

## View Point



### Leveraging Outsourcing during Economic Uncertainty

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#### Abstract

The fears of a looming economic crisis have put business decisions under a scanner. Whether the economy is headed for a full-fledged recession or not, might still be debatable. However, this period of uncertainty has given an opportunity for organizations to improve their business models and develop strategies that are more rational, prudent and better aligned with market realities. In these trying times, outsourcing is proving to be a great enabler.

Many organizations have realized that outsourcing initiatives, if properly executed, can help them deal with economic uncertainties better. IT and Business Process Outsourcing, earlier mainly seen as means to cutting costs, are today known to offer much more in terms of benefits. The Global Delivery Model (GDM) provides an organization with far more flexibility and scalability. Overall productivity and efficiency also increases as a company can focus better on core areas.

Not so surprisingly therefore, the economic downturn of 2001-02 had, in fact, provided a huge stimulus to outsourcing. As customers demanded more in terms of cost savings, service providers were forced to develop more innovative solutions. They expanded their boundaries across new locations and built new capabilities that could add more value to their clients. Thanks in part to the burst in outsourcing activity initiated in that period, the outsourcing industry has now expanded its range of services. It can now contribute better to the overall growth of organizations in a number of ways, thereby helping them deal with economic uncertainties.

A more mature approach to global sourcing and lessons from the past experiences can go a long way in dealing with the brewing recession. This paper examines how organizations can leverage global sourcing to their advantage in the current economic scenario. It provides a framework to understand how the key attributes of global sourcing can be used to manage uncertainty.

## Era of Uncertainty

Rising inflation, the tumbling dollar, the housing crisis, higher unemployment and the huge credit defaults that have impacted economies and consumers worldwide are all ominous signs of global economic downturn. From financial markets to the Federal Reserve in the US, political leaders to the common man, everyone has been in a state of panic. As the world is becoming flat and the global economy is getting more and more interdependent, the tremors of the downturn are being felt almost everywhere. While economists are divided in their opinion on how bad and how global the impact of this looming recession can be, the warning signals are enough to set an alarm across the industry and lead to an uncertain business environment.

Though shifts at the macro-economic level might seem far away, they affect business and even IT decision-making. When companies enter an industry downturn, managers at all levels exhibit similar behaviors in avoiding or denying the imminent budget cuts. Despite the slowdown, many companies continue with their IT projects as if it were business-as-usual. Even if managers and executives could take early steps to prepare for a budget cut, they often neglect to do so. Eventually IT managers are either forced to cut costs or reduce fixed costs wherever possible. Soon after, lines of business also make similar cost adjustments. If the economic situation becomes more severe and IT departments have not made the necessary shift in spending, managers could lose control or be forced to delay or cancel programs.

These stages are familiar to IT professionals who lived through the last economic slowdown in 2001-02 and are going through one now. However, lower budgets, if planned properly do not always result in complete loss of control. Economic uncertainty can become a strong opportunity to transform IT departments. A strategic outsourcing program can not only stretch the dollar in tight budgetary environments, but also create new dollars with which companies can pursue other pressing initiatives. Global sourcing efforts can help companies realign themselves with current market realities. The historical example of the 2001-02 recessions demonstrates the advantage companies can gain from thinking strategically about their approach to outsourcing.

