

Outsourcing IT Strategies & Best Practices

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Agenda

- Enterprise 2.0 (World is changing)
- IT Outsourcing & Business Process Outsourcing
- Managing Risk
- Practical Outsourcing
- Case Study : Cathay Pacific

Enterprise 2.0

World is changing !!



Web 2.0 Definition

- Web 2.0 is the combination of:
 - tools and technologies
 - business strategies (like blogging, external wikis, customer participation)
 - and social/cultural trends
- which drive the individual creation and sharing of content on the Internet

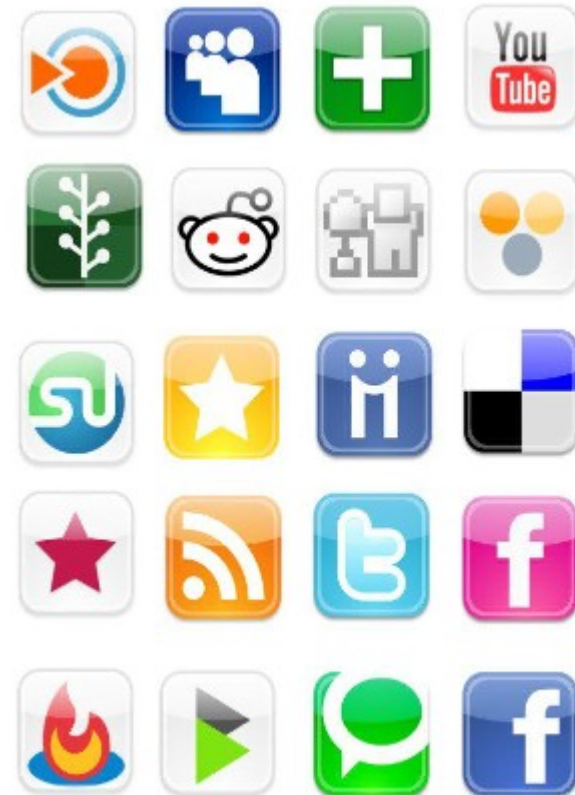
Types of Web 2.0

- Social Networks
- RSS
- Wikis
- Blogs
- Podcasts
- Citizen Journalism



Chances are you've used Web 2.0

- Gmail
- Wikipedia
- Facebook
- Twitter
- Google Map
- Slideshare
- OKNation Blogs
- Youtube

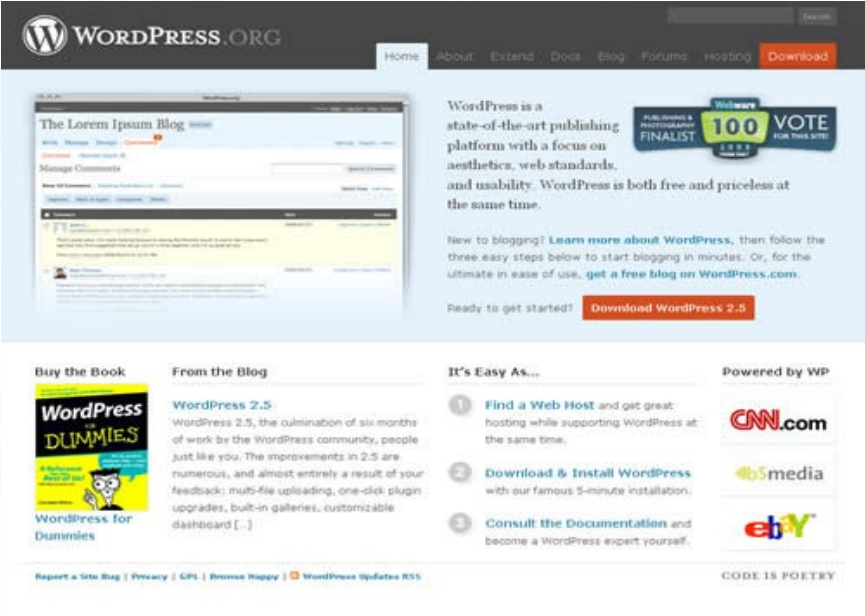


Web 2.0 : Business Changes

- Empowering employees
 - Let them blog - internally & externally
 - Let them collaborate with wikis
- Encouraging external collaboration with [wikis](#)
- Long Tail phenomenon
- Product vs. Service (MS Office vs. Google Docs; Web-based calendars, etc.)
- Publishing

Web 2.0 : Social Change

- Blogs
- Trust in Wikipedia
- Emphasis on communities
- “People power”
- Political commentary



The screenshot shows the WordPress.org homepage. At the top, there is a navigation bar with the WordPress logo and the text "WORDPRESS.ORG". Below this, there are links for "Home", "About", "Extend", "Docs", "Blog", "Forums", "Hosting", and "Download". The main content area features a large image of a WordPress blog interface on the left and a text block on the right. The text block describes WordPress as a state-of-the-art publishing platform and includes a "100 VOTE" badge. Below the main content, there are four columns of information: "Buy the Book" (WordPress for Dummies), "From the Blog" (WordPress 2.5), "It's Easy As..." (a three-step process), and "Powered by WP" (logos for CNN.com, 5media, and eBay). At the bottom, there are links for "Report a Site Bug", "Privacy", "GPL", "Become Happy", and "WordPress Update RSS", along with the slogan "CODE IS POETRY".

New Ways of Doing Business

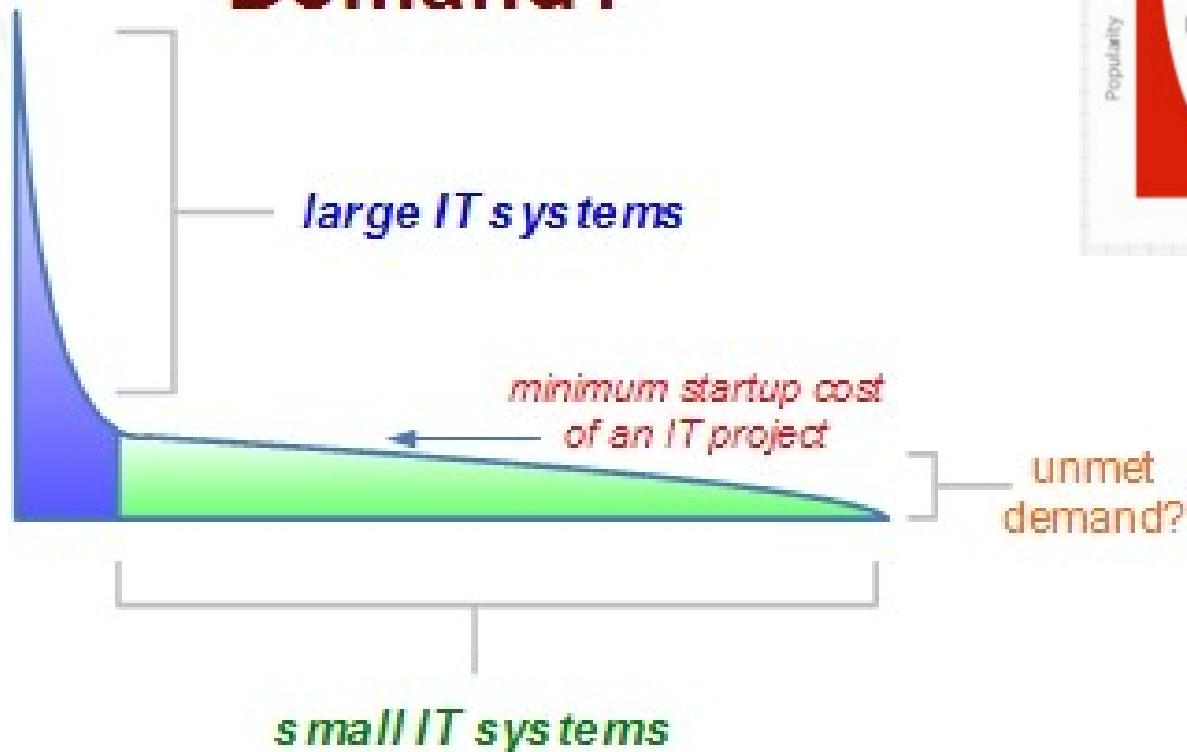
- Driven by changes in your marketplace probably not you
- Proven outside the corporation for applications other than business
- In use by some of your customers, contractors, employee at home / offices
- Familiar to your new employees
- Conversation
- Collaboration
- Community

New Ways of Doing Business

- Traditional
 - Communication: “I want to tell you something”
 - Fix roles and responsibilities
 - Spheres of interest, market, smokestacks
- Evolution
 - Communication: “Let's talk”
 - Collaboration :”Let's work together”
 - Communication “ Let's share our common values and interests”

Enterprises versus SMB (s)

The Long Tail of Enterprise Software Demand?

