INST0031
Systems Management

Lecture 9

IT Outsourcing

Outline

- What is IT Outsourcing?
- Different Sourcing Models
- Arguments in Favour of Outsourcing
- Arguments Against Outsourcing
- Measuring Performance

What is IT Outsourcing?

- As complexity and change in IT increase perhaps it is only natural that organizations seek to contract out key IT services to those with specialist technical and professional skills.

Different Sourcing Models

1. Facilities Management
2. Selective Outsourcing
3. Tactical Outsourcing
4. Strategic Sourcing
5. Transformational Outsourcing
6. Transitional Outsourcing
7. Business Process Outsourcing
8. Joint Ventures
9. Benefit-based Relationships
10. Insourcing
11. Offshore Outsourcing

Facilities Management

- Business owns the computer assets but hires an external service provider to run the computer operations either at the customer's premises or elsewhere.
- Example:
  - BT awarded a $40 million managed services deal to Unisys to run and maintain its growing consumer voicemail service.

Selective Outsourcing

- Selectively outsource IT functions.
- The IT services most commonly outsourced are infrastructure management and support.
- It is flexible and leaves sufficient IT capability within the customer organization
- Allows to adapt to changes and new technological innovations and advances.
- Can prove more expensive than a more comprehensive outsourcing model.
- Example:
  - HSBC and GT Nexus partner to offer digital supply chain platform
  - WARDY IT Solutions and Linchpin People helps Media Radar focus on strengthening their competitive edge

Tactical Outsourcing

- A rapid and often short-term solution to a particular need or problem, such as:
  - Website design
  - Infrastructure upgrade
  - Specific applications
- Examples:
  - Archstone-Smith Trust, outsourced a revenue management application
  - The application requires a Unix host with an Oracle database on the back end
  - For other internal systems company uses Windows NT and SQL Server.

Strategic Sourcing

- Puts decisions about what to outsource, how and when, into a wider business context.
- Aim to achieve a significant improvement in business performance rather than a short-term targets.
- This approach is commonly referred to as a partnership.
- Examples:
  - UK mapping agency, Ordnance Survey, outsource to Siemens Business Service

Transformational Outsourcing

- Combines the outsourcing of an IT department with a comprehensive reorganization.
- To transform business processes and the technology infrastructure to reduce costs, improve services and empower employees.
- Example:
- TalkTalk awards five year transformational outsourcing contract to CGI (2018)

Transitional Outsourcing

- To introduce major change such as moving from one technological platform to another.
- Here there would be three phases:
  - 1. Management of the legacy systems;
  - 2. Transition to the new technology; \
  - 3. Operation and management of the new platform.
- Any or all of these phases may be outsourced.
- Example:
  - CSC(Computer Sciences Corp) Signs Major Five-Year IT Services Contract Extension With UTC(United Technologies Corp)

Business Process Outsourcing(BPO)

- Organizations are looking to bring in specialist service companies to manage entire business processes.
- BPO deals are not limited to IT.
- The entire function, assets and staff are transferred to the external service provider.
- Commonly outsourced functions include hotlines, help desks, call centres, document processing and storage, payroll and internal auditing.
- Example:
  - Lloyds TSB signed a 7-year, multi-million pound deal with BT Ignite to provide a range of services spanning all areas of the business including Internet banking, key financial services and service delivery.
  - CSC outsourced its UK hiring and running of contractors to a third party, Harvey Nash.

Joint Ventures

- To set up a separate joint venture organization with an external service provider to gain access to technical skills and resources without transferring staff and losing control over the new IT organization.
- Example:
  - CSC and HCL Form Joint Venture to Deliver Digital Software and Services to Global Banking Clients (July 2015)

Benefit-based Relationships

- Both parties making an up-front investment in the relationship and sharing the benefits as they accrue.
- If the benefits previously forecast and agreed do not materialize the supplier may not be guaranteed any recompense for their effort or input.
- Example:
  - The UK government's Employment Service formed a Public Private Partnership with EDS to deliver IT services through a network of 1,000 job centres and 35,000 staff.

Insourcing

- Most companies retain some IT activities inhouse, may invite their own IT department to submit proposals for quality and efficiency improvements.
- These may prove more attractive than any bids received from an external service provider.
- Example:
  - Insurance group AXA rejected outsourcing and cut technology costs by 6 per cent by consolidating its IT operations using the in- house IT department.

Offshore Outsourcing

- Remote sourcing has been growing rapidly and the market is now maturing.

Arguments in Favour of Outsourcing

- Enabling the Organization to Focus on Its Core Business
- New Business Development
- Assisting Major Reorganizations
- Quality and Service Improvements
- Access to Technical Expertise
- Financial Advantages
- Flexibility and Control

Focus on its Core Business

- IT operations consume a lot of resources and management attention but do not help distinguish a company from its competitors.
- Outsourcing helps change the emphasis from operations and problem solving to thinking about how IT can be used most profitably.
- The focus is on interpreting information and exploiting IT systems rather than data processing and maintenance work.
- Organisations can focus on:
  - What do we do best? – How can we do it better?
  - What distinguishes us from our competitors?
  - What value do our customers derive from our products and services?
  - What competitive advantage could outsourcing provide?

New Business Development

- Companies need to continually develop if they are to survive.
- Outsourcing can help in two ways:
  - By freeing up resources, outsourcing helps organizations to focus on strategic new developments.
  - Outsourcing can be used selectively to introduce new technology or applications.

Assisting Major Reorganization

- Makes the inevitable reorganisations smooth and quick transitions.
- Helps with company mergers, acquisitions and divestments.
- IT professionals can benefit too, as service providers can generally offer a wider range of alternative opportunities.

Quality and Service Improvements

- Outsourcing is done in anticipation to get a world-class service.
- It is vital to critically examine service level requirements.
- Both company and service provider to understand what is and what is not acceptable.
- A track record of achievements in other organizations.

Access to Technical Expertise

- IT is the outsourcing suppliers core business.
- Potential advantages:
  - 1. New technology, tools and techniques. more structured methodologies, procedures and documentation
  - 2. IT professionals with a wider span of technical knowledge and experience. Better cost estimation of new solutions.
  - 3. Better negotiation skills with multiple suppliers and can use volume purchasing agreements.
  - 4. Better IT career opportunities for those who transfer to the IT service provider.
  - 5. Can be used for implementation of leading edge technology to help minimize losses if the technology fails to take off.
  - 6. Enables an organization to use obsolete technology beyond its normal life span.
  - 7. Avoids high costs of continually re-training in-house IT professionals in the latest technologies.

Financial Advantages

- The financial advantages of outsourcing fall into three categories:
  - 1. Cost reduction:
    - Economy of scale
    - Spreading research and training costs
    - Technical expertise as and when
    - One-off purchase of IT assets
  - 2. Predictable costs:
    - Specific service level
  - 3. Capital expenditure reduction:
    - Reduce the need to invest capital funds in IT functions
    - contract them as an operational expense (variable cost)

Flexibility and Control

- Flexibility and ability to quickly and efficiently change the development and maintenance need.
- Better defined accountability in contractual obligations makes it easier to react to external resource's poor performance.

Arguments Against Outsourcing

- 1. Negative Impact on Business Strategy
- 2. Escalating Costs as Business Changes
- 3. Loss of Flexibility and Control
- 4. Service Provider Concerns
- 5. Demotivated IT Professionals
- 6. Loss of Technical Expertise
- 7. Security and Confidentiality Risks

Negative Impact on Business Strategy

- Outsourcing is unwise where an application or process gives an organization strategic or competitive advantage.
- Other reasons why outsourcing should not be used for projects or operations of strategic importance to the organization include:
  - The business benefits of outsourcing are difficult to quantify analytically.
  - Outsourcing is rarely appropriate for applications or processes that directly interact on a personal level with customers.
  - The outsourcing supplier may not be able to keep pace with increasing market demand.
  - The introduction of outsourcing may have drastic and unforeseen effects on the business.

Escalating Costs as Business Changes

- 5- 10 years agreements
- Major business changes
  - Customer needs
  - Technology developments
  - Political or legislative change
- New and changed requirements can easily lead to escalating costs.

Loss of Flexibility and Control

- New services and changed requirements have to be negotiated and agreed with the IT service provider. There is no guarantee that its needs and priorities will be recognized and adopted by the supplier.
- In case of unacceptable services, provider maybe penalised but the business risk remains with the organization.

Service Provider Concerns

- Organizations can become heavily dependent on their IT service provider and this presents various risks:
  - The supplier may become financially unstable or even go bankrupt. Another company with a different and unwelcome approach to the outsourced service may acquire the service provider.
  - There may be a lack of responsiveness, possibly as the supplier loses interest (or wins more lucrative outsourcing deals).
  - Service levels may fall to unacceptable levels as a result of internal problems within the service provider.

Demotivated IP Professionals

- A loss of talent and expertise within the organization.
- A threat and a vote of no confidence in the IT services.
- IT professionals may feel betrayed or unappreciated.
- Lengthy process of outsourcing creates uncertainty
- Uncertainty about future can be the most demoralizing and demotivating factor

Loss of Technical Expertise

- No longer employs the specialists, therefore it is difficult to:
  - Monitor the service provider use of technology
  - Develop IT strategy for the organisation
  - Assess the supplier being economical
- The loss of technical expertise through outsourcing can leave an organization vulnerable to poor service and inflated prices.

Security and Confidentiality Risks

- The increased potential for misuse of confidential information.
- Increased difficulties in protecting other people's confidentiality.
- Loss of control over physical and electronic security especially if the supplier transfers processing to a new site.

Measuring Performance

- It has been said that if you cannot measure an activity, you cannot control it and if you cannot control it, you cannot manage it. Without dependable measurements, intelligent decisions cannot be made.

A good performance measurement system

- Reflect your organization's overall business objectives;
- Contain a balanced mix of financial and non-financial measures;
- Collect performance data frequently enough for timely action to be taken to resolve issues and problems;
- Encourage your supplier to provide the outsourced services your organization needs;
- Help you predict what standard the outsourced services will reach in the future as well as enable you to understand what has happened in the past.

Outsourcing performance measures help to:

- Improve communication
- Assess the overall health of the outsourcing relationship
- Stimulate learning by sharing best practice

The measures should cover:

- Cost and benefits obtained
- Service volumes
- Service quality
- Service security and audits
- Service delivery improvements
- Added value and innovation
- Strength and responsiveness of your outsourcing relationship.

Questions?

OK…

Take a break!