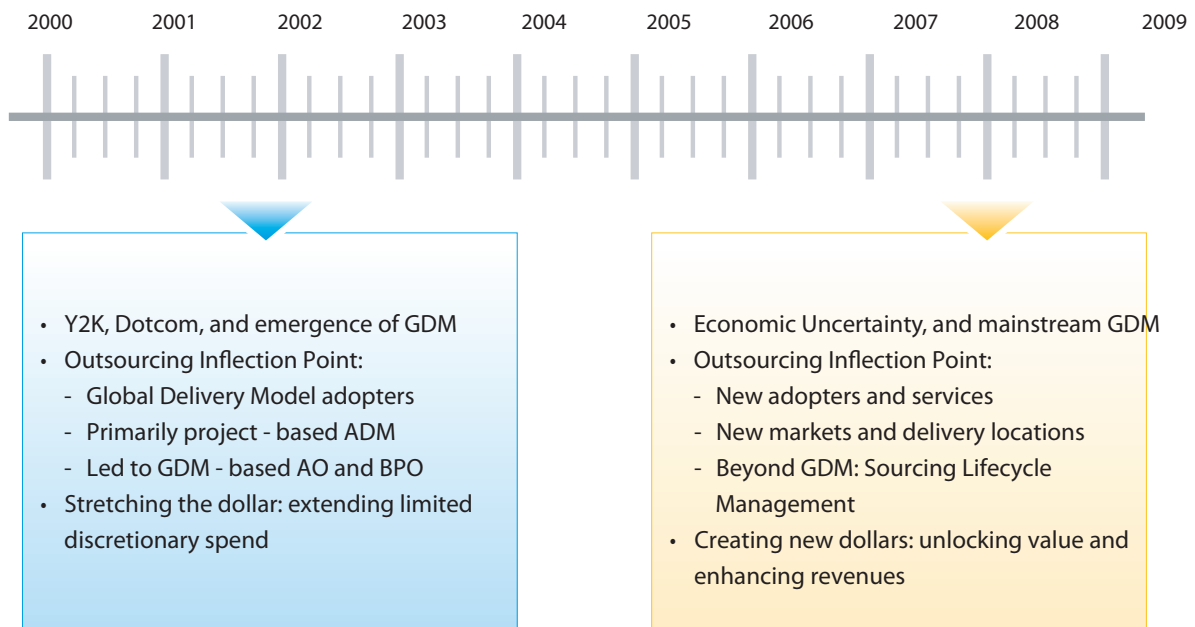
## Evolution of Outsourcing through the Key Inflection Points

The ups and downs of the global economy have been powerful contributors to the evolution of outsourcing. The previous economic slowdown that occurred in 2001-02, proved to be a major inflection point for outsourcing IT services. The uncertainties created by the Y2K and the dotcom crisis were instrumental in pushing forward the growth of the IT services industry. There were pressures to deliver and squeeze more value from every dollar that was invested. Service providers responded by honing their skills and expanding their portfolio of services; consequently outsourcing evolved into a much stronger and dependable service for businesses.

The emergence of GDM initially provided companies with new methods for reducing **costs**. The outsourcing of simple application development and maintenance to emerging economies dramatically lowered the fixed costs of IT departments. Global sourcing and GDM also gave organizations a wider choice in terms of **capabilities** across multiple locations. Rapidly evolving technologies meant that it was difficult to find relevant expertise within a company's IT department. Outsourcing providers could offer knowledge and resources, that companies lacked, or did not have the time or budget to acquire. In its early stages, the GDM focused mainly on reducing costs and improving efficiencies within IT and certain basic business processes. The effort was aimed at 'stretching the dollar' or extracting maximum value from every investment that was made.

The 2001-02 downturn, was an inflection point in the history of outsourcing. GDM has become mainstream in the Outsourcing space. Companies have begun to understand and take a more mature approach to outsourcing. No longer seen as either a risky proposition or low-skill venture, providers are brought in to handle some critical business functions and processes.

In the many years since the previous economic slowdown, outsourcing services and delivery models have evolved to encompass even more advanced **capabilities**. GDM has already been accepted as a given and organizations are now taking a more strategic view of their global sourcing initiatives; coinciding with the inflection point during the 2007-08 economic downturn.



## Inflection Points for Global Sourcing

While the initial goals of outsourcing programs were **cost** and **capabilities**, mature outsourcers discovered two more: outsourcing has enabled companies to enhance their **competitiveness** and drive transformational **changes**. Global Sourcing initiatives have today become far more pervasive and wider in their reach. The distinction between Offshoring and Outsourcing has evaporated - it is all about Global Sourcing now!