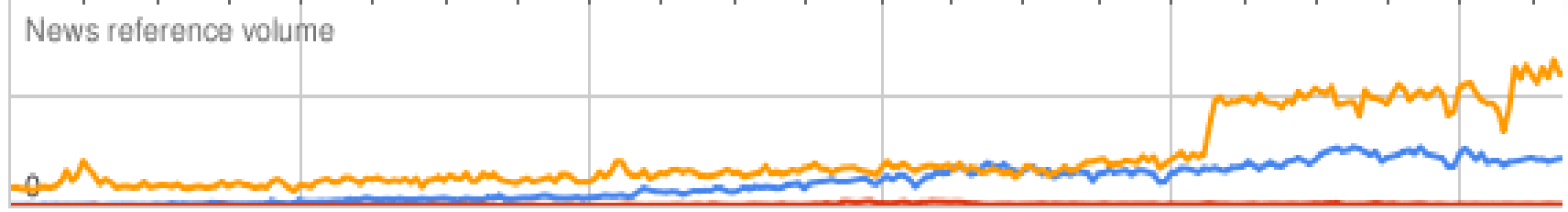
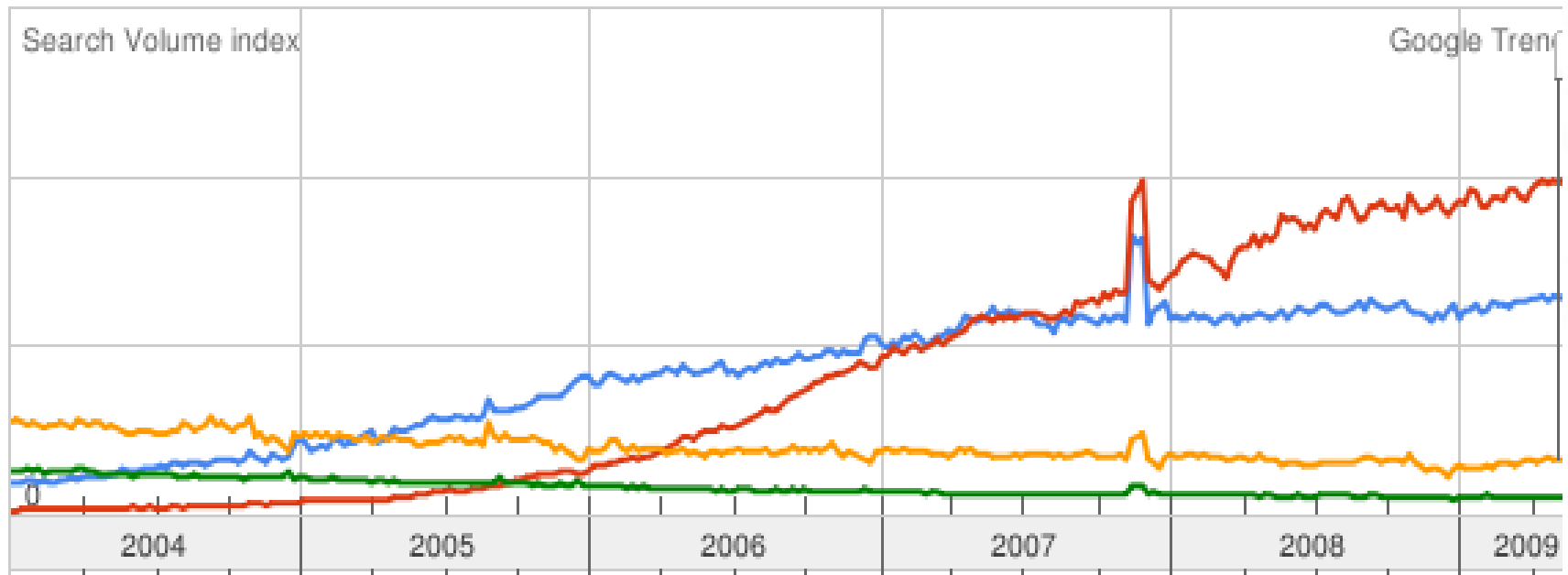


Long Tail Concepts

- Selling more and more to fewer and fewer
- [Pareto's Principle](#) (80-20) less relevant today
- Relationship to Web 2.0
 - Shift from the monopoly of the “big hits” favors tiny publishers and creators of Web content
 - Encourages “niche” producers to collaborate with “aggregators” like Amazon, iTunes, NetFlix, etc.
 - Sometimes a niche product can become an unexpected “blockbuster” through viral marketing, word of mouth

Enterprise 2.0 Adaptation Curve

● blog ● wiki ● newspaper ● e-mail



Business : Basic Issues

- Strategic :

- Use Web 2.0 (including related concept like Long Tail) to find new products, services, markets
- Use Web 2.0 to increase revenue, dramatically reduce costs
- Use Web 2.0 to empower individual customers, employees and outsiders like retirees, alumni..
- Use Social networking tools to find scarce skills, like IT people

- Tactical :

- Encourage collaboration with wikis
- Encourage communication with blogs
- Improve UI of web-based products and services with AJAX

Trends : Business

- Web 2.0 will put some Web 1.0 companies out of business
- Web as a platform?
- Appearance of next Google?
- Decreased relevance of venture capitalists?
- Boundary between customers and companies blurs

Gartner Top 10 IT Trends 2009

- Virtualization
- Cloud Computing
- Beyond Blade Servers
- Green IT
- Web-Oriented Architecture
- Enterprise Mashups
- Social software and Social Networking
- Unified Communication
- Business Intelligence
- Specialize Systems

What does it mean to us?

- IT is more complicate ?
- Larger data center?
- Heterogeneous platforms
- Various IT skills require..
- IT security issue
- More complicate infrastructure / Networks
- Need quicker time to market

IT Outsourcing and Business Process Outsourcing

What is outsourcing?

- Outsourcing is nothing new
- Outsourcing is essentially an elaborate description an arrangement whereby a company carves out certain services that it has been providing internally and retains a third party to provide these services
- Offshoring is sometimes described as outsourcing to service providers in another country.

IT Outsourcing

- Contracting ?
 - “Contracting is the purchasing of goods or services when the buyer owns the process.” Bendor-Samuel
 - If the buyer owns a process but purchases time, products or services to facilitate that process, then the buyer is in a contractual relationship.
- Outsourcing?
 - “Outsourcing takes place when an organization transfer the ownership of a business process to a supplier” Bendor-Samuel
 - . The key is the concept of *transfer of control or transfer of ownership*.
 - This is why IT outsourcing is very challenging and often a painful process.

Benefit of outsourcing

- Allows focus on “core” competence of the company
- Cost-savings from reduced overheads and consequent reduction in training needs
- Cost-savings through economies of scale gained by the outsourcing service provider
- Higher levels of service and performance due to specialization of the service provider
- Reduction of capital expenditure (IT systems, support systems)
- Shorter times to market for a customer’s services
- Standardized IT infrastructure and processes
- Improvement in processes and their documentation

What functions are being outsourced?

- **IT Outsourcing (ITO)** was the original and still leads in terms of outsourcing
- **Business Process Outsourcing (BPO)** has emerged as an effective sourcing strategy for organisations seeking to reduce their operating cost base while also improving service delivery and support for their customers, suppliers and employee.
- **Knowledge Process Outsourcing (KPO)** is the new wave. It is different from business processes in terms of the value proposition to the client, which leads to a clear demarcation in process complexity, the amount of intellectual intervention in the process, the skills required and the ability to scale.

IT Outsourcing Evolution

- EDS
 - Regulated, then to non regulated industries
- CSC
 - First to governments then to industries GD
- ADP
 - Payroll, data center, etc
- IBM
 - The “big bang” internationalization, etc.
- Others
 - (Gap Gemini, Perot Systems, Andersen Consulting, etc.)

IT Outsourcing Factors

- Two factors have affected the growth of IT outsourcing
 - Recognition of strategic alliances
 - Changes in the technological environment

Acceptance of Strategic Alliances

- Finding a strong organization partner to complement an area of weakness gives an organization an island of stability in a turbulent environment.
 - It is difficult to fight on all simultaneously on all fronts
 - Alliances allow a company to simplify its management agenda safely.
- Alliances allow a firm to leverage a key part of the value chain by bringing in a strong partner that complements its skills.
- Both firms should legitimately be benefiting

IT Changing Environment

- Today, firms are not focusing IT only on internal processing systems: but, in a network fashion, - integrating internal system with those of customers, suppliers, - to be more efficient in globally market place.
- This integration places extraordinary pressures on firms trying *to keep the old system services running* while developing the interconnections and services demanded by the new environment.
- On the one hand, firm are looking for low-cost maintenance of the old systems to ensure they operate reliably, while, on the other hand, gaining access to new skills to permit their transformation to new model.

