

Deloitte Outsourcing (“Storm Warnings”) Report
Calling a Change in the Outsourcing Market (April 2005)

Background – In 2004, Deloitte Consulting conducted an in-depth study of services outsourcing strategies, their impact on organizational performance and emerging organizational trends at 25 world class organizations in the consumer business, energy, financial services, health care, manufacturing, media/ telecommunications and public service sectors. The participating organizations account for a market capitalization of \$1 trillion US dollars and employ over 1 million workers. In 2004, they spent \$50 billion on outsourcing contracts. Four of the 25 are headquartered outside the United States.

Findings – Outsourcing of services originated and became popular as a cost-saving strategy in the business recession following the Dot-Com bust of the late 1990’s. Since then, many companies have engaged in the practice to reduce costs, expand capabilities and increase flexibility. Rather than simplifying their operations, however, outsourcing often introduces complexity, increases costs and adds interpersonal friction – all requiring far more managerial attention and skill than had been anticipated.

Although outsourcing usually results in the transfer of financial and operational risks to vendors, organizations are discovering that contracts never fully protect them against customer damage and business losses resulting from service disruptions. Many are responding by bringing outsourced operations back in-house and/or exploring new alternatives to traditional outsourcing.

Services outsourcing requires a complex series of trade-offs: cost savings versus growth, speed versus quality of service delivery as well as organizational discipline in the face of constant pressures for new knowledge and better ways to meet customer needs.

Vendors and outsourcing organizations have inherently conflicting objectives. Vendor perceived structural advantages do not always translate into more, better, faster or cheaper service delivery. Only organizations prepared to structure and manage deals from inception to execution can expect to reap long term benefits.

Conclusions - In today’s economy and labor markets, organizations should avoid outsourcing based solely on anticipated cost savings. In addition, companies should only outsource commodity functions to guard against unintended knowledge transfers and should only plan on short-term contracts in order to prevent vendor dependency.

Only by demanding transparency, negotiating for simplicity to reduce unanticipated or hidden charges and actively managing outsourcing contracts can client organizations hope to avoid a loss of control to vendors as the supply side consolidates.

Contrary to optimistic portrayals by vendors, outsourcing is an extra-ordinarily complex process and, absent skilled management, anticipated benefits often fail to materialize.