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Suggestions for Effective Outsourcing

An Interactive Qualifying Project Report
submitted to the Faculty of
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by

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Introduction

In the 21st century, American businesses have sought new ways of solving old problems. The effect of globalization and the opening of new markets have caused a previously defined course of action for cost reduction to become obsolete. As new markets have developed, the goals of Outsourcing, and its cousin, Offshoring has had to change and adapt to the modern world of business.

Multiple definitions of outsourcing and offshoring exist, and during the team's research the following definitions were used: Outsourcing will be defined as the delegation of non-core operations or jobs from internal production (services or goods) within a business to an external entity that specializes in that operation. Offshoring is defined as transferring operations to another country, typically overseas. Offshoring is similar to outsourcing when companies hire overseas subcontractors, but differs as companies transfer work to the same company in another country.

Popular countries for outsourcing and offshoring activities include Canada, China, Eastern Europe, India, Israel, Ireland, Pakistan, Philippines, and also the Caribbean. Many companies have received significant negative publicity for their decisions to outsource, most notably AT&T Wireless and Dell, for their use of non-US labor for customer service and technical support. However "McKinsey Global Institute has estimated that for every dollar spent on outsourcing to India, the United States reaps between $1.12 and $1.14 in benefits".[1] More research is needed to determine if US companies are truly increasing value to shareholders and the general public.

The desire to improve operations and equity is the driving force behind the modern economic system. In particular, using these foreign providers provides several

benefits which include: reduce operational costs, improve service levels, be free to focus on core business, gain access to specialist information technology (IT) skills, improve ability to respond to business change, and reduce risk are a few. However many doubt these improvements and a number of critics view the "benefits" not as benign, but see them as causing great damage to our national economy and pride.

Ideally companies would be able to produce goods and services domestically, but trying to balance cost reduction, quality of service and jobs for the domestic public is very difficult. Additionally, companies have a hard time realizing their goals, which if it is a US company means benefits to Americans, without outside interference. There are many problems stemming from the current situation, and public dissent is readily apparent.

A Zogby International poll reports that 71% of American voters believe that "outsourcing jobs overseas" hurts the economy and another 62% believe that the US government should impose some legislative action against companies that transfer domestic jobs overseas, possibly in the form of increased taxes on companies that outsource. This poll of over 1,000 Americans was conducted in August 2004.[2] Public opinion is not the only obstacle that stands in the way of US companies seeking to outsource operations. Security is also a major concern for companies, in April of 2005, a high-profile case involving the theft of $300,000 from four Citibank customers occurred when Indian call center workers in Pune, India, acquired the passwords to customer accounts and transferred the money to their own accounts opened under fictitious names. Citibank did not find out about the problem until the American customers noticed discrepancies with their accounts and notified the bank.[3]

Problem Statement

This IQP looked at the process with which companies decided to outsource and to whom, and through this the team saw the strict guidelines and objectives companies used to ensure proper conduct while maintaining the stakeholder's goals. The team found out what companies that choose to outsource rely on to ensure that they achieve their goals without mismanagement. Outsourcing is now an important part of organizational life. Current estimates of the world-wide scale of outsourcing range from $300 billion to $1 trillion. The market for IT outsourcing is smaller but significant.[4] Outsourcing is evolving from being a solution to a shortage of a resource to having a fundamental influence on the business models of many organizations. Companies seeking to outsource need to apply the same business model, meaning they should seek a long term, results orientated relationship with an external service provider for activities traditionally performed, or capable of being performed, within the organization and maintaining a degree of management control over the supply of the service and in risk taking.

Currently, there are no set guidelines for companies seeking to outsource. There is substantial risk associated with outsourcing. Questions that were investigated were: what process do managers utilize when deciding what functions should be outsourced? What are the Criteria for selection of vendors? After organizations outsourced, did they realize all of their anticipated gains? What problems did they encounter? What types of companies are most likely to benefit from outsourcing? How likely are companies to participate in outsourcing activities again? What organizational structures are arising that aim to protect the stockholder's interests, and therefore the public? As the outsourcing

market continues to grow these questions needed to investigated to provide a proper guideline for outsourcing.

Many companies are encountering severe losses from a lack of management control, and, even worse, some are experiencing backlashes due to miscommunication especially ambiguous contracts. When outsource contracts are signed, the press reports expected outcomes, including reduced IT costs, better service, access to new technology, and an ability to refocus in-house staff on higher-vale work, but there is substantial debate about the long-term consequences of such deals. There is no documentation of the proper method for initiation of an outsourcing process. The team has reached a more definitive answer in conducting research in many different areas.

Methodology

Brief Overview of Methods

1) Literature Review: Gained knowledge on the topic.

2) Developed questionnaire that will develop mindset behind outsourcing.

3) Interviewed professionals with experience in outsourcing.

4) Transcribed the recorded interviews.

5) Analyzed Interviews.

Interview Questionnaire

1. What is your **most important strategic reason** for outsourcing?
   - That is, what are (or have been) the **drivers/triggers** for outsourcing?
   - Was there a specific **event** that led you to outsource (e.g., budget problems or management edict, etc.)?
2. What **process** do you go through before deciding to outsource?
   - Do you conduct an analysis (quantitative and qualitative) to determine whether to outsource?
   - How do you **identify your needs**?
   - How is the **decision made**?
3. What **criteria** do you use to evaluate what services, functions or products will be outsourced?
   - What services, functions (e.g., back office functions, business processes, IT functions –software development) or products (e.g., automobile industry) will be considered for outsourcing? Why?
   - What services, functions or products will **not** be considered for outsourcing? Why?
4. What criteria do you use to select an outsourcing provider?
   - What process do you utilize to analyze the ability of different providers? Do you ask for bids from different providers?
     Do you ask for references from other clients that the top three providers have already provided outsourcing work for?
     Do you prefer outsourcing to one country over another?
5. Once you have made the decision and have selected an outsourcing provider, were there any structural changes (e.g., manager layoffs, reduction in office space, etc.) that had to be made within the company?
6. Any staff retraining/repositioning?
7. What are the key challenges in working with an offshore partner? Please list the challenges that you see or have experienced after you outsourced?
   - Methodology challenge (i.e., do your methods of conducting business in the U.S. match and/or coordinate with the methods of the offshore partner)?
   - What is the most difficult aspect of outsourcing?
8. Will any of the outsourced services, functions or products be brought back into the company? If so, why? If not, why not?
9. What do you believe are the critical success factors in making outsourcing work effectively?
10. Are there any long-term implications of outsourcing to the U.S. economy?
11. What functions, services, or products benefit the most from outsourcing?

Results
Interview Analysis

Each of the interviewees were chosen because of their involvement and experience with outsourcing and ability to provide appropriate knowledge about the topic.

Richard O'Brien is a sole proprietor professionally known as Nagog Hill Partners whose clients are trying to either manufacture or outsource. He does his best to understand both sides of that issue, put people together, and bring in the right partner at the right time. Because of his experience with many types of companies his outsourcing knowledge and ideas were very helpful.

Mitch Sanders, President of ECI Biotech, is a leader in the field of protein engineering, purification and assay development. ECI Biotech's product pipeline includes a diagnostic sensor for urinary tract infections, as well as advanced wound care systems that provide early warning of emergent infections and promote healing. ECI presently has corporate partnerships with medical device industry leaders.

Dan Richards of Fidelity Investments has worked for many companies, but gave the team his expertise working in the information systems department by giving us a technical focus on outsourcing. The following is each question from the questionnaire with each participants response.

1. **What is your most important strategic reason for outsourcing?**
   - **That is, what are (or have been) the drivers/triggers for outsourcing?**
   - **Was there a specific event that led you to outsource (e.g., budget problems or management edict, etc.)?**

According to Richard O'Brien, the most important strategic reason for outsourcing is the use of money. A company no longer has the burden of many upfront costs because the costs are assumed by the company being outsourced to. Typical upfront costs relieved by outsourcing are hiring workers, establishing facilities, and preparing tooling. The flow of cash in this situation is favorable because they don't have to spend money until they receive the product. By outsourcing a company's strategy is aligned to using money and resources more effectively.

Mitch Sanders, president of ECI Biotech listed his strategic reasons in order of importance to his company. The most important strategic reason for his company to outsource is cost savings. This is followed by human capitol and finally the need for experts in the field. He points out that without the experts in which he chose to outsource to his company would be lost.