Why should you outsource?

- Mounting margin pressure, global competition, and an increased focus on core business are driving companies like never before to look for new ways to get things done at a lower cost.
- While cost saving is a primary driver of outsourcing, companies benefit in other ways, including freeing up internal resources and accessing world-class skills and capabilities.
- Typical objectives desired from outsourcing include:
 - Improving strategic positioning through increased focus on core functions.
 - Improving competitiveness through operational performance improvements and access to cheaper and more specialist skills.

Drivers of outsourcing

- Cost or internal headcount needs to be reduced
- Internal capacity is constrained by increasing market demand
- Internal manufacturing or service performance is insufficient or does not meet requirements
- Regulatory, Legal or Environmental

IT Outsourcing : Examples

- Data center operations outsourcing
- Help desk outsourcing
- Desktop support outsourcing
- Application development outsourcing
- Application maintenance outsourcing
- Database administration outsourcing
- Website or e-commerce systems outsourcing
- Data network operations outsourcing
- Disaster recovery services outsourcing
- IT security outsourcing

Business Process Outsourcing

- BPO is outsourcing of business function
- To achieve various benefits such as cost saving, better quality and able to focus on core competency.
- BPO involves outsourcing processes that are not core to a company.

BPO Evolution

- 1960s Time Sharing
- 1970s Data Processing
- 1980s Entire IT Operations
- 1990s Shared Business Services
- 2000s B2B partnerships via Internet
- 2000s Process outsourcing via Internet
- 2000s IT-Enabled offshore services

Drivers of BPO

- Advantages offered by outsourcing are valid for BPO as well
- Robust IT and telecommunication infrastructure
- Pressure to lower cost
- Little infrastructure for automation

What constitutes BPO?

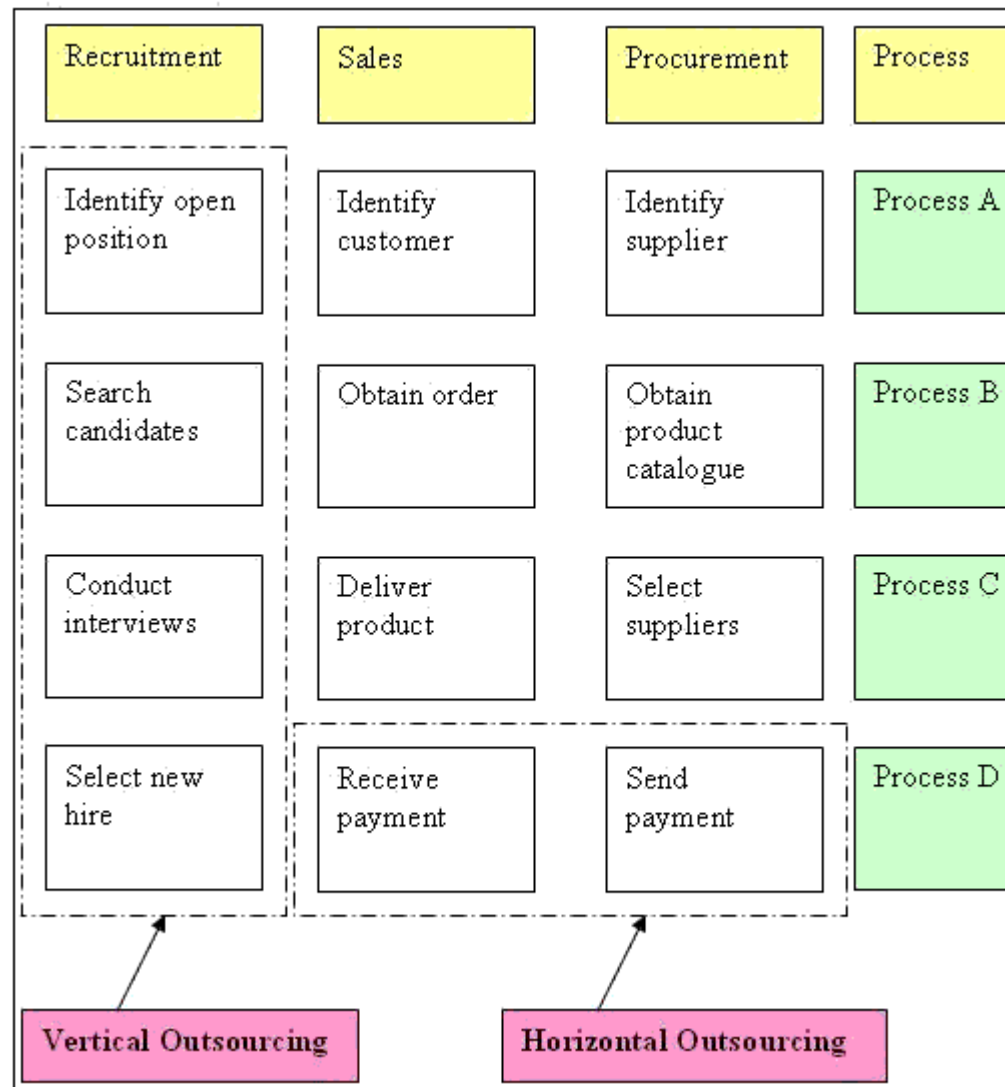
- Administrative support
- Customer relationship management
- Document processes
- Finance and accounting
- Human resources and training
- Intellectual property research and documentation
- Legal service
- Medical transcription

What constitutes BPO? (cont.)

- Payroll maintenance and other transaction processing
- Product development
- Publishing
- Research and analysis
- Sales and marketing
- Security
- Supply change management

Types of BPO services

- Horizontal BPO
 - Involves function centric outsourcing
 - Vendor specializes in carrying out particular function across different industry domains
- Vertical BPO
 - Focus on proving various functional services in a limited number of industry domains.



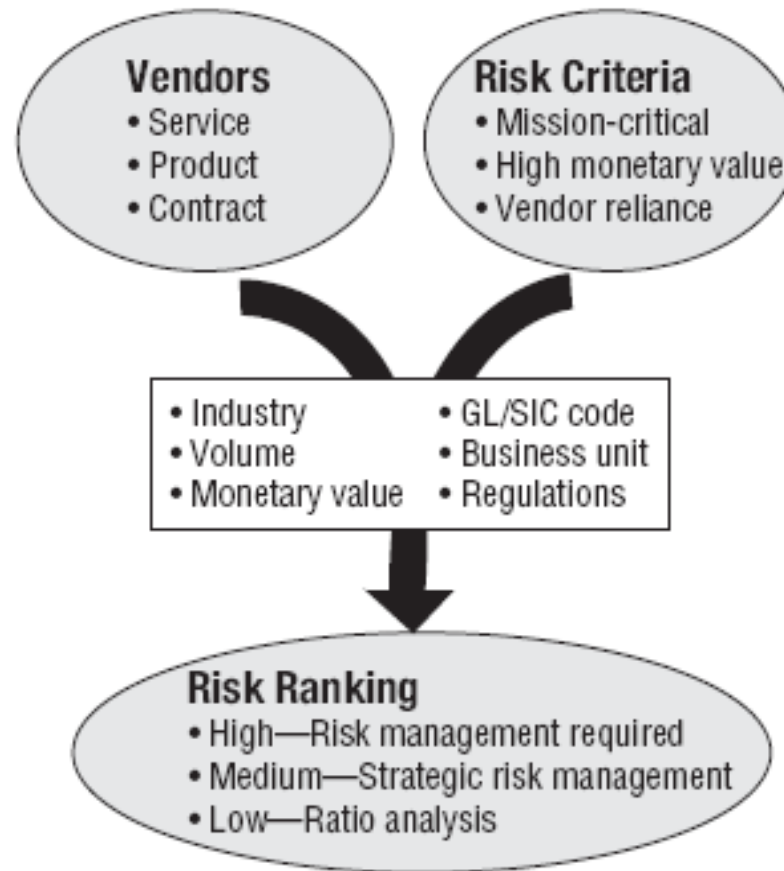
Source :BPO The purcursor of digital farm

Managing Risk

Risks of outsourcing

- Loss of control and excessive dependence on the vendor
- Financial instability of the vendor
- Loss of Expertise
- Potential risk of IPR theft
- Data security
- Regulatory obligations still responsibility of company
- On-time delivery performance and end-customer satisfaction levels may decline because of delays at third parties.

