

## **Top 10 Reasons Why Companies Outsource**

### **1. Reduce operating costs**

Companies that try to do everything themselves may incur vastly higher research, development, marketing and deployment expenses, all of which are passed on to the customer. An outside provider's lower cost structure, which may be the result of a greater economy of scale or other advantage based on specialization, reduces a company's operating costs and increases its competitive advantage.

### **2. Improve company focus**

Outsourcing lets a company focus on its core business by having operational functions assumed by an outside expert. Freed from devoting energy to areas that are not in its expertise, the company can focus its resources on meeting its customers' needs.

### **3. Access to world class capabilities**

World class providers make extensive investments in technology, methodologies, and people. They gain expertise by working with many clients facing similar challenges. This combination of specialization and expertise gives customers a competitive advantage and helps them avoid the cost of chasing technology and training. In addition, there are better career opportunities for personnel who transition to the outsourcing provider.

### **4. Free resources for other purposes**

Every organization has limits on the resources available to it. Outsourcing permits an organization to redirect its resources, most often people resources, from non core activities toward activities which serve the customer. The organization can redirect these people or at least the staff slots they represent onto greater value adding activities. People whose energies are currently focused internally can now be focused externally -- on the customer.

### **5. Resources not available internally**

Companies outsource because they do not have access to the required resources within the company. Outsourcing is a viable alternative to building the needed capability from the ground. New organizations, spin-offs, or companies expanding into new geography or new technology should consider the benefits of outsourcing from the very start.

## **6. Accelerate reengineering benefits**

Reengineering aims for dramatic improvements in critical measures of performance such as cost, quality, service and speed. But the need to increase efficiency can come into direct conflict with the need to invest in core business. As non-core internal functions are continually put on the back burner, systems become less efficient and less productive. By outsourcing a non-core function to a world class provider, the organization can begin to see the benefits of reengineering.

## **7. Function difficult to manage or out of control**

Outsourcing is certainly one option for addressing this problem. It is critical to remember that outsourcing doesn't mean abdication of management responsibility nor does it work well as a knee jerk reaction by a company in trouble.

When a function is viewed as difficult to manage or out of control, the organization needs to examine the underlying causes. If the requirements expectations or needed resources are not clearly understood, then outsourcing won't improve the situation; it may in fact exacerbate it. If the organization doesn't understand its own requirements, it won't be able to communicate them to an outside provider.

## **8. Make capital funds available**

There is tremendous competition within most organizations for capital funds. Deciding where to invest these funds is one of the most important decisions that senior management makes. It is often hard to justify non-core capital investments when areas more directly related to producing a product or providing a service compete for the same money.

Outsourcing can reduce the need to invest capital funds in non-core business functions. Instead of acquiring the resources through capital expenditures, they are contracted for on an "as used" operational expense basis. Outsourcing can also improve certain financial measurements of the firm by eliminating the need to show return on equity from capital investments in non core areas.

## **9. Reduce risk**

Tremendous risks are associated with the investments an organization makes. Markets, competition, government regulations, financial conditions and technologies all change extremely quickly. Keeping up with these changes, especially those in which the next generation requires a significant investment, is very risky.

Outsourcing providers make investments on behalf of many clients, not just one. Shared investment spreads risk, and significantly reduces the risk born by a single company.

## **10. Cash infusion**

Outsourcing often involves the transfer of assets from the customer to the provider. Equipment, facilities, vehicles and licenses used in the current operations have value and are sold to the vendor. The vendor then uses these assets to provide services back to the client. Depending on the value of the assets involved, this sale may result in a significant cash payment to the customer.

When these assets are sold to the vendor, they are typically sold at book value. The book value can be higher than the market value. In these cases, the difference between the two actually represents a loan from the vendor to the client which is repaid in the price of the services over the life of the contract.

Source: The Outsourcing Institute's Annual Survey of Outsourcing End Users