Fidelity Investments pin-pointed their most important strategic reason for outsourcing to be IT expenses. Outsourcing some costs enables the company to support new business products, which is an important piece to Fidelity's success.

2. **What process do you go through before deciding to outsource?**

- **Do you conduct an analysis (quantitative and qualitative) to determine whether to outsource?**

- **How do you identify your needs?**

- **How is the decision made?**

In summary, each interviewer indicated that he outsourced chiefly because of costs. According to Richard O'Brien before deciding to outsource a company should perform some sort of make or buy analysis. That is, the company decides what it would cost to do it in-house, and what it may potentially cost outside the company. The

organization must also determine if the skill, experience, and familiarity with the product are there. Quality is a major concern and if the skills and experience aren't available then the company must recognize this in order to make a good decision.

Mitch Sanders uses consultants to help with his decision-making. He brings in experts in order to decrease risk. The big picture also has to be looked at. He believes that you look at what needs to get done, and then you just do it.

Dan Richards uses data from company analyses. From this data his company is able to ascertain whether or not outsourcing is applicable for them. "It is a very in depth process. There is the idea that maybe outsourcing would be useful to our company. We then usually have some people gather data on it. From this date we are usually able to see pretty easily that it would be in our favor to outsource or not."

3. What criteria do you use to evaluate what services, functions or products will be outsourced?

- **What services, functions (e.g., back office functions, business processes, IT functions –software development) or products (e.g., automobile industry) will be considered for outsourcing? Why?**
- **What services, functions or products will not be considered for outsourcing? Why?**

Richard O'Brien says managing outsourcing is critical. Since it is your product you should be in a position to participate in the entire process. This means negotiations, arrangement, and making decisions throughout the process.

Mitch Sanders makes sure the people he is working with are experts, and is very careful about who he works with. "If there is an expert in the field and I already know

them or respect them either through someone I know or what have you then we can start a relationship. If it's somebody new although they may want a full blown consultant agreement, I typically I always go with an hourly rate till I know that the person is worth the money."

Dan Richards states that they try to use the global clock as a resource. Whatever work that doesn't get done during the day gets sent over to a foreign country to be completed by the following day. He believes this is extremely advantageous because twice the amount of work is getting done in one day.

4. **What criteria do you use to select an outsourcing provider?**

   a. **What process do you utilize to analyze the ability of different providers?**

   Do you ask for bids from different providers?

   Do you ask for references from other clients that the top three providers have already provided outsourcing work for?

   Do you prefer outsourcing to one country over another?

Deciding to outsource is the first big decision in the whole outsourcing process, but after this first step, the next most important is who your outsourcing provider will be. To make this decision many options must be weighed. Quality of provider and cost of provider seem to be two of the most important options. ECI Biotech believes that using the best people is a high priority. They know that they are expensive, but they believe that in the long run that it would be more cost effective. They say,

"I would say that you seek the best people in the field and they stand out and are typically busy, and unfortunately some of these people are expensive, others a little more

cost effective, but as I say you always want to kick their tires and make sure they can work with you and it's going to be a meaningful long term relationship. But if they are out to just gouge you which some consultants can do that is why I like them hourly because you can just pay them ten hours and then get rid of them. If they fail to perform or they have a pattern of gouging you for money in just the first couple hours, then there is something wrong there."

Fidelity Investments believes that cost is very important, but their most important topic they are looking for is security. They don't want to have any problems with information getting out to the wrong people. They acknowledge that it is a dog eat dog world, so competition is fierce. They just want to be sure that they are safe with their security. Nagog Hill Partners has two priorities for making this decision. They first want someone who has the resources for success. They want someone to be able to do the job, and do it well with the resources they have. Their next most important quality is expertise. They don't want someone who isn't ready for anything in the job. Someone with experience is usually able to handle whatever their job can throw at them, because of experience. With all of this they still look at culture, and how it would affect them. They want to be sure there aren't any insurmountable problems. Language is probably their biggest difficulty, but if it is important enough, they find a way around it.

5. Once you have made the decision and have selected an outsourcing provider, were there any structural changes (e.g., manager layoffs, reduction in office space, etc.) that had to be made within the company?

When the actual outsourcing process begins, there may be changes to the infrastructure within the company. These changes may take the form of layoffs, closing

of offices, and redistributing resources. ECI Biotech said that they didn't have any infrastructure change. This is surprising because when a company spends money for outsourcing vendors, you usually have to cut spending from different areas. The most affected area is usually personnel. But ECI says that it made them faster, because they had consultants which made the transition more efficient. Fidelity Investments has a similar stance as ECI Biotech. They say that if the company plan well, then you shouldn't be decreasing your personnel, but will be increasing it. They did have to change a few jobs in the time frame that they worked. They had to change this because of the off shoring partners different time zone. To work with them when they were working they had to change their hours of work. They also changed jobs to have extended periods of work in their offshore partner's country.

Nagog Hill Partners says that how it is managed determines everything. "It depends on how it is managed. It doesn't have to end up in lay-offs. If it's done well those people can end up doing other things than being laid off." It also can't be managed in the short term. They say that it isn't responsible to be looking for the short term benefits, without looking at the long term benefits also. They also say that layoffs don't usually happen because of outsourcing. They say that it is because of the tendency to "…hire people to do things that may not be essential…" If companies just controlled their hiring practices and only hired for what they need, then they would be fine.

In Dan Richard's department they have not laid off anyone; instead they actually add members to the staff. The only change that takes place is training on how to do global business. If outsourcing works out then that in turn makes the company grow.

6. Any staff retraining/repositioning?

With changes to infrastructure, there may need to be some form of staff retraining and repositioning. ECI Biotech didn't have any form of retraining or repositioning. They said, "We pretty much hire what we need." Because of this there really isn't a problem with adjusting to changes in the company. When people are needed, they are hired, and it is that simple.

Fidelity investment says that there was a fair amount of retraining for personnel. "Project managers need to train people in different situations-how to manage globally. They take part in certification courses. A number of my staff went through that. Also, cultural training. Our instances have been mostly positive." The retraining mostly takes into account the differences in outsourcing to another country, mainly culture.

Nagog Hill Partners' answer is very similar to Fidelity Investment's answer. They say that there is a large amount of retraining. This is mostly because, not many people know how to work with new outsourcing partners and new cultures. They also retrain people so that they can adjust to the new way the company is doing things. With outsourcing many changes come, so the company wants its employees to understand the company's objectives. "Some companies give classes to their employees and tell them what they are doing and their strategy and suggest ways to take advantage of this approach. This retraining puts them in tune with company strategy."

7. **What are the key challenges in working with an offshore partner? Please list the challenges that you see or have experienced after you outsourced?**

   - **Methodology challenge (i.e., do your methods of conducting business in the U.S. match and/or coordinate with the methods of the offshore partner)?**

- **What is the most difficult aspect of outsourcing?**

There are various challenges in working with offshore partners. Sometimes there is a methodology challenge where methods of conducting business in the U.S. doesn't coordinate with methods of the offshore partner. However, ECI Biotech believes the challenges are becoming increasingly smaller. President Mitch Sanders believes the technology is advancing at such a rapid pace that it connects a company to an outsourcing provider in a relatively easy fashion. He states, "I think in this global economy and with the internet and secure servers and secure socket layers it is much easier to partner with anyone anywhere." ECI Biotech's philosophy for outsourcing is that it can be done for anything and done everywhere because networking to foreign contractors has never been so effortless. He also reminds us that, "We have clients in UK, we work with folks in Florida, California, and other areas of Europe…so the notion of having to be in a major city is long gone."

Along these same lines, Fidelity Investments believes that there will always be a place for the US to outsource and a country that has a structure in place to provide aid to the US. Fidelity believes that whatever country "speaks English and has a good educational system" will be a possible place to outsource. Furthermore, Fidelity believes that a major challenge is finding the lowest price to manufacture a product or conduct a service. The representative refers to this as looking at "the arbitrage or the differential pricing in two places for the same product." A substantial task is researching the seemingly infinite providers that exist overseas.

As stated previously in the Literature Review section, many experts think else wise and believe there is a communication breakdown wherever a company goes because

numerous times the US is going to countries where English is not the primary language. Nagog Hill Partners is an advocate of this opinion. They believe culture and language is a huge barrier because this could lead to confusion and possible finished products having undesirable characteristics. Nagog Hill Partners articulates "that substitution of materials might happen because of less availability or familiarity."