Risk Analysis Process



Source :Information System Control Journal, Vol 5, 2005

Generic Risk Management Model



Source :Information System Control Journal, Vol 5, 2005

Provider Selection Risk

- Identification of best provider/sources
- Comprehensive request for proposal (RFP) and request for quote (RFQ)
- Provider financial viability
- Technical evaluation
- Third party risk analysis

Common Challenges

- Understanding the hidden risks
- Meeting operational performance targets
- Achieving end-user satisfaction
- Achieving the promised cost savings

Reasons for Failure

- Outsourcing a function that is strategic or broken
- Lack of understanding of the total cost structure, value improvements or savings, and/or avoidance
- Misunderstanding the service levels
- Strategic sourcing process not effectively employed
- Contract management process not used
- Upfront risk assessment not performed

Practical Outsourcing

What should we outsource?

- Considerations in outsourcing
 - The company's core competency 82%
 - Quality of product or service 77%
 - Cost of internal vs external 72%
 - Need for specialized capability 64%

Decision : IT Outsourcing

- When do the benefit of outsourcing outweigh the risks?
 - 1. Position in the strategic grid
 - 2. Development portfolio
 - 3. Organizational learning
 - 4. A firm's position in the market
 - 5. Current IT organization
 - 6. Make, Buy, Outsource
 - 7. Sourcing Strategies
 - 8. Resource dependence theory

High

Outsourcing

Current Dependence on Information

Factory-uninterrupted service-oriented information resources management

Outsourcing Presumption: Yes,
unless company is huge
and well managed

Reasons to consider outsourcing

- Higher -quality services and backup
- Management focus facilitated

Strategic information resources management

Outsourcing Presumption: No.

Reasons to consider outsourcing

- Rescue an out-of-control internal IT unit
- Tap source of cash
- Facilitate cost flexibility
- Facilitate management of divestiture

Support -oriented information resources management

Outsourcing Presumption: Yes.

Reasons to consider outsourcing

- Access to consider IT professionalism
- Access to current IT technologies
- Risk of inappropriate IT architecture
- reduced

Turnaround information resources management

Outsourcing Presumption: No.

Reasons to consider outsourcing

- Internal IT unit not capable in required technologies
- Internal IT unit not capable in required project management skill

Low

Importance of Sustained, Innovative Information Resources Development

Decision : IT Outsourcing

- Development Portfolio

- The higher the percentage of the systems development portfolio in maintenance or **high-structured projects**, the more the portfolio is a candidate for outsourcing
- Outsourcers with access to high-quality, cheap labor pools (e.g. in Russia, India or Ireland) and good project management skills can consistently outperform, on both cost and quality, a local unit that is caught in a “**high-cost**” geographic area and lacks the contacts, skills and confidence to manage extended relationship
- The growth of global fiber-optic networks has made all conventional thinking on where work should be done obsolete
 - Research have pointed out that more than 150,000 programmers are working in India on software development for US and European countries
- Large, low-structured projects pose very difficult coordination problems for outsourcing.

Decision : IT Outsourcing

- Organizational Learning

- “Many times people will change just the structure and the reporting relationships. But if you want to change a company, you’d better change more than that. There’s the formal structure and then there’s the way the company really works. You have to change the way it really works” *Allaire Xerox CEO 1992*

- The more experience the firm has had in implementing redesign the easier the outsourcing will be
- Process reengineering seeks to install very different procedures for handling transactions and doing the firms work. Responsibility for such development work (low structure by its very nature) is the hardest to outsource.
- A significant component of many firms’ applications development portfolios comprises projects related to business process reengineering or organizational transformation.

Decision : IT Outsourcing

- A Firm's Position in the market
 - The further a company is from the network era in its internal use of IT, the more useful outsourcing can be to close the gap
 - Firms still in the DP era and early micro era do not have the IT leadership, staff skills, or architecture to move ahead
 - The outsourcer, by contrast, cannot just keep its old systems running, but must drive forward with contemporary practices and technology.

Decision : IT Outsourcing

- Current IT Organization
 - The more IT development and operations are already segregated, in the organization and in accounting, the easier it is to negotiate an enduring outsourcing contract.
 - A stand-alone differentiated IT unit has already developed the integrating organizational and control mechanisms that are the foundation for an outsourcing contract.
 - Separate functions and their ways of integrating with the rest of the organization already exist.

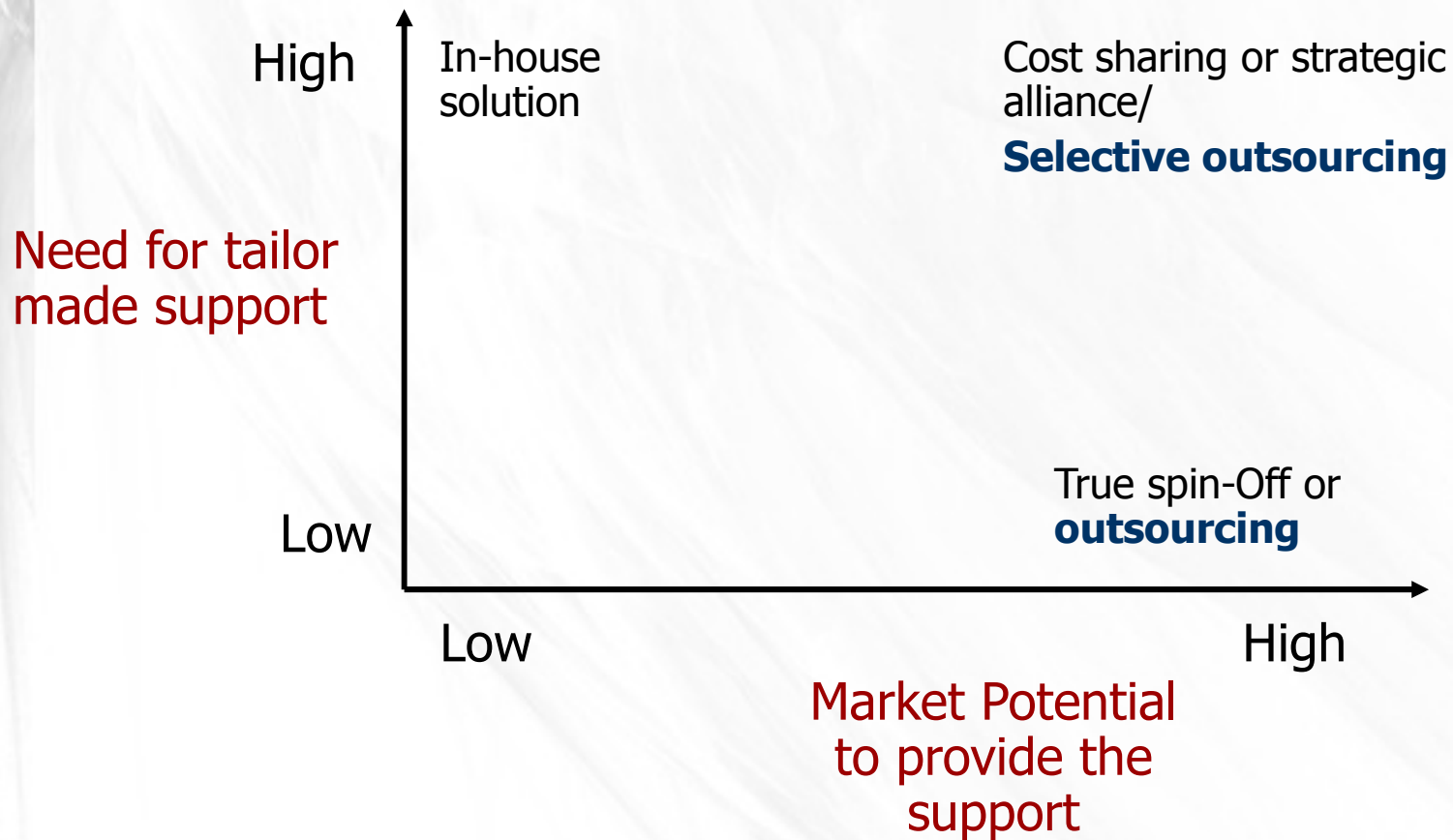
Make, Buy or Outsource

Rands (1993)