From R&D and Engineering Services to Lifecycle Management Solutions, companies are entrusting service providers with more upstream and strategic functions. The integration of IT and BPO services has also provided customers with more choice in aligning business with technology. A whole new range of services -- SaaS, remote asset-light Infrastructure Management, Agile IT, Learning Services, Legal Process Outsourcing (LPO) etc - are being offered under the sourcing umbrella. The plethora of options has added to the complexities of global sourcing, but the opportunity to extract more value is that much greater. The emphasis has moved beyond 'stretching the dollar' to 'creating new dollars' by unlocking more value and enhancing revenue.

Service providers have expanded their operations to many new markets and low-cost delivery locations such as Latin America, Eastern Europe and China. As a result more companies, including small and medium size firms, are embracing global sourcing in a big way. Developing economies such as India - which were mainly seen as delivery locations earlier - have now come up as major markets for these services. As service providers have proven themselves and gained more confidence, even large organizations with their own captive offshore centers are willing to divest their captives and shared service centers. Volume and scale were important during the last inflection point and they continue to be so now; but, the current era of global sourcing is also about differentiation and focus.

## Dealing with Uncertainty - The Opportunity beyond Cost Reduction

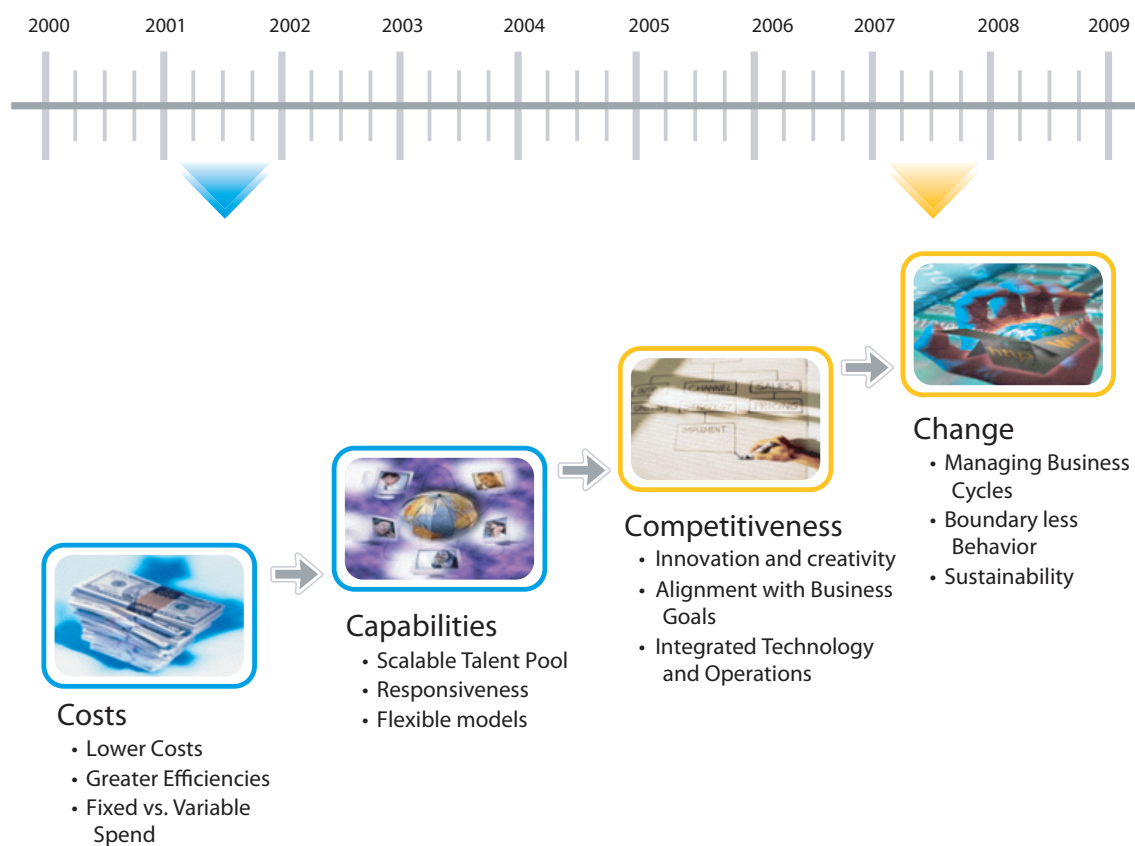
It is obvious that most of the attention during a downturn is on managing costs. Managers would remember from the economic downturn of 2001-02, that drastic and ad hoc budget cuts forces the abandonment of several strategic programs. This results in significantly lower levels of operational and IT capabilities in the organization and a lack of preparedness when the economy turns around and new market opportunities emerge. However, successful managers are able to justify investment in programs that give the companies an edge over competitors coming out of a recession. For instance, despite the economic uncertainty at the beginning of the decade, DHL transformed itself from a single data-center model to a global operating model with IT centers across multiple locations in strategic time zones. This enabled the company to develop new products and quickly launch them simultaneously in many countries. Once business picked up in 2003, it gained significant global market share over competitors. Apple, Amazon and Walmart are frequently cited examples of companies that continued investing through the downturn to come out stronger while other competitors were slow in responding to