8. **Will any of the outsourced services, functions or products be brought back into the company? If so, why? If not, why not?**

All the companies agreed that after a certain time that it's necessary to bring back a portion of the outsourced services, functions, or products. ECI Biotech supported a theory found in the literature review that the number one reason top management wanted to outsource was for the expertise. Mitch Sanders elaborates more precisely that "outsourcing expertise is needed much more crucial in the beginning stages and after a considerable amount of time and after learning the business it's sensible to do it yourself." He also tells of his own experience that "there has been certain expertise that we outsource that eventually we found a person who was really good and other examples of that are we had some partners that have great employees and rather than outsource that we chose to hire them right out of the company that they we are working with."

Nagog Hill Partners believes in the same philosophy. They believe that a company has to go through the outsourcing process and then it can decide whether its company is responsible enough to bring affairs internal or not. Most of the time a company reaches a point where bringing back in house is a wise decision because it is fully developed and capable of making their own rational decisions. Richard O'Brien explains hypothetically testifies that if "Company has one large product, outsources it and makes room. They

start three more products now, and now have four items. They decided now that they are a mature enough company to take the 1st mature product in-house."

Fidelity Investments is on the fence and believes it all depends on the situation. Fidelity Investments claimed, "if it ain't broke don't fix it," but also stated that even if a company is producing revenue it could possibly produce more if takes cautionary steps to bring it back in-house.

9. **What do you believe are the critical success factors in making outsourcing work effectively?**

The employers of the companies interviewed once again agreed in their response to the question asked referring to the different critical success factors in making outsourcing work effectively. ECI Biotech, Nagog Hill Partners, and Fidelity Investments all harmonized in their opinion that managing the process and keeping a watchful eye on the services being performed is quite possibly the most sizable factor in outsourcing. Mitch Sanders claimed that the most three important factors were "cost, value, and delivery on time" but these theories need to be expanded to make apparent that the underlining theme in all of these is that close observation must be in place. He recollects in his own situation that "most times that I have been burned from outsourcing I keep them on a very short leash I've only lost five thousand dollars or ten thousand dollars. It's not that I've lost a hundred thousand dollars." This is due to the fact that he understands that companies have to get exactly what they expect or discontinue the service and move on. ECI Biotech has had other instances where outsourcing is used cautiously and has brought value to the organization. He claims that, "getting an expert that knows exactly

what you need but you're only paying them a week over a year and you're not paying for benefits makes a lot of sense."

Nagog Hill Partners also recognizes that managing of the process is vital in running a successful organization. O'Brien voices that "the strategy of using outsourcing needs to be looked at more carefully. A lot of things that are being outsourced don't have to be. They are short term solutions to long term problems." He goes on to contest that it all comes down to supervising the process and making decisions based on prudent thinking. He also touches on the fact that delivery is an essential aspect in outsourcing. If a product or service is done correctly, but ends up being received behind schedule it's a massive problem. O'Brien claims that "being prepared to deliver a product and have it ready for when someone needs it" is a priority that can't be overlooked.

Fidelity Investments acknowledges that controlling what it wants achieved is a daily challenge. Fidelity believes that communication and chemistry have to go hand and hand. Also, another mutual opinion is things getting done on schedule. Fidelity declares that "tasks getting accomplished in a timely manner is a key factor because if something doesn't get done all time it holds up all your other operations."

10. Are there any long-term implications of outsourcing to the U.S. economy?

When the interviewees were asked if there are any long-term implications of outsourcing to the U.S. economy two general views arose. The first viewpoint was outlined in the team's interview with Richard O'Brien of Nagog Hill Partners. His view, held by many, is that the long-term implications of outsourcing activities are the loss of jobs. His emphasis is that job loss is not a product of companies outsourcing but opting "out of responsibility of retaining the value added character of what we do in business. If

Americans want to keep jobs, we need to keep raising the level of education and improve a lot of things that we do." He continues to say that job losses due to outsourcing is not mandatory. He says that the loss of jobs is because "managers are not thinking creatively on how to contain costs, how to be more effective at building and assembling things so that they can create much less expensive products and less costs. It's management's responsibility to understand both its employees and its stockholders and appreciate the difference." However, he adds that this is not a solution to all reasons for outsourcing.

ECI Biotech claimed that Americans can do the same work, but the US needs to keep raising the level of education and managers need to think more creatively and not just outsource when they're a lazy. Time will tell if American workers can raise the bar and become just as valuable as providers.

Fidelity Investments believes there aren't any long term implications on the economy. Economies usually seem to handle and balance themselves out on their own. The economy reacts to whatever is in demand.

11. What functions, services, or products benefit the most from outsourcing?

When asked what functions, services, or products benefit the most from outsourcing all replied that almost any function or product can benefit from outsourcing activities with a few exceptions. These exceptions are generally core-competencies, or have strenuous externalities that make outsourcing ill-advised. One such example suggested by Richard O'Brien of Nagog Hill Partners would be the outsourcing of medical products or drugs. This would be difficult to outsource due to the complicated regulations imposed by the Federal Drug Administration on the development and manufacture of medical devices and drugs. This is problematic to the outsourcing

benefits because of the rigorous testing and inspection required for all medical devices and products sold in the United States and the constant need for approval from FDA officials would constitute a large travel cost that could potentially offset outsourcing cost savings.

Additional products and functions that are not good candidates for outsourcing would be those of national security interests. For instance, the company would not want to outsource nuclear fuel or weapons dismantling to North Korea. Also, countries would not want to depend on a foreign country for conventional arms manufacture because foreign alliances and goals change often and without warning.

The chart below summaries the answers each company gave for each question.

ECI Biotech - Mitch Sanders	Fidelity Investments - Dan Richards	Nagog Hill Partners - Richard O'Brien
1. - Cost savings - Human capital - Experts in the field	- IT expenses - Enables the support of new business products	- Use of money - Smaller burden of upfront costs - Use money and resources more efficiently
2. - Uses consultants - The consultants help decrease risk	- Analysis to see if it is applicable and useful - Decisions are made after discussion and presentation of data (costs vs. savings)	- Make or buy analysis - Quality of skills and experience
3. - Makes sure the people he is working with are experts - Starts people off slowly to see if they are worth the investment	- Sensible decision making - Night support is important - Gets more work done in a day than an eight hour day	- Managing outsourcing is critical - Involvement of every aspect of the process
4. - Use the best people - Feel that in the long run they save more money	- Security is most important - Want to be sure they are safe - Costs is of secondary importance	- Want someone with the resources for success - Expertise, someone who is ready for anything on the job

ECI Biotech - Mitch Sanders	Fidelity Investments - Dan Richards	Nagog Hill Partners - Richard O'Brien
5. - No changes -Used consultants to prevent any structural changes	- Had to change a few aspects of certain positions - Planned well so there were no layoffs	- Changes depend on how you manage everything - Control hiring practices so layoffs aren't necessary
6. - No real changes - They hire what they need - Use consultants	- Fair amount of retraining - Mostly cultural training	- Large amount of retraining - Cultural training and new ways to work with new partners
7. - Challenges are becoming increasingly smaller - Technology makes the world smaller and tasks easier	- Finding the right provider for the lowest cost. - Takes lots of research to find the right provider	- Culture and language are the biggest challenges to face
8. - Expertise is needed more in the beginning of a project - Bring back some services	- Depends on the situation - Believe in the saying "If it ain't broke, don't fix it."	- After maturing and learning they are able to bring back some of the services

ECI Biotech - Mitch Sanders	Fidelity Investments - Dan Richards	Nagog Hill Partners - Richard O'Brien
9. - Cost - Value - Delivery on time - Use outsourcing cautiously	- Communication - Chemistry - On-time task completion	- Supervising the process - Making sound decisions
10. - Unsure - The economy and industry has its ups and downs	- Long-term, the economy usually balances out - Economy is always changing and adapting	- Job loss - Outsourcing isn't entire to blame - Bad management and decision making
11. - Regulatory clinicians, saves lots of money outsourcing them - Use student resources to save money also	- Outsourcing touches all industries - There is no standard template for outsourcin	- Medical field is difficult to outsource

Discussion

Literature Review

Role in the Global Economy

This topic is important because of the large role that outsourcing has taken in the world economy and the businesses that comprise it. Arguments among differing viewpoints are common when it comes to the topic of outsourcing and its positive and negative effects. "Outsourcing remains one the most controversial issues facing American corporations today," says president of TheLadders.com, Marc Cenedella.[1] Research has shown that there is evidence for critics favoring outsourcing as well as those opposed. For example, one study suggests that compared to five or ten years ago there seems to be a lot more approval with the outsourcing process and there has been a substantial trend toward more subcontracting in recent years. However, in a study in the late 1990's, experts agree there were increases in the amounts of outsourcing projects, but state that the level of dissatisfaction in them had been steadily growing.