Company's Skills Related to Best External Source

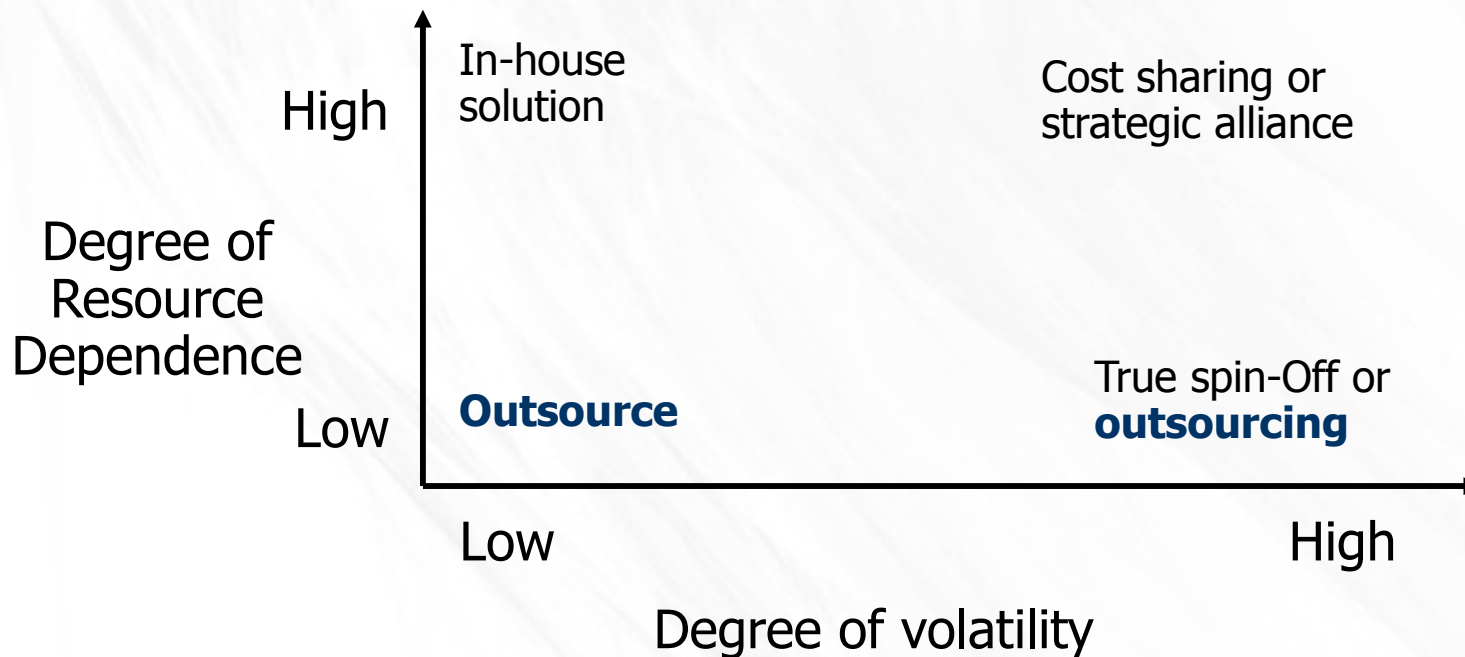
		Low	Equal	High
Strategic Importance	Low	Buy/Outsource	Make or Buy/Out.	Tend to make
	High	Strategic Alliances	Tend to make	Make

Sourcing Strategies

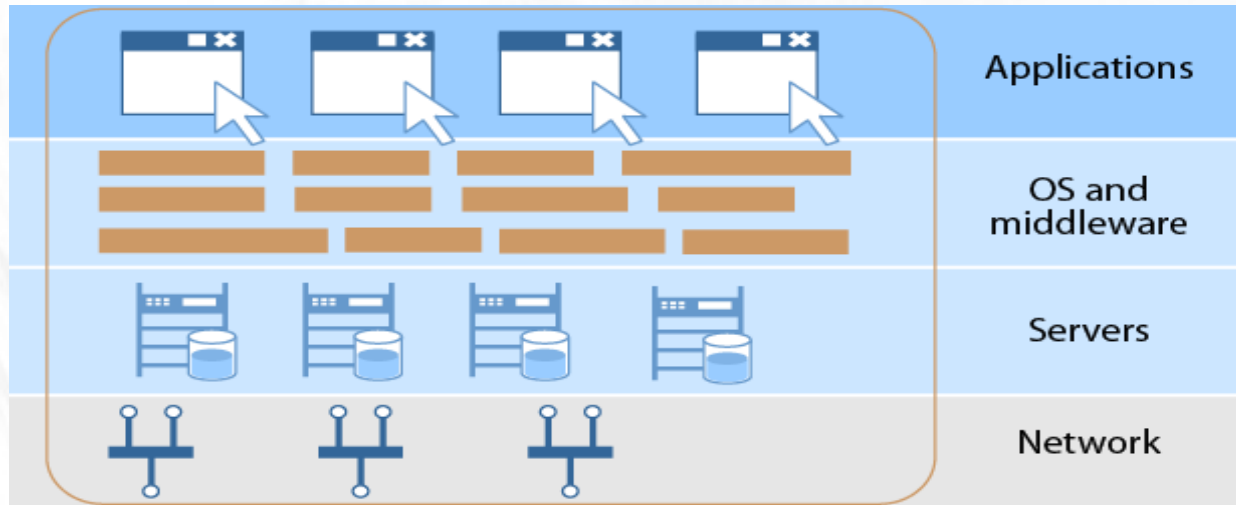


Resource Dependence Theory

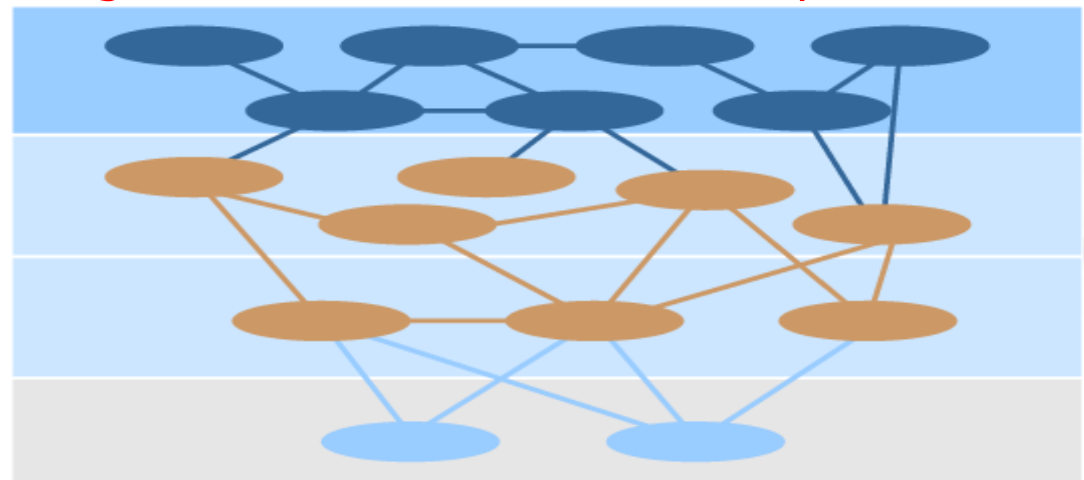
Strategic Choice Framework for the IT Professional Resource



Companies Suffer Without A Systematic Outsourcing Approach



Fragmented Outsourcing Contracts Constitute A Complex Puzzle



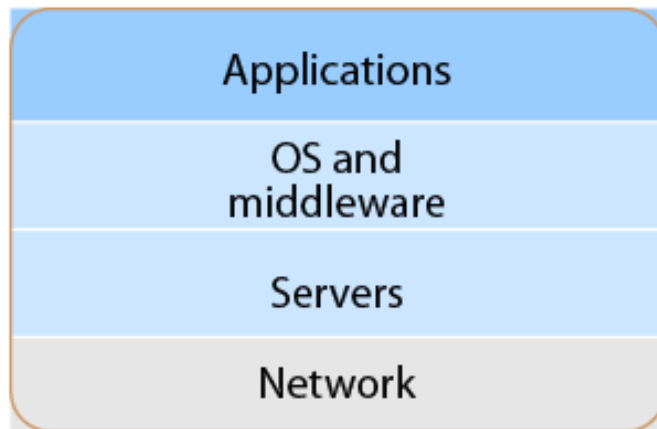
Source: Forrester Research, Inc.