the resurgent market. The emergence of leading India-based companies into the top tier of the Consulting and Outsourcing landscape (previously dominated only by US-based majors) is another example of how investing in building expertise and in sales and marketing activities can lead to huge gains in market and mind share as the economy picks up.

To see economic uncertainty as an opportunity, it is crucial that business and IT managers have a strong handle on costs. At the same time, these decision-makers must also have the ability to respond strategically to budget cuts without compromising on current capabilities of the organization or putting future competitiveness at risk. It is in this context that companies should look at how global sourcing can play a role in not only managing costs in the short term, but also in providing the agility to invest for future competitiveness or change.

## 4C Framework for Global Sourcing

The 4C Sourcing Framework uses Costs, Capabilities, Competitiveness and Change as the basis for defining and deploying a sourcing strategy to deal with economic uncertainty. As outlined in the previous section, these 4 Cs played a key role in the evolution of outsourcing through the past decade. This 4C framework also applies to companies with current sourcing programs. It serves as a means of reviewing and refining programs to better deal with upcoming downturns or business cycles.



### Costs

A strong handle on costs is the first competency in dealing with an uncertain economic environment. Outsourcing is a proven approach for companies to reduce and manage costs in IT or specific business processes. Taking an enterprise-wide view of sourcing assets is critical for realizing the full potential of cost savings, starting with removing redundancies in processes and assets, and leading to the identification of opportunities for shared costs and resources across the organization. The principle of Modularity can help separate and convert fixed costs to variable costs in the sourcing portfolio. This is accomplished through scalability of capacity as well as asset transfers in an outsourcing arrangement. Different parts of the portfolio can be clustered and sourced for operational efficiencies with appropriate sourcing metrics and service level agreements.

In this context, the role of global delivery is to significantly enhance the cost management potential of a sourcing strategy. While cost savings may be the obvious benefit of global delivery, it is equally relevant in creating cost variability as well as improving operational efficiencies that companies desire in an uncertain economic environment.