When individuals were asked about outsourcing generating value, two surveys taken, differed in opinion. In one survey it was reported that nearly two thirds of the respondents believe that they are not receiving good value for what they spend on outsourcing. This number is very different from the same question asked in a 1995 survey where nearly sixty percent answered affirmative to receiving value for the money they put in.[2] Companies looking to begin to outsource are torn between the advantages and limitations it can bring. Information is available to support both sides.

Advantages

The advantages for companies involved in hiring out are cost savings, expertise, and overall improvement of business performance. One research project executed by The Bureau of National Affairs (BNA) provides evidence that the desire for expertise is a driving factor in deciding to outsource. They surveyed more than 940 HR executives and came up with some surprising results. The number one reason top management wanted to outsource was for the expertise. Neither costs nor a desire to achieve a more strategic role most often drives the decision to outsource, the BNA report says. Sixty-nine percent claimed they wished for expertise, followed by improved service quality (44%), and cost savings (28%).[3]

Even though cost savings is high up on the priority list BNA found that evaluation is difficult. Many respondents report difficulty with evaluating the success of outsourcing in terms of cost savings and re-allocation of resources. In reality, these companies said the net cost savings and reallocation of resources were "undetermined" because of the complexity of measuring outsourcing.[4] Along these same lines, the FMLink Group who conducted a survey found that companies are starting to realize the hidden costs and why some of the "undetermined" savings might be misleading. FMLink Group found that the time taken by in-house staff to manage outsourcing contracts is not insignificant, ranging from 13 to 44 hours per month, depending on the type of function being outsourced.[5]

Today a successful business usually excels by reaching its target markets effectively. By setting up on the opposite side of the globe they are able to expand their potential markets and reach additional clients with greater ease. Consumers may also

benefit from these reduced costs to companies. Once the cost savings are completely realized the company can sometimes have the option to sell its products for less.

A writer from TechNewsWorld points out the benefits of outsourcing by looking at the principle of comparative advantage. This principle says that even if the United States enjoys an absolute advantage in producing all goods and services, the benefits of trading with another country are mutual and worth pursuing. This enables the U.S. to focus on some of its strengths such as business creation and product development, which are key parts of outsourcing.[6]

In a recent Accenture survey of more than 800 executives in the US and Europe, 86% said outsourcing gives them more control over business outcomes in a variety of critical areas, the most important being the ability to plan. Executives feel they have more freedom to make discussions because the results come quicker. While cost-cutting is among these key areas, the executives also reported equal levels of control in reliability, cost variability improvements and effective implementation of ideas. Surprisingly 55% of respondents said outsourcing allows their companies to implement strategies and change at a faster and more controlled rate.

As for the overall prevalence of outsourcing, more than 80% of respondents said they are committed to outsourcing at least one business function permanently. Executives feel that instead of putting the burden and extra stress on themselves they can be relieved by an outside provider. Only 14% plan to use outsourcing on a temporary basis to improve key functions and return them in-house once efficiencies are realized.[7]

In most businesses, "time is money" and efficiency is crucial. Sean Walsh, President, Symphony Services' Commercial Software Group, analyzed some data to

conclude that a reason not so obvious to upper management deciding about outsourcing is what he calls "the ramp up factor". A key finding he encountered was that companies don't realize that if they do decide to do a project in-house, it will take a considerably longer time to start up than shipping it somewhere else. He claims an outsourcer can get the center up and running a lot faster, sometimes as much as twelve months sooner.

Another hidden fact Walsh uncovered is that Indian workers, for whatever reason, appear to be more productive than the average American worker. He has observed that Indian workers are 60-75 percent as productive as American workers when they start a project. Initially, he needs ten offshore employees to do the work of seven Americans until they get into the rhythm of the project. He says they typically take six to nine months to achieve productivity parity with their American counterparts. With a good portion of projects not even lasting that long he feels that outsourcing is crucial.[8] Furthermore, investing in new technology is very costly and often risky. As the technology market develops rapidly, it is difficult to keep up with latest innovations and solutions. Thus outsourcing to companies that have the resources, expertise and desire to continuously update their technological solutions, offers a true competitive advantage. Outsourcing streamlines firm operations in ways to cut cycle time, speed decision-making, and reduce coordination costs. Hiring an outside provider allows a company to spend less time on tasks which means it will have more time to focus on core components. With the ability to make quicker decisions, companies have more slack and room for error. Also, eliminating major in-house efforts ultimately makes fixed costs turn into variable costs.

In the U.S. today it is common to hear that India and other such countries are stealing American jobs. But not many people actually take a look at the research and numbers associated with the number of jobs being outsourced, and the number of new jobs being created in the U.S. It is true that the U.S. sends a larger portion of its software development and call center work to India than other countries. But the concern over job loss in the US following outsourcing to India is an exaggeration. Only 274,000 jobs moved to India from 2000 to 2003 compared to the net annual job increase of about 327,000 in the US during the period, consultancy firm McKinsey has said. "The figures so far suggest that the number of jobs transferred to India is tiny relative to employment in the US service sector," it said.[9] Many consider the job loss to outsourcing to be a drop in the bucket compared to that of the U.S. economy. But some wonder why there are declines in the U.S. employment rate. Some say that the post 2000 job decline was following a technology boom, so it is only natural to have a decline. "Since trade and offshoring weren't the primary reasons for the weak post-2000 US employment performance, they shouldn't be the focus of policies to create or restore jobs," it said. However, there was a big loss in the area of technical occupations such as programmers and support personnel, said McKinsey. Outsourcing probably caused 99,090 computer programmer jobs to be sent to India.[10] Researchers from the Information Technology Association of America (ITAA) reported that twice as many jobs as are put out of place will be created a through IT outsourcing in the U.S. This group figured that in the year 2008 there will be 317,000 jobs created due to effective outsourcing. The key fact of lowering business costs is that money is more abundant for paying American workers. The advantages of new jobs are vast, ranging from U.S. economic efficiency to boosts in

exports and raised wages.[11] Another viewpoint is that there is a tradeoff of job loss and gain between certain types of industries. "On one hand, U.S. manufacturing jobs are being lost to overseas competition, yet we're seeing a large amount of job creation in the US at higher levels in industries like advertising, IT and marketing", said Marc Cenedella. (Arrison, 2004)[12] This is insight to a process where lost jobs in one area are made up for with job creation in other areas.

Disadvantages

The first big problem between outsourcing deals, and the reason why so many of them fail or are not satisfactorily completed, is the lack of communication and lack of work from the start to design and set the parameters of the relationship. Executives and vendors see outsourcing from two extremely different philosophies, and don't realize or understand the effects of the others view. The executives expect the outsourcer to act and behave in the same manner as their own people. This is not a rational thought, because the vendor is its own company in a way. To them, they are just doing business with another company. The vendor will do extra work, if asked to do it, but will charge the company for it. The outsourcer, on the other hand, sees itself as providing a set amount of service for a set price. They see extra work as additional service, which requires additional payment. Companies expect that little extra, whereas vendors see everything as part of a contract and nothing more. The problem is that the executives and vendors don't discuss these vast differences in ideas. The problems is ignored and keeps growing as the vendor keeps charging the company more and more, and the company sees the vendor as leeching off the company, trying to make a few extra bucks. This results in many failed relationships and deals. It all has to do with incentives. The company's

workers have incentives in the form of bonuses or raises to put in the extra work, but the vendors have not real incentives to make the company better. Vendors have no incentives to do work they are not getting paid for. Because of this the company believes that the service it receives is sub par, and degrades the relationship even more.

The next issue is the lack of understanding of the specifics of the deal. The proposals made to the executives by the vendors are usually a general description of the expectations of the vendors. A proposal may not be specific of what is going to be done. To make something specific usually takes a large amount of effort and discipline. The people that make and define boundaries of proposals don't want to spend weeks in meetings trying to define the contractual parameters. It isn't worth it to them to spend so much time on a proposal that may not even be implemented. So, the parameters end up being poorly designed and described, and each side has a different idea of what they are responsible for doing. The company executives assume that the vendor will do everything that the people who work for the company do, even if specifications weren't in the outsourcing contract for those jobs. The vendor thinks that it has specifically defined the jobs to do, which wasn't very specific to start with, and is going to get paid for the work done as described in the contract. With these different views it is only a matter of time before the relationship goes sour and both sides end up losing out.[13]

Among the topic of American jobs controversy has arisen with some arguing occasional negative effects. A temporary displacement of jobs can occur when a company begins outsourcing, creating large amounts of job loss. This is not to say though that large economic efficiency occurs. One researcher, Maury Harris, reports "Over the past three years U.S. companies' foreign job outsourcing caused a gross job

loss of just over 400,000 per year." This will eventually even itself out with economic returns, but those who suffer the initial job loss are very against this cycle and their position in it.