Integration Methodology for Outsourcing

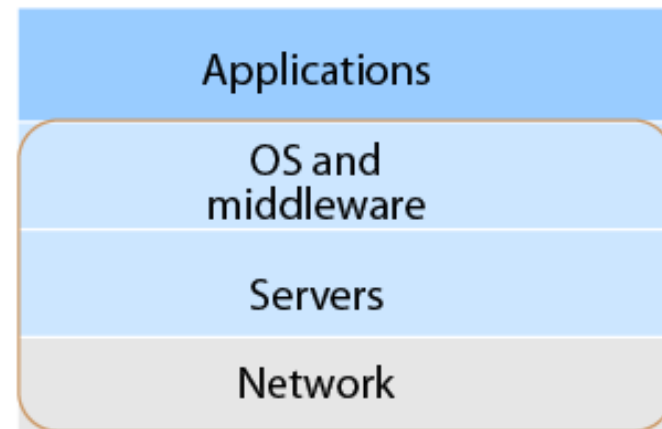
- 6 Basic Sourcing Models Cover Most Situations
- 3 Steps To Defining A Strategic Approach To Outsourcing
- IT Centralization & IT Archetype Shape Basic Options
- How A Typical Company Managed Forrester's Three-Step Methodology
- Select Sourcing Models That Fit Your Foundations

Six Basic sourcing method

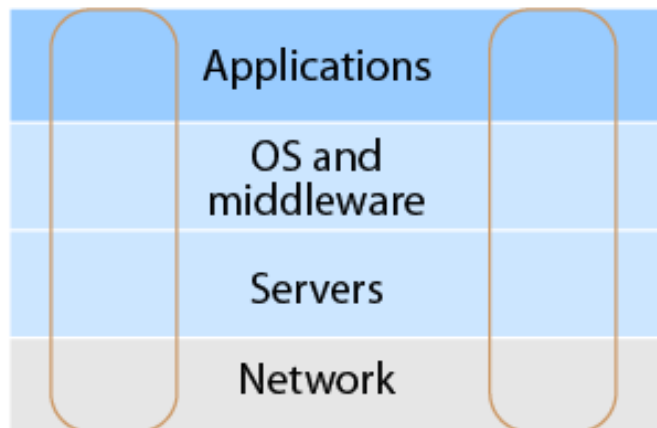
Model 1: Global outsourcing



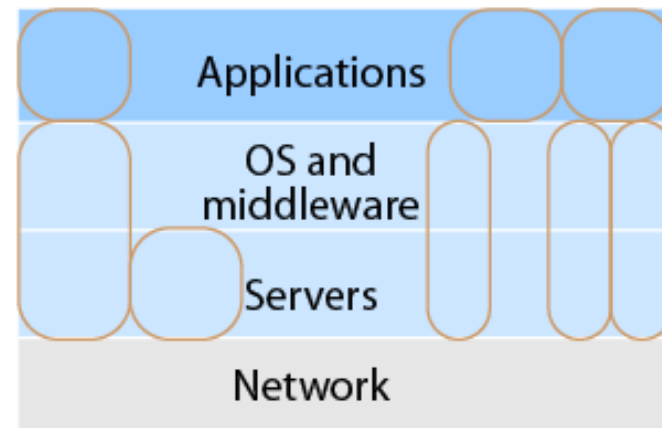
Model 2: Infrastructure outsourcing



Model 3: Vertical outsourcing



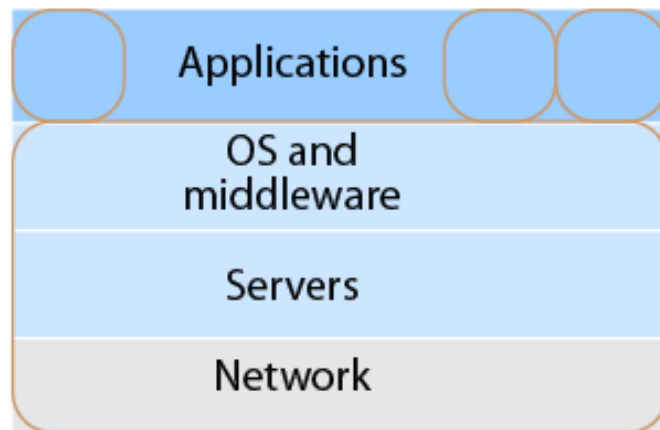
Model 4: Best-of-breed outsourcing



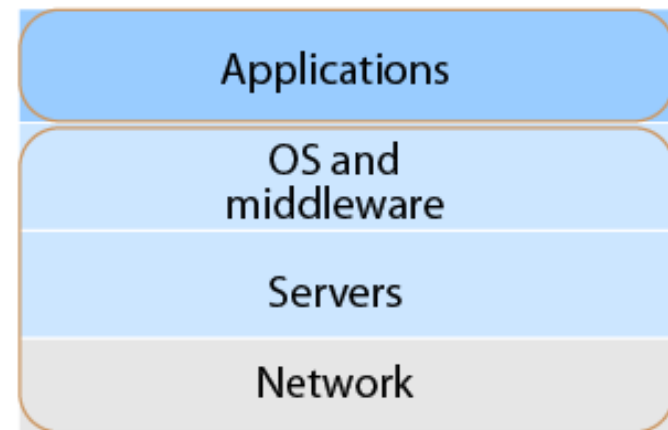
Source: Forrester Research, Inc.

Six Basic sourcing method

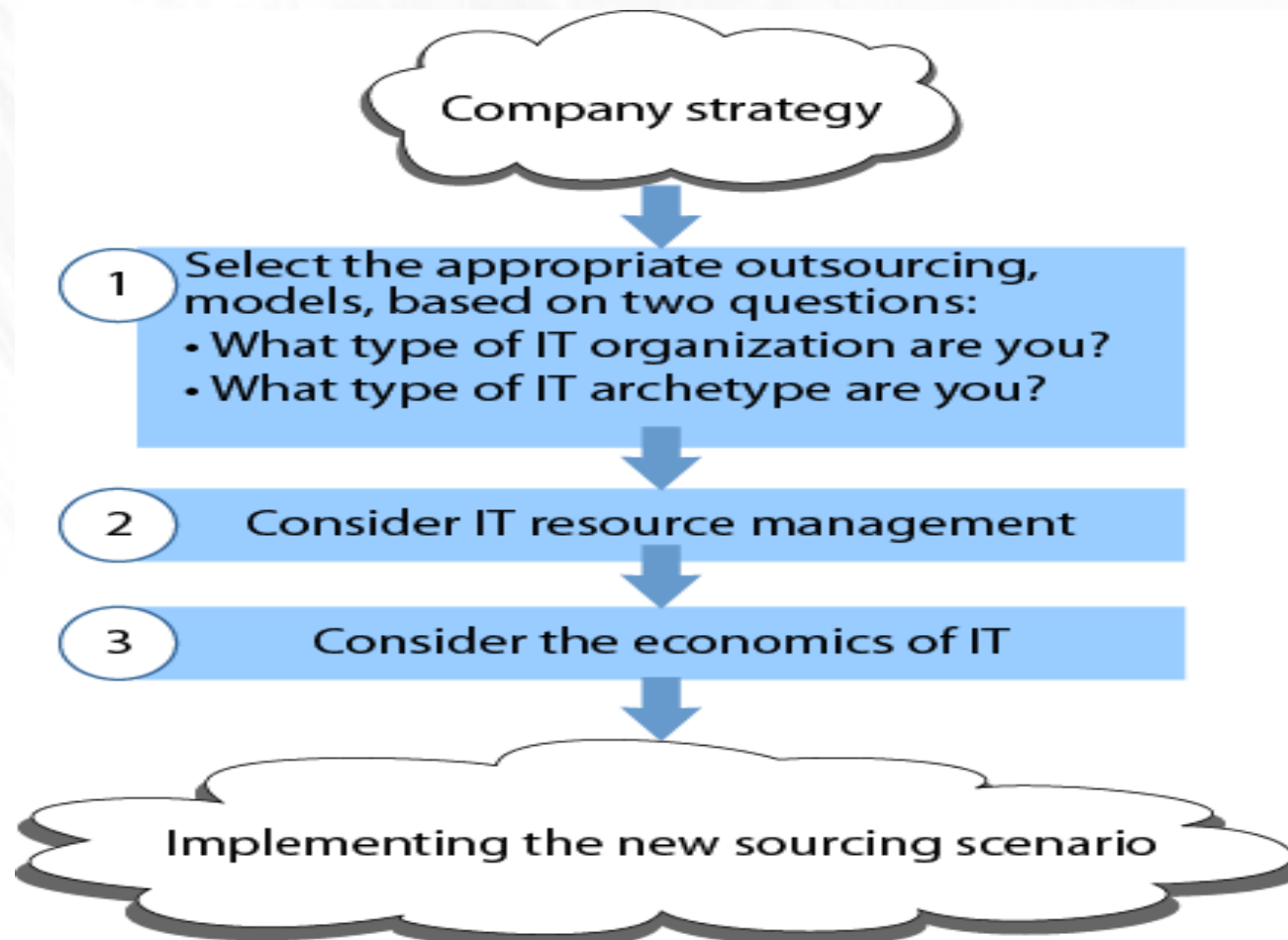
Model 5: Infrastructure and vertical applications



Model 6: Horizontal outsourcing



Defining A Strategic Approach To Outsourcing Approach

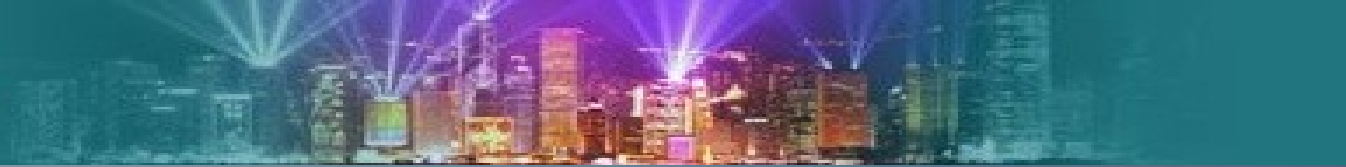


Source: Forrester Research, Inc.