## Capabilities

Even as cost draws the most attention, a smart sourcing strategy in an uncertain environment focuses on sustaining and enhancing the IT and operational capabilities of an organization. Loss of organizational capability can become a major deterrent for an organization to respond to a positive turn in the environment. The emphasis here is on scalability of sourcing assets and also scalability in access to talent. Similar to taking an enterprise-wide inventory of sourcing assets and costs, an enterprise-wide view of critical talent and operational assets is vital. Other important factors in the sourcing decision include creations of specific Centers of Excellence (CoE) within the organization (captive sourcing) or outsourcing to a vendor partner, and to optimally leverage global locations for specific skills. Typical service levels focus on talent scalability (both up and down), as well as responsiveness to changing demands due to an uncertain environment. The maxim to 'hire where the best talent is available and execute where it is most economical', has never been more apt than in a Global Sourcing context.

It has become all the more important for organizations to carefully define and plan for the kind of short- and long-term capabilities they wish to have and who might be the best sourcing partner (whether in-house or external) for achieving this. The acquisitions and integration activities that are prevalent in the business world today also point to an increased focus on Capability building that can help the organization be responsive and flexible. Strategic use of global sourcing is a key enabler towards these goals.

## Competitiveness

The definition of what is core and what is context is changing within organizations. Some decisions that may have been made a few years ago to set up their own captive (in-source) or shared services center may no longer be justifiable. A strong handle on costs and the assurance that an organization can sustain its capability through periods of uncertainty in the economy provides it with the ability to focus on future competitiveness. This in turn depends on defining the core and non-core assets in the enterprise sourcing portfolio and aligning them with business goals or objectives. Innovation and creativity are key to ensuring competitiveness.

Service levels in such outsourcing arrangements must emphasize innovation and creativity and are typically geared towards outcomes. A focus on future competitiveness and strong understanding of core and non-core enables organizations to adopt outcome-based sourcing models such as Software-as-a-Service (SaaS) or Platform-based BPO. These models inherently share the uncertainty and associated risks with the sourcing partner.

At times, companies incur a lot of wastage on large projects due to their misalignment with business goals and lack of integration across various functions. Such redundancies can also be contained with the help of strategic outsourcing. With integration in technology and emergence of boundary-less organizations, today it has become much easier to execute complex large-scale projects on a global scale.

One of the areas that are a key determinant in enhancing competitiveness is integrating technology and operations. Not only does integration allow for business alignment, it also allows for opportunities to generate new revenue and profit streams by making better use of the information across the organization.

## Change

The focus of organizations during an uncertain economic environment is typically only on the short term. However, drivers of change - including major disruptive forces in many industries - could all impact at the same time. These disruptive forces or change drivers vary from simple technology refresh cycles or business cycles to new technology enabled business models; they could be fundamental shifts in customer and consumer behavior to shifts in the customer base or globalization of the customer base. Especially in an uncertain environment, it is important that organizations do not lose sight of such forces but are constantly monitoring them. The opportunity to leverage them in a downturn can provide significant first-mover advantage.

4Cs / Sourcing Strategy Deployment	Think Enterprise	Structure Modular	Source Optimal	Act Global
Costs	Reduction & Sharing Opportunities	Clustering around Variability & Efficiencies	Optimization & Savings Criteria	GDM Leverage and Execution
Capabilities	Current Assets & Future Requirements	Clustering around Scalability & Specialization	Responsiveness & Flexibility Criteria	Location/Partner Choices & Transition Approaches
Competitiveness	Core and Context Redefinitions	Clustering around Differentiation & Integration Opportunities	Innovation & Outcome Criteria	Operational Alignment & Risk Mitigation
Change	Readiness & Maturity Assessments	Clustering around Transformation & Business Cycles	Sustainability & Collaboration Criteria	Boundary-less Behavior & Organizational Learning

### 4C Framework for Global Sourcing

*Think Enterprise, Structure Modular, Source Optimal and Act Global are the 4 stages in Sourcing Strategy and Execution within Infosys' MGS methodology*

There are several new imperatives for organizations that are driving change, not the least of them being the need to create sustainable business models using green policies. The globalization imperative is driving boundary-less behavior within organizations and forcing the knowledge workers to collaborate with virtual teams, share best practices, institutionalize learning, and lean more on partners. Even functions such as Product Design and Development - in the Electronics, Automotive and Aeronautics industries - are undergoing changes in the way they are executed.