A typical problem for companies is the feeling of loss of control since operations are now far away and they heavily rely on a vendor. Complete trust in the vendor is necessary but risky. In general though oversees vendors are honest and minimize risk. It is bad for their business if they aren't, because people won't hire them if they can't meet standards set by companies. Outsourcers are a team of experienced developers who have already proven themselves as an effective unit. In most cases the company outsourced to will always be sure to reach given targets, deliver on time, ensure stringent security and maintain a level of productivity which will keep its business partners for a long time. Outside partners more than not want to show their worth by providing honest work.[14]

"Outsourcing is frequently considered a panacea - a vendor promises that because of their experience, knowledge base, proprietary tools and systems, leverage with its suppliers, etc., they can do what you do better and for less money. Unfortunately, it rarely seems to work out as well as it should. Why?"[15] Salespeople and executives can be problematic. The sales peoples' job is to sell their product. They tell the executives what the executives want to hear in order for the executives to buy the product being sold. Executives like to do big, flashy projects for their company to look good and succeed. Outsourcing is one big way to show that you are doing something to help the company.

However there are some negative effects of outsourcing that are worth mentioning. Experts on the field argue issues of risk such as job loss, communication breakdowns,

data privacy, and poor publicity. The economy as a whole experiences changes and one major focus area is job creation and loss.

Three major issues with vendors were investigated:

- Job Creation

- Culture Difference

- Boomerang Effect

To U.S. workers, foreign companies, such as Wipro, were seen as a threat to their job security; but that is all changing now. All types of companies based in offshoring countries such as India, China, and Taiwan have begun setting up bases in the U.S. and hiring U.S. workers. This is an example of the boomerang affect, where jobs being offshored to other countries are returning to the U.S. for a multitude of reasons. These companies want to be closer to the markets they are selling to so they see that as reason enough to move to the U.S. Also, many U.S. companies are concerned about by the bad publicity and failures offshoring is causing for them. Because of this companies may start creating more U.S. jobs than they are shipping away to other countries. A recent study by economic think tank McKinsey Global Institute has found that every dollar a U.S. company spends on outsourcing results in $1.12 to $1.14 in additional work here. Foreign investment for setting up U.S. subsidiaries and plants doubled, to $82 billion, between 2002 and 2003, according to the Commerce Dept. That translates to 400,000 new jobs in the U.S. Most of these jobs are tech-related, says the Organization for International Investment. Over the same period of time, it is estimated that 300,000 U.S.

jobs have been lost to outsourcing, according to tech consultancy Forrester Research. So

in total, foreign companies have actually resulted in the addition of some 100,000 U.S.

jobs. Foreign companies are also hiring out U.S. workers to work for them overseas.

Such companies are willing to pay top dollar for top talent. Many of the U.S. workers are

usually consultants or specialized workers in the tech industry.

CONCLUSIONS AND RECOMMENDATIONS

This project has provided many answers to the team's questions. From the data gathered from literary sources and interviews with corporate officials, the team has been able to see a trend in the outsourcing decision making process. The big questions are why companies choose to outsource, and what is the method that is undertaken to accomplish the decision to outsource.

Obviously the biggest concerns to companies are profits and expenditures. From this "big picture" view, companies see outsourcing as a cost savings mechanism. The team found that, no matter what the size of the company, their primary reason to outsource was to lower expenditures. This was the primary reason, but from our analysis, the team found other subsidiary reasons. Efficiency was also important. They want to get a bigger bang for their dollar, which means they will get more work and production with less costs in another country than if they did the same in the U.S. Another reason is time savings. By outsourcing, companies are able to give a portion of their labor to the outsourcing provider. This allows them to concentrate their time on other tasks, and in the business world, time is money.

Knowing that a company is going to outsource is a small portion of the big picture. Next companies must decide what tasks are going to be outsourced, and where these tasks will go. Each company has different tasks and work that can be outsourced so it is impossible to say that they all outsource IT or fabrication work. Although, it was found that companies believe in outsourcing work that will cost less elsewhere. They usually start off small, to see if the outsourcing process is actually going to work for them. They

look to see if they are actually saving money, and if they aren't losing any quality of work. If it appears to be going as planned, then they will usually increase the amount outsourced.

Companies look for experts and experienced outsourcing providers. With experience comes an ability to adapt to new situations, which allows for a higher chance of success. Outsourcing providers are also expected to have a certain degree of security to protect their clients' products or interests. It is also interesting to find that companies look for outsourcing providers that are in different time zones. This allows them to double productivity. So when one group is working the other is sleeping and vice versa. This means that instead of an eight hour work day in a normal setting, the company is getting two eight hour work days in one day, or 16 hours of work per day. This increases productivity, which saves money.

When the outsourcing starts to take place, companies may experience restructuring or retraining. Most companies find that if they plan well then they won't have many job losses. There is some restructuring, but retraining is probably the biggest part. There are many types of retraining that companies use. The most important one is cultural training. This is to prepare them for their future partners overseas. The other retraining that is prevalent in outsourcing situations is team work retraining. This is also to prepare people for working with new people in new situations. These types of retraining will ultimately result in savings. If people are able to work together better then efficiency will be increased, which results in cost decrease and savings.

At this time the team has a few recommendations that are ancillary and tangent to our project. More interviews should be undertaken to get a broader scope and a more

varied opinion. These interviews should also be taken from a variety of people from different industries and fields. The team also believes that outsourcing providers should be interviewed to get another perspective on outsourcing and its effects. The questionnaire should be more refined to get more in depth answers. By seeing the conclusions drawn from the data, the questionnaire questions should also be more tailored to test the conclusions our team has arrived at.

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APPENDIX

Methodology

<u>Brief Overview of Methods</u>

1) Literature Review: Gained knowledge on the topic.

2) Developed questionnaire that will develop mindset behind outsourcing.

3) Interviewed professionals with experience in outsourcing.

4) Transcribed the recorded interviews.

5) Analyzed Interviews.

Interview Transcriptions

Interview A:
OUTSOURCING INTERVIEW MANUSCRIPT
ECI BIOTECH- PRESIDENT MITCH SANDERS

11. What is your **most important strategic reason** for outsourcing?
    a. That is, what are (or have been) the **drivers/triggers** for outsourcing?
    b. Was there a specific **event** that led you to outsource (e.g., budget problems or management edict, etc.)?

"Cost, savings, and strategic focus, human capital (not having the resources). I guess the second is needs. And I guess the last would be experts in their field, and without them we would be lost."

12. What **process** do you go through before deciding to outsource?
    a. Do you conduct an analysis (quantitative and qualitative) to determine whether to outsource?
    b. How do you **identify your needs**?
    c. How is the **decision made**?

"I think that you have a profound understanding at what your good at and you know who the leaders in the field are. For example on our grants we always have our consultants who represent experts in the field whether clinicians, or people who focus on clinical research, or animal research. There are expert consultants. The management team consisted of me up until a week ago so for eight years I've been working with consultants. Consultants to help me negotiate deals, consultants in different areas of expertise in different industries. We do a lot of outsourcing for animal studies with large animal facilities. One out in Michigan and another in the Boston area. So I guess it comes down to what you need to get done, what is your strategic focus, and how can you get it done faster in a relatively cost effective way. And it always comes down to the overhead and the costs on some of these people would be enormous up front. Now that said, as your company gets bigger you may need to start pulling some of those in and as an example we spend a lot of money on lawyers. I've probably got enough lawyers to field a soccer team right now and there may come a time when we may consider to bring someone in house to reduce our bills."

13. What **criteria** do you use to evaluate what services, functions or products will be outsourced?
    a. What services, functions (e.g., back office functions, business processes, IT functions –software development) or products (e.g., automobile industry) will be considered for outsourcing? Why?
    b. What services, functions or products will **not** be considered for outsourcing? Why?

