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GLOBAL OUTSOURCING AND OFF SHORING

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Abstract:-Global outsourcing is enabling business without barriers in a borderless world. As enterprises think global, their outsourcing models have changed to follow suit.

Outsourcing is no longer just a short term quick-fix to achieve cost reduction. Global outsourcing uses a blend of onsite, offshore and near shore outsourcing solutions to achieve strategic business objectives for the outsourcing company. Today, there are job titles like "Chief Globalization Officer" and "Strategic Services Manager" - which just goes to show that organizations are taking seriously the impact of global outsourcing on the revenue growth and business value of their companies.

Keywords: Global outsourcing ,off shoring , strategic business objectives.

INTRODUCTION

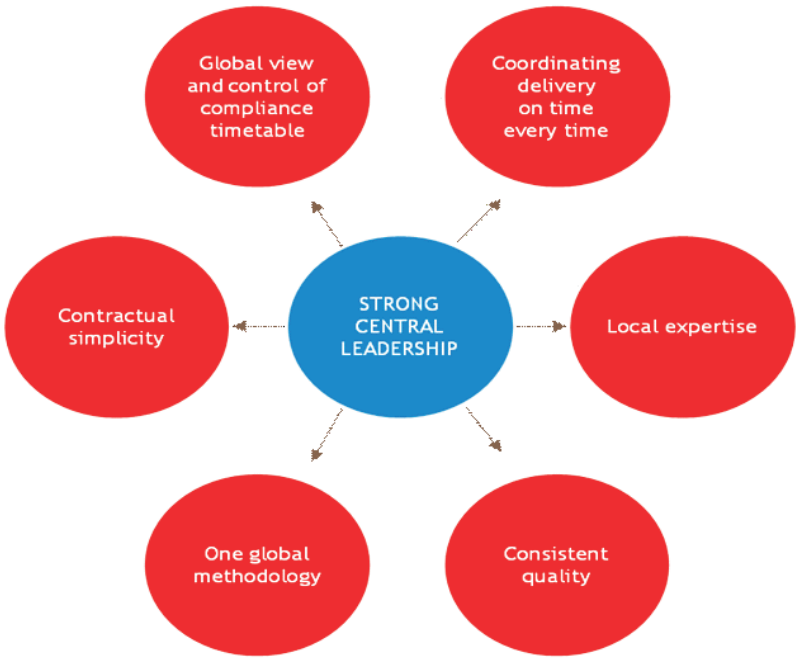
As customers get more demanding, competition gets more intense and product life-cycles shrink, there is increasing pressure on operating margins. The complexity of global cross-border business management presents new challenges as companies try harder to stay agile, profitable and innovative. Business processes need to be flexible and adaptable to enable people to respond faster to changing business needs. Services outsourcing must be aligned to business goals, rather than be seen as just a tool for enhancing operational efficiencies.

Global outsourcing takes a long-term holistic view of the client enterprise and aligns its business goals to the outsourced service offerings, in contrast to tactical short-term contracts that take a piecemeal project-by-project or simple "out-tasking" approach to outsourcing.

The field of sourcing is replete with jargon and acronyms. For example, the term “bestshoring” has become one of the recent “buzz” words which, while widely used by managers, are poorly defined by the professional press and academic publications. Even more worrying is the inaccurate use of the terms “outsourcing” and “off shoring” by both managers and academics wish to explain what we mean by the term sourcing.

Sourcing is the act through which work is contracted or delegated to an external or internal entity that could be physically located anywhere. Sourcing encompasses various in-sourcing and outsourcing arrangements such as offshore outsourcing, captive offshoring, nearshoring and onshoring.

Clearly, almost any firm is somehow engaged in sourcing activities; however, each of these firms applies a sourcing arrangement that suits its particular nedds.