Select Sourcing Model That Fit Your Foundation

		IT organization		
		Centralized IT	Decentralized IT	Federated IT
IT archetype	Solid Utility	Model 3 (possibly 2, 5, 6)	Model 3	Model 3 (possibly 5)
	Trusted Supplier	Models 2, 3, 4, 5 (possibly 6)	Models 3, 4	Models 3, 4 (possibly 2, 5)
	Partner Player	Models 1, 2, 5, 6	Model 3 (2 when common infrastructure)	Model 3 (possibly 2, 5)

Source: Forrester Research, Inc.



IT Outsourcing of Cathay Pacific





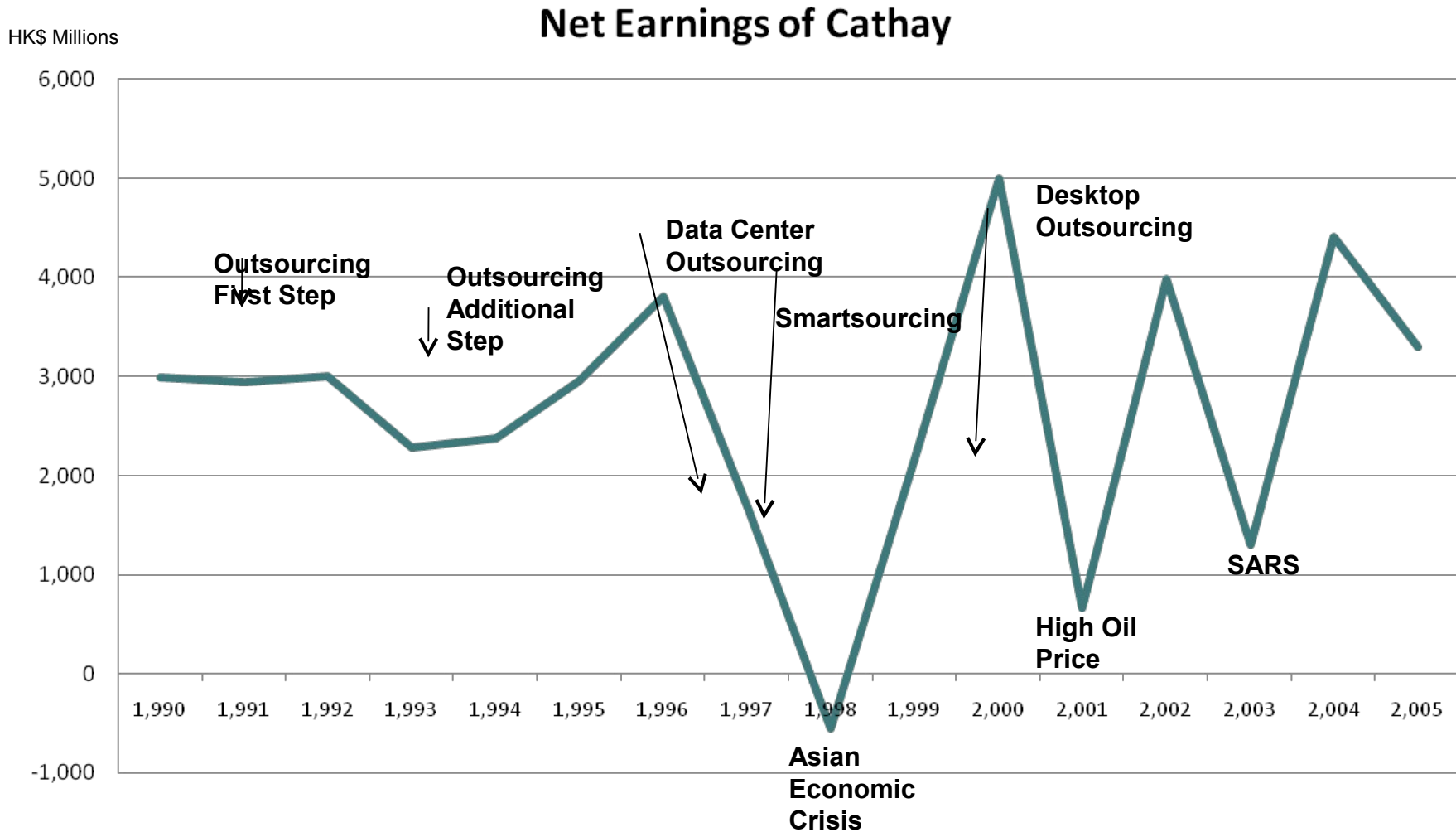
The Company Profile

- Founded in 1946
- First connection between business and IT in the 1970s
 - Adopted the cutting edge technology developed in-house
- Today,
 - Revenue HK\$75,358 million, Net earnings HK\$7,023 million
 - World's 7th most profitable airline and the 18th largest airline
 - 1.28 million passengers every month
 - 17,996 worldwide staff
 - 118 destinations in 37 countries