"Well I have a rational for this. If there is an expert in the field and I already know them or respect them either through someone I know or what have you then we can start a relationship. If it somebody new I typically although they may want a full blown consultant agreement which is ridiculous retainer fee I always go with an hourly rate till I know that the person is worth the money."

14. What criteria do you use to select an outsourcing provider?

a. What process do you utilize to analyze the ability of different providers?
Do you ask for bids from different providers?
Do you ask for references from other clients that the top three providers have already provided outsourcing work for?
- Do you prefer outsourcing to one country over another?

"I would say that you seek the best people in the field and they stand out and are typically busy, and unfortunately some of these people are expensive, others a little more cost effective, but as I say you always want to kick their tires and make sure they can work with you and it's going to be a meaningful long term relationship. But if they are out to just gouge you which some consultants can do that is why I like them hourly because you can just pay them ten hours and then get rid of them. If they fail to perform or they have a pattern of gouging you for money in just the first couple hours, then there is something wrong there."

15. Once you have made the decision and have selected an outsourcing provider, were there any structural changes (e.g., manager layoffs, reduction in office space, etc.) that had to be made within the company?

"Not at all. We probably use consultants from everything, from our human resources to business development consultants to consultants to get us through regulatory and it enhances the team that have here. It doesn't result in any layoffs. It just allows us to be faster, quicker, smarter. You don't need a full time regulatory person until you're really in the throws of several products. If you only have one going to market, or two or three going to market at a time then you can probably deal with a regulatory consultant that will team you up with the FDA and get you to the dance on time. So you save money so you know it allows you to focus on being nerds, focus on development and get the expertise you need in other areas."

16. Any staff retraining/repositioning?

"No, no. We pretty much hire what we need. We have gone through little bursts of reduction in staff just because of cash flow reasons back in 2002 for example but after about six months we ran back up and we are kind of continue to run at a reasonable clip and grow at about twenty percent a year."

17. What are the key challenges in working with an offshore partner? Please list the challenges that you see or have experienced after you outsourced?
a. Methodology challenge (i.e., do your methods of conducting business in the U.S. match and/or coordinate with the methods of the offshore partner)?
b. What is the most difficult aspect of outsourcing?

"I think in this global economy and with the internet and secure servers and secure socket layers it is much easier to partner with anyone anywhere. We have clients in UK, we work with folks in Florida, California, and other areas of Europe. In this day and age they can be a phone call away and we've only met them once but you can get a lot done. So the notion of having to be in a major city is long gone."

18. Will any of the outsourced services, functions or products be brought back into the company? If so, why? If not, why not?

"So as the company grows you start to realize that you need a person full time. We hired a CEO out of a billion dollar diagnostic firm. Prior to that we weren't running that burden. We were probably paying for one third of a CEO. Conversely there has

been certain expertise that we outsource that eventually we find a person who was really good and other examples of that are we had some partners that have a great employees and rather than outsource that we chose to hire them right out of the company they we are working with. "

19. What do you believe are the critical success factors in making outsourcing work effectively?

"Cost, value, delivery on time. So you've gotta get what you pay for, you can't be taken for a ride, and you gotta add value. And if you don't then you terminate that relationship and go on to the next and I would say that most times that I have been burned from outsourcing but since I keep them on a very short leash I've only lost five thousand dollars or ten thousand dollars. It's not that I've lost a hundred thousand dollars. And the ones that are gems like our HR person we keep, we've been working with a long time our phone person who does all our CAT5 and all our phone service we've been working with for five years. The guy who does all our upgrades to all our computers we don't have any IT groups we just use Macs at work to come in and give a one terabyte server get it running and walk away. And so for the money and getting an expert that knows exactly what you need but you're only paying them a week over a year and you're not paying for benefits makes a lot of sense. Computers today are fault tolerant they run themselves and if the drive goes down then you just swap for another one."

20. Are there any long-term implications of outsourcing to the U.S. economy?

"I don' know. I would say that there are a lot of outsourcing people in the US economy so I would say that typically what happens when you have boom and bust industries and the .com and computers have kind of had their ups and downs, you find a lot of people become consultants because they lost their job and that doesn't mean they are any good but I guess that I would say that when the economy slides a little bit you start to see a lot more people opening their door front calling themselves consultants. And just because they call themselves consultants doesn't mean they are competent or able to provide the services that you need."

21. What functions, services, or products benefit the most from outsourcing?

"Well I would say that in our field regulatory outsourcing make a lot of sense. These regulatory clinicians can be very expensive. They charge you a grand or two grand a day. If they are on your pay roll you would cry. So you are much better off outsourcing that. When you are getting into a new field and you haven't really bought into whether you are going to launch a product in that field sometimes its really worthwhile to getting a technical innovator in the field or getting a lead consultant in the field to come in and say this is the game you have to play to get into this field. Think about these things and get back to me and maybe I can help you more. We outsource a lot to students to have us analyze market opportunities and on those needs and often times we get that data from our billion dollar partners so I think that you can do a lot with marketing and a lot with financial modeling and doing that all outsourced. It's not until you're a billion dollar company you start needing to bring in a full blown marketing team. Now it depends on how you sell things. If you sell things with a licensing model then you don't need a big sales force, but if you sell things direct then you are going to need it. It really depends on what you do. In our case we can go through distributors so even if we had a sales force it would only be a

team of two to four people that would be regional sales reps working through distributors. But because most of our stuff is being sold to billion dollar firms that are gonna market our stuff we don't need sales reps but occasional we do need marketing input and understanding what the value proposition and what the unmet need is."

Interview B:
OUTSOURCING INTERVIEW MANUSCRIPT
NAGOG HILL PARTNERS – RICHARD O'BRIEN

The business he is in is to be the person that sets up and creates opportunities. His clients are trying to either manufacture or outsource. He tries to understand both sides of that issue and put people together. Interesting problems…. He is a sole proprietor. He has been in this business for 30 years. It is convenient to work alone, but he brings in the right partner for the right situation.

22. What is your **most important strategic reason** for outsourcing?
   a. That is, what are (or have been) the **drivers/triggers** for outsourcing?
   b. Was there a specific **event** that led you to outsource (e.g., budget problems or management edict, etc.)?

By far it's the use of money. By outsourcing a product a company doesn't have to put up the upfront costs to hire workers, to establish facility, to prepare the tooling: the upfront costs. They can now depend on someone with experience and with quality assurance. The use of money, the flow of cash, so they don't have to put the money up front and they don't have to spend it until they receive the product is the most important aspect of outsourcing.

Choosing outsourcing is usually about money and using your resources more effectively.

23. What **process** do you go through before deciding to outsource?
   a. Do you conduct an analysis (quantitative and qualitative) to determine whether to outsource?

It is kind of a make or buy type of an analysis: where you decide what it would cost you to do it inhouse and what it may potentially cost out-house. Its also not just pure money, but recognizing the skill, the experience, the familiarity with a product or new technology or whatever it is that is going to be prepared just isn't there. It takes education, culture and a lot of other things. If you want to be sure that your shipping something that works and that the customer can rely on you want to go to experts that can do that. If you are smart enough to recognize that up front and have a customer, then you want to put the best possible product in his hands. So, it's about money but it's also about the quality of the product you deliver.

   b. How do you **identify your needs**?

I don't think historically managers worried about this. Until globalization occurred and competition reached the level it is today most people weren't too worried and were confident and were more concerned about retaining information and being secure about what they are handling. Today, it's not about security, its about getting to market, and getting there with the strongest package possible. So, identifying what your strengths and

weaknesses are is the first thing. Many think just because they are creating something unique you are prepared to compete, when really they haven't even formed a business. They need to create a real business and market it and give it life. So identifying those needs isn't obvious but it should be something that most people come to grips with. For example, if you find you're good at creating and selling things but not so good at manufacturing then you have to consider options, like outsourcing.

24. What **criteria** do you use to evaluate what services, functions or products will be outsourced?

One important thing is you need to manage outsourcing. It is your product, so you better be in a position to not only negotiate and arrangement, but also be able to manage and participate in the process, and if its not there, without direction they may make decisions you might wish they hadn't made.

It's really important for you to learn from the process. Whether or not you intend to bring this initial outside production in-house at some point or not, you still better understand what it is you are doing. Because if you hit a point where you aren't happy with the production and the development, you going to want to make another selection, and if you haven't learned from that process you're in trouble and the problem may be repeated. So it's MANAGEMENT: engineering, management talent.