Centrally controlled, locally delivered global outsourcing

With the advent of globalization and enhanced levels of competition, many organizations have started to have considerable difficulties in developing and maintaining the range of expertise and skills needed to compete effectively. The emergence of American, European, Japanese, and Third World Multinationals has created a new competitive environment, requiring the globalization, or at least semi-globalization of corporate strategy. This need has led many companies to engage with various kinds of sourcing strategies, such as outsourcing, offshoring, offshore outsourcing, nearshoring, and onshoring. Therefore, main focus is on

• the key terminologies used in the sourcing literature;
• the key drivers of global sourcing;
• the benefits for clients and vendors from engaging in global sourcing;
• present market trends in the global sourcing market;
• future developments of the global sourcing market.

Sourcing is the act through which work is contracted or delegated to an external or internal entity that could be physically located anywhere. Sourcing encompasses various in-sourcing (keeping work in-house) and outsourcing arrangements such as offshore outsourcing, captive offshoring, nearshoring and onshoring.

Outsourcing is defined as contracting with a third service provider for the management and completion of a certain amount of work, for a specified length of time, cost, and level of service.

Offshoring refers to the relocation of organizational activities (e.g. IT, finance and accounting, back office, human resources) to a wholly owned subsidiary or an independent service provider in another country. This definition illuminates the importance of distinguishing whether the offshored work is performed by the same organization or by a third party)

Global Sourcing Background

Offshoring strategies appear to be promising in terms of the reduction of costs, as certain organizational activities would be moved to a subsidiary or an independent service provider in a country with favorable conditions. The US is a major player in the offshoring of IT and business process applications. However, over the past few years offshoring has appeared to be gaining momentum in Europe as well.

Drivers, benefits, and risks of global sourcing

The growth of global sourcing has been attributed to many factors. First, technological advances in the telecommunications industry and the Internet have shrunk space and time and have enabled the coordination of organizational activities at the global level. Other reasons include the supply of skilled, yet low-cost, labor in countries such as India; the investments in infrastructure; the improved business, economic, and political climate in a number of developing countries; and the standardization of IT processes and communication protocols that contribute to the efficiency of inter organizational activities. Along these lines, many countries invested heavily in improving their telecommunications infrastructure, which is essential for electronically transmitted services. For example, Barbados has had a fully digitalized communications system with direct international dialing since the beginning of the 1990s. Jamaica constructed its "Digiport," with a 20,000-telephone-line capacity and speeds of 1.5 Mbps. Furthermore, many countries provided specific tax advantages to attract offshoring. For example, the standard tax rate in Ireland is 43%, but BPO firms get a favorable rate of 10% until 2010. Jamaica has a 34% tax rate, but the "Digiport" BPO free trade zones are tax free. The US tax code also favors offshoring over keeping work domestic. US corporations are allowed to defer taxes on offshore units until the money comes back to the USA. Thus, firms are given an interest-free loan on taxes owed if they offshore work.

