

Outsourcing Isn't Just for the Big Guys Anymore

Companies that launched to fill outsourcing needs are themselves becoming outsourcers.

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for Office.com*

July 14, 2000 - Outsourcing. It started as a defensive measure for big businesses in the 1980s. They needed to cut costs. But more importantly, they needed to spend more time on core or "mission critical" activities where they could add value and be more competitive.

Velocity was the name of the game against fast international competitors — and outsourcing non-strategic activities was the way for the big guys to achieve it. In the process, they created many new, small and highly specialized businesses to fill this need.

Now, we've come full circle. Those small businesses created by the outsourcing mania are — or should be — outsourcing themselves.

In today's environment of dizzying change, even small businesses should look to others to execute non-essential functions. No one, large or small, can do it all and do it well.

Outsourcing from End to End

It's difficult to find any U.S. companies left that produce their value proposition themselves. Automakers work through a huge web of suppliers. Tech hardware companies often touch little or no inventory themselves. Huge operations, such as Flextronics or Solectron, manufacture archrivals' electronics brands on adjacent assembly lines. These companies also help design products, organize parts procurement, and even organize distribution. Then, when the customer needs technical support or repairs, the agent answering the phone may be working for an outsourcing firm such as Convergys or Precision Response.

Service providers do the same, outsourcing everything from human resources to accounting.

Big pharmaceutical companies are essentially outsourcing part of their R&D efforts when they link up with a small biotech firm. Cisco and Intel are

constantly investing in new companies that can exhibit promising new technologies.

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Outsourced operations have produced a huge gain in warehouse space in America — an increase of some 700 million square feet in the past decade. According to Armstrong & Associates, a consulting firm based in Wisconsin, much of this growth came from outsourced operations, which grew by nearly 17 percent to \$45 billion last year. Consulting firm Bain & Co. estimates that a company must handle at least 15,000 transactions a day to justify owning its own warehouse. Many observers estimate that defunct Boo.com would not have burned out so fast if it had not tried to do everything itself. Etoys and even Wal-Mart have outsourced warehousing operations to Fingerhut.

A Look at Strategic Outsourcing ...

Outsourcing is simply the action of turning over a business function to an outside company. A member survey run by The Outsourcing Institute ranks the following reasons as the most important:

- Reduce and control operating costs. Can another company perform the function as well or better, for equal or less money?

- Improve company focus. Is this a critical function for your business? Does it contribute to your overall strategic objectives or directly affect customer service?

- Gain access to world-class capabilities. Do you have the skills and knowledge internally to perform this function as well as your competitors? Are your people able to stay abreast of the latest technology, say, or the changing legal environment? Can a company that is an expert in this area do it better?

- Free internal resources for other purposes. Can some of your employees contribute more to the bottom line if they aren't tied down with peripheral administrative duties? Can you sell more products/services or serve your customers better if your employees are redirected toward core competency areas?

In today's entrepreneurial environment, most functions can be outsourced for a reasonable price. Perhaps more importantly, the focus has changed from "Who is the cheapest?" to "Who will be the best partner?" When every Internet service provider is offering corporate rates for less than \$20 a month, the one that will complement your strategic objectives should win your business.

... and the Pitfalls

Outsourcing should not be adopted as a knee-jerk cost-cutting measure; there are dangers that can sometimes outweigh the advantages. The outsourcing firm may let you down. At a critical time, a contracted company may not have the same sense of urgency or ownership that your own employees would have. And, there will naturally be some loss of control.

Outsourcing could also cost you more because another company's margin requirements and per-transaction fees may push the cost above what you could have paid to do the job in house. There may also be opportunity costs if the company's response times or service levels cause you to sacrifice sales opportunities. Moreover, your company may fail to develop skills or expertise. Outsourcing may prevent your personnel from developing key skills, and your company may lose expertise in one facet of your industry.

Yes, there are dangers to outsourcing. But they should not stop you from actively considering it for every non-core function in your company. Just be sure to ensure that you have a strategic win-win (and shared risk/reward) agreement with your outsourcer and the backing of your top management.

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