You regard this outsource as a partner, and if you manage it well through financing etc. you can get there. Software development- helps you to keep on time, keep the process in check. Part of the learning, understanding, and control generally.

Control is a funny thing in a business. Some people are over the edge and some are far too lenient. The larger the organization the larger the control issue becomes: there is much more at stake: big numbers and hard to recover from poor decision. Most of the outsourcing is delegated to a principal in the company that is manufacturing oriented and effects that portion of the operation.

a. What services, functions (e.g., back office functions, business processes, IT functions –software development) or products (e.g., automobile industry) will be considered for outsourcing? Why?
b. What services, functions or products will **not** be considered for outsourcing? Why?
25. What criteria do you use to select an outsourcing provider?

One of the first things and the most important area is you have to find somebody who has the resources to be successful, or financial stability. It needs to be someone who can show you they're not on their last legs and they need you to stay in business because its just too risky. Maybe they can show you their balance sheet and income statement to show you that they manage their business.

Two is the expertise. You really want to understand what the resources are on the outsourcing side. To have just a few people who can assemble and tool the product is absolutely minimum. You need quality control like ay organization so you have some oversight, understanding and experience. You want the right support and supervision necessary. You need experience in exchanging information and that is very significant. If they can put a product together but don't listen to you about your experiences b/c they are

"confident" , that is bad news. This is the value creation portion of what you're doing and you need to understand them, talk to them, be able to exchange comfortably. They have to show you examples of things they've done so you can sense how they've done them and have a comfortable feeling about of their expectations and levels of quality, cost, approach and willingness to give feedback. Once you start building something you learn about it quickly and find things that can change, so feedback is huge.

    a. What process do you utilize to analyze the ability of different providers?
       Do you ask for bids from different providers?
       Do you ask for references from other clients that the top three providers have already provided outsourcing work for?
       Do you prefer outsourcing to one country over another?

I wonder why we are going offshore to find these cost advantages when I believe we could do that here. But there are reasons why you do go over: Medical devices in Ireland: in U.S. you need to approve your products, not there. And you can talk to them easily. When you go to China, the cultures are an issue. They value certain things and have certain things we don't. We in turn bring things they don't understand. They work hard and long. There are intellectual property issues, they are frequently substituting materials and cost issues that are hard to find and surprising: is it my product and am I in control? That is a problem. Some say here are my specs, no make it. This is alright but most companies have to be much more competent than that. The hours of difference are interesting. You cana send a message to China at 5 pm and that's their morning, so you have the answer the next morning. Some buiy facilites in China, and in his experience only half have success. Some work closely with local population and they can assimilate, and then they really benefit. Others who act as the owners and above the workers, they will not succeed. The language and culture problems will catch up to them and they won't overcome them.
The benefit of language is significant in Eastern Europe, in asia the problems of intellectual property is significant.

26. Once you have made the decision and have selected an outsourcing provider, were there any structural changes (e.g., manager layoffs, reduction in office space, etc.) that had to be made within the company?
It depends on how it is managed. It doesn't have to end up in lay-offs. If it's done well those people can end up doing other things than being laid off. Operating leaner is a help no matter what company you are. You don't need a lot of employees to be successful, and so the tendency to hire people to do things that may not be essential is pretty widespread. A company in a mature industry that is having difficulty competing globally and are losing sales and are worried about there future suddenly decides to outsource and close a plant, that can be quite significant. Some of that is a natural phenomenon that occurs with globalization. Priorities and fundamentals change. A company with dedicated employees and decides to outsource and close a plant is not thinking very long term about themselves and their employees, and this move is a cop-out. This is something that managers today are not addressing.

27. Any staff retraining/repositioning?

Big time. There is such a skill to communicating with these companies and supervising their work. The people who know how to do that are being hired by certain companies because they realize the delicacy of this management problem. Your own employees can't think of the outsourcing folks as enemies, or as people challenging their jobs. If that's the case the company has done a poor job of making a good strategic decision and communicating to the world. But it occurs and you have to help people to realize that these are advantages that the company can use and it doesn't necessarily enhance every individual job but it certainly improves the ability of the corporation to compete and they need to look for ways to understand, appreciate, and use it. It's a big deal, subtle but difficult type of retraining. Some companies give classes to their employees and tell them what they are doing and their strategy and suggest ways to take advantage of this approach. This retraining puts them in tune with company strategy

28. What are the key challenges in working with an offshore partner? Please list the challenges that you see or have experienced after you outsourced?

Culture, language.

Substitution of materials because of availability or familiarity. You may end up with things that are different than you thought you were buying.

   a. Methodology challenge (i.e., do your methods of conducting business in the U.S. match and/or coordinate with the methods of the offshore partner)?
   b. What is the most difficult aspect of outsourcing?
29. Will any of the outsourced services, functions or products be brought back into the company? If so, why? If not, why not?

Absolutely. Ex: Company has 1 large product, outsources it and makes room. They start 3 more products now, and now have 4 items. They decided now that they are a mature enough company to take the 1st mature product in-house.

30. What do you believe are the critical success factors in making outsourcing work effectively?

Managing of the process is critical.
The strategy of using outsourcing needs to be looked at more carefully. A lot of things that are being outsourced don't have to be. They are short term solutions to long term problems. Managements call to outsource needs to be carefully examined.
Being prepared to deliver a product and have it ready for when someone needs it.

31. Are there any long-term implications of outsourcing to the U.S. economy?

Yes. We've opted out of responsibility of retaining the value added character of what we do in business. If Americans want to keep jobs, we need to keep raising the level of education and improve a lot of things that we do. But bottom line is why are we giving these jobs away? We don't have to. Managers are not thinking creatively on how to contain costs, how to be more effective at building and assembling things so that they can create much less expensive products and less costs. It's management's responsibility to understand both its employees and its stockholders and appreciate the difference.

Its an effective management technique but it needs to weighed very carefully and it isn't the answer to a lot of the problems companies have. It's a simple way for managers tro get out from underneath some issue, not a solution long term.

32. What functions, services, or products benefit the most from outsourcing?

Almost everything can be potentially outsourced and be profitable. It can apply to almost anything and be successful if it was a strong business strategy that worked towards long-term viability.

One area where there might be less outsourcing and there is less is in the medical device area. The problem there is the FDA had to approve of and supervise the production of products. If you decide to make a medical device in China, you have to be prepared to fly the FDA to China a lot and its difficult to supervise that type of thing because of complexity.

Some things don't transfer well, nuclear facilities for example.

Interview C:
OUTSOURCING INTERVIEW MANUSCRIPT
FIDELITY INVESTMENTS– DAN RICHARDS

Pre-Interview

"This is more generic discussion; more what industry is doing rather than what Fidelity is doing. Outsourcing is one thing. Off shoring is another. Need to differentiate because a lot of large companies are not outsourcing but off shoring. Motorola, Texas Instruments have presence in India. They're only off shoring. The outsourcing trends are the HR payroll/benefits. Don't want to keep in house so they outsource it. Let's say you're spending a billion on IT and you want to get more for your billion dollars than what you're getting today so lot of people think you're trying to save costs. For most companies it's not about saving costs it's more about productivity and more for your dollar. So they're still going to spend that billion dollars but if you spend 25% of that in India by using resources in India for that 25% which is 250 million you're probably getting 500 million of additional work. Let's say total cost of operations is four billion dollars which 25% is IT and revenue is six billion dollars. Your business grows, revenue goes up to eight billion dollars so your cost structure should go up but meanwhile if you outsource some of that but for the same billion dollars you're able to support a growing

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business but your cost haven't gone up. This is a decision where you decide to do off shoring than you have two paths you can outsource that or start you own center there. You need to know what you're doing. Are you outsourcing or off shoring? You start with that. Then if you decide to off shore you have another decision after that. Do you off shore or do it through your own? Must companies do both.

33. What is your **most important strategic reason** for outsourcing?
    a. That is, what are (or have been) the **drivers/triggers** for outsourcing?
    b. Was there a specific **event** that led you to outsource (e.g., budget problems or management edict, etc.)?