All this is creating an impetus for organizations to work with sourcing partners who are not just capable of helping them with Costs, Capabilities and Competitiveness, but also be their trusted Change Agents in helping them successfully implement and internalize the change. Some organizations have managed to also involve their customers in driving such transformational changes to improve their products. For example, P&G's open innovation network, which includes customers, partners, and external services, produces 35% of product innovation. Sourcing Partners are ready to offer much more than their mainstream services. They are helping the organizations cope with change, training their far-flung workforce on the necessary capabilities, creating competency roadmaps and knowledge systems to further corporate goals, are just few examples of how service providers have risen in the value chain. A leading adopter of Global Sourcing - one of the largest financial conglomerates in the US - leverages its service provider's Outsourcing Academy program (conducted in India) for its managers to build capabilities needed on various aspects of Global Sourcing.

Strategic outsourcing also provides the requisite change management and transformational solutions to cope with changing market conditions. Most of the established service providers have also started providing solutions oriented for multi-vendor governance, green policies and sustainable outsourcing that can be used to take these initiatives to much greater heights.

### The Way Forward: Deploying the 4C Framework for Sourcing Strategy and Execution

A few years ago, Infosys had developed Modular Global Sourcing (MGS<sup>1</sup>) - our vision to sourcing strategy and execution - for outsourcing to have a wide reaching impact (not merely restricted to costs) across an enterprise. Applying the 4C Framework with Infosys' MGS methodology helps to deploy a sourcing strategy based on specific objectives, leveraging best-of-breed service provider capabilities and customized deal governance. Importantly, metrics, risk reward mechanisms and service level agreements can be designed based on cost, capability, competitiveness and change, the 4 Cs.

As the industry prepares itself to weather yet another economic storm, outsourcing can play a significant role. Past experience shows that outsourcing has been aggressively pursued by companies during economic downturns. However, the extent of benefits is dependent on organizational readiness and maturity as also the nature of outsourcing efforts. Companies looking for 'quick fix' solutions might need to modify their approach and take a broader and long-term view to their sourcing strategies.

The last few years have seen many organizations successfully leverage Global Sourcing to their advantage. The coming together of enterprise needs in this new era of uncertainty and the ever-increasing service provider capabilities could lead to a new wave in the evolution of outsourcing. A carefully planned sourcing strategy combined with an overall mature business approach could go a long way in dealing with the uncertain environment.

*Modular Global Sourcing (MGS1) is Infosys' framework for a mature sourcing strategy and execution. It distributes the enterprise portfolio in a modular manner to align with specific business objectives and based on client business drivers. Please refer to our White Paper "The Roadmap to Modular Global Sourcing" for more details. This sourcing framework pioneered by Infosys can be leveraged to optimize sourcing capabilities to master the Flat World Shifts. Please refer to our paper on "Mastering Flat World Shifts through Modular Global Sourcing" for more details.*

