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Panel 10 Strategic Directions for IT Outsourcing: Past, Present and Future

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PANEL 10

STRATEGIC DIRECTIONS FOR IT OUTSOURCING: PAST, PRESENT AND FUTURE

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When Kodak outsourced major components of its IT function in 1989, the information systems world viewed it as a watershed event. This event subsequently resulted, however, in a robust and thriving outsourcing services industry. Today, the US market exceeds $10B annually and is growing at an annual rate of 16% per year while the smaller European outsourcing market is growing even faster at an annual rate of more than 20%. Outsourcing arrangements that were once considered large are being dwarfed by recent deals such as those signed by Xerox, Hughes Aircraft and JP Morgan. As the market matures, it is apparent that numerous companies are routinely outsourcing large components of their information systems activities. Increasingly, the conventional rationale for outsourcing — vendor economies of scale and specialization — is becoming less convincing as client companies that should be able to accrue the same benefits as a vendor given their size are also engaging in outsourcing deals. Indeed, a closer examination reveals that many recent outsourcing arrangements are strikingly innovative. These deals display a stunning diversity in their objectives and in their structure, varying in scope, size, duration and contract. Accordingly, while there has been a spate of new deals, there is a dichotomy of deals: many continue to follow the traditional model and a few companies are blazing new trails.

These innovative companies — British Home Stores, British Petroleum Exploration, JP Morgan, BTI Americas, Delta Airlines and Swiss Bank are good examples — have pushed the envelope of IT outsourcing in new directions. British Home Stores is using its outsourcing contract with Computer Sciences Corporation to enhance the value of IT to the business by extending its impact on its operations. British Petroleum Exploration, on the other hand, continues to focus on improvement in its information systems activities in its selective outsourcing arrangement, but has adopted an innovative approach to managing its multiple vendors. BTI Americas, recently formed through the merger of US Travel Systems and Business Travel International is taking US Travel Systems' IT outsourcing relationship with EDS to a new level, partnering with the IT service firm to develop the next generation of travel agency point-of-sale systems. When Delta Airlines outsourced its IT operations, it did do by spinning off its systems department in which AT&T Global Information Solutions took a fifty per cent stake. The new company, TransQuest Information Solutions, will not only provide outsourcing services to the airline, but also attempt to leverage its IT assets and its knowledge of airline operations in the marketplace. Swiss Bank acquired a stake in Perot Systems as part of its outsourcing arrangement with the objective of offering outsourcing services to financial services companies. Unsurprisingly, the risks underlying more ambitious deals are significant. When AT&T decided to reorganize, the Delta-AT&T partnership was dissolved and Delta Airlines took over Transquest Information Solutions.

These examples suggest that the nature of IT outsourcing is changing in significant ways and that the strategies and options that managers can pursue are becoming more diverse and varied. Increasingly, we are observing a range of underlying strategic intentions for outsourcing. These objectives range from the traditional objective of improving service delivery to a desire to significantly improve business performance and, increasingly, to leverage IT assets in the marketplace. Even when senior managers at companies view IT as strategic, they do not always believe that they ought to retain ownership and control of the production process for information systems. In fact, in many companies, outsourcing is often regarded as the means by which companies can realize the strategic potential of IT, which they have been unable to realize through in-house IT departments. As more and more companies recognize the growing role and importance of information and communications technologies, they are increasingly confronted with the disparity between the organization and skills necessary to realize the potential of these technologies and the reality of their own in-house systems capabilities.

As outsourcing contracts vary in intention, and grow in scope and complexity, the nature of the relationship, and in particular, the contract, must also evolve. Recent contracts reflect this evolution by incorporating innovative contractual elements — ownership structure, performance measures and risk and gain sharing agreements — that address this need.

This panel will explore some of the most critical questions about IT outsourcing. What role should outsourcing play in business and IT strategy? What should a company's strategic intent for IT outsourcing be? Can, in fact, strategic activities be outsourced? What kinds of outsourcing relationships should it enter into? How should they be structured to meet company objectives? What must senior managers do to ensure the success of these arrangements?