"Your IT expenses. Your cost is divided into three kinds of musts: first cost is nondiscretionary cost: things that you have to spend to keep business alive (all these applications and machines). Then is discretionary. Break up into two. One is non-strategic. R & D and future infrastructure. The main thing is to support new business products. In financial services your website keeps changing (new software and different ways to manage your phone calls). The business will come and say I need these capabilities. If you go to different parts of the business they'll be marketing folks, product folks, customer service guys, and so forth. And you ask them what do you want IT to do this year and they'll have a list of things to do. When you add that all up, they're demands is more money than you have. So you ask them to prioritize because we cant do all of these. You only have a discretionary amount and they need to decide on most important projects. They're not happy but they don't have a choice because the discretionary bucket is fixed. Every year your nondiscretionary gets bigger and bigger so your discretionary money gets smaller and smaller. Every year the company loses the ability to develop new products because most of the money is going into supporting what you developed in the past. At some point if your budget is the same you want to tell the business we are running our data bases and machines we have any money to do any new development. You can solve this by adding money to the budget, you can outsource some discretionary prices to get more bang for your buck, or you can take nondiscretionary pieces and outsource that. If you need one hundred people to run your machines and it cost you ten million dollars and you take those one hundred people and do same things off shore then it probably costs you five million dollars that is freed up to develop new products. 45-50% of the budget goes to maintaining the past and goes up five percent annually. Other triggers are talent pool and get access to the best people. For example, Fidelity has outsourcing not just in India but also in Ireland. Another is business contingency. You have geography dispersed so risk is dispersed. Say something happens in Boston you'll have folks in India who could pick up the slack. In the case of Fidelity, we started doing software outsourcing. People traveled back and forth and got very excited about the country. Some of the portfolio managers went, "Hey, this is a pretty cool place to do business" so we actually opened up a mutual fund there in India and there's a portfolio manager doing that. It's the second largest mutual fund in India. What triggers it off is cost and its really not the cost but trying to get more out of the savings. People want more for the same amount. The other thing you realize is. . . "Let's say years ago I have a project and it would be a cool thing to do and I present my numbers for the project. Say if you do this project its going to cost a million dollars.

34. What **process** do you go through before deciding to outsource?
    a. Do you conduct an analysis (quantitative and qualitative) to determine whether to outsource?
    b. How do you **identify your needs**?

"It is a very in depth process. There is the idea that maybe outsourcing would be useful to our company. We then usually have some people gather data on it. From this date we are usually able to see pretty easily that it would be in our favor to outsource or not. A few people then discuss what the data and future decisions could mean for the company. But in the end it is pretty easy to say it is going to save us money and it should be done."

35. What **criteria** do you use to evaluate what services, functions or products will be outsourced?
    a. What services, functions (e.g., back office functions, business processes, IT functions –software development) or products (e.g., automobile industry) will be considered for outsourcing? Why?

"Let's talk about off shoring. I'll give u an example of Micro. What makes sense to off shore first? What makes sense is your nondiscretionary core. The reason you outsource that is that most of the operational worth happens in the night and it's daytime in India. People get paid in the middle of the night, software is done, computers are up. If they want to install hardware boards they can't do it during the day because people are trading. You have to do it during the night. The most obvious ones are nightly supports. The second kinds of things you outsource are testing of software. So you develop that software then you go through a testing cycle. When you do testing in the daytime it takes 1/3 of the time to develop software and it's a biggest from the time perspective. You can two testing teams. One here and one off shore. Now you're getting 16 testing hours a day because once you finish here u send it over. You're taking advantage of what they call the global clock. If you take advantage you can get 24 hours of work done in a day instead of 8 hours. You're not spending any less and getting the project done faster. The current thinking is there is no such thing that can't be outsourced. The mindset that these are good things to outsource and these are not is fading away. You may not want to outsource something but off shore it. We have R & D at Fidelity overseas. Those guys we never see them they're in the labs and they just play around with technology. Like in my group I had 10 architects and 70 people doing development. Now I have 30 architects and 80 doing development with 40 of them in India. I hired people who can do bigger picture, connect the dot, being able to talk to the business folks and the actually programming work is slowly shifting there. Nothing you cant off shore.

Kevin : Do you think outsourcing will shift around the globe and move from India?

"It will move around the globe but India right now has the advantage because they speak English and have a good education system. There's going to be a labor shortage in India and companies will have to move somewhere else. Just like here in 2001 when companies started moving elsewhere. When you talk about pure labor arbitrage…My definition of arbitrage means that there is a differential pricing in two places for the same product. Cost is not only criteria, but you have other things like talent pools etc. China

has tremendous potential in software. Pakistan is trying to get in there. Philippines set up a place. I think the trend will be that people will open up places in multiple continents.

> b. What services, functions or products will **not** be considered for outsourcing? Why?

You could offshore everything. You'll get different answers from everyone. You would think that call centers are the most obvious thing to outsource. At Fidelity Brokerage Company we think that customer service is so critical to abandon. We don't have one single call center operator for brokerage. We need to train them and haven't made that leap. Some companies it's the most obvious thing and some companies the CEO will say it's the last thing we'll do.

36. What criteria do you use to select an outsourcing provider?
> a. What process do you utilize to analyze the ability of different providers? Do you ask for bids from different providers? Do you ask for references from other clients that the top three providers have already provided outsourcing work for? Do you prefer outsourcing to one country over another?

We asked for bids from different providers. We checked profitability and stability. Huge for us was our security people visiting their data centers. What is their security process? We actually found out that their security was better than ours. You don't have any access to the hard drive, no zip drives; you can't get anything out of the computer. Right now I can walk into my office and go on the computer and take information from a zip drive. We picked 3 big ones and 2 small companies so they would be competitive against each other. The small ones actually do better business sometimes because they want your business more and they put their best people on it. We do fixed or variable bids. Variable is when the work content isn't very defined. If they'll be overruns or if things are defined we do fixed bids.

37. Once you have made the decision and have selected an outsourcing provider, were there any structural changes (e.g., manager layoffs, reduction in office space, etc.) that had to be made within the company?

Not if u plan well. You're actually adding people. All you're doing with that net additional growth you're actually now getting people from offshore. You do need to train your managers on how to do global business. You may have to hire specific off shore project managers. You may have to restructure your organizational structure. What new tasks do people do? In my group we haven't laid off anyone. The net effect is hiring 3 or 4 hardcore project managers. We have to plan on the expenses for people going back and forth. We need to find office space. We had to change things like working hours because if you work 9 to 5 here then we want to change their time to correspond to overlap. There's a whole bunch of things you need to do but u don't need to lay off people. People in our company go on extended assignments and stay for a couple years. Generally in the industry in the IT side it's been growth. We have more high value jobs here then start up jobs.

38. Any staff retraining/repositioning?

Project managers you need to train people in different situations-how to manage globally. They take part in certification courses. A number o f my staff went through that. Also,

cultural training. Our instances have been mostly positive. On the offshore side we have some problems with retention. Companies try to hire your employees by giving them-let's say a 10 % raise. We make sure they document everything so if they leave someone else can pick it up. The hardest part is transferring the knowledge off shore.

39. What are the key challenges in working with an offshore partner? Please list the challenges that you see or have experienced after you outsourced?
    a. Methodology challenge (i.e., do your methods of conducting business in the U.S. match and/or coordinate with the methods of the offshore partner)?
    b. What is the most difficult aspect of outsourcing?

As previously stated in another one of my answers two difficult aspects in working with off shore providers are the language barrier and finding a country with a solid educational background. In my experience, I always try to find aid in a country which a good educational structure and thus they are more reliable to do an efficient job because they have the skills necessary.

40. Will any of the outsourced services, functions or products be brought back into the company? If so, why? If not, why not?

Well, it all depends on the situation. If a product or service is working out sometimes its just best to let it be. As they say, "if it ain't broke, don't fix it." However, sometimes the situation arises when a service or product is making the company money but it's clear that by bring it back in house the company could make more money."

41. What do you believe are the critical success factors in making outsourcing work effectively?

Communication and working well together. If you communicate well and can work with people that you haven't had much experience with then the team should be able to complete every goal it sets out for. We found that in most outsourcing situations communication and chemistry are repetitive problems that we keep seeing. Also, tasks getting accomplished in a timely manner is a key factor because if something doesn't get done all time it holds up all your other operations.

42. Are there any long-term implications of outsourcing to the U.S. economy?

As of right now we don't really see many impacts on the US economy. In the long run, economies usually seem to balance themselves out when there is a change. For example, if a specific industry such as textiles sends most of its work to India you'll usually see another industry pop up in their wake. Like the economy never stays stagnant—it's usually always changing and evolving.

43. What functions, services, or products benefit the most from outsourcing?

There isn't much that outsourcing doesn't touch in the industry these days. From computers to clothing to research and development…it's everywhere. I don't believe there is a standard template that a company can look at to know what to outsource and what not to outsource.