## Case Study

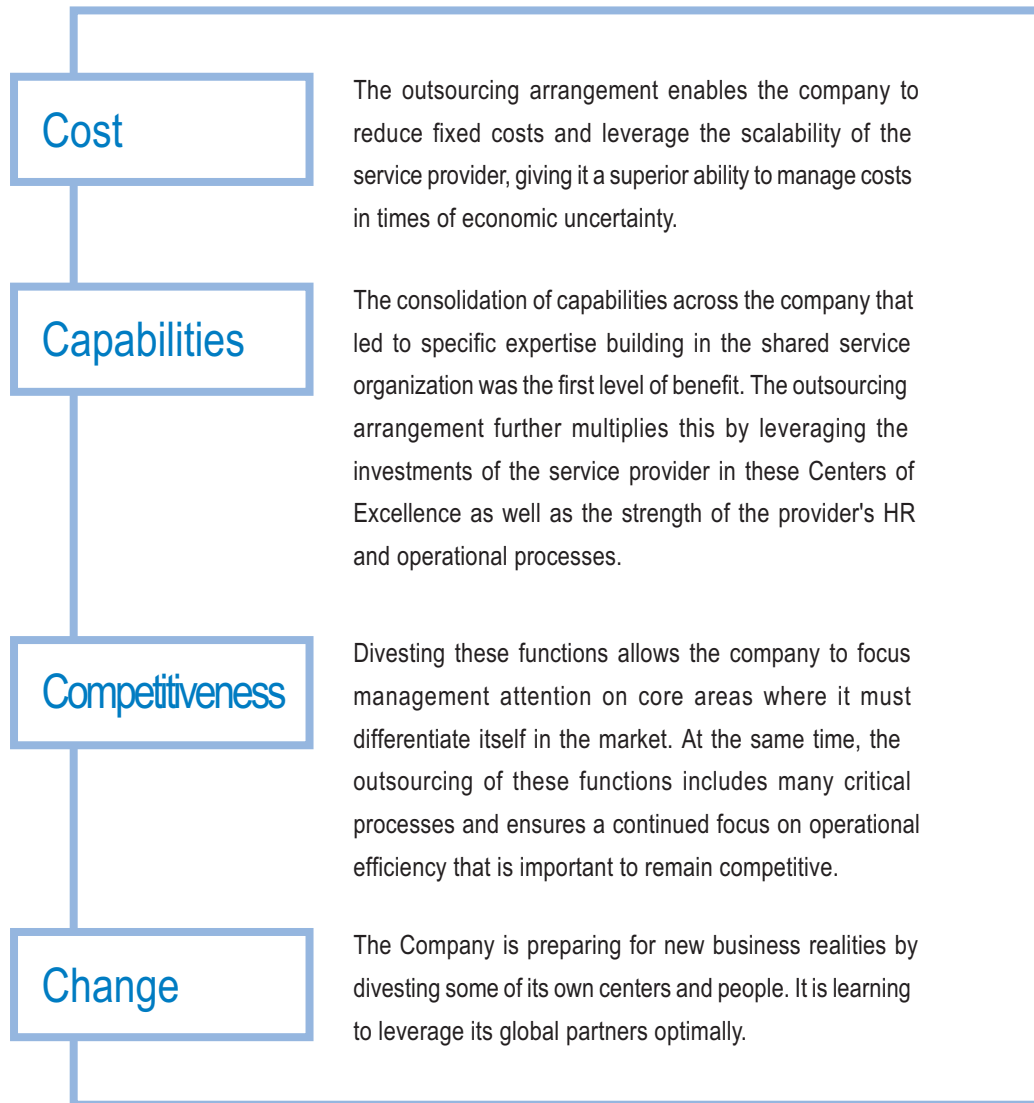
### Overview

The approach to outsourcing adopted by a global leader in electronics with operations spanning multiple geographies exemplifies the evolution of the outsourcing discussed here. The case study illustrates how the current era of outsourcing is about differentiation and focus, and traces the key steps of this approach to divest the majority of their back office operations through outsourcing.

### The Approach

- The first step taken was to consolidate all F&A functions across the globe into an internal shared services organization. The shared services organization was based out of three countries in Eastern Europe and Asia to optimize costs and talent availability, while supporting business operations across the globe
- The next step was to build specific expertise in the shared services organization, eventually creating internal centers of excellence for the company
- A key step in the redefinition of core and context was to outsource the functions in the shared services organizations to an external service provider while also leveraging the strengths and additional capabilities of the service provider
- F&A as well as non-product related transactional procurement BPO services were identified as the services to be outsourced. The shared services centers were transferred to the service provider as part of the arrangement

# Benefits



## About the Authors

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### About Infosys

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