customers buying the company’s product or service direct. Non-competing companies operating within the same industry may be a potential customer as well, but those create new risks.

As stated previously, the risks of turning an insourced business unit into an outsource provider are many, and identical to the risks one assumes if they outsource a service. The risk of conflict of interest, assuming the increased employee overhead, and the responsibility for the contracting company’s data present special considerations. Companies seeking to enter the outsourcing marketplace must realize that the company reputation will both precede and follow from contract to contract. Outsourcing is a service, and the customers are very particular. No company will engage the outsource provider without some expectation of return on their investment, and the provider must follow through, striving to adhere to quality standards above the contracting company’s expectation.

Perhaps the best way to avoid these potential pitfalls, is to separate the outsource business from the traditional revenue streams, possibly forming it as a separate company. Though this may create additional costs, it very likely will prevent issues arising from conflict of interest, and over-reliance of its revenue and contributions to the company bottom line. As outsourcing contracts are fluid, becoming reliant on the income it generates to operate a larger business is poor planning.

The most important consideration, when planning to provide outsourcing, is whether the company is ready to engage in it. The proper planning of this, as with all efforts, will prevent larger issues from occurring.

Of this, the level of competency and trustworthiness of the employees who will be the ones providing the service is the ultimate consideration. Forming a cadre of core employees, who are able to train, guide, and ultimately lead newer members of the team will result in a greater chance of success. Conversely, a mass hiring, followed by rapid implantation of the outsource provider model is a formula for disaster. Companies who have outsourced key components of their business, and found that outsourcing does not meet their requirements, are more likely to tailor their offered service to a higher standard. In any undertaking, leadership has in mind what they desire, and what is less desirable due to personal preference and experience. Interactions with previous outsource providers will provide examples of best and worst practices, and incorporated into company’s policy and service offerings.

Realizing that insourcing may create unexpected revenue streams, or adds value in unexpected ways is the first step necessary, however. Companies and related stakeholders must realize the benefits of adding insourcing to their company’s repertoire outweigh the risks and disadvantages created by it. Adding jobs, building or reactivating infrastructure, and training employees for new tasks creates challenges, yet opens doors. A properly trained and equipped staff creates an asset to any company, despite their task and direction.

In summary, this paper has examined the differences between outsourcing, offshoring, and insourcing, while discussing key advantages, risks, disadvantages and rewards of each. It has provided examples of outsourcing and insourcing, showing how two similar companies have benefitted, or not, resulting from their decision.

When approached properly, outsourcing may be a means for a business to save money while it focuses on key aspects of its operations. Freeing resources to concentrate on the design and distribution of products, while outsourced factories domestically and in foreign nations manufacture goods is in wide use today, and a practice that will not disappear, but expand drastically in the future. Yet the contracting company must pay close attention to the standards, practices, operations, in in many cases, the supply chain of the outsource provider. Issues with quality control, customer satisfaction, improper integration or part compatibility, use of inferior materials, or mishandling of data will result in lower customer satisfaction, a breach of trust, and an increase of costs required, that are necessary to correct these issues. Ultimately, the cost of outsourcing, if improperly managed, will outweigh the savings sought by the contracting company, and result in poor economic performance. Outsourcing will not disappear, so it is important to manage it properly.

Insourcing, however, is the current trend of business, particularly in the United States. Though insourcing carries its own risks and challenges, properly managed it becomes a key factor in the success of business. Properly vested employees, happy with their work and circumstances, will contribute to the bottom line of any company through increased productivity and as possible customers. In addition, local, state, and federal government may provide additional cost savings or incentives to businesses choosing to bring jobs to their local areas. Finally, the positive public image and goodwill of insourcing provides a form of free advertisement to these companies, keeping the brand in the forefront of consumer minds.

The final, and often un-realized, benefit of insourcing is creating an unexpected revenue stream. This paper discussed the pitfalls and risks of turning the now insourced business unit into an outsource provider, and examine the challenges of getting started. Business seeking to enter the outsource market, whether through an newly created unit, or by turning their own resources outward, must realize the mistakes of the past and of other companies, and avoid recreating them.

The final summary of this paper is that neither outsourcing, nor insourcing is a cure all for businesses, nor does it represent a detriment to economies. Though offshoring has negative connotations, globally it is responsible for raising the standards of living for persons in foreign nations, creating jobs, and therefore a demand for goods that will result in increased profits for businesses providing them. Properly managed outsourced and insourced business efforts will generate income for companies in unexpected ways, but the companies providing or demanding these services must not do so blindly.

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