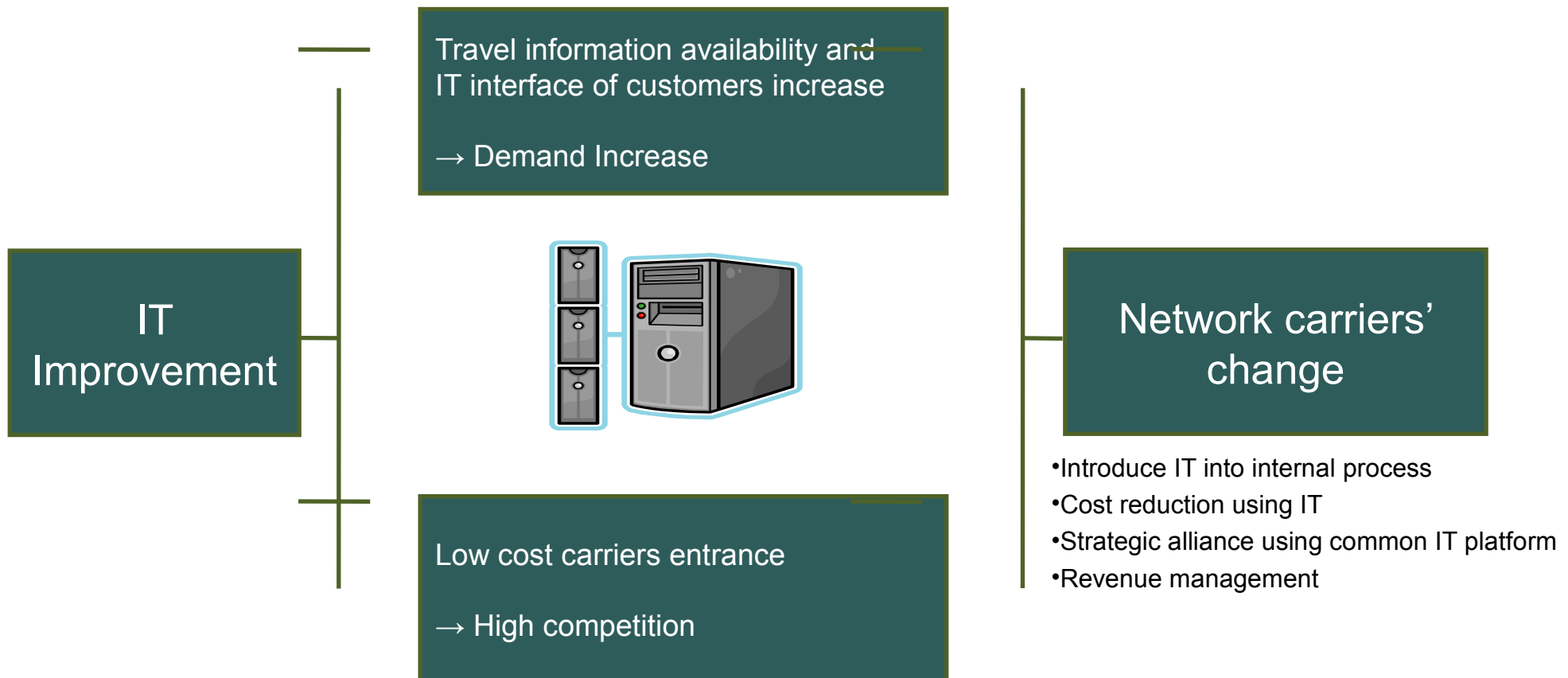


Financial Performance



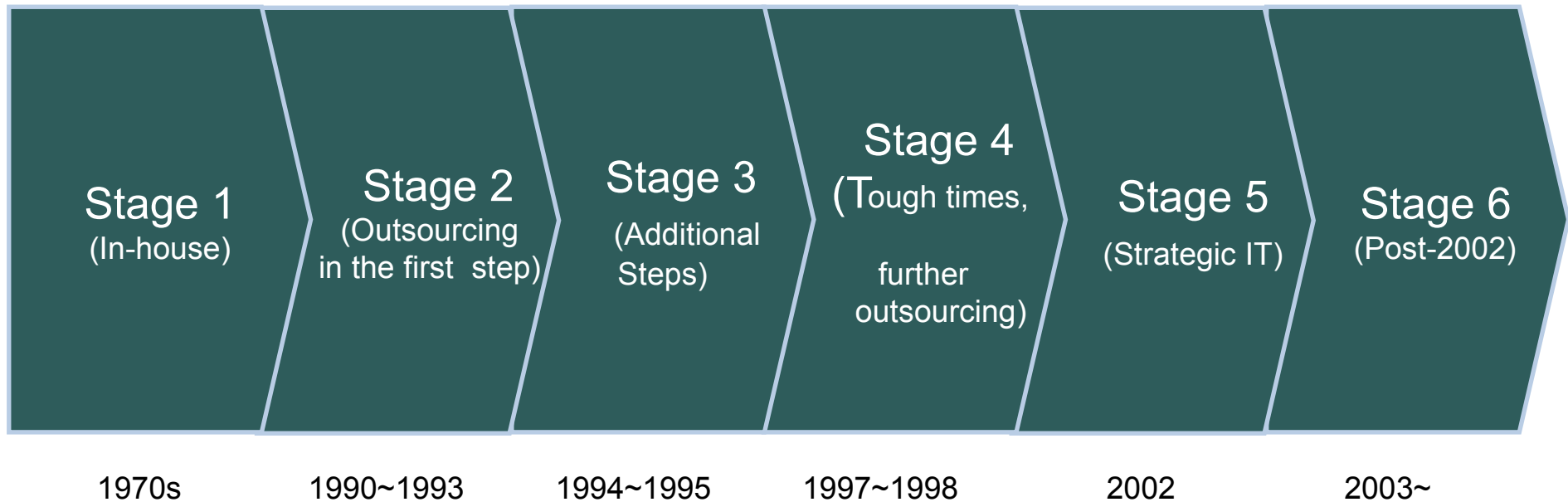


Airline industry and IT





Outsourcing history overview





Outsourcing history - Stage 1

In-house IT service



- Developed most of its systems in house
 - Accounting systems, Engineering systems, Personnel systems, and Flight systems, etc.
 - IT staffs: 30 in 1970 → over 400 by the mid-1990s
- Highly, vertically integrated
- Extremely high cost of maintaining data centers



Outsourcing history – Stage 2

Outsourcing in the first step

- A critical approach to cutting costs
- Nonstrategic functions outsourcing
- “Systems Development and Support” → “Systems Delivery”
- Outsourced its networks to SITA

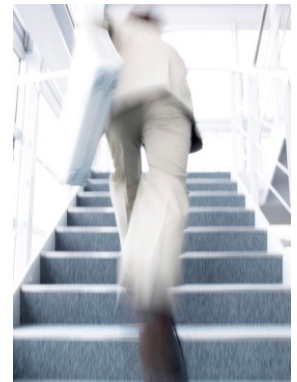




Outsourcing history – Stage 3

Additional Steps

- From 1994 to 1995, a new general manager of IM
- Outsourcing was no longer questioned
- Operating principles of IM's new IT ideology:
 - Acquire and manage rather than develop and operate
 - New vendor strategy



Outsourcing history – Stage 4

Tough times, further outsourcing

- From 1997 to 1998, Economic difficulties
 - Hong Kong's 1997 handover to PRC rule
 - Asian economic crisis
- Drive Cathay to further outsourcing



Outsourcing history – Stage 4 (Continued)

Smartsourcing

- Two fronts, infrastructure and airline application
- Why:
 - Strategic suppliers that could fulfill the company's burgeoning IT needs
 - Move from fixed cost to variable cost
- What:
 - IBM, IT infrastructure management and industry best practice
 - Sabre Airline Solutions, its application portfolio



Outsourcing history – Stage 4(Continued)

▪ Data Center Outsourcing

- Contract

- Absorb all of the Cathay data center staff
- Fee structure : 10% to 15% below in-house cost
- As good or better services

- Governance

- Integrating meeting
- Assessed IT operations and projects on a regular basis

▪ Desktop outsourcing

- Nonstrategic IT resources





Outsourcing history – Stage 5

Strategic IT

- In 2002, still a significant portion of its IT in-house
 - IT planning and architecture
 - Internally developed legacy system
 - Project management and systems implementation
 - Support of the 3200 outport workstations located worldwide
- However, implementing best-practice purchasing process





Outsourcing history – Post 2002

- **IM Excellence:**
 - Urgency: respond rapidly to business requests
 - Transparency: IM transparent to users
 - Simplicity: simplifying the complex infrastructure
- **IMFit:**
 - Moving from proprietary network to open IT
 - Eliminating redundant service from existing contracts
 - Holding staff headcount constant



New EVOLVE IT Strategy

Replaced the 10-year-old Smartsourcing IT Strategy

Remain reliability, flexibility, and cost, and focus on creating additional value to the business

- Support business strategy development
- Create and deliver business value solutions
- Run reliable, flexible, and cost effective business

applications



General pros and cons of outsourcing

Pros	Cons
<ul style="list-style-type: none">• Corporate resources can be focused on core function• Financial risk from high fixed assets (facilities and labors) can be reduced in vulnerable business environment• Fixed costs can be changed into variable costs	<ul style="list-style-type: none">• Outsourcing results in low competitive advantages in core sectors• Outsourcing makes it difficult to create the innovation and improve the technology• Risks to heavily depend on external company about corporate destiny



Evaluate Cathay's IT outsourcing Strategy

- A slow process, but with rapid growth
 - Under competitive pressures, and turbulent economic conditions, it became crucial for the survival of the company
- Cautious approach + Deep researched + Determined implementation
 - Cathay began with the areas that were not directly associated with the core business, but were necessary in the support roles. These were the “low hanging fruit” and easy to implement



The strengths of IT Strategy

- Identifying business process areas
- Dividing the Information Technology function between infrastructure and applications
- Searching the best suppliers to maximize the needs
- Identifying strategic partners that could successfully deliver solutions
- continually managing and maintaining contract relationships



Risks and Disadvantages

- Exposing Cathay Pacific to unnecessarily excessive expenditures (smart sourcing contract)
- Cathay Pacific has essentially foregone the opportunity of providing data services to other industries due to human IT capital transfers to IBM



How could Cathay have done differently?

- Train the procurement staffs on how to bid and manage an outsourcing contract, OR
- Hire new procurement staffs with extensive outsourcing experience
- Setup a core outsourcing team
- Develop a competitive pricing process to ensure the outsourcing costs

Resources

- IT Outsourcing of Cathay Pacific; *Kimmy Chen et.al.*
- Practical Outsourcing What, Why and How... *An Op2i Perspective, April 2008 (www.op2i.com)*
- Business Process Outsourcing,
<http://www.tutorial-reports.com/book/print/298?PHPSESSID=faaf736>
- Outsourcing -A Risk Management Persepective, *Nicholas A. Benvenuto, Information Systems Audit and Control Association*

Thank you

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