Case 7: Petrochemical Spin Off (I of II)

Booz Allen – ITG, Round 1

Problem statement narrative

A commodity petrochemical division has spun off from a major oil company. The new company called ITG group of BAH to look into IT issues and suggest ways to optimize IT expenses.

- Initial Facts
  - The parent company has $300 B in Sales whereas the new company has $30B in Sales.
  - There is tremendous cost pressure on all areas of operations in the new company.
  - The parent company has an ERP system. The maintenance of the ERP system is outsourced to a US based company.
  - The new company will also need an ERP system.
- Problem Statement
  - To the new company, what are the IT issues to separate the ERP system from the parent company? How would you approach these issues.

Guidance for interviewer and information provided upon request

Candidate should identify core issues including the following:

- Vendor management
- Accounting
- Migration issues
- Cost

Information given upon request:

- The existing vendor has scale advantage. It has maintained the ERP system for a long time and is therefore Subject Matter Expert (SME). It is very capable of handling the complexity of the system.
- The IT expenditure of the new company is $10M. The IT expenditure of the parent company before spin off is $65M.

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Interviewer Guide
Ask candidate to interpret the IT expenditure/Sales ratio (a way to measure the efficiency of IT expenditure). The parent company before spin off: IT Expd./Sales = \$65M/\$300B = 0.0216%; The new company: IT Expd./Sales = \$10M/\$30B = 0.033%. The industry Benchmark is around 0.02-0.025%. Therefore, the IT expenditure of the new company is not efficient. Ask: what are the ways to increase the IT expenditure efficiency? Guide candidate towards considering off shore vendors to reduce IT cost.

Cost savings of using offshore vendor	The cost of offshore vendor is 50% less than that of US vendor. However, the productivity of US vendor is 20% more than that of offshore vendor. Therefore, the overall cost savings through off shoring would be 37.5% (50/80=?/100) The new IT expenditure/Sales ratio: \$6.25M/\$30B = 20.83333%.
Risks and strategic consideratio ns	Risks: issues of managing offshore vendors – learning curve, cultural conflict, change management, application support, etc. •Though off shoring might not be an immediate option, the client can use the fact that using offshore vendors will save 37.5% to negotiate better terms with the existing vendor. •The client could use a mix of offshore and US vendors depending on system criticality and comfort level of users. (this is what the client ended up doing.)