Global sourcing may offer several benefits which are basically associated with the advantages of outsourcing in general. Along these lines, a company may accomplish significant cost advantages through the creation of economies of scale, access to the unique expertise of a third party, and the reduction or stabilization of overhead costs. Furthermore, a company may benefit from outsourcing by concentrating on core activities, on organizational specializations, or focusing on achieving key strategic objectives. More specifically, following a "core competency through outsourcing strategy" may enable a company to focus its resources on a relatively few knowledge-based core competencies where it can develop best-in-the-world capabilities (Quinn and Hilmer, 1994).Concentration on a company's core business may allow it to exploit distinctive competencies which will constitute significant competitive tools. Another major benefit of outsourcing is that it can give the organization access to the service provider's capabilities and innovative abilities, which may be expensive or impossible for the company to develop in-house (Quinn and Hilmer, 1994). Some analysts contend that an important source of user value is the firm's access to economies of scale and the unique expertise that a large provider can deliver. Since providers are typically servicing many clients, they often achieve lower unit costs than any single company cans (Alexander and Young, 1996). Even more, a network of suppliers can provide any organization with the ability to adjust the scale and scope of their production capability upward or downward, at a lower cost, in response to changing demand conditions, and at a rapid rate. As such, outsourcing can provide greater flexibility (McCarthy and Anagnostou, 2003). Furthermore, outsourcing can decrease the product/process design cycle time, if the client uses multiple best-in class suppliers, who work simultaneously on individual components of the system, as each supplier can contribute greater depth and sophisticated knowledge in specialized areas and thus offer higher quality inputs than any individual supplier or client (Quinn and Hilmer, 1994). On this basis, having several offshore centers can provide around-the-clock workdays. In other words, development and production can take place constantly by exploiting the time difference between different countries. However, there exist several disadvantages to adopting sourcing strategies. Loss of critical skills or overdependence on an outside organization for carrying out important business functions may evolve into significant threats to a company's well-being. Furthermore, security and confidentiality of data can be a major issue for many companies. Another major issue is losing control over the timing and quality of outputs since these will be undertaken by an outside vendor which may result in a poorer quality of the final product or service and may generate effects which could be very negative to a company's image. Even more important is the fact that, unless the buyer's core competency is a true block to entry into the marketplace, some suppliers after building up their expertise with the buyer's support, may attempt to bypass the buyer directly in the marketplace (Quinn and Hilmer, 1994). On these grounds, it is critical that a company manages its sourcing strategy in a way that is not nurturing a future competitor. With regard to outsourcing arrangements, it is important to note that there are some risks that are specifically linked to these. For example, outsourcing is usually followed by changes in the organizational structure. Redundancies and layoffs are commonplace in outsourcing situations. Research and experience indicate that outsourcing effectively signals to employees their employer's intention to initiate a change that may involve de-skilling and redundancies (Kakabadse and Kakabadse, 2000). Such initiatives generate internal fears and employee resistance.

Moreover, Hendry (1995) highlighted the fact that outsourcing can be associated with problems related to the company's ability to learn, as it can increase the insecurity and decrease the motivation of the workforce, reducing willingness to question and experiment (Hendry, 1995). While interactions among skilled people in different functional activities often develop unexpected new insights or solutions, there is the fear that outsourcing will make such cross-functional synergies of ideas and knowledge less likely (Quinn and Hilmer, 1994).

The future of outsourcing and offshoring

By the end of 2009, ITO revenues exceeded US$ 250 billion while those for BPO were more than US$ 140 billion. The revenues from offshore outsourcing of business and IT services exceeded US$ 60 billion, and over the next five years the compound annual growth rate for offshore outsourcing is expected to be about 20%. Willcocks and Lacity (2006) identify the following 11 trends for the future of global sourcing markets:

1. Spending will continue to rise in all global sourcing markets despite 2004–2005 media attention on backsourcing: Irrespective of some major backsourcing ventures (such as JP Morgan in 2004 and Sainsbury in 2005), Willcocks and Lacity maintain that these do not represent a major trend towards backsourcing, and they specifically emphasize that on their figures "the most popular course of action at the end of a contract will continue to be contract renewal with the incumbent supplier." The authors also estimate that a quarter of contracts will be re-tendered and awarded to new suppliers and only atenth will be backsourced.
2. Developing countries beyond India will become important players in the global business and IT services market: Countries that appear to have the potential to follow India as attractive destinations for global sourcing include the Philippines and China. On the other hand, large Indian suppliers have gained much expertise and experience in dealing with and building relationships with US customers, which will enable them to demand higher prices. In the US, the recent Central American Free Trade Agreement (CAFTA) is expected to further open up IT and Business Process outsourcing in Cost Rica, El Salvador, Guatemala, Honduras, Nicaragua, and the Dominican Republic. In Western Europe, companies are expected to increasingly source IT and business providers to Eastern Europe and North Africa.
3. Large companies will give application service provision (ASP) a second look: Large organizations will reconsider ASP for several reasons. First, large companies will want net-native applications that can be delivered only through ASP. Second, large companies appear more willing to give up on their expensive proprietary suites for more cost efficient ASP alternatives.
4. Business process outsourcing will overshadow IT outsourcing: According to Willcocks and Lacity, the market for mainstream BPO expenditure is likely to grow worldwide by 10% a year from US$ 140 billion in 2005 to over US$ 220 billion by 2010. The major business functions to be outsourced include human resources, procurement, back office administration, call centers, legal, finance and accounting, customer-facing operations, and asset management. The business logic that is expected to drive BPO is that organizations recognize back office administration as a secondary activity and do not wish to invest in back office innovations. Suppliers, on the other hand, are rapidly trying to build capabilities that will enable them to offer beneficial alternatives to inefficient processes and functions. Along these lines, many BPO deals are expected to dominate much of the back offices IT systems.
5. IT outsourcing will continue to grow but with new value propositions from the market: One example of new, innovative value propositions may be the consolidation of networks in the same way suppliers consolidated data centers during the 1990s. The reason for this is that it is becoming increasingly expensive for companies to manage private networks while there are a lot of opportunities to consolidate private networks among a few large suppliers.
6. Selective sourcing with multiple suppliers will remain the dominant trend: According to Willcocks and Lacity, over 75% of organizations in the developed economies outsource 15%–50% of their IT budgets, typically with multiple suppliers. They also predict that the average percentage of corporate IT budgets is set to rise, with IT outsourcing reaching 34%, IT-intensive BPO 15%, and offshoring 9% of the IT budget.
7. Clients will control in driving and designing deals: Contrary to the 1990s, when most deals were designed by suppliers, clients are recognizing the need to understand and control the conditions under which the outsourcing venture is executed. Over 80% of contracts are now being drafted by the client, or based on appropriate templates, a change that represents a significant power shift towards clients. On this issue one supplier recently noted "we own 80% of market here, yet clients are now dictating to us, if we want to stay in business, we have to do it on their terms." However, client control can have reverse effects if it results in the suppliers winning a "cursed" deal.
8. Clients will invest much more in contract management: According to Willcocks and Lacity, the cost of getting to contract is between 0.4% and 2.5% of the contract value. Ongoing management costs are between 3% and 8% of contract value. These costs are expected to increase. This is primarily because of three reasons. The first is related to the rise of offshoring, where management costs typically fall between 12% and 15% of contract value. Second, clients will try to build their internal core capability to levels that give better payoffs from outsourcing. Third, contract management is a major determinant of outsourcing success.
9. Outsourcing will help in-sourcing: In-house operations are increasingly adopting the techniques of the market. One such example is the use of Service Level Agreements (SLAs). SLAs define the services provided, the metrics used to evaluate services, as well as the reporting and governance put in place. While prior to outsourcing only a few organizations employed the SLA technique internally, after outsourcing nearly 60% have some form of internal SLA.
10. Outsourcing failures and disappointments will continue: Outsourcing will continue to be a venture which is very promising in terms of rewards, but which also carries high amounts of risk. Extrapolating past evidence into

2006–2011, Willcocks and Lacity estimate that 70% of selective sourcing deals will be considered relatively successful. In contrast, they estimate that only 50% of large-scale deals involving complex processes that represent more than 80% of the relevant budgets will be successful.
11. Clients will move en masse from "hype and fear" into maturity: According to Willcocks and Lacity, the typical learning curve for outsourcing includes four stages. In the first stage senior executives become aware of an outsourcing market through marketing "hype" or irrational propaganda. In the second stage most senior executives initially engage in outsourcing to seek lower costs. In the third stage senior executives recognize outsourcing as a strategy aiming at quality of operations as well as the reduction of costs. In the fourth stage, more mature adopters use outsourcing to strategically enable corporate strategies, such as increasing business agility, accessing new markets, creating new markets, and so forth. On this basis, the authors suggest that IT outsourcing organizations are at different points in this model, but the mass are in phases 3 and 4. In fact, with offshore and business process outsourcing, the bulk of organizations are much lower down this learning curve. However, as outsourcing moves in 2006–2011 to become a core part of budgets and organizational management, learning and cross-learning in all three areas (IT, business process, and offshore outsourcing) will increase and organizations will become more mature in managing their outsourcing ventures.

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