WHAT TO CONSIDER WHEN OUTSOURCING IT AND NON-CORE OPERATIONS

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For decades, companies have outsourced many functions to reduce manufacturing and labor costs. Information technology (IT) outsourcing has allowed companies to quickly implement new technology and access talent for specialized areas such as cybersecurity, data analytics and mobile app development. Outsourcing enables company executives to remain focused on their core businesses with the assurance that non-core operations are being managed efficiently.

Outsourcing remains attractive for many companies because it offers several advantages in addition to cost savings, particularly in addressing talent gaps and shortages, exploiting Big Data capabilities and implementing new technology quickly.[1] Yet many companies struggle to transition their IT and non-core operations effectively to an outsourcing model.

THE HUMAN FACTOR

Outsourcing business functions, especially moving them overseas, can sometimes hamper morale and productivity in the workforce. Consulting firm Deloitte found that many companies focus on achieving cost savings, transitioning processes, and managing new outsourcing relationships, but fail to fully consider the personal impact of outsourcing on remaining personnel or on the company's recruiting efforts, corporate image and culture. If a company hopes to attract specialized talent, a reputation for outsourcing may make it less attractive to candidates looking for a career ladder.[2]

Human capital considerations are crucial, especially in situations where domestic jobs are lost and remaining personnel may question the company's commitment to its employees. The loss of productivity from a poorly managed outsourcing transition can easily cancel out the anticipated cost savings. Current employees may need to train and interact with overseas staff on critical projects while struggling with change management issues as well as cultural and language challenges.

A well-defined change management program can address the human resources concerns and refocus attention on developing and enabling the retained staff as they face the company's new challenges. Communications throughout the process are critical to help employees understand the challenges, why outsourcing makes sense, and how every employee plays a critical role in helping the company move ahead.

IT OUTSOURCING CONSIDERATIONS

As technology continues to drive business strategies for digital transformation and efficiency, IT investment remains strong. A survey of senior business and IT executives by consulting firm McKinsey & Company found they plan to increase their investments in new technologies from 32% of overall IT spending in 2016 to 40% in 2019.[3]

A crucial factor driving the continued outsourcing of IT functions is the ongoing shortage of technology talent. McKinsey & Company reports that IT expertise is critically needed for data analytics and to support joint business and IT initiatives for cloud computing, mobile app development and cybersecurity.[4] By outsourcing IT projects to overseas teams, companies can find the needed skills and move quickly to transform their digital and technology processes.

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A considerable number of IT projects are outsourced to India, where overall outsourcing represents approximately 20% of the country's exports of goods and services.[5] For decades, Indian technology companies have provided global businesses with skilled technology engineers at very low cost to develop custom programs, maintain in-house computer networks, write code for databases and enterprise software, and handle labor-intensive computer conversions.

The rise of cloud computing is beginning to shift some companies away from overseas IT outsourcing. Cloud servers are accessible through the internet and can be concentrated in fewer locations. The cloud enables closer proximity to a company's home operations and requires fewer skilled technicians to monitor systems.

Major companies such as IBM, Amazon and Accenture PLC are switching from outsourced data centers to cloud storage and replacing custom-made software with more generic cloud versions.[6] Although companies will continue to use outsourcing arrangements for special IT projects such as Big Data implementation, they now have more options for data storage and management and other IT operations.

To discuss these topics in more detail, please contact your PNC Relationship Manager.

1   "Top global market trends and predictions for 2016 and beyond," Key findings from KPMG's Global Sourcing Advisory 4Q2015 Pulse Survey, February 2016.
    Executive summary available at: http://www.kpmg-institutes.com/institutes/shared-services-outsourcing-institute/articles/2016/02/sourcing-advisory-global-pulse-report-4q15.html

2   "Avoiding the common pitfalls of outsourcing: An integrated approach to effective outsourcing initiatives," Deloitte, 2015.
    Available at: http://www2.deloitte.com/us/en/pages/operations/articles/avoiding-common-outsourcing-pitfalls.html

3   "Five questions boards should ask about IT in a digital world," by Aditya Pande and Christoph Schrey, McKinsey & Company, July 2016.
    Available at: http://www.mckinsey.com/business-functions/business-technology/our-insights/five-questions-boards-should-ask-about-it-in-a-digital-world

4   "Partnering to shape the future — IT's new imperative," McKinsey & Company survey, May 2016.
    Available at: http://www.mckinsey.com/business-functions/business-technology/our-insights/partnering-to-shape-the-future-its-new-imperative

5   "India's Outsourcing Firms Change Direction as 'Cloud' Moves In," by Sean McLain, *The Wall Street Journal*, July 12, 2015.
    Available at: http://www.wsj.com/articles/indias-outsourcing-firms-change-direction-as-cloud-moves-in-1436740981

6   "India's Outsourcing Firms Change Direction as 'Cloud' Moves In," by Sean McLain, *The Wall Street Journal*, July 12, 2015.
    Available at: http://www.wsj.com/articles/indias-outsourcing-firms-change-direction-as-cloud-moves-in